Metropolitan Fiscal Disparities

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In 1990 central-city residents had a median income equivalent to about 74 percent of that earned by suburban residents. The central cities have become home to a disproportionate share of social problems: Their infrastructure is arguably in poorer condition, their unemployment rates higher, and their governments more impoverished than those of the suburbs. The evidence suggests that these conditions have remained the same or worsened over the past 20 years. Urban areas are not all the same, and suburbs are not all wealthy, but it would not be at all misleading to say that America's poor places have become poorer over the past two decades.

This article reviews the evidence on the chronic problem of fiscal disparities among city and suburban governments in metropolitan areas. There is a nexus between the fiscal disparities problem and the spatial mismatch problem—the suburbanization of jobs and housing discrimination have led to a surplus of workers relative to jobs in inner-city neighborhoods. One of these problems argues that there are market and discrimination constraints on the ability of the central-city population to realize its full potential in the job market, and that these constraints exacerbate the social problems that plague the city. The other argues that there are market and government policy constraints that limit the ability of urban governments to deliver adequate services at reasonable, competitive tax rates. There are no equilibrating forces in place that would reverse either disparity, and the policy options open to redress the imbalances are very limited.

Fiscal Stress and Fiscal Disparities

City-suburb fiscal disparities are a policy concern that dates back to the 1960s. Campbell and Sacks, writing about metropolitan fiscal disparities in 1967, said (p. 179):

> Of particular importance . . . is the impact on service needs caused by the "sorting out" of population that is taking place within metropolitan areas. The resulting pattern of different kinds of service needs in central cities and their outside areas becomes one of the most crucial metropolitan aspects of the service issue. Of most concern currently is the adequacy of those services for the poor who reside in increasing numbers in central cities.

There was some optimism about policy solutions to this problem 25 years ago, and no shortage of suggested government actions: Federal and State assumption of responsibility for the local government functions that aided the poor, increasing amounts of equalizing State aid, regional tax base sharing, and various forms of metropolitan government.

Observers felt that the Federal Government, the State governments, or even the courts would step in and redress the situation sooner or later.

But that never happened. Twenty-five years after the Campbell and Sacks book was published, a National League of Cities report (Ledebur and Barnes, 1992, p. 4) concluded that:

> Major demographic shifts are also causing increased disparities between cities and suburbs. More than 5.5 million more people lived in poverty at the end of the decade of the 1980s than 10 years previously. Over this period, poverty became increasingly concentrated in the nation's central cities. These trends result in systematic differentials among localities in income, wealth and poverty. These differences create fiscal stress in many central cities. Changes in the intergovernmental system are compounding these disparities and increasing the fiscal squeeze on cities as they attempt to respond to these problems.

This state of affairs should cause those who help frame national urban policy to raise three questions: have the city fiscal condition and city-suburb fiscal disparities changed so little since the 1960s; how have Federal, State, and local government policies affected this situation; and what prospects may the future hold for redressing this imbalance?

The Concept of Disparities

What is fiscal disparity, and can we distinguish the "disparities problem" from the more general fiscal problems facing local governments in metropolitan areas? Suppose metropolitan areas are each fragmented into *n* local governments and, for simplicity, assume that neither tax exporting nor suburban exploitation occur and that none of the jurisdictions overlap.[1] In this case, one might define a resource-requirements gap, d_{ij}, for the i^{th} jurisdiction in the j^{th} metropolitan area as

$$d_{ij} = R_{ij} + F_{ij} + S_{ij} - N_{ij},$$

where: R_{ij} = revenues raised from own sources, from a uniform tax effort, by the i^{th} jurisdiction in the j^{th} metropolitan area,

F_{ij} = Federal aid,

S_{ij} = State aid,

N_{ij} = expenditures required to produce a "standard" package of local public services, and all values are expressed in per capita terms.

Variations across metropolitan areas in d_{ij} for central cities mark the relative fiscal problems of urban areas, whereas variations in d_{ij} across local governments within a metropolitan area point to the fiscal disparities problem. This needs-resources gap is a far cry from the ratio of observed expenditures, taxes, or aid between central cities and suburbs that most studies have used as a measure of disparities.

