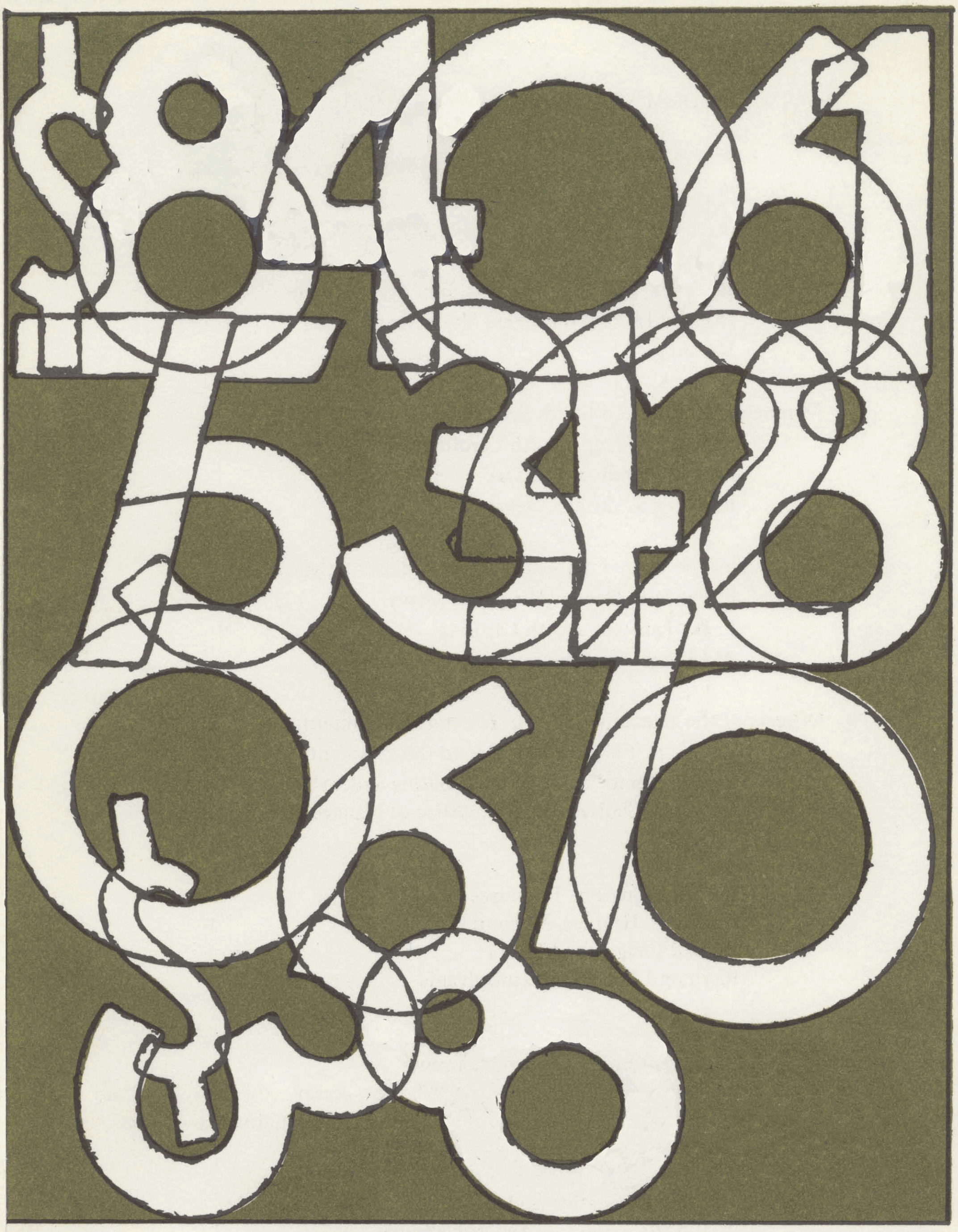

Information Report

Revenue Sharing -- An Idea Whose Time Has Come

visory Commission on Intergovernmental Relations ● December 1970

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Revenue Sharing--An Idea Whose Time Has Come

ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS
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PREFACE

The Advisory Commission on Intergovernmental Relations strongly believes that the ability to perform needed services at the right level of government is a critical ingredient for an effective, working federal system of divided responsibilities. With this objective in mind, the Commission has developed a plan for a massive rearrangement of financing responsibilities among Federal, State, and local governments. Specifically, the Commission has called for:

- Sharing of a percentage of the Federal personal income tax with States and localities (Revenue Sharing)

- Assumption by the Federal Government of all costs of public welfare and medicaid

- Assumption by State government of substantially all local costs of elementary and secondary education

- Encouragement of a high-quality, high-yield State tax system through a Federal income tax credit for State income taxes paid.

- Creation of a more manageable and streamlined categorical aid system through consolidation and joint funding of existing Federal grant programs

The Commission believes that the enactment of the revenue sharing idea, as one vital part of this fiscal re-sorting package, is essential to the cause of decentralized government. Because of this belief and the keen public interest in the subject, the Commission directed the staff to prepare an information report setting forth as forcefully as possible the case for revenue sharing. The Commission recognizes, of course, as it did in 1967, that revenue sharing of itself is no panacea. It is one component—albeit an important one—of a comprehensive program to restore the fiscal balance in our federal system. The Commission authorized publication of this report at its meeting September 11, 1970.

As can be expected with a Commission whose members are drawn from all levels of government and the general public, it is rarely possible to secure unanimity of opinion with respect to any proposal that calls for far-reaching changes. The revenue sharing proposition is no exception to this general rule. While it enjoys strong Commission backing, Representative Al Ullman of Oregon has indicated that he does not want the publication of this report to be construed as his endorsement of direct revenue sharing, although he strongly favors the tax credit features of the Commission's proposal.

Robert E. Merriam
Chairman

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REVENUE SHARING: AN IDEA WHOSE TIME HAS COME

Federal revenue sharing with State and local governments stands out as the next logical development in our system of shared power.

Barring a sharp rise in the Nation's foreign commitments, the revenue sharing idea has a fairly good chance of being translated into the law of the land. This optimistic assessment is underpinned by an impressive array of favorable developments that have occurred since the idea was broached seriously to the Johnson Administration in 1964 by Walter Heller, then Chairman of the Council of Economic Advisors and Joseph Pechman, Director of Economic Studies at Brookings Institution.

(1) The revenue sharing idea now enjoys widespread public support–71 percent of the American people favor this proposition according to a recent Gallup poll. Revenue sharing enjoys overwhelming support across the entire political spectrum–76 percent of the Republicans, 71 percent of the Democrats, 68 percent of the Independents–believe that revenue sharing is a good idea.

(2) Representatives of State and local governments give revenue sharing top priority billing and agree on the basic outline of the plan for the distribution of revenue sharing funds.

(3) The Nixon Administration assigns high legislative priority to revenue sharing.

(4) Notwithstanding its power sharing characteristics, revenue sharing also enjoys strong Congressional backing. Over 30 percent of the members of Congress have either introduced or co-sponsored revenue sharing bills.

