working paper
department
of economics

Fiscal Disparities in a Metropolitan Area:
The Public Policy Perspective

by
Jerome Rothenberg

Number 60 October 1970

massachusetts
institute of
technology

50 memorial drive
cambridge, mass. 02139
Fiscal Disparities in a Metropolitan Area:
The Public Policy Perspective

by

Jerome Rothenberg

Number 60 October 1970
Fiscal Disparities in a Metropolitan Area:

The Public Policy Perspective

Jerome Rothenberg

Massachusetts Institute of Technology

I. Conditions for an Optimal Federalism

The problem of fiscal disparities within a metropolitan area is different from that of fiscal disparities among urban areas generally, or across state lines, or inter-regionally. The difference is that the disparities across metropolitan areas are primarily descriptive of differences in circumstances among the several communities, but the disparities within metropolitan areas do not simply describe these circumstances, they help determine them by influencing the politico-economic interactions among the communities: they are functional as well as descriptive. Thus, any attempt to spell out the implications of disparities for the proper structure of a federalistic system of government must take these functional consequences on community interaction into account.

We begin by asking how political federalism is related to the existence and magnitude of fiscal disparities and follow this with a consideration of how difficulties associated with such disparities can be ameliorated by changes in the federal structure.

One could argue that a federal form of government represents an attempt to solve some fundamental problems in collective choice and action, problems basic to the very rationalization of collective action on allocative and income distributional grounds. The problems
concern political externalities, efficiency in planning and administration, and ability to achieve desired distributional goals.

Political externalities. Political action involves coercion whenever the collectivity acts in ways which are disapproved of by some of its members, since participation in the action and its impact is obligatory for all (with the authoritative monopolization of force by government the ultimate guarantor of such participation). The possibility of disapproval arises from the fact that action need be decided upon by only a majority of citizens -- rather, a majority of their representatives, which implies actually the possibility of decisive approval by considerably less than a majority of citizens. The ability of majority-represented citizens to impose the costs of disapproved public actions upon minority-represented citizens indicates a potential structural defect in collective action, since if such action is justified because of a private sector deficiency it may simply substitute one form of "unnecessary" real cost situation for another. The ideal case for collectivizing an action is where the entire electorate desires to see realized the same specific outcome, impossible to achieve privately, given the pattern of atomistic, decentralized incentives and the nature of market coordination of individual actions, but which can be brought about by explicitly centralized coordination of decision making and action. Unanimity, with only a substitution of collective for atomistic action, is not, however, to be observed in the real world.

An approximation to unanimity -- and thus an approximation to the generation of zero negative political externalities -- occurs if the population is divided into groups, each of which is as similar in tastes
for public action as possible. But there are many forms of public action -- many functions of government -- and the partitioning of the population that best approximates unanimity in each set differs from function to function. Moreover, they differ significantly with respect to inclusiveness. Some functions involve much less decentralization -- larger and fewer, population sets in the partition -- than others. A federal system can be looked at as a way of meeting this problem of political externalities when the inclusiveness of partitions on different sets of public functions differs notably and dependably. National, state, county, city and town, special district jurisdictions, represent an allocation of political responsibilities that follows a "home rule" philosophy of "bringing government as close to the people as possible" — to minimize the need for coercion and disagreement, to engage individuals in problems they experience directly so that a high degree of responsibility of citizenry to their collective apparatus and of responsiveness of that apparatus to its constituents can be elicited and maintained.

Efficiency in planning and execution. "Home rule" is not sufficient to avoid waste within the public sector. The production function of various public functions displays important scale economies and diseconomies. The cost of both planning and operating public programs is significantly influenced by the size of the jurisdiction that undertakes them. Besides this, political jurisdictions are influenced by both the private and public actions occurring within, and by constituents of, other jurisdictions, without these giving rise to corresponding formal transactions. The existence of these real inter-jurisdictional externalities means that public actions are decided upon and implemented without fully taking into account the impact
of, and on, persons outside the jurisdiction's authority. The composite of public actions taken among a number of such interrelative public jurisdictions will therefore fail to represent an optimal allocation of economic resources just as in general externality-laden actions of decision-makers interacting in the private market sector would fail to do so.

On both grounds, therefore, the assignment of governmental responsibilities among jurisdictions cannot be based solely on "home rule" if efficient resource allocation is to be approximated: it must be modified by scale and inter-jurisdictional considerations. In general, these will recommend larger jurisdictional units at all sub-national levels, but especially at the local levels, where the smaller areas involved are more vulnerable to the exercise of the resource mobilities that accompany and sometimes constitute the externalities.

Achievement of distributional goals. An important set of goals for political action is the modification of the income distribution resulting from the private market sector. Indeed, political scientists, in their emphasis on power and in formulating the political system as a zero-sum game, seem to urge that the primary, even exclusive, function and/or consequence of political action is distributional (rather than allocational). Execution of distributional goals depends very heavily on the constituent composition within each jurisdiction and at each federal level. Highly homogeneous jurisdictions will tend to leave the distributive function unused; the greater the heterogeneity the greater is likely to be the use made of the public sector to achieve distributional objectives. Heterogeneity is a function of the population size and public function distribution among
jurisdictions. It is as possible for a given overall population to be frustrated in achieving distributional goals within a too decentralized public sector, as it is for that population to be frustrated in achieving allocational goals under a too decentralized private sector. Under greater centralization within the public sector the same distributional goals could be both formulated and achieved. Recognition of this means that jurisdictional assignments must be further modified either by enlarging the average size of jurisdictions, or by shifting functions especially rich in distributional impact or strategic for achieving distributional goals, to higher -- and thus more heterogeneous -- jurisdictional levels.