A resource-requirement gap is more easily conceptualized than measured, because local government tax effort has never been satisfactorily estimated, and the notion of a "standard package" of public services raises the difficult problem of measuring government output. A few studies have attempted to estimate something like this resource-requirements gap. Bradbury et al. (1984) proposed a definition that suggests "fiscal disparities exist when local governments must levy different tax rates to provide the same level of public service" (p. 151). Thus fiscal disparities exist if there are differences between jurisdictions in the cost of providing a given level of services, and this cost is largely due to "environmental factors" outside the control of the local government. The strength of this approach is that it is truer to the idea of measuring differences in the balance between resources and needs. Its weakness is that it requires estimation of the cost of providing a standard package of services although the correct cost determinants have not been identified and consumer preferences not adequately taken into account.[2]

Perhaps for these reasons, most studies have started by examining ex post fiscal disparities—in per capita expenditures, taxes, and aid. There has been no attempt to adjust the initial baseline measure of disparities for differences in need, tax effort, or preference for public versus private goods. The raw disparities in per capita expenditures, taxes, and aid are acknowledged to be due to some combination of choice, environmental factors, resource endowment, and so on. Most of these studies have then turned to an explanation of the city-suburb differences, usually in terms of needs, resources, and environmental differences. Campbell and Sacks (1967); Sacks and Callahan (1973); Advisory Commission on Intergovernmental Relations (1984); and Bahl, Martinez-Vazquez, and Sjoquist (1992) are all in this tradition.

Financial Condition and Fiscal Disparities

The 1970s were a time of great concern about the fiscal and economic problems of cities. New York and several other cities teetered on the edge of bankruptcy; city-suburb fiscal disparities were pronounced and attracted much attention from the courts and the Federal Government; and there was policy action. Direct Federal grants to cities in the form of Comprehensive Employment and Training Act (CETA), Antirecession Fiscal Assistance (ARFA), and Local Public Works were substantial, General Revenue Sharing had a passthrough provision, and there was a push for equity in school financing.

The 1980s brought new economic growth to the country, a new view of cities, and a new set of priorities for city officials. As the economy improved at the end of the 1970s and grew in the 1980s, most policymakers seemed willing to accept the "rising tide" argument—the absence of evidence notwithstanding. The Federal Government decreased its direct support of cities, the courts pulled back on the school financing issue, and city governments became more focussed on financial solvency than on economic viability.

In fact, there were few rumors of imminent default in the 1980s, and many cities were applauded for their remarkable recoveries. A survey of 67 percent of U.S. urban counties showed that the great majority perceived that their financial condition had improved in 1988–89 as compared to the situation 5 years earlier (Downing, 1991). New York City, the prototype of a troubled city in the 1970s, went from "basket case" to success story, even running enough of a surplus by the end of the decade to prepay expenditures for certain local services.

However, all U.S. cities did not fare equally well during this decade. Comparative analyses in the 1970s and 1980s identified a number of Eastern and Midwestern cities as fiscally "distressed." Though these studies were subjective to some extent, they usually came to similar conclusions about the cities in trouble. In the most recent analysis of this type, Ladd and Yinger (1989) analyzed the fiscal and economic performance of large cities through 1986. They concluded that the average improvement in city fiscal health in the 1980s was modest and that the average city was in worse fiscal shape in 1986 than it had been in 1972, with cities in the Northeast and Midwest again heading the list.

One can conclude from this analysis that cities tightened their belts in the 1980s, and that many of them entered the recession in the early 1990s in reasonably good shape compared with earlier decades (Bahl, Martinez-Vazquez, and Sjoquist, 1992). In order to do this, however, some cities may have shifted their resources to protect fund balances and to service debt (Dorsey, 1990). In the course of this fiscal belt tightening, they may have weakened their long-run potential for development, hence Ladd and Yinger's observation about their continued distress.

Cities in the 1990s

As the decade ended, another recession began, revealing many cities as still having fundamental fiscal problems. While there was much variation in the performance of cities in the first part of this decade, some suffered far more than others and have not shown signs of easy recovery. Pagano found a gap of more than 5 percent between expenditure and revenue growth for a sample of 525 cities in 1991, suggesting a widespread drawing on accumulated balances. Other evidence included the aggregate National Income Accounts surplus for the entire local government sector becoming negative and the National Association of Counties reporting that 4 of every 10 populous counties in the Nation faced budgetary shortfalls in 1991. In many cases "service cutbacks" has become a watchword, and the newer issues of AIDS, homelessness, and drug abuse have not received adequate attention. In a few cases, a city's financial condition has approached bankruptcy.

