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NINETY-SIXTH CONGRESS

FIRST SESSION

JUNE 28, 1979

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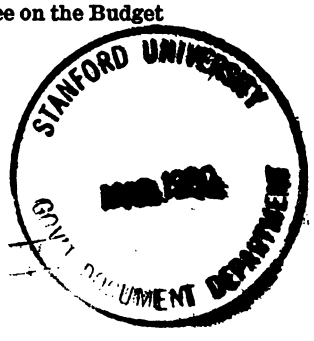

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JUNE 28, 1979

HOUSE OF REPRESENTATIVES,
TASK FORCE ON BUDGET PROCESS
AND
TASK FORCE ON STATE AND LOCAL GOVERNMENT,
Washington, D.C.

The task forces met, pursuant to notice, at 9:30 a.m., in room 2200, Rayburn House Office Building, Hon. Elizabeth Holtzman, chairwoman of the Task Force on State and Local Government, presiding, and Hon. Norman Mineta, chairman of the Task Force on Budget Process.

Ms. HOLTZMAN. This morning the Task Force on State and Local Government and the Task Force on Budget Process are holding a joint hearing on H.R. 3697, the State and Local Government Cost Estimate Act.

This bill is designed to protect hard-pressed State and local governments from the unanticipated and unexpected fiscal hardships resulting from Federal legislation by requiring the Congressional Budget Office to provide estimates of these costs when the bills are reported by congressional committees.

This is a period of great economic uncertainty for State and local governments, when inflation and recession are eating away at their ability to maintain essential services, such as police and fire protection, education, and maintenance of capital infrastructure. At the same time, the level of Federal support for State and local governments is also being closely reexamined. In the First Resolution for Fiscal Year 1980, for example, aid to State and local governments will decrease in real terms by approximately 3 to 5 percent if inflation continues to skyrocket at its current annual rate of 12 percent or more. It would be irresponsible for the Federal Government to impose additional fiscal burdens on these governments at the same time that their support is being cut back.

As Chair of the Budget Committee's Task Force on State and Local Government I have seen first hand the costs of Federal legislation for State and local governments. I feel strongly that Congress ought to know what these costs will be before making decisions on pending legislation but, at present time, there is no mechanism for learning them. H.R. 3697 will provide this much needed information routinely, allowing Congress to act with full knowledge of the likely consequences of its actions.

I would like to thank Congressman Mineta, who ably chairs the Task Force on Budget Process, for agreeing to hold this joint hearing today. He has been concerned with the costs of federally man-

dated programs for State and local governments for some time and I am happy to have his assistance and support.

Mr. MINETA. Thank you very much, Madam Chairperson. Along with Congresswoman Holtzman, I would like to welcome the witnesses and express my gratitude for their willingness to appear before us today.

I would also like to take this opportunity to thank Ms. Holtzman for the excellent work she has done on H.R. 3697 and for the efforts she has made in exposing the issue of federally mandated costs imposed on State and local governments.

As communities try to cope with inflation, growing demands for services and dwindling revenue sources, we here on the Federal level must be much more cognizant of the intergovernmental ramifications of our legislation.

While there has been considerable discussion over the past few years concerning the issues of Federal constraints on locals, I am afraid analysis has been short and rhetoric long. Enactment of a bill such as H.R. 3697 will better equip us to undertake detailed analysis rather than rhetorical speculation.

As a former mayor, I have experienced the Federal-local relationship from both ends. I must say, a description I once heard of Washington from a local comedian strikes a sympathetic chord: "It's like 10,000 ants floating downstream on a log, and every one of them thinking he is steering."

The Federal grant-in-aid system is a little like that: 10,000 Federal programs trying to steer local governments in 10,000 different directions. And the cost of that chaos is borne in large measure by local officials.

It seems ironic that after the decade of "New Federalism" and consolidated block grants that we must once again raise the issue of excessively compartmentalized arrays of Federal programs.

I am not taking issue with the nearly 490 categorical grant programs, but simply with the fact that no matter how justifiable they are individually, collectively they present an unworkable and confusing mass of programs, each with its own conditions and requirements and deadlines.

I will be interested to hear from the witnesses today with their views about the impact of the myriad and often contradictory Federal requirements that accompany Federal aid in many instances. Thank you, Madam Chairperson, for this opportunity to have this joint hearing.

Ms. HOLTZMAN. Thank you, too, Mr. Mineta.

It is my pleasure to welcome as our first witness James A. Brigham, Jr., director of the Office of Management and Budget of New York City. Mr. Brigham has the distinction of being the youngest budget director in the history of the city of New York. He was one of the principal architects of New York's financial plan that was instituted in January 1978 and, therefore, has played a major role in helping New York City recover from severe fiscal difficulties.

STATEMENT OF JAMES R. BRIGHAM, JR., DIRECTOR, OFFICE OF MANAGEMENT AND BUDGET, CITY OF NEW YORK

Mr. BRIGHAM. Madam Chairwoman, Congressman Mineta, Congresswoman Holtzman, I am James R. Brigham, director of the Office of Management and Budget for the city of New York.

I am grateful for the opportunity to testify before you on the State and Local Government Cost Estimate Act of 1979.

I have a prepared statement that I would like to submit for the record.

Ms. HOLTZMAN. Without objection, it will be included in the record in its entirety.

Mr. BRIGHAM. I would like to touch on some of the highlights in that area.

The national thrust to balance budgets must take account of the complex interaction among Federal, State and local governments. The objective is a sound one, to contain the cost of Government and match recurring expenses with recurring revenues. But it is wrong for one government to balance its budget simply by passing costs along to others and it is wrong for higher levels of government to mandate programs, however worthy their objectives, and not fund them.

It is vital that the Congress and the executive branch understand the implications of their actions on State and local governments in order to make informed decisions on proposed legislation.

The bill before you would require the Congressional Budget Office to supply estimates of the State and local costs of every bill reported out of committee. This type of data is already supplied on the Federal costs of these bills. Together these two estimates will improve each Representative's understanding of the legislation which will require his or her vote.

Let me turn to a brief discussion of the costs imposed on the city by the Federal Government.

First, as an overview, New York City receives approximately $2½ billion or 20 percent of its revenues from the Federal Government.

The great bulk of these revenues is associated with categorical aid, that is to say, welfare and medicaid, where we spend roughly $1 to get 50 cents in Federal aid.

The more difficult and expensive programs—the Federal level are not necessarily cost reimbursed but are mandated programs, and I would like to discuss a few of these and their costs.

First, a series of Federal laws relating to the environment and the protection of water supply requires certain standards to be maintained in the city's water system.

In New York City this has meant that water pollution control plants had to be constructed over the past decade or so, and the cost of these plants has been in excess of $2 billion; 75 percent of these costs were reimbursed by the Federal Government, but the State and city split the remaining costs or roughly $500 million.

The operation and maintenance costs of those plants today are in excess of $38 million per year. None of these costs are reimbursed by the Federal Government.

In total the State and city have increased $500 million of capital in these plants and, given itself $38 million in expense costs and

counting the cost of capital, we are spending more than $55 million annually in our expense budget to maintain these plants and pay for the cost of capital of constructing them.

An additional environmental act that affects the city is the Marine Protection Research and Sanctuaries Act that requires cities to cease the practice of dumping sewage sludge into the ocean by December 31, 1981.

This deadline was set in an amendment passed in 1977 and many cities are rushing to comply with it.

The result for New York is to find the quickest possible alternative solution to the sludge disposal problem. Four years simply is not enough time to design and construct a facility that will correct this problem in the long term.

Thus we have to develop two plants to comply with the act, one an interim plan which is not the most cost-effective plan we could have and a longer term plan. If the deadline were delayed, we could work toward a more cost-effective system.

The cost of the arbitrary deadline will be that we will have to develop two separate systems each costing us approximately $250 million in capital expenditures.

Again, the Federal Government will reimburse the city for 75 percent of these costs, and the city and State will split the remaining amount.

However, we estimate, and it's only an estimate, but we do include it in our financial plan that the operating costs of these facilities will amount to $37 million a year and again none of these costs will be reimbursed by the Federal Government.

Then, given our capital investment of $125 million, we will be experiencing recurring annual costs of $42 million, which include the operating costs plus the cost of capital.

Another example is the Education for Handicapped Children Act of 1975. That requires that all handicapped children receive special instructions in schools receiving Federal funds. In New York City in our 1979 budget we are spending $171 million of that program of which $22 million is reimbursed by the Federal Government. If you add these three programs that I have just mentioned, and there are others, the city has a total of $247 million of recurring annual expense budget charges as a result of just these three programs.

An additional example that we have not been able to estimate our operating costs yet, is section 504 of the Rehabilitation Act of 1973 requiring that the handicapped not be excluded from any program receiving Federal assistance.

With respect to our mass transit system, we estimate total capital investment of between $1½ billion and $2 billion to comply with this program. These are just a few examples, as I said.

An additional benefit of the proposed legislation would be that it would improve our access to data necessary for us to estimate the cost of legislation and to estimate our own budget and financial plans. New York City, as you are probably aware, engages in an extensive budgetary planning process, including a complete 4-year projection of revenues and expenses, and this legislation would help our planning enormously.

It would be even more helpful if the local cost figures were broken down by States, regions, or localities. I would like to suggest

that your bill require such a breakdown, although I do recognize it would be difficult to do.

Actually, we would like to see these figures incorporated into the annual Federal budget process in order to assist all local governments in preparing their own budgets. To summarize, I would like to reiterate my support for the intentions of this bill.

We think that a fully informed Congress insures a more knowledgeable debate and decision. This bill strives to make the cost of Federal mandated programs known to Congress and to localities before votes are cast, and I believe ultimately that the legislation would reduce the total cost of Government. Thank you.

[The prepared statement of Mr. Brigham follows:]

PREPARED STATEMENT OF JAMES R. BRIGHAM, JR.

Congresswoman Holtzman, members of the House Task Force on State and Local Government. I am James R. Brigham, Jr., Director of the Office of Management and Budget for the city of New York. I am grateful for this opportunity to testify before you on the State and Local Government Cost Estimate Act of 1979.

The national thrust to balance budgets must take account of the complex interaction among Federal, State and local governments. The objective is a sound one—to contain the cost of Government and match recurring expenses with recurring revenues. But it is wrong for one government entity to balance its budget simply by passing costs along to others and it is wrong for higher levels of government to mandate programs, however worthy their objectives, and not fund them.

It is vital that the Congress and the Executive Branch understand the implications of their actions on State and local governments in order to make informed decisions on proposed legislation. The bill before you—H.R. 3697—would require the Congressional Budget Office to supply estimates of the State and local costs of every bill reported out of committee. This type of data is already supplied on the Federal costs of these bills. Together these two estimates will improve each Representative's understanding of the legislation which will require a vote. I am wholly in support of this effort.

I would now like to discuss certain costs imposed on the city by the Federal Government. New York City receives funds from the Federal Government in both categorical grants-in-aid and unrestricted aid. The following is a summary of estimates of Federal funds to be received in the city's fiscal year 1980. These figures may change depending upon the level of Federal appropriations now being considered in Congress:

Federal categorical grants in aid

CETA	$384,000,000
Community development	237,000,000
Welfare	1,005,000,000
Education	300,000,000
Other	122,000,000
Federal unrestricted aid:	
Revenue sharing	293,000,000
Other	22,000,000

Thus, approximately $2.5 billion, or 20 percent, of the city's total revenues are from the Federal Government. The great bulk of these revenues are associated with mandated programs and costs. The importance of a CBO analysis of the local cost impact of proposed changes is best illustrated by the following examples:

1. A series of Federal laws, such as the Clean Water Restoration Act, the Water Pollution Control Act, the Clean Water Act, the National Pollution Discharge Elimination System, and others, require certain standards be maintained in our water system. In New York City this has meant that water pollution control plants had to be constructed. The costs of building these plants were in excess of $2 billion; 75 percent of these costs were reimbursed by the Federal Government; the State and city split the remaining costs. The operation and maintenance costs of these plants are in excess of $38 million per year; none of these costs are reimbursed by the Federal Government. In total figures, the State and city were required to pay $500 million for the capital costs of these plants, and $38,634,000 per year in expense costs.

2. In addition to the laws I just mentioned, the Marine Protection, Research and Sanctuaries Act requires cities to cease the practice of dumping sewage sludge into the ocean by December 31, 1981. This deadline was set in an amendment passed in 1977 and many cities are rushing to comply with it. The result for New York City is to find the quickest possible alternative solution to the sludge disposal problem. Thus we are developing two plans to comply with this act: An interim plan which is not the most effective long-term solution, and a permanent solution. If the deadline was delayed we could immediately work toward the most efficient means of resolving this problem.

The cost of this arbitrary deadline will be to develop two separate solutions, each amounting to approximately $250 million in capital expenditures. Again, the Federal Government will reimburse the city for 75 percent of these costs; the city and State will split the remaining amount. This double effort will cost the city and State approximately $125 million in capital costs in the next years.

3. Section 504 of the Rehabilitation Act of 1973 provides that the handicapped will not be excluded from any program or activity receiving Federal financial assistance. In New York City alone, it is estimated that improvements to our transportation system will cost between $1.5 billion to $2.5 billion in capital expenditures. Spread over 30 years with an anticipated 7 percent inflation rate, this figure amounts to $9.6 billion. We expect that some of this money will be reimbursed by the Federal Government. Because the regulations have just been completed it is impossible to predict the amount borne by the city alone.

4. The Education for All Handicapped Children Act of 1975 mandates that all handicapped children receive specialized instruction in schools receiving Federal funds. In New York City's fiscal year 1979 budget, this law required the city to spend $171.3 million. Of that amount $22.2 million or 13 percent was reimbursed by the Federal Government.

These are just a few examples of the local cost estimates incurred from Federal laws which Congress may have been unaware of at the time it voted on them.

An additional benefit to States and localities of H.R. 3697 would be to improve our access to data necessary for localities to estimate local costs of Federal legislation. This is especially necessary for cities such as New York which must approve its budget before the Federal budget is finalized. The local cost estimates by the Congressional Budget Office of each piece of legislation would become an important part of the information we would use when projecting our revenues and expenditures for the coming fiscal year. The city, as you are probably aware, engages in an extensive budgetary planning process, including a complete 4-year projection of revenues and expenditures, and the proposed legislation would help our planning enormously.

Although I have indicated my strong support for the intention of this bill there are specific features of it which cause some concern. The bill states that these local cost estimates should be available to Congress for every bill reported out of committee immediately upon passage of this bill. CBO has stated that it took approximately 2 years to develop a fully operationalized Federal cost estimates division; we must assume that it would take at least as long to develop similar capabilities for estimating local costs. Yet, during this time H.R. 3697 requires that such data be made available to Congress.

I suggest that H.R. 3697 be changed to require local cost estimates when the Congressional Budget Office is fully capable of generating the necessary data. Considering the experience of CBO when developing the Federal cost estimate division, we suggest the bill read, "this act shall apply with respect to bills and resolutions reported by committees of the House of Representatives and the Senate 2 years on or after the date of enactment of this act."

As I stated above, the total local cost figure will be useful to local fiscal officers in developing their own budgets. It would be even more helpful if these aggregate figures were broken down by States, regions, or localities. I suggest that your bill require such a breakdown. Eventually we would like to see these figures incorporated into the annual Federal budget process to assist us in projecting our annual estimates for Federal aid.

In sum, I would like to reiterate my support for the intentions of this bill. A fully informed Congress ensures more knowledgeable decisions. In the past, many Federal mandates have imposed unsuspected costs on States and localities. This bill strives to make these costs known to Congress before votes are cast.

Ms. HOLTZMAN. Thank you very much, Mr. Brigham. You mention on the second page of your testimony that about 20 percent of the city's revenues are from the Federal Government.

Can you give any estimate of what percentage of the costs mandated by the Federal Government are not paid for by the Federal Government?

Mr. BRIGHAM. That is——

Ms. HOLTZMAN. And can you give a dollar figure for that as well?

Mr. BRIGHAM. Let me just say I don't have a specific estimate for the question that you have asked. However, in the examples I gave, I had mentioned more than $250 million of mandated costs that we are paying. These are probably the most significant examples of that.

I don't include in that the cost of welfare and medicaid, which are to the city in excess of $1 billion a year in local city funds.

So if you would include those programs we are easily well over $1 billion in mandated costs that the city is absorbing. There are other examples, and I would be happy to supply the committee with a more complete list.

Ms. HOLTZMAN. Thank you. Is it your opinion that if the Congress were to make such cost estimates available to its Members before they voted on legislation, we would be more sensitive to the costs imposed on State and local government and possibly alleviate such burdens?

Mr. BRIGHAM. I think so, and it would make all of us focus on the cost of many of these programs that are quite desirable, but since the costs are not costs to the Federal Government they are often ignored.

They are ignored not only with respect to State and local governments but the private sector as well, and I think that a more informed debate would take place on these programs if the costs were known and disclosed.

Ms. HOLTZMAN. At the end of your testimony you suggest that the bill be amended so that it does not take effect until 2 years after the date of enactment, since you claim that the Congressional Budget Office might have some problems in gearing up adequately to fulfill the role mandated by H.R. 3697.

Perhaps you are not aware of the fact that the legislation proposed amends section 403 of the Budget Act which we begin with the phrase: "The Director of the Congressional Budget Office shall, to the extent practicable, prepare for each bill or resolution the following information."

Mr. BRIGHAM. I was not aware of that. That would seem to cover that need, but we were aware of the difficulty in complying in a short period of time.

Ms. HOLTZMAN. Wouldn't the existing legislation cover the problem that you raise?

Mr. BRIGHAM. It would.

Ms. HOLTZMAN. Thank you very much. I have no further questions. Mr. Mineta.

Mr. MINETA. Thank you. Mr. Brigham, thank you very much for your very fine testimony and your experience in New York City.

Having drawn on New York City's experience in the past—we brought James Cleveland, who had been a former member of the OMB of the city of New York when I was mayor of San Jose—so we relied on your experience in New York.

I am wondering to what extent—because some of these measures are goals we all want to achieve, Clean Water Act, trying to get to clean, swimmable, and drinkable water and by the same token, they are good objectives—having this kind of a requirement, do you think that this will be more a learning curve for the Members of Congress about what the impact of the legislation will be on local government, and if that is the case, do you think that some of these measures might not pass because of the knowledge of that impact on local govenment?

Mr. BRIGHAM. I think it's possible that some of them might not pass, but I think also that it might result in the setting of more realistic objectives, more affordable objectives, and more reasonable timetables. I think the example on ocean dumping that I gave is a good one, because the amendment that was passed in 1977 required an operating plant insistent to be in effect only 4 years later, and that was at a time when technology simply was not available to meet the desires of the legislation.

I think any of us who are familiar with the capital construction process, as well as the complexities of engineering and designing a facility like that, would recognize that that was simply an unrealistic timetable, and the result is that the city really will be paying twice for a system, one, a temporary one that we know is not going to be adequate to do the job over the long term, and another, a longer term facility that may take a decade or more to bring into full effect.

I think, therefore, that the result may be the setting of more reasonable standards, the avoidance of duplicative efforts, and the avoidance of setting standards that simply are not cost-effective for the goal that is desired.

Mr. MINETA. What if we are to go along this line, whether or not we should really step back and try and figure out what our local responsibilities are, our State responsibilities, and where can the Feds fit in? What kinds of program areas should we be involved in that mandate certain things at the local level? Do you think that that is something that we ought to also be getting into?

Mr. BRIGHAM. I think that that certainly would be part of the debate that would be the result of focusing on these costs of mandated programs.

Special education is a good example of a very worthy objective which is very expensive to New York City. We have added in the last 2 years 2,000 teachers to our payroll to meet the goals of special education, and I think that in large part the needs of the handicapped are a Federal responsibility, and I think that that is an issue that would have been raised earlier if the Congress had focused on the cost of that mandated program. Pollution control is another example wherein the private sector——

Mr. MINETA. In the case of Public Law 94-142, the aid for physically handicapped, the education for the physically handicapped, are you saying that that should have been 100 percent because that ought to be a Federal responsibility?

I think under our present law it's 14 percent or maybe 12 percent. Yesterday we tried to get that jacked up to 14 percent on the bill on Labor, HEW with an appropriation bill but didn't make it,

but I am wondering, how would you even determine what would be the reasonable local share of some type of program?

Mr. BRIGHAM. I don't think it's reasonable to have a 100-percent reimbursed program, because then there is no incentive on the local government for cost control. I think you need that incentive.

On the other hand, 12 percent funding, given the significance of this program and the cost of it, is too low, and I think that roughly in the 50-percent range or so is a reasonable sharing of the cost and the responsibility of the program. But I think it's important to maintain a local share in order for the incentive to control cost.

Mr. MINETA. What about more block grant type programs in contrast to the categorical type programs? Would that help?

Mr. BRIGHAM. Grant programs would help, I think, more so than categorical programs, and I think it would result in the ability of the Federal Government to contain its own costs, because many local governments are under the delusion that it is effective to spend more money to bring more Federal dollars into their areas.

The city of New York has discovered it cannot afford to do that, but there is a tendency to, I think, for local governments to spend more money in categorical programs because of the automatic reimbursement of costs, and I think that block grant programs are probably more cost-effective for the Federal Government as well as for local governments in giving them more discretion on how to spend the money.

Mr. MINETA. And from a Federal perspective, it costs us less to administer the block grants. Thank you very much, Mr. Brigham. Thank you, Madam Chairwoman.

Ms. HOLTZMAN. Mrs. Holt.

Mrs. HOLT. Thank you very much, Madam Chairman. I appreciate the testimony of the gentleman and appreciate your holding these hearings. I think we are moving in the right direction to solve some of the problems that we have created here.

We have been talking around my concern and the chairman of the Budget Process Committee, Mr. Mineta, has touched on it.

We are now getting pressures from States to balance our budget. The legislatures tell us to get our shop in order while many States have surpluses. We are finding this out.

What if we reduced Federal taxation and permitted the States to raise more of their own money? Do you think that this would ever be an acceptable concept in New York?

Mr. BRIGHAM. No one likes to raise taxes.

Mrs. HOLT. Right.

Mr. BRIGHAM. I think that from our point of view in the city, we have about $8 million of revenue that are what we consider to be unrestricted revenue that we can use to support local services.

About $3 billion, actually $4 billion of that are local taxes that are sensitive to the economy and to inflation and, therefore, grow with our costs.

We also have a real estate tax that is relatively static; that is, it does not grow much. Then we have some unrestricted and Federal aid that has stayed relatively constant, largely revenue sharing.

Our experience and certainly looking at the Federal budget, Federal revenues benefit much more from an economic flow and inflation generally than local revenue sources do.

Certainly that is the experience of New York, and we in the city would be much more responsive to a larger revenue sharing program that grows with inflation because our own revenue sources do not grow with inflation entirely.

I think that the revenue sources of the Federal Government would enable the Federal Government to continue and expand such a program.

Mrs. HOLT. But ultimately it's the taxpayers' money that we are taking, and as we try to decide the responsibility of each level of government, it just seems to me that it's self-defeating when, as you say, we create the inflation here and then continue to provide for the inflation. If somehow we could mandate policy and take this into consideration—including how much it's going to cost to implement it—and then leave the provision for local jurisidictions to raise the necessary revenue would you feel that we should continue to tax people because it's easier to do? Is that correct?

Mr. BRIGHAM. Not exactly, but I do think that local governments generally and it varies, of course, widely, especially if you look at some of the major industrial cities, their revenue sources simply are not capable of supporting the kind of increased revenues that would be required, and I think that what may result is a continued deterioration of major central cities by imposing a requirement for them to raise additional tax sources.

Mrs. HOLT. Thank you.

Ms. HOLTZMAN. Any further questions? Mr. Mineta.

Mr. MINETA. No further questions.

Ms. HOLTZMAN. I want to thank you very much, Mr. Brigham, for your very fine testimony and presentation here this morning. It has been very helpful to both task forces.

Mr. BRIGHAM. Thank you.

Ms. HOLTZMAN. The next witness is a resident of the district of the chairman of the Budget Process Task Force who, I am sure, would like to introduce her.

Mr. MINETA. Thank you very much. If I might have this opportunity to introduce to the members of the committee Jane Decker, director of intergovernmental relations, Santa Clara County, Calif.

I have had the honor of knowing Ms. Decker for probably 12 to 15 years when she was starting out as an activist at the community street level, so to speak, and then slowly became involved in local governmental affairs, having the opportunity to work as the administrative assistant to a State senator from our area.

Frankly, I am really pleased to see Jane Decker here, because I just know from her own background and her experience with State government, tying it in with her experience of being very active as a community worker, as a volunteer at the local level, she brings to us a great deal of wealth and background and experience, and our panel will benefit from her testimony.

STATEMENT OF JANE DECKER, DIRECTOR OF INTERGOVERNMENTAL RELATIONS, SANTA CLARA COUNTY, CALIF.

Ms. DECKER. Thank you, Congressman Mineta. Good morning, Madam Chairperson and members.

I am Jane Decker representing Santa Clara in California. I have some very brief written testimony, and I would like to supplement it with a few remarks.

Ms. HOLTZMAN. Your statement will be included in the record in its entirety.

Ms. DECKER. Thank you. We support the spirit and intent of H.R. 3697. I know you don't have to be convinced of the importance of examining the impact on local government of decisions made by Congress.

Many Members of Congress are products of local government and are well aware of the problems inherent in mandating programs without sufficient knowledge of their fiscal impact on the body that implements them.

One small example is the change in CETA regulations recently that has actually affected the county of Santa Clara more adversely than proposition 13. The cost of absorbing 600 CETA people would be about $5 million to the county.

Rather than citing other specific instances of burdens imposed on local government, let me say instead that local government does not want to be in an adversary position but rather to work with you to implement the policies that you adopt. The resistance only appears when local government feels taken advantage of with regard to hidden mandated costs.

Recognizing that these same problems existed with State policies, in 1972 California enacted S.B. 90, which required the State department of finance to determine any local government cost associated with State legislation.

The intent was to prevent the State from passing legislation which would impose new costs on local government.

Mandated local programs are to be funded by the State unless a disclaimer is provided within the legislation. There are various kinds of disclaimers, but the most troublesome to local government is the one that recognizes that local costs exist but chooses to exempt the bill from the reimbursement provisions of S.B. 90.

The hearing board was established and recently strengthened to hear appeals from local governments on this substantial number of disclaimers. The board is able to appropriate reimbursement funds, if necessary.

I would think that this might be an appropriate mode for you to consider also with respect to this legislation. Again, we applaud your intentions with regard to H.R. 3697 and I would be happy to answer any questions that you may have.

[The prepared statement of Ms. Decker follows:]

PREPARED STATEMENT OF JANE DECKER

It would be foolhardy for local government not to support H.R. 3697. As written it is a "motherhood and apple pie" offer.

Local government is impacted by Federal legislation in at least two ways. First, as consumers we are significantly impacted by such increases as postal rates or the deregulation of petroleum with its resultant increase in fuel costs. Second, we are impacted as a Government agency charged with the administration Federal regulations or impacted by the elimination of funding for programs, such as CETA or health programs originally established as the result of Federal funding.

In 1972 the State of California enacted S.B. 90, which required the State government to determine any local government costs associated with State legislation. Mandated local costs are to be funded by the State unless a disclaimer is provided within the legislation. As you can well imagine the number of disclaimers is

substantial, thus a hearing board was established to review testimony from State and local government on the issue of the legislations' financial impact. The Board is able to appropriate funds if necessary. I would hope that a similar mode would be adopted when implementing H.R. 3697.

We support the spirit of H.R. 3697 and look forward to its passage.

Ms. HOLTZMAN. Thank you very much. Mr. Mineta.

Mr. MINETA. Thank you very much, Madam Chairperson. First of all, let me ask, when was this hearing board established?

Ms. DECKER. That was a part of the legislation that created S.B. 90. It was strengthened through legislation about 2 years ago when it found that it was not working as well as it could.

Mr. MINETA. It says that the hearing board has the ability to appropriate funds, if necessary. Is this a board made up of members of the State legislature?

Ms. DECKER. No; it is a board of control of which there are three members and they are not members of the legislature. They hear testimony from State and local government with regard to the issue and then can direct the legislature to appropriate money.

I will say this, that the counties have felt that the board has not been entirely supportive of their appeals. We feel that they do not in fact always receive the reimbursement that they should. It's an ongoing problem.

Mr. MINETA. The problem is most pieces of legislation that might have some impact on local government have this boilerplate language in there that talks about this disclaimer.

What has been the experience of this hearing board in terms of number of applications received, the numbers of dollars that might be involved, and how much has the board itself appropriated to relieve the local government of some of these mandated costs?

Ms. DECKER. I don't have that specific information, but I will be happy to get that for you. I know in 50 percent of the legislation there is this disclaimer or boilerplate, as you refer to it, but I don't know of those cases and how many are actually reimbursed.

Mr. MINETA. If it's possible for you to get those figures of the experience of that hearing board that would be most helpful to us as well.

[At time of printing, the information had not been supplied.]

Mr. MINETA. Has S.B. 90 itself slowed down legislation that might impact on local government and/or has it heightened the knowledge of the members of the State legislature about legislation that might adversely impact on local government financially?

Ms. DECKER. Very definitely. The major impact it has had is it has forced members of the legislature to consider the impact on local government, and instead of mandating many programs, many have become permissive as opposed to being mandated. If they do not desire to put the funds into legislation, the choice is fund it or make it permissive.

If the cost is too great for the State to provide the funds, then they feel that the appropriate manner is to make the legislation permissive.

Mr. MINETA. Has there been more legislation to absorb those costs or has there been, as you say, the direction to go to permissive?

Ms. DECKER. I think it's a combination. Many conscientious legislators would not dream of putting a disclaimer in a bill with substantial cost, that they would either provide the money which forces them to prioritize and to determine whether the program is in fact that valuable or make it permissive.

Mr. MINETA. Has proposition 13 impacted on this process?

Ms. DECKER. Absolutely; in fact there have been very few in the past year in California, very few programs, and I don't think anyone would consider putting in or mandating a local program now without providing the cost, the reimbursement. It's just not possible now.

Mr. MINETA. Because of the State surplus, has there been more of an assumption of some of these mandated costs?

Ms. DECKER. No; the State surplus has mainly been used this past year as a bailout tool.

The first year it was given to local government in the form of block grants, and some actual, I guess, on the part of the counties anyway, they did assume some of the county costs that had formerly been picked up by the counties.

On the whole, it was more in the form of block grants rather than specific assumptions, but I think that in the future they will probably go toward assuming some of these costs.

Mr. MINETA. Is there more of a demand or organized effort on the part of local government, because of proposition 13, to get State legislative programs and then also thereby to have the State pick up more of these costs?

Ms. DECKER. Absolutely.

Mr. MINETA. Other than the block grant through the use of the State surplus, are there more categorical type programs?