An optimal federal system, designed to accomplish allocational and distributional goals efficiently, must thus compromise a number of factors which are not generally complementary but competitive. There are tradeoffs among the goal dimensions of public performance which must be heeded. An improvement in one aspect will generally worsen performance in another. This intrinsic deficiency in the structure of public sector operation must be kept in mind when addressing the problem of fiscal disparities.

II. Fiscal Disparities and Federalism

"Home rule" is in an important sense the generative principle of the public sector: collectivization to accomplish highly consensual tasks. The additional criteria are qualifications on its implementation. Suppose then that a population group with special tastes and appropriate high incomes decide to create a local community in which an elaborate fine arts museum, a ballet company and a repertory theatre group will be
established and supported by public funds. The per capita income of the community, the housing value per household, and so the property tax base, are substantially higher than the average community nationally, or in the same state or metropolitan area. Moreover, the quality of cultural services provided by the local public sector is far higher than anywhere else. In what way does the fiscal disparity between this community and others constitute a problem?

If we concentrate on the community in question (A) and one of comparable size far away in another state but with average wealth (B), it is not clear that the disparity between them does constitute a problem. The achievement of desirable collectivization by A does not impose a burden on B. Nor does it represent a real opportunity cost on B in that the absence of the formation of A would have permitted an improvement in B's circumstances. This is an example where A's collectivization is essentially irrelevant to B's well-being. The disparity represents a difference, but the difference is not relevant to political action.

A fiscal disparity would seem to constitute a problem warranting public action where one of the following is true: (1) the disparity itself reflects an inter-jurisdictional interaction whereby the poorer jurisdiction has actually been damaged; (2) the disparity results from a spatial distribution of economic activities that frustrates the use of the public sector for carrying out desired income redistribution; (3) the poorer community is poor, and is unable to provide public services at a minimum quality level for its constituents.

A. Interjurisdictional Interaction

There are two types of situations in which interjurisdictional
interaction actually damages a poorer community. The first can be called an existential externality, the second a conditional externality. As to the first, consider the effect on the same communities A and B of a national military draft law under which a national quota, but neither state nor local quota, is set, and where exemptions (or even deferments) are granted to college students and professionals like physicians. Then the interaction lies in the fact that the magnitude of the draft liability for every community depends on the magnitude of this liability for the others. Assuming that the richer community A has a larger percentage of its population made up of the exempted groups than the poorer community B, B will bear a disproportionate share of the burden of the draft: B is damaged by A's more fortunate circumstances. These circumstances refer to the specific federal program we are considering, but they are assumed to be directly related to the overall economic strength of the respective communities.

There are many examples where a federal or state program brings about similar redistributions from poorer to richer communities. In this case it is not the federalistic decentralization of political powers that is responsible for what problem may exist, but the centralization. A case in which it is decentralization that produces the adverse redistribution, and where the resulting problem may be generally more serious, refers to inter-jurisdictional interactions within large metropolitan areas.

What characterizes the relations among the several jurisdictions of a metropolitan area is both daily direct public and private sector interactions among the inhabitants and high locational substitutability
for these activities across borders. There is likely to be asymmetry in the daily reciprocal advantage that inhabitants of different jurisdictions take of one another's public facilities and services, which asymmetry can be only incompletely offset by tax and other charges. This especially describes the relationship between the central city and its suburbs. In this context, it both aggravates and is aggravated by the high locational mobility of resources among the jurisdictions, because it is a component of the resulting self-selected, but publicly enforced, distribution of land uses, densities, socio-economic styles and thus spatial interdependencies that constitute a metropolitan area. The consequence is twofold: (1) problems that are simply a function of the given magnitude and character of resources in the area as a whole will tend to become spatially clustered within certain jurisdictions, notably the central city and a few "poor suburbs"; (2) problems will be created simply because of the distinctive spatial clustering of homogeneities resulting from the distribution of resources and activities. In both cases the situation is worsened because of the spatial interaction: negative externalities are created. Problems like the matching of jobs to workers, the short-and long-run public service needs of the poor, would be manageable if the full resources of the metropolitan area were brought to bear on what are truly problems of the whole metropolitan area. Other problems, like crime, social alienation, segregation-generated resource immobilities and inaccessibilities, would conceivably be significantly less serious without the distinctive spatial-jurisdictional distribution that arises from the jurisdictional interactions. Instead, problems are worsened and the public means available for resolving them are
reduced substantially. There is an artificially created mismatch between the size and character of public needs and the public means of meeting them.

The problem-augmenting spatial distributions of resources and activities are often strongly associated with jurisdictional differences in per capita incomes. These disparities of fiscal capacity are, then, both a cause and a reflection of social damage to poorer communities by richer ones. These are most relevant to public policy.

