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Volume Title: The Defining Moment: The Great Depression and the American Economy in the Twentieth Century

Volume Author/Editor: Michael D. Bordo, Claudia Goldin and Eugene N. White, editors

Volume Publisher: University of Chicago Press

Volume ISBN: 0-226-06589-8

Volume URL: http://www.nber.org/books/bord98-1

Publication Date: January 1998

Chapter Title: The Impact of the New Deal on American Federalism

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Chapter URL: http://www.nber.org/chapters/c6892

Chapter pages in book: (p. 155 - 180)

5 The Impact of the New Deal on American Federalism

John Joseph Wallis and Wallace E. Oates

5.1 The New Deal and Fiscal Centralization

A cursory look at the course of federal fiscal structure in the United States might suggest that the Great Depression and the New Deal merely accelerated already existing tendencies toward centralization of the public sector. Indeed, at least two of the most insightful political observers of the nineteenth century had forecast just such a trend. Alexis de Tocqueville, writing in the first half of the century, was convinced that democratic "sentiments" exerted a powerful force encouraging the centralization of political power. From his analysis of these "natural tendencies," Tocqueville concludes that "I am of the opinion that, in the democratic ages which are opening upon us . . . centralization will be the natural government" ([1835] 1945, 2:313).

Later in the century, Lord Bryce, although more circumspect about such a broad generalization, reached a similar forecast for the United States. After considering both the "centrifugal" and "centripetal" forces at work in American government, Bryce found that while the centrifugal forces were "likely, as far as we can now see, to prove transitory . . . the centripetal forces are permanent and secular forces, working from age to age" (1901, 2:844). Bryce went on to predict that "the importance of the States will decline as the majesty and authority of the National government increase" ([1888] 1901, 2:844).

From such a perspective, the New Deal might be seen against the backdrop of history as a major event hastening the underlying tendencies toward centralization. But such a view, on closer inspection, is seriously incomplete if not

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The authors would like to thank Robert Margo and Claudia Goldin for helpful comments.

quite misleading. Even a straightforward examination of the standard measures of fiscal centralization (such as the central government share of total public spending or revenues) does not lend unambiguous support to this view. But, as we shall contend, simply looking at such measures of fiscal centralization provides only a superficial view of the evolution of intergovernmental fiscal structure in the United States. The New Deal meant much more than just a movement toward centralization of the public sector. It brought with it some fundamental and dramatic changes in the very character of American federalism, changes that would leave a permanent imprint on the intergovernmental system.

In this paper, we explore the impact of the New Deal on the structure and workings of U.S. fiscal federalism, drawing on an extensive database on intergovernmental fiscal flows. We try to place the New Deal programs in the context of earlier intergovernmental structure and to follow their legacy into the second half of the twentieth century. It is our sense that the New Deal irrevocably altered the evolution of American federalism and did this largely through the widespread introduction of a fiscal instrument that had seen only modest use earlier: intergovernmental grants. The introduction of major grant programs in a form that involved close cooperation between federal and state authorities marked the end of a period in which different levels of government functioned with a high degree of independence. To make use of the terminology of the political scientists, we moved from a system of "coordinate" (or "dual") federalism, in which the various levels of government function in relatively independent spheres, to one of "cooperative" federalism, in which there is much more sharing of fiscal functions and greater interplay among levels of government in the management and funding of public programs.[1] In this way, the New Deal set American federalism on a new course that has brought increasing interaction among levels of government; its legacy is unmistakable.

Much of our work has involved the careful assembling of the relevant data on public expenditures, revenues, and intergovernmental financial flows. This, as we shall see, is a tricky business involving some critical issues of definition, timing, and assignment of spending and revenue data. But when properly assembled and interpreted, the data reveal a striking evolution of the structure of the public finances in the United States over the course of the twentieth century. While the rise to prominence of the central government is a major feature of the fiscal landscape, it does not come primarily at the expense of state and local governments. It is rather part of the growth of the public sector as a whole and the extension of public responsibilities into a number of new functions, including a major role in social insurance and the assistance of low-income households. Many of the programs established in the New Deal and certainly much of the new "spirit" of cooperative federalism that it introduced were not

1. See, e.g., Geoffrey Sawer (1969) and William Stewart (1984) for discussions of these concepts.

temporary in character; they have become essential elements of fiscal federalism in the United States over the remainder of the century. We shall contend that without the New Deal, the course of American federalism would likely have been quite different from that which we have experienced.

5.2 U.S. Fiscal Federalism in the Twentieth Century: An Overview

To put the New Deal programs in perspective, it is helpful at the outset to take a broad look at some summary measures of tendencies in U.S. fiscal federalism over the present century. Table 5.1 reports the shares of public expenditure of federal, state, and local government for selected years. In addition, the table indicates for those years the share of the public sector in GNP and the percentage of revenues of state and local government coming from national intergovernmental grants.

The numbers reveal some important tendencies in U.S. fiscal size and structure. Three such trends are of particular importance for us. First, we see that over this century the government sector as a whole has grown in size relative to the economy. At the turn of the century, public spending accounted for only 8 percent of GNP; this had grown to 38 percent by 1992 (where the considerable difference in revenue and expenditure shares is the result of deficit financ-

Table 5.1 **Government Fiscal Measures, 1902–92**

	Total Expenditures Share by Level (%)			Total Government as a Share of GNP (%)		Federal Grants as a Share of State and Local Revenues (%)
Year	Federal	State	Local	Revenues	Expenditures	
1902	34.16	8.22	57.62	7.84	7.66	0.7
1913	29.89	9.27	60.84	7.53	8.09	0.6
1922	39.39	11.69	48.92	12.58	12.52	2.1
1927	30.57	12.98	56.44	12.85	11.78	1.5
1934	38.69	16.83	44.48	17.36	19.56	13.7
1940	44.91	17.51	37.58	17.86	20.36	8.7
1946	82.43	6.24	11.33	29.51	38.22	5.7
1952	69.10	10.80	20.10	28.51	28.40	9.0
1957	62.11	13.48	24.41	28.64	27.82	9.1
1962	59.98	14.50	25.52	29.19	30.56	12.8
1967	58.76	15.64	25.59	30.81	31.44	16.8
1972	52.41	18.42	29.17	31.49	33.09	19.7
1977	53.04	18.95	28.01	32.82	34.65	24.6
1982	57.45	17.42	25.13	36.11	38.82	19.0
1987	59.33	16.50	24.17	36.97	38.34	15.8
1992	58.33	17.99	23.68	33.94	38.42	21.4

