

Causes and Features on the Reform of American Inter-government Transfer Payment*

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Abstract Different from most transfer payment patterns in other countries, American inter-government transfer payment adopts the condition based pattern, mainly concerned with block grants. This article summarizes the background and causes of the reform of block grants and points out its characteristics during the evolvement process in recent decades. The analysis shows that the appearance and stable development of block grants have changed the original transfer pattern of which the categorical grants were dominant, resulting in a distribution phase and consisting of both categorical and block grants with conditional payment and equal scale

Key Words Inter-government transfer payment; Block grants; Categorical grants

1 Introduction

Ever since 1960s, the American federal government has been going through a merge wave by turning the huge and detailed transfer payment system into the block grant pattern. At present, the biggest transfer payment project, including public medical subsidy system, AFDC (replacing TANF since 1996) and educational transfer payment, has moved to block grant pattern instead of the original detailed categorical grants, which proves it to be one of the main forms of transfer payment from the federal government to local governments. Therefore, to know the background and causes of block grant and summarize its characteristics during the evolvement process as well as analyze its effects and features in recent decades could give us beneficial enlightenments.

2 Background and Causes of the Reform

The transfer payment reform of American federal government started from 1960s with the sign of the birth of block grants in America. After the development in 1980s, it reached the pinnacle in late 1990s and has a history of 40 years till now.

The reform background dates back to the crisis between 1929 and 1933 as well as the “Great Society” plan carried out by the federal government. The crisis pushed American federal government to use transfer payment to deal with the intervention of state and local governments, which directly led to the rapid development of federal transfer payment. Indeed, the federal grants became the important financial source of state and local governments after the WWII, especially in the areas of social welfare and public service. However, the grants to state and local governments mainly adopted the categorical form, which resulted in small proportion of general grants. Particularly, after the implementation of the “Great Society” plan in 1960s, the federal government carried out hundreds of aiding plans which aimed at supporting or helping those who were officially defined as “receiver”, including the plan for countryside sewage treatment system as well as those for education of disabled children, covering a wide range of public service areas. There had been totally 530 categorical grant projects till 1970. It was the implementation of those huge and complicated categorical grant plans that activated the birth of block grants. Specifically, there are two important causes.

Firstly, compared with categorical grants, the block grant pattern meets better requirements of federal finance, which can bring higher management efficiency. The categorical grants of the federal government have a huge size which nearly covers everything from the angle of specific targets. For example, there are 50 different grant projects used in health area, 57 in social service area, 32 in ground traffic and 16 in control and elimination of pollution among the total number of block grants (Hamilton,1999) . It means if the urban government wants to carry out a plan for certain economic or social problem, they need to apply for multiple grant projects and hand in multiple applications as well

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as dealing with different grant management communities. The rapid growth of categorical grants directly

leads to repetition of establishing aiding projects, trivial application process, complicated management and low efficiency. The discontent of categorical grants reflects the demand for establishing a granting system, which values more of the application of block grants.

The implementation of block grants can improve efficiency in many aspects. Firstly, we can classify social service with the same type into block grants and deal with the problems of jumbled projects and repeated settings. Meanwhile, through the merge with others, they can share a common principle, that is, block grants are renowned as a tool for dominating state governments' reform and conducting nationally targeted experiments in the way of granting more management mobility to state governments for improving the efficiency of transfer payment. Particularly, in those places which considered federal grants as a failure and deficient efficiency, block grants are known as a tool for dominating state governments' reform and conducting nationally targeted experiments. A typical example was the failure of the urban reconstruction plan in 1974, which brought forth basic principles and thoughts for the establishment of Community Development Block Grants (CDBG). Under CDBG, the federal government tried to use various community development strategic experiments to meet the demand for different areas. Meanwhile, the federal government noticed in the process of grant distribution that local governments knew better of the requirements and existing problems in their own areas. What they needed was an urban comprehensive development plan, but not a single urban reconstruction grant. The decision-makers in the National Congress hoped to establish a wider range of nationally targeted grants in welfare work experiments based on local situations. In addition, some scholars reckoned that the reason for more importance attached on block grants was related to the conserved economic ideology of Reagan government after 1980s. "Neo-Federalism" claimed more roles in state and local governments, the grant form of which manifested in increasing the proportion of block grants with no additional conditions and reducing the proportion of those with strict additional conditions^①.