To be sure, several major obstacles must be overcome before revenue sharing can be enacted. It must compete for Congressional attention and support with some dramatic specific problems–cleaning up the environment, speeding the development of urban mass transit, enlarging Federal support for education and restructuring public assistance programs. In addition, because to some Federal revenue sharing seems to imply Federal power sharing, the depth of support for and understanding of the concept must be demonstrated forcefully before favorable action can be expected.

For reasons that will be made apparent in the following pages, this Commission favors early Congressional enactment of the revenue sharing principle. To focus public attention on this issue and to rally both public and Congressional support for the adoption of revenue sharing we seek to answer three questions about it.

- What is the basic idea behind revenue sharing?
- What are the major arguments in its favor?
- What are the major objections to it and how can they be answered?

The Idea

The basic idea behind revenue sharing is quite simple—to strengthen the fiscal capabilities of State and local governments by requiring the National Government to share with them a designated portion of the Federal personal income tax revenue *on a no expenditure strings basis.* In essence, revenue sharing would establish the principle that State and local governments should have a guaranteed, albeit limited, access to the Nation's prime power source—the Federal personal income tax. Then, and only then, will they be able more effectively to carry out their assigned task of delivering the bulk of domestic public services.

THE CASE FOR REVENUE SHARING

The abiding American belief in the positive virtues of "grass roots" government underpins any effort to strengthen the fiscal independence of State and local governments. This preference for decentralized government reflects the widespread recognition that the National Government lacks the perspective to heal all the Nation's domestic ills. More importantly, it recognizes the great strength of decentralized government—a flexibility that stimulates individual response to diverse local conditions and needs.

This concern for strengthening the position of State and local governments also reflects the powerful attraction that the concept of "balance" exerts within our federal system. We are still receptive to the idea of "leaning against the wind," of resisting those tendencies and forces in our system that if unchecked would result in lodging a disproportionate amount of political power at one level of government. During the days of the Confederation, the federalists sought ways of strengthening the National Government without undue sacrifice of the powers of the State. Contemporary "federalists" are now searching for ways to strengthen the States and localities without undue sacrifice of National goals. Because money and political power are so inexorably intertwined, this search concentrates on developing fiscal mechanisms such as revenue sharing—a means best calculated to use the unquestioned revenue superiority of the National Government to reinforce the advantages of decentralized government.

Revenue Sharing—Redressing the Power Imbalance

Federal revenue sharing is needed to check the steady centralization of power in Washington—an imbalance situation that can be traced to the growing Federal revenue superiority and increasing Federal control over State and local expenditure decisions.

Growing Federal revenue superiority. An increasingly interdependent economy, a vastly superior jurisdictional reach and a near monopoly of the income tax enable the Congress to raise far more revenue at far less political risk than can all of the State and local officials combined. While the careers of many State and local officials have been wrecked by courageous decisions to increase taxes, similar action at the Federal level is seldom necessary and rarely if ever fatal to a political career.

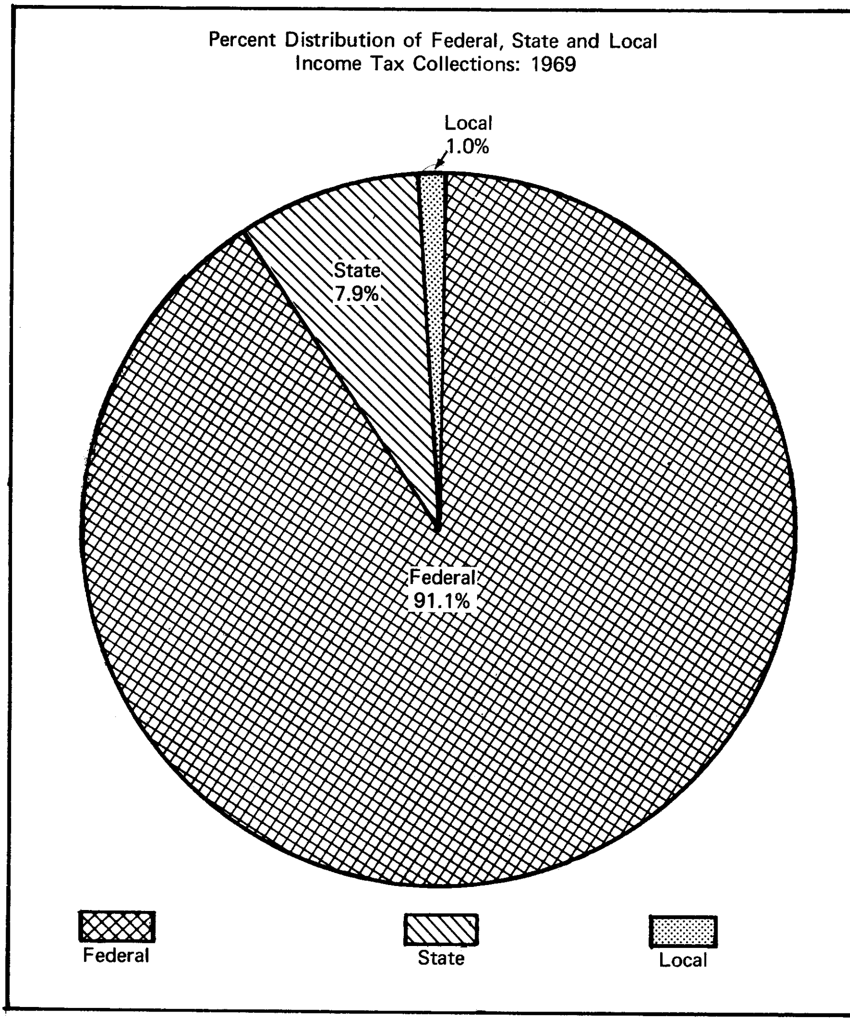
It is not surprising therefore that power gravitates to the place (Washington) that can command resources more readily. To put the matter in more philosophical terms, the growing revenue superiority of the Federal Government undercuts a basic premise that supports our federal system—that officials at each level of government will experience about the same degree of resistance when making demands on the taxpayer's pocketbook.

The dominant income tax position enjoyed by the Federal Government helps to insulate Federal policymakers from irate taxpayers. Because the National Government now collects about 90 percent of all personal income tax revenue, it has virtually "cornered" the revenue producer that is most sensitive to economic growth. For every one percent of growth in the Nation's economy, individual income tax receipts automatically rise by about 1.5 percent. In contrast, most of the State and local tax levies behave rather sluggishly—their "automatic" growth performance lags somewhat behind economic growth.

While the National Government can count on automatic higher revenue yields generated by economic growth to accommodate most of its growing expenditure needs, almost every year State and local policymakers are forced to take the politically risky course of imposing new taxes and raising the rates of existing taxes to meet the rising expenditure requirements of an urbanized society. In 1960, nineteen States were imposing both general sales and personal income taxes. Ten years later the number had climbed to thirty-three. Over this same time span, the growth in State and local tax collections out-paced national economic growth. State and local taxes rose from the equivalent of 7.3 percent of the Gross National Product in 1960 to 8.6 percent of GNP at the close of the decade. A study by the Commission staff revealed that between 1950 and 1967 only 47 percent of the increase in major State taxes—income, and general and selective sales taxes—was the result of economic growth while 53 percent resulted from legislative enactment.