Sources: 1902–82, U.S. Census of Governments (1985); 1987 and 1992, Advisory Council on Intergovernmental Relations (1995).

ing). Second, we find a striking trend in the public sector toward increased fiscal centralization. This trend is evident both in the growing role of the federal government and in the expansion of state governments relative to their local counterparts. In 1902, for instance, the federal share in public expenditure was only 34 percent; local government accounted for the lion's share, 58 percent, of public expenditure in the United States. These shares have changed dramatically over the course of the century, with the federal and state sectors expanding at the expense of local government. By 1992, federal, state and local shares were 58, 18, and 24 percent, respectively. And third, we see an important change in the pattern of finance within the public sector. At the beginning of the century, state and local reliance on federal grants was minuscule; in 1902 less than 1 percent of state and local revenues came from transfers from the federal government. Now, of course, federal intergovernmental transfers are a major feature of the fiscal landscape; in 1992, for example, federal grants accounted for 21.4 percent of gross state-local revenues.

In thinking about the role of the New Deal in this process, it is helpful to look more closely at table 5.1 to see what it suggests about the rate of change of these variables during the 1930s. Certain important fiscal changes stand out. First, although government's share of GNP does increase during the 1930s, this growth is not abnormally rapid. Government's share of GNP slightly less than doubled between 1902 and 1922, and it slightly less than doubled again between 1922 and 1940. Although the comparison can be affected by the choice of years, if we take the period from 1913 to 1927 and compare it to the period from 1927 to 1940, we get roughly the same effect.[2] We see continuing growth in the public sector in the 1930s, but not an accelerating growth. Second, what does stand out about the 1930s is the sharp increase in the national share of government activity. Accepting that 1922 and 1946 (and to a lesser extent 1952) are exceptional postwar years, the national share of public expenditure prior to 1934 was roughly 30 percent, while after 1952 it had risen to about 60 percent. The local share, which was roughly 60 percent before the 1930s, fell to about 25 percent, while the state share rose from approximately 10 percent to 18 percent. Third, we see that in 1934 federal intergovernmental grants suddenly became an important source of revenue for state and local governments. And this new feature of the fiscal system became permanent (with certain wartime exceptions), with federal transfers accounting for a significant share of state-local revenues over the second half of the twentieth century.

This overview of fiscal trends provides some perspective on the historical impact of the New Deal. But before turning to a more detailed examination of the changing fiscal structure of the U.S. federal system, it is important to treat at least briefly some fundamental issues regarding the data. As we shall see,

2. The data for 1922 include relatively large interest expenditures for the federal government. This manifests itself in table 5.1 in the large central share of expenditures in 1922.

the various measures of government growth and structure depend in critical ways on just how the data are assembled and interpreted. Much of our effort in this study has involved a careful analysis of the data themselves and how they are to be understood. We find that it is impossible to get an accurate sense of the significance of the New Deal from these data without addressing some key issues of definition and timing.

5.3 Some Basic Issues Concerning the Fiscal Data

Although some partial information on public finances had been collected since 1850, the first complete "census of governments" in the United States was undertaken in 1902. Subsequent censuses were taken in 1913, 1922, 1932, and 1942, but the coverage of these later censuses varied, leaving some serious gaps in the fiscal data. In 1950, the Congress enacted legislation providing for a quinquennial census in years ending in "2" and "7," but funds were not appropriated for 1952. Since 1957, a census of governments has been conducted every five years.

In spite of these problems with the infrequency and erratic coverage of the census of governments in the first half of the century, it is possible to construct consistent and reliable estimates of national aggregates for national, state, and local fiscal activity for most years. The census of governments regularly updates the twentieth-century figures in volumes entitled *Historical Statistics on Government Finance and Employment.* We begin with these data but examine several important modifications in the way the accounts can be presented.[3]

The issue before us is the structure of American government over the long term, and the selection of the years we chose is critical. Both world wars and the depression left deep footprints in the government data. Wars caused enormous increases in federal government military expenditures, financed in part by taxes and in part by borrowing. Debt repayment lingered in the record for decades. The Great Depression likewise had a major impact, in this instance leading to a sharp reduction in federal government revenues. Unfortunately, two of the benchmark census years, 1932 and 1942, are profoundly affected by depression and war. The use of these years can thus introduce some serious distortion when trying to develop a perspective both on the fiscal trends over the longer period and on the impact of the Great Depression. It is interesting in this respect that by the 1982 census of governments, the authors of the *Historical Statistics* volume chose not to present data for 1932 or 1942; instead they chose the years 1927, 1934, 1940, and 1946. This selection conveniently straddles the Great Contraction and the worst of the war years. We have followed their selection, but it is important to point out that, for some purposes,

3. We will gladly provide interested readers with an appendix, describing the census sources and alternative ways of measuring government activity, that contains detailed tables.

the selection of other years is more appropriate. The patterns and changes in the fiscal aggregates can look quite different depending on the years that are chosen.

A second issue revolves around the categories of federal expenditure that we include when computing the fiscal shares of the different levels of government. The federal government has widely varying and large expenditure commitments to the military and increasingly for interest on its debt. But for the purpose of measuring the relative shares of the federal, state, and local sectors in carrying out domestic programs, it often makes sense to exclude federal spending on national defense and on interest payments from total expenditure and to focus attention on the shares for domestic expenditure programs. This adjustment can also make a major difference in our reading of both the pattern and trends in fiscal centralization in the United States.

A third critical issue concerns a basic ambiguity in the way in which the relative fiscal sizes of the different levels of government are measured. This involves the treatment of intergovernmental grants. Although this issue is of minor importance early in the century, it looms much larger as these grants become a major feature of the intergovernmental fiscal system. The issue concerns the attribution of these grants to the revenues and expenditures of the different levels of governments. Gross revenue and expenditure totals involve substantial double-counting. And the way in which we choose to adjust for this double-counting affects our picture of what happened over the century.