Another cause mainly lies in the financial crisis of the federal government. At the time of implementing its governmental intervention, the federal government also faced the financial deficit. In other words, the financial crisis of the federal government actually strengthened the reform of transfer payment and the support of giving birth to block grants. Especially in 1980s, the federal financial deficit tripled. Under such circumstance, the grants from the federal government and local governments were naturally considered as the most meaningful projects to minimize financial deficit. It was at that time block grants appeared as an important factor to reduce payouts of the federal government. In the Overall Budget Regulation Act (OBRA) of 1981, the federal government cut down 12% transfer payment by granting more authority and mobility to local state governments. Through the merge of these categorical grants, the federal block grants decreased by the percentage of 10 to 30%. Generally speaking, in the first ten years of "Deficit Reduction Efforts", the federal grants reduced from 89 billion in 1978 to 51 billion in 1988. From the angle of budget, block grants had apparent advantages in minimizing management. While, from the angle of federal government, the combination of reducing budget and granting as well as regulating and almsgiving could win necessary support from local state governments to cut down federal payouts. It was especially true under the circumstance when local state government believed that the reduction was unavoidable. The federal government actually transferred these miserable decisions to local state government, which could in return obtain the dominant decision-making power of block grants at the expense of grant reduction. It has been proved till the present government that the federal financial crisis is an important factor to motivate the federal government and local state governments to interest in block grants.

To the author, if the jumbled and lowly efficient categorical grant is the direct cause of the reform of federal government transfer payment and the birth of block grants, then the further expansion of block grants is closely related to the great pressure of federal financial deficit and the management of budget reduction.

3 Main Features

According to the Evolution of block grants in US, there are following features of the reform:

Firstly, from the perspective of the transfer pattern, we can see that the appearance and stable development of block grants have changed the original transfer pattern of which the categorical grants were dominant, resulting in a distribution phase consisting of both categorical and block grants with

^① Zhong Xiaomin: Theory on Inter-government Financial Transfer Payment. Lixin Accounting Press, P92, 1998.

conditional payment and equal scale. As a new transfer payment pattern, block grants have played important roles in public service with nationally targeted meanings and have received popularity from both the state and local governments. From the angle of government roles, block grants could be considered as a logical stage of the evolvement of federal subsidy system.

From the perspective of federal government, the implementation of block grants has played direct roles in releasing the pressure of financial deficit. Through the reform of public medical subsidy, temporary subsidy to poor families as well as education, housing and urban development, the federal government actually accomplished the purpose of adjustment. Under the condition of better realizing its national goals, the federal government dispersed part of the public service duties to the state and local governments, which helped it to get rid of trivial business. The dispersal effect and the simplified management of block grants not only saved the cost, but also improved management efficiency.

The merge of categorical grants into block grants has brought significant influence to relative social welfare, public service and the aided objects. In particular, the change from AFDC to TANF and the implementation of education subsidy have caused wide concern on the aided objects, such as poor families, single-parent families and foreign immigrations, etc. Furthermore, the pass of 1966 act has brought noticeable changes to poor families. Compared with the unlimited cash subsidy of AFDC, TANF could only provide limited aid and encourage poor people to use self-saving ways to get employment. Therefore, during the implementation process, many state governments reduced the aid range and put emphasis on employment training and opportunity making of poor families. As a result, a heated argument was initiated. Some people even claimed that the Clinton government turned over American social welfare system which had lasted for half a century.