In addition to this automatic growth superiority, the National Government enjoys another revenue raising advantage—its freedom from the hobbling fears of interlocal and interstate tax competition. The more limited a government's juris-

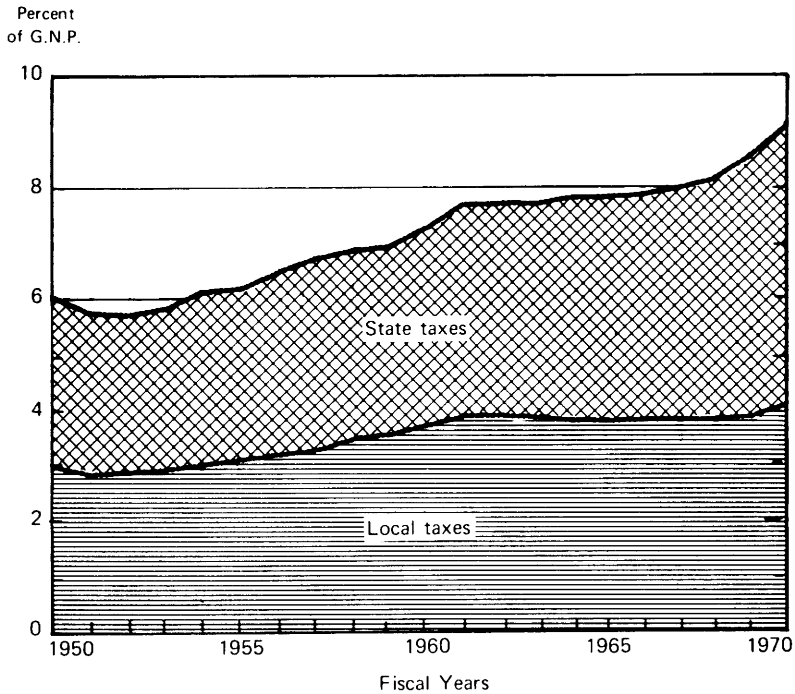
FIGURE 1—FEDERAL GOVERNMENT DOMINATES INCOME TAX FIELD



Source: U.S. Bureau of the Census, *Governmental Finances in 1968-69.*

FIGURE 2–STATE AND LOCAL GOVERNMENTS CONTINUE TO INCREASE THEIR TAX EFFORT

State and Local Taxes As A Percentage of Gross National Product, 1950 through 1970



Number of States With General Sales and Broad-Based Personal Income Taxes, As of January 1, 1950, 1960 and 1970

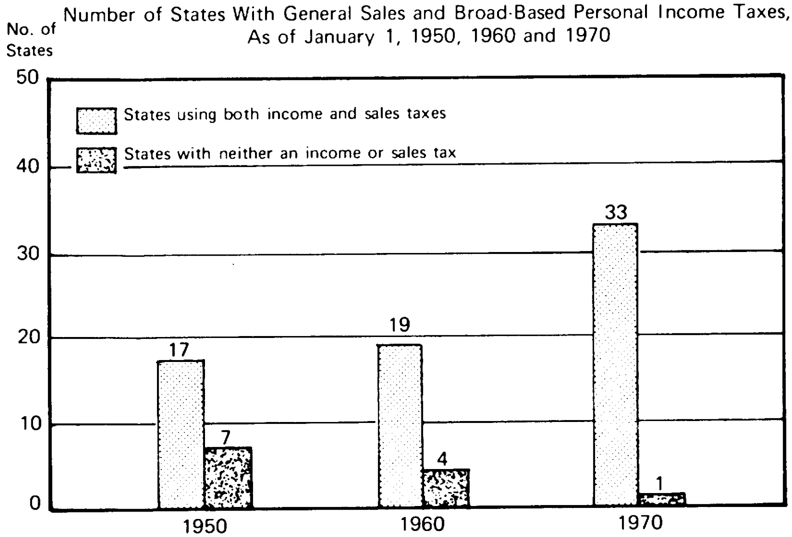
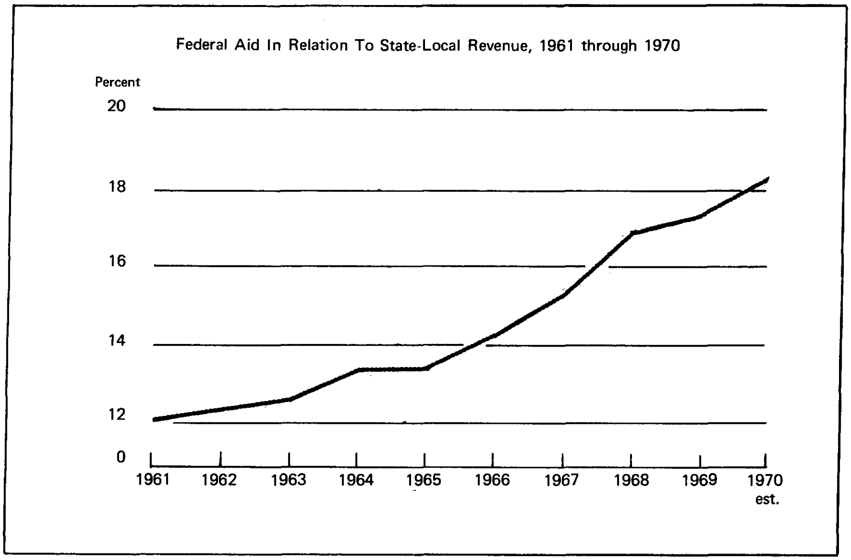