Dearborn (1992) studied the financial conditions of 30 large cities and found substantial deterioration as a result of the 1991 recession. He noted (p. 31) that:

> 1991 saw a sharp reversal of fiscal fortunes of cities. Imbalances became more pervasive and much larger, thereby diminishing reserves, and revenues stopped growing at rates sufficient to maintain basic services. . . . Historically, such patterns have signaled impending financial emergencies.

Dearborn's view is that some cities, such as Detroit and East St. Louis, have run out of financial options and cannot escape their budget crises. Other cities, such as Cleveland, St. Louis, and New Orleans, have very few options for dealing with chronic fiscal problems. In general, the picture he paints is one of cities coping with recession by drawing on accumulated balances, some finding one-time adjustments, while others muddle through with little hope of fundamental improvement. It would be an overstatement to say that all large cities are coming out of the 1991–92 downturn fiscally sound.

A National League of Cities survey (Pagano, 1993) supports Dearborn's conclusions. Its findings may be summarized as follows:

- City fiscal conditions will not improve in 1993, compared with the 1990–92 period. Expenditure growth will exceed revenue growth by a factor of 2.5, and expenditures will grow at less than the rate of inflation; ending balances will drop by nearly 10 percent; and two-thirds of cities reported that they are less able to meet their needs in 1993 than they were in 1992.
- General fund balances appear to be lower in Northeastern cities, central cities, and cities with populations over 300,000.
- More than 70 percent of all cities report that they increased taxes and charges during 1992 and early 1993. Nearly 40 percent of large cities (17 percent of all cities) claimed to have cut services. About 38 percent froze hiring, and 40 percent actually cut employment.

There was also some good news in the League's survey, highlighting the great variation in the financial condition of American cities. Three of every four cities expected positive fund balances at the end of 1993, and two in five identified areas in which productivity improvements have been made. Still, even discounting for the expected bent towards a crisis reply to such a survey, the picture appears to be one of a slow financial recovery for many cities.

Fiscal Disparities

The most recent measurement and analysis of metropolitan fiscal disparities was carried out by Bahl, Martinez-Vazquez, and Sjoquist (1992), who analyzed 1987 data for a sample of 35 large metropolitan statistical areas (MSAs).[3] The results show that the average per capita expenditure disparity between city and suburb in 1987 was 1.51, that is, cities spent $1.51 per capita for every $1.00 spent by suburban governments (Table 1). This disparity was due to the much higher level of noneducation expenditures made by central cities, presumably because of the service “overburden” they faced. Suburban governments, by contrast, maintained an advantage in per capita spending for education. This pattern is not markedly different from that of earlier years. If anything central-city budgets have become even more weighted toward noneducation responsibilities, and there is no evidence that education spending disparities have narrowed in the past decade.

On the financing side, the per capita level of taxes remains about 25 percent higher in cities than in suburbs. However, when this level of taxation is adjusted by family income, the results suggest that the overall level of tax effort is 44 percent higher in central cities than in suburbs. The pattern over the past decade has shown a declining per capita tax revenue advantage for the central city relative to the suburbs, but a growing disparity in tax burden in favor of the suburbs. This situation may be interpreted as a consequence of the slower growth in income in the central city and the pressures on the expenditure budget brought by the increasing concentration of needy families in the central city.[4]

To what extent has the Federal and State aid system been structured to reduce these disparities, or at least to relieve some of the fiscal disadvantages of central cities? In 1977, central cities received $1.69 in State and Federal aid for every $1 received by suburban governments. By 1987, the amount had fallen to $1.53, due to the phasing out of large Federal urban aid programs and to State governments not stepping in to offset the loss.