There are basically two choices: to attribute grants to the grantor or to the recipient. On the revenue side, grants are typically credited to the granting government. Under this approach, grants received by state or local governments are deleted from their gross revenues. Thus state and local revenues will include only the funds that they themselves raise through their own taxes, fees, and borrowing. These are often referred to as "own revenues."

Expenditure measures typically attribute grants to the recipient, the level at which they are actually spent. Using this definition, intergovernmental grants are excluded from the expenditures of the granting government and remain in the expenditures of the recipient.[4] Thus, it will be important, as we shall see, whether we measure the fiscal shares of the different levels of government by the monies they raise (revenue shares) or by the monies that they spend (expenditure shares).

The importance of these alternative measures can be seen by looking closely at the measure of expenditure used by the National Income and Product Accounts (NIPA). They report "expenditures from own funds," an expenditure measure that attributes expenditures for grants to the granting government. Figure 5.1 depicts the share of total domestic expenditures at each level of government using the more traditional measure of expenditures, while figure

4. In fact, it would be virtually impossible to exclude certain lump-sum grants to governments from the recipient's expenditures given the fungibility of such monies with own revenues.

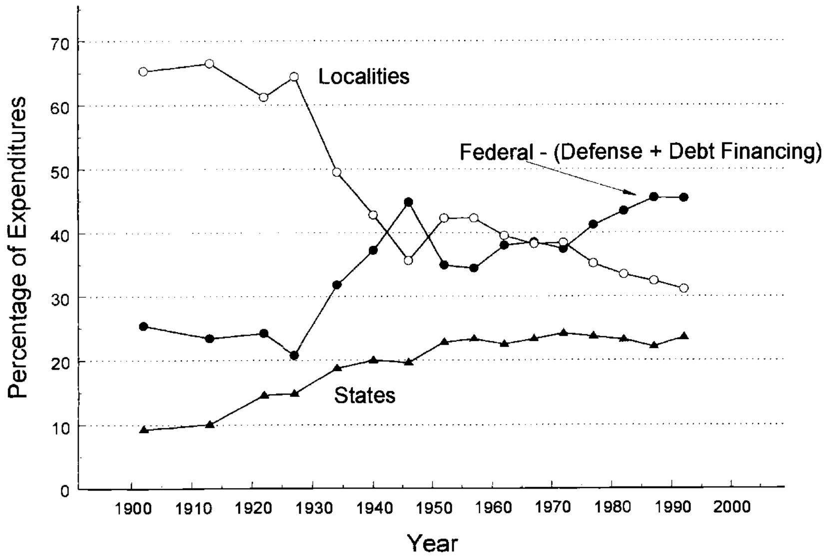

Fig. 5.1 Shares of domestic expenditures: intergovernmental grants attributed to receiving government, 1902–92

Sources: 1902–82, U.S. Census of Governments (1985); 1987 and 1992, Advisory Council on Intergovernmental Relations (1995).

Note: Federal domestic expenditures are total federal expenditures minus expenditures for defense, international relations, and interest on the government debt.

5.2 shows the shares based on the NIPA own-funds definition. Each figure incorporates data for the years listed in table 5.1.[5]

The reversal of the national and local shares in figure 5.1 occurs in the 1940s, while this reversal of national and local shares occurs in the 1930s in figure 5.2. The reason for the difference between the two graphs is straightforward. During the 1930s the central government incurred what for these times were relatively large peacetime deficits, while state and local governments actually ran surpluses. Revenues from new borrowing are not counted as revenues in the traditional measures, nor is retirement of principal included in expenditures. Since a large part of the growth in central fiscal activity in the 1930s took the form of intergovernmental grants, what the expenditures-from-own-funds measure (NIPA)picks up as an increase in the size of the central government during the 1930s is missed by the more traditional measure. And since most of the increased central expenditures were financed through borrowing, revenue measures produce results like those in figure 5.1.

5. As we noted, the selection of years excludes the massive military buildup in World War II. Including the war years would introduce a bulge in the federal share in both figures but would not affect the arguments of the paper.

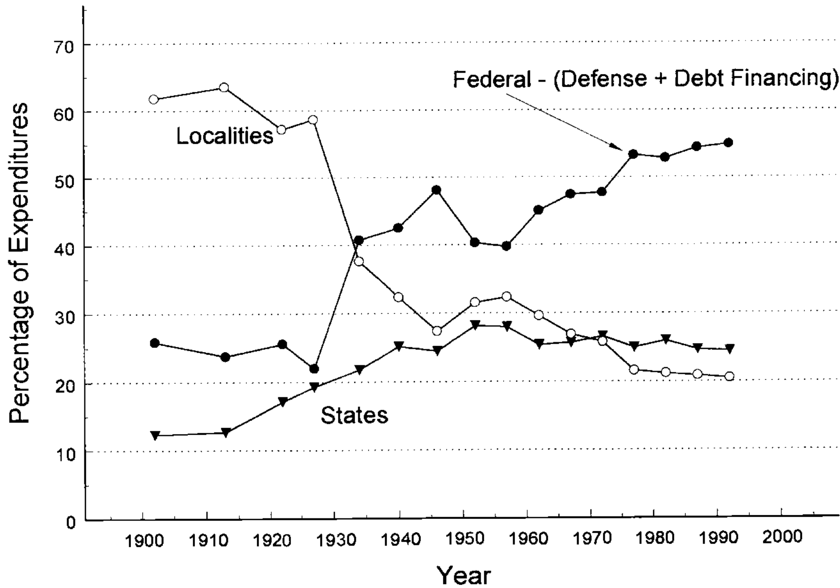

Fig. 5.2 Shares of domestic expenditures: intergovernmental grants attributed to granting government, 1902–92

Sources: 1902–82, U.S. Census of Governments (1985); 1987 and 1992, Advisory Council on Intergovernmental Relations (1995).

Note: Federal domestic expenditures are total federal expenditures minus expenditures for defense, international relations, and interest on the government debt.