Ms. DECKER. There is a division. I think actually people would prefer, you know, block grants on one hand, and yet certain of the counties would prefer assumptions of the social services cost in its entirety.

We are also facing in California, which I know you are aware of, a possible spending limitation which is making local government desire the State to pick up a lot of these programs, so it's charged off to their spending limitations rather than local governments, when the limtiation does pass which it probably will either in the fall or next spring.

There is also a possible income tax limitation, so there may not be any money at all to provide for any programs. We are in a state of dismay and chaos, I think, to some extent.

Mr. MINETA. You said wherever the Nation goes, California will get there first.

Ms. DECKER. Unfortunately; we will let you know how it feels.

Mr. MINETA. That has been our experience with gasoline. We have managed to transfer it to this area. Thank you very much, Ms. Decker. We appreciate it.

Ms. HOLTZMAN. Mrs. Holt.

Mrs. HOLT. Thank you for coming. We don't want to let you get away without a little more questioning.

Do you think that we should go further in H.R. 3697? You say that you support the spirit of H.R. 3697, so I detect there that you think it should have a little more to it.

Ms. DECKER. Of course, the difference between this measure and the S.B. 90 process, your process, you are not guaranteeing reimbursement in this measure.

Mrs. HOLT. Do you think we should do it?

Ms. DECKER. How could I say otherwise? I realize that that is probably impossible, and I think the first step is at least realizing the value of analyzing the impact and sometimes it's not even costs which are sometimes minimal to local government but having the knowledge that there will be cost rather than having it suddenly determined at the last minute.

Mrs. HOLT. It would slow down the legislation if it did produce the money. Maybe it would slow down the legislation if it didn't produce the money.

Ms. DECKER. Yes.

Mrs. HOLT. Thank you, Madam Chairman.

Ms. HOLTZMAN. Has there been any serious difficulty under S.B. 90 in determining what the local governments' costs would be?

Ms. DECKER. There has been some. There is a local cost unit within the department of finance that routinely contacts local government budget people whenever a measure is introduced, so the estimates are actually coming from local government up to finance which makes a lot of sense.

I think that sometimes it's difficult, but they have been fairly accurate.

Ms. HOLTZMAN. Has it imposed an extraordinary burden on the State government in California to develop those local costs?

Ms. DECKER. I don't know the financial burden, how many more staff people they have needed, but everyone agrees it has been worth it.

Ms. HOLTZMAN. What would be the impact of not having S.B. 90 in California?

Ms. DECKER. I don't know the financial impact in terms of dollars, but I think that it has had an impact in making people aware of what new programs are going to cost local government.

Just a minor program, changing the street signs, can cost a very small city in the thousands of dollars, and they just don't have that kind of revenue available to them, so maybe some of the not so essential kinds of programs have been eliminated.

Ms. HOLTZMAN. So you think it has had a healthy effect in restraining the State's desire to mandate costly programs that are not essential to local governments?

Ms. DECKER. Yes; I do.

Ms. HOLTZMAN. Do you think it has had an impact in terms of getting the State to provide moneys for the implementation of mandated programs that it wouldn't otherwise have done?

Ms. DECKER. Absolutely. I think they are just not thinking in terms of offering new programs because of the process that it has to go through. It's assigned to a special committee to in fact hear the special problems associated with S.B. 90, with mandated costs, so we are insulating the issue and it is impossible to ignore, and it's embarrassing to be mandating very expensive programs without reimbursement.

Ms. HOLTZMAN. Do you think it has been helpful in getting extra money for local governments when mandated programs have gone into effect?

Ms. DECKER. Yes.

Ms. HOLTZMAN. Do you think the same results would happen if we did this on a national level?

Ms. DECKER. I think so. I would not like to see it used as an excuse to not provide worthy programs, but I think that it would have a very beneficial effect in just making everybody think.

Mrs. HOLT. Will the chairman yield? How about some unworthy ones?

Ms. DECKER. Of course, that is subjective. I realize that.

Ms. HOLTZMAN. But I think what the witness is saying, if I correctly understand her, is that if this legislation is passed, we will understand the full fiscal impact of programs and we may decide that some are really not important enough to require State and local governments to spend money on them.

Mrs. HOLT. Most of them are commendable.

Ms. HOLTZMAN. I have no further questions. Mr. Mineta.

Mr. MINETA. In California what agency determines these impacts on local government?

Ms. DECKER. It's the department of finance, and there is a local mandated cost unit that contacts local governments to get their estimates, so the estimates are coming from the governments that are affected.

Mr. MINETA. What role does the State legislative analysis officer play in that function, if any?

Ms. DECKER. I don't think he really plays a particular role. His analysis may be colored by the fiscal impact on local government that has been provided to him by the department of finance, but he doesn't really play a role in determining the costs.

He may decide that the program is valuable or not valuable based on that estimate that has been provided to him by local government.

Mr. MINETA. Or do they really more emphasize the cost impact on State government of any given piece of legislation?

Ms. DECKER. That is their main function.

Mr. MINETA. To finance through this local government to a unit, determine the impact of any State-passed legislation?

Ms. DECKER. That's right.

Mr. MINETA. I see. Fine; thank you very much.

Ms. HOLTZMAN. I want to thank you again for coming to testify.

Mr. MINETA. Would the chairperson yield for 1 minute? Not that I want our hearing to be impacted by Santa Clara County, but today I noticed in our office a very close friend of mine who is also a State court judge, the Superior Court of California, and I would like to introduce Judge Flaherty. It is great to have you here. We are being inundated by Santa Clara County today. They feel at home now here.

Ms. HOLTZMAN. We want to welcome you to the committee. Our next witnesses will be a panel composed of Stephen Farber, executive director, National Governors Association; Jack L. McRay, Washington director of the Council of State Governments; and John Bragg, chairman of the State-Federal Assembly, National

Conference of State Legislatures, and a member of the Tennessee General Assembly.

Gentlemen, we are very pleased to have you for the task force hearing.

Without objection, your testimony will be incorporated in the record in its entirety. We would appreciate your summarizing your testimony very briefly.

STATEMENT OF JACK L. McRAY, WASHINGTON DIRECTOR, COUNCIL OF STATE GOVERNMENTS

Mr. McRAY. I am honored to appear at the joint hearing today as a representative of the Council of State Governments, and to testify on behalf of H.R. 3697, the State and Local Government Cost Estimate Act.

To basically summarize I would like to point out that our executive committee very recently met in Coeur d'Alene, Idaho. At that executive meeting the attendees unanimously endorsed H.R. 3697, and at this time, Madam Chairman, I would like to offer this letter to you from the executive committee to have put on the record, if possible.

Ms. HOLTZMAN. Without objection, the text of the letter will be included in the record.

[The letter referred to follows:]

COUNCIL OF STATE GOVERNMENTS,
Washington, D.C., June 28, 1979.

Hon. ELIZABETH HOLTZMAN,
Rayburn House Office Building,
Washington, D.C.

DEAR CONGRESSWOMAN HOLTZMAN: The Executive Committee of the Council of State Governments, in conference at Coeur d'Alene, Idaho, on May 27, 1979, instructed me to send you a letter supporting your work on Federal mandates.

Particularly, the committee commends your introduction of H.R. 3697, which provides for congressional consideration of cost impacts of Federal legislation on State and local governments. That bill, if enacted, would be a major step toward responsible restraint in the imposition of costly and burdensome requirements on State and local governments.

The executive committee encourages early expansion of your legislative initiatives to provide similar restraint of Federal regulatory activity which compounds the general problem that you have addressed. In addition to the burdensome costs of administrative regulations, States are adversely affected by conflicting mandates issued by different Federal agencies, by delays and frequent changes in such issuances, and by the overburden of the regulatory mandates.

Please understand that the executive committee does not seek a halt of appropriate regulatory activity but it emphatically seeks the elimination of excesses which plague intergovernmental operations.

Governments cannot defend the cost, confustion, and intergovernmental conflicts produced by irresponsible or insensitive mandates, be they statutory or regulatory. Again, the Council of State Governments encourages and supports your efforts to improve the quality of Government.

Sincerely,

WILLIAM J. PAGE, Jr.,
Executive Director.

Mr. McRAY. H.R. 3697, to the members of the Council of State Governments, really brings focus to the Federal nature of the congressional legislative process. State governments recognize that Congress, under the Constitution, has a positive role to play in formulating national policy, but that power must be wielded with awareness of the impact of congressional actions on the other partners in our Federal system.

As you know, State and local impact analyses have not been required in the Federal legislative process, although they may be requested. But, at the same time, because of inflation, tax restructuring, State governments must now more than ever reevaluate their ability to undertake many projects.

In light of the proliferation of Federal statutory and regulatory requirements and consequent costs, the cost squeeze dilemma has become chronic for State governments.

The alternative for States, when they find that they are in noncompliance with laws because they cannot pay for them, is to not participate in federally mandated programs. Basically, when Congress passes statutes without adequate appropriations or when it conceives program objectives which cannot be met, it is my opinion that it does a disservice to the providers of direct services for programs, raises false expectations in those persons for whom the laws were targeted, and increases the disdain of the citizenry for Congress itself.

There are several acts which are examples of instances where States are having difficulty complying because of the enormous cost. Examples are section 504 of the 1973 Rehabilitation Act. Although technically voluntary for participation, because of the Federal funding involved there really is not a lot of choice.

Public Law 94-142 is another example where there are enormous difficulties for complete compliance. These are two examples of laws which cost States extraordinary amounts of money.

To be sure, Congress has addressed pressing needs, but had Congress, as a matter of course, analyzed the fiscal impact of its action perhaps better enabling legislation would have been forthcoming. Perhaps we would have seen legislation that was more realistic and which did not raise false expectations.

The Federal Paperwork Commission, for example, has estimated that in 1977 alone, simply the cost of the paperwork for State governments for Federal programs was $5 to $9 billion.

It also found that the paperwork was itself little more than a bureaucratic control mechanism, particularly concentrating on process rather than product. Control of process, no matter how extensive, is no guarantee for achieving the statutory purposes.

H.R. 3697 might not prevent the imposition of burdens, but it would let Congress know how much of a burden it imposes before, not after, the fact. This bill is particularly timely. There is likely to be less, not more, money in real dollars flowing to and within the States next year, especially in light of the reduced growth rate in the Federal expenditures projected by current budget resolutions for fiscal year 1980.

I think very importantly, this bill is not only a bill to focus attention on the impact on State and local governments, but I would stress to you that this is a congressional management bill. It provides Congress with an excellent tool for more effective oversight of congressional statutes and their Federal agency activity.

As a part of the legislative histories, the analyses could provide guidelines to the Federal agencies. If in fact programs under the enabling statute were proposed which had extraordinary cost, there would be at least some evidence that they were or were not considered to be part of the congressional intent.

Likewise for Congress, the converse would be demonstrable. If there were programs and mandates that were conceived and considered by the Congress that were not enacted or implemented by the Federal agencies, that also would be demonstrable.

In summation, I believe that H.R. 3697, if enacted, will provide an essential managerial oversight tool for Congress and will provide a vehicle for determining the fiscal impact of proposed national policies on State and local government.

In addition to improvement of congressional performance, you will provide encouragement to thousands of adversely affected State and local governments.

On behalf of the Council of State Governments, I urge speedy passage of this bill. Thank you for the opportunity to present my views.

[The prepared statement of Mr. McRay follows:]

PREPARED STATEMENT OF JACK L. MCRAY

I am honored to appear at this joing hearing today as a representative of the Council of State Governments (CSG), to testify on behalf of H.R. 3697, the State and Local Government Cost Estimate Act. If enacted, the law will amend the Congressional Budget Act of 1974 to require the Congressional Budget Office to prepare and submit to Congress estimates of the costs which would be incurred by State and local governments to carry out or comply with bills or resolutions reported in the House or Senate.

H.R. 3697 brings focus to the Federal nature of the congressional legislative process. State governments recognize that Congress, under the Constitution, has a positive role to play in formulating national policies—but Congress must wield that power with awareness of the impact its actions have on the other partners, the State and local governments within the Federal system.

The CSG executive committee (composed of State legislators, State executives and lieutenant governors, State attorneys general, and State chief justices), received Representative Holtzman's bill enthusiastically because the members perceive the bill as a step by the Federal Government to adopt within its legislative process a management tool which the majority of State legislatures and executive branches have employed to protect local governments. In light of the prospective benefits, the executive committee adopted unanimously in Coeur, d'Alene, Idaho, on May 26, 1979, a resolution supporting H.R. 3896 and commending Representative Holtzman for her effort.

There is a presssing need for H.R. 3697. As you know, State and local impact analyses have not been required in the congressional process. Because of inflation, tax restructuring, and spending limitations, State and local governments now must reevaluate their ability to fully undertake many projects. In light of the proliferation of Federal statutory and regulatory requirements and consequent costs, the cost-squeeze dilemma has become chronic for State governments. States even find themselves at times in noncompliance with laws because they cannot pay for mandates. The alternatives for States are to no longer participate in Federal programs or to be in contempt of law. Thus, when Congress passes statutes without adequate appropriations or when it conceives program objectives which cannot be met, it does a disservice to the providers of direct services under those programs. It also raises false expectations in those persons for whom the laws were targeted, and importantly, increases the disdain of the citizenry for Congress itself.

Section 504 of the Rehabiliatation Act of 1973 is a case in point. Section 504 declares . . . "No otherwise qualified handicapped individual . . . shall, solely by reason of his handicap, be excluded from participation in, be denied benefits of, or be subject to discrimination."

Recipients of HEW dollars must comply with his statute by making existing and new buildings accessible to the handicapped or the recipients risk loss of Federal funding. Although a token—$50 million for building improvements—was allocated by the Federal Government for this fiscal year, most States are not in compliance because of the overwheliming cost of architectural changes and the failure of Federal dollars to filter down to the States.

Let's look at Public Law 94-142, which is designed to encourage States and local governments to provide education for handicapped children. In 1975, it was estimated that approximately half of these children were not receiving proper education.

When the act is fully funded (if it is fully funded) in 1982, $3.2 billion will be needed to provide these children with appropriate education. But in 1977, only $200 million was appropriated by Congress for this purpose.

One State estimated a cost of $670 million to educate its handicapped children in 1977-78, yet the Federal Government provided only 5 percent of that State's total education costs. The expense of carrying out this mandate comes out of State and local school funds—or the provisions of Federal law are not met.

These are but two examples of laws which costs States extraordinary amounts of money. To be sure Congress has addressed pressing needs, but had Congress as a matter of course analyzed the fiscal impacts of its actions, perhaps better enabling legislation would have been forthcoming. Perhaps we would have seen legislation that was more realistic and which did not raise false expectations.

The Federal Paperwork Commission reported in late 1977 that State and local governments expected an estimated $5-$9 billion annually to comply with reporting requirements. It also found the paperwork to be little more than a bureaucratic control mechanism concentrating on process and not product. Control of process, no matter how extensive, is no guarantee of achieving statutory purpose.

H.R. 3697 might not prevent imposition of burdens but it would let Congress know how much of a burden it is imposing before, not after, the fact. Also, it is particularly timely. There is likely to be less, not more money in real dollars, adjusted for inflation, flowing to and within States next year, especially in light of the reduced growth rate in Federal expenditures projected by current budget resolutions for fiscal 1980.

Finally, this is a congressional management bill. It not only focuses Congress' attention on the impacts of its decisions on State and local governments, it also provides Congress with an excellent tool for more effective congressional oversight of Federal agency activity. As part of legislative histories, the analyses could serve as guidelines for agency rulemaking. For example, if a Federal agency promulgates rules with dramatically increased administrative costs for State governments, the Congressional Budget Office analyses would be relevant to determine if such activity was contemplated by the Congress when passing the enabling legislation. Conversely, if Federal agencies fail to implement intended congressional policies, such would be equally demonstrable.

In summation, I believe that H.R. 3697, if enacted, will provide an essential managerial oversight tool for Congress and will provide a vehicle for determining the fiscal impact of proposed national policies on State and local government.

In addition to improvement of congressional performance, you will provide encouragement to thousands of adversely affected State and local governments.

On behalf of the Council of State Governments, I urge speedy passage of this bill. Thank you for the opportunity to present the council's views.

Ms. HOLTZMAN. Thank you very much, Mr. McRay. Our next witness will be Tennessee State Representative John Bragg. We are very pleased to have you here before us and since your statement will be incorporated in the record, will you please summarize it briefly?

STATEMENT OF HON. JOHN BRAGG, MEMBER, TENNESSEE GENERAL ASSEMBLY AND CHAIRMAN, STATE-FEDERAL ASSEMBLY, NATIONAL CONFERENCE OF STATE LEGISLATURES

Mr. BRAGG. The statement is in the record. I would say that I was at that meeting at Coeur d'Alene where we adopted that. I also serve on the board of governors of the Council of State Governments. My primary concern is for the legislative process.

I have been chairman of the Finance Ways and Means since 1973. In 1974 we passed a bill which required us to get a fiscal note on the impact of all State laws on local governments and that is what we would like for you to do at the Federal level on the impact on State and local governments.

I might say to you that I don't know how we could operate any more without those impact statements. I would say further to you that in the process I think at first we had fiscal notes from the executive branch alone and we finally found out that they were

padding them or cutting them, depending on the position of the Government, so we set up our own agency to prepare fiscal notes.

We now prepare our own fiscal notes. We even follow behind our own staff in getting fiscal notes. We do a spot check on fiscal notes to be sure that staff is not also telling us what is wrong or what is right or doesn't take a position.

I would say to you that in the preparation of fiscal notes of the impact on State and local governments that the State and local agencies, mayors, counties, and legislators, Governors, could be of great assistance in assisting the Congress on those impact statements.

Let me just point out to you an experience in Tennessee. We checked our payroll last fall and had it not been for the Federal impact and the mandate of the Federal Government alone we would have had 632 less people on the State payroll than we had 4 years ago, in order to meet the Federal standards on some of the human service requirements we had. Also, according to employment security we added approximately 2,700 people to our Federal payroll, our Federal mandate, when it last passed and on which there was no impact statement on what it would do to Tennessee and the other 49 States. What I am saying is, really, I think we must come to a point that the Congress will know what the impact is on State and local government when they pass a bill.

I realize that Federal employment has remained about static for the last 10 years, but State and local employment has skyrocketed because of Federal mandates and Federal standards, and I urge the Congress to find out what the impact is going to be on us in employment, in payroll, and in other things, through some system of accurate fiscal notes so that you can know when you vote here what you are doing to us. Thank you.

[The prepared statement of Representative Bragg follows:]

PREPARED STATEMENT OF HON. JOHN BRAGG

It is a pleasure to sit before the distinguished members of the Task Force on State and Local Governments, chaired by Representatives Elizabeth Holtzman and the Task Force on Budget Process chaired by Representative Norman Mineta this morning to address H.R. 3697 an amendment to the Congressional Budget Act.

I am John Bragg, member of the Tennessee General Assembly and chairman of the State-Federal Assembly of the National Conference of State Legislatures. I appreciate this opportunity to lend our vigorous support which requires the Congressional Budget Office to prepare and submit estimates of costs to be incurred by State and local governments in implementing or complying with bills or resolutions under consideration by Congress.

Approximately 33 State legislatures require the attachment of fiscal notes to bills and resolutions under considerations in the legislatures which would increase or decrease revenues, expenditures or the fiscal liability of the State and its political subdivisions. Five State legislatures (Connecticut, Georgia, Nevada, Rhode Island, and South Carolina) adopted fiscal note legislation last year. New Hampshire's fiscal note bill was signed into law earlier this month.

In my State (Tennessee), fiscal notes for bills impacting local governments have been required since 1974. A constitutional amendment passed in 1977 further required that the State provide funding to local governments to implement or comply with State-mandated programs or services. California, Florida, and Montana have similar requirements.

The need for fiscal notes on the Federal level becomes increasingly apparent as laws are passed requiring State government expenditures, while at the same time, State budgets are being stretched beyond their limits, due to inflation and increased demands for services by citizens. We have found in Tennessee that the number of State mandated programs and services have decreased since the adoption of the 1977 constitutional amendment. Fiscal notes provide a framework from which a

more careful consideration of the costs and benefits of proposals can be made. Bills or resolutions with hidden and often significant costs can be identified immediately and decisions related to the feasibility of such proposals can be made early on. In addition, this early warning system allows more time for amending proposals to make implementations more cost effective.

At least seven States—Arkansas, Florida, Illinois, Michigan, Missouri, South Dakota, and Wisconsin—require the attachment of fiscal notes to administrative rules and regulations. In addition, 17 States require fiscal or actuarial analysis be completed before consideration of proposals affecting retirement systems. NCSL submit that these requirements should also be considered on the Federal level.

Many of the costs State and local governments are costs incurred by complying with Federal regulations promulgated to implement Federal programs. The examples are numerous, the costs are significant. Among the most notable examples are regulations implementing requirements of the Clean Air Act, the Clean Water Act, and the Resource Conservation and Recovery Act. We believe the State and local costs resulting from compliance with such regulations should be estimated and indicated prior to the issuance of final regulations. We hope you will give this recommendations your careful consideration.

In closing, I would like to again submit our support of this measure. We at NCSL are familiar with the fiscal note process as we are required to attach fiscal notes to all of our policy positions, it is indeed a useful tool. If we can provide additional information on fiscal notes, please feel free to contact the NCSL Washington, D.C., staff.

Thank you for affording me this opportunity to speak to the fiscal notes issue. I would be pleased to answer any questions you may have.

Ms. HOLTZMAN. Thank you very much for your statement.

The next witness is Stephen B. Farber, who is the executive director of the National Governors Association.

We are very pleased to have you here, Mr. Farber. Without objection the text of your testimony will be incorporated fully in the record.

STATEMENT OF STEPHEN B. FARBER, EXECUTIVE DIRECTOR, NATIONAL GOVERNORS' ASSOCIATION

Mr. FARBER. Thank you, Madam Chairman and Mr. Chairman. I will summarize my remarks in three points. First, I think it is worth noting that the Advisory Commission on Intergovernmental Relations has reported that fully 25 States now require fiscal notes on legislation affecting their local governments and 10 States provide State reimbursement for mandated costs.

There are variations, of course, from State to State as to the extent of these provisions and precisely how they are worked out, but I think it is significant that we have now, according to ACIR, fully one-half the States that have taken this approach with respect to their local governments.

The second point I would make is this: I think the effort you are making with this significant legislation is one that all of us must take to heart these days. We at the National Governors Association take it to heart, and we have now begun to impose upon ourselves, with respect to the policy positions that we adopt a fiscal note requirement that really bears great similarity to what you are talking about here. Beginning with the policy positions that are adopted later this year we will be implementing a fiscal note requirement for the impacts of our policy positions on Federal as well as State government.

Our executive committee in February unanimously recommended this procedure. We think it is entirely consistent with what you are trying to do here.

The final point I would make, Madam Chairman and Mr. Chairman, is this: The legislation which you are supporting and which we strongly endorse represents an idea whose time has come. It is timely; it is significant; it is vital to the effective functioning of the intergovernmental system and the sound future of fiscal federalism.

We believe that you are making a tremendous contribution in supporting this approach and working so hard on it. We are committed to work with you to see its passage now. Thank you.

[The prepared statement of Mr. Farber follows:]

PREPARED STATEMENT OF STEPHEN B. FARBER

Madam Chairwoman, Mr. Chairman, and members of the task force. I am appearing before you today to advise you of the strong support of the Nation's Governors for a requirement that the Congressional Budget Office assess the cost to State and local governments of legislation reported by House and Senate Committees. As you know, CBO now generally limits its analysis on the cost of such legislation to the impact on the Federal Treasury. A bill consistent with the change the Governors advocate has been introduced by you, Madam Chairwoman, and has been assigned the number H.R. 3697. The bill has attracted wide support in Congress; it had 113 cosponsors, I believe, at the last count.

As members of the Budget Committee, I know that you hardly need to be reminded that resources available to governments at all levels are severely limited. Gone are the days when little attention was focused on the size of budget deficits and when Federal intergovernmental aid grew at 15 percent each year. Increased skepticism of the ability of Government to run programs effectively and growing concern about public spending have put Federal, State and local officials on notice that they must be prepared in the future to make do with less and to do more with less.

Enactment of programs without careful analysis of the needs they are to serve, of how they relate to efforts already underway to meet the same goal, and of how much full implementation will cost contributes to public dissatisfaction with Government initiatives. New and revised Government programs must be carefully constructed to address specific problems. They must avoid wasteful duplication. They must not make false promises to beneficiaries which only embitter them when they are left unfulfilled and which deflect attention from effective, pragmatic solutions.

The question of the legitimacy of unfunded mandates placed on one level of Government by another has been extensively debated in recent months. The intent of the mandates—to make this country cleaner, safer, more equitable and more responsive to the needs of retirees and handicapped persons—is beyond reproach. The debate turns not on the intent of the mandates but on the quality of the analytical work on which they are based.

To describe the Governors' position on this matter, I would like to quote from a letter of March 7 which Gov. Julian M. Carroll, chairman of National Governors' Association, and Gov. Richard A. Snelling, chairman of the NGA Committee on Executive Management and Fiscal Affairs, sent to you, Madam Chairwoman:

"The Governors have recently spoken out on the relationship they believe should exist between the three levels of government during the current period of fiscal restraint. Last year we adopted a policy position that called upon the Federal Government to pay for the costs it imposes on State and local governments and for States to pay for the programs they mandate local governments to implement. Your bill (H.R. 3697) is an important step toward full disclosure of the cost of Federal policies and open discussion of how such costs can best be paid. There are too many unmet needs facing this nation, and the cost of alleviating them is too great, to permit anything less than fully informed program design and goalsetting.

"A major recommendation of the National Governors' Association to the administration on its fiscal year 1980 budget was that the budget itself and all legislation supported by the administration should be analyzed to determine what costs the proposals would impose on state and local governments. We also urged the administration to support legislation of precisely the type you have drafted."

I will submit a copy of the letter for the record of these hearings.

The National Governors' Association strongly urges you to recommend to the Budget Committee and then to the Rules Committee the adoption of the change to section 403 of the Congressional Budget Act proposed in H.R. 3697. And we strongly

commend you for your sensitivity to this question, which is of fundamental importance to State and local governments and to the future of fiscal federalism.

Enclosure.

NATIONAL GOVERNORS' ASSOCIATION,
March 7, 1979.

Hon. ELIZABETH HOLTZMAN,
Longworth House Office Building,
Washington, D.C.

DEAR CONGRESSWOMAN HOLTZMAN: Thank you for sending us a copy of the bill you have drafted which would require the Congressional Budget Office to assess the cost to state and local governments of legislation reported by House and Senate Committees. Your bill has the full support of the National Governors' Association.

The Governors have recently spoken out on the relationship they believe should exist between the three levels of government during the current period of fiscal restraint. Last year we adopted a policy position that called upon the Federal Government to pay for the costs it imposes on State and local governments and for States to pay for the programs they mandate local governments to implement. Your bill is an important step toward full disclosure of the cost of Federal policies and open discussion of how such costs can best be paid. There are too many unmet needs facing this Nation, and the cost of alleviating them is too great, to permit anything less than fully informed program design and goalsetting.

A major recommendation of the National Governors' Association to the Administration on its fiscal year 1980 budget was that the budget itself and all legislation supported by the administration should be analyzed to determine what new costs the proposals would impose on State and local governments. We also urged the administration to support legislation of precisely the type you have drafted.

During the opening plenary session of the NGA winter meeting last week the Governors discussed their budget recommendations and their suggestions for improving the management of Federal grants-in-aid. Your bill was specifically mentioned during the session by Governor Riley, who had been asked to outline the recommendations of the Governors on Federal fiscal practices.

The National Governors' Association is committed to the principle of full cost assessment of Federal policies which you have incorporated in your proposal. We look forward to working with you toward enactment of your bill.

Sincerely,

Gov. JULIAN M. CARROLL,
Chairman.

Ms. HOLTZMAN. Thank you very much for your testimony. Mr. Mineta.

Mr. Mineta. Thank you very much, Madam Chairperson. Mr. Farber, in your statement I notice you say, "New and revised Government programs must be carefully constructed to address specific problems."

In my opening statement I had indicated that the difficulties with the Federal grant-in-aid system is its compartmentalization and the increase in categorical grant programs, and my experience as mayor was that as the number of narrowly focused programs increases, so did my administration costs, and so I am afraid that the sentiment you express here of trying to "address the specific problems" really mandates programs that tend to move the decisionmaking process from the local community to Washington. I wonder if you would care to comment on that?

Mr. FARBER. That certainly is not our intent, and by "specific problems" we mean precisely the kind of approach you are alluding to.

You are entirely correct, Mr. Chairman, when you say that categorical grant programs have increased in scope and complexity. When this administration took office, there were 442 categorical grants. There are today 492, according to the Advisory Commission

on Intergovernmental Relations, and that is not a problem endemic to this administration or to any other.

It is a problem that we have seen growing increasingly in intensity over the years. Our position is strongly consistent with yours with respect to these categorical programs. We wish to see them reduced in number. We wish to see them consolidated, and we received a commitment from James McIntyre, the OMB Director, and from the President in a meeting with him last December, that in the construction of the fiscal year 1981 budget there would be an explicit attempt made to consolidate programs in areas where effective and well-considered consolidations can be worked out.

We are currently working with James McIntyre and OMB in this regard. We will be meeting in Louisville in a few days. The President will be joining us, as will James McIntyre, and we hope to receive from them an update on the progress being made in the genesis of the fiscal year 1981 budget precisely in this regard. We entirely support your position in this respect.

Mr. MINETA. This paper probably being prepared would be something we would want to include in our record and, if possible, if we could get that as well, it would be very helpful. I would like to just ask a general question.

As we talk about costs, it seems to me we also have to talk about benefits. How do we get to that point of saying, for instance, in the case of the Clean Air Act, as being mandated, there is a benefit that comes out of that, so how do we then impose let's say a cost to local government on something as broad and expansive as let's say the Clean Air Act, or the Clean Water Act, as two examples?

Mr. BRAGG. That would be a difficult question for me to answer. I was just looking in Tennessee—I will speak to that—in categorical grants, we budget everything we know about and then during the time when our legislature is not in session, by law, all expansion requests and all Federal grants must come through the Joint Finance Committees.

In fact, our committee is meeting this morning in Nashville approving new Federal grants that have been made as to whether or not we will accept the funds.

I notice in 1978–79 in public health we received something like $318,000 for air pollution control. That was a project that was just in Nashville.

I don't know that anything is going to come from it, but money came down and we took it. We didn't want Kentucky to get it, so we put the program in. In fact, in that fiscal year in categorical grants, the fiscal year 1978–79, thus far we have received something like $36 million in grants that we didn't budget. In 1977–78, we received $99 million that we didn't anticipate in categorical grant programs.

