Question.—Why is the per capita method used to distribute funds? Why not return the money where it came from?

Answer.—The per capita method of distributing the grants among the States was chosen because it is the best available index of both fiscal capacity and need. It allocates more money to the relatively populous States; at the same time, it automatically distributes relatively more to a poor State than to a rich State. For example, a $25 per capita distribution would amount to 10 percent of the budget of a State that can afford to spend $250 per capita and only 5 percent of the budget of a State that can afford to spend $500 per capita.

As we have already indicated, more equalization could easily be provided if desired. We favor using a small part of the fund—say, 10 percent—for the poorest third of the States. This additional allotment—though a small part of the aggregate grants—would raise the average per capita grant in the ten poorest States by over 50 percent.

Tax effort might also be given some weight in the formula to give the States an incentive to maintain or increase tax collections out of their own sources. Such a spur could be built in by weighting the per capita grants to each State by the ratio of that State's tax effort to the average tax effort in the country—tax effort being defined as the ratio of State-local revenues to personal income. An interesting and rather mixed set of above- and below-par States emerges by this standard. For example, in 1964:

> Louisiana, New Mexico, and North Dakota would have had effort indexes of 120 or above.
>
> Nine States would have had an index of 85 or less: Connecticut, Delaware, Illinois, Maryland, Missouri, New Jersey, Ohio, Pennsylvania, and Virginia.

On the other hand, it would be totally inappropriate to allocate the funds in proportion to the amounts collected from each State. This would give disproportionately larger shares to the wealthiest States, and would widen rather than narrow differentials in State fiscal capacities.

Question.—What happens during a recession? Aren't you worried that the States and local governments would be in trouble if the revenue sharing funds declined?

Answer.—The tax base has declined only twice since the end of World War II—by 4 percent in 1949 and by less than one-tenth of 1 percent in 1958. These are within the range of fluctuations that State and local governments have become accustomed to in their own tax sources. Nevertheless, in a deep recession, there would be no problem. In such circumstances, the Congress could easily add to the normal amounts going into the revenue sharing reserve fund to prevent financial distress at the State-local level. Few anti-recession measures would be as efficient from both the efficiency and stabilization standpoints.

Question.—The Federal Government already has a well-developed system of categorical grants? Why do we need general-purpose grants?

Answer.—Categorical and general-purpose grants have very different functions and these cannot be satisfied if the Federal system were limited to one or the other.

In distributing future fiscal dividends, the Federal Government can and should give high priority to categorical aid. Their dramatic growth will doubtless continue. They tripled in the 1950's, reaching $7 billion by 1960. They are well on the way to tripling again by 1970, as is reflected in the President's request of $17.5 billion in categorical aids for fiscal 1968.

In appraising the relative role of conditional or unconditional grants, one must be clear on the distinction between the defects or flaws in the administration of the existing grant-in-aid system—those which can presumably be overcome by improvements in it—and those which are intrinsic to the conditional grant-in-aid instrument.

Keen awareness of the limitations in practice was expressed in testimony before the Senate Subcommittee on Intergovernmental Relations last year by the Director of the Bureau of the Budget. He identified the problems as:

> Proliferation of programs to a total of 162 by early-1966, under 399 separate authorizations.
>
> Excessive categorization of grants which, together with direct negotiations between individual bureaus and their counterparts in State-local governments, have led to bypassing cf governors and mayors and weakening of their control over their own administrations.