Figures 5.1 and 5.2 illustrate the importance of keeping definitions straight. Compare the national and local shares after 1940 in the two figures. In figure 5.1, where grants are credited to the receiving government, local expenditures are roughly equal to national expenditures until the late 1970s. In figure 5.2, where grants are credited to the granting government, the domestic expenditures of the national government not only exceed those of local government by 1940, but the difference continues to grow, with some interruptions, for the remainder of the century. The relative fiscal importance of national and local governments over the last half-century is critically dependent on how one attributes intergovernmental grants.

5.4 U.S. Federal Fiscal Structure in the Early Twentieth Century

As we saw in table 5.1, the fiscal role of the federal government at the turn of the century was tiny. The federal government tended to operate in its own sphere of activity encompassing national defense, foreign relations, the postal service, and various judicial functions. States and their local governments pro-

vided the bulk of public services including public education, police protection, roads and sanitation, public welfare, and health and hospitals. Moreover, the state and local sectors funded their expenditures almost exclusively from their own sources. Federal grants were less than 1 percent of state and local revenues as late as 1913.

There had always been some central aid to state and local governments, beginning with the national assumption of state debts in the 1790s. But intergovernmental grants in existence by 1900 were a small part of the public sector. They included textbooks for the blind (1879), agricultural experiment stations (1887), state soldiers' homes (1888), resident instruction in land grant colleges (1890), and irrigation (1894). These were followed by grants to state marine schools (1911), state and forestry operations (1911), the agricultural extension service (1914), vocational education (1917), and vocational rehabilitation (1920). But these programs were, by 1920, overshadowed in fiscal terms by the highway construction grants begun in 1916. By 1922, $92 million of the $118 million in federal grants, or 78 percent, was for highways. A maternity and infancy health plan was begun in 1921, which gave rise to the famous decision in *Massachusetts v. Mellon* (262 U.S. 447 [1923]) that conditional grants did not impinge on state sovereignty, since states were free to forgo the grants. By 1930 there were 15 federal grant programs to state and local governments in operation, dominated by the highway construction grants. But they were still small in the aggregate; state grants to local governments were about five times as large as federal grants to state and local governments combined.

The federal system in the early part of the century was one in which the central government operated largely independently of the state-local sector. It might be reasonably described, drawing on the political science literature, as "coordinate" or "dual" federalism. Lord Bryce provided a nice metaphor for this view when he described the federal system as "a great factory wherein two sets of machinery are at work, their revolving wheels apparently intermixed, their bands crossing one another, yet each set doing its own work without touching or hampering the other" ([1888] 1901, 325). But the New Deal would change all this.

5.5 The Transformation of the Federal Fiscal System under the New Deal

Keeping track of national, state, and local government programs and activity during the Great Depression is complicated. During the contractionary phase from 1930 to 1932, national government revenues fell from $4,057 million to $1,923 million, while the national debt rose by $3,302 million (numbers are given in table 5.2, panel A). As noted earlier, this dependence on borrowing throughout the 1930s has to be accounted for when we calculate the shares of

Table 5.2 National Government Fiscal Activity, 1929–40 (million current dollars)

A. Revenues, Outlays, and Debt

Year	National Revenues (1)	National Outlays (2)	Gross National Debt (3)	Change in Debt (4)	Outlays – Outlays in 1933 (5)
1929	3,861	3,127	16,931	−673	
1930	4,057	3,320	16,185	−746	
1931	3,115	3,577	16,801	616	
1932	1,923	4,659	19,487	2,686	
1933	1,996	4,598	22,538	3,051	0
1934	3,014	6,644	27,053	4,515	2,046
1935	3,795	6,497	28,700	1,647	1,899
1936	3,997	8,421	33,778	5,078	3,823
1937	4,955	7,733	36,424	2,646	3,135
1938	5,588	6,764	37,164	740	2,166
1939	4,979	8,841	40,439	3,275	4,243
1940	6,879	9,055	42,967	2,528	4,457
Total					21,769

B. Distribution of Grants

Year	Census Grants (6)	Cooperative Grants (7)	Relief (8)	Works (9)	Agriculture (10)	Highway (11)
1932	214	250		108	13	186
1933	190	432	154	196	12	161
1934	1,803	2,857	2,126	356	303	219
1935	2,197	3,649	2,221	459	664	272
1936	1,015	3,969	2,343	618	573	221
1937	818	4,273	2,405	624	636	331
1938	790	3,518	2,047	504	431	217
1939	1,031	4,794	2,671	691	743	185
1940	967	3,922	2,188	521	865	171
Total		27,414	16,155			

Sources: Panel A, U.S. Bureau of the Census (1975); panel B, Wallis (1984).

government activity undertaken at each level. Traditional revenue measures, which exclude borrowed funds, tend to understate the growth of the national government during the New Deal.

Likewise, the procedures used in the census of governments for classifying New Deal programs are misleading. These procedures label as grant programs those that make "indirect expenditures" in contrast to programs involving "direct expenditures." But even this classification was not applied entirely consis-

tently over the decade. As we will discuss in more detail shortly, expenditures in the earliest New Deal programs were heavily weighted toward relief programs, particularly the Federal Emergency Relief Administration (FERA). After 1935 FERA was replaced by a combination of the Works Progress (later Projects) Administration (WPA), the categorical relief programs, and the unemployment insurance program created by the Social Security Act. Funds expended under the WPA were, technically, national government direct expenditures (not grants) because the WPA "employed" its relief recipients directly. Moreover, since WPA projects were typically for construction of various types (e.g., schools, highways, and parks), WPA expenditures were not classified by the census as relief or public assistance expenditures; instead, they were assigned to other functional categories, primarily natural resources.[6]

Panel B offers an alternative measure of grant activity and the functional distribution of these grants. Column (6) provides the census total for national government grants by fiscal year. Column (7) gives the total of national expenditures in programs "administered cooperatively with states." The remaining columns give grants in cooperative programs by major function.