FIGURE 3–STATE AND LOCAL GOVERNMENTS ARE BECOMING INCREASINGLY DEPENDENT ON FEDERAL CONDITIONAL AIDS



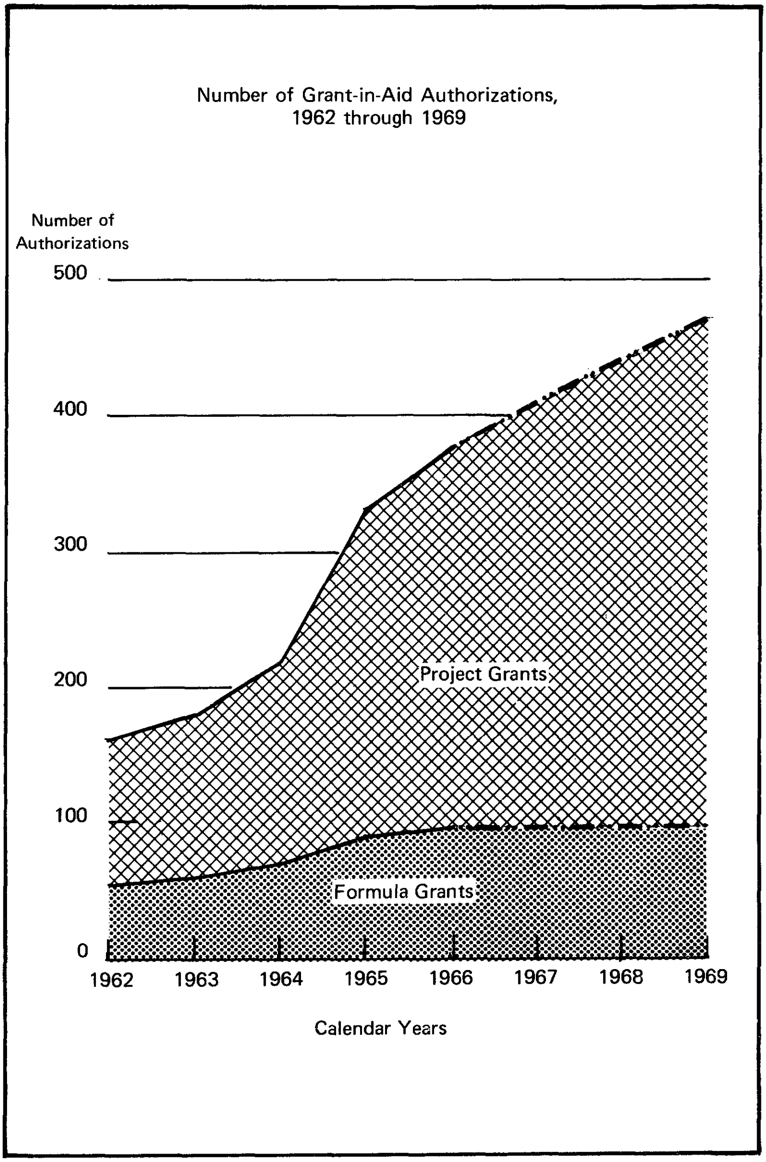
Source: Special Analysis O, Budget of the United States, Fiscal Year 1971.

dictional tax reach, the more apprehensive the government becomes about its relative tax climate. Two great forces are heightening this sensitivity to intergovernmental tax competition–the growing desire of State and local policymakers to promote economic development and the increasing interdependence of our economy.

Growing Federal control of State and local programs. The lopsided Congressional reliance on the narrow categorical or conditional aid tips the power scales even further toward the Federal Government.

The Congress is now dangling almost 500 large and small conditional aid carrots collectively worth more than $25 billion a year before State and local governments. The hope was that each conditional aid would provide sufficient financial incentive to spur the States and localities on to greater action in some more or less narrowly defined field of "National interest." But there is overwhelming evidence that State and local governments cannot

FIGURE 4—FEDERAL CONDITIONAL AIDS ARE PROLIFERATING



Source: Advisory Commission on Intergovernmental Relations, *Fiscal Balance in the American Federal System, Vol. 1;* and Library of Congress, Legislative Reference service.

readily absorb such a large number of diverse programs over restricted periods of time. The sheer number of these Federal incentives, each designed to accomplish a different objective, has produced managerial apoplexy if not financial exhaustion for those jurisdictions not able to devote the time and resources necessary to track down and match every available Federal aid dollar.

Progressive loss of freedom of choice, therefore, is an additional price that must be paid by all State and local jurisdictions for categorical aid dollars. Professor Walter Heller, both a keen student of our intergovernmental fiscal system and a prominent member of the liberal establishment, has pointed up the dangers of this trend toward centralized power. "Unless this trend is reversed," he wrote, "Federal aids may weave a web of particularism, complexity, and Federal direction which will significantly inhibit a State's freedom of movement."* The illusion of Congressional "control" has in reality disappeared into the dark jungles of bureaucratic red-tape.

Because Federal revenue sharing is "power sharing" in the very best tradition of equal partners in a joint governmental endeavor, this Federal aid approach stands out as the most direct and the most effective method to redress the fiscal and power imbalance caused by both the growing revenue raising superiority of the National Government and the lopsided and increasing Federal reliance on conditional aids with its inevitable loss of responsible "control."

Revenue Sharing—A Versatile Fiscal Tool

Another outstanding strength of revenue sharing is its versatility—the capacity to achieve many different objectives.

Accords with federalism. Revenue sharing harmonizes with one of the strengths of the American system—its diversity. States and localities must take different approaches to problems and all benefit by their experimentation. The National Government has a clear-cut interest in creating a fiscal environment that is conducive to experimentation. If the benefits of diversity are to be exploited,

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*Walter W. Heller, *New Dimensions of Political Economy,* (Cambridge: Harvard University Press, 1966) p. 142.

and indeed enhanced, the National Government must help create a fiscal environment that will enable its federal partners to exercise wide latitude in determining their budgetary priorities.

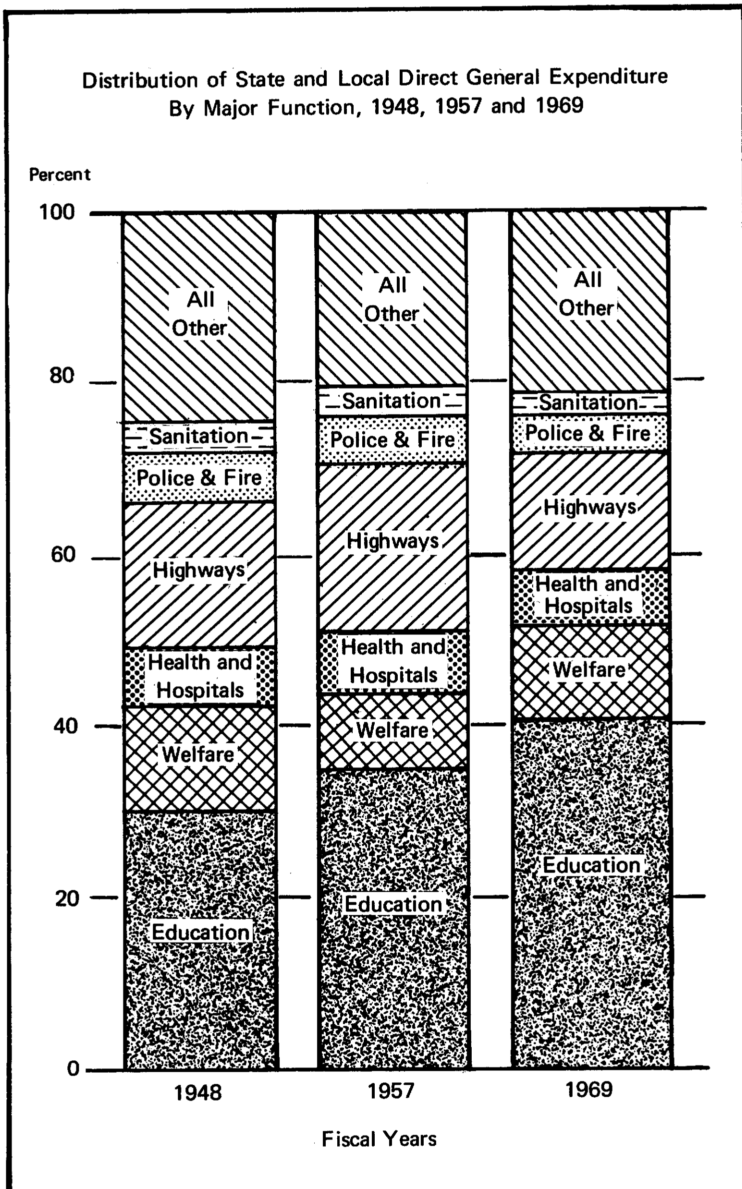
Revenue sharing would promote the use of State-local funds in a manner that accords best with National political priorities. Because this form of financial aid could be free of expenditure strings, each State and locality would have complete freedom to use these funds, as it would those raised by its own taxes, on items of greatest urgency in accordance with the jurisdiction's peculiar needs. As State-local expenditures go, this suggests that at least 40 percent of the revenue sharing funds might be spent on education, another 20 percent, on welfare and health programs, with substantial portions for police and fire protection and the provision of sanitation services.