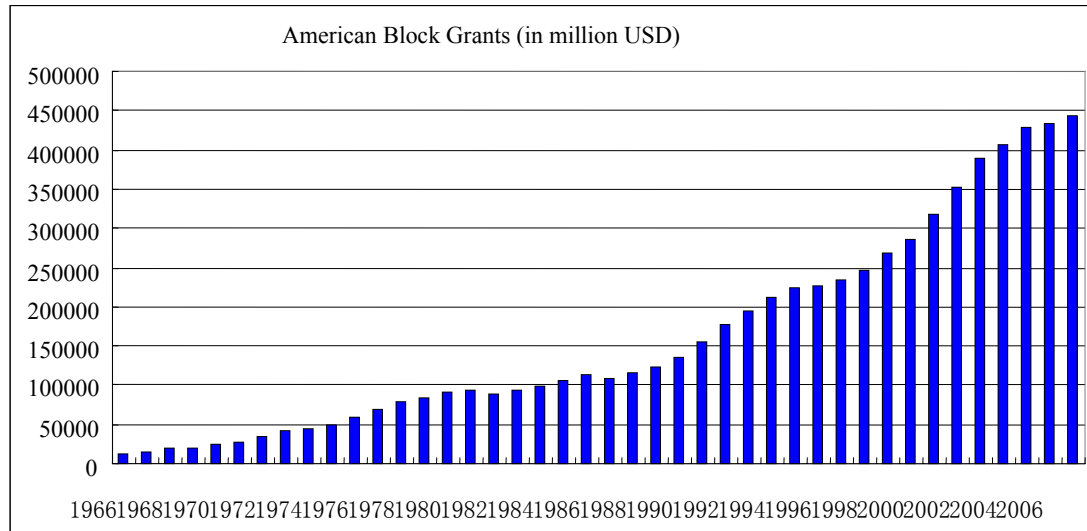


Figure 1 American Annual Block Grants Scale (1966-2007)

Data source: <http://origin.www.gpoaccess.gov/usbudget/fy09/hist.html>

Secondly, the type number and capital scale of block grants have shown the growing trends. The type number increased from 2 in early 1960s to 20 at present. The earliest two block grants appeared in 1966 as the health plan and 1968 as the road safety plan^①. However, according to recent federal budget, we can see that there have been as many as 25 types of block grants. Viewed from the overall scale (shown in the following Chart 1), we can find that the overall scale was heading toward a growing trend. The value increased from 12.89 billion dollars in 1966 to 44.38 billion dollars in 2007. While, viewed from the proportion of block grants to the federal budget payout (shown in the following Chart 2), we can see that the overall scale was also growing. The value increased from 9.7% in 1966 to 16.3% in 2007. Meanwhile, we can also notice several different development stages. From middle 1960s to the year 1980, the value was growing; but from 1980 to 1990, it was decreasing and the proportion dropped

^① Kenneth Finegold, Laura Wherry, Stephanie Schardin , Block Grants Historical Overview and Lessons Learned , April 21, 2004, <http://www.urban.org/url.cfm?ID=310991>.

from 14% to 10.9%. Then in 1990, it went back to growth again. What was more, in 2003 it reached the pinnacle of nearly 18%. In recent years, the proportion mainly kept at 16-17%. Viewed from the proportion of block grants to GDP (shown in the following Chart 2), we can see that the basic trend accounts for the same proportion with block grants in the federal budget. In general, the overall situation is manifested in a growing trend. In 1966, it was 1.6%; while, in 2007, it was 3.2%. From 1966 to early 1980, it was keeping growing. However, there appeared a decrease in 1980s. Later in 1990, it went back to growth again and in 2003 it reached the pinnacle of 3.5%.