This description of city and suburban fiscal disparities applies to all regions, although there is some variation in the extent of the disparity. By comparison with the other regions, the Northeastern and Midwestern MSAs spend more than their suburbs for noneducation services and less for education. Their cities receive much more aid relative to their suburbs than do those of the South and West, and have lower per capita taxes relative to their suburbs. The pattern among Southern and Western MSAs seems to be one of less disparity, less Federal and State aid equalization, and higher relative levels of city taxation.

Nathan (1992, chapter 2) reached a similar conclusion about the deteriorating condition of cities relative to their suburbs. His index of hardship—based on unemployment, educational attainment, income level, crowded housing, and poverty—shows that there was continued deterioration in the most distressed cities.

The Role of Policy: 1980s and 1990s

When the financial problems of cities and metropolitan fiscal disparities held the attention of policymakers in the 1970s and early 1980s, there were hopes for reform. In contrast to the present condition of some cities, characterized by Dearborn as “out of options,” there seemed to be an optimism about feasible solutions to the problems. Most of these options centered around ways to spread the wealth: by capturing the suburban tax base to finance urban functions, by receiving a greater share of the State and Federal government budgets to support urban functions, or by reassigning important functions (especially redistributive functions) to the State or Federal government. However, few of the reforms have materialized, leaving economists to speculate as to whether they are still options for U.S. cities.

Federal Aid

One possible way to resolve the fiscal problems of cities and redress disparities in fiscal capacity would be to increase the flow of Federal aid to cities and target the most distressed areas. In fact, this happened for a time with CETA, ARFA, Local Public Works, and General Revenue Sharing, using mandated passthroughs. In 1980, Federal aid to cities accounted for 14.4 percent of Federal expenditures, 26 percent of State and local government revenues, and 3 percent of the gross national product (GNP).

But the large, targeted programs were eventually dropped, and the aggregate flow of Federal aid to State and local governments slowed markedly throughout much of the 1980s. By 1991, Federal aid accounted for less than 2.7 percent of GNP, 20 percent of total State and local government revenues, and 11.5 percent of Federal Government expenditures. The decline in the percentage of Federal expenditures most clearly makes the case that State and local governments have become much less of a Federal priority now than in the pre-1980 period. The result of these declines is that the real per capita amount of Federal aid to State and local governments is about the same in 1993 as it was in 1972.

The targeting of Federal assistance has also changed. There has been no clamor for a return to the urban aid programs of the mid- and late 1970s. In fact, direct Federal aid to local governments has slowed more than Federal aid to State governments since the 1980s. The share of total Federal aid going to local governments has declined from a high of 28 percent in 1978 to about 12 percent in 1991. Federal aid to cities was $63 per capita in 1980 but only $30 per capita in 1993 (Pagano, 1993).

Federal assistance to support infrastructure financing has also been reduced. Mann and Bell (1993) point out that nominal Federal funding of infrastructure grants remained virtually unchanged during much of the 1980s, but the purchasing power of these grants declined by 29 percent.

Another aspect of Federal assistance is the increased costs imposed by the Federal Government on State and local governments. Certainly the tax reform of 1986 increased the “price” of State and local government taxes by disallowing the deductibility of sales taxes and reducing the marginal income tax rate, thereby eroding the value of deductibility. To date, most empirical research points to a small effect for these changes (Courant and Rubinfeld, 1990), but there is some debate about the correctness of this conclusion. Moreover, a proliferation of mandates also increased the costs of local government finances.

State Assistance

Because State governments rely on the most elastic and productive tax bases—those of income and sales—they can generate funds to relieve the fiscal problems of cities. This can be done in two ways: by direct assumption of responsibility for government functions that weigh heavily in urban budgets and by an increased flow of equalizing State aid. State legislatures may also assist cities by authorizing increased taxing powers, making boundary changes possible, and instituting regional taxing districts.