Helps ease State and local fiscal tensions. A well-financed Federal revenue sharing plan is needed to ease a growing fiscal squeeze at the State and local levels. On the revenue side, these governments, already hobbled by fears of intergovernmental tax competition, are meeting increasing taxpayer resistance as they push property, sales, and income tax rates ever higher. On the expenditure side, the unremitting demand for safer streets, better schools, a cleaner environment, and rapid urban transit, all combine to place massive expenditure pressures on these jurisdictions. If State and local governments are to continue to provide the bulk of the Nation's domestic services, they must be placed in a stronger revenue position. Revenue sharing will accomplish that objective by guaranteeing them a designated proportion of the Nation's prime revenue source—the personal income tax.

Responds to need for equalization. Revenue sharing would operate in the right direction from the standpoint of interstate equalization and could be adjusted to serve as a powerful equalization instrument below the State level. A per capita distribution formula alone produces a moderate degree of equalization between wealthy and poor States, at the same time providing the most aid to the most populous States. Still more equalization can be built in with sophisticated tax effort and fiscal capacity measures.

Strengthens the Federal aid system. The present Federal aid system results in fiscal rigidity at the State and local level. By providing unconditional aid, revenue sharing will correct this

FIGURE 5—STATE AND LOCAL GOVERNMENTS PUT THEIR MONEY



Source: U.S. Bureau of the Census, Governments Division.

major deficiency. Along with the present efforts to consolidate and simplify categorical aids, revenue sharing would provide State and local governments the added financial flexibility needed to package the many narrow Federal categorical aids into well-rounded public service programs.

Introduces greater equity into the Nation's intergovernmental tax system. The sharing of Federal personal income tax revenue would enable State and local governments to make somewhat less intensive use of local property and State sales taxes—levies that are most burdensome for low-income families. Indeed, some States may use revenue sharing funds to build greater equity into their tax systems by shielding basic family income from undue burdens of sales and property taxes. The Commission has recommended that the States finance property tax relief for low-income families and pull the regressive stinger from the sales tax by means of a food exemption or tax credits.

Protects the domestic front. The emergence of this Nation as a super power with massive foreign commitments makes it all the more necessary to develop new safeguards designed to prevent the shortchanging of our domestic needs in general and our domestic instrumentalities (State and local governments) in particular. Witness this assessment by Daniel P. Moynihan:

> As far as I can see, an American national government in this age will always give priority to foreign affairs. A system has to be developed, therefore, under which domestic programs go forward regardless of what international crisis is preoccupying Washington at the moment. This in effect means decentralizing the initiative and the resources for such programs.*

The sharing of Federal revenue with State and local governments in good times and bad times is responsive to this need to decentralize both initiative and resources.

**Congressional Record,* September 26, 1967, p. H. 12499. Speech to meeting of Americans for Democratic Action, September 23, 1967.

Revenue Sharing No Panacea—Public Welfare Financing A Case In Point

While revenue sharing is a remarkably versatile fiscal instrument, it is by no means a panacea for all the major ills that afflict our intergovernmental fiscal system.

No amount of Federal revenue sharing is likely to eliminate the tremendous inequities in our present public welfare system. The States are beginning to view this program as an intergovernmental "boomerang." States that are unable or unwilling to provide a minimum level of public assistance find their caseloads diminishing while those meeting this obligation are faced with rapidly expanding caseloads and costs. This is a classic situation where virtue does not have its own reward. To make matters worse, recent Federal judicial and administrative actions have largely eliminated State control of eligibility standards. As a result, a growing number of State and local officials now strongly endorse Federal Government assumption of complete responsibility for the financing of public assistance programs.

Although both Federal takeover of welfare financing and Federal revenue sharing would reduce State and local fiscal tensions, they cannot be viewed as alternatives or substitutes for one another. Federal revenue sharing is urgently needed to strengthen the financial foundation of our system of decentralized government while the "nationalization" of public welfare financing is absolutely necessary to secure a just method for assisting the poor and a fair procedure for spreading welfare costs across the body politic.

REVENUE SHARING: CHALLENGE AND RESPONSE

Divorces Taxation and Spending

Allegation: By divorcing tax and spending authority, revenue sharing would dismantle the present control system and thereby encourage wasteful State and local spending.

Response: Under revenue sharing, the political accountability of State and local officials to the electorate would stand as a powerful and natural defense against wasteful fiscal practices. These policymakers are keenly aware of a hard political fact–that they would be forced to ask their constituents to pay higher taxes if they frittered away revenue sharing funds.

Moreover, revenue sharing funds flowing through the regular local budgetary process would be scrutinized far more sharply than the "sheltered" Federal aid dollars funnelled through the categorical aid system. The "control" factor, often cited as an argument against revenue sharing, would be shifted, but it would most certainly not be lost.

Also underpinning this allegation is the most highly questionable assumption that Federal policymakers now exercise effective *program* control over the present system of conditional grants. The sheer size and complexity of the current \$25 billion categorical aid system with its 500 different spigots defy effective Presidential and Congressional oversight. Authority must be delegated to thousands of program administrators who police this vast aid system by creating a jungle of regulations an almost impenetrable obstacle to efficient State and local use of Federal aid dollars.

The progressive erosion of Presidential and Congressional *budgetary* control over this sprawling Federal aid system is also becoming increasingly apparent. It stems from the growing Congressional reliance on trust funds, long-term contract authorizations, and debt service grants to help finance highways, airports, mass transit facilities, college housing and public housing units. The great gap between Federal aid promises (program authorizations) and funding performance (annual appropriations) was one of the most powerful factors working in behalf of the demand that Congress sear a high degree of certainty into the funding of these and other capital facility programs. The price that must be paid for this type of certainty is also evident—the President and the appropriations committees are stripped of most of their annual budgetary control over these major categorical aid programs.

Confronted with these fiscal realities on the Federal level and the fact that Federal revenue sharing dollars will be spent in accordance with State and local expenditure priorities the "control" argument can be viewed for what it really is—theoretically a highly plausible objection to the revenue sharing concept, but in reality a rather specious one.

More Pressing National Priorities

Allegation: While revenue sharing might be a useful addition to the Federal aid system, there are more pressing National expenditure requirements that must be financed first. Furthermore, there are no Federal income tax "profits" to share with State and local governments now or in the near future.