A "conditional externality" differs from this "existential" form in that the damage is not direct but a question of favorable circumstances lost to the poorer community by the sheer existence of the richer. One example is where, if the richer community did not exist as a separate and unpoachable jurisdiction, the poorer jurisdiction would encompass the resources of the richer. Another is where, if the richer community did not physically exist, some of its resources would have located in the poorer. In both examples -- simple jurisdictional inclusion and alternative physical location of resources -- the poorer jurisdiction would have enhanced its fiscal base. Both situations, moreover, are likely to arise where the communities in question are physically close together. Once again, it is the metropolitan region or region slightly larger that is likely to form the setting for the most significant of these interjurisdictional interactions.

Conditional externalities have to be interpreted carefully. Damage to communities is not the same as damage to individuals. If a rich household voluntarily moves from B to A, this may decrease the fiscal capacity of B; but it simultaneously increases the fiscal capacity of A -- and it
presumably improves the well-being of the rich mover as well. This in itself does not constitute net social damage. Suppose though, that the move changes the household income distribution as a result of the different total community tax revenues, and the overall population prefers the original to the subsequent distribution. This still does not constitute net social loss. Inter-individual distribution has been damaged via community-oriented distributional instruments, but this can be offset by the state - or national-oriented distributional instruments. A problem arises only if there are constraints on the offsetting use of these instruments. And the problem, unlike that arising from existential externalities with its allocational component, is essentially distributional. As such it strongly resembles the second major circumstance in which fiscal disparities constitute a problem warranting remedial action.

B. Local Government and Income Redistribution

This represents a broadening of the concept of "conditional externality". There a change of local jurisdictional boundaries could affect the fiscal base of different jurisdictions and through this, influence income distribution. At most, aggregating the "local" jurisdiction to metropolitan area size was envisioned. Here even wider aggregating is envisioned. Local jurisdictions may differ substantially among one another, not solely because of functional relationships within a metropolitan area, but because of the spatial distribution of economic activities arising from broad locational forces. In general, changing a local boundary slightly or intra-metropolitan location incentive, would not much change the size of these differences. Thus, the explicit externalities of the last section are missing. In its stead is the issue
of the ability of local government to achieve redistributional goals.

The possibility for using local government to achieve income redistributional goals depends on the population and business composition of each jurisdiction, and thus depends on the distribution of economic resources and activities across jurisdictions. We have already noted that internal heterogeneity favors local income redistribution. When the "local" level of government is instituted in terms of towns, cities and even counties, natural location forces may make substantial income redistribution possible within many local jurisdictions, but by no means all. The vagaries of spatial distribution can leave certain communities, metropolitan areas, and even larger regions, with segments of population warranting net government aid but without the complementary internal population composition that could bring it about. This phenomenon is a distinct legacy of the highly decentralized governmental system of the United States. Here too no real problem need exist if the overall federal structure makes provision for achieving the desired redistributions by resort to supplementary measures at higher levels of government. It is in fact the present inadequacy of such measures that makes this hypothetical difficulty a real problem.

C. Minimum Acceptable Services Standards

The two previous grounds concerned an artificial aggravation of problems, both allocational and distributional, due to externalities and a governmental redistributional dysfunction. Neither spoke directly about poverty. Poverty is the heart of the third ground.

The "home rule" criterion says more than that a specialized group should have the right to set up and operate a collective apparatus that
maximally represents them. In order that this be effective, the corollary is that outside groups not have the right to supersede the choices they make for themselves. How much, how, and for what purposes, they wish to tax themselves locally is their own business. On the two grounds dealt with before an unusually high incidence of poverty in a community would be met by changing adjacent jurisdictional boundaries or through intergovernmental grants designed to pass through to needy households. No direct supersession of local collective choices need be envisaged. The present ground changes this.

Some local public services are deemed to be critically important for household and community life: e.g., education, medical services, sanitation. It is quite conceivable that a social consensus now exists which considers that at least a specified minimum level of services like these be provided in every community as a precondition for satisfactory life. It is also conceivable that some communities with very low average income levels find provision of this minimum level too expensive at terms of what must be sacrificed for it, or provide it, but of the high sacrifice called for. In both cases, fiscal disparities within these circumstances designate real social costs. The presumed social consensus which values these merit goods and thereby potentially supersedes local evaluations implies a willingness to act upon the supersession. Action can take two forms: intergovernmental grants to supplement impoverished local resources, or a shift, partial or whole, in the locus of responsibility for providing certain services from the local to higher governmental levels.

To summarize the discussion so far, federalism leads to a process of
forming jurisdictional boundaries, and a broad outline for the distribution of powers to different levels of government, which together make some fiscal disparities reflective—both as causes and symptoms—of social problems. These call for public action. The present essay is not concerned with fiscal disparities generally, but with fiscal disparities within a metropolitan area. The previous discussion should suggest the significance of the metropolitan context. For one thing, the noticeable income stratification which occurs among the jurisdictions of a metropolitan area are likely to be associated with the kind of existential externalities we adduced as a ground for policy concern. Indeed, the metropolitan area is likely to be the most important context within which such externalities occur.