I don't know how you would say if you are going to clean up the air what is going to be the impact on local government, but I think some attempt should be made to at least see what really needs to be done and not just make a mandate to clean up the air, but to say, let's see what we are going to do and then see what we decide to do is going to cost.

I think that is how you have to get down to specifics. I don't think you can just say let's clean up the air. I think you have to

say what are we going to do; are we going to have stations at so many places in every State to see what the air pollution is? Are we going to check every highway? Are we going to check every city? Are we going to Denver to see why the sag is there? I think that is what we have to do.

The problem is, it is easy to pass a law to say let's clean up the air and everybody go home and say, look, we passed a law that will clean up the air, but nobody has seen what we are really going to do.

Mr. McRAY. I recently came to Washington out of State government, the State of Florida, with the Department of Health and Rehabilitative Services there. I think the approach that the Florida Legislature has begun to use in response to having a requirement for economic impact analyses, that for the issues, for example, like public health issues, safe drinking water, Clean Air Act amendments, or even, for example, the education of the severely handicapped, when the costs are difficult to determine, the step that the legislature in Florida was taking was, and I think it follows upon what Representative Bragg is saying, they established pilot projects and set parameters for the product they wanted to see.

Pilot projects and seed money gave the localities the opportunity to demonstrate what they could do.

The following year they came back in the budget request and demonstrated what worked and what didn't work. Then the legislature and the agency could sit down and define a broader, more acceptable program, and I think that has worked considerably.

Mr. MINETA. In your case, Mr. Bragg, you indicated that because the executive department, depending upon how they felt about something, would either overestimate or underestimate costs and so the State legislature then set up its own committee.

In commenting on these bills where you put in these fiscal notes as to the impact on local government, does that committee then come up with the moneys that would relieve local government of those State-mandated costs?

How do you arm wrestle with this other body in the executive branch? Would you explain a little more?

Mr. BRAGG. Some of the legislation does state what we spend and what we send to local government and what they get.

I might say to you that Tennessee in 1978, March 7, 1978, passed a constitutional amendment which states that the growth of our State budget cannot exceed the growth of the Tennessee economy as determined by law.

It also states that for any bill that we pass that impacts local government, we shall share in the cost. Now, we were getting local government fiscal notes long before this. We have attorney general's opinions which state that on insignificant impacts, that is, small impacts, less than, say, a statewide impact of $1 million, it is not necessary for us to spell out what each city and county gets, but in major impacts we do have to spell out what each county and city gets and the law must be specific.

Mr. MINETA. Let me relate to it a specific example. Suppose the State says, yes, we will allow 80,000 pound trucks on our roads. You recognize that you have to do your engineering work on your State highways, but what about that impact on local government

in terms of its own streets that may not be capable of carrying trucks of 80,000 pound weights? How do you then deal with that kind of an issue?

Mr. BRAGG. Well, we haven't dealt with that issue because we have 73,000 pound trucks in Tennessee.

Mr. MINETA. 73,000 pound trucks. How do you deal with them?

Mr. BRAGG. We have had a gasoline tax of 7 cents in Tennessee for 50 years and we give 2 cents to the county and 1 cent to the city to maintain their roads and streets. We keep 3 cents at the State level and we use one penny for highway construction bond issues. So we are already sharing on the earmarked taxes for roads and streets with our local governments.

Now, studies have shown if we increased the weights it will have about a $26 million a year impact on our roads in Tennessee and if that happens we will need another penny for the gas tax to do it.

Of course, the problem is, we anticipate a real lag in gas taxes in Tennessee for the next 5 years. We anticipate that all highway-related earmarked taxes are going to decrease in real dollars, not inflation dollars, but in real dollars.

We anticipate that our automobile registration is going to decrease; we anticipate that our gas tax is going to decrease, our inspection fees will decrease in real dollars over the next 5 years.

Mr. MINETA. I am just wondering whether or not there isn't more emphasis being placed on cost through that approach rather than benefits? I wonder if any panel member might want to respond to that?

Mr. FARBER. I think, Mr. Chairman, that is a fair question and the benefit side must be looked at very carefully.

In my testimony I indicated that a number of the mandates or objectives to which the fiscal note would be attached are beyond reproach.

They are objectives that all of us share because they are proper and legitimate and important goals of public policy. But I think, as Representative Bragg was suggesting, what is useful to consider is the best way of achieving those goals I think that the fiscal note approach provides a discipline that helps in constructing of the best kind of program.

The process is what really counts here. We, for example, at the National Governors' Association, are now working with the Department of Transportation on issues of coal transportation—how to improve transportation of both Appalachian coal and western coal.

Now, because we are going to a fiscal note process, we have found that we are looking at a whole range of alternatives, perhaps more carefully, more thoroughly, than might otherwise be the case.

The process itself is extremely helpful because it forces a constructive and affirmative, not a negative, kind of discipline that we think is helping us think through the issues more clearly and will help us arrive at a sounder public policy outcome.

From that perspective, it seems to me that the benefit side, as well, can gain from this kind of approach.

Mr. MINETA. Let me have Mr. McRay comment on that because he says that the paperwork is concentrating in process and not product. Is there a contradiction here?

Mr. McRAY. No; I don't think so. When we are talking about process versus product, we are talking about basically regulatory control under the enabling legislation. The regulations define how a State, in managing a particular project under the Federal legislation, is to reach an end point.

The concentration is on how we go about doing it rather than say, for example, on a contractual basis demonstrating that we can do it. There is so much effort put on the process of getting to the end point.

By defining the process, you are not legitimatizing all of the other methods which perhaps would be more cost effective and more productive. That is what I am making reference to there.

Mr. BRAGG. Mr. Chairman, if I may, being in my fourth term as chairman of the Finance Ways and Means, I have never had anybody yet come to my office and tell me how to save money. They have all told me what they wanted.

Mr. MINETA. That has been our experience as well.

Mr. BRAGG. I have found there is very little difference between need and greed, frankly, and the entire presentation is always on the benefits, and I can understand that, but then when we put the fiscal notes to it to see whether or not we can afford it and whether or not it is cost effective, then we judge the benefits against the cost effectiveness.

As an example, we studied last year what it was costing us per juvenile offender to try to take care of the juvenile offenders in Tennessee. It is $9,600 a year. We could send them to Harvard for that amount.

Ms. HOLTZMAN. No; you couldn't.

Mr. BRAGG. Well, we could send them somewhere, and it costs us $5,700 a year to keep an adult in prison, but $9,600 a year to keep a juvenile in an institution. There are many programs that are desirable and I think when you get down to a point where you have so much revenue you have to decide the priorities and you have to see where it goes. I wouldn't say there is not a program, of all of the $99 million that we got last year in grants outside of our budget that came down during the months in which we approved them, I wouldn't say that there isn't one of them that we didn't use the money well, but at the same time, had we had to raise those taxes in Tennessee and voted for those taxes, we might not have voted for them.

Mr. MINETA. You are talking about the $99 million Federal moneys in Tennessee. How much did that impact as far as impact on State government and local government to administer, or local matching share, or whatever it might have been?

Mr. BRAGG. In State funds we spent $786,000. We approved that many; not a bad return.

Mr. MINETA. Thank you very much, members of the panel. I appreciate the indulgence of the chairperson as far as the 5-minute rule is concerned.

Ms. HOLTZMAN. Let me just ask two very brief questions. First of all, you mentioned that there are 25 States that now have a procedure for requiring fiscal notes for legislation before it has been adopted. Have you done any analysis of whether or not those

States have experienced any major difficulties in determining this fiscal impact?

Mr. FARBER. I don't believe they have, Madam Chairman, but I would be happy to obtain further information from the Advisory Commission on Intergovernmental Relations which has that specific information.

Ms. HOLTZMAN. Representative Bragg, have you experienced any difficulty in Tennessee?

Mr. BRAGG. No; we have had a balanced budget. We have to have one. We now constitutionally have to have one. We didn't until last year, but we now have one. In fact last year we put in our constitution that any bill that passes, if it is not funded, is null and void.

Ms. HOLTZMAN. What do you think the impact has been of having these fiscal notes? Do you think that it has provided money for programs that would not have been funded otherwise by the States?

Mr. BRAGG. I think it has helped us establish priorities.

Ms. HOLTZMAN. In other words, it has helped to eliminate some kinds of programs that would be too expensive because of their cost impact on localities?

Mr. BRAGG. Yes.

Ms. HOLTZMAN. Has it ever, in your experience, produced the situation where, recognizing the cost of the program, the State decided that the State itself would have to pay for it?

Mr. BRAGG. Well, I guess I can best say that in 1973 we passed a 3-percent cost of living for our retirees. The actuary told us it cost us $530,000. I notice in the budget next year it went to $1 million and the following year to $2 million so I called the actuary and asked him to give me a projection.

I found in 20 years on a pay-as-you-go basis it would run at $100 million and still be growing; in fact, in 40 years with cost of living it would surpass what our regular fund would be costing.

We now are funding it on a 40-year basis so we avoid an impact of $100 million 16 years from now.

Ms. HOLTZMAN. I think that helps you to fund the program in a sound way.

Mr. BRAGG. It helps us to fund the program. It helps us to determine whether or not we really have the resources to do a program. Every request we have has a constituency and the only problem is which constituency do we serve in a cost-effective manner that we can go to the taxpayers and say, "Look, we put this program in. Here is what it is costing you and we believe it is right and this is what it is going to cost you to pay for it."

Mr. MCRAY. Within the executive agency in which I worked in Florida, I think the ramifications of having the economic impact analysis requirement was that, as often is the case, the legislative proposals in the first round came out of the agencies themselves.

What we found was that when we had to stop, list, examine, and investigate what those costs were to the constituency and to taxpayers, et cetera, that as a department if we could not demonstrate effectiveness then those proposals were not chosen as legislative priorities. I can tell you that the quality of the legislation submitted by the department increased geometrically.

Ms. HOLTZMAN. That is an interesting observation. I have no further questions. Mr. Mineta.

Mr. MINETA. Let me just ask if I might, Representative Bragg, you mentioned a State requirement for a balanced budget. Do you have two budgets, one for capital expenditures and another for operating budget?

Mr. BRAGG. Yes.

Mr. MINETA. So that is how you maintain your balanced budget?

Mr. BRAGG. We do, and I don't want to get into the Federal balancing, but I understand the problem and I have made the statement, and it has been questioned, that if you budgeted the way in Washington that we do in Tennessee, you would have a balanced budget.

Mr. MINETA. We would have a surplus.

Mr. BRAGG. You would have a surplus of about $60 billion.

Mr. MINETA. $60 billion. Let me ask, because State legislatures don't meet annually and we have a budget process that is on an annual basis and you have to do a lot of programing, what happens in the case of State government, being impacted by what we are doing?

You said that you have an executive committee of some nature that meets on the off years.

Mr. BRAGG. Our Joint Finance Committees, yes, Mr. Chairman. In 1967 we had passed legislation which required Tennessee to meet annually and we do meet annually. We budget annually. We budget on the old fiscal year, July 1, and you are now in on October. That gives us some concern in the budgetary process, but we do budget annually in Tennessee and most of the States have now gone to annual budgets. Texas has not yet. William Clements wants to meet once every 2 years.

Mr. MINETA. If he can find the bumblebees.

Mr. BRAGG. Yes.

Mr. MINETA. That is no problem any more now as far as State government? Either Mr. McRay or Mr. Farber.

Mr. FARBER. No. Different States have different approaches, but I think what Representative Bragg says about the capacity of the States to deal with this problem is correct.

Mr. MINETA. So that the time involved from the Federal Government budget process doesn't impose any kind of uncertainties at the State-local level?

Mr. FARBER. I do think, Mr. Chairman, one objective that the Governors, the mayors, the county officials, and the State legislators have had for a long time is advance appropriation, in one form or another, of Federal funds for the purpose of effective planning and effective utilization of those funds.

That is an objective that you, as a mayor, I am sure had high on your list of priorities simply for the purpose of good and effective planning, and we certainly would applaud that objective wherever possible.

Mr. MINETA. Multiyear budgeting?

Mr. FARBER. Multiyear, advance funding, advance appropriations. There are different forms that can be adopted for to different programs, and some of those techniques have already been used for a very limited number of Federal programs; but, for exam-

ple, in the water pollution construction grant program we have strongly advocated advance appropriations, and we have not been successful. In other areas too we feel this approach is essential to good and effective planning. That would be a very useful approach for the Congress to adopt on a more consistent basis.

Mr. MINETA. What about the impact of the change of fiscal year from October 1 to September 30? What impact has that had in your case in the State governments?

Mr. FARBER. Most State governments have not adopted the Federal fiscal year. At the present time there are 46 State governments that maintain the July 1 fiscal year. Consideration has been given in some States to change, but the July 1 date has not posed insuperable obstacles at this time.

Mr. MCRAY. There are States where the change of the fiscal year has been fitted. In fact, in Florida, although they have not yet changed their fiscal year, most effective dates for enabling legislation that that body passes are delayed until October 1. Congress likewise could legislate sufficient leadtime from the date of passage of Federal legislation until implementation so that whatever a State's budgetary cycle it can accommodate the program.

Mr. MINETA. Thank you very much.

Ms. HOLTZMAN. Thank you. Our next witness, Dr. Robert D. Reischauer, who is the Deputy Director of the Congressional Budget Office. We welcome you before the joint hearing and we are very pleased to have you before us. Without objection, the text of your statement will be incorporated in the record in its entirety. We would appreciate your summarizing it briefly.

STATEMENT OF DR. ROBERT D. REISCHAUER, DEPUTY DIRECTOR, CONGRESSIONAL BUDGET OFFICE, ACCOMPANIED BY JOHN SHILLINGBURG

Dr. REISCHAUER. Thank you. Let me take this opportunity to introduce John Shillingburg on my right, who has been working on some of these issues at the Congressional Budget Office.

In accordance with your request to summarize my statement, I would like to elaborate on two of the points made in that statement.

The first of these is that we feel strongly that it would be valuable for the Congress to know the cost and benefits that proposed legislation would have for the Federal Government, for State and local governments, for private industry, for individuals, and for other sectors of society. Currently, the only such information that is available on a regular basis is the estimates of the cost to the Federal Government that CBO provides in accordance with section 403 of the Budget Act. H.R. 3697 would move us one step further toward assembling all of the information a decisionmaker would need to make a fully informed judgment on a proposed piece of legislation.

The second point I would like to make is that the task laid out in H.R. 3697, while very important, would not be easy. There are likely to be a fairly large number of bills that impose some direct impact on State and local governments. However, the majority of these are likely to impose relatively minor costs on these governments. Nevertheless, calculating these minor costs will be as diffi-

cult as calculating the impacts of bills that would impose very significant burdens on State and local governments.

From the experience we gained writing the paper "Federal Constraints on State and Local Government Actions" for this task force, we also know that the lack of data and of appropriate methodologies is likely to seriously hamper our ability to provide high quality and timely estimates of the impacts of proposed legislation. These difficulties will be exacerbated by the lack of specificity of some pieces of legislation. Often the rules and regulations needed to implement a piece of legislation have much more influence on the magnitude of the costs imposed on State and local governments than does the legislation itself; here the experience under section 504 would seem to be an appropriate example. Unfortunately, CBO would not know the form these regulations would take until long after the time at which a cost estimate would be of most use to the Congress.

Representing an institution that avoids making recommendations, but provides options, let me conclude by describing three alternatives for dealing with the situation you have before you.

One is to follow the path laid out in H.R. 3697, which is to ask CBO to provide cost estimates for every reported bill or regulation.

The second is to follow the example of CBO's inflation impact effort. Under this effort CBO was provided with additional resources to create a small 10-person unit that estimates the inflationary impact of selected legislative proposals that the Budget Committees and CBO and the Appropriations Committees decide are likely to have large impacts on the CPI.

The third approach would be to spend the next year doing a detailed analysis of the nature of the task called for in H.R. 3697. This analysis could calculate the number of bills with State and local impacts, because we don't really have a good feel for that number right now, and categorize these impacts with respect to both type of impact and size of the impact. The analysis could also indicate which State and local cost estimates would run up against problems of inadequate methodology, which would run up against data limitations, and which might be limited by the fact that they depend too much on implementing regulations and therefore leave CBO unable to provide the timely, specific estimate that the Congress would require.

With that, let me stop and answer any questions that you might have.

[Testimony resumes on p. 37.]

[The prepared statement of Dr. Reischauer follows:]

PREPARED STATEMENT OF ROBERT D. REISCHAUER

I am pleased to present to the Committee on the Budget the views of the Congressional Budget Office on H.R. 3697, the State and Local Government Cost Estimate Act of 1979. As introduced by Representative Holtzman, H.R. 3697 requires CBO to estimate the costs that would be incurred by state and local governments in compiying with the provisions of each reported bill or resolution. These estimates are to be included in the regular estimate of the five-year costs for the federal government of reported bills or resolutions required by Section 403 of the Congressional Budget Act.

Without doubt, it would be valuable for Congressional decisionmakers to know the costs that a bill or resolution would impose on state and local governments. It would also be useful to know the costs and benefits of proposed federal legislation on private industry, individuals, or other sectors of the economy. Currently, the only such information available on a regular basis is the estimated costs to the federal government, as required by Section 403.

While the objectives of H.R. 3697 are important, CBO's ability to achieve them would limited for several reasons.

In the first place, the task could be significant. Last year, CBO prepared 995 cost estimates for bills reported from committees or under consideration by committees. Of course, not all legislation affecting federal spending imposes costs on state and local governments. We estimated last year that 10 percent of all reported bills or resolutions have some impact on state and local governments, and of these probably not more than half are likely to have a significant impact. Furthermore, in the past, CBO has considered state and local budgetary impacts in some of its cost estimates of the federal budgetary impact. For example, our cost estimates of the various welfare reform proposals considered in the last Congress included estimates of the fiscal relief that would have been accorded the state governments.

Second, the lack of data and of appropriate estimation techniques would limit our ability to estimate the impact on state and local governments. The impact of some types of legislation would be relatively easy to estimate. The increased costs to state and local governments of a Social Security tax hike or an increase in the minimum wage would fall into this category. It might be very difficult, however, to estimate the impacts of other types of legislation. Let me offer two examples.

Consider, for example, the difficulty of estimating the costs to state and local governments where the impact varies from jurisdiction to jurisdiction and the data on that variance is not easily available. This difficulty can be illustrated by noting the complexities that would have been involved in estimating the cost impacts on state and local governments of Section 504 of the Rehabilitation Act of 1973. That section states:

> No otherwise qualified handicapped individual in the United States . . . shall, solely by reason of his handicap, be excluded from the participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance.

This sweeping requirement covers not only the rehabilitation services provided by that act, but also all other activities receiving federal assistance. This included, to name just two major areas affected, the construction of any educational facilities--on the elementary, secondary, or postsecondary level--funded in part by federal grants, and the construction and purchase of equipment for subway systems, funded by grants from the Urban Mass Transit Administration. Estimating the costs of just one aspect--the modification of existing state university and community college facilities to permit barrier-free access for the handicapped--would require detailed data on the characteristics of the educational plants of institutions receiving higher education grants. Lacking such data, estimates would have to be developed for a sample of universities with campuses of various sizes,

terrains, layouts, and building ages. Then, the total cost for institutions would have to be estimated from profiles of the value of university buildings and changes in enrollments over time, based on an assumption that the cost for an individual university is proportional to the value and age of its structures.

Or consider the difficulty of estimating the costs to state and local governments of legislation that is written very generally but will have implementing regulations, which will not be written until after the legislation has been enacted into law. Again, Section 504 of the Rehabilitation Act can serve as an illustration. The estimate of costs to educational institutions of complying with the regulations on removal of physical barriers could not realistically be done until the Department of Health, Education, and Welfare (HEW) had promulgated its standards. The standard finally adopted for existing buildings required that federal grant recipients must--through the elimination of physical obstacles or through other methods--operate their programs so that a program viewed in its entirety is readily accessible to handicapped persons. In order to estimate the costs of this bill before the regulations were issued, CBO analysts would have been required to make policy judgments, such as whether or not methods other than removal of physical obstacles would be permissible.

In both of these cases, where data are lacking and where the impact depends on regulations written after a bill's enactment, the preparation of the cost estimates would be marked by uncertainty and would take a long time--too long perhaps to be timely for the filing of a bill's report after final committee approval.

A third problem is that these estimates would have to be for the nation as a whole. In many cases, it would be impossible to break down the costs on either a state-by-state basis or a state-versus-local-government basis. This limitation may affect the utility of CBO's estimates for some users. It might not be possible to determine whether the burden would fall unfairly on certain jurisdictions--for example, on rural western counties versus eastern cities.

In view of the limitations I have just listed, a more limited approach under which CBO would be required to prepare estimates of the impacts on state and local governments for only those bills likely to have a major impact would seem to be more feasible than such a requirement for all bills. CBO's experience with inflationary impact analysis might serve as a model. This year, at the direction of the Appropriations and Budget Committees, CBO developed the capability to provide inflation impact estimates for selected bills. Additional funds and staff were provided in the Legislative Branch appropriations bill for fiscal year 1979. A ten-person unit was created to prepare these estimates for selected bills identified by the Budget Committees as being important in terms of their impact on inflation.

With a limited increase in staff and funds for computer support and special surveys, a similar unit could be established to do a select number of state and local impact estimates. After some period of time during which CBO could build its capacity and develop appropriate data bases and methodologies, the Congress could reassess the usefulness of state and local impact statements and decide whether the effort should be expaned to cover additional bills.

Ms. HOLTZMAN. I take it that you are familiar with the fact that the legislation amends section 403 of the legislation and that the introductory phrase which is left untouched, says, "The Director of the Congressional Budget Office shall, to the extent practicable, prepare for bills," and so forth.

Dr. REISCHAUER. Yes. We have made an effort to have that phrase mean 100 percent. With respect to cost estimates we have come very close to that 100 percent. When you get into a situation where you are running this system well below 100 percent, you are always open to criticisms, such as, why did you apply your resources to doing that State and local impact rather than this one? Are you making these selections in an unbiased and open way? If possible, we would like to avoid placing ourselves in that kind of situation.

Ms. HOLTZMAN. I think it would be clear in the legislative history of this bill and in the report that there would be no expectation that the Congressional Budget Office could immediately give detailed and meticulously, well thought through analyses of the fiscal impact of all Federal legislation on State and local governments immediately.

I don't think that anyone would reasonably have such an expectation. With that understanding, do you think the legislation imposes a burden that you can't fulfill? I don't mean you personally, but rather the Congressional Budget Office.

Dr. REISCHAUER. The answer to that, I think, is that if we had to do 20 or 30 of these a year involving the kind of complexity we anticipate, we could not do it with our existing resources unless we cut substantially into some other activity.

Ms. HOLTZMAN. So you would need extra people to fulfill the requirements of this bill?

Dr. REISCHAUER. Yes.

Ms. HOLTZMAN. In other words, we would have to do a fiscal impact statement for this bill. Do you need extra people to do that impact statement for us?

Well, I can appreciate your point of view and I would certainly do my utmost to make sure that those extra persons were provided to the Congressional Budget Office so that it could, as quickly as is practicable, and feasible, develop the expertise to respond to the mandate of this legislation.

Two bells have now rung. We will go vote and come back shortly. The hearing will be in recess.

[After recess.]

Ms. HOLTZMAN. Mr. Mineta.

Mr. MINETA. Thank you very much, Madam Chairperson. Dr. Reischauer, you mentioned the idea of estimating cost for bills that would require implementing regulations. Perhaps if Congress were required to do a cost-impact analysis of the type required in H.R. 3697, we would give more concern to how programs will be run. Do you think this might be the case?

Dr. REISCHAUER. I think that it would lead to much more specificity in the way the legislation was written. Whether that is good or bad is for you to determine.

I am suggesting that, faced with the kind of situation reflected in section 504, CBO could come back with a statement saying the impact of the bill could be close to zero, or could be close to $10 billion, depending on regulations. Now, this might lead the Congress to say, "Well, we should provide more guidance on this," and that certainly would be a step in the right direction.

Mr. MINETA. What about Executive Orders 12074 and 12044 establishing the interagency urban impact analysis procedure within the executive branch?

Do you feel the administration is more aware of the impacts that its regulations might be having at the local level?

Dr. REISCHAUER. I think the answer is yes, that there is a new awareness. But the extent to which this awareness has actually changed the direction of policy or the proposals is not noticeable to date. A lot of the urban impact analyses have been retrospective, catching up on initiatives that were proposed over the preceding 3 years.

Mr. MINETA. Even though it is retrospective, do you think that might be helpful in developing methodology?

Dr. REISCHAUER. There is no question about that. But if you read some of the urban impact analyses which have been prepared by HUD, you do get the feeling that I was trying to convey earlier, which is that there is a tremendous amount of uncertainty surrounding these estimates. That doesn't say that the process won't improve with practice. We are just very new at this game.

Mr. MINETA. Should OMB prepare similar types of State and local impact statements to be included with proposed legislation?

Dr. REISCHAUER. I think it would be very helpful from our standpoint if OMB was required to provide such statements with Presidential initiatives. We would obviously carry the congressional side of this, much as is done in cost estimating.

Mr. MINETA. You mentioned in your statement about your experience with inflation impact statements as a more modest approach to this issue. How much have these estimates cost CBO to prepare?

Dr. REISCHAUER. I don't have the exact figures involved, but we can provide those for the record.

[The information referred to follows:]

CBO PREPARATION OF INFLATION IMPACT STATEMENTS

This is the first year CBO has been preparing inflation impact statements. Consequently, much of the effort has been devoted to recruiting staff. We therefore are not able to provide a precise estimate of the average costs to CBO of preparing inflation impact statements.

When fully operating, the inflation impact estimating effort will involve a 10-person staff and a total cost of $397,000. Of this, $278,000 will be for personnel costs,

$100,000 more for computer costs, and $19,000 for supplies, utilities, and other items.

Dr. REISCHAUER. We created a 10-person unit with a considerable amount of computer resources to do this. That unit to date has done something in the neighborhood of 10 estimates, which probably doesn't sound like very much, but the nature of the task is just very, very complex. For example, how you determine the impact on the CPI of the hospital cost containment bill is a very complex economic problem.

Mr. MINETA. You say that this 10-person unit was created to prepare these estimates for selected bills. How do you identify which ones you are going to analyze?

Dr. REISCHAUER. We select these on the advice of the House and Senate Budget Committees. We have had meetings from time to time with the appropriate staff members and the members of the committees themselves, asking which pieces of legislation should be analyzed.

Over the years, we have received numerous letters from Members of Congress asking for inflation impact statements, in large measure because House rules require that such a statement be included in the report. There is no shortage of demand for these analyses. It is mainly a question of which bills we think the impact is going to be significant, and which ones from a methodological standpoint would we be fairly comfortable with the results.

Oil decontrol was an example of one of the ones that everybody agreed was an important and double task.

Mr. MINETA. On page 6 you indicate, "With a limited increase in staff and funds for computer support and special surveys, a similar unit could be established to do a select number of State and local impact estimates."

One of the objectives, of course, of this legislation is specificity. How much do you think that limited increase is? Is there any estimate as to how much in staff and dollars?

Dr. REISCHAUER. My seat-of-the-pants guess is that it would be about the same magnitude as for the inflation impact unit. Now, it could turn out that if we went back and did a very careful analysis of the legislation in the last year, the conclusion would be that there are only 9 or 10 pieces of legislation where such impacts are significant and where the Congress really would be very interested in having an analysis. Of those, two might be being done already by CBO, the same way we did an impact of the welfare reform legislation. In one case, the methodology might just be impossible and that would leave us with seven. If there were 7, clearly a 10-person staff would be way too large. I think this is an area of a good deal of uncertainty.

Mr. MINETA. Thank you very much, Doctor. Madam Chairman, if I might, I would like to ask unanimous consent that the study prepared by CBO at your request and my request entitled "Federal Constraints on State and Local Government Actions" be made a part of the record.

Ms. HOLTZMAN. Without objection, it is so ordered.

[Testimony resumes on p. 90.]

[The study referred to follows:]

FEDERAL CONSTRAINTS ON STATE AND LOCAL GOVERNMENT ACTIONS
(Prepared by the Congressional Budget Office)

PREFACE

In recent years, state and local government officials have expressed concern over the extent to which federal laws and regulations constrain their actions and impose costs on their jurisdictions. To assist the House Budget Committee Task Force on State and Local Governments in evaluating these concerns, Representatives Elizabeth Holtzman and Norman Y. Mineta requested the Congressional Budget Office to prepare this study. The paper discusses different types of constraints and assesses what might be involved in measuring their costs and benefits. It also outlines some policy options that the Congress might consider if there is a consensus that intergovernmental constraints do pose a problem. In keeping with CBO's mandate to provide objective analysis, this paper makes no recommendations.

Federal Constraints on State and Local Governments was written by Peggy L. Cuciti of CBO's Human Resources and Community Development Division under the supervision of Robert D. Reischauer and David S. Mundel. Several other people, both at CBO and elsewhere, contributed to this report. In particular, the author wishes to thank Catherine Lovell and her associates at the University of California-Riverside who are doing research on the effects of federal and state mandates on local governments. They generously shared their work in progress and helped clarify many issues. Other people who provided valuable criticism include Stan Collender, Alfred Fitt, Richard Gabler, Sophie Korczyk, Martin Levine, Robert Levine, Dave O'Neill, and Charles Seagrave. The paper was typed by Jill Bury and edited by Johanna Zacharias.

Alice M. Rivlin
Director

SUMMARY

FEDERAL CONSTRAINTS AS AN ISSUE

The constraints that federal laws and regulations impose on state and local government actions are a subject of concern to both state and local officials and to Members of Congress. As federal financial support of state and local functions has increased, and as federal regulatory policy has expanded, so too has the number of federal constraints. Critics contend that certain constraints impose excessive costs and require actions that are counterproductive to the achievement of federal programs' goals. They also argue that the extensive use of constraints compromises the principles of local self-governance and political accountability.

The counter argument is that constraints are necessary to further important national social and economic goals. While contending that most regulations are appropriate given the expansion in federal responsibilities, some constraints might nevertheless be criticized for being ineffective in furthering federal goals.

TYPES OF CONSTRAINTS

There are two general types of federal constraints on state and local action—mandates and contractual obligations:

- o Mandates, the more coercive of the two types, are direct federal orders that state and local governments must follow. Most mandates are the result of court decisions interpreting the Constitution; for example, directives to provide legal counsel to the indigent, or orders to desegregate schools. Some, but not many, mandates derive directly from federal law. Examples include the various laws prohibiting discrimination in employment, and the Safe Drinking Water Act of 1974, requiring that drinking water be tested for impurities and that corrective steps be taken whenever necessary.