Keeping in mind that fiscal 1933 ended on 30 June 1933, national government outlays in 1933 were primarily the result of the Hoover administration.[7] Column (5) of table 5.2 gives the difference in national government outlays in each of the New Deal years compared with fiscal 1933. The total increase in national government outlays over 1933 levels was $21,769 million (in current dollars). Of that increase, $16,155 million went for grants in relief programs, 75 percent of the total. Total expenditures in cooperatively administered programs rose by $27,414 million. This total was larger than the rise in total expenditures. It indicates how important cooperative programs had become to the national government, which actually reduced the "noncooperative" part of its activities after 1933.

Some programs were more cooperative than others. Of the four major groups shown in table 5.2, both relief and highways consisted primarily of programs that were jointly funded but that were administered by the state or local government, even the WPA with its odd accounting.[8] Agricultural price supports and other programs initiated under the Agricultural Adjustment Act (AAA) of 1933 were funded entirely by the national government and rarely involved the financial participation of state and local governments. But the AAA programs were often administered locally by county extension agents. For example, although crop allocations were determined nationally, within local areas the awarding of contracts was done by extension agents and commit-

6. These issues are discussed in detail in Wallis (1984) and in U.S. Bureau of the Census (1955, 5–7).

7. A small amount of New Deal grants were made in May and June 1933, particularly for relief under FERA.

8. There were exceptions. The Civilian Conservation Corps was a relief program run entirely by the national government.

tees of local farmers. Finally, public works programs involved a mix of national, state, and local arrangements. At one end were purely national projects under the Public Works Administration and at the other the direct grants made to local governments for public housing.

The New Deal programs with the largest effect on state and local governments were the relief programs. This was not only the result of the large amount of funds expended for relief but also because work relief programs like the WPA made a significant contribution to a number of state and local functions through construction activity: education, highways, parks, and natural resources. Understanding the relief programs is central to understanding intergovernmental relations during the 1930s. These programs had both a major economic and a psychological impact. In fiscal 1934, the national government made over $2 billion in grants to state and local governments for relief, which in turn made more than $2 billion in relief grants to needy individuals and families. In 1933, $2 billion was 4 percent of GNP. Imagine what the effect would be today if the national government announced it would pass out $240 billion (4 percent of 1996 GNP) in relief to needy individuals, who need only apply to their local (typically county) relief office to see whether they qualified. And this in the depths of the nation's greatest depression.

Whereas granting $2 billion a year for relief was an unprecedented act of government largesse, it also created the possibility of unprecedented political patronage for the politicians in control of the money. The administration of public relief had always been intertwined with the issue of graft.[9] Professional social workers were themselves deeply disturbed by the "politics" of relief. This partially explains the existence of two major professional organizations, the more prestigious of which had a membership of *private* sector social workers. When FDR appointed Harry Hopkins to head FERA in May 1933, it was not at all clear what the organization of relief would look like in coming years (see Brown 1940).

The FERA legislation made it clear that FERA was to restrict itself to making grants to state governments. Half of the original $500 million appropriation was to be allocated among the states on the basis of matching grants. But the other half of the appropriation was to be allocated at the discretion of the relief administrator on the basis of need. The discretionary grants posed a problem for Hopkins: if he gave larger grants to states that spent less of their own (or local) funds, then states had an incentive to reduce their contributions. But the discretion allowed to him by Congress enabled him also to do the opposite, to reduce grants to states that made smaller contributions. The threat, and in a

9. As Howard put it, "So accustomed have the American people become to the infiltration of venal politics in many areas of public service, that doubt is frequently expressed whether public relief and politics can ever be divorced completely enough to assure decent care to those who are really in need and to prevent dissipation of resources among political favorites. As a result, there has been a great reluctance by many persons to expand relief programs lest they serve only to extend spheres of influence of corrupt political practices" ([1943] 1973, 49).

few cases the reality, that Hopkins would reduce national grants encouraged states to spend more of their own funds. State and local expenditures for relief expanded markedly after 1933. In extreme cases, the FERA legislation gave Hopkins the authority to "federalize" relief and take over the administration of relief in a state. This occurred seven times.[10]

State governors, glad to get the national grants, were not happy to have Hopkins announce that grants would be reduced if the state government did not come up with a larger relief appropriation. State officials expressed their displeasure actively. Governor Davey of Ohio actually had an arrest warrant sworn out for Hopkins after he had charged Davey with using relief for political purposes.

The original FERA appropriation had been $500 million for two years, and FERA was in charge of the nation's entire relief effort. By the end of 1933, however, the funds were running low. Congress continued to appropriate funds for FERA on an emergency basis. FERA made roughly $2 billion a year in grants between May 1933 and August 1935.[11] After the initial matching grants were exhausted, all further grants were discretionary. The grants were conditional, and FERA promulgated an extensive set of regulations covering how relief programs were to be administered. Hopkins was able to enforce several simple and important regulations; for example, all relief funds had to be spent through public agencies. But FERA's ability to affect personnel policies and recipient selection criteria was limited. As Williams (1939) noted, the ability to enforce these policies was much greater in states where the national contribution was larger.[12]

Like many New Deal programs, FERA was an emergency program, intended to pass with time. Although FERA was given additional funds several times, Roosevelt and Hopkins were working on a more permanent solution to the relief problem. The Committee on Economic Security (CES), chaired by Frances Perkins, the secretary of labor, and of which Hopkins was member, began drafting a plan for an Economic Security Act (ESA) that would ultimately create the social security system. In his state of the union address in January 1935, Roosevelt announced that the national government "must and will quit this business of relief" and sent the committee report to Congress. A strong case can be made that the Social Security Act was the most important legislation not only of the decade but of the century.

As it emerged from Congress, the act created three basic welfare programs. First, it introduced what we now call social security: old-age insurance (OAI, now OASDI) was a nationally administered program of old-age insurance.

10. The logic of how Hopkins could use discretionary grants to pry more funds out of state governments is developed in Wallis (1991).