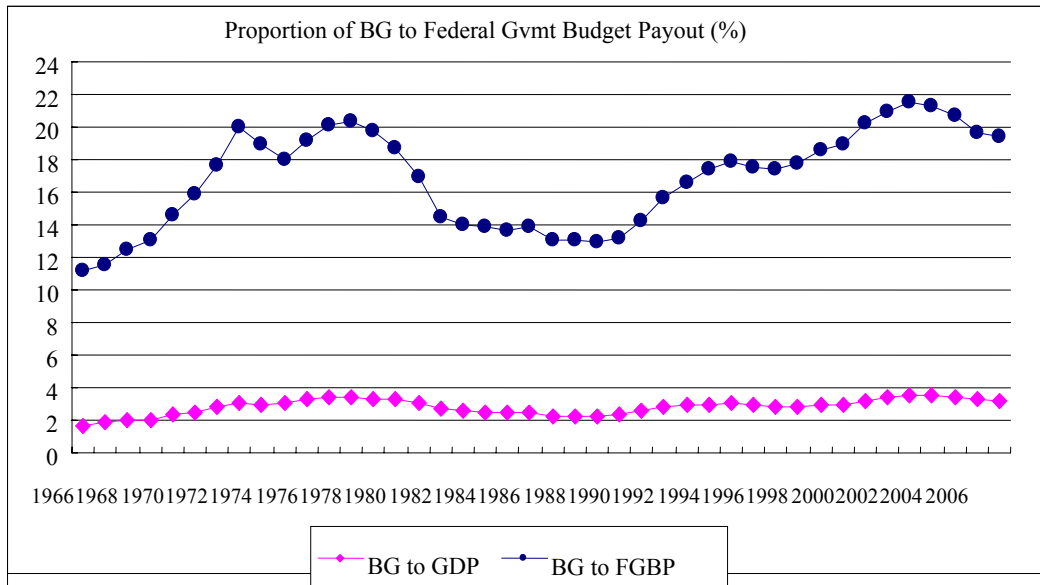


Figure 2 The Proportion of Block Grants to the Federal Government Budget Payout (1966-2007)

Data source: <http://origin.www.gpoaccess.gov/usbudget/fy09/hist.html> The 2007 GDP data comes from: <http://www.imf.org/external/pubs/ft/weo/2008/01/weodata/index.aspx>

Thirdly, viewed from the utility orientation and the changes of the trend, we can find that there existed a dynamic trend. According to the utility, on one hand, America should reinforce the traditional roles of the federal government. What's more, the grants should mainly focus on national public service, especially on social welfare. In recent years, the top two grants have been medical subsidy and education subsidy. The aided areas also covered payouts of food, nutrition, social service and child welfare. On the other, during the above grant projects, we can also notice rapid growth of capital projects, such as housing and urban development, which had become No. 3 of all the grant projects. In all, different block grant projects have different disparities.

4 Conclusion

When conducting an overall view to the reform of American inter-government transfer payment, we can find out an important achievement—the birth of block grants. As a new pattern which is different from traditional transfer payment, its appearance has caused great concern of different governments and academic fields. As the result of the reform, block grants is actually an innovation of transfer payment pattern of the original and traditional patterns, which successfully realizes the organic merge of both the conditional and unconditional grants. The reform has realized the ideology of equalization in public service by adopting the pattern of block grants. From the angle of financial scale, we can see that the federal government has played a major role in public service. The reform initiated by the federal government has actually aroused the activity and initiative of local governments in participating the process of equalizing public service.

The overall scale of categorical grants in China ranks No. 2 in the whole transfer payment system, which is only next to revenue returns. In some years, it even surpasses the revenue returns. However, the problems of usage orientation, whether used in public service or not, the proportion of each region and the surveillance as well as the evaluation system still need further research. Viewed from categorical

grants, we can notice various types and the lack of scientific basis and standards of distribution. Therefore, we'd better tease, adjust and regulate the categorical grants based on duties of governments in new eras and framework requirements by public finance. Meanwhile, we should also clarify the proportion of categorical grants to the whole transfer payout and thus define the utility range and orientation, so as to coordinate the duty division of categorical grants and general transfer payment. Finally, we can also obtain experience of block grants from the areas of education, public medical hygiene and social security and then adopt block grants to replace trivial and complicated categorical grants.

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