of the social programs would thus be made at a lower cost to the Federal Government than would be involved in the local taxable bond approach—where the size of the annual debt service grants of the Federal Government would be governed by the *local taxable* bond rate and not the rate on Federal obligations.

Finally, the State and local governments could participate directly in the management and control of the Bank itself. Use of the Bank would be on a voluntary basis however—any State or local government could still finance projects directly through its own obligations. Hence the accommodation to independence of State and local governments, that factor which these governments see as the essence of the tax-exemption privilege, can be achieved through a proper structuring of the Bank.

I commend the concept of a Development Bank to you for your close study and consideration. Here also you have the opportunity through objective analysis to weigh the possibilities of this new approach and then if it offers promise, to use your experience and wisdom to shape its structure and its future.[4]

Conclusion

In conclusion, let me return to the summary I gave you at the outset:

The possible high level of new issues of tax-exempt State and local bonds over the next decade—a level required to meet the huge financing requirments of the vast array of needed social programs—raises very serious problems for both State and local governments and the Federal Government. The price for the State and local governments in the use of tax-exempt bonds on such a greatly increased basis under those programs will be in very sizable increases in their interest costs. The price for the Federal Government will be in serious inroads on the equity of its tax system.

Those anxious to preserve the strength of State and local governments should seek to develop new financing techniques that avoid such a high price.

Two possible new financing techniques are offered for consideration: One is the use of local taxable bonds placed directly on the market. The second is a pooling of local obligations through a central non-Federal new financial institution which would raise its funds in the private market on a taxable basis.

Both approaches involve Federal guarantees for the obligations to be issued, and both permit the local governments to receive an interest subsidy to offset their departure from the use of the tax-exemption privilege. But also permit the social projects initiated by the local governments to receive Federal assistance for those projects according to the particular substantive programs affecting them. Finally, both approaches permit that independence of local government which is now obtained through the tax-exemption privilege, but do so without the inefficiency and consequent wastage of funds now associated with that historical solution to one of the problems of our Federal system.

In sum, there are paths to be explored by those who are willing to face this serious problem in a constructive way. That very exploration can in turn open up still other avenues for consideration. The proper Federal role and the proper State and local government role in the necessary Federal-State-local partnership required to meet the fast growing credit demand for new public facilities and social projects can thus be structured in the light of our pressing present needs.

For we are at a crucial crossroads. One way, a blind following of the past, could financially weaken State and local governments and thereby weaken the independence of these governments though outwardly preserving the trappings of independence. The other way, utilizing our knowledge of newly developed credit tools and the new financial institutions to operate them, can preserve and advance that independence.

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[4] One financing technique *not* suggested here is that of Federal tax incentives to private industry. This is not to say that Federal assistance to industry may not be part of the overall program to provide the needed social projects. It is to say that such assistance could far better come through direct Federal outlays, in the form of payments for industry services, or loans or grants. It is believed that such a direct approach rather than "back door" financing through tax incentives, with its inefficiencies and waste and non-disclosure in the Federal Budget, is far more appropriate. Indeed, for many similar reasons the direct approach of the financing techniques suggested in the text is presented as offering advantages over the tax route of tax-exempt obligations. But this is not the occasion to discuss tax incentives at length. Those interested may consider my remarks before the Dallas Chapter of the Financial Executives Institute, Dallas, Texas, *Taxes and the Federal Budget,* February 13, 1968 (Treasury release F–1161).