11. The $2 billion a year figure includes the amount spent by the Civil Works Administration in the winter of 1933.

12. For a discussion of the rules and regulations, and their enforceability, see Williams (1939) and Wallis (1981).

Second, the act established a program of unemployment insurance (UI). UI was funded through a 3 percent payroll tax, 2.9 percent of payrolls to be automatically credited to state UI trust funds in any state with an approved UI program. States were given wide latitude in setting up their programs. The third set of programs was categorical assistance: old-age assistance (OAA), aid to the blind, and aid to dependent children (ADC, the forerunner of aid to families with dependent children [AFDC]). Categorical programs were to be administered by the states and funded through automatic matching grants. National grants were open ended, but grants per relief case were capped. Although the independent Social Security Board created by the act had to approve each state's categorical program, there were strict limits on the board's ability to interfere with the actual administration of the programs. For example, the board was explicitly forbidden from withholding grants because of personnel decisions at the state level.

The legislation submitted to Congress proposed each of these three programs but would have administered them in far different ways. The OAI program was national, but the categorical programs would have been administered by FERA, or a FERA-like agency, using discretionary rather than matching grants. The discretionary grants did not make it through the first committee hearings in the House. It was the strong state control over the categorical relief and UI programs, along with the fact that general relief (i.e., care of the needy who did not fit into one of the other categories) was left completely to state and local governments, that caused such a strong outcry among the social work professionals. "Returning relief to the states" was something they vigorously opposed.[13] Hopkins, who had gone to the professional social workers' meetings in 1934 as a hero, came to the meetings in 1935 as a goat. Social work professionals opposed returning relief to the states because they saw that as returning control to the politicians. Hopkins, in fact, had been trained as a social worker and had done everything he could to improve relief administration in his tenure as the FERA administrator.

Understanding why the social security system was set up as it was is critical to understanding the New Deal's legacy and position in the political and economic history of the century. With the addition of Medicaid and Medicare in 1967, the social security system remains in place in an expanded form. In 1992, expenditures for social insurance, unemployment insurance, and public assistance were one-quarter of total government expenditures (at all levels). Medicaid was set up as a categorical assistance program, with matching grants and state administration. Medicare was set up like old-age insurance, with national administration and standards.

13. This story is told in a number of places. Brock (1988) and Bremer (1984) are very good on the details. The notion that returning relief to the states was an attempt to return control of the relief programs to local economic elites is elaborated in Piven and Cloward (1971) and Block et al. (1987). For a reformulation of this hypothesis based on the interest of Southern legislators, see Alston and Ferrie (1985).

There are several places we can turn to find evidence on the motives of Congress and the president in 1935. One is to note the incredible opportunities that relief (and indeed all of the New Deal programs) offered for political patronage. Johnson and Libecap (1994) have pointed out that the New Deal is the one significant period since the Pendleton Act created the civil service system that the portion of national government employees who were not classified as civil service actually rose. Roosevelt and Hopkins asked Congress to put the relief program's administrative employees under the civil service, but Congress refused until 1939. The attraction of patronage was simply too strong for the new Democratic majorities who had been out of power for decades. Johnson and Libecap (1994) argue that civil service reform was adopted in the first place because the cost of monitoring patronage employees had grown larger than the benefits from hiring them. Roosevelt and Hopkins learned this quickly during the New Deal. By 1935 Governor Langer of North Dakota was in jail for manipulating relief programs. While FDR stood to gain the most from thankful relief recipients, he also stood to lose the most when political abuses of relief were uncovered. Hopkins's attempts to eliminate political manipulation through rules and regulations, control over hiring, or civil service status for administrative employees was contingent on his ability to coerce states through discretionary grants. But this was effectively countered by congressional policies that located administrative control, particularly over personnel policies, at the state level.

Additional evidence can be found in the sister legislation to the ESA. FDR submitted another piece of relief legislation to Congress in the winter of 1935, the Emergency Relief Appropriations Act (ERAA) of 1935. Under the ERAA, Congress appropriated $4.8 billion for relief of the unemployed, to be spent through agencies that the president was authorized to create via executive order through methods not specified in the act. If the ESA was an attempt by Congress to secure state administrative control over the permanent part of the welfare system, the ERAA was an admission by Congress that for the remainder of the depression, the president would be allowed to exercise his discretionary powers to deal with the unemployment problem. Under the act's authority, Roosevelt created the WPA, the Rural Electrification Administration, and several smaller agencies.

Because of the unusual way it was created, the WPA could have been administered in any way that Roosevelt wanted. As we noted earlier, the fact that the WPA was a national program created some problems in the way its expenditures were treated, both in terms of grants and functions. In practice, however, and with a few important exceptions, the WPA was administered cooperatively with the states and came to be more cooperative as time went on. The two administrative mechanisms by which this cooperation was insured were project sponsorship and recipient selection.

Hopkins became the WPA's administrator, and he continued the FERA policy of encouraging state and local government participation in the program.

Although regulations regarding project sponsorship went through several changes after 1935, the basic structure was always the same. WPA projects were initiated by a sponsoring government, which could be local, state, or national, forwarded to the state WPA office for recommendation for approval, and then forwarded to the Washington office for final authorization. Between July 1935 and August 1937, 96 percent of all WPA projects were sponsored by local or state governments.[14] "Federal projects" were sponsored by the WPA itself, the most prominent of which were in the arts. After 1939 all federal projects were eliminated, and Congress insisted on a strict proportion of matching funds from sponsors of at least 25 percent of project cost.[15] The growing importance of sponsor contributions and the initiation of most WPA projects by local and state governments ensured a great deal of cooperation within the program.

Cooperation was even more pronounced in the selection of WPA recipients. Although the WPA was free to hire its own administrative employees and supervisory employees (though sponsors also had some say in supervisory employees), in order for an unemployed worker to obtain WPA employment he first had to be certified as needy by the local relief agency. The WPA could not go out and provide relief to members of the community that the local government had not certified. Unlike the sponsorship policy, the WPA ultimately wished to control the certification process. Congress would not authorize money for the WPA to do this, however.[16]

Project sponsorship and recipient selection demonstrate the extent to which intergovernmental cooperation pervaded the nominally "national" administration of the WPA. They also show that two forces were at work to produce such cooperation during the New Deal. First, the WPA itself sought cooperation from state and local governments to enable it to do its job more effectively. State and local governments were important sources of funds, administrative talent, and local expertise. By utilizing state and local cooperation, the WPA strengthened those governments even as it expanded its own role. Second, cooperation often gave state and local governments a measure of control over national administration. As such, cooperative policies were often mandated (or protected) by Congress even in the face of presidential opposition, as was the case with recipient certification. State and local independence was extremely valuable to congressmen.