Response: The presence or absence of a Federal "surplus" is no excuse for failing to give highest priority to National purposes, particularly the strengthening of the financial foundation of decentralized government. Revenue sharing would reinforce the fiscal independence of State and local governments and help them finance the programs needed to make our streets safer, our air and water cleaner, our urban traffic move faster, and our educational attainment higher. Thus, because it can promote progress along the entire domestic front, revenue sharing rates a top budgetary priority.

Throughout the history of American federalism, the Federal Government has used its resources to aid States and localities in dealing with domestic problems. The classical response to the emergence of a major domestic problem has been to create a new Federal aid program. While these individual categorical programs have helped and will continue to help, there is increasing recognition of the need not only to deal with "National problems" but also to strengthen the institutions—State and local governments—that must handle them.

Practically speaking, there is never a time when the Federal budgetary pickings are easy. The powerful contending forces that operate in the Federal budgetary arena are quite capable of consuming any surplus on hand or in sight. Thus, adoption of revenue sharing should under no circumstances be contingent on the availability of Federal "profit" or "fiscal dividend." The National interest in strong State and local government persists in good times and bad. Once revenue sharing is enacted in recognition of the National interest, tax reduction and the host of competing proposals for "surplus" Federal revenue can be considered on their own merits.

Undermines Categorical Aids

Allegation: Revenue sharing would undermine categorical aid programs and therefore the ability of Congress to use special incentive grants to achieve National objectives in particular program areas.

Response: The allegation that general support assistance would drive out categorical grants is a faulty assessment of Congressional and bureaucratic interest in specific programs. There is no reason to believe that having once enacted revenue sharing Congress would then preside over the liquidation of the categorical aid system thereby renouncing its influence over so many of the great domestic programs operated by State and local governments.

Experience indicates that the particular always tends to drive out the general interest. Legislative and executive bodies at all levels are organized along particular functional lines and tend, therefore, to focus on specific programs rather than on the overall strength and vitality of the governmental entities. It is not surprising, therefore, to find that the short-run demand of pressure groups to beef up their programs invariably overrides the long-range need to strengthen the instrumentalities for delivering services—the State and local governments. As a result the Federal Government now distributes over $25 billion through about 500 separate conditional aid channels but not one aid dollar for unconditional support, apart from shared public land revenue.

For years, State governments have made both unconditional and categorical grants to local governments without one or the other being impeded. Only the National Government—specifically the Congress—has failed to utilize the dual approach.

State-Local Revenue Systems Not Exhausted

Allegation: Until virtually all State-local revenue systems make effective use of the "Big-Three"–property, sales, and income taxes–Congress should not share any of its revenue on an unconditional basis with State and local governments.

Response: Expenditure requirements and resource capabilities vary so widely among our 50 State-local systems that we are not likely to see the day when all revenue systems exhibit the same essential characteristics. Thus, to require such "lock step" type of uniformity as a pre-condition for revenue sharing is not only to insist on the attainment of a fiscal impossibility, but to negate the principle of diversity that is central to the American concept of federalism.

There is no blinking away the fact that the popular case for revenue sharing would be strengthened considerably if most States were making fairly effective use of the income tax. At the present time 13 States do not levy this tax and many others make only anemic use of this prime revenue source.

In the Commission's judgment, extensive use of the personal income tax by the Federal Government has retarded the State personal income tax movement. In order to lessen this deterrent effect the Commission has recommended that the Congress provide a partial tax credit for State income tax payments. In our judgment, adoption of this proposal by the Congress would restore to the States the personal income tax option–a tax policy alternative that became less attractive to the State political leadership as the Federal take from this tax escalated.

The basic case for revenue sharing does not rest on the contention that most States have exhausted their revenue capabilities and are on the verge of bankruptcy. Rather, it rests on the proposition that revenue sharing appears to be the most effective way to deal with a basic power and fiscal imbalance within our federal system. More specifically, if we are to maintain strong State and local governments and to check the centralization of power in Washington, the number one fiscal and power source–the Federal income tax–must be converted into the Nation's rather than the National Government's patrimony. This can be done by guaranteeing State and local governments a designated share of the revenue derived from this source.

Increases State-Local Dependency

Allegation: By providing a revenue alternative to greater State and local tax effort, Federal revenue sharing would encourage these governments to become unduly dependent on the National Government for their financial support.

Response: In theory, this challenge appears highly plausible, but from a practical standpoint it lacks substance. While it is true that each Federal aid dollar helps ease somewhat the State and local fiscal crunch, political realities would hold Federal revenue sharing aid at a level far below that necessary to free State and local officials from pressure to raise revenue from their own resources.

Congress and the President are being urged constantly to expand existing Federal programs, to undertake new spending incentives, and to reduce Federal taxes. This fierce competition for Federal resources shows no sign of abating—in fact, Federal revenue sharing would only intensify this perennial budgetary struggle as it becomes one more contender for Federal dollars.

Confronted by the host of powerful claimants for National budgetary priority, Congress could hardly be expected to turn over the keys of the Federal Treasury to State and local officials. No responsible plan for sharing Federal revenue with State and local governments sets a level of aid support that comes within hailing distance of $10 billion—the current annual growth in State-local revenue.

The possibility that revenue sharing would result in undue dependency can be reduced by adjusting each State-local share of the total fund by a factor measuring relative revenue effort, as all major revenue sharing proposals do. With this type of provision and the virtually insatiable demand for public services, it is unlikely that States and localities would supplant their own effort with revenue sharing funds.

In actuality, revenue sharing's simplicity not only makes it inexpensive to administer, but easy to police (hence "control"). The net result must be less State and local dependency, not more.

State-Local Modernization Should be a Condition

Allegation: States and localities should be required to modernize their organizations and to restructure their politically fragmented metropolitan areas before they are given "no expenditure strings" aid.

Response: There is no denying that much remains to be done to modernize State government and to restructure local government. In particular, fragmented local government in most of our major metropolitan areas has contributed significantly to the imbalance between responsibilities and fiscal resources at that level. Indeed, much of this Commission's time and effort has been devoted to pointing up the organizational and structural shortcomings of State and local government and to recommending policies for correcting them. As is appropriate to the basic tenets of American federalism, most of these recommendations have been directed to the States, which are constitutionally responsible for the governmental structure and organization through which most domestic public services are provided.

The Commission is keenly aware that progress on this front is painfully slow. Some of the proposed reforms, such as the reduction in number of local units and the creation of metropolitan-type governments are highly controversial. Others suffer from the lackluster appeal all too often associated with "good government" causes, such as the short ballot, annual legislative sessions and gubernatorial succession.

It would be a disservice to the cause of balanced federalism to insist that every State put its structural house in perfect order before the principle of revenue sharing is enacted. While revenue sharing is a remarkably versatile fiscal instrument it is no panacea for all the basic ills of federalism. Its primary objective always will be that of redressing the fiscal and political imbalance between the National Government on the one hand and fifty State-local fiscal systems on the other.

