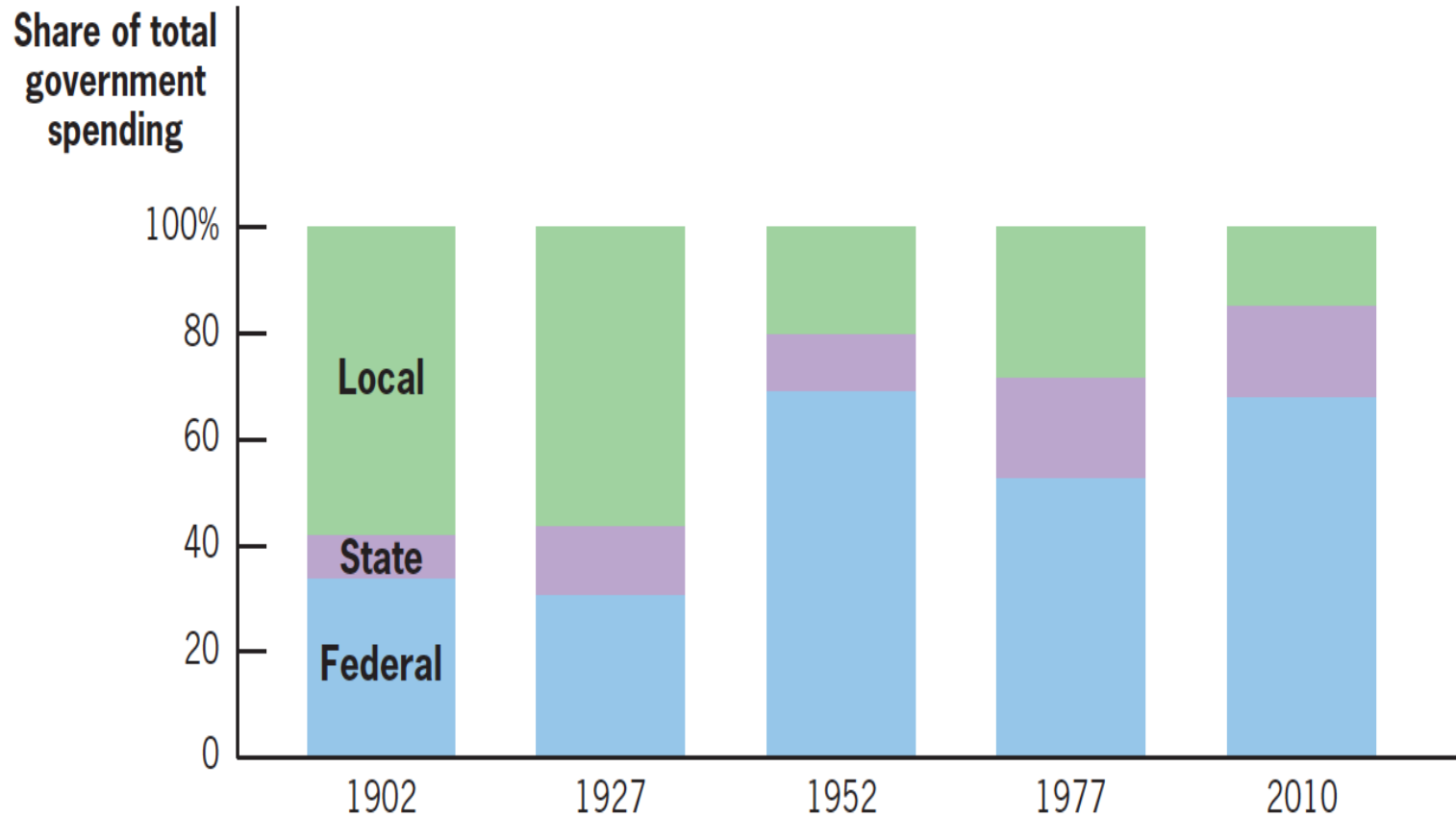


Fiscal Federalism in the United States and Abroad

- The distribution of government spending has changed dramatically over time in the United States.
- Local state and spending have declined considerably.
- Much state and local spending now supported by intergovernmental grants.
 - **Intergovernmental grants:** Payments from one level of government to another.