In summary, the New Deal initiated a pattern of cooperative intergovernmental activity with a distinctive bent: fiscal centralization and administrative decentralization. Not only were New Deal programs administered at the state

14. These figures are taken from Howard ([1943] 1973, 145). Howard provides an excellent history of the WPA.

15. Sponsor contributions to total WPA project costs were 10 percent in 1936, 14.7 percent in 1937, 21.4 percent in 1938, 19.3 percent in 1939, and 26 percent in 1940 (Howard [1943] 1973, 149).

16. The certification issue was quite complicated, see Howard ([1943] 1973, 356–79).

level, but state governments in particular possessed real decision-making power. It was states, more than welfare recipients, who were entitled to categorical relief under the Social Security Act. State and local governments had their say in what projects the WPA would undertake, and by the end of the decade, the WPA could not build projects without state and local sponsorship and a 25 percent contribution. There were important differences between programs. The agricultural programs were cooperative, but state and local governments never became directly involved in their operation. The Civilian Conservation Corps, in contrast, was a national program, as were many public works projects. On the other hand, the WPA was a very important way that the national government financed education, water and sewers, parks, and highways. And the old highway programs continued their cooperative structure from 1916.

5.6 The New Deal and the States

One other point needs to be addressed. Although the national government increased its share of total government activity during the New Deal, by no measure was the state share of government activity reduced. The state share of total government revenues from own sources rose from 16.4 percent in 1927, to 21.7 percent in 1934, to 28.2 percent in 1940. The state share of total government expenditures rose from 13 percent in 1927, to 16.8 percent in 1934, to 17.5 percent in 1940 (the own-expenditure shares are even higher). All of the growth in the national shares come at the expense of local governments. The reason for this is clear. National grants were given primarily to the states. Most of these grants offered incentives for state governments to increase their own spending. Whether these incentives were explicit, like the strict matching provisions in the categorical relief programs, or implicit as in Hopkins's use of FERA grants, they were real. Wallis (1984) found that, in the late 1930s, every dollar of national grants increased state expenditures from own revenues by $0.31. At the same time combined state and national grants actually reduced local government expenditures. Similar effects are found in a longer analysis of grants and state and local fiscal activity (Wallis 1997).

Where did these state revenues come from? In 1930, 16 states had individual income taxes, 17 had corporate income taxes, and none had a general sales tax. During the 1930s, 16 states added personal income taxes, 15 added corporate income taxes, and 24 created a sales tax. It is impossible to say that these taxes were the result of New Deal grant programs because the majority of new state taxes were put in place in 1933 at the same time that the New Deal grant programs were just getting under way. But one of the legacies of the New Deal was a much stronger state government sector with new and more flexible tax instruments.

Another way to see this is in the structure of state government programs. In 1932, before FERA, only 7 states had spent money for unemployment relief

and had state relief agencies. By the end of 1933, all 48 states did. By 1939 all the states had approved UI schemes, and almost all had approved OAA, ADC, and aid to the blind programs in place. State highway boards were the result of the 1916 grants, but they too were still in place.

The New Deal's predilection for decentralized administration resulted in stronger and larger state governments.

5.7 Federal Fiscal Evolution Subsequent to the New Deal

The New Deal created a new and major role for the federal government in domestic policy and set intergovernmental fiscal relations in the United States on a new course of joint responsibility for both the funding and the management of public programs. Since World War II, this course has involved not only the expansion and extension of certain New Deal programs but also the creation of new forms of cooperative enterprise, some of which have flourished and others of which have proved much less successful. In this section, we explore briefly this later experience in order to provide some sense of what the New Deal might have bequeathed to us.

The war, of course, had a dramatic impact on American government. During the fighting, the role of the national government expanded enormously, and both state and local government shrank in absolute terms. The war, and its employment policies, eliminated the need for the New Deal's emergency relief programs, and the permanent programs became much less important.

During the 1950s the national government returned to more active support for highway construction through the National Defense Highway Act in 1956, which began the interstate system. From 1952 to 1962, national grants for highway construction rose from $415 million to $2,748 million. The interstate system was built cooperatively, with states supervising the planning and construction in conjunction with national guidelines and direction. National grants for public welfare and education rose slowly in the 1950s, roughly in line with the overall rise of government. Social security, of course, became steadily larger as a growing portion of the labor force became eligible for benefits upon retirement.

In the 1960s, the federal government took the design and operation of grant programs a step further. Responding to a sense of frustration with the lack of progress toward the attainment of certain basic social goals, including, for example, the elimination of poverty and the renewal of decaying center cities, it undertook the "War on Poverty." The federal government enacted a whole series of grant programs that bypassed the states and, in some instances, even locally elected officials in an attempt to get resources "where they were needed." Individually tailored project grants went to cities or special groups on the basis of approved grant applications.

The emphasis of part of the War on Poverty was to encourage "maximum feasible participation." It was intended to be empowering, and to the extent

possible, the national government officials in charge of the programs were interested not in increasing the power and size of state and local welfare systems but rather in putting resources and control directly into the hands of the recipients. This brought federal officials into much closer contact with the "projects" that the money was intended to fund. Inevitably, it provided the national government much greater control over the specific ways in which grant funds were used. This was particularly true where project grants were specifically intended to circumvent the established political hierarchy. In this sense, these programs went well beyond the New Deal framework.

At the same time, the national government redoubled its efforts to support the traditional, New Deal social welfare system. This effort continued well into the Nixon years. Part of this came through an expansion of the old programs: AFDC rolls exploded, supplemental social security expanded benefits for the aged, blind, and disabled. Part of this took the form of new programs: food stamps, Medicare, and Medicaid. Nixon's Family Assistance Plan, which would have guaranteed all families with dependent children a minimum yearly income, was the most far-reaching proposal. It was not enacted by Congress, but it would have been a major change from the New Deal structure. At the same time the national government significantly increased its support for state and local government in a range of functions, including education, water and sewage, and natural resources.