- Contractual obligations include constraints imposed as a result of agreements between the federal government and state and local governments. Such agreements are generally prompted by the availability of federal grants in aid. Conditions are specified as prerequisites for program participation. Some conditions are "program specific"; that is, they specify when and how money for a certain program is to be spent to insure consistency with stated objectives. Other conditions are generally applicable to grant programs; their purpose is to insure that all federally funded activities are consistent with broad national goals, such as nondiscrimination and environmental protection. Not all contractual obligations stem from grant-in-aid programs. Some, for example, arise as a result of federal regulatory programs. For example, under the Occupational Safety and Health program, states have the option of assuming administrative responsibility, provided they agree to abide by certain federal standards and guidelines.

ANALYSIS OF COSTS AND BENEFITS

Federal constraints involve costs, some of which fall on state and local governments. At present, little is known about the magnitude or distribution of these costs, although interest in developing an aggregate cost figure is great. Such an estimate would be very difficult to produce, since it would involve compiling a full inventory of constraints, as well as developing acceptable methodologies for estimating costs. Furthermore, the usefulness of such an aggregate figure would be limited, since decisions are made with respect to specific laws and regulations. Moreover, a judgment about whether or not these costs are excessive could not be made without a corresponding analysis of benefits and a review of possible alternatives.

Estimating the state and local costs and benefits resulting from specific laws or regulations is difficult. Many different types of effects--some of which are not readily measured--have to be considered. For example, analyses ought to take into account private as well as public, indirect as well as direct, intangible as well as tangible, and continuing as well as one-time costs and benefits.

Furthermore, incremental costs should be distinguished from total costs. Only those costs and benefits associated with actions that would not have occurred were there no federal intervention should be attributed to a mandate or to a condition of aid. Since there is overlap in the constituencies of policymakers at the federal, state, and local levels, it is not surprising that many constraints require actions that at least some state and local governments would have taken anyway.

Total and incremental costs may also differ, because of a redundancy in federal requirements. For example, as a condition for receiving federal aid, a state or locality may be required to prove compliance with an already existing federal law. Only those costs and benefits associated with a change in compliance can be attributed to the newer program.

The distribution of effects among jurisdictions is another consideration in the analysis of costs and benefits stemming from intergovernmental constraints. Analyses based on data aggregated at the national level may prove insufficient to the federal policymaker who wants to know not only whether a given course of action makes sense overall, but also whether it imposes unacceptably heavy burdens on specific jurisdictions.

POLICY OPTIONS

Critics who contend that intergovernmental constraints pose a problem want the Congress and the Executive Branch to consider changes in decisionmaking procedures and policies that would lower the number of constraints, increase their efficacy, and lighten the financial burdens they impose. There are several approaches the Congress might consider in response to this issue.

The first alternative is to take no explicit action, relying instead on the political process to prevent or change laws or regulations that impose excessive burdens on state and local governments.

A second course that the Congress might consider is to alter decisionmaking processes so that concerns about constraints on state and local governments are more likely to be addressed. Possible changes include:

- Requiring that analyses of state and local impact be undertaken before the Executive or Legislative Branch makes major decisions. Such a stipulation would complement recent executive orders requiring agencies to prepare urban and community impact analyses for major program changes and analysis of economic consequences—including effects on state and local governments—for all proposed regulations. State and local impact analyses would also supplement the information on the federal costs of most bills that the Congressional Budget Office now regularly gives to the Congress.

- Increasing Congressional oversight over agency rule making. Since many constraints are imposed as part of regulation, careful scrutiny of agency rule making could result in fewer problematic constraints.

A third approach would be for the Congress to attempt to lower the number of constraints by changing the structure and substance of federal policy. Specifically, it might consider the following:

- Reforming the administration of grant programs. Although steps have been taken to improve the management of grant programs, the number and complexity of requirements could still be reduced by better coordination and by more standardization of procedures among different programs and agencies.

- Consolidating existing grant programs or relying more on block grants as opposed to categorical grants. At present, there are more than 440 categorical grant programs, many of which are very narrow in scope. Administration would be smoother if grants with similar purposes were consolidated. If this were done, however, the federal government's ability to set priorities would be weakened.

- Establishing a policy of fiscal reimbursement for some or all of the costs that federal constraints impose on state and local governments. Proponents of this approach argue that if Congress were required to appropriate funds, it might limit the number of requirements to those of most importance and proven effectiveness.

CHAPTER I. INTRODUCTION

In recent years, state and local officials have been troubled by the degree to which their actions are dictated or constrained by decisions made at the federal level. They see the system of regulation that has developed as costly, inefficient, and inflationary. Their concerns parallel many of those of private businessmen.

In addition, there is the fear that two important principles—local self-governance and political accountability—are both being undermined by federal actions. Local resources and energy are finite. When resources are allocated to follow dictates from higher authorities, they are diverted from locally identified needs and priorities. The principle of political accountability may be compromised inasmuch as state and local officials are identified with—and held responsible at the polls for—actions over which they have little control. Federal officials, meanwhile, may escape the political onus of the unpopular actions they order.

THE FEDERAL PERSPECTIVE

Most federal officials would agree that some regulations are ineffective or too costly. At the same time, however, they would argue that most regulations are necessary for implementing federal programs and for achieving national policy objectives.

Many of the regulations imposed on state and local governments are part of federal grant programs that have been enacted over the years in response to proven problems or needs. Because federal lawmakers are accountable to their own constituents, they must take steps to insure that federal funds are spent for the purposes intended. When state and local governments choose to participate in a grant program, they do so with the knowledge that their actions will be subject to federal review and regulation. Continued participation by state and local governments suggests that, regardless of regulation, they perceive that the programs' benefits outweigh their costs.

Some intergovernmental constraints stem from federal regulatory policies designed to end practices determined to have high social costs. Most such regulations are directed toward the private sector: private businesses are prevented by federal law from engaging in unfair labor practices; they must meet safety standards for work places, adopt pollution control technology, and so forth. Occasionally, regulatory policies also dictate or constrain state and local government actions. Some people argue that, to the extent that state and local governments engage in practices similar to those of businesses, their exclusion from federal regulation raises questions of equity and prevents the full achievement of national policy objectives.

Other constraints have been imposed because state and local governments have failed to fulfill their responsibilities under the Constitution. Both the federal courts and the Congress have acted to ensure that individuals' Constitutional protections are honored when state and local governments serve as employers, law protectors, and providers of services.

FEDERAL CONSTRAINTS AS AN ISSUE

The major reasons why intergovernmental constraints have emerged as an issue is that, over time, federal regulations have increased in number and complexity. As the federal government has expanded its role as social and economic problem solver, it has established numerous new programs and a concomitant number of regulations. Since many of the problems new programs address are inherently technical and complex (for example, environmental pollution), so too must be the accompanying regulations. Furthermore, as programs mature and administrators face diverse and unforseen circumstances, regulations tend to multiply.

Contributing to the concern over federal constraints is the increasing number of governments affected. Many of the newer grant programs involve local governments that had never before participated in the federal grant system. The burden of compliance with regulations may be greater in these smaller jurisdictions, which have less specialized staffs and less experience in dealing with federal officials.

Judicial actions have also contributed to the emergence of the issue. Besides handing down some controversial rulings based on the Constitution, the courts have assumed an important

role as enforcers of statutory and administrative law. This has occurred because citizen and other interest groups have increasingly resorted to litigation as a way to change government behavior. For example, the discretion of welfare program administrators has been reduced and the welfare rolls expanded as a result of successful litigation by welfare rights organizations. Public works projects have been halted or delayed by court orders following the discovery that procedures for environmental review had not been carried out.

As concern over inflation has mounted, attention has been drawn to all possible causes, including federal regulation. Although the regulation of private sector activity is more often cited, federal constraints on state and local governments also can be inflationary. If the federal government requires actions that are inefficient methods of achieving goals, inflation is a certain outcome. Regulations resulting in different or better state and local services could also cause the cost of services to increase, but these changes would not necessarily be inflationary.

The salience of the issue of intergovernmental constraints goes beyond these developments, however. To state and local officials, certain constraints seem more onerous in times of budgetary stringency than they do in periods of budgetary expansion. Inflation, recession, taxpayer revolts, and tax and expenditure limitation laws have all combined to force state and local officials to reexamine their budgets. As a result of these reexaminations, they realize the degree to which their options are constrained and their costs increased by requirements imposed by higher levels of government.

While intergovernmental constraints are often discussed by public officials and have been the subject of resolutions by their organizations, there is little common understanding of the range of federal actions being disputed or of the cost burden. This paper is a preliminary step in sorting out the issues. It is purely conceptual, and it provides neither an inventory of intergovernmental constraints nor an estimate of associated costs.[1] The study has four objectives: to categorize the types of constraints (Chapter II); to discuss types of costs and benefits that should be considered in deciding whether constraints should be adopted or continued (Chapter III); and to examine various approaches the Congress might take in dealing with the issue of intergovernmental constraints (Chapter IV).

CHAPTER II. TYPES OF CONSTRAINTS

The different types of federal requirements that directly affect state and local governments and that involve some degree of coercion are examined in this chapter. These requirements fall into two categories--mandates and contractual obligations:

- Mandates are formal orders issued by the federal government, which is legally the higher government and is thus entitled to give orders under certain circumstances. State and local governments have little option but to comply with federal orders.

- Contractual obligations are conditional; they come about when state and local governments enter into binding agreements with the federal government. Most contractual obligations are associated with federal grant programs.

According to the Constitution, there are limitations on the right of the federal government to mandate the actions of state and local governments. Thus most federal requirements stem from contractual agreements. Compared to the federal government, states are much less restricted in their behavior toward local governments. As a result, state laws include many more direct orders.[1] It should be noted, however, that numerous state mandates have their origin in federal constraints imposed on the states by way of the grant-in-aid system.

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1. For a full discussion of state mandates, see the Advisory Commission on Intergovernmental Relations, State Mandating of Local Expenditures, (A-67, July 1978). See also, State Limitations on Local Taxes and Expenditures, (Rept. A-64, February 1977).

MANDATES

Direct orders, in the form of mandates, may come from any of the three branches of the federal government. They may be based either on federal statutes or directly on the Constitution. Most mandates affect only the private sector, so they are outside the purview of this discussion. Some, however, are directed exclusively toward state and local governments, and others apply to the public and private sectors simultaneously.

Mandates Based on Court Orders

Most federal mandates that apply only to state and local governments stem from judicial interpretation of the Constitution, in particular, the Bill of Rights and the 14th Amendment. A wide range of state and local activities have been affected by such rulings. For example, the Supreme Court has ordered that electoral districts be redrawn, schools be desegregated, free counsel be provided for indigents, juvenile court procedures be reformed, and prisons and mental institutions be upgraded.

While direct court orders are issued to certain specific jurisdictions named in adjudicated cases, the principles articulated in court opinions often have general applicability. Jurisdictions not named in the cases are in effect mandated to change their behavior, too, since not to do so would expose them to court challenge. For example, as a result of Brown v. Board of Education, the court ordered Topeka, Kansas, to desegregate its schools. The impact of the Brown decision, however, was very far reaching: school systems across the country were signaled that the time had come to end de jure segregation of schools.

Mandates Based on Federal Statute

The Congress often attempts to achieve social and economic objectives by using its regulatory powers. Laws are passed and administrative regulations are promulgated proscribing certain actions and prescribing others. Mostly, these mandates have been directed toward the private sector. The scope of some social and economic regulatory policy, however, includes state and local government actions.

Most mandates affecting state and local governments are found in laws concerning either the environment or civil rights. A number of examples follow:

- The Clean Air Amendments of 1970 (Public Law 91-604) require states to develop plans acceptable to the Environmental Protection Administration (EPA) to attain federal air-quality standards. The EPA can require states to plan changes in state transportation policies (for example, by giving additional support to mass transit) as well as to regulate the pollution-creating activities of private persons (by establishing, for example, emission-control requirements and inspection programs for private cars).

- The Federal Water Pollution Control Act of 1972 (Public Law 92-500) requires state and local governments to adopt better methods of treating sewage in order to curb the discharge of pollutants.

- The Safe Drinking Water Act of 1974 (Public Law 93-523) requires all suppliers of drinking water (including, but not limited to, publicly owned systems) to test their water regularly for impurities. If "maximum contaminant levels" are exceeded, acceptable treatment processes must be introduced or another source of potable water used.

- The Equal Employment Opportunity Act of 1972 (Public Law 92-261) prohibits state and local governments from discriminating in their employment practices on the basis of race, color, religion, sex, or national origin.

- The Age Discrimination in Employment Act of 1967 (Public Law 90-202) prohibits discrimination in employment practices on the basis of age.

The constitutionality of efforts to regulate state and local actions has recently been called into question. Authority to regulate both the private and public sectors stems from the Commerce Clause, the Necessary and Proper Clause, and the 14th

Amendment of the Constitution.[2] Since the 1930s, the Supreme Court has consistently upheld Congressional regulation of private business, including, for example, laws prohibiting discrimination in employment, housing, and public facilities; statutes establishing minimum wages and other fair labor practices, and so forth. While for political reasons, the Congress has rarely passed laws mandating state and local government activities, until recently, it was widely assumed to have the legal authority to do so. In 1976, however, the Supreme Court ruled in National League of Cities v. Usery that the 10th Amendment guarantee of state sovereignty implies certain restrictions on Commerce Clause powers as applied to state and local governments. Specifically, the Court invalidated the 1974 amendments to the Fair Labor Standards Act (Public Law 93-259) that extended minimum wage and overtime pay protection--rights that had long been enjoyed by employees in the private sector--to non-supervisory state and local government employees. The Court ruled that the extension of these provisions impermissably interfered with the integral functions of state and local governments and threatened their "separate and independent existence."[3]

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2. The "Commerce Clause" and "Necessary and Proper Clause" are both part of Article I, Section 8 of the Constitution. It reads, "The Congress shall have the power . . . [3] to regulate commerce with foreign nations, and among the several states and with the Indian tribes . . . [18] to make all laws which shall be necessary and proper for carrying into execution the foregoing powers and all powers vested by this Constitution. . . ." Additional authority is granted in the 14th Amendment. Section 1 reads: ". . . No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty or property without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws." Section 5 reads: ". . . the Congress shall have power to enforce, by appropriate legislation, the provisions of this article."

3. National League of Cities v. Usery, 426 U.S. 833 (1976).

How broadly the legal reasoning articulated in the National League of Cities decision will be applied is as yet unclear. Clarification is required on two major issues. First, what is the range of activities that are crucial to the states' "independent existence" and that must be protected from Congressional action? And second, is the protection offered absolute or only partial--subject to a balancing of the federal interest in the objective to be achieved by the regulation and the state's interest in freedom of action?[4]

Although the National League of Cities decision suggests limits on the Congress' authority to issue direct orders to state and local governments, the decision does not preclude the use of other, less coercive means to achieve similar ends. As discussed in the next section, the Congress can offer inducements of various sorts to get state and local governments to change their behavior.

CONTRACTUAL OBLIGATIONS

Numerous intergovernmental constraints have their bases in contractual relationships. When the Congress determines that a national policy objective can be furthered by some change in state or local behavior, it may seek voluntary cooperation. In effect, the federal government proposes to enter into a contractual arrangement: it offers some benefit (generally, but

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4. Major questions regarding the scope and implications of this decision remain for several reasons. First, while five Justices were in agreement on the outcome in the National League of Cities case, there did not appear to be a consensus regarding the legal standard; only four Justices signed the Court opinion with a fifth filing a separate concurring opinion. Second, the decision is a clear departure from past reasoning by the Court (for example, Maryland v. Wirtz 392US183 [1968]), so there are few precedents to draw on for clarification. And finally, the court has not had occasion since the National League of Cities decision to decide whether the principles enunciated in that case affect statutory mandates other than those for minimum wage and overtime pay. The lower courts have tended to decide related cases on narrower grounds and have not extended the reach of the case to other areas.

not exclusively, in the form of financial assistance), in return for state and local government agreement to act in a given way subject to federal regulation. For numerous historical and political reasons, intergovernmental constraints stemming from voluntary agreements are more common than are federal mandates.

Federal grant programs are the source of most contractual obligations. Occasionally, however, other circumstances will prompt such agreements imposing requirements on both parties. These are discussed briefly following the section on conditions of aid.

CONDITIONS OF AID

Federal grants are made available to state or local governments contingent on the potential grantees' willingness to implement certain programs and/or to meet conditions specified in federal law or in administrative regulations.

Voluntary or Mandatory?

Although constraints that are imposed as conditions of aid technically are incurred voluntarily, they may, for a variety of reasons, seem mandatory from the perspective of state or local officials. This is the case for the following three reasons:

- The choice to participate in the federal program may be made by state officials, but the burden of administering the program in accordance with federal regulations falls on local governments. For example, Aid to Families with Dependent Children (AFDC) is a grant program available to states. Yet in 18 states, local government agencies are responsible for administering the program. The regulations guiding local administrators come from their state governments, but many have their source in federal regulations.

- Conditions of aid may have changed since the decision to participate was originally made. While participation remains voluntary, state and local officials may believe that, despite the change in regulations, they have no option but to continue participation, since constituents rely on the service provided. Since it is not

feasible for states to assume the federal share of program costs, regulations imposed after a program is underway are perceived as tantamount to mandates. The 1976 amendments to the Unemployment Insurance (UI) law offer an example. In order for states to continue to qualify for grants for administration and for employers within the state to continue to receive a federal tax credit for UI taxes paid to the state, coverage must be extended to all public employees. The costs of noncompliance are perceived as being so high as to make the change in regulation seem coercive.

- Current constraints may stem from decisions made several years earlier. For example, in order to receive federal aid for the construction of a highway, a state must agree to keep the road up to federal highway safety standards. Decisions made as long ago as 20 years thus constrain the budgetary choices available to present day state and local officials.

Program-Specific Versus Generally Applicable Grant Requirements

Certain grant program regulations are described as "program-specific," meaning that they apply to a single program and are intended to guide program administration in ways that federal officials deem best for achieving that program's goals. Other regulations are general in that they apply to many grant programs and are designed to further national policy goals more or less independent of specific program goals. The two types of requirements described--program-specific or general--represent polar opposites, and many program requirements fall somewhere along the continuum between the two. For the sake of discussion, however, various program requirements are classified here as either program-specific or general.

Most aid requirements are program-specific, and these are of two sorts: programmatic and procedural. Programmatic requirements specify the scope, quality, or quantity of the service to be provided with the program money. For example, medicaid regulations specify and describe a certain eligible population (all AFDC and Supplemental Security Income recipients) and kinds of services to be provided, (for example, inpatient hospital care, physician services, laboratory and X-ray charges, and so forth). Procedural requirements dictate some aspects of

how the programs are to be administered. The most common procedural requirements relate to planning, reporting, and fiscal management. For example, General Revenue Sharing (GRS) recipients are required to report annually to the Department of the Treasury on how they use their GRS funds. They must also have an outside audit done according to generally acceptable auditing standards once every three years.

Program-specific regulations are often objected to on grounds that they are cumbersome, costly, and inefficent. State and local officials argue that conditions are so diverse that no single set of regulations can be appropriate everywhere. On the other hand, if an effort is made to write regulations applicable to every set of circumstances, the system becomes so complex as to be unworkable. State and local officials also argue that the problem is exacerbated by lack of coordination among federal agencies and by a tendency to write regulations that are more concerned with how a program is to be run rather than with what is accomplished.[5]

Sometimes federal regulations draw complaints on grounds that they amount to inappropriate extensions of federal authority. Most people would agree that the federal government has a legitimate interest in how federal funds are spent and that regulations directed toward that end are acceptable. But when regulations are written to further federal goals by directing state or local actions that may be related in function but that are otherwise independent of the grant-aided activity, state and local officials object. The following are some examples:

- The Land and Water Conservation Act includes a provision that no land purchased by the state with federal funds can be used for anything other than recreation without the consent of the Secretary of the Interior. This provision has been interpreted as meaning that if federal funds are used to purchase a 10-acre parcel of land to be added to a several-hundred-acre state forest, then

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5. See National Governors Conference, Federal Roadblocks to Efficient State Government, Vol. 1, February 1977, pp. 1-8 and pp. 13-19.

the whole state forest comes under the rules of the Bureau of Outdoor Recreation.[6]

- The 1976 amendments to the Unemployment Insurance Compensation Act make the federal tax credit for private employees' contributions to state unemployment insurance funds and the state governments' participation in grants for administration contingent upon the extension of unemployment insurance to state and local employees.

- The National Health Planning and Resources Development Act of 1974 makes receipt of federal health grants contingent on the establishment of health planning agencies that administer "certificate of need" programs, regulating decisions by hospitals and nursing homes to expand facilities or to purchase major new equipment.

Some conditions of aid have little to do with the specific purposes or objectives of the programs to which they are attached. On the contrary, in an effort to further broad national policy objectives, such as environmental protection or nondiscrimination, generally applicable grant requirements are put in place. The objectives are deemed sufficiently important to disallow federal support of any project that would interfere with their achievement. Generally applicable requirements are an important means of insuring consistency with federal policy. For example, the general environmental review requirement prevents the federal government from doing more harm to the environment with a local public works grant than it does to help it through a conservation program.

Generally applicable grant requirements are put into effect in two ways. Separate laws may be passed making a requirement applicable to all grant programs across the board. Title VI of the Civil Rights Act of 1964 (Public Law 88-352), which prohibits discrimination in any program or activity receiving federal financial assistance, is an example. Alternatively, the requirement may be appended to each statute authorizing a grant program. For example, most statutes authorizing grant programs for construction contain a clause invoking the

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6. See National Governors Conference, Federal Roadblocks to Efficient State Government, Vol. 1, February 1977, p. 11.

Davis-Bacon Act, which requires that all laborers employed on a federally funded project be paid at rates not lower than those being paid on private construction in the same locality.

In a major study of the federal grant system, the Advisory Commission on Intergovernmental Relations (ACIR) identified several groups of general policy requirements.[7] Several of these categories are described in the following paragraphs:

- o Nondiscrimination. Mandated prohibitions against discrimination in employment are supported by grant-in-aid regulations prohibiting the use of federal funds for discriminatory practices. Title VI of the Civil Rights Act of 1964 offers the most general protection against racial bias. It states that "no person in the U.S. shall on the ground of race, color or national origin, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving federal financial assistance." Similar protection has been accorded to the handicapped and to the aged.[8] The provisions regarding handicapped persons are particularly controversial, since compliance can involve considerable outlays of money to modify existing structures in order to accommodate handicapped persons. Although sex discrimination has not been prohibited in federal aid programs on an across-the-board basis, provisions have been appended to a number of the statutes authorizing specific programs.

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7. See Chapter 7, in ACIR "Generally Applicable National Policy Requirements," Categorical Grants: Their Role and Design, (Report A-52, 1978).

8. Section 504 of the Rehabilitation Services Act of 1973 (Public Law 93-112) states that "No otherwise qualified handicapped individual in the U.S. shall, soley by reason of his handicap, be excluded from participation in, be denied the benefits of, or be subjected to discrimination under any program or activity receiving Federal financial assistance." The Age Discrimination Act of 1975 (Public Law 94-135), using similar language, prohibits discrimination based on age.

Environmental Protection. The National Environmental Policy Act of 1969 (Public Law 91-190) requires that all financial assistance programs, including both loans and grants, be reviewed to determine whether they will have a "significant impact" on the environment. A statement of the anticipated environmental impact must be prepared before the proposal can be funded. Specific things to be considered in the review process are stated in several laws and executive orders. These include the effects on air and water quality, on fish, wildlife, and endangered species, on "wild and scenic" rivers, on historic and archeological sites, and so forth.

Relocation and Property Acquisition. The Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 requires that anyone displaced as a result of a federally funded activity be compensated fairly. The law and its regulations set standards governing the acquisition of property and the benefits and services to be provided to displaced residents.

Labor and Property Procurement Standards. Two laws with general applicability regarding the use of grant funds are the Davis-Bacon Act of 1931 and the Work Hours Act of 1962. As written, the Davis-Bacon law required that workers on federal construction projects be paid at locally prevailing wage rates. Its provisions have now been extended to state and local government construction projects that are funded by the federal government under any of 60 different grant programs. The Work Hours Act specifies that employees carrying out federally funded activities must be paid overtime rates for hours worked in excess of eight-hour days and 40-hour work weeks. The Federal Procurement Policy Act of 1974 allows federal regulation of the procurement of services and goods other than real property using federal grant funds, but to date no generally applicable regulations have been issued. "Buy America" provisions, however, which currently constrain federal government purchases to domestically produced raw and manufactured materials, have been extended to four large federal grant programs during the past two years.

- o Citizen Participation. Requirements for citizen participation in the implementation of grant-aided programs are increasingly common, though the exact stipulations vary from program to program.

Conditions of aid designed to further broad national policy goals have been objected to on several grounds. The major complaint is that they divert resources away from--and thereby hinder the achievement of--the primary goals of grant programs. General policy requirements are often imposed without any increases in program funding. To the extent that these requirements are costly to implement, resources are either diverted from program operations or an additional commitment of state/local revenues is required. For example, the requirement for environmental review is likely to increase the costs of any project to which it is applied. It costs something to perform environmental impact analyses. Furthermore, if a project is delayed or modified to meet environmental objections, its costs are likely to increase. So long as appropriations are fixed, added costs may mean fewer projects can be undertaken and that specific program goals (for example, improved transportation) would be sacrificed in favor of environmental considerations.

Another criticism lodged against generally applicable regulations is that they may not be cost-effective. State and local officials dispute whether the means set forth by the federal government for the achievement of national policy objectives are the most efficient ones available. For example, some critics have argued that public transportation is better made available to the handicapped by means of taxi vouchers or some other form of personalized service than by adapting existing buses and subways, as is now proposed by the Department of Transportaton.[9]

Some generally applicable regulations are disputed on grounds that they further goals that the grant recipients care little about achieving. For example, the Davis-Bacon Act requirement that prevailing wage rates be paid to workers on grant-funded projects is perceived by many state and local

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9. Department of Transportation, "Nondiscrimination on the Basis of Handicap, Federally Assisted Programs and Activities; Notice of Proposed Rulemaking," Federal Register, June 8, 1978, Part V.

officials as doing little more than increasing the power of unions in the construction trades. Some officials object to incurring costs that further this goal.

OTHER CONTRACTUAL OBLIGATIONS

State and local governments sometimes enter into agreements with the federal government for reasons other than the availability of financial aid. These agreements vary in terms of the benefits derived and the requirements imposed. Some examples are discussed below:

- Social Security coverage. Participation in the Social Security system is mandatory for private employers, but it is optional for public employers. At present, nearly 9.5 million, or 75 percent, of state and local employees have Social Security coverage under 50 state agreements. Wherever there are agreements, state and local governments and their employees are subject to requirements governing taxation and benefits.

- Occupational Safety and Health. In 1970, to help curtail work-related injuries and illnesses, the Congress authorized the establishment of safety standards in private places of business. In general, enforcement of these standards is a federal responsibility. The law provides for intergovernmental agreements, however, whereby states would assume responsibility for the administration of health and safety standards. A condition of any such agreement is the willingness of states to extend equivalent protection to public employees within the state. At present, 21 states have chosen the state-enforcement option.[10]

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10. When states assume responsibility for administering Occupational Safety and Health Administration (OSHA) standards, they receive small grants covering part of the costs. One state in addition to the 21 cited above administers an OSHA program for public employees but leaves administration of the private sector program to the federal government.

CONCLUSIONS

Of the two types of federal constraints discussed in this chapter--mandates and contractual obligations--the former are the more coercive. They are less of an issue, however, since not so many of them exist, and of those that do, many are beyond the control of the Congress. Of greater concern are constraints originating in contractual obligations, particularly those that are conditions of receiving federal financial aid.

CHAPTER III. ASSESSING COSTS AND BENEFITS

The total costs associated with federal constraints—particularly that portion of costs not borne by the federal government—are matters of widespread interest. At present, no estimate of total costs exists, and it is not clear that one could be produced. The difficulties of compiling an inventory of constraints and of estimating the costs of compliance for all state and local governments are formidable.[1]

Even if an estimate of total costs were available, its usefulness to federal policymakers is uncertain. This is the case for several reasons:

- Costs considered without regard to benefits offer little basis for evaluation. If federal constraints are a problem, it is not because they are costly per se but rather because they are costly relative to the benefits they yield or relative to the benefits that other uses of the same money could yield.

- Aggregate costs give little guidance to policymakers who must make decisions on specific laws or regulations. Even if the total costs imposed by federal constraints were found to be too high, more information would be needed to know what policy changes would correct the problem. In other words, an estimate of total costs would only be useful if it were backed up by an estimate of costs for each federal mandate or condition of aid.

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1. A major research effort funded by the National Science Foundation is currently underway in the School of Administration, University of California-Riverside. The study's aims are to inventory federal and state constraints affecting local governments and to develop a methodology for estimating the costs associated with these constraints. The completed study will also contain preliminary cost estimates.

- Aggregate costs provide little information regarding the burden imposed on specific types or levels of government. Costs are not distributed evenly among state and local governments. A situation that seems satisfactory or beneficial for state and local governments in general may nevertheless be problematic for certain specific governments. Focusing on aggregate costs would reveal nothing about particular jurisdictions' problems.

Although the utility of an estimate of total costs is uncertain, knowing the effects of specific laws or regulations on state and local governments would be useful to federal policymakers. Judgments regarding equity and efficiency would be facilitated if decisionmakers knew the magnitude of the costs and benefits imposed, how the costs and benefits are distributed among states and different types of local governments (for example, cities and counties), and whether they compare favorably with what could be achieved by alternative actions.

This chapter discusses the various types of costs and benefits that ought to be considered when any government action is evaluated. In addition, it examines the particular conceptual and measurement difficulties that arise when intergovernmental constraints are at issue.[2]

TYPES OF COSTS AND BENEFITS

Public and Private Costs and Benefits. Intergovernmental constraints, by definition, have as their primary goal a change in state and local government behavior. Government actions involve costs (personnel, equipment, and so forth), which are generally referred to as public, even though they are ultimately borne by tax-paying private citizens. But government actions may result in direct private costs as well, that is, costs apart from taxes. Such costs occur when a mandate or condition of aid causes changes in private as well as public actions.

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2. See Julius Allen, Estimating the Costs of Federal Regulation: Review of Problems and Accomplishments to Date, Congressional Research Service, Report No. 78-205E, for a related discussion focusing on federal regulation of the private sector.

As an example of these costs, consider a mandated state plan to improve air quality standards. Such a plan is likely to involve auto emission control standards and inspection. The state would incur costs in the development and administration of the state plan. Owners of older cars would bear the costs of the additional equipment and maintenance needed to keep cars operating up to standard. These costs would be in addition to those borne at the time of car purchase as a result of the direct federal regulation of car manufacturers regarding the installation of air pollution control equipment.