Similarly, the conditional externalities which refer to genuine prospective inter-jurisdictional mobilities, have more relevance to the metropolitan area than to larger spatial contexts. The larger redistributional issues are somewhat less salient here, but are still present. One should not expect to find the very large differences in per capita income among jurisdictions of a single metropolitan area that one encounters across sections of the nation. However, in the former, income stratification tendencies, encouraged by the high inter-jurisdictional interdependence and mobility, do lead to a greater degree of income homogeneity across jurisdictions than one would encounter even where differences in level were greater. Thus, on the one hand, directly redistributional policies are likely to be thwarted within metropolitan areas, but on the other, substantial differences within the metropolitan area in the ability of jurisdictions to provide consensually
minimal service needs are less likely to be encountered. Since we shall argue immediately below that the kinds of policy that are called for depend on the kinds of problem represented by the disparities, it is important that the relative seriousness of these several grounds be clearly determined.

III. Public Policy Issues

The choice of appropriate public policy concerning fiscal disparities depends on the exact significance of the disparities involved in terms of our previous discussion. Policies which serve best the problem of externalities may be inefficient for the problem of general redistribution or minimum service standards, and vice versa. We shall therefore examine the question of policy from the point of view of each of the three sources of difficulty.

A. Externalities

This problem stems from the high degree of interdependence within a metropolitan area, the high substitutability of alternative locations, the high spatial mobility of resources to take advantage of these substitutabilities — all within the context of a local government extremely fragmented on home rule grounds. Public policy is not likely to be able to — or even desire to — mitigate the level of interaction. But it can change the public sector's biased impact on that interaction, and insulate the resulting reverberation of that impact back onto itself.

Insofar as asymmetries in city-suburb interaction result in both a direct and indirect "artificial" weakening of the city's net fiscal ability to meet its needs, there are measures that can be taken to decrease the net monetary disadvantage of such asymmetries. A wider variety of user charges can be imposed by the city government on suburbanite
presence in the central city. Congestion charges on motorists to approximate their marginal social costs (including congestion, pollution, accidents, noise, etc.), while levied on everyone, will have a disproportionate impact on suburbanites. Other charges on an approximately quid pro quo basis, as for cultural and recreational facilities, would similarly help to internalize some of the inter-jurisdictional externalities.

But one should not be deluded into thinking that this can resolve most of the problem. Most local public services intrinsically involve significant externalities that have nothing to do with jurisdictional multiplicity. They would exist under even an all-encompassing metropolitan jurisdiction. They can not be feasibly supplied on a fee-for-service, extreme benefit principle, basis. Yet differences in their provision in the area, and in the tax rates necessary to finance them, abet the income group stratification that aggravates metropolitan social problems. Other tools are necessary.

First is a city tax that will draw levies from the suburbanite presence but with a looser linkage between tax liability and social cost engendered. A sales tax, employment tax, or income tax are examples. These share some of the same advantages as user charges, but possess distinctive disadvantages as well. They tend to discourage location in the city of activities that probably serve, in themselves, to enhance the net fiscal capacity of the city. So their influence in offsetting artificial decentralization forces is to some extent itself offset. Their actual efficiency depends of course on the particular locational elasticities, both in aggregate and in the composition of the activities and population involved. Such magnitudes need to be, but have not yet
been, calculated in order to make fully informed policy decisions.

Another tool is intergovernmental transfer payments. There are many types of intergovernmental grant, and they differ in efficiency for the present task. That task is to offset the overall unattractiveness of the city relative to the suburb as an economic site, stemming from the relatively high tax burden and/or low service quality level of the former. It calls not for an augmentation of specific programs but rather for a general enhancement of fiscal capacity. Thus, the most appropriate form of transfer is either shared taxes or block grants. The former is generally less restrictive than the latter (which may be restricted as to basic function — like health). But it is also potentially less amenable to substantial redistributions among communities, since a natural formula is for the higher level of government to allocate revenues back to the localities on the basis of the relative amounts collected there. As such, it has the positive effects of, say, a city income tax without its negative locational impact. More outright redistribution between suburb and city is likely to be achieved through block grants, since these can allocate negatively in terms of per capita income and positively in terms of various indices of governmental burdens (like the size of the welfare client load).

Shared taxes and block grants do possess an additional drawback in terms of efficiency for the present problem — although possibly an additional strength from the point of view of a wider variety of problems. That is, they are inherently universalistic: they are most unlikely to be restricted to city-suburb transfers. They will typically involve a state donor transmitting to all of its local subdivisions, urban and rural
alike; the federal government transmitting to all states, and through
the agency of the states down to the community level. This means that
the most promising origin of such transfers, the federal government,
is apt to have to provide flows to be shared for state as well as local
purposes and, at the local level, among all or most localities, regardless
of the seriousness among them of the problem being considered. Not
only are the overall effects of universal grants on the present problem
unclear (because of the variety of cross-incentives involved), the amount
used for the program would have to be very large indeed for that part of
it which directly affects the problem at hand to be of adequate magnitude.
The obvious tailoring of such instruments for the present purpose is to
limit the flows, regardless of origin, to metropolitan areas, and adopt
equalization formulae with elements like those mentioned above. Unfortunately
for the present context, this is politically very difficult to do.
Moreover, within the larger context of the problems to which ubiquitous
interjurisdictional flows would be addressed, general, unrestricted
grants may not be the best form they should take.