Not surprisingly (in retrospect at least), central intervention into the federal system eventually produced a strong reaction. Beginning in the late 1970s and especially under the new Republican administration in the 1980s, moves were initiated to cut back on the grant programs. This was typically described as an attempt to "return control of the programs to the states." Narrowly targeted conditional grant programs were replaced by broad block grants that stipulated only very general areas in which the funds were to be used. Discretion in the employment of grant funds was supposed to devolve back to the states. Moreover, these reforms were accompanied by a general reduction in the relative size of grants; in the 1980s, federal grants as a fraction of state-local revenues and spending declined.

In the early 1970s, another new intergovernmental structure was put in place. The Nixon administration and the U.S. Congress introduced a quite different sort of intergovernmental fiscal innovation: "general revenue sharing." Under this program, the federal government distributed funds by formula to state and local governments with fairly loose restrictions on their use only at the local level. The objective of this program was to channel funds from the highly income-elastic federal revenue system to the state-local sector, where expenditure "needs" were growing rapidly—to link the most growth-responsive revenue sources to the most rapidly expanding forms of public expenditure. Revenue sharing, however, was a short-lived program. With the enormous federal deficits in the 1980s, the central government, not the states and localities, was under fiscal duress. The states (with their healthy treasuries)

were eliminated from the program in 1980, and with the support of the Reagan administration, the entire program was allowed to expire in 1986.

This is curious in one respect. Revenue sharing in one form or another has played a major role in many federal countries such as Canada and Australia from very early days. Central government in these countries has been a basic and regular source of revenues for provincial, state, and local governments. But in the United States such programs have little history. The New Deal, while introducing large-scale transfers of funds from the center, certainly did not do so in a "hands-off" fashion. In this sense, revenue sharing was not, in any direct way, a child of the Great Depression.

With the massive deficits at the central level, there has been considerable pressure to cut back on federal transfers to the states and localities. But this has not proved easy. Intergovernmental transfers are now a basic part of the fiscal system; in 1992, for example, federal grants still accounted for over 20 percent of state and local revenues.

Most recently, attention has focused on nonfiscal forms of central intervention, namely, various regulatory measures that impose responsibilities on state and local governments but do not provide the financial assistance to carry them out. These "unfunded mandates" have been the source of much contention and debate. This is a complicated issue. Many mandates seem well founded in terms of needed regulation of externalities (e.g., various environmental statutes). But others have a much less clear rationale.

5.8 Intergovernmental Grants and the Growth of the Public Sector

It is clear, in retrospect, that New Deal programs were the vehicle for the widespread introduction and heavy reliance on intergovernmental grants in the U.S. federal fiscal system. In addition to transforming the character of American fiscal federalism, there is evidence in the public finance literature that this reliance on grants has made a significant contribution to the growth of the public sector in the American economy.

As we have seen, many New Deal programs had as their very purpose the expansion of public sector spending to create new jobs and income and to stabilize the economy. To this end, they employed matching provisions that induced additional spending on the part of recipient state governments. The purpose of these grants was emphatically *not* to supplant spending by state and local governments with federal funds. From this perspective, New Deal grant programs clearly played an important role in extending the size and scope of the public sector as a whole.

But at the end of this century, we find that federal grants (and state grants to local governments as well) no longer have economic expansion as their objective. Later grant programs are quite diverse in both form and purpose; most of them have aimed to provide fiscal support either for specific types of projects (e.g., highways, treatment plants, and retraining programs) or for income main-

tenance. In the case of revenue sharing, the basic objective was simply to provide general purpose funds to state and local governments. Some of these programs contained matching requirements for recipients, but many others have not.

Basic economic theory has some interesting implications for the effects of intergovernmental grants on the size of the public sector. In the case of most nonmatching grants, for example, grant funds simply augment the resources of the recipient community; they have no direct price effects, only income effects.[17] At the theoretical level, it has been established that such nonmatching grants have allocative and distributive effects that are no different than if these funds were distributed in a particular lump-sum fashion to the residents of the recipient jurisdiction (Bradford and Oates 1971). In short, nonmatching intergovernmental grants are formally equivalent in *all* their effects to a federal tax cut directly to the individuals in a community. In both cases, the measures simply increase the disposable income available to the community; in one case, the increased dollars show up in the public treasury and in the other in the pockets of the individual residents. But this should, in principle, make no difference to the ultimate outcome. This suggests that such grants should have no expansionary effect on the public sector. If the federal government collects taxes and redistributes the funds in the form of nonmatching grants to states and localities, then the negative income effects associated with the increased federal taxes should offset (approximately) the positive income effects from the rise in grants. Matching grants, in contrast, will have a net expansionary impact on the public sector since the income effect of the grants is accompanied by a price effect (i.e., the grant effectively reduces the price of services that the recipient purchases). But nonmatching grants should, in principle, be nonexpansionary.

What is of interest here is the pervasive empirical finding in the public finance literature that this prediction of the theory is flat-out wrong. Dozens of studies of the stimulative effects of intergovernmental grants find that not only matching grants but nonmatching grants as well have a highly stimulative effect on the spending of recipients (Gramlich 1977; Hines and Thaler 1995). Based on income effects alone, we might expect nonmatching grants to state and local governments to induce an increase in spending on the order of 10 to 15 cents on the dollar (representing roughly their share in national income). But econometric (and other types of survey) studies find time and again that such nonmatching grants result in much more in the way of additional state-

17. This proposition is true so long as the grant does not exceed the amount in total that the recipient would have spent on the program in the absence of the grant. Moreover, even matching grants will have only income effects if they are closed ended (i.e., if matching stops at some prescribed level of spending by the recipient) and if recipients' spending exceeds the sum for which they are eligible at the margin for additional matching funds. Many matching grant programs in the United States are, in fact, closed ended in structure, and the evidence suggests that in the great majority of the cases recipients spend more than the sum necessary to exhaust their grant entitlements. On the analytics of intergovernmental grants, see Oates (1972, chap. 3).

local spending, typically on the order of about 50 cents per dollar of additional grant monies. This anomaly has become known in the public finance literature as the "flypaper effect" (i.e., "money sticks where it hits"). And there is now a body of papers that seek in various ways to reconcile these empirical findings with the basic theory of intergovernmental grants (