10.1

State and Local Spending in the United States, 1902–2010



10.1

Spending and Revenue of State and Local Governments

| | Spending | | | Revenue | |
|----------------------|----------|--------|--------------|---------|-------|
| | State | \$/PC | | State | \$/PC |
| Education spending | AK | 3,010 | Income taxes | NY | 2,311 |
| | MA | 2,643 | | MT | 854 |
| | TN | 1,50 | | Many | 0 |
| Health care spending | DC | 10,349 | Sales taxes | DC | 1,847 |
| | LA | 6,759 | | Iowa | 698 |
| | UT | 5,031 | | Many | 0 |

10.1

Fiscal Federalism Abroad

| | Spending (% of all) | Revenue (% of all) |
|---------------|------------------------|-----------------------|
| Greece | 0.0 | 0.8 |
| Portugal | 13.7 | 5.5 |
| France | 20.3 | 12.1 |
| Norway | 33.5 | 11.9 |
| United States | 50.0 | 35.7 |
| Denmark | 63.3 | 24.7 |
| OECD Average | 24.8 | 26.5 |

- Many countries engage in fiscal equalization.
- **Fiscal equalization:** Policies by which the national government distributes grants to subnational governments in an effort to equalize differences in wealth.

EVIDENCE: Evidence for Capitalization from California's Proposition 13

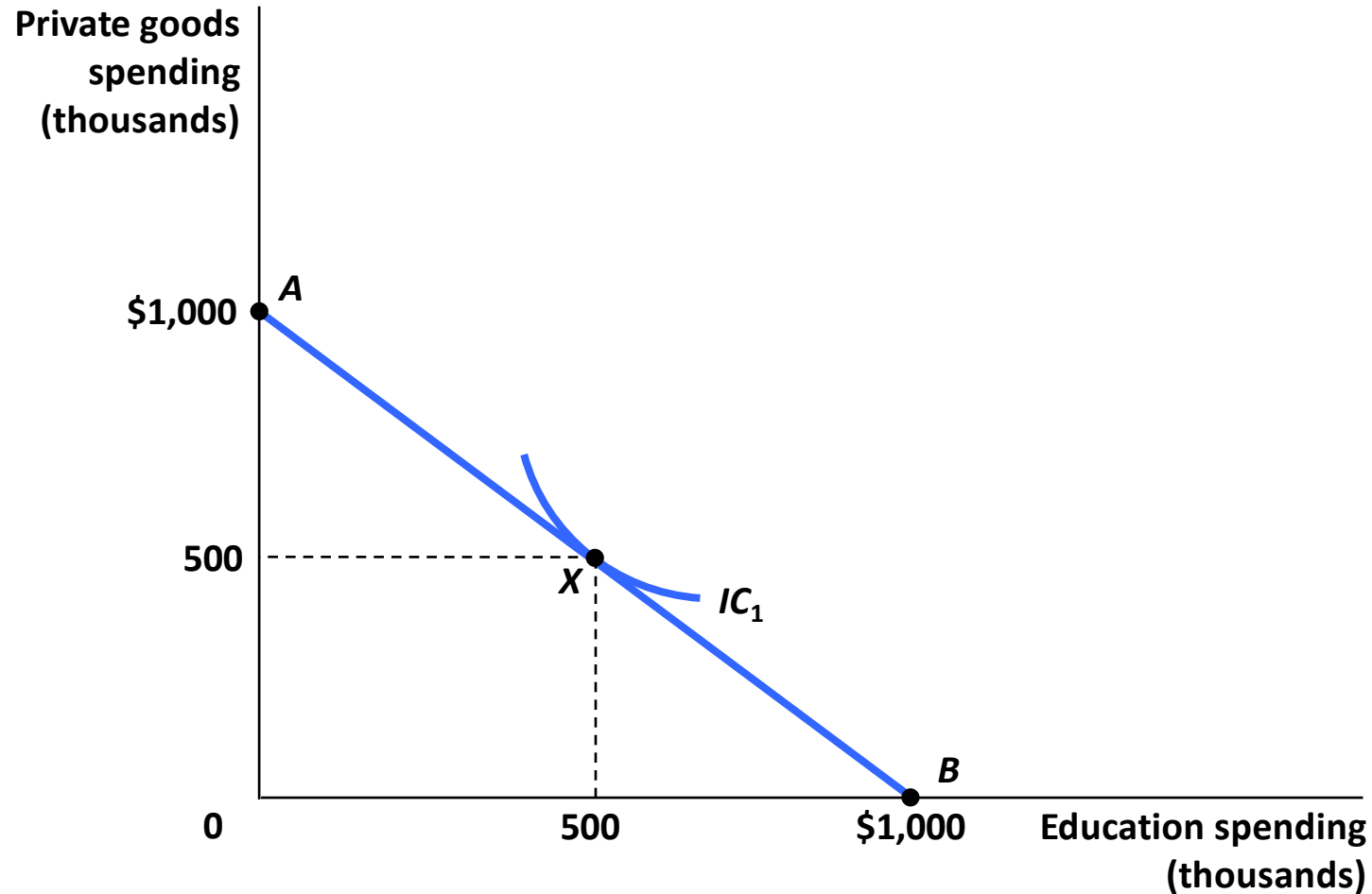
- California's Proposition 13 became law in 1978.
 - Set the maximum amount of any tax on property at 1% of the “full cash value.”
 - Full cash value: Value as of 1976, with annual increases of 2% at most.
- Reduced property taxes immensely in some areas, little change in others.