The last two decades have seen an increased role for State governments in the Federal system. The State government share of total State and local government spending rose from 37 percent in 1970 to 40 percent in 1990, and the State government share of taxes rose from 55 percent to 60 percent over this period. However, even though State government budgets increased in the 1980s, grants to local governments declined as a share of total State government expenditures (Table 2), although as a share of total personal income they remained the same. Gold and Ritchie (1993) showed that if welfare and education grants are excluded, State aid to local governments has grown at a slower rate during each successive year in the 1990s. There is also some evidence of reduced targeting. City-suburb fiscal disparities have not been reduced by a greater allocation of State aid to central cities. Bahl, Martinez-Vazquez, and Sjoquist found that the city-suburb ratio of per capita Federal and State aid declined from 1.64 in 1981 to 1.53 in 1987 (Table 1).[5]

Why have State governments not come to the rescue of local governments? A number of reasons might be cited. First, the era since California's Proposition 13[6] has been a time of slow growth in State government taxes—a factor often attributed to the antigovernment bias of voters. The effective rate of total State and local government taxes in 1991 was 10.9 percent, compared with 10.4 percent in 1970. When coupled with reductions in Federal aid and new mandates, States felt that they did not have enough money to fund all activities, and local governments apparently had a low priority. Instead of stepping in to assist local governments, States borrowed a page from John Shannon's "Fend for Yourself Federalism" (see Shannon, 1991) and passed the reductions along to their constituent local governments.

Second, the recession's impact on State budgets was substantial. The resulting revenue shortfalls—particularly those in medical assistance expenditures—forced States to near-record levels of discretionary rate increases in 1991 and 1992 (Mackey, 1992, p. 4). Gold (1992) points out that Medicaid grew rapidly as a component of State budgets because of (a) health cost inflation, (b) increased participation due to mandates, and (c) increased participation due to the recession and the AIDS virus. Not surprisingly, States sought to cut their expenditures by passing the costs on to their local governments.[7]

Third, with a changing mix of population, the dominance of suburban representation in State legislatures became even stronger. The new mix should lead one to expect greater protection of the fiscal position of suburban residents through such measures as less targeting of State aid, resistance to authorizing legislation for various forms of metropolitan governance, and regional taxing measures. Fourth, there may be an anticity bias in some legislation, and sometimes a notion that cities have brought many of their problems on themselves. Even the bailouts of troubled local governments are more likely to take the form of State control than that of State subsidies. A recent NCSL survey (1993) found that 13 States have general statutes to meet local fiscal emergencies, and 6 others passed special acts to bail out local governments during the preceding 3 years. The survey concludes, however, that the most common form of help available to local governments is State technical assistance. Many States provide for the setting up of financial control boards, and four States—Illinois, Michigan, Ohio, and Tennessee—require that such boards be established as a condition of receiving other emergency assistance.

The results of State government fiscal restraint were predictable, and local governments responded by increasing taxes. In fact, local taxes have increased faster than State taxes over most of the past decade. Gold (1993) reports that from 1985 to 1991, local taxes increased by 60 percent and State taxes by only 44 percent—a pattern that holds for 39 of the 50 States. Remarkably, there has been a revival of the property tax in recent years after a long period of decline. The property tax accounted for 18.3 percent of total State and local government taxes in 1990 in comparison with 17.4 percent in 1985.

Metropolitan Government

The expansion of city boundaries to include the wealthier suburbs has always been seen as one solution to the urban fiscal problem. At one time, such a move would have eliminated intergovernmental fiscal disparities and increased the financial capacity of the central cities, but very little consolidation of metropolitan governance occurred in the 1980s. Aside from Jacksonville, Nashville, and Indianapolis, relatively little has happened in the bigger metropolitan areas. Some of the largest cities, such as St. Louis, New York, and Philadelphia, also hold county status but even in those cases few of the wealthier suburbs have been captured in the central county tax base.

Why so little consolidation? The reasons are clear. The more affluent suburban residents are loathe to take on the severe problems confronting cities and are convinced that they can escape these problems through physical separation. Moreover, black leadership in the cities is unwilling to give up its political gains, as metropolitan government would surely require. In short, there is no constituency for metropolitan government, nor is there a good, salable rationale. Metropolitan government and consolidation have usually been sold as methods of increasing technical efficiency in the delivery of public services, that is, as cost-cutting measures. It seems intuitively correct that fragmentation of government leads to duplication of services and diseconomies of scale, but there is little evidence that consolidation captures economies of scale. It is more likely that the chief gain from areawide governance would be equity, that is, the provision of better services to lower income communities. Moreover, the strong sentiment for home rule always weighs heavily against regional governance.