A third technique depends on the close association between the size
of the overall fiscal burden and the size of burden for specific functions.
In particular the size and expense of the local welfare program may well
reflect the overall fiscal load being carried. The policy suggested is
for the function(s) to be shifted to a higher level of government. Thus,
the state or federal level should assume more or total responsibility for,
say, welfare. This kind of policy is not really arbitrary nor does it
represent special pleading. The vicissitudes of large central cities
with respect to their welfare loads stem largely from inter-regional
migration flows. They represent, indeed, national, not local, events, and are controllable only at the national level. National responsibility for the function not only tends to offset some of the city-suburb imbalance, it probably promises the only efficient means of gaining effective control. Some of the foregoing is true for education as well, except that local responsibility for the shaping -- if not the "quality level" -- of the function to local tastes and circumstances is important to preserve. The resource shift here would consist primarily in state and partly Federal assumption of financial responsibility. These measures do not attack the problem directly but in a strategically indirect fashion. They have the additional advantage of making possible some public coordination or control over deeper locational phenomena that cannot be so controlled on a local level.

The last, and possibly most radical proposal, is to integrate the several local jurisdictions into an all-encompassing metropolitan government. This is the most direct way of dealing with the problem, since it completely internalizes the inter-jurisdictional externalities. As a result locational decisions would no longer be influenced by artificial fiscal segregations and would be left to more "natural" market considerations. Not only would the remaining problems of the metropolitan area be likely to be less serious, there would be by definition no fiscal disparities left.

This approach has two difficulties. Recent events surrounding racial tension particularly have emphasized the importance of political responsiveness to, and responsibility of, local communities on as low as the neighborhood level. Not only local public differences on the city-town level, but a fortiori on the neighborhood level as well, would tend to be severely
suppressed by metropolitanization. This may be a price worth paying, but that decision depends on the efficacy and side effects of other alternatives relative to this.

The second difficulty is the likelihood that metropolitanization may be politically infeasible to bring about. The present political fragmentation serves many strong home rule interests within the population, so metropolitanization is not likely to obtain widespread support among the affected population. To the extent that suburbs must voluntarily vote themselves into a metropolitan government it will probably not be done. To the extent that integration can be imposed by a higher level of government — the state — suburban interests especially are likely to make the necessary political consensus on the state level difficult to achieve.

For both these reasons it is useful to examine a variant of the metropolitanization proposal. It is that an exercise of metropolitan-wide functions be superimposed upon the existing jurisdictions but that they not arrogate power over all local functions. The metropolitan jurisdiction would be a special district, exercising a few special functions, side by side with the present jurisdictions only moderately changed. Collective agreement is indeed possible and fruitful in internalizing externalities among an impacted population. These mostly occur where the resulting allocative gains are great enough to make feasible compensatory payments adequate to offset any resulting income redistributions, and especially when the income redistributions are small enough so as not to have to call forth substantial compensations out of the overall allocative gains. The example of a general agreement to add traffic signals to a particular intersection is the prototype of an
externality situation where consensus is easy to elicit: little or no redistribution is involved; everyone stands to gain directly from the general agreement, without the need to negotiate compensation procedures.

There are some externality components like these within the metropolitan area: some aspects of transportation coordination, water supply, air pollution. For these, metropolitan-wide planning could presumably gain adequate political support. But the problems we earlier referred to stemmed from externalities involving significant asymmetry and therefore whose rectification would involve systematic income redistributions. It is these that are reflected in the jurisdictional fiscal disparities that constitute a social problem. Thus, metropolitan-wide exercise of easily-agreed-upon functions, while productive of allocational gains, will not itself offset the systematic distortions of incentive concerning intra-metropolitan location and its attendant income stratification.

It may, however, have an indirect impact in this direction. To set up an apparatus for making and carrying out metropolitan-wide decisions provides an ongoing agency for considering possible extensions of direction and depth. It provides a forum for generating more complicated bargains among constituent groups than those which it was originally called upon to administer. Thus, relevant metropolitan government may have to come into being gradually, piece by piece, agreement by agreement, function by function: a process of organic growth.

B. Income Redistribution

The problem of optimal inter-jurisdictional structure for purposes of achieving income distribution goals involves some overlap with the preceding, but does in addition possess a distinctness for policy purposes.
The failure here concerns a failure of local governmental action with respect to household income. Consequently, three types of approach would seem to be relevant. The most direct approach consists in a higher level of government assuming responsibility for achieving household income distribution targets. The second, more indirect, consists in the higher government making intergovernmental grants positively weighted toward jurisdictions with low per capita income. The third consists in combining jurisdictions together to attain greater internal heterogeneity and thereby to set the stage for greater local redistribution.

As we mentioned earlier, local redistributive efforts can be substituted for by action on a higher governmental level. While the latter is a substitute for the former, they operate via different instrumentalities. Local redistribution is likely to take the form of services specialized for the poor (except for outright relief grants, which is not the most important part); redistribution at the state level also has this character; but federal action can more easily take the form of direct cash income supplements. In today's context the most direct mechanism is a federal income supplement program of the negative income tax form. This can be made to accomplish a great variety of distributional goals flexibly. Moreover, the federal level is the one at which distributional goals for the population as a whole can be best acted upon without contaminating locational incentives. Thus, a problem of fiscal disparities among jurisdictions can be efficiently resolved by a ubiquitous system of positive and negative grants, not to jurisdictions, but directly to households, thereby
bypassing lower levels of government. In effect, the redistributio
function, employable only imperfectly at lower governmental levels, can, if assumed by the federal government, be exercised much more completely.