EVIDENCE: Evidence for Capitalization from California's Proposition 13

- Each \$1 of property tax reduction increased house values by about \$7, about equal to the PDV of a permanent \$1 tax cut.
- In principle, the fall in property taxes would result in a future reduction in public goods and services, which would lower home values.
- The fact that house prices rose by almost the present discounted value of the taxes suggests that Californians did not think that they would lose many valuable public goods and services when taxes fell.

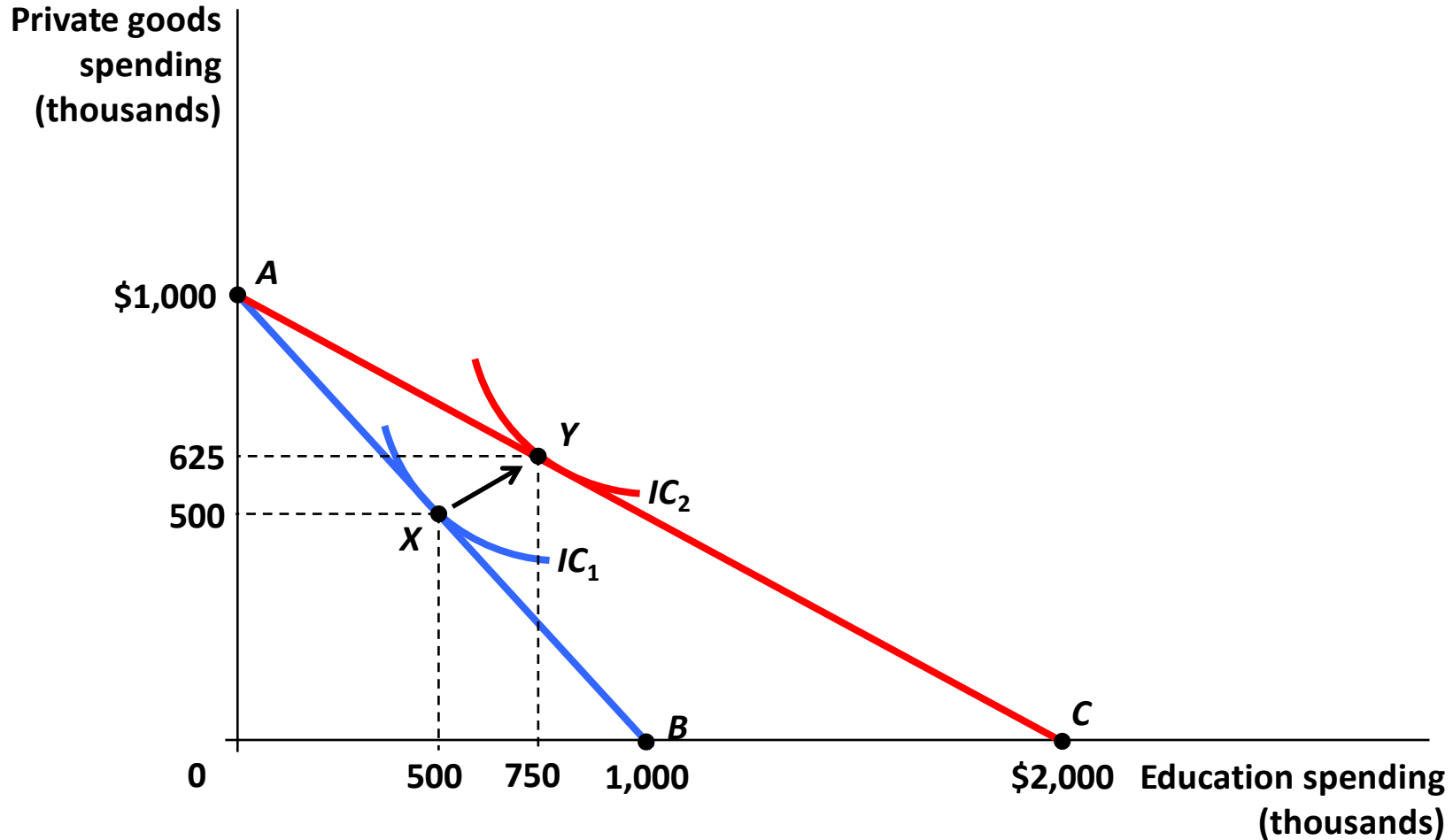
10.3

Tools of Redistribution: Grants



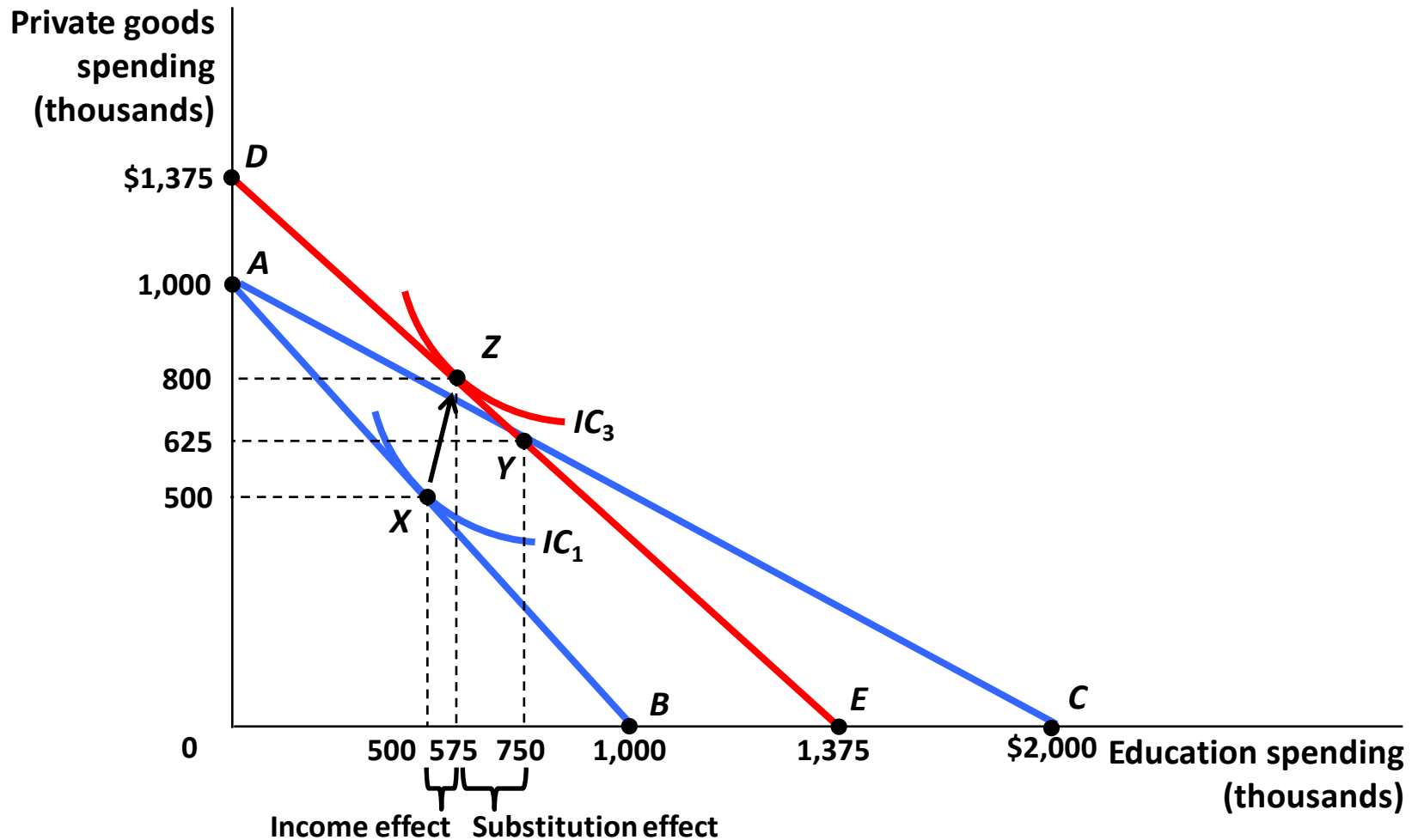
10.3

Matching Grants



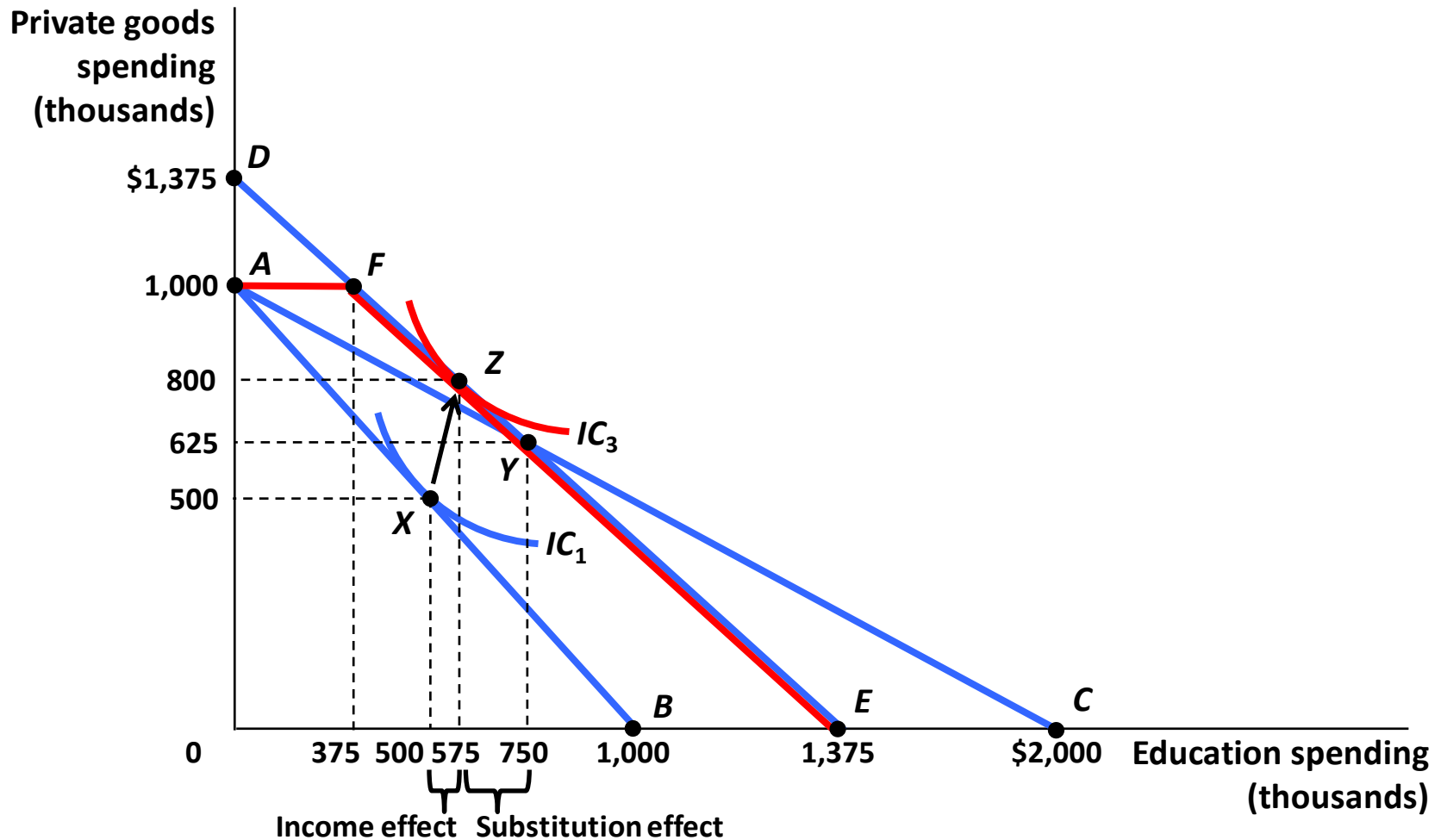
10.3

Block Grant



10.3

Conditional Block Grant



APPLICATION: School Finance Equalization and Property Tax Limitations in California

If residents perceived that property taxes were “too high” in California, why did they wait until 1978 to lower them?

- Proposition 13 actually a response to school finance equalization in California.
- Taxes no longer financed local school spending; just taxes, rather than prices. Tax price became infinite.
- Voters were happy to limit property taxes once those taxes no longer brought them any benefit.