Benefits arising from state or local governments' response to a federal directive may accrue to particular client groups, to the public at large, or to the government itself. For example, a reduction in air pollution achieved by state implementation of federal air quality standards should result in several benefits. If the air is cleaner, health problems should be decreased; the populace as a whole may profit from this improvement, but the benefit would be greatest for the elderly and anybody with respiratory problems. The benefit should also be felt by state and local governments to the extent that they finance or directly provide health-care services. Clean air should also result in lower maintenance costs (less cleaning, less frequent painting, and so forth) and a longer useful life for physical objects such as cars, buildings, and bridges.

Direct Versus Indirect Costs and Benefits. Some costs and benefits follow directly from the action specified by a federal constraint. Direct costs include those incurred by state or local governments, or by private parties, as they comply with the mandate or condition of aid. Direct benefits are generally those that were intended and that justified the imposition of the constraint in the first place; however, other direct benefits may also be realized. Indirect costs or benefits are those that follow, generally with some lag, as economic and social adjustments to the change in government policy are made.

These distinctions are best illustrated by an example. Consider the requirement that states adopt a 55 miles-per-hour speed limit, which in 1974 was made a pre-condition for the receipt of federal highway aid.[3] Direct, one-time costs were imposed on governments because speed limit signs had to be

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3. Federal Aid Highway Amendments of 1974 (Public Law 93-643).

altered or replaced. Continuing costs could include additional police patrol and court costs because more people would be inclined to violate the limit. Another continuing cost would be reduced revenues from gasoline taxes if compliance led to better fuel efficiency and fewer gas purchases. Of course, private businesses and individuals also bear costs. At lower speeds, it takes longer to get from one place to another. Ultimately, reflecting the higher costs of transportation from production through marketing, the consumers must pay higher prices. Direct benefits include energy conservation and accident reductions attributable to slower driving speeds.

Indirect costs are borne as production and consumption patterns change in response to price changes. Some companies may find their markets contracted, and others may go out of business when added transportation costs make their product noncompetitive. Interstate trucking firms may lose business to railroads; firms and places with access to rail transportation may benefit, while those that rely exclusively on trucking may lose.

From the perspective of any given individual, business, or place, these second-order effects can be very real and very important. From a national perspective, indirect gains and losses may balance out, and as a result, they are often omitted from analyses seeking to determine the efficiency of a given action. The pattern of gain and loss may be an important consideration, however, in evaluating whether an action is fair and equitable.

Tangible Versus Intangible Costs and Benefits. While dollar values can be assigned to many costs and benefits expected from a government action, certain effects are less tangible and more difficult to quantify. Indeed, a number of services—pollution control or police services, for example--are provided publicly rather than privately precisely because of the difficulties in pricing the benefits.

Costs, too, can be intangible. Consider the requirement that there be "maximum feasible" participation by affected citizens in planning and operating a Community Action Program in the 1960s.[4] That requirement gave rise to relatively few

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4. Title II of the Economic Opportunity Act of 1964 (Public Law 88-452).

tangible costs. In some instances, however, intangible costs in the form of city-wide tension and conflict were very high. Likewise many of the benefits from the citizen participation requirement were also intangible—for example, the development of leadership skills in impoverished communities.

More common is the case in which costs are quantifiable but benefits are not, leading to an imbalance in analysis and possibly to misleading conclusions. Requirements of the National Environmental Protection Act of 1969 (NEPA) provide a good illustration. Cost considerations include: staff time to research and prepare environmental impact statements; price increases attributable to the combination of inflation and the lengthened time between project conception and actual construction; and project changes necessary to minimize adverse environmental effects (for example, rerouting a highway in a way that adds to its length). Calculating the benefits is more difficult. How do you quantify the value of preserving marshes or coastal wetlands so that birds can maintain their migration patterns or that an endangered species can survive? Yet it is precisely because such things are valued that there was at least an initial willingness to require environmental review despite the costs it was known to entail.

One-Time Versus Continuing Costs and Benefits. Some costs and benefits occur only once, while others continue. Regulations under Section 504 of the Rehabilitation Services Act, requiring program accessibility to the handicapped, impose both kinds of costs. The prohibition of architectural barriers in new buildings results in one-time costs. Proposed Urban Mass Transit Authority regulations, however, could impose both one-time and continuing costs, since buses accessible to the handicapped—so-called "kneeling buses"—are more costly both to purchase and to operate than are ordinary buses. Operating costs are expected to increase because mechanical equipment that allows accessibility requires additional maintenance. Also, since buses usable by the handicapped carry fewer passengers, a city transit system may need more of them to maintain an adequate level of service.

Total Versus Incremental Costs and Benefits. Analyses of government regulations must take account of the distinction between total and incremental costs. Total costs and benefits are usually calculated assuming that all actions consistent with a federal regulation are in fact attributable to that

regulation. This approach results in an overstatement, because the federal government rarely requires something to be done that some state or local governments would not do of their own volition. In other words, some actions would have taken place anyway. Only the costs and benefits of actions that would not have occurred were there no federal intervention should be attributed to a federal mandate or condition of aid.

Consider, for example, the costs and benefits associated with the mandate that all sewage be treated using the "best practicable" technology before the sewage is discharged into any waterway.[5] Presumably, by 1983 all municipalities will be in compliance, and the nation's waterways will be substantially cleaner than in 1972 when the mandate was imposed. But what proportion of the total costs and benefits will be directly attributable to the federal mandate?

One alternative is to consider the mandate responsible for all costs incurred in the treatment of sewage and for all the associated benefits. This seems unreasonable since many municipalities had sewage treatment programs before 1972. No mandate should be credited with costs or benefits accrued prior to its adoption.

A second alternative is to count the full cost and all of the associated benefits of adopting or upgrading technology to meet standards specified by the mandate. The resulting estimate assumes implicitly that no municipality would have changed its sewage treatment procedures after 1972 had the federal law not been passed. This assumption seems unrealistic, however, since at least some state and local decisionmakers would probably have been influenced by the same environmental movement that brought about federal action.

A third alternative for assessing the costs and benefits of the federal mandate, then, is to compare the level of activity in sewage treatment specified by the mandate with a projection of what the level would have been if there were no mandate. This approach seems reasonable, but it is extremely difficult to carry out because it requires a causal model of state and local behavior.

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5. Federal Water Pollution Control Act of 1972.

Redundancy of regulation may also result in incremental costs and benefits being less than total costs and benefits. Sometimes state or local governments will be subject to some prior law or regulation mandating the same action. The requirement may be repeated to reiterate federal commitment to the policy and to increase the speed or level of compliance on the part of state and local governments. When a regulation is redundant, it is not clear how costs and benefits should be counted. For example, nondiscrimination in employment is a condition for receiving most federal grants; at the same time, state and local governments are prohibited by federal law from engaging in discriminatory employment practices. Does nondiscrimination as a condition of federal aid result in additional costs or benefits? The answer would depend to a large extent on the degree to which there was or would have been compliance with the previously enacted federal law.

Compliance. In general, a maximum level of costs and benefits would be calculated by assuming full compliance with federal requirements by state and local governments. In reality, compliance will be less than 100 percent; a lower estimate of costs and benefits taking this into account might provide a more realistic basis for making decisions.

Variations Among Jurisdictions. An intergovernmental constraint will have different effects in different jurisdictions. This is due both to place-to-place variations in policy and to differences in objective circumstances. Consider again the case of the sewage treatment mandate. The cost of the federal mandate can, of course, be relatively large for communities with no prior treatment capability. Little if any additional costs will result for municipalities that were already using the best available treatment technologies when the new mandate went into effect. For some jurisdictions, however, substantial benefits may accrue if the mandate forces municipalities upstream to reduce the discharge of pollutants.

Because costs and benefits are likely to vary so much from jurisdiction to jurisdiction, analyses conducted using data aggregated at the national level may provide insufficient information to the decisionmaker. While the ratio of costs to benefits may be satisfactory for the nation as a whole, unacceptably large burdens may nevertheless be imposed in some jurisdictions. Clearly, it would not be feasible to consider the effect

of proposed mandates and requirements on each and every jurisdiction. But because of the variation among jurisdictions, it would be desirable to consider the consequences of decisions for a sample of jurisdictions representing diverse situations.

EXAMPLE OF A COST/BENEFIT ANALYSIS

To illustrate the problems discussed above, and to demonstrate the complexity of the analytic task, the costs and benefits of a specific set of regulations are discussed here. The regulations proposed by the U.S. Department of Health, Education, and Welfare (HEW) in 1976 to implement Section 504 of the Rehabilitation Services Act will serve as the illustration. This example was chosen because the economic impact analysis accompanying those regulations is one of the most comprehensive ones ever undertaken.[6]

The Requirements. HEW's regulations prohibited recipients of federal aid (including educational institutions, health-care providers, and social service agencies) from discriminating against handicapped persons. The discusion here is restricted to those regulations that deal with the exclusion of handicapped persons because of physical barriers in buildings and other structures.[7]

Two standards were established, one governing new construction, and the other, existing facilities. New facilities must meet standards set by the American National Standards Institute

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6. See Dave O'Neill, Discrimination Against Handicapped Persons: The Costs, Benefits, and Economic Impact of Implementing Section 504 of the Rehabilitation Act of 1973 Covering Recipients of HEW Financial Assistance (revised version of an impact statement published in the Federal Register, May 17, 1976, Office of Civil Rights, HEW, May 4, 1977). This analysis is cited as an example of the type of analytic effort expected for a regulatory analysis under Executive Order 12044 by the Council on Wage and Price Stability.

7. See Subpart C of the regulations. The Section 84.22 sets standards for existing facilities; Section 84.23 deals with new construction.

by having no barriers. For programs operated in existing facilities, a standard of "program accessibilility" was established. The proposed regulations stated that the recipient must ". . . through the elimination of physical obstacles or through other methods, operate each program or activity . . . so that . . . when viewed in its entirety is readily accessible to handicapped persons." The HEW economic impact analysis interpreted this as meaning that if modifications to facilities were too difficult to achieve, then other types of program adjustments would be acceptable. For example, in a university library that is inaccessible to students in wheelchairs because of narrow stack aisles and no elevators, establishing a stack search service for handicapped students might be sufficient accommodation.

Analyzing the Costs. The major costs for most recipients were expected to be the direct cost of achieving compliance by modifying existing or proposed structures. The analysis led to the following conclusions:

- The standard for new construction was estimated to entail relatively low costs. Based on previous studies done by HEW and the General Accounting Office (GAO), the regulatory analysis indicated that meeting the barrier-free standard could increase the costs of buildings by one-half of one percent or less. Much new construction already meets the standard. This might be the case because owners and architects have been made aware of handicapped persons' needs or because buildings are already subject to state laws or the federal Architectural Barriers Act of 1968, which mandate similar standards. Since many buildings are already being built to be barrier free, the incremental cost (as opposed to the total cost) imposed by the proposed regulations was estimated to be very small.

- In contrast, the requirement that programs run in existing structures be made accessible to the handicapped was estimated to entail substantially greater costs--between $299 and $544 million. To reach these totals, the analysis considered the cost implications for each major category of recipient. Educational institutions were expected to bear the greatest burden.

In the absence of information on the characteristics of the physical structures in which HEW grant recipients operate

programs, the methodology for estimating the costs of making the structures accessible to the handicapped is inevitably somewhat rough. For example, the HEW analysis built up its estimates of costs for higher education based on existing surveys of what compliance would cost several universities in diverse situations. Assuming costs were proportional to the value and age of structures, and using data on the value of university buildings and changes in enrollments over time (a proxy for age of structures), the HEW analysis extrapolates from cost information available for a few specific universities to all universities. Whether or not there were slightly better ways to arrive at the estimate is not at issue; what is clear is that severe data limitations result in very uncertain estimates.

The costs resulting from HEW's proposed regulations will fall on grant recipients in both the public and the private sectors. HEW's economic impact analysis did not distinguish how much of the total costs would fall on state and local governments, although it seems that the methodology used would have allowed at least a crude estimate of the split. Given that educational institutions were expected to bear the greatest cost burden, and that state and local governments finance a large part of education at all levels, the cost impact on state and local governments would be relatively large.

The possibility of indirect costs is an additional consideration in the analysis of the proposed regulations. If direct costs of compliance are relatively large and if they differ among recipients that are in direct competition with each other, then indirect costs could result. For example, to cover the cost of making their programs accessible to the handicapped, universities may have to raise tuition. Since compliance costs are bound to differ, some schools will raise tuition more than others. If, as a result, enrollment declines, then the regulation has imposed an additional indirect cost. The HEW analysis did not include any estimate of indirect costs.

Most of the costs imposed are of a one-time nature. For recipients that must shift the way a service is delivered, however, as opposed to modifying a facility, the costs could be of a continuing nature. The HEW analysis asserts that such costs would be relatively small. To facilitate comparison with benefits, which are expected to be recurring over time, one-time costs are expressed on an annual basis.

Analyzing the Benefits. The benefits of the proposed regulations are expected to accrue to handicapped individuals whose opportunities for education, jobs, and other social services are now restricted by the inaccessibility of physical facilities. Many of the benefits will be unmeasurable because it is difficult to quantify the improvement in morale that can follow from a handicapped person's ability to lead a more "normal" life.

Some benefits, however, will be tangible. Access to jobs could increase the number of handicapped employees. Increased education might make a severely handicapped person more self-reliant, reducing the need for constant supervision. It could also increase the potential earnings of the handicapped.

The premise underlying the analysis of benefits is that better access will result in increased attendance in schools and that, with more education, disabled persons will hold more jobs and have higher earnings. This assumption seems reasonable since handicapped persons are apt to undertake work requiring more mental than physical skills, and many such jobs demand higher levels of education.

The benefit from making higher education accessible to the handicapped will mount over time as each year more handicapped students graduate and enter the work force. The HEW analysis attempts to measure benefits over the long run. The measurement approach taken was to compare the existing levels of education and earnings for handicapped persons with what they might have been if the regulations had been in effect for a long enough period to have achieved the final steady level of benefits. Specifically, based on the 1970 census, it was found that 3.3 percent of all severely disabled people aged 18 to 44 had completed college. It was assumed that had all institutions been accessable, this proportion might have been twice as high. It was further assumed that a college degree would enable a severely disabled person to earn at the same rate as a partially disabled person. The result of these calculations is an estimated benefit of $100 million earned annually by handicapped persons.

An alternative approach would have been to estimate the number of additional college-educated handicapped persons entering the labor force in each year, and to estimate the increase in their lifetime earnings. The present value of the future flow of benefits could then have been compared with the present value of the total costs of achieving compliance.

Impact on State and Local Governments

From the perspective of state and local officials, the cost calculation is more important than the benefit calculation. After all, costs will be realized in the short run, and to a large extent they will be financed by state and local taxes. For any particular jurisdiction, costs will depend on the degree to which its activities are funded by HEW (in particular, whether it finances higher education) and the characteristics of that area's public buildings.

If handicapped persons benefit as they are estimated to in the HEW analysis, state and local governments will also benefit, albeit indirectly. Greater self-reliance for handicapped prsons could lessen the need for special services. Also, higher earnings would bring more revenue in the form of taxes.

CHAPTER IV. POLICY OPTIONS

State and local officials have raised the issue of intergovernmental constraints in hopes of reducing the number of constraints and lightening the financial burden imposed on states and localities by the federal government. Many of these officials argue that the constraints are excessive and that, in many instances, the political and financial costs exceed the benefits. Whether or not the Congressional policy changes urged by state and local officials should be adopted is essentially a political question. Quite possibly, the constraints imposed—though burdensome for state and local officials--are necessary to achieve important national goals.

The Congress might consider several responses to the critics of intergovernmental constraints. One is to take no explicit action. This approach is based on the premise that the political process can be relied on to prevent or correct excesses of federal authority and to modify regulations that are not cost effective.

A second approach would involve the Congress' changing its decisionmaking procedures to increase attention to--and provide greater information on--the costs and benefits that proposed federal actions might impose on state and local governments. The Congress might consider two specific changes:

- Requiring that analyses of state and local effects be made part of legislative and administrative decisionmaking, and
- Increasing Congressional oversight over rule making in the agencies.

A third approach would be to attempt to decrease the number of intergovernmental constraints by changing the structure and substance of federal policy. Three specific sorts of changes have been proposed:

- Reforming the administration of grant programs;

- o Consolidating existing grant programs and relying more on block, as opposed to categorical, grants; and
- o Establishing a policy of fiscal reimbursement for costs imposed on state and local governments by federal constraints.

These procedural and policy changes are discussed in the remaining sections of this chapter.

STATE AND LOCAL IMPACT ANALYSES

State and local impact analyses have been proposed as a way to provide more information to federal decisionmakers. The desired effect would be to lessen the number of new constraints which, relative to their alleged benefits, are either very costly or inefficient. Such analyses could be required for any bill considered by the Congress and for proposed administrative regulations. The scope of the requirement might also be extended to include periodic review of existing laws and regulations.

While primary emphasis has been placed on the need for reliable estimates of the costs that federal actions would impose on state and local governments, a full state/local impact analysis ideally would consider what benefits are to be achieved and whether alternative actions might be more effective.

Current Practice

The Legislative Branch. State and local impact analyses are not currently part of the legislative process, although the implications for state and local governments of proposed federal actions are often explored in committee hearings and reports.

The Congressional Budget and Impoundment Control Act of 1974 requires the Congressional Budget Office to prepare estimates of costs for public bills reported by all Committees except Appropriations.[1] To date, most of CBO's analyses have

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1. See Section 403 of the Congressional Budget and Impoundment Control Act (Public Law 93-344).

been limited to federal costs, although state and local impacts have occasionally been considered. For example, cost analyses of the various welfare reform proposals considered by the Congress last year included estimates of the fiscal relief to be accorded to the states. The House Committee on the Budget has recommended that CBO's cost estimating responsibilities be expanded to include--whenever possible--consideration of state and local government costs.

Some precedent for federal action requiring state/local impact analyses is established by the 26 state legislatures, which require "fiscal notes" detailing for all proposed legislation the resulting local government costs. Usually such analyses are limited to estimates of direct costs; no consideration is given to benefits or to alternative actions that could produce similar results more efficiently. Estimates are generally produced by Executive Branch agencies and reviewed by legislative staff.

The Executive Branch. Two recently issued Presidential orders require agencies to analyze proposed regulations and legislation. These analyses may fulfill the need identified by state and local officials. The two orders are described in the following paragraphs:

- Executive Order 12074 requires that "urban and community impact analyses" be prepared to identify "aspects of proposed federal policies that may adversely impact cities, counties, and other communities." The analyses are to consider possible economic, demographic, and fiscal changes and their associated costs and benefits as they affect central cities, suburban areas, and nonmetropolitan areas.

- Executive Order 12044 requires federal agencies to analyze "the economic consequences for the general economy, geographical regions or levels of government" of any proposed "significant" regulation and of possible alternatives. (Any regulation that would result in an annual effect on the economy of $100 million or more, or that would result in "major" increases in costs or prices for individual industries, levels of government or geographic regions is defined as "significant.") Agencies are also directed to establish procedures for a

periodic review of existing regulations. In support of the process, two interagency groups have been established. The Regulatory Council is charged twice a year with compiling a comprehensive list of all regulations being developed. The lists are to include preliminary assessments of costs and statements of the legal constraints within which agencies are operating. The Regulatory Analysis Review group, chaired by the Council of Economic Advisors, will review and comment on selected regulatory analyses produced by the agencies.

Although it is too early to evaluate the effect of these orders, they do seem to set up procedures for analyzing federal actions that impose costs on state and local governments. Whether the analyses will be used to influence rather than justify decisions remains to be seen. A possible problem is that the threshold for determining "significance" as defined above is set too high to subject many important regulations to analysis. Some regulations, when taken singly, may have little effect but when considered as part of a larger course of action may impose sizable burdens. For example, the application of Davis-Bacon wage standards specifically to the Urban Development Action grant program involves relatively few dollars. But when all the grant programs to which the Davis-Bacon standards apply are considered altogether, the cost implications may be substantial.

The Judicial Branch. No proposal for analysis of state and local impact prior to decision involves the judiciary. Although the courts frequently make decisions affecting state and local governments, a decision process based on the adjudication of particular cases is not well structured for analysis of broader implications for categories of people, businesses, or governments.[2]

Assessment

Although in principle, requirements for comprehensive analysis offer great promise, in practice they are likely to fall short of expectation. The discussion in the preceding

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2. For a discussion of the limited capabilities of the courts as policymakers, see Donald Horowitz, The Courts and Social Policy, Brookings Institution, 1977.

chapter indicated the complexity of performing state/local impact analysis. Better data and causal models need to be developed before reliable estimates can be produced of the various types of costs and benefits that might result from intergovernmental constraints.

Tangible, direct, public costs would be the easiest to estimate. Whether incremental costs--that is, those directly attributable to the requirement--could be distinguished from total costs would depend on the substance of the mandate or the contractual agreement. Less tangible, indirect, and private costs, as well as most benefits, would be harder to measure. Furthermore, breaking down costs and benefits to the level of individual jurisdictions would be difficult if not impossible given the speed with which analyses would have to be performed to be useful in decisionmaking. Whether, despite a positive assessment in the aggregate, a proposed constraint would put significant burdens on certain jurisdictions would be difficult to know. Despite these difficulties and the inevitable uncertainties that surround estimates, however, analysis of state and local impact would nevertheless produce information useful to decisionmakers.

Good analysis will more easily be done for proposed administrative regulations than for new laws. This is so because costs and benefits depend to a large extent on administrative interpretation and practice. When a statute is considered, interpretation and practice are not known.

Perhaps the greatest benefit could be derived from a selective but intensive review of existing intergovernmental constraints. The possibility for good analysis is much greater in evaluating past experience than in projecting future impacts. The Congress, in consultation with state and local officials, could direct that studies be done to assess whether changes in certain mandates and program requirements are warranted.

INCREASED CONGRESSIONAL OVERSIGHT

Federal policy is to a large extent shaped by administrative regulations. Statutes cannot include the level of detail needed to guide all the decisions necessary to implement a program; indeed, this is the essence of the Executive Branch's

function.[3] That state and local officials' ire is mostly directed toward federal agencies for excessive and unwise rule making is not surprising. State and local officials also argue that agencies issue regulations that are contrary to, or that go beyond, legislative intent.

The Congress is an important point of access for state and local officials having difficulty implementing federal agency regulations. The Congress can direct agencies to change the rules and guidelines governing program administration, and it has done so. In its reauthorization of housing and community development programs last year, the Congress directed the Department of Housing and Urban Development (HUD) to change its interpretation of law in several respects.[4] For instance, in developing housing assistance plans, communities are required by statute to allow for the needs of low-income individuals who are not at the time residing in the community but who might be expected to if appropriate housing were available. HUD's regulations were based on a "fair share" approach--estimates of "expected to reside" were to be based on the size of the low-income population in the metropolitan area. The Congress directed that a much narrower interpretation was intended; that the estimate of the low-income population expected to reside in a community should be based on the number of existing and projected job opportunities within that community.

The Congress has indicated its intention of scrutinizing HUD regulations closely. It has directed the agency to notify it of proposed rulemaking and to provide it with draft language in advance of public release. If the relevant Committee in either House has difficulty with the regulation, the date the rule goes into effect is to be delayed to allow the Congress time to give further legislative guidance to the agency. Similar procedures could be adopted with respect to other federal agencies.

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3. In the case of General Revenue Sharing and block grants, much of the Executive function is assigned to state and local officials.

4. Housing and Community Development Amendments of 1978 (Public Law 95-557).

IMPROVING GRANTS MANAGEMENT

While many conditions of aid governing program administration seem not to be particularly burdensome when considered singly, taken together they absorb considerable resources and generate frustration in state and local officials. Improved management of intergovernmental grant programs, they argue, could make a considerable difference--that the number and complexity of requirements could be reduced by better coordination and greater standardization across programs and agencies.

Steps have been taken over the past 10 years to improve the grants management system.[5] Prompted by the Intergovernmental Cooperation Act of 1968 and several interagency studies, three major federal management circulars (FMCs) were put into effect:

- FMC 74-7 standardizes and simplifies 15 areas of grant administrative requirements, for the most part affecting financial management.
- FMC 74-4 establishes principles for determining allowable costs under grant programs.
- FMC 73-2 standardizes procedures for federal audits and calls for the coordination of federal/state/local audit requirements.

In addition, the Joint Funding Simplification Act of 1974 requires federal agencies to facilitate state and local governments combining grants from several programs in support of a single project.

Despite these steps, however, state and local officials argue that more needs to be done to eliminate duplicative planning and reporting requirements, to standardize rules and regulations (particularly with respect to the generally applicable conditions of aid such as the environmental and nondiscrimination provisions discussed in Chapter II), and to increase consultation among federal, state, and local officials at early

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5. For an extensive discussion of efforts to improve grants management, see ACIR, Improving Federal Grants Management, Report A-53, February 1977.

stages of the federal rulemaking process. State and local officials maintain that a stronger central management staff is crucial to further progress. They argue that central coordination is necessary both to enforce agency compliance with existing management policies and to initiate additional changes.[6]

GRANTS CONSOLIDATION

The overall number of federal grant regulations can be cut if the Congress is willing to give state and local government officials greater authority over the use of federal grant funds. It can do so by consolidating narrow categorical programs that are similar in purpose and by reversing the tendency to recategorize and add additional strings to existing block grant programs.

Federal grant programs are generally considered to be of three types:

- o General purpose fiscal assistance, typified by General Revenue Sharing, whereby funds are allocated by formula and are given to state or local governments with few, if any, restrictions regarding use.

- o Block grants, such as the Community Development Block Grant program, whereby the Congress specifies the objective to be achieved and a broad range of permissible uses. Funds are generally allocated by formula. Local officials decide what activities are to be supported.

- o Categorical grants, which are given by the Congress to finance narrow, circumscribed kinds of activities.

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6. Similar recommendations for improving the administration of grants programs have been made by several groups. See for example, ACIR, Improving Federal Grants Management; Commission on Federal Paperwork, Federal/State/Local Cooperation (July 1977); National Governors Conference, Agenda for Intergovernmental Reform, Vol. 2 of Federal Roadblocks to Efficient State Government (February 1977). See also The Federal Assistance Monitoring Project of the ACIR, Streamlining Federal Assistance Administration: An Interim Report to the President (September 8, 1978).

Examples include Aid to Families with Dependent Children, Environmental Protection Agency grants for wastewater treatment construction, and project grants for the promotion of the arts. Funds may be distributed by formula or on a project basis. Either way, federal administrators retain a fair amount of control and responsibility for overseeing programs, which are administered by state and local governments.

For the most part, general purpose fiscal assistance and block grants are developments of the last decade. Whereas in 1968, categorical programs accounted for 98 percent of all federal grant outlays, by 1977 their proportion had declined to 76 percent.[7]

In the last couple of years, the trend toward decentralization in the federal grant system has, to some extent, been reversed. The tendency in the reauthorization process and in the administration of block grants and General Revenue Sharing has been to recategorize and to increase restrictions and regulations. For example, when General Revenue Sharing was reauthorized, provisions regarding nondiscrimination, financial management, and citizen participation were strengthened. A second example is the reauthorization in 1978 of Comprehensive Employment and Training (CETA) programs. Although CETA is commonly considered to be a block grant, it now contains numerous requirements concerning individual eligibility and the mix of employment services that may be provided.

An analysis of which grants are appropriate for consolidation is beyond the scope of this paper. The ACIR, however, has analyzed the topic in some depth and has proposed the merger of 170 categorical grant programs into 24 programs.[8] Some of the bigger consolidations suggested (involving nine or more separate programs) are in the areas of transportation safety, comprehensive regional transportation, comprehensive state transportation, pollution prevention and control, omnibus education assistance and preventive and protective health. The ACIR has also recommended that the Congress enact legislation

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7. ACIR, In Brief the Intergovernmental Grant System: An Assessment of Proposed Policies (1978), p. 8.

8. ACIR, Categorical Grants: Their Role and Design (1977), A-52, pp. 298-305.

giving the President authority over program consolidation similar to his involvement in government reorganization. Under such legislation, upon submission of a Presidential plan, the Congress would be required to approve or disapprove the plan by resolution within 90 days.

FISCAL REIMBURSEMENT

A policy of full fiscal reimbursement has been proposed to minimize the financial burden placed on state and local governments by intergovernmental constraints. If such a policy were adopted, the federal government would be obligated to pay the full cost of any state or local actions taken in response to federal requirements. As proposed by the National Governors Association (NGA), the principle would not apply to court ordered mandates. It would apply, however, for all other mandates or contractual obligations put into effect by statute or administrative regulation after the date of adoption.[9]

State Precedent

The primary model for a policy of fiscal reimbursement is the one adopted by the State of California to govern its relationships with local governments.[10] In 1972, the California state legislature passed the Property Tax Reform Act of 1972 (SB90). This law established rate and revenue limitations for local governments and at the same time adopted the principle of reimbursement for increases in local costs attributable to new state mandates regarding service provision or local taxing.

Under the provisions of SB90, the State of California is to reimburse local governments for revenue losses arising from new exemptions granted by the state affecting property, sales, or use taxes, and for the costs of new services or increases in service levels mandated by state law, administrative regulation, or executive order subsequent to 1972. A local government may

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9. National Governors Association, Policy Positions 1978-1979, p. 26.

10. Other states such as Montana, Louisiana, and Pennsylvania have also adopted the principle of reimbursement for state mandates.

apply for reimbursement of the full cost of a mandated service even if that government had been providing the service before the state mandate. If it does so, however, it must reduce its maximum property tax rate or revenue limit by an equivalent amount. Excluded from coverage are: legislation specifically requested by local governments, programs mandated by the federal government, court decisions, or voter initiatives, mandates that provide for self financing or result in no new duties; and laws that define crimes or establish new penalties.

The reimbursement process works as follows. The State Department of Finance is responsible for estimating mandated costs associated with new legislation. The department also reviews agency-prepared estimates of costs associated with administrative regulations. Appropriations are to be provided to cover both one-time and continuing costs associated with covered mandates. Each year local governments submit claims for reimbursement to the State Controller. If local governments believe that reimbursement ought to be forthcoming and none is provided, they may lodge a claim with an independent administrative Board of Control. The Board reports to the Legislature on the number and amount of claims it awards. Upon receipt of the report, an appropriations bill sufficient to cover all approved local government claims for reimbursement must be introduced in the legislature. Decisions of the Administrative Board of Control may be appealed in the state court system.

The reimbursement policy has resulted in only a small increase in state aid for local governments. Between 1972 and 1976, the California State Government provided $85 million in reimbursement for newly imposed mandates. Over the same period, total state aid equalled $26,500 million.[11]

Current Practice

Neither a clearly articulated policy nor consistent practice exists regarding the placement of financial responsibility for costs incurred by state and local governments in meeting

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11. Reimbursement amount reported in ACIR, State Mandating of Local Expenditures, p. 26. Total state aid reported in Bureau of the Census, State Government Finances, volumes for 1973 through 1976.

federal requirements. In some instances, state and local governments must bear the costs; in others the federal government provides full or partial compensation.