Reduces Federal Budgetary Flexibility

Allegation: By earmarking a designated percentage of the Federal personal income tax base for unrestricted State and local use, revenue sharing would cut into the budgetary flexibility of the President and the Congress.

Response: The President and the appropriations committees of the Congress are bound to experience some reduction in budgetary discretion if revenue sharing is enacted. This is one of the necessary and unavoidable costs associated with any plan that earmarks a portion of the personal income tax for strengthening State and local governments.

Revenue sharing would add a new dimension to Federal fiscal policy deliberations. It would harness a small measure of the massive Federal fiscal force to the task of preserving and enhancing federalism itself.

Federal Tax Cut Would Obviate Need for Revenue Sharing

Allegation: At the appropriate time Congress could cut Federal taxes thereby both freeing up more resources for State and local tax collectors and obviating the need for Federal revenue sharing.

Response: Powerful political, equity and jurisdictional considerations argue against the contention that the mere reduction of the Federal income tax can solve the State-local fiscal dilemma.

Such a policy would place governors and mayors in the untenable political position of wresting from the citizenry the tax reduction granted by the Federal authorities. National policymakers would reap all the political credit for granting tax reduction while State and local policymakers would be denounced for short circuiting this beneficent Federal policy.

This proposition would have the overall effect of weakening our total State-local revenue system if States and localities made more intensive use of property and consumption taxes. When compared to the local property tax and the State sales levy, the Federal income tax stands out as a far more equitable and productive revenue instrument.

The extreme reluctance of State legislative bodies to make intensive use of corporate and personal income taxes—an unwillingness generated in part by interstate tax competition fears—places powerful constraints on the ability of States to pick up *all* or even most of the slack on the income tax front. This fear of interstate tax competition points up both the growing economic interdependency of our Nation and the fallacy of composition—i.e., the assumption that by adding together the limited jurisdictional reach of each State (the parts) it is possible to duplicate the revenue raising capability of the National Government (the whole).

THE TIME IS NOW

In the foregoing pages we have set forth the reasons why revenue sharing should be made an integral part of American fiscal federalism. We believe strongly that our governmental system of shared powers and shared responsibilities must be preserved and enhanced.

Giving the Federal income tax an additional task merely underscores the versatility and power of this revenue instrument. Originally, it was viewed almost exclusively as a revenue raising device. During the 1930's it was called on to bring about a better distribution of personal income through the introduction of a high degree of progression into its rate structure. Beginning with World War II this tax became the major fiscal device for assuring stable economic growth and dampening pricing fluctuations. Now is the time to charge this tax with the task of preserving the institutional structure of our federal system.

Chairman Robert E. Merriam recently summed up the need for early enactment of the revenue sharing principle when he stated before a Congressional Committee:

> The greatest value of revenue sharing, however, may be psychological. The enactment of revenue sharing, after all, would provide the most persuasive evidence that national policymakers have confidence in our system of federalism, in general, and in State and local governments, in particular. In a time of cynicism and discontent, it is more important than ever to reaffirm our confidence in our basic institutions, State and local governments, and in the American people they are designed to serve. Coupled with a hoped-for development of a national urban policy in which the President and the Congress could spell out priorities of national interest, perhaps we can in the 1970's point the way toward a more rationalized, and more workable, federal system.
>
> Above all else . . . I would urge the Congress this year, if possible, to make a start down the revenue-sharing road, no matter what the precise formula. In our opinion, the principle far exceeds in importance any proprietary formula for its execution.*

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*U.S. Congress, Senate Committee on Government Operations, Subcommittee on Intergovernmental Relations. *Intergovernmental Revenue Act of 1969 and Related Legislation; Hearings.* (Washington: Government Printing Office, 1970) p. 301.

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Concludes that serious consideration should be given to the Administration's revenue sharing plan, which, because of its tie-in with the States' revenue effort, will, it is hoped, persuade municipalities across the country to make effective use of the income tax.

American Enterprise Institute for Public Policy Research.
Revenue Sharing Bills; Legislative Analysis. (Washington: 1970) 45pp.

Discusses the background of federal revenue sharing; briefly describes the various proposals currently pending before Congress; and discusses the major arguments for and against federal tax sharing.

Babb, Jervis J.
"Alternatives for Intergovernmental Finance." In National Tax Association. *Proceedings of the Sixtieth Annual Conference, 1967:* 26-40 (Columbus: 1968).

Discussion of the alternatives for intergovernmental finance in the context of a study on fiscal federalism made by the Committee on Economic Development.

Barlow, Joel
"Toward a National Tax Structure." In Tax Institute of America. *Federal-State-Local Fiscal Relationships; A Symposium:* 131-148 (Princeton: 1968).

Contends that revenue sharing must be viewed as part of a larger goal: achieving a truly integrated national tax structure, rationalizing the tax structure vis-a-vis those who are taxed as well as between those who do the taxing. Calls for a dual solution that couples redistribution of tax moneys with reform of our federal and State tax systems.

Brady, Patrick R.
"Local Revenues vs. Shared Taxes," *Municipal Finance,* Vol. XLII, No. 2, November 1969: 103-109.

Concludes that revenue sharing poses some problems which are at first not apparent, but the inadequacy of the local revenue base and the nature of the urban problem makes use of this revenue device imperative.

Candilis, Wray O.
"Revenue Sharing: A Solution to State Financial Problems," *Banking,* Vol. 59, August 1966: 39-404.

Discusses the concept of revenue sharing and describes several plans for its implementation.

Congressional Quarterly Service.
"Revenue Sharing." In *Guide To Current American Government:* 118-124 (Washington: Spring 1970).

Historical and legislative background of President Nixon's revenue sharing proposals.

Harkins, Peter B.
"Revenue Sharing: Is This the Year?" *Nation's Cities,* Vol. 8, No. 3, March 1970: 10-12.

Opposition to revenue sharing may mean extremely rough going as Congress debates several proposals.

Harris, C. Lowell
Federal Revenue Sharing: A New Appraisal. (New York: Tax Foundation, Inc., 1969) 27p.

Summarizes, and develops criteria for evaluating, the various revenue sharing plans.

Heilbroner, Robert L.
"The Share-the-Tax Revenue Plan," *New York Times Magazine,* December 27, 1964: 8+.

Contends that the real issue in the revenue sharing debate is the role that State governments should play in shaping the economic and political future.

Heller, Walter W.
New Dimensions of Political Economy. (Cambridge: Harvard University Press, 1966). 203p. Chapter III.

A detailed explanation of the "Heller Plan."

Heller, Walter W.

"Should the Government Share Its Tax Take?" *Saturday Review* March 22, 1969: 26-29.

Sums up the case for revenue sharing as the instrument that will (1) fill a major gap in our fiscal federalism; (2) strengthen the fabric of federalism by infusing funds and strength into the State-local enterprise and (3) increase our total governmental capacity to cope with the social crisis that confronts us.

Keyserling, Leon H.

"Sharing Revenue with the States." *The New Republic,* Vol. 156, March 25, 1967: 14-18.