The second approach attempts to resolve community fiscal disparities on a community basis. This calls for grants by a higher authority, state or federal, to local jurisdictions. Since the present problem is not in fact a problem of "community poverty" but only of unwanted household poverty, a system where grants to "poor jurisdictions" are larger than grants to "richer jurisdictions" is designed to approximate, or leak down, a relative distribution to poor households at the expense of richer households. The extent to which this may occur varies from community to community. It depends on the existing pattern of public services and transfers and how the local government would respond to a change in the size of its effective fisc. In general, a governmental downflow based on per capita jurisdictional income will only approximately find its way to households in any inter-household pattern formulated at the donor level. Moreover -- and this repeats an earlier assertion -- the program is most likely to have to encompass all jurisdictions within the purview of the donor level, so the percentage of any total grant flow which directly affects the target metropolitan area disparities may not be very high. It would take very large total flows to have significant impact of the sort desired in the present context.

The nature of the grants is another issue. Unlike the case of externalities, where the most effective form of the grant is likely to be unrestricted, there is more room in the present category to envisage
grants restricted as to function or even as to particular mode of operation of the function, since there are specific functions, and particular modes of operation (eligibility, level of benefits, quality of service, etc.), which have special relevance for the achievement of redistributonal goals. Given the existing panoply of local programs, the grants may well be more effective when worked through those programs that most relate to the appropriate types of distributional impact than through the general fiscal ease resulting from unrestricted grants, where much of the impact may be dissipated in a number of programs which are either not salient or outright inconsistent with, the distributional aims of the grants. Thus, the grants should probably be patterned to attempt to elicit an overall local program of the sort that might have emerged if the locality had had considerably greater heterogeneity of constituency. The functions where restricted and conditional (matching) grants might well be given probably include education, welfare and health, and possibly also housing.

The third approach is similar to the structural recommendation made under the last category -- metropolitan government. Here the purpose would be to heterogenize the local population within a single jurisdiction. Since the explicit purpose would be to redistribute well-being, the prediction of unfeasibility is probably even stronger here, since the prospective beneficiaries have little bait with which to bargain. Of course, the same action of metropolitanization would make possible both allocational and distributional gains, and so, hypothetically the gains from the former could be used to create favorable incentives for the latter. But we have already argued that the impact of the externalities within the metropolitan area serve to abet income stratification over space,
so that substantial redistribution is entailed even in the allocational consequences of metropolitanization. Thus, there may not be enough with which to bargain to gain support for such amalgamation. Moreover, the setting up of metropolitan decision-making for certain functions only is likely to have even less success for the present problem than for the externalities problem, since the functions which are likely to command consensual approval are those with only trivial distributional impact.

Thus, even more than in the externalities context metropolitan government would go a long way toward solving the problem if it could be set up by imposition from higher levels of government. But political alignments in the higher levels, especially the states, which alone possess the legal power to bring about the legal amalgamation (except where annexation by mutual agreement is permitted by state constitutions), also reflect the distributional gains inhering in the present fragmentation of government at the local level and are thus unlikely to relinquish them voluntarily.

C. Minimum Service Standards

The problem here is both that minimum levels of some specific public functions may presumably be considered nationally as necessary conditions for satisfactory household welfare, and that some communities within a metropolitan area are too poor either to decide voluntarily to provide it for themselves or provide it only at great sacrifice. Three approaches seem most relevant here, corresponding to the three suggested for the last category. First, and most direct, is to have the level of government at which the supposed consensus about universally necessary minimum standards exists assume responsibility to provide either the whole of the function
or only the prescribed minimum level. The second is for higher jurisdictions to subsidize the local provision of such minima. Third is to change the governmental structure to elicit the desired minima either more dependably or at less sacrifice, by creating special districts responsible for the critical functions.

Shift of function to a higher level is an effective instrument, but it involves more problems in this context than in the previous ones. We have said that provision of a certain minimum level might be deemed universally warranted. Levels above this minimum however, would retain their status as variables appropriate to home rule differences. Thus, a complete shift of the function to higher levels would create genuine controversy as to the most appropriate overall level of provision, and thus political externalities. A partial shift would therefore seem preferred, with the higher government providing the minimum service level and the local government providing anything above this. Some functions are capable of being split in this way without causing a considerable elevation of administrative costs (or decrease in efficiency); but many are not so capable. For the latter, costs could well rise substantially and/or efficiency fall. Indeed, real conflicts might emerge in the provision, if major coordination of effort were not achieved. Such administrative difficulties might be worth the cost if alternative measures were not available. But alternatives exist which merit close consideration. To these we now turn.

The second approach consists of the higher level of government assuming responsibility not for the actual provision of the salient services but only for some or all of their financing. The most appropriate technique
that can be employed to this end is probably a specific or matching grant, in which intergovernmental transfers are made for the express purpose of financing the provision of particular services at particular quality levels. This intergovernmental subsidization avoids the previous problems stemming from an actual operational split between jurisdictions at different levels.