Regional Tax Base Sharing

Cities could strengthen their positions dramatically by taxing the entire region rather than just their own base, and there are a number of ways that this might be done. Commuters could be taxed explicitly or indirectly through local sales and payroll taxes, or tax bases could be shared between cities and suburbs.

One justification for commuter or regional taxes is the so-called exploitation hypothesis. The argument supporting this hypothesis is that central cities are overburdened by the service demands placed on them by suburban residents and are not fully compensated by suburban commuters or by businesses that depend on suburbanites. But research has not clearly shown that such exploitation does exist, and the competitive position of the central city is fragile enough to dissuade local politicians from pushing too far with such taxes.

The Minneapolis/St. Paul property tax base sharing scheme is an example that has been spotlighted perhaps as much as any local tax scheme, but it has not been imitated to any significant extent. Many cities enacted sales and payroll taxes and commuter taxes that served them reasonably well in the 1980s but as Dearborn points out, these taxes made several of the cities susceptible to the recession, and revenues fell precipitously. Moreover, such taxes could make the city less competitive for the economic development it so badly needs. Detroit is a good case in point. Dearborn (p. 3) reports that:

> The city's wage tax revenues declined in 1990 and 1991; the total revenue received in 1991 was less than the amount received in 1987. In the past, rate increases have helped increase revenues, but the city is reluctant to increase the wage tax rate beyond its current 3 percent for fear of accelerating the decline in the number of filers. In recent years, this decline in filers has, in effect, offset growth in the tax base from wage increases.

The Property Tax. During the 1980s, many analysts felt that reliance on the property tax was a major problem facing central cities and a major underlying cause of fiscal disparities. Cities were declining, and the decline was reflected in property values. A substantial part of the cities' economic growth was related to nonprofit activities, and much of the property in central cities was not taxed. There was also a hesitancy to revalue or raise tax rates because of the fragile economic setting in most cities. The result was that city finances became tied to a slow-growing tax base.

Some thought that time would heal this problem, because the property tax was inherently unpopular, sales and income taxes were more elastic and would increasingly dominate the revenue structure, and the future held an increasing fiscal role for State governments. There has, in fact, been a revival of the property tax, and local governments have become increasingly reliant on it in recent years.

The increased dependence on property taxes raises some especially worrisome problems for cities because declining property values will eventually erode the tax base. Petersen and Edwards (1993) showed that the drops can be substantial once assessment lags are eliminated. Their case study of Loudoun County, Virginia, where assessment lags are short, showed that declining commercial-industrial property values led to a 15-percent decline in assessed value between 1990 and 1992, forcing the local government to increase the tax rate significantly and cut expenditures.

Gentrification. Planners and other optimists in the late 1970s saw a rebirth of cities as centers of residential, commercial, and cultural activity. This rebirth was supposed to bring a larger tax base to cities and an influx of citizens who impose low public service costs relative to the taxes they pay. However, gentrification never occurred on a scale that could have offset the declines elsewhere in the city, and much of the new construction was not taxed.

School Finance. Many believed that a major part of the solution to the disparities issue rested with the courts and the school finance cases. The basis of the argument was that, since per-student property values varied widely across school districts, property-tax financing of public schools did not provide access to education of equal quality for all students. To make matters worse, there were States in which State school aid per student was greater for suburban than for central-city districts, but the court actions that would have redressed these imbalances flagged during the 1980s.

Clearly, central cities are at a disadvantage because of the present methods of school finance. Bahl, Martinez-Vazquez, and Sjoquist (1992) showed that expenditures in central-city school districts are about 90 percent of those made in suburban school districts and have remained at that level since the early 1980s (see Table 1). Why does such a disparity exist? A long-held hypothesis points to municipal overburden; that is, because cities have so many other functions to deal with, the amount left over for education is too small. The data in Table 1 seem to support this argument. Central cities spent 1.5 times more per capita on noneducation functions than did suburban governments in 1987, and the gap widened over the preceding decade. The results of a linear regression analysis to explain the variation in per capita education expenditure disparities between cities and suburbs show that disparity is smaller if (a) the average family income level in the suburbs is greater, and (b) the per capita level of Federal and State aid coming to the city is greater.