Costs imposed by mandates are more likely to be borne by state and local governments than are the costs associated with other constraints. This is so because many mandates derive from the courts and only rarely is federal assistance provided to cover the costs of compliance. Federal financial assistance is more common when mandates stem from federal statute and associated regulations. For example, when the Congress passed the Water Pollution Control Act of 1972 mandating sewage treatment, it also established a capital grant program for wastewater treatment facilities to share the cost of constructing required municipal facilities. Not all mandates have corresponding grant programs, however. For example, no grant funds are earmarked for assisting local governments to establish treatment capabilities required to meet safety standards for drinking water.

The federal government pays most of the costs associated with grant-in-aid requirements. This is true almost by definition, since the primary purpose of grant requirements is to govern the use of federal funds.

In certain circumstances, however, state and local governments bear direct costs generated by grant requirements. When actions or standards are required for participation in a grant program, but the cost of taking those actions or achieving the standard is not covered by the grant, a financial burden is imposed on the recipient. For example, a state that must upgrade its hospitals in order to receive medicare or medicaid payments may face significant costs. Similarly, the requirement that public facilities be accessible to the handicapped before federal aid can be received could impose high costs on state and local governments.

A comparable situation arises when state and local governments are required to share the costs of a grant funded activity; in such instances, any requirements increasing the cost of that activity will create financial burdens. For example, if the federal government pays 75 percent of the cost of constructing sewage treatment plants, and Davis-Bacon requirements increase total project costs by 5 percent, then state/local costs will increase by the same proportion.

In addition, grant requirements can result in indirect costs the full burden of which fall on state and local governments. For example, Davis-Bacon requirements might affect the price of state and local construction that has no federal funding.

Whenever federal regulations specify actions that are contrary to program goals, prohibit grantees using the money as they choose, or impose a financial burden, the benefits to state and local governments of participating in a federal grant program are lessened. So long as states and localities continue to participate, however, one must assume that there are net benefits for the recipient governments and their citizens.[12]

Analysis of Reimbursement Option

A policy of fiscal reimbursement can be justified on three grounds:

- To minimize the extent to which federal requirements claim local resources, thereby crowding out actions with greater local priority;
- To make the distribution of costs more equitable; and
- To deter the federal government from imposing additional requirements.

Crowding Out. Advocates of a reimbursement policy argue that the resources available to state and local governments are limited. When such resources are used to pay for actions ordered by the federal government, they are unavailable for activities judged to be important by the local citizenry. In other words, residents' choices regarding local public services are crowded out by federal requirements.

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12. There are instances of state and local governments' refusing assistance for which they are eligible on the grounds that the conditions associated with the program impose costs that exceed benefits. For example, Montgomery County, Maryland, has refused Urban Mass Transit Authority assistance grants because of objections to Section 13(c), which requires labor sign-off on grant applications.

 ERRATUM

In the course of producing this paper, a page was accidentally omitted. This page should be read between pages 43 and 44.

When tax and expenditure limitations exist, making resources legally finite, the crowding out argument takes on greater significance. California adopted its fiscal reimbursement policy in conjunction with its decision to impose, by state law, rate and revenue limitations on local governments. The state agreed to fund newly mandated services in order not to crowd out existing local services. The state thereby avoided placing local officials in the untenable position of having to cut back existing local services to free up revenues to finance newly mandated ones. After studying state mandates, the ACIR concluded that the California action was a responsible one under the circumstances. It recommended that all

> ...states imposing tax or expenditure limit laws either reimburse local governments for all the direct costs imposed by state mandates or exempt from all state imposed local levy or expenditure limits those local cost increases mandated by the administrative, legislative, or judicial actions of the state government.[13]

Since the federal government is not directly responsible for tax and expenditure limitations, the case for reimbursement is somewhat weaker at the federal level. So far as the federal government is concerned, state and local governments have the option of raising sufficient taxes to meet federal requirements and to carry on other activities.

Whether or not explicit limitations are in effect, fiscal reimbursement is at best only a partial solution to the crowding out problem. After all, in the aggregate federal funds derive from the same taxpayers who support state and local governments. If federal taxes are raised to finance a reimbursement policy, the willingness of citizens to pay additional state and local taxes may decrease.

Equity. A second consideration in determining the desirability of a fiscal reimbursement policy is whether costs would be distributed more equitably if they were financed by the federal government. Judgments regarding equity are frequently based on one of two principles: that costs should be distributed either in proportion to benefits or in accordance with

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13. ACIR, State Mandating of Local Expenditures, p. 4.

ability to pay. In the case of some regulations, other considerations may affect equity judgments. For example, if the purpose of a regulation is to curb abuse, having the offending parties bear the costs of remedial action seems reasonable. Few would argue that the federal government should reimburse private business for the cost of complying with minimal health and safety standards for places of work.

An across-the-board policy of fiscal reimbursement is unlikely to enhance equity regardless of how equity is defined, since the circumstances underlying federal regulations differ. Depending on the geographic pattern of costs relative to benefits, the fiscal ability of governments facing the greatest costs, and the reasons for the imposition of the federal requirement, equity may or may not be enhanced by the federal assumption of costs. Equity is more likely to be advanced by a flexible policy of considering each federal requirement on its own merits.

Deterrence. A third reason for supporting a policy of fiscal reimbursement is that it might act as a deterrent to the imposition of new constraints. If federal officials have to raise taxes to cover all of the costs, some advocates reason, they will think twice before requiring that actions be taken by state and local governments. A reimbursement policy might be limited in scope to areas judged to be better left to state and local discretion.

ACIR's recommendations regarding reimbursement by state governments seem in large part to be based on the "deterrent effect." In policy areas where the state interest is large, and/or where the effects of local actions "spill over" to places outside their jurisdictions, partial reimbursement is considered appropriate. But "to minimize state intrusion into matters of essentially local concern," such as public employee working conditions, the commission recommends that full reimbursement be required to accompany relevant mandates.[14]

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14. ACIR, State Mandating of Local Expenditures, Report A-67, July 1978, pp. 9-12.

Possibility for Limited Reimbursement

While the NGA has recommended a policy of fiscal reimbursement applicable in a broad range of circumstances (including some not caused by intergovernmental constraints), the Congress may prefer to embrace the concept but to a limited extent. The scope of applicability of such a policy could be restricted by attention to the following factors:

- Types of constraints to which the policy would apply. Determining when reimbursement would apply is much harder at the federal level, where constraints take a variety of forms involving different degrees of coercion, than at the state level, where mandates are the common practice.

- Types of costs eligible for reimbursement. Reimbursement could be limited to only certain of the costs described in Chapter III (for example, incremental direct public costs). Measurement problems identified as posing difficulties for the analysis of costs and benefits would make implementation of a reimbursement policy very difficult.

- Extent of reimbursement. State and local governments could be reimbursed in part or in full.

CONCLUSION

Relations between levels of government in the U.S. federal system have clearly been changing over time. Constraints have increased in number and, with them, the degree of federal control over state and local government actions has grown. Whether or not this change in intergovernmental relationships should be viewed as problematic is essentially a political question.

Regardless of one's judgment concerning the desirability of the expanding federal role, particular constraints may be ineffective or they may impose relatively high costs. If there are to be changes, inquiry must be redirected from the general to the particular. Individual programs and requirements must be analyzed to determine their costs and benefits and to discover whether better courses of action exist.

Mr. MINETA. Thank you very much, Dr. Reischauer.

Ms. HOLTZMAN. Thank you very much, Dr. Reischauer. We appreciate your testimony and your presentation.

Our next witnesses are Alan Beals, executive director of the National League of Cities; Bernard Hillenbrand, the executive director of the National Association of Counties; and Ann Michel, coordinator of the Federal-State Aid, Syracuse, representing the U.S. Conference of Mayors.

Mr. MINETA. If I might interject, I had the pleasure of working with all these people over a long period of time, and we are specially pleased to see you, Ms. Michel and have this opportunity of working on the Legislative Action Committee of the U.S. Conference of Mayors.

When Mayor Lindsay asked me to join that committee, Ms. Michel was one of those people who was staffing and was on the staff of Mayor Lee Alexander. She was a great resource to us, as was Mr. Beals.

Ms. HOLTZMAN. I am very pleased to welcome them all.

I understand that Mr. Beals does not have a prepared statement. Without objection, the statements of the other two witnesses will be included in their entirety in the record. We will begin by hearing from Mr. Beals.

STATEMENT OF ALAN BEALS, EXECUTIVE DIRECTOR, NATIONAL LEAGUE OF CITIES

Mr. BEALS. It's a great pleasure to appear before you on behalf of the National League of Cities which represents some 15,000 city governments throughout the United States. The National League of Cities strongly endorses the passage of H.R. 3697 introduced by you and your distinguished colleagues.

This bill represents a long-sought goal of the National League of Cities. It is one of the 10 most urgent national pieces of legislation that our board of directors has put on our action agenda for this year.

The high priority that we place on this legislation comes about primarily as the result of the work of a special revenue and finance task force of the National League of Cities has been engaged in over the course of the past year, chaired by the former mayor of Kansas City, Charles Wheeler, with a charge to look at the emerging issues in local government finance and to design a series of recommendations to cope with the increasing financial difficulties that our cities are facing.

The task force concluded that a primary area on which attention had to be focused was the whole area of mandated costs. This received a very high priority because of the trends that we have seen, not only at the Federal level but at the State level, to mandate performance levels or standards of public service and the resultant costs imposed on local property taxpayers and elected officials.

We are deeply appreciative of your leadership in having the Congressional Budget Office undertake the study that resulted in the publication that has just been introduced in the record, "Federal Constraints of State and Local Government Actions." This report outlines the expansion of existing Federal mandates that impact on

those of us who are concerned about the future of cities and local government.

We could speak in some detail on almost any of those different mandated areas, but one of the most important conclusions that one derives out of this experience is the fact that there has been very little discussion about how these programs will have to be managed at the local level, what the cost is to manage them, and who will ultimately pay for them.

There is a reference in that congressional study to a case that the National League of Cities was involved in, known as *NLC* v. *Ussery*, which was a challenge to the constitutionality of the Fair Labor Standards Act of 1974. That case was important because of the fiscal consequences to cities. During the congressional debate it is fair to say that the overwhelming consensus was there would be almost no fiscal impact at the local level from the amendments adopted by the Congress.

We undertook, with the help of the International City Management Association, a comprehensive national study of that issue after the passage of those amendments. By the time the Supreme Court considered the constitutional issues involved in that piece of legislation, all of the parties had stipulated that there was indeed a huge fiscal impact. Just in the field of administering the overtime provisions in fire services alone, in excess of $1 billion a year on local government was involved.

That I think is a very sharp example of the problems that we have seen from the standpoint of managing cities and the issue of fiscal impact.

The Advisory Commission on Intergovernmental Relations last year published a very thorough study on the issue of State mandates. In that study, the ACIR points out that some 22 States have some form of fiscal requirement on legislation that is considered at the State level that impacts on local government. So there is considerable precedent for the type of legislation that you are considering in terms of our experience at the State level.

I understand that there has been some skepticism or concern about the capacity of the Congressional Budget Office to undertake this additional work. My recollection is that there were similar views expressed some 4 or 5 years ago in terms of the requirement that there be a fiscal impact analysis just on Federal legislation that was being considered. I think it is fair to say that over time those concerns have been allayed.

For those of us at the local level, we don't expect perfection in the immediate implementation of H.R. 3697. We do feel that the kind of process that is laid out in your legislation will begin to elevate the conduct of the national debate and the process of fully assessing how these programs are managed at the local level, and what the costs of meeting those problems will ultimately be.

From the standpoint of the National League of Cities, we feel that this is the most important improvement that can be made at this time in the intergovernmental system, and we strongly support the passage of your proposals.

Ms. HOLTZMAN. Thank you very much. Going in alphabetical order, we will hear next from Bernard F. Hillenbrand. We would appreciate your summarizing your testimony briefly.

STATEMENT OF BERNARD F. HILLENBRAND, EXECUTIVE DIRECTOR, NATIONAL ASSOCIATION OF COUNTIES

Mr. HILLENBRAND. Madam Chairwoman, we want to thank you and your colleague, Mr. Mineta, for giving us an opportunity to come here this morning and appear and we very strongly endorse your legislation, H.R. 3697. This is to me a very personal thing, I would like to add.

The first assignment I had in government was in the city of Syracuse. It is represented here today by Ann Michel, and the question came up, a very highly political one, we had to in one of the previous incarnations of proposition 13, we had to economize and close a fire station, and one of the councilmen said—he was with the research bureau—and he said, "Well, let's open it; we have extra firetrucks; yes."

He came in with an estimate that it would require four firemen and a firetruck to open that station.

I had the job of making an impact statement, but it doesn't require four. It takes almost 16 with vacations and sick leave and time off, and people have to be rotated, and you have to have so many drivers and tillermen, et cetera, and the stations have to be heated, and so on. So from the very beginning of my career in the public sector, I understood the importance of these impact statements.

I might also add that we in the National Association of Counties have for the past 2 years been operating under a requirement that our members have passed that we at the staff level have to make an impact statement, an analysis of any resolution that goes through the National Association of Counties.

We do it imperfectly, but we do it, and we do find it very, very helpful and, Madam Chairman, we would very strongly endorse this and are happy to do it and join with our colleagues at the National League of Cities and the Conference of Mayors and urge the passage of this bill as a matter of very, very high priority.

The formal statement that is being submitted for the record is replete with a great number of specific examples of the hardships that this is a very well-meaning regulation, like the section 504 handicap regulation.

If an analysis were made at the beginning, Congress would be a whole lot more selective about the impact of this kind of legislation because, if it is fully carried out, it will be absolutely devastating at the local level.

[The prepared statement of Mr. Hillenbrand follows:]

PREPARED STATEMENT OF BERNARD F. HILLENBRAND

Chairwoman Holtzman, Chairman Mineta, and distinguished members of the joint Task Forces on State and Local Government and Budget Process, my name is Bernard F. Hillenbrand. I am the executive director of the National Association of Counties (NACo),[1] the only national organization representing more than 3,000 county governments in the United States. I appear before you today to present the

[1] The National Association of Counties is the only national organization representing county government in the United States. Through its membership, urban, suburban and rural counties join together to build effective, responsive county government.

The goals of the organization are to: Improve county government; serve as the national spokesman for county government; act as a liaison between the nation's counties and other levels of government; and achieve public understanding of the role of counties in the Federal system.

views of our Nation's county governments on H.R. 3697, the State and Local Government Cost Estimate Act of 1979.

Let me begin by thanking you, Chairwoman Holtzman and Chairman Mineta for this opportunity to appear before you today. More importantly, I thank you for your sponsorship and serious consideration of this significant measure. I can assure you that the nation's county governments are wholeheartedly supportive of a more rational means through which policy development considers the fiscal impact of proposed programs. H.R. 3697 would provide this. The most significant, and from our view, important element of this particular measure is that it considers not only the fiscal implications for the Federal Government, but also that for the State and local governments. In so doing, this bill recognizes the vital role each level of government plays in cost effective program delivery, and cements our partnership role more firmly. It is virtually impossible for the Federal Government to hold down costs without consideration of the financial obligations placed on State and local governments in meeting national policy objectives.

In March of this year, the directors of the seven major organizations representing State and local governments jointly endorsed this bill. On March 20, NACo sent a letter supporting this vital measure. The purpose of my testimony today is to highlight the problems and costs local governments have faced as a direct result of the failure of the Federal Government, including Congress, to consider the costs of programs prior to enacting them. Many of these examples result from Federal mandates, such as environmental standards or accessibility of the handicapped. I wish to point out that we in no way object to the intent of these mandates. Philosophically, counties believe in clean air and clean water; we believe the handicapped have the equal rights to participate fully and freely. However practically speaking, the counties take issue with who shall pay the costs to achieve this well-intended objective.

Before presenting these examples, I wish to address a few important, but pervasive, misconceptions which deal directly with this issue.

There is an overriding belief in the Congress, and the Federal executive branch, that most mandates and costly requirements placed on local or State governments are a condition of aid. Therefore, a county government has the option to assume the liability for these requirements. Thus, those costs incurred are a local option. This is just not so. Although it is true the county has the right to choose which Federal program it wishes to participate in, it no longer has the option to ignore the help the Federal Government offers. Counties are fiscally hardpressed. They have citizens who rightly demand a quality level of service. But, the tax base is limited, and costs continue to skyrocket. In these times of severe inflation, counties cannot provide the same level of services without tax increases. We are forced to turn to the Federal Government to stay afloat. Given this consideration, there is no option.

Local costs are complicated by Federal mandated objectives that are not conditions of aid. These mandates, such as environmental protection, prevailing wage rates, civil rights protection, cross-sect all county operations. The Advisory Commission on Intergovernmental Relations (ACIR) has recently identified more than 30 of these types of requirements in meeting these mandates, local governments are forced to shift their financial resources and staff from equally important functions to meet these requirements. This undermines the ability of the county government to govern itself effectively and at a price it can afford from existing own-source resources.

The second misconception I would like to address is that concerning the amount of Federal aid presently available for State and local governments. It relates to this topic in that any demands from State and local governments to seek Federal support of the full cost of federally imposed mandates is invariably answered in terms of the amount of dollars already available to provide assistance. The Federal Government cites $80 billion. This is totally inaccurate. The Federal Government provides only approximately $33 billion annually to State and local government. The $80 billion figure includes funding to individuals, military installations operating in local areas, and payments to the nonprofit private organizations. The purchase value of the $30 billion figure is greatly shrinking, while the mandates to county governments continue to climb. A recent study conducted by the University of California at Riverside has found that a local government is forced to comply with an average of 1,000 State and local mandates in a given year. Conditions of aid account for only 500 of these, while the remaining 500 are a result of direct orders. The costs of these mandates cannot be adequately determined in that a large portion of these costs result from internal management changes which are difficult to measure in terms of cost.

COSTS OF FEDERAL PROGRAM REQUIREMENTS ON LOCAL GOVERNMENTS

With the committee's permission, I now turn to the impact of congressional and administrative actions on local budgets.

A study completed by the Congressional Research Service regarding the costs of implementing the 504 handicap requirements for the New York Metropolitan Transit Authority and New York Staten Island Rapid Transit System has shown: the purchase of equipment and placement of 481 elevators in the two systems will cost $649 million; costs for property acquisition will be $50 million; costs to change the collection systems will be $11 million; structural modifications for stairs and ramps will cost $11 million; removal of obstacles and placement of emergency exits will cost $150 million; and new graphics in the stations will cost $5 million.

It is important to note that the total cost estimates for Metropolitan Transit Authority of New York will remain equivalent to the U.S. Department of Transportation's total estimate for retrofitting all rail systems throughout the Nation. In addition, the operating costs for buses to meet these requirements exceeds the initial estimate of the Department of Transportation as well. The Congressional Research Service estimated the costs of operation will run between $210 and $314 million a year. This figure is 4½ times that of the DOT estimate.

Fred Cooper, county supervisor of Alameda County, Calif., has included in testimony before this Congress that the total cost of the 504 regulations to county governments in this Nation will be $10 to $20 billion; almost one-half of these costs are to retrofit county schools.

The University of California at Riverside study on State and Federal mandates, which incidentally is available to the members of this committee, found a number of interesting and costly effects of Federal mandates on local budgets. For example:

—San Bernardino County, Calif., as a result of Federal requirements dealing with historic preservation was forced to move a historically significant stone wall 50 yards at a total cost to the jurisdiction of $50,000.

—The Southern California area governments (SCAG), has, after 2 years of negotiations, received final approval for its air quality plan to meet federally mandated standards. It will impact six counties and 127 cities. The plan will cost: for bikeways—$10 million; for ride sharing—$12 million; and for traffic signals using lower energy—$5.4 million.

These costs are only a part of the total for this plan.

Another significant finding of this study, which supports an earlier study conducted by NACo in 1977, found that the cost of using Federal assistance to conduct constuction or capital outlay projects is 30 percent more than cost using local dollars. This a a result of a more detailed design standard requirement by the Federal Government and the cost of excessive paperwork, the various Federal and State reporting requirements, necessary to complete the project.

IMPACT ON COUNTY OPERATIONS

The costs of Federal requirements on local budgets is only one aspect of the detrimental effect congressional and administrative requirements have on local operations. Just as important is the impact these requirements have on county government's ability to manage effectively, or to improve their management capacity and hold down costs. A recent NACo survey of 200 county governments cited the impact of Federal requirements are detrimental to the structure and administration of county governments. Those named most frequently were: EPA regulations; section 504 handicap requirements; welfare regulations; OSHA regulations; 1972 Water Pollution Control Act; and Health Systems Act.

Although Federal regulations are cited frequently, in many instances these regulations are accurate interpretations of congressional intent. This is most certainly true of many of the reporting requirements placed on county governments by the Comprehensive Employment and Training Act. In the 1977 NACo paperwork study of three program areas, CETA, the Community Development and the Federal Aid to Highway Acts, CETA faired the worst for brudensome and unnecessary paperwork requirements. Many of these requirements were the direct result of congressional, not regulatory, action. These requirements force county governments to maintain increased staff levels to meet compliance. In Montgomery County, Md., a county determination has proven the adverse impact of Federal requirements in the financial reporting area. Montgomery County could eliminate one full-time senior accountant if Federal financial reporting requirements were streamlined.

CONCLUSION

A large part of the probem has been that the Congress has never had the means or a method by which it could access the cumulative effect requirements placed on

State or local governments. Although the ideas sound good at first glance, they become a horror story in the reality of implementation. Counties believe, however, that the Congress will seriously weigh these well-intended requirements against the costs of implementation when the facts are presented. H.R. 3697 will provide the method through which the Congress can take a more rational approach to policy development.

The National Association of Counties supports H.R. 3697. We believe the provisions of this legislation will bring a more rational and realistic approach to enacting laws, and commit ourselves to its implementation. Over 25 States have implemented some form of assessing State and local costs prior to enactment. We in State and local government know that the intent of this measure, and the provision it offers, will work.

Chairwoman Holtzman, Chairman Mineta, and members of this joint task force hearing, I thank you again for your patience and the opportunity to appear today, and will be happy to answer any questions you may have. Thank you.

Ms. HOLTZMAN. Thank you. Now we will hear from Ann Michel, whom I have had the pleasure of meeting before and who has done an outstanding job in Syracuse. We would appreciate it if you would you summarize your testimony briefly.

STATEMENT OF ANN MICHEL, COORDINATOR OF FEDERAL-STATE AID, SYRACUSE, N.Y., ON BEHALF OF THE U.S. CONFERENCE OF MAYORS

Ms. MICHEL. I am very glad to be here to represent the U.S. Conference of Mayors.

As someone who works within a city government structure we often find that cities are the one level of government on the receiving end of mandates from all levels above without necessarily receiving appropriate level of resources to implement them. So this is a subject of great concern.

The Conference of Mayors has been on record for some time in support of more frequent and thorough analysis of the impact of Federal action on local governments. We continue that support today.

H.R. 3697 is a necessary and commendable step in assuring that Congress will address the cost impact of Federal legislation on State and local governments.

The conference, like the two groups sitting here with me today, wants to go on record firmly in support of that legislation and your leadership in this regard.

We would like to see Congress go one step further, however, and analyze the urban impact of all legislation, including tax measures reported in the Congress. Often those are the kinds of measures that have an impact that is not always identified in the very early stages.

More recently there have been a number of Federal mandates, as has already been articulated, that are direct, definable, and that we can point to as having a direct dollar impact on local governments. In and of themselves, those mandates are not necessarily inappropriate.

In fact, some of them have come into being because of a significant national need, and certainly I would not want to give the impression that we are opposed to increased accessibility for the handicapped.

The issue is not disagreement with the national objective or goal but a desire to be certain that when those goals are made law they are done so in a way that are realistically implementable and there

are adequate resources available for their implementation at the local level.

It is important to emphasize what each of you know—that local resources are finite.

This is not an age in which we can continue to request great increases in the resources available to run local governments, so the kinds of recommendations your legislation will bring into being are important in helping us understand the impacts of some of these national objectives.

I would point out one further thing in reference to the ACIR report that Mr. Beals has already mentioned. It had in it one full chapter on New York State mandates, and that calls to mind what I said in my opening statement—that we are not only on the receiving end of Federal mandates but of State mandates or State interpretation of Federal mandates which become State mandates, often with another set of regulations on top of those suggested at the Federal level. We are often unable to find the resources without redirecting our priorities to implement such requirements.

In conclusion, the Conference of Mayors is strongly committed to this effort. We do feel that it should include the issues of tax measures.

It is our hope that the legislation will come into being, that it will result then in fewer and less costly mandates, or adequate resources for their implementation at the local level. Thank you very much.

[The prepared statement of Ms. Michel follows:]

PREPARED STATEMENT OF ANN MICHEL, ON BEHALF OF THE U.S. CONFERENCE OF MAYORS

Madam Chairman and members of the committee, thank you for the opportunity to present the views of the U.S. Conference of Mayors on H.R. 3697, the State and Local Government Cost Estimate Act.

The Conference of Mayors has been on record for some time in support of more frequent and thorough analysis of the impact of Federal action on local governments. Federal regulations and requirements, tax policies, spending programs, and monetary policies all have a significant impact on local governments and economies. Yet, the effects of Federal action are often unanticipated or unexplored before Federal action is taken.

H.R. 3697 is a necessary and commendable step in forcing the Congress to begin to address the direct cost impact of Federal legislation on State and local governments. The Conference of Mayors supports this measure. However, we would like to see the Congress go one step further and analyze the urban impact of all legislation including tax measures reported in the Congress. Often the effect of Federal programs and tax policies are indirect and do not translate into increased local costs per se. For example, Federal actions designed to aid housing or spur investment, may unintentionally encourage migration from the cities or hurt local economies. The impact of such measures on urban areas should be also analyzed.

Along these lines, there are several significant and familiar examples of large-scale Federal programs which were enacted without analysis of their likely impact on urban areas and which turned out to be antiurban in their effects. The Federal highway program, Federal subsidies for water and sewer lines, VA and FHA housing assistance and the investment tax credit have all acted to the detriment of urban areas. This is not to say that these programs were not necessary or important, but at the least the Congress should have been aware of what they were doing so as to make more informed programmatic decisions.

More recently, there have been a number of Federal mandates which impose direct and unreimbursed costs on State and local governments—costs which were unknown or ignored at the time the bills were enacted. It is, of course, these costs which H.R. 3697 addresses. Examples abound which illustrate this recent trend of enacting Federal legislation which places expenditure burdens on State and local governments, including the new requirements that all buildings and transportation

services be accessible to the handicapped, the "mainstreaming" of the handicapped in public schools, environmental protection laws which require water and air cleanup, and safe drinking water requirements.

At present, little is known about the magnitude or distribution of the costs imposed by Federal mandate. Certainly, such an aggregate estimate would be difficult to produce. Moreover, I do not underestimate the difficulties involved in trying to estimate the State and local costs resulting from specific laws or regulations. Many different types of effects have to be measured—indirect as well as direct, intangible as well as tangible and continuing as well as one-time costs.

It is important to emphasize that local resources and energy are finite. When resources are allocated to follow dictates from higher authorities, they are diverted from locally identified needs and priorities. Federal requirements are particularly burdensome in view of the fact that may local and State governments are reeling under the effects of inflation, high unemployment, taxpayer revolts and expenditure limitation laws. It is difficult to cut back on budgets when many expenditures are mandated by Federal law.

In conclusion, the Conference of Mayors is strongly committed to every effort which requires the Congress or Federal agencies to analyze the urban impact of Federal action, as well as the impact on State and local budgets. Thus, we support the bill which you have introduced, Madam Chairman, as a constructive and important step. We are hopeful that the Congress will expand these analyses to include the impact of legislation on urban areas and that Federal agencies, the Federal Reserve Board and Regulatory Boards and Commissions will institute similar procedures to review the urban impacts of their actions.

It is, of course, our hope that a change in the decisionmaking structure which requires Congress to address the costs imposed by the Federal Government on State and local governments will result in fewer and less costly mandates.

We thank you for the opportunity to express our views and we look forward to working with you and the Congress to secure the adoption of this legislation.

Ms. HOLTZMAN. Thank you very much for your testimony. Let me say first that we have discussed the issue of whether tax measures would fall within the gambit of this bill, H.R. 3697, with counsel for the Budget Committee and with the House parliamentarian.

I should inform you that it is their judgment that tax measures would be covered. I am particularly concerned about this because, in the last Congress, legislation was proposed to provide a special tax credit for constructing new industrial plants that would have enormous hidden costs for urban areas.

We analyzed that legislation, and ultimately got others to analyze it, and it was clear that the impact of that special tax credit would have been to encourage the flight of businesses and jobs from the cities.

It would have had an extremely detrimental impact, and we think that kind of analysis would be required by H.R. 3697. Mr. Mineta.

Mr. MINETA. Thank you very much. In most of what we have heard today the emphasis has been on costs as they are impacting State and local government. What about benefits? How do we measure that?

Is that even more difficult to measure than cost, and shouldn't that be taken into consideration while we try to measure these costs?

Mr. HILLENBRAND. Mr. Congressman, I am glad that you have made that point, and it gives us a chance to emphasize that we are not necessarily opposed to any of the mandates that we have. We want to know the total cost. We had an interesting experience in Los Angeles County where they were comparing hospital statistics, the costs and different kinds of operations, and it leads to the kind of conclusion that you are talking about, that a great number of

people who are there have expensive hospital costs, but are absolutely completely cured, heart bypasses, and that sort of thing, and they formerly would have been dead.

It's much more difficult to measure the positive side of it, but it's important in total equation, those advantages also should be considered.

Mr. MINETA. We have heard, as a result of the CBO study on fiscal constraints on State and local government actions, a number of options, including consolidation of existing grant programs or more block grants, and establishing this policy of fiscal reimbursement for those costs that are imposed on State and local governments by Federal mandates.

I am wondering what about sunset legislation? What about administrative rulemaking also as a means of reducing Federal constraints?

Mr. HILLENBRAND. Mr. Beals has mentioned his priorities, and we would also say one of our priorities is sunset legislation. We have been very active on the Advisory Commission on Intergovernmental Relations, and they are one of the first governmental bodies to come out with that idea.

It is at the top in our priorities. We believe we should have to defend every one of those programs periodically, that they ought to automatically expire.

Mr. BEALS. I referred to the work of our Revenue and Finance Task Force. One of the other areas, in addition to the mandated question having to do with Federal programs, was the question of program evaluation.

While we do not have policy formally endorsing the "sunset" approach, our board of directors and our task force strongly feel that there should be ongoing efforts to vigorously provide program evaluation across the board.

We do have a policy that endorses the whole concept of grant consolidation and the use of block grant efforts, and we would view that as a complementary step to the passage of this particular legislation.