Matching grants attempt to decrease the risk that a complete divorce between financing and administration will lead to operational irresponsibility and waste on the local level. On the other hand, matching grants rarely discriminate donor-recipient shares in terms of the fiscal capacity of the recipients. Such discrimination is useful to prevent these functional grants from having adverse income distributional effects. Richer communities could afford a higher level of service provision than poorer, and could therefore actually receive larger per capita grants than the poorer. To avoid regressiveness the matching grant should have the percentage of local program costs which is provided by the higher jurisdiction decrease by schedule the larger is service level provision. At some high level it should disappear entirely. Another component of the problem is met by a matching grant where the percentage subsidy remains the same over different service levels but increases inversely with the per capita income of the recipient jurisdiction. These two suggest the attractiveness of a combination: the percentage subsidy should be on a sliding scale with respect both to service level provision and recipient income level. This integrates concern about both minimum service level and broader income distributional goals. Moreover, it permits the flexibility which is necessary to be
consistent with home rule differences in tastes and resources. On these grounds, as on the ability to avoid split responsibility for actual service provisions, grants of this sort could well be preferable to a total shift of responsibility for functions.

There is one circumstance under which a total shift seems preferable. This is where the socio-economic conditions under which one particular federalistic assignment of functions was appropriate have changed substantially, warranting a new assignment of some or all functions. Substantial industrialization, or important changes in resource mobility constitute examples. To be relevant to the present category, some of the functions involved would have to be those whose minimum provision is consensually deemed "essential". A case could be made that a shift in the welfare function is desirable. We have already suggested that this could combine both a partial substitution of national for local responsibility and a partial substitution of household cash supplements for income in kind. It is not clear that other current local functions can be so profitably shifted, especially "essential" ones.

A final approach to be considered here is one in which no higher governmental responsibility is taken, but the local jurisdiction providing the essential services is reconstituted to permit more dependable provision of the required minima. This can be brought about by setting up special districts to provide each service. There can be as many different kinds of special district as there are essential services. For each function the special district boundaries are designed to compromise the operational efficiencies connected with scale and the degree of population agglomeration necessary to obtain financing of minimum level provision without hardship.
Attention to either consideration alone would threaten success by raising the cost or failing to provide enough jurisdictional heterogeneity (i.e. fail to decrease relevant fiscal disparities).

The method has been used for a variety of functions, some of them, like education and water, "essential". It has become a very popular method. Within the present context it has, however, certain disadvantages.

Its major use seems to have derived from the need to agglomerate small jurisdictions to achieve scale economies. Thus, it has been associated largely with allocational gains stemming from cost savings (or higher quality level attainments, often in the form of variety and specialization). These gains have generally been available to all the participating communities without notable inequalities. Under these conditions, general agreement is relatively easy to elicit, and the special districts and their programs can be serviceably administered. But the amalgamation envisaged here explicitly is motivated by the desire to achieve distributional, not allocational, goals. There is no reason to suppose that the communities which might still profitably coalesce to capture scale advantages are those that ought to coalesce to solve this problem of fiscal disparities, or even that the functions for which such might be possible are "essential" services.

The upshot is that to form a special district to provide essential services that the richer participating communities could easily do separately, for the benefit of the poorer communities has an entirely different political prognosis. The former would seem to have little or nothing to gain from it. The situation for consensual agreement here is even bleaker than for metropolitan government, since in a multiple function,
general governmental jurisdiction it is possible to elicit approval for programs on one function by bargaining across functions. This opportunity is essentially absent in the special district.

It is not only that political agreement on the formation and operation of these special districts would be difficult to obtain, any success of its kind would entail disadvantages. By creating a set of partially overlapping, partly exclusive amalgamations on a function-by-function basis, the population making decisions on each function would differ from one another. Thus, it would be extremely difficult for the population of any one special district to consider the possibility of making political tradeoffs across functions.

While tradeoffs would conceivably not be entertained for any function below minimum service level provision, provision above these levels is within their purview and are as much subject to local tastes and circumstances as any services with less "essentiality". Thus the need to make rational budgetary allocations involving these special functions is present, but is substantially frustrated by fragmentation into special districts.

The subsidization of poor communities to realize universal provision of minimum essential public services can probably not be efficiently accomplished by accentuating intra-metropolitan redistribution on a narrow functional basis. If the burden of redistribution is to be expressly intra-metropolitan, this seems more feasibly attainable through metropolitanization of general government. Metropolitan general government is a more indirect way of attempting to guarantee minimum essential service levels, but if these service levels are indeed consensually favored
the ample fiscal resources available to metropolitan government should make their provision relatively dependable. There are grounds for believing, however, that, at least as far as this problem category is concerned, the less extreme shifting of financial responsibility to the higher level of government at which the targets might have been formulated is advantageous. If the locus of decision-making is truly at the higher level because the issue is statewide or nationwide, then some operational responsibility should inhere there, especially if this can be done without sacrificing either administrative efficiency or home rule considerations. Grants can accomplish this. Intra-metropolitan redistribution, given inter-metropolitan differences as well as the more overtly exposed character of the redistribution involved, is less likely to be able to do so.

IV. A Strategy for Public Policy

We have argued that each of the three main problems warrants different public policies as most appropriate. This poses a separate problem. Which quantitative mix of problems does the real world actually present? Nothing in what we have so far discussed gives an answer to this question. But it is a question that clearly must be faced. Moreover, it is a question that must be faced in quantitative-empirical terms, not simply hypothetically. This requires special studies of particular cases. In what follows are a few empirical surmises and strategic principles.