Conclusions

When policy analysts discuss distressed urban areas, they usually mean the central cities in the Nation's largest metropolitan areas. If one takes this to mean the central cities of the 60 largest MSAs, then only abut 20 percent of the national population is involved. But the problem is one of national dimensions. The well-being of these cities is linked to the economic viability of the most important part of urban America, and these cities are home to a disproportionately large share of America's urban poor. The well-being of these cities is a national issue.

Neither the financial conditions of the most distressed cities nor the fiscal disparity between cities and suburbs improved during the last decade. If anything the situation worsened, because these urban areas missed out on the economic gains of the 1980s. Tax burdens remained higher in the central cities, and per capita expenditures for education were lower. Those cities on the "distressed lists" in the 1970s remain there in the 1990s, and in some cases they appear to be out of options.

Policy at the Federal and State levels has failed the central cities. The Federal Government has pulled back its assistance to local governments, States have not stepped in to fill the gap, and local governments have resorted more heavily to property taxes to make up for the shortfalls. For political and economic reasons, various forms of metropolitan governance have not caught on, nor has a meaningful program of regional tax-base sharing.

There are no automatic forces that will create a new equilibrium, free of disparities. The economic base of central cities has not been revitalized, as some thought it would be. Manufacturing and service jobs alike find the suburbs appealing, and the vision of bargain prices in housing attracting the middle class back to the city never materialized. Suburban governments have not come to regard their vested interest in central cities in a way that would cause them to vote for regional taxes or consolidation. In the absence of a concrete government policy, the fiscal disparities and the weakened financial condition of the distressed cities will likely continue.

The policy options available to deal with the urban fiscal issue are limited. Given the fiscal condition of the Federal Government and the paucity of new urban initiatives, large amounts of new, targeted Federal aid would not appear to be a likely alternative. Instead, responsibility is apt to be shifted to the States in four areas: initiatives to promote regional taxation, increases in targeted assistance to local governments, facilitation of regional governance solutions, and direct assumption of responsibility for certain social services. All of these areas will require increased revenue mobilization by State governments.

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Notes

1. The model is discussed in Bahl, 1970.

2. For a good discussion of the conceptual problems involved in measuring disparities, see Oakland, 1993.

3. The 35 cities were included in the set of 37 cities used in the earlier ACIR (1984) study of fiscal disparities. A common definition of the MSA has been used. Two cities (Paterson, New Jersey, and San Bernardino, California) are omitted because of missing data.

4. Of course, if the central city can export a greater share of its taxes than can the suburban governments, this ratio overstates the relative disadvantage of the central city.

5. State and Federal aid were not separated in this article, so it is not possible to determine how much of the reduction is due to each component.

6. California's Proposition 13 (1978) rolled back property taxes and significantly limited property tax growth.

7. Gold and Ritchie (1993) report that 14 States cut aid to local governments in 1992, while 10 increased aid.

Table 1

Average values of fiscal disparities for a common sample of MSAs

	Fiscal disparities[a]				
Year	1957	1970	1977	1981	1987
Per capita expenditures					
Total	1.32	1.39	1.47	1.40	1.51
Education	0.77	0.86	0.95	0.90	0.91
Noneducation	2.07	2.13	2.04	1.87	2.17
Per capita taxes	1.59	1.42	1.32	1.31	1.25
Taxes as a percent of income[b]	1.54	1.53	1.31	1.18	1.44
Per capita Federal and State aid—total	0.99	1.36	1.69	1.64	1.53
Taxes as a percent of State and Federal aid—Disparity central city/outside central city	1.76	1.20	0.89	0.89	0.91

Notes:

[a]All variables are measured as the ratio of central city (CC) to outside central city (OCC).
[b]An index number computed as the CC/OCC ratio of the following: per capita taxes divided by average family income.
[c]The ratio of per capita taxes to per capita Federal aid.

Table 2

State government grants to local governments

	Real per capita amount[a]	As a percent of total State government expenditures	As a percent of total personal income
1980	$441	36.7 percent	3.7 percent
1985	466	34.7	3.6
1990	536	34.4	3.7

Notes:

[a] Deflated using the consumer price index, 1982–84 = 100.

Sources:

U.S. Department of Commerce, Bureau of the Census, Government Finances, various years; U.S. Department of Commerce, Bureau of the Census, Survey of Current Business, various years.

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