Opposes no-string revenue sharing, because it represents essentially the same errors which have been deeply embedded in the policies of the "new economics." These errors are founded on the proposition that federal fiscal policy should concern itself with the *aggregates* of taxation and spending and manipulate these from time to time, but should be "neutral" by paying relatively less attention to the resource allocation and income distribution aspects which are essential to optimize our economic performance, meet the great priorities of our national needs, and enlarge social justice.

League of Women Voters.

Facts and Issues, May 1970, "Revenue Sharing: The Three-Way Stretch." 4p.

A well balanced, popularized discussion of the revenue sharing issue.

Levy, Michael E. and Juan de Torres

Federal Revenue Sharing with the States: Problems and Promises. (New York: National Industrial Conference Board, 1970) 103p.

Reviews and analyzes revenue sharing within the framework of the U.S. system of multiple and overlapping governments, and in the light of two major recent revenue sharing proposals of the Advisory Commission on Intergovernmental Relations and the Nixon Administration. The study takes account of the existing system of intergovernmental aid, as well as the often conflicting requirements of equity, need, and administrative feasibility. Includes a brief review of the varying uses of revenue sharing by three foreign governments.

Nathan, Richard P.
"The Tax Sharing Approach." In *Federal-State-Local Fiscal Relationships; A Symposium:* 107-121 (Princeton: Tax Institute of America, 1968).

The case for tax sharing developed with emphasis on two main themes: first, the tax sharing idea must be seen in political as well as in economic terms; second, the tax sharing idea must be viewed in the broader post-Vietnam fiscal policy context in which it is but one of several competing alternative uses for a potential future "fiscal dividend."

Pechman, Joseph A.
"Money for the States," *New Republic,* Vol. 156, April 8, 1967: 15-17.

A rebuttal to opponents of revenue sharing, identified as conservatives who prefer tax reduction to better public services, and liberals and bureaucrats who believe that major decisions about public services should be made in Washington.

Perloff, Harvey S. and Richard P. Nathan, ed.
Revenue Sharing and the City. (Baltimore: published for Resources for the Future, Inc., by the Johns Hopkins Press: 1968) 112p.

Proceedings of a session of a conference on "Issues in Urban Economics." Participants were Walter W. Heller, Richard Ruggles, Lyle C. Fitch, Carl S. Shoup and Harvey E. Brazer.

"The Question of Federal Revenue Sharing with the States: Pro and Con," *Congressional Digest,* Vol. 48, No. 10, October 1969: 225-256.

Summarizes the history of federal-State fiscal relations, the recent history of the tax sharing concept, main features of the Administration's plan and alternative proposals, and the pro and con viewpoints on the question "Is Proposed Federal Revenue Sharing with the States a Sound National Policy?"

Republican National Committee. Task Force on the Functions of Federal, State and Local Governments.
Financing the Future of Federalism: The Case for Revenue Sharing. (Washington: 1966) 9p.

Offers proposals designed to meet two objectives: to provide for the States and their localities a steady source of funds with which to meet public demands for governmental services, and one which will grow more or less proportionately to increases in the gross national product; to free the States and local governments from the maze of regulations, paperwork, red tape, and restrictions which hamper them in their efforts to serve their citizens.

Reuss, Henry L.
Revenue-Sharing: Crutch or Catalyst for State and Local Governments? (New York: Praeger, 1970) 170p.

Describes Congressman Reuss' plan for unrestricted block grants, with one big string—that the States themselves prepare for their own financial and organizational modernization and that of their local governments.

Robinson, William H.
"Revenue Sharing and Creative Federalism—Some Perspectives." In *Federal-State-Local Fiscal Relationships; A Symposium:* 149-171. (Princeton: Tax Institute of America, 1968)

Contends that revenue sharing has emerged from the misty realms of fiscal theory into the harsh light of political reality and examines it in that light.

Tarr, David R. and Harley H. Hinrichs.
"Nixon Revenue Sharing Plan Faces Major Obstacles in Congress," *National Journal,* Vol. I, December 20, 1969: 403-409.

Analyzes the political and economic effects of fiscal federalism alternatives, identifies opposition and support, and evaluates the chances for congressional action.

Turnbull, H. Rutherford III
"Federal Revenue Sharing," *Maryland Law Review,* Vol. XXIX, 1969: 344-376.

Attempts to explain revenue sharing, illustrate how it might work with respect to the States, using Maryland as an example, and call attention to some noteworthy legislative trends and proposals, focusing particularly on problems of "pass-through" to local governments.

U.S. Advisory Commission on Intergovernmental Relations.
Fiscal Balance in the American Federal System. (Washington: Government Printing Office, 1967) 2 vol.

Describes the size, shape and significant features of fiscal federalism; the development and present operation of the fiscal grant-in-aid system; and fiscal disparities among local governments within metropolitan areas. Recommends greater fiscal flexibility in Federal aid programs through grant consolidation and general support payments; strengthening State and local fiscal and tax systems; reducing disparities in educational financing; and greater involvement of private enterprise in urban programs.

U.S. Congress. Joint Economic Committee. Subcommittee on Fiscal Policy. *Revenue Sharing and Its Alternatives: What Future for Fiscal Federalism?* Hearings before the... (Washington: Government Printing Office, 1967) 194p.

Hearings designed to study and evaluate revenue sharing in the context of being one of many alternative means to deal with a changing array of problems facing the Federal, State, and local governments. Alternative means that have been suggested include revenue sharing, improved or consolidated Federal categorical grants, Federal tax programs, such as for model cities, and the negative income tax or family allowances. The purpose of the hearing is to take a broad and deep view of the policy alternatives and what "policy mix" may be most effective.

U.S. Congress. Senate. Committee on Government Operations. Subcommittee on Intergovernmental Relations.
Intergovernmental Revenue Act of 1969 and Related Legislation; Hearings. (Washington: Government Printing Office, 1970) 379p.

Hearings on legislation designed to redress fiscal imbalance by (1) supplementing the tax base of State and local governments through a system of Federal general payments and (2) encouraging State and local governments to adopt strong tax systems of their own by establishing Federal tax credits for State and local income and estate taxes. Testimony by William G. Colman emphasizes that revenue sharing and Federal tax credits for State income tax payments are both necessary and interrelated components of a well-balanced Federal aid system.

U.S. Library of Congress. Legislative Reference Service.
Resolved: That the Federal Government Should Grant Annually a Specific Percentage of Its Income Tax Revenue to the State

Governments; A Collection of Excerpts and Bibliography Relating to the Intercollegiate Debate Topic, 1969-70. (91st Congress, lst session, House Document No. 91-158) (Washington: Government Printing Office, 1969) 136p.

Historical background as well as articles examining both the pro and con on this subject and items suggesting alternative approaches to the fiscal problems of the States.

Weidenbaum, Murray L. and Robert L. Joss.
"Alternative Approaches to Revenue Sharing: A Description and Framework for Evaluation," *National Tax Journal,* Vol. XXIII, No. 1, March 1970: 2-22.

Compares five well-known revenue-sharing plans, which together contain most of the features which have been suggested for incorporation into such a proposal. Provides a framework for identifying and evaluating the primary variables in each revenue-sharing proposal.