It seems to us we need this. It's not an either/or situation. We need this legislation, but we also need to have some consideration given to the whole arena of consolidation of many of the categorical programs, so they are more manageable at the implementation stage.

Ms. MICHEL. Very briefly, I think from the local administration point of view, our very basic objective is to have maximum flexibility, recognizing that there are national objectives that need to be implemented by virtue of national direction, but direction that they be implemented, not necessarily direction as to how they be implemented so the whole range of grant consolidation, block grant kinds of initiatives, increases our flexibility and permits us to respond to the precise situation in our own community within the national constraints. This is obviously something we would support.

Mr. MINETA. In the CBO study they said that there are two groups of constraints that impose costs. One being mandated, such as direct court orders, and the other being contractual obligations, those being the ones that arise from agreements entered into between the Federal and local governments, and so this morning

most of the discussion has been centering around constraints of the contractual obligation variety.

I wonder if the panel might give us some thought about this other type of cost? Don't direct Federal mandates such as a court decision that legal counsel must be provided for indigents of similar impact on providers of local services and how do we get at that, if we can?

Mr. BEALS. It's clear in the implementation of Federal legislation that the executive branch plays a very large role in terms of setting the rules and guidelines for program implementation.

We have felt that a good bit of work could be done with many of the crosscutting executive branch requirements that are often prescribed as a condition to local governments participating in various programs.

We have been encouraging the Office of Management and Budget and other agencies of the executive branch to formulate clear and consistent policies on many of those issues.

We have strongly supported the use of an urban impact analysis process that was a part of the President's urban policy announcements of 1 year ago and their implementation.

For the same reasons that we use in supporting H.R. 3697, there is a good bit of work that needs to be done on the executive branch side in assessing fiscal impact questions.

Mr. HILLENBRAND. I would like to respond to that by strongly urging that we do have some mechanism to analyze administrative rules. Some of the States have experimented with this. In the State of Tennessee, for example, when a committee of the legislature passes an enabling legislation, the administration must come back before that same committee with their rules and regulations that they propose to implement the program with, and this would be a good opportunity then to study the cost.

The handicap regulations might, had this been applied at the Federal level, that would have been very interesting to see what the analysis would have been had it come back to the original enabling committees of the Congress.

For example, there have been proposals on the question about tax policy. There have been proposals to rebate the Federal tax on gasoline, diesel fuel in highway user commodities. This we would really like to see an analysis of. We have at the county level 2½ million miles of roads, and those funds, if they are rebated as part of an energy plan, would greatly impact on the amount of work that they could do at the local level.

Another example comes to mind. Many of us had supported in concept the idea of a taxable bond option, but we wanted to see the rules and regulations first before we would endorse the legislation.

I think that would be a very useful component of what you are trying to do here.

We perceive that what you are doing is very, very profound. It will have impacts that people don't really imagine right this minute. We have heard the standard joke when the Federal Government gets a cold, we get pneumonia at the local level.

What kinds of diseases do we get when you get a mild infection at the Federal level?

Mr. MINETA. There are many requests from State and local government for assistance in certain areas.

We get many of these kinds of requests from all of you, and I was part of that mechanism at one point. But being on the other end of it, rather than more or few categorical type programs, is there another way of approaching it in terms of the consoldiation of some of these categorical programs or going to other kinds of block grant programs?

I am wondering if you have been in the position of suggesting where those consolidations might take place?

Mr. BEALS. That is an excellent point, and while we are not in a position at this time to give you the answer to that question, I can tell you that we are undertaking that kind of study within our own institutional policy framework.

We are hoping that over the course of the next 4 or 5 months that we will be in a position to make some concrete recommendations in that regard.

As a part of the Budget Committee's earlier hearings to review the President's fiscal year 1980 budget, that question was often posed to us, State and local government levels, both on this side and on the Senate side, and I can only tell you at this point that we are discharging our commitments to you.

We are very seriously examining the options, and we hope to be in a position by this fall to make some firm recommendations to the Congress on additional areas where consolidation can be achieved.

Mr. HILLENBRAND. We have under way some similar and we will be discussing it at our annual meeting in another couple of weeks.

We also want to endorse what you just said. We have been a very strong voice for most of the 429 categorical grant programs through the years, and as you say, you were part of the total operation, and one of the things that we all discovered, and let's talk about a specific piece of legislation, the legislation to help the mentally ill.

We started a national program without any real understanding of how many people we were going to deal with and, as you know, Congressman Mineta, in the State of California we discovered that the university we were dealing with, it got much larger than any of us had ever believed could exist out there, and we get the strongest kind of a pollutant mandate once you start a program for handicapped children, and so on.

Mr. MINETA. As your studies progress, keep us informed. Thank you very, very much.

Ms. HOLTZMAN. I want to thank you and say Congressman Mineta has raised some important points regarding consolidation of grants.

I think it's very important for the Federal Government to determine what the costs are of mandated and other types of programs on State and local governments, But we also need to analyze how we can all use our money more effectively, including State and local governments, and that is another thing our task force will address itself to very soon. The hearing is adjourned.

[The following is additional material submitted for the record:]

PREPARED STATEMENT OF HON. JIM MATTOX, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS—IN SUPPORT OF H.R. 3697, AN AMENDMENT TO THE CONGRESSIONAL BUDGET ACT

I would like to compliment Representative Holtzman on this innovative bill which I like to refer to as "preventive legislation." Like preventive medicine, it will allow us to analyze certain signs of trouble before they become major or fatal problems.

For years, the Corps of Engineers has been employing this method of analysis of their proposals. It is called a cost-benefit ratio, and anyone who has ever tried to vote responsibly on the public works legislation which routinely comes through Congress is familiar with how valuable this tool can be. The ratios tell it all. Often, programs sound like absolute necessities for communities, but take a look at the cost-benefit ratio, and the project is not justified.

Even in cases where a CBO report required by this bill shows a high cost in a Federal mandate, the Congress could decide to go ahead with it. But we will benefit from knowing up front just what we are doing. The bill will result in more public accountability at voting time, but at least we won't have to be surprised later to find out that we are one-four-hundred-thirty-fifth responsible for a multimillion boondoggle. I am sure we have all been embarrassed this way from time to time. Today, I have several thousand 235 housing units sitting in my district abandoned and vandalized. These serve as a constant reminder to the community that the Federal Government most certainly doesn't know what it is doing much of the time. I'm hoping that requiring CBO estimates of potential hidden costs to State and local governments of federally mandated activities, will help to prevent this kind of disease. This is a form of oversight we have yet to see enough of and in which all Members can participate when legislation comes to the floor. I have thought for a long time that such a statement on legislation affecting small businesses might be just as beneficial as the ones we now require for environmental projects.

Perhaps a specific example of how this bill might prevent unwise legislating might prove my point more directly.

Last year, the Environmental Protection Agency issued a regulation pursuant to 93-523 which, in my opinion, has such a negative cost-benefit ratio. 93-523 sought to assure the quality of the Nation's drinking water and, with too few statutory specifics written in by Congress as to how this was to be accomplished, told the EPA to issue the regulations to get this job done. Part of those regulations are now out and no matter how laudable we all feel the goal of this legislation is, I want to tell you what the actual costs are to the Dallas area providers (governmental entities) and eventually to the taxpayer's pocketbook. First, the agency was forced by law to set treatment criteria on the basis of suppositive evidence. In other words, the studies which were to determine what the minimum standards would be were also mandated by the law. In Dallas, the criteria arrived at by the EPA would require an initial capital investment of $275 million for the installation of granulated carbon filters, and an additional $33 million per year in operating costs. All of this would have served to increase the filtering capacity of the city's water by 400 percent, despite the fact that only a small portion of the water produced by the system is actually ingested by the people. The law didn't treat this issue, however. I had these figures compared to those of several other large cities around the country because I thought them high, and believe it or not they were not. If anything, they were low.

My cities would have had to adopt a bond program in order to raise the moneys necessary to install GAC filtration systems. However, in some cases, it would not have been possible to hold an election in time for the affected city to raise funds needed to comply with EPA time schedules. Also, the law did not mention the question of what would have happened to a community who chose not to support a bond program.

In my discussions with local water officials in trying to deal with these potential costs being mandated by the Federal Govrnment, I learned that such an increase in the costs of bringing water to the households of Dallas County, Tex., would eventually have resulted in a doubling of water rates.

Now, even if this were true, I might have been able to see the value of such a program if it could be shown that cancer could have been prevented. But no such evidence exists. There has never been a study which can show conclusively that water as it is now being purified in Dallas County contains substances which could cause cancer if ingested over a lifetime. There simply is no proof. When there is, as I said, I would be happy to support such a program which would stop this from happening. But as of now, we are a Government swinging wildly at a problem the dimensions of which we still don't know. Incidentally, the EPA has seen the wisdom of delaying these requirements. But the fact remains that thousands of valuable hours and dollars were spent by local governments trying to determine what the

costs of this requirement would be to them, and then trying to convince people like me that it is not worthwhile.

My point is that all of this could have been avoided if an impact statement of the type described by Representative Holtzman's bill would have been provided at the time of consideration of the bill.

I support this bill finally because I believe that it will force us to put more statutory language into the legislation we pass. For the first time, in order to get certain provisions passed, Members will have to begin writing more preventive language.

It is entirely appropriate that the Budget Committee be concerned with this type of legislation, for it is these kinds of hidden geometric costs which wreak havoc yearly with our attempts to set realistic spending targets, and to ultimately help control inflation for this country.

PREPARED STATEMENT OF JOSIAH BEEMAN, CHIEF DEPUTY DIRECTOR, DEPARTMENT OF FINANCE, STATE OF CALIFORNIA

Thank you for the invitation to testify before this committee on H.R. 3697. As you may know, the State of California enacted a law in 1972 that is in some ways similar to this bill. I would like to describe the California law, which is known as S.B. 90, and, in general terms, try to answer any questions about the law that you might have, as well as offer some general comments on H.R. 3697.

Actually, the impetus for the enactment of our S.B. 90 law came from two somewhat similar, but yet divergent, problems: a California State Supreme Court case (*Serrano* v. *Priest*) which held that the State's system of funding education in our elementary and secondary schools was unconstitutional. The court found that the heavy reliance on property tax revenues afforded those children who lived in school districts which encompassed property with a relatively low assessed value an unequal opportunity for education in comparison with those children who lived in districts whose property had a higher assessed value.

The second problem had to do with a growing concern over rapidly increasing property taxes, which form the largest source of revenue for virtually all local governmental agencies and programs. Between 1965 and 1972, for example, while the personal income of California residents increased an average of 6–7 percent per year, property tax levies increased an average of 12 percent per year. There had been attempts during that time to somehow slow down these increases, but not until the administration and legislative leaders were able to work out a compromise solution to both problems was there any real progress made. This compromise program involved several key features which include the following: Increasing the State support for elementary and secondary education; imposing revenue limits on school districts; imposing property tax limits on cities, counties and special districts; increasing the State sales tax; increasing the homeowners property tax exemption; establishing renter's relief; and the feature most relevant to our discussion, providing a mechanism whereby the State would reimburse local government for any costs resulting from a State statute or regulation.

Current California statutes require the State to reimburse cities, counties, school districts, and special districts for the costs of all programs which the State imposed or mandated on them after January 1, 1973. Specifically, the law says that any time the legislature passes a bill which requires a new program or an increased level of service in an existing program at the local level with additional costs to local government then that bill is supposed to include an appropriation in an amount, as estimated by the State Department of Finance, sufficient to reimburse all local entities for the costs which they incur when complying with the new law. Similarly, any State agency which issues any order or regulation which requires a new or increased program on the part of local entities is required to cite an appropriate funding source so that those local entities can obtain reimbursement of their costs.

You can see that our S.B. 90 goes considerably beyond H.R. 3697 in some ways in that our law requires, once the costs to local government have been identified and estimated, that the State provide a means for reimbursing those costs. I think it might be appropriate at this point to describe for you how these estimates are developed, who uses them, how they are used, and what the "track record" for the estimators has been.

I mentioned earlier that our State Department of Finance, which is in the executive branch, is specifically designated by the S.B. 90 law as the agency responsible for developing the estimates of these State-mandated costs. Our legislative analyst's office, which is roughly comparable to the Congressional Budget Office, has found the Department's estimates to be reliable enough that a separate estimate, independently prepared by an office of the legislative branch, is not generally

needed. The Department of Finance established a separate "local mandate" unit which is currently comprised of ten full-time analysts who are involved on a daily basis with analyzing and estimating the costs of the thousands of legislative bills each year. The local mandate unit addresses the single issue of whether or not a bill imposes a State mandate on a local government and, if so, identify the costs involved.

Because we have 58 counties, 418 cities, 1,100 school districts, and about 4,200 special districts, it is important that input from as many agencies as possible be obtained and that the inputting agencies be as representative of the affected universe as possible. The department obtains this input in several ways: First, a formal network of local agencies has been established. Each of the agencies has assigned persons on their staffs to coordinate requests for information regarding the possible impact of State legislation when requested by the department. Second, after the department has prepared its analysis of a bill copies are distributed to the bill's author, to the Legislative Analyst's Office, to the fiscal committee which has scheduled a hearing, and to organizations representing local agencies (e.g., League of Cities, County Supervisors' Association, County Auditors' Association, etc.). These organizations make copies of the analyses available to member agencies and also publicize the findings in newsletters and bulletins. You can see that the analyses get a lot of exposure at the local level and if any local agency finds any erroneous data or that any aspect of the bill has been overlooked, they contact the department to so inform us so that the analyses can be reexamined.

The process and procedure I've been describing may sound as though it extends over considerable periods of time. Normally, though, it extends over perhaps only a week or two or, in some instances, a few days. The reason for this urgency is that the analyses, with their estimates of local costs, which are comparable to the CBO cost estimates, are needed at any legislative hearing by a fiscal committee on a particular bill. I should mention that the Department of Finance actually prepares two separate analyses for many bills: One is the local mandate unit's factual report on a bill's impact on local government, and the other, prepared by our "budget operations" unit, focuses on State costs and policy. This latter analysis is reviewed up through the chain of command and is approved by the Director of Finance and the Governor's Office.

When a fiscal committee conducts a hearing on a bill, then, it has before it a policy analysis from the Department of Finance, a "local mandate" analysis from that department, a report from the Legislative Analyst's Office, and notes from the committee's own staff. If the bill involves State mandated costs to local government, the law requires that an appropriation be included when the bill is passed. However, this is a *statutory* requirement, not a constitutional one, and the legislature is perfectly within their authority to enact a bill as law in a manner which supersedes any existing law. Therefore, the legislature can, and sometimes does, explicitly waive the requirement that local agencies be reimbursed for State mandates. Normally, there are fairly legitimate reasons for these waivers or disclaimers, e.g., the actual costs are relatively insignificant, there are other appropriate means of financing those costs, there are offsetting savings, etc. You may be aware that an initiative measure known as the "Gann Initiative," after its sponsor Paul Gann, will soon be put to the voters of California. That measure would place the requirement for the State to reimburse local government for the costs of State mandated programs in the State's constitution. This will undoubtedly strengthen the S.B. 90 program and limit the use of waivers. In any event, whether a State mandated cost is funded or disclaimed, the legislature record reflects that cost data were provided by the Department of Finance for each measure enacted.

On the positive side, at least from a local perspective, the State has enacted a number of laws since 1972 which provided appropriations to reimburse State mandated local costs. For those laws which established continuing programs, funds are included in subsequent State budgets. The 1979-80 State budget, for example, included approximately $80 million for this purpose.

You may be interested in knowing that our S.B. 90 law also includes an appeals mechanism. If a local agency believes that a State agency or the legislature inappropriately included a S.B. 90 waiver in a regulation or law, that agency may file an appeal for a hearing on the issue with the Board of Control. This board is an administrative appeals body comprised of an administration representative, the independently elected State Controller, and a public member appointed by the Governor. For purposes of hearing S.B. 90 claims, this board is augmented by two representatives of local agencies also appointed by the Governor. That board has approved approximately $30 million worth of claims to date which will be presented to the legislature for consideration. If the legislature provides funding, then the

total amount of funded mandates would be about $110 million (including the $80 million currently funded.)

On the whole, the cost estimates developed for State mandates have been reasonably accurate. The estimates are intended to provide the legislature with an idea of the relative magnitude of costs in a bill, i.e., whether they would be enormous, moderate, or insignificant. When it is possible, and in most cases it is, a specific dollar figure is developed, based on data from local agencies and as necessary on reasonable assumptions about the potential impact of the bill. In virtually all instances, the amount appropriated by the legislature for mandates is based on the finance estimate. In some cases, the appropriation exceeds the amounts claimed and the balance simply reverts and the subsequent years' budgets are adjusted accordingly. If the initial appropriation is not adequate to pay all claims, then those claims are paid on a pro rata basis and a deficiency bill enacted to pay the differences.

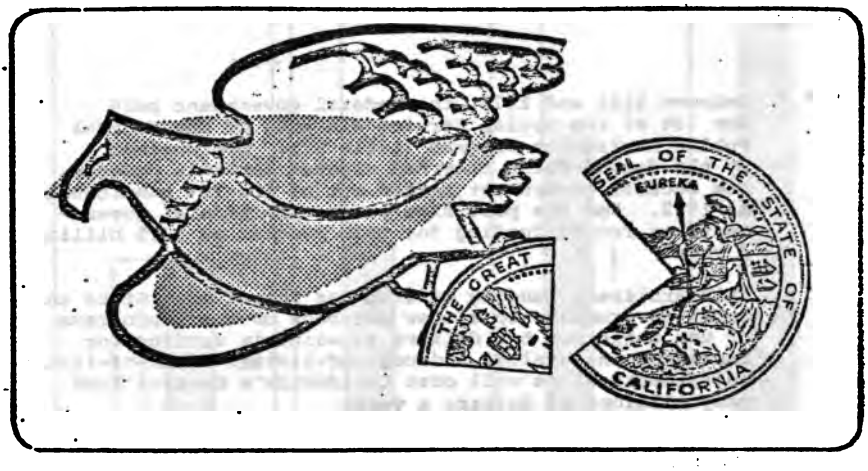
In closing, I'd just like to make the observation that H.R. 3697, while it does not address the question of the Federal Government reimbursing the State and local governments for the costs of federally mandated programs, is, nevertheless, a significant step forward in the area of Federal-State relationships. You may recall that Governor Brown has endorsed the concept of Federal reimbursement of Federal mandates and has offered a "Proposal for a Federal Fiscal Impact Act," also known as "The Buck Stops Here." This proposal calls for the adoption of a Federal policy requiring the Federal Government to pay State and local government agencies for the full costs of implementing congressional and executive directives. These directives would include new programs, increased levels of service for existing programs, maintenance of effort actions and actions which result in revenue losses. The procedural aspects of this proposal are similar to those of our S.B. 90 law which I have described earlier and, in fact, the California experience could be a model for the Federal program. This proposal would also include a feature not found in our S.B. 90 law which would hold harmless State and local agencies for failure to comply which an unfunded Federal directive. My office would be happy to try to answer any questions you might have regarding the S.B. 90 program or the proposal, and we have copies of this proposal available for anyone who might want to review it.

Enclosure.

THE BUCK STOPS HERE

- A Proposal for a Federal Fiscal Impact Act -

BY
THE HONORABLE EDMUND G. BROWN JR.
GOVERNOR, STATE OF CALIFORNIA



PROBLEM: State and local taxpayers are spending more and more of their own dollars for programs initiated because of federal law.

PROPOSAL: Require the federal government to pay state and local agencies for the full costs of implementing Congressional and Executive directives.

A model for such a program has been working successfully in California since 1973. We are convinced that our local mandate reimbursement program can serve as a model for a Federal Fiscal Impact Act.

THE PROBLEM

State and local taxpayers are spending more and more of their own dollars for programs initiated because of federal law, without receiving adequate federal reimbursement. For example...

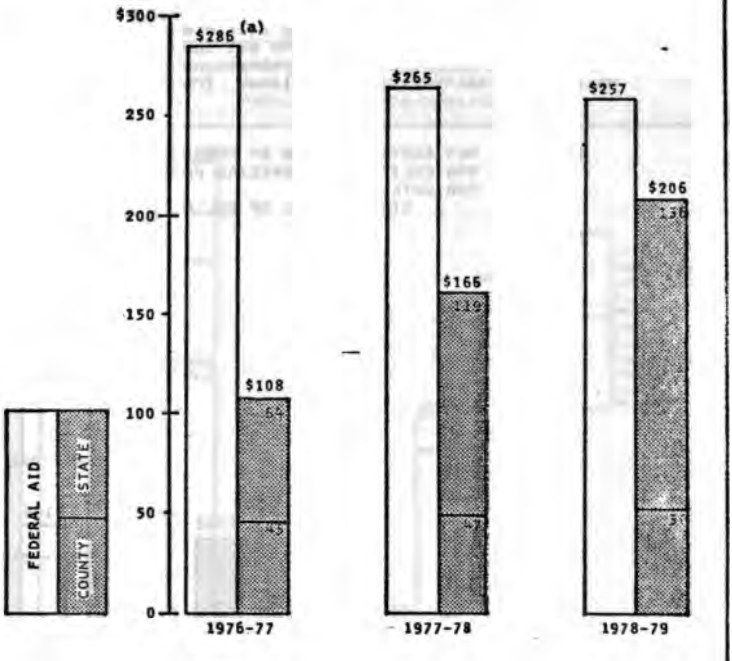
• • • Between 1962 and 1972, the federal government paid for 75% of the Social Service elements of the Federal Public Assistance Program (Title XX). Overwhelmed by the demand which they had created for this program, the federal government backed out of its 75% commitment in 1972. For the past five years, the federal government has frozen funding for this program at $2.5 billion a year.

This arbitrary funding ceiling has forced many State and local governments to either cut back on their programs or use their own tax dollars to maintain funding for increases in caseload and cost-of-living. Cost-of-living adjustments alone will cost California's General Fund many millions of dollars a year.

The Federal HEW estimates that thirty-seven states will have reached the limit of their potential federal participation by fiscal 1979-70. Before you know it, the taxpayers of practically every State in the Union will be called upon to shoulder a mushrooming percentage of the federal government's share of these Social Service programs. If these programs are good enough to keep on the federal books, then it is time to demand that they be federally funded on a full partnership basis.

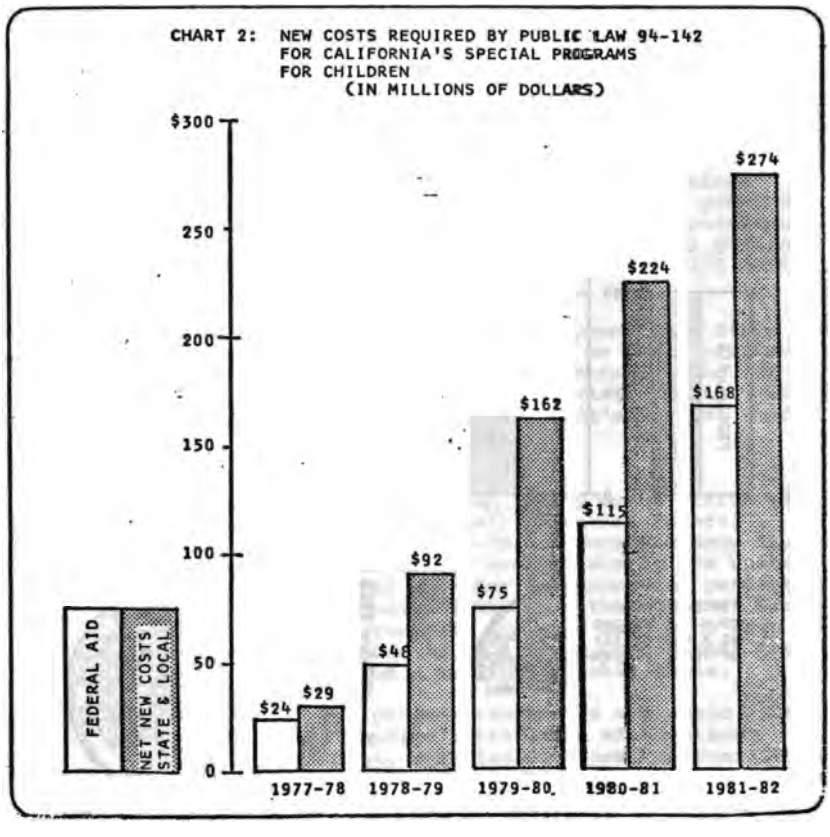
The history of this program represents a classic example of the federal government's tradition of creating financial enticements, stimulating a program constituency and then withholding the financial support necessary to sustain the program. (Chart 1)

CHART 1: CALIFORNIA'S SOCIAL SERVICE PROGRAM
(IN MILLIONS OF DOLLARS)



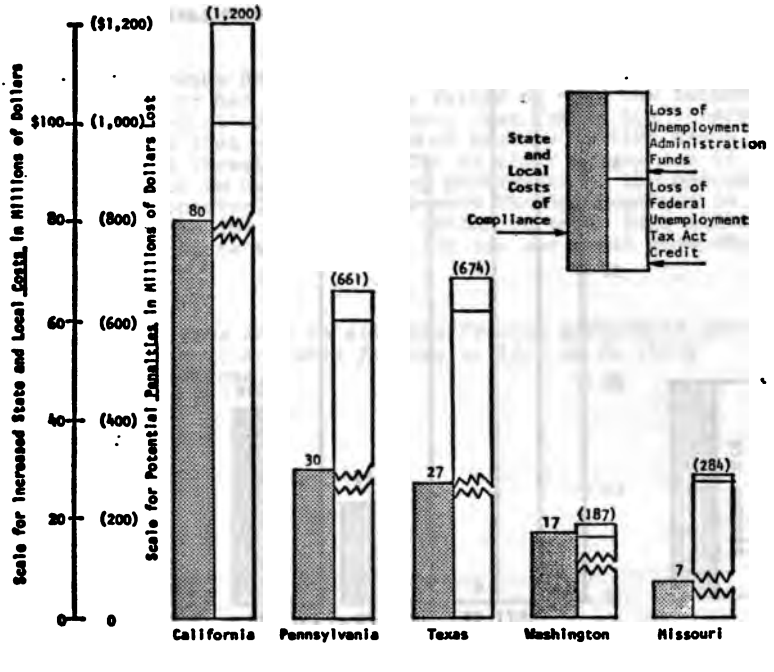
(a) Includes transition quarter

• • • Public Law 94-142 requires an "appropriate" education for all children but fails to establish the level or form of education appropriate for children with various learning and physical impairments. California is already committed to providing educational opportunities for all of its children. However, the federal law mandates haste and introduces new confusion without providing sufficient dollars during program development. The net increase in costs to California taxpayers between now and 1982 will be approximately $781 million. (Chart 2)

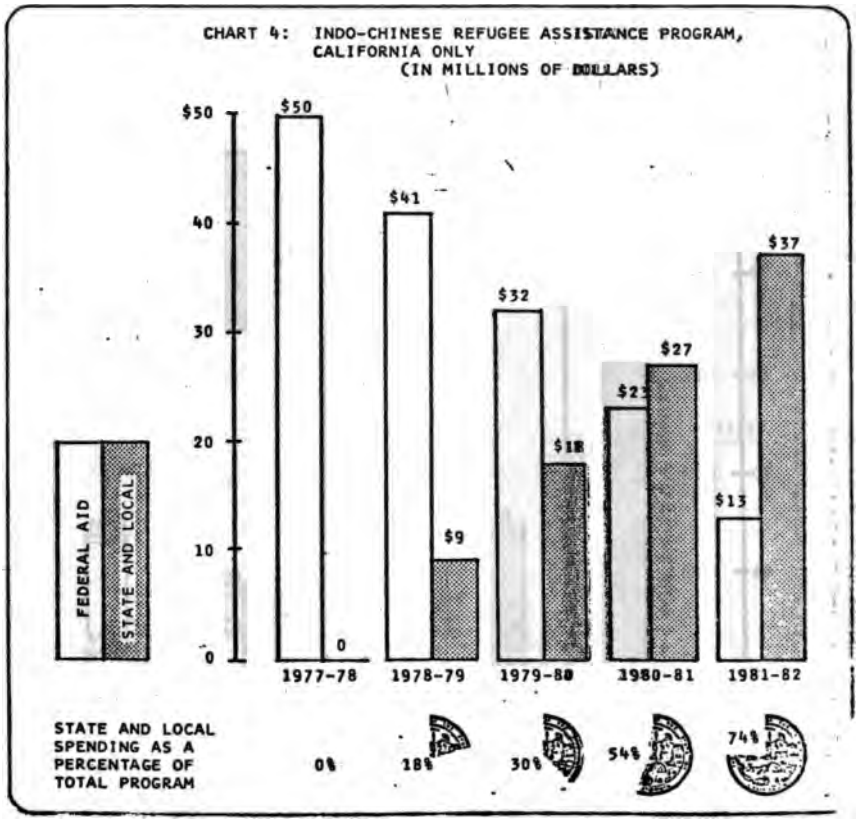


• • • Federal Unemployment Insurance for State and local government employees has been mandated by Public Law 94-566. It is estimated that this mandate will cost New York City $40 million. For California, the costs to our governments will exceed $80 million a year. Most State and local governments face major costs as a result of this program. Failure to comply can result in major penalties. (Chart 3)

CHART 3: ONE YEAR STATE AND LOCAL COSTS OF PUBLIC LAW 94-566 AND MAXIMUM PENALTIES FOR NON-COMPLIANCE



• • • Public Laws 94-23 and 94-24 created a program for refugees from Vietnam and Cambodia. Nationwide approximately one-third of these refugees are receiving public assistance. In California it is estimated about half of the refugees are receiving benefits. California's programs for these new residents include annual costs for medical services, social services, education and cash grants. Federal participation is scheduled to be phased out by 1982, but it is not anticipated that the problems will be resolved (Chart 4)



• • • States are required to seek out potential users of food stamps in an agressive "outreach" program. States failing to comply with this federal directive are threatened with financial sanctions. In California, our $350 million food stamp program is at the mercy of our $836,000 share of this "outreach" effort.

• • • States are required to make extensive improvements to State Hospitals. States which fail to make these improvements face loss of federal Medicaid funding. In California, our hospital improvement program will cost $50 million or more.

• • • Even Revenue Sharing has strings attached. The federal government has consistently failed to meet the letter of its equal opportunity laws. Yet Public Law 94-488 mandates that any recipient of Revenue Sharing funds shall be threatened with loss of their allocation if they fail to comply with any provisions of the nation's equal opportunity laws. Revenue Sharing receipts in California for 1978-79 are estimated to be $250 million for the State and $500 million for our local governments.

Something has to be done to stop the federal government from initiating programs and then failing to live up to their financial obligations.

