The appropriation action would commit the Government to an ex-ended period of contract payments in accordance with the provisions )f the statute.

Mr. BLATNIK. On the same page 4, under paragraph 3:

Under the contracts the Federal Government would pay the principal and nterest on that portion of the bonds that represents the normal Federal grant hare under the present act.

That is understandable, and I think reasonable.

Later on, if I could have an explanation of this proposal:

Contracts would also provide a Federal guarantee of the non-Federal share ınd the payment of an interest subsidy to reduce the net effective interest rate o States and localities to a rate reasonably comparable to rates on tax-exempt nunicipal bonds.

Contracts would also provide the Federal guarantee of the non-Federal share.

The question would be: Is that unusual or what is the justification or that guarantee?

Mr. HUGHES. This is a new sort of approach, Mr. Chairman. The oncept basically is that the Federal Government in extending the Federal guarantee to the Federal share of the obligation extends a ubstantial benefit to the community and in effect supports the whole obligation. I think the committee is aware of our concern that the Sec-etary expressed over tax exemptions as a means of supporting—as a ubsidy means, in effect, of supporting local obligations.

We recognize, however, that the withdrawal of tax exemption in his particular situation would cause the community to pay a some-vhat higher rate than would be charged for the tax-exempt obliga-ion. And the interest subsidy which is referred to in the last sentence vould be in recognition of that somewhat higher rate and would be Federal subsidy to lead the community into essentially the same osition as it would have been had it borrowed on a tax-exempt basis.

I think it might be well, if you wish at this point, to talk a little bout the tax-exempt problem; and briefly the situation is this: Ve feel that a number of factors make it wise in a program of as direct Federal concern that this one is to provide an alternative to normal ocal tax-exempt financing. There is a great deal of evidence of pres-ure on the tax-exempt bond market, pressure which has resulted in ncreased interest rates and the prospect of even further increases.

The taxable market is a much broader market. And it would take orrespondingly heavier pressure. So that concern has caused us to uggest this guaranteed, Federal guaranteed approach rather than a ax-exempt approach.

Also, and of more direct concern to us and I believe to the committee, ; is quite clear that tax exemption per se is a relatively inefficient ubsidy means to carry out Federal objectives.

The tax exemption has two effects really. It provides somewhat lower nterest rates to the community, but it also provides higher income han would be provided by a taxable security to the investor. The ower interest rates to the community are not—they are not pro-ortionately lower in consideration of the cost in lost taxes to the Federal Government. As a consequence, this approach which we have utlined in this legislation, would achieve the same result with the