Metropolitan areas generally experience much higher per capita income levels than non-metropolitan areas. While considerable fiscal disparities exist within such areas so that large relative differences occur, the absolute levels of achievement among the poorer jurisdictions are not
likely to be low enough to endanger the provision of minimum level vital services within the area. The central city, while the site of an unusually high concentration of poor people, is also likely to have a sizable population of the wealthy. While these wealthy can, it is true, substitute private provision of some services — like schools, health, recreation, etc. — for public, there are other services — like water, sanitation, some health and recreation, etc. — for which private provision would be very costly or actually infeasible. Adequate provision of at least the latter is likely to be provided publicly. The case is somewhat worse for moderate to lower-income "worker's suburbs". These are likely to be more homogeneous. Some inadequacy may genuinely occur. Such specialized communities are not, however, very numerous within metropolitan areas. All in all, the problem of minimum standards may not be as widespread and important as are the other two.

The problem of inter-jurisdictional externalities and its associated geographical income stratification does seem to be of the essence in many metropolitan areas. It is likely to be intimately related too, to the ability of local government to handle redistribution. As a first approximation a complex of these two problems would seem to be the significant dimension in which the existence of fiscal disparities appear. It is to this, therefore, that we shall direct attention concerning public policy.

The chief instruments suggested for inter-jurisdictional externalities are more user charges, intergovernmental grants from richer to poorer jurisdictions, a shift to higher government of especially salient functions, and some form of metropolitan government. Those suggested for the income redistributional inadequacy are an offsetting higher governmental action
directly on the distribution of household income, and some form of metropolitan government. Metropolitan government appears in both lists, probably more effectively for the resolution of externality problems than of household income mal-distribution. We have gauged, however, that the necessary degree of metropolitanization might not be politically forthcoming. Evaluation of the other measures must take this uncertainty into account. One measure whose attractiveness is high regardless of the uncertainty, is direct Federal redistributional grants to households. A negative income tax type of graded income supplements seems most appropriate. In the presence of some metropolitanization it handles more directly and dependably the achievement of household income distributional goals. Indeed, by forming the main line of attack on such goals it frees metropolitan government of the disruptive responsibility for achieving them, and thus makes more possible the very establishment of metropolitan area government. In the absence of metropolitan-wide collective action, it serves to remove from existing local government budgets an element which is especially reflective of, and influential on, the income-locational stratification. As a result, central city and suburban government budget differences become less marked and therefore serve less to distort locational decisions. Thus, the measure helps to internalize the relevant externalities (with moderate effect) as well as to achieve distributional goals (with greatest effect). It is both complementary to metropolitan government and a partial substitute.

Another instrumentality with high attractiveness regardless of the status of metropolitan government is user charges. In its absence, user charges accomplishes some internalization of externalities concerning the asymmetric presence of suburbanites in central cities, thereby adding
to the influence of direct Federal income supplements in this respect.
In its presence, it is not needed with respect to city-suburb relations per se, as much as it is to internalize some of the more general externalities of which the metropolis is replete arising out of the failure of a price system -- public or private -- to confront highly interrelated actors with the true marginal social costs of their actions on the system as a whole. These two opposing circumstances may well differ as to identity of the services which should be charged for, the first concentrating primarily on public services, and in which a suburbanite presence is especially heavy (like express highway use), the second on services and activities that need not even be public, but where, for example, congestive and pollutive configurations emerge (as for example, private incineration). Large overlap is, however, to be expected for the two.

Other measures listed do depend on the status of metropolitan government. Intergovernmental grants on a jurisdictional-recipient basis, and upward jurisdictional shifts of other than the explicit distributional function are chiefly substitutes -- albeit imperfect ones -- for metropolitan government in terms of both externality and distributional resolution. The first is likely to be quite helpful with externality problems, less so with distributional ones, especially in the presence of direct household grants. The second might be useful in externality problems if a function like education were involved, but this aid could be offset by important losses in terms of home rule considerations. As a distributional aid it is distinctly inferior to, and superfluous in the presence of, direct household grants. It takes on significance only where minimum service level issues are important, but even here we have argued that interjurisdictional categorical grants
are to be preferred.

Thus a policy strategy emerges. Attempt to institute a program of direct Federal income supplements to households to accomplish distributional goals. Supplement this with as much metropolitan-wide collective apparatus as possible under this redistributional umbrella, to help internalize the numerous externalities present as well as to aid modestly with collective redistributional efforts. Add further a campaign to impose user charges where beneficiary-impact relationships can be discerned. If instrumentalities for metropolitan-wide collective action are inadequate, concentrate these charges on activities where the inter-jurisdictional aspect of externalities is especially notable; if not, concentrate them solely in terms of the magnitude of the externalities. Finally, with inadequate metropolitan government, institute a set of preponderantly block grants from higher, preferably Federal, to local jurisdictions, in order to offset some of the locational impacts of inter-jurisdictional externalities.

These recommendations are of course subject to modification from the results of special studies to discover the actual strengths and complexities of the several kinds of problem we have argued can be associated with fiscal disparities. That such special studies be carried out is one of the most emphatic—possibly the most emphatic—recommendation of the present essay. Our ignorance on this score is just too great to enable us to ignore it.

This realization leads to the final point. While ostensibly an examination of policy issues connected with fiscal disparities, the present work has turned to a tangent: it has been our conviction that fiscal