THE PROPOSAL

The Congress of the United States should be encouraged to enact a law to protect state and local taxpayers from being overwhelmed by actions of the federal government. The proposed law should include the following...

• • • REIMBURSEMENT POLICY

The federal government shall pay state and local government agencies for the full costs of implementing Congressional and Executive directives.

• • • ACTIONS REQUIRING REIMBURSEMENT

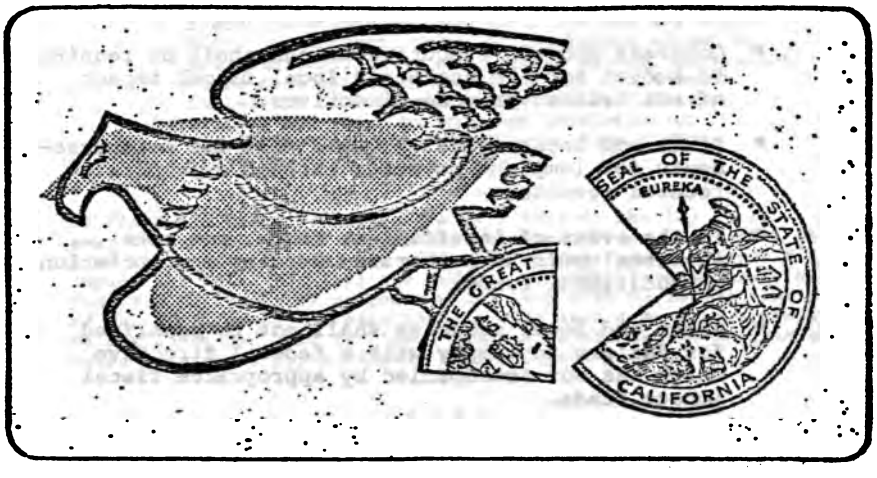
State and local government agencies shall receive...

- Reimbursement for the full costs incurred in the implementation of any new program directed by Congressional enactment or Executive Branch action.
- Reimbursement for the full costs incurred in providing for increased levels of service for an existing program directed by Congressional enactment or Executive Branch action.
- Reimbursement for the full costs of revenue losses resulting from Congressional enactments or Executive Branch action.
- Reimbursement for any "maintenance of effort" requirements directed by Congressional enactments or Executive Branch action.

THE BUCK STOPS HERE

- A Proposal for a Federal Fiscal Impact Act -

BY
THE HONORABLE EDMUND G. BROWN JR.
GOVERNOR, STATE OF CALIFORNIA



APPENDIX

• • • **PROCEDURES**

* Sponsors of proposed federal actions shall be required to file a fiscal impact analysis and proposed funding plan with the Office of Management and Budget or the Congressional Budget Office.

* The appropriate Staff Counsel shall be required to certify proposals which in his judgment would not impose a fiscal impact on state or local governments.

* Congress and the Executive Branch shall be required to budget for the state and local fiscal impact of all federal program directives.

* State and local agencies would file for reimbursements for lump sum payments through appropriate federal agencies.

* In the event of insufficient funds, pro rata payments could be authorized pending appropriation of additional funds.

* State and local agencies shall not be penalized for failure to comply with a federal directive which was not accompanied by appropriate fiscal impact funds.

• • • **APPEALS**

State and local agencies could file individual or consolidated appeals to a designated federal agency in cases where:

* The available appropriation is insufficient to cover the claims for reimbursement.

* Claims have been rejected by the disbursing agent.

* Fiscal impact funds or program funds have been "impounded" due to a fiscal impact dispute.

* The State or local agencies wish to challenge the federal government's claim that there are no fiscal impacts.

• • • **EXEMPTIONS**

Costs resulting from Constitutional Amendments, actions of the Courts and requests by the affected state and local agencies would not be subject to reimbursement.

• • • **DEFINITIONS**

* Congressional enactments shall include any act having a fiscal impact on state or local government agencies.

* Executive Branch actions shall include any order, plan, requirement, rule, or regulation issued by the President, or by any federal agency, department, board or commission; including any order which implements or interprets an existing federal statute and which by such implementation or interpretation increases program levels above those required by the statute.

As State and local taxpayers are left holding the bag on an ever increasing number of federal programs, it is clear that the time for action is now. We will all benefit from a Federal Fiscal Impact Act which requires the federal government to evaluate and fund the full cost of programs which they wish to impose upon all of us. California has been working with such a program since 1973. We are convinced that our local mandate reimbursement program can serve as a model for a Federal Fiscal Impact Act.

* * * *

FOR MORE INFORMATION

California's Department of Finance is preparing an Appendix to this report which includes the history and provisions of California's local mandate law, as well as a rough discussion draft of a possible Federal Fiscal Impact Act.

If you are interested in receiving copies of the Appendix, call the Department of Finance at (916) 445-9862, or write: Director, Department of Finance, Room 1145, State Capitol, Sacramento, California 95814.

A Proposal for a Federal Fiscal Impact Act
Discussion Draft of Possible Legislation

Sec. 1. It is the intent of Congress to establish a means by which states and local governments shall be reimbursed for costs incurred as a result of a Federal statute or regulation. It is the intent of Congress that by providing such reimbursement, programs resulting from Federal legislation and regulations will be implemented equitably throughout the nation without placing the burden of finance upon state and local governments. Such policy does not intend to encroach upon state and loca power to continue to provide existing programs as well as initiate programs deemed necessary by such political units.

Sec. 2. "Local entity" means any agency of a state for the local performance of governmental or proprietary functions within limited boundaries. "Local entity" includes a city, county, school district community college district, county superintendent of schools county service area, a manitenance district or area, an improvement district or improvement zone, or any other zone or area formed for the purpose of designating an area within which a property tax rate will be levied to pay for a service or improvement benefiting that area. "Local entity" does not include any entity which is not authorized by state or federal statute to levy a property tax rate.

Sec. 3. "Costs initiated by the Federal Government" means any increased costs which a state or local entity is required to incur as a result of the following
(a) Any law enacted after January 1, 1979 which initiates a new program or an increased level of service of an existing program;
(b) Any federal regulation issued after January 1, 1979, which (i) implements or interprets a federal statute and (ii), by such implementation or interpretation, increases program levels above the levels required prior to January 1, 1979.

Sec. 4. "Federal regulation" means any order, plan, requirement, rule, or regulation issued:
(a) By the President, or
(b) By any officer or official serving at the pleasure of the President, or
(c) By any agency, department, board or commission of Federal government.

Sec. 5. "Law enacted after January 1, 1979" means any statute enacted by Congress after January 1, 1979.

Sec. 6. "Property tax rate" means any rate of tax or assessment which is levied per unit of assessed value of property. "Property tax rate" includes any rate or assessment which is levied on the value of land only, as well as any rate or assessment which is levied on the value of land and improvements.

Sec. 7. The Federal government shall annually reimburse states and local entities for the net loss of revenue from each statute or regulation enacted or issued after January 1, 1979, which provides for an exemption or restriction of collection of sales or use tax, property tax, or state or local income tax. The reimbursement shall be made when funds have been appropriated by Congress.

Sec. 8. (a) The Federal government shall reimburse each state and local entity for all "costs initiated by the Federal government" as defined in Section 3.

(b) For the initial fiscal year during which such costs are incurred reimbursement funds shall be provided as follows: (1) any statute initiating such costs shall provide an appropriation therefore and (2) any regulation initiating such costs shall be accompanied by a bill appropriating the funds therefore, or alternatively, an appropriation for such funds shall be included in the Budget for the next following fiscal year.

In subsequent fiscal years appropriations for such costs shall be included in the Federal Budget.

(c) The amount appropriated for such purposes shall be appropriated to the appropriate department for disbursement.

(d) The department shall disburse reimbursement funds to states as follows: (1) For the initial fiscal year during which such costs will be incurred, each local entity to which the program is applicable shall submit to its respective state, within 90 days of the operative date of the program, a claim for reimbursement as well as its estimate of the costs required by such program for the current fiscal year. Each state shall then submit an itemized total of such local agency claims within 120 days of the operative date of the program. States shall submit state claims for reimbursement within 120 days of the operative date of the program. The department shall pay such claims from the funds appropriated therefore, provided that (i) records of any state or local entity may be audited to verify the actual amount of the reimbursable costs and (ii) any claim may be reduced when it is determined that such claim is excessive or unreasonable, and (iii) payment may be adjusted to correct for any under payments or overpayments which occured in the previous fiscal year. (2) Payments shall be made to each state for all costs incurred by the state. Payment shall be made to the state for distribution to the local entities which filed claims pursuant to subdivision (1) If the department has adjusted the total amount requested by the state for reimbursement to local entities, the state shall prorate the individual local agency claims.

Sec. 9. Any funds received by a state or local entity pursuant to the provisions of this chapter may be used for any public purpose.

Sec. 10. No claims shall be made pursuant to Sections 7 and 8 nor shall any payment be made on claims submitted pursuant to Sections 7 and 8 unless such claims exceed two thousand dollars ($2,000.00)

Sec. 11. If a state or local entity has, at its option been incurring costs which are subsequently required by the Federal government, the Federal government shall reimburse the state or local entity for such costs incurred after the operative date of such action and the state or local entity shall reduce the amount of tax collected for such purpose by an equivalent amount.

Sec. 12. Claims for direct and indirect costs filed pursuant to Sections 7 and 8 shall be filed in the manner prescribed by the General Accounting Office.

Sec. 13. When a proposed statute is introduced in Congress, the Committee Staff Counsel of the house of origin shall determine whether such bill requires federal reimbursement to states or local entities pursuant to Section 7 or 8. Such determination shall be printed in the Congressional Record.

In making the determination required by this section the Committee Staff Counsel shall disregard any provision in a bill which would make inoperative the reimbursement requirements of Section 7 or 8, and shall make such determination irrespective of any such provision.

Sec. 14. Whenever the Committee Staff Counsel determines that a proposed statute will require Federal reimbursement to a state or local entity as provided in Section 7 or 8, the department shall prepare estimates of the amount of reimbursement which will be required. Such estimates shall be prepared for the respective committees of each house of Congress which consider taxation measures and appropriations measures and shall be prepared prior to any hearing on such a bill by any committee designated to consider legislation.

Sec. 15. The estimate of cost required by Section 14 shall be the amount estimated to be required during the first fiscal year of a bill's operation in order to reimburse states and local entities pursuant to Section 7, or 8, for costs initiated by such bill. In the event that the operative date of such a bill does not begin on October 1, the estimate shall also include the amount estimated to be required for reimbursement for the next following full fiscal year.

Sec. 16. In the event that a bill is amended on the floor of either house, whether by adoption of the report of a conference committee or otherwise, in such a manner as to require reimbursement pursuant to Section 7 or 8, the Committee Staff Counsel shall immediately inform, respectively, the Speaker of the House and the President of the Senate of such fact. Such notification from the Counsel shall be published in the Congressional Record.

Sec. 17. In every subsequent fiscal year, the Federal Budget shall include appropriations to continue to reimburse states and local entities for costs initiated by the Federal government, and previously approved for reimbursement in accordance with Sections 7 and 8.

Sec. 18. Before the end of each calendar year the General Accounting Office shall review all statutes enacted during such calendar year which (1) contain provisions making inoperative Section 7, 8, or 11, or (2) have resulted in costs or revenue losses required by the Federal government which were not identified when the statute was enacted. Such review shall identify the costs or revenue losses involved in complying with the provisions of such statutes. The General Accounting Office shall submit to Congress an annual report of findings and recommendations as it may deem appropriate.

Sec. 19. The General Accounting Office, pursuant to the provisions of this article, shall hear and decide upon a claim by a state or local agency that such state or local agency has not been reimbursed for all costs required by the Federal government.

Sec. 20. In the event a claim submitted pursuant to the provisions of this article has been denied by the General Accounting Office the claimant may appeal such denial for reimbursement to the appropriate federal court authorized to adjudicate claims against the federal government.

THE HISTORY OF CALIFORNIA'S LOCAL MANDATE PROGRAM

For many years the California State and local government relationship worked well because of a well-defined division of responsibility between the two levels. In recent years however, there has been a trend toward a heavier emphasis on centralized State government. Legislation at the state level often required local government to provide its residents with designated services, furnish information, or otherwise perform duties without any additional fiscal resources from the State. Therefore, the burden of financing these state-mandate programs fell on the shoulders of the local property taxpayer. As inflation began to impact the tax roles and local government costs began to soar, it became clear to local government that some kind of a lid had to be put on either the expenditures mandated by the State or the amount of taxes levied against the homeowners.

In 1972 the Legislature responded to the concerns of the local governments by declaring its intent to have the State pay for mandated programs. The 1972 property tax relief act did two things for the homeowners:

1) It provided tax relief by:
   - A) Increasing State support for elementary and secondary education;
   - B) Imposing property tax limits on cities, counties and special districts;
   - C) Imposing revenue limits on school districts;
   - D) Increasing the homeowners property tax exemption by $1000 of assessed value to a total of $1750 per year;

E) Increasing the State sales tax from 3 3/4 percent to 4 3/4 percent; and,

F) Establishing renters relief based on adjusted gross income.

2) Provide a mechanism for the State to pay for state-mandate programs by:

A) Reimbursing cities and counties for property, sales and use tax exemptions;

B) Reimbursing cities, counties, and special districts for the full cost of any new state-mandate program or increases in the level of service of an existing program;

C) Reimbursing cities, counties and special districts for the full cost of any new program or any increased level of service of an existing program mandated by any state executive regulation;

D) Reimbursing local agencies for programs mandated by the State which local government had been performing at their option but which became mandated by the State.

The bill also provided other technical language primarily directed to controlling the local government tax rate and by providing exclusions (i.e. disclaimers), such as:

1) Legislation requested by local government;

2) A program mandated by the Federal government;

3) Costs incurred as a result of a court decision;

4) Mandates that provided for self financing, incurred no new duties, or would result in no net cost;

5) Mandates that created a new crime or infraction.

The bill also created a mechanism whereby local government could seek relief and obtain reimbursement through a non-judicial administrative procedures system.

Subsequent legislation was enacted to expand the State-mandate law to include school districts reimbursement in a manner similar to other local government entities. The most recent legislation enacted provided some additional changes to the program.

1. The law directs the Attorney General to include the costs of any initiative presented to the people in the title or summary of that initiative;

2. It provides that the State Controller will prorate amounts paid to local entities if the appropriation contained in the mandate legislation is insufficient;

3. The Legislative Council is directed to determine whether a bill requires State reimbursement and to make that determination known in the digest of the bill.

4. The Department of Finance is required to prepare cost estimates of a bill containing a mandate prior to hearings in the fiscal committees;

5. Funding for continuing local mandate mandated costs is to be included in the annual State budget and related budget bill;

6. The State Controller is given the authority to audit additional tax rates imposed by local entities for the purpose of paying for Federal or court mandates or initiative enactments (there is a provision for the Attorney General to bring an action to force a local government to reduce its tax rate if it has been legally required by law to do so and failed to take appropriate action).

The 1979-80 Governor's Budget includes in excess of $80 million to be appropriated for the purpose of reimbursing local governments for one-time and continuing costs mandated by the State. This is an increase of over $22 million above the original amount expended in 1977-78. The cost of State mandates is expected to continue its growth trend. However, the Legislature is fully conscious of the need to evaluate each piece of legislation for its impact on local government.

Appended hereto is an abstract of those code sections related to the state-mandate law and the procedures to be followed for the reimbursement of costs to local government by the state.

FOOD STAMP OUTREACH PROGRAM

The Food Stamp Outreach Program is mandated by the Food Stamp Act of 1974 and 1977, and by federal regulations. The law requires that the state agency (DBP) shall be responsible for employment and training of a sufficient number of qualified personnel to carry out the mandate of outreach requirements. Recent court interpretations have specified the types of outreach activities to be performed, the role of other agencies and organizations in the outreach effort, and state responsibilities in terms of organizing, supervising, monitoring, and evaluating outreach programs.

In FY 1975-76, the county welfare departments were responsible for administering the program. This did not prove to be an effective approach because of strong county resistance to the concept of outreach. A number of CWD's refused to implement outreach programs and many others had inadequate programs. It was alleged that county-operated outreach efforts were not in conformity with federal regulations, and the state was threatened with financial sanctions.

In FY 1976-77, the state initiated its own outreach effort. Fifty percent state match is required to fund the outreach program. The state has used PWEA - Title II funds to meet this match requirement. Proposed budget year programs level is $836,000.

Expenditures in other states are unknown but appear comparable with California expenditures.

INDO-CHINESE REFUGEE, CUBAN ASSISTANCE, AND UNDOCUMENTED PERSONS

The Indo-Chinese Refugee Assistance Program (IRAP) was established under authority of the Indochina Migration and Refugee Assistance Act of 1975 (Public Law 94-23), Special Appropriations for Assistance to Refugees from Cambodia and Vietnam (PL 94-24) and federal policy directives. Effective July 1, 1976, Laotians were added. The IRAP is to be phased out over the next four federal fiscal years in accordance with PL 95-145. Under this federal law, IRAP will be 100 percent federally funded in the current federal fiscal year (October 1, 1977 - September 30, 1978). In subsequent federal fiscal years, federal reimbursement will be based on the following cost sharing arrangement 1979 at 75 percent; 1980 at 50 percent; and 1981 at 25 percent.

About 150,000 Vietnamese Refugees have been admitted to this country, with something over one-third presently residing in California. Other states with significant caseload include Washington, Hawaii, Oregon, Virginia, Texas, Pennsylvania, Wisconsin, Illinois, New York and Minnesota.

According to HEW, about one-third of the refugees are believed to be drawing Public Assistance although California's experience is somewhat higher. The total California Vietnamese population of between 50,000 and 75,000 includes 1,000 SSI/SSP recipients, 11,000 federally eligible AFDC recipients, and 11,000 General Assistance cases. An additional 7,500 refugees receive benefits from the Medi-Cal program. Total IRAP Public Assistance caseload in California is just over 30,000 persons, or roughly half of the total IRAP population.

The Cuban Refugee Program is similar to the Vietnamese Program except that it is older and has less impact on Western states. It was established by Presidential proclamation in 1961 and was implemented in accordance with the Migration and Refugee Assistance Act of 1962 to meet the needs of Cuban refugees. It provides financial assistance, medical assistance, and social services to Cuban refugees. The Cuban Refugee Program, which was 100 percent federally funded through 1976-77, will be phased out over the next six years. Expenditures during 1976-77 provide the base for determining future federal funding. Ninety-five percent of 1976-77 expenditures will be available in 1977-78, 85 percent during 1978-79, 75 percent in 1979-80, 75 percent in 1980-81, 60 percent in 1981-82, 45 percent in 1982-83, and 25 percent in 1983-84.

Undocumented persons. If Federal law is amended to permit presently undocumented persons to legally remain in California, state and county costs will be increased enormously.

Projected Costs - California IRAP
Millions of Dollars

	1977-78	1978-79	1979-80	1980-81	1981-82
Federal	$50	$41	$32	$23	$13
State and County	--	9	18	27	37
Total	$50	$50	$50	$50	$50

UNEMPLOYMENT INSURANCE PROGRAM

In October of 1976, the Federal government passed PL 94-566 (HR 10210). This bill, entitled the "Unemployment Compensation Amendments of 1976," mandated numerous changes to state unemployment compensation laws. Included among these changes was the mandatory coverage provision for state and local governmental employees. The measure had a few exceptions, including elected and appointed officials, members of the National Guard, inmates, and other similar classifications of individuals.

Under California state law in effect at the time PL 94-566 was passed, full-time state employees were covered for unemployment insurance if a layoff occurred due to a budget cutback or other economy move. An exception had been made for temporary and part-time state employees and they were not covered. These individuals were often "on call" and worked during periods of peak workload in various state departments. These employees, as well as all others in state government, were required to be covered in a state's ordinary UI program under the mandates of PL 94-566.

Local governmental entities in California had long been given the option of participating or not participating in the unemployment insurance system. (See California Unemployment Insurance Code Sections 710, 710.2, and 1461 et seq.). While some elected coverage, the overwhelming number of jurisdictions did not. Under the mandate of PL 94-566, all local governmental jurisdictions must provide coverage This is a considerable departure from existing circumstances in California and many other states.

In 1974 the Federal government did extend unemployment benefits to these uncovered workers (both the state and local) through the Supplemental Unemployment Assistance Program (SUA, PL 93-567). This was a federally initiated and financed program. To participate, a state signed an agreement with the Secretary of Labor and the Federal government agreed to reimburse all benefits and costs of administration. PL 94-566 revoked this Federal program. This effectively transferred a federally initiated financial liability away from the Federal Government and mandated it upon the states.

As a partial incentive for states to enact this new coverage, PL 94-566 included a transitional funding provision. Federal revenues would be used to pay unemployment compensation benefits to the extent that qualifying base wages were earned prior to January 1, 1978 In addit on, Federal unemployment laws provide a convincing disincentive for those states considering noncompliance. Employers in the states without laws n substantial compliance are in jeopardy of losing the 2.7 percent FUTA tax credit. The FUTA tax is a Federal tax separate and apart from those taxes levied by the State to pay the cost of benefits for state unemployment systems. Loss of the credit against the Federal tax would amount to double taxat on. In a large state such as California, this penalty could amount to increased taxes on business and a corresponding drain on the economy in excess of one billion dollars per year. Noncomplying states would also be n jeopardy of losing their Federal allocation for administration of the UI program.

The fiscal effect on state and local government of complying with this mandate in Californ a is estimated to be approximately $80 million. This includes estimated increased expenditures of approximately $10 million at the state level. Local governmental entities and school districts, many of which are financed to a great extent by property taxes, would have increased annual expenditure requirements of $55 million and $15 million, respectively. The full impact of these increases w be experienced in 1979, after cessation of the Federal transitional funding provisions.

As previously indicated, the penalty provisions for noncompliance would impact California significantly. In addition to the $1 billion drain that would materialize by a disallowance of the FUTA tax credit, California could also lose the Federa allocation for unemployment administration if it failed to enact complying legislation. In California this could mean a loss of almost $200 million per year.

Among the several states, many are similarly impacted by this mandate. In most cases, the cost is substantial and the potential penalties devastating. In Missouri for examp e increased benefit costs were estimated to be $7.3 million, with most of the burden fa ing on the shoulders of local government. Fai ure to comply would have cost Missouri business approximately $250 million with the loss of the FUTA tax credit, and approximately $34 million in unemployment administration funds.

Washington State estimated similar effects with increased coverage costing local government and schools an estimated $17 million. The State had previously extended coverage to state employees. The FUTA tax credit loss would have cost Washington business approximately $153 million and loss of Federal unemployment administration funds would have amounted to an additional loss of approximately $33.8 million.

Pennsylvania and Texas estimated the potential loss due to the penalty provisions to be $661 million and $674 million, respectively. The respective increased benefit costs to ocal government was estimated to be $30 million and $27.3 million (both states had previously covered state employees).

The following list is of perceived characteristics of this single example of a Federal mandate:

1. Congress passes PL 93-567 initiating the Supplemental Unemployment Assistance Program (SUA) as part of the Emergency Jobs and Unemployment Assistance Act of 1974. This measure covers many previously uncovered workers for unemployment insurance. This is a federally initiated and federally financed program, and commits government to providing these benefits.

2. California and other states participate in administering the program and are fully reimbursed for both the administrative and benefit costs.

3. Congress passes PL 94-566 shifting the costs of this program from the Federal government to the states.

4. The State of California and its local governmental subdivisions are burdened with additional annual expenses estimated to be up to $80 million per year. Other states and local governmental entities are similarly burdened.

SOCIAL SERVICES UNDER TITLE XX OF THE SOCIAL SECURITY ACT

Social services are part of the Federal Public Assistance Program. Prior to 1962, Federal matching funds were available to the states for service-giving within the Public Assistance Program, but without much encouragement. The Public Welfare Amendments of 1962 required the states to provide services to former, current, and potential welfare recipients, and authorized Federal payment of 75 percent of the cost. Federal financial participation in social services was available on an open-ended basis, with either the states or counties providing the remaining 25 percent. Federal law did not define the services; it merely stated their purpose.

With such open-ended and ill-defined social service participation available from the Federal Government state administrators and county welfare directors in California attempted to maximize Federal grants wherever possible. As a result, California experienced an explosion in social service spending. From 1967 through 1971, Federal grants for social services in California increased from $59,907,000 to $216,633,000, an increase of over 250 percent.1/

In FY 1972-73, the Federal Government placed a $2.5 billion ceiling on Federal financial participation in social services. By 1974-75, California reached its federally allocated ceiling. Federal allocations to the states are based on population (California's share is approximately 10 percent) and are adjusted annually. California was allocated $245.7 million for FY 1972-73 1973-74, 1974-75; $245.5 million in FY 1975-76; $246.8 for FY 1976-77; $247.3 for FY 1977-78; and an estimated $250.6 for FY 1978-79.

With the strong initial impetus and full recognition of unmet needs, California's caseload and costs continue to grow. The State has funded program growth in social services program areas by General Fund augmentations. The In-Home Supportive Services and direct county service programs have required the greatest General Fund augmentations. California, state and local is substantially overmatched in these areas. In-Home Supportive Services for 1978-79 will be 56 percent General Fund. Current year funding ratio is 46 percent Federal/54 percent State. In addition, many social service programs such as adoptions and family planning are almost 100 percent state funded.

The counties have funded program growth either with local augmentations or by reducing the scope of services. Counties overmatched county social services by $5 million in fiscal year 1975/76, $6.5 million in FY 1976-77

1/ Martha Derthick, "Uncontrollable Spending for Social Services Grants," The Brookings Institution, March 1975, p. 29.

and is estimated to overmatch by $8.6 million in the current fiscal year. Cost of living for these programs was funded by a $6.9 million General Fund augmentation in 1976-77. These programs historically had been 75 percent Federal and 25 percent county funds with any overmatch funded by the counties and at their option. In FY 1977-78, the $6.9 million became part of the base upon which a 6 percent cost-of-living on the Federal and State share was calculated. Thus, the General Fund cost in FY 1977-78 is $13.8 million and is estimated at $22.1 in FY 1978-79.

Twenty-six states in federal fiscal year 1977 were within 95 percent of their allocation. The Department of Health, Education and Welfare estimates that in FFY 1978 thirty-one states will reach maximum allocation, and in FFY 1979 thirty-seven will reach maximum allocation.

As each state reaches its ceiling, the issue of funding program growth and cost-of-living increases must be addressed by the State Administration and Legislature. In some states, where the Legislature is unwilling to use state funds for federally mandated programs, reductions in program content have been forced in order to absorb cost-of-living increases. For example, Utah has already overmatched its $14.5 million program by $.5 million in state funds and the Legislature is unwilling to provide any additional funds. This has forced a reduction in services in Utah's In-Home Supportive Services Program. This reduction is being accomplished by limiting eligibility through elimination of the income eligible category.

Other states have pursued funding shifts to the extent possible. New York has restructured its In-Home Supportive Services Program to capture federal medical assistance funds for medically related services.

Overall, as the Title XX ceiling is reached by each state, either additional state and local funds must be placed in the programs or alternatives such as program reductions, funding shifts or freezing program levels must be pursued. These alternatives tend to reduce services and limit their availability.

Under the California law for reimbursing mandated costs, even if a local agency voluntarily is performing a function, the State will pay the cost of that function if the State requires the local agency to perform the function. Our position on P.L. 94-142 is similar. California was moving in the direction of free appropriate education for handicapped children even before P.L. 94-142 was enacted. However, California has been forced to move faster and more comprehensively than would have occurred without P. L. 94-142. We agree with the concepts of the legislation but believe the Federal Government should pay the full cost of this mandate just as California would have paid had we enacted this legislation. Although some may argue that P.L. 94-142 is not a mandate because the states can choose not to participate, and thereby lose some existing federal funds, this is not a realistic choice and would be poor public policy. P.L. 94-142 is a mandate on the states and if the Federal Government believes it is a necessary requirement, then the Federal Government should pay the costs of the mandate.

I. Service Levels Required by Public Law 94-142.

1. Public Law 94-142 requires California to guarantee all handicapped children a free appropriate education. Unfortunately, neither the legislation nor the regulations contain specific definitions of the terms appropriate education or handicapped children.

2. The legislation also contains "due process" provisions which provide parents rights to participate in decisions (placement and program level) which affect their handicapped child. Additionally, parents may appeal the decisions made by the school district and they may request educational services be provided by private schools at no cost to the parent.

3. Because P. L. 94-142 and the associated regulations do not define service level by either number of children or type of service (special class or remedial assistance), it is impossible to determine an exact cost for the legislation. California has assumed that 11 percent of the children will require special education assistance.

II. State Law Prior to P. L. 94-142.

1. Prior to P. L. 94-142, California's special education program was serving about 320,000 children in the regular special education program and the Master Plan for Special Education Pilot Program which was scheduled to terminate on June 30, 1978.

2. Service was provided in special residential schools, special classes, and remedial assistance programs to children with severe and moderate handicaps.

3. State and local costs (in millions) for the special education programs prior to P. L. 94-142 are estimated as follows:

1977-78	1978-79	1979-80	1980-81	1981-82
$575	$562	$577	$592	$607

4. The current special education system has been changed to allow service and funding for mild handicaps increased parent participation, and the due process provisions.

III. California Master Plan for Special Education: A Means of Meeting the Requirements of Public Law 94-142.

1. California's Master Plan for Special Education meets the requirements of Public Law 94-142 by guaranteeing free appropriate education to all handicapped children and requiring the due process provisions of Public Law 94-142.

2. The number of children receiving services will increase by approximately 130,000.

3. Funding is provided for local costs to meet due process provisions. The state support funding model provides state aid on the basis of level of service rather than handicapping condition.

4. State and local costs (in millions) for the Master Plan for Special Education and regular special education are as follows:

	1977-78	1978-79	1979-80	1980-81	1981-82
State	$298	$347	$403	$465	$526
Local	306	307	336	351	355
Total	$604	$654	$739	$816	$881

TABLE I
COSTS OF SPECIAL EDUCATION DUE TO PUBLIC LAW 94-142a/
(in millions)

	1977-78	1978-79	1979-80	1980-81	1981-82
State & Local	$604	$654	$739	$816	$881
Federal	24	48	75	115	168
Total	$628	$702	$814	$931	$1,049
Less State and Local Pre 94-142	-575	-562	-577	-592	-607
Net New Cost	$ 53	$140	$237	$339	$442
Less Federal Aid from 94-142	-24	-48	-75	-115	-168
Net Increased Cost to Calif. Taxpayers	$ 29	$ 92	$162	$224	$274

a/ Cost of Special Education assumes full implementation of the Master Plan for Special Education. P. L. 94-142 funds are estimated. California is assuming that only 11 percent of the students will require special administration, residential schools or other federal and state categorical aid program support for special education.

[Whereupon, at 12:10 p.m. the task forces adjourned.]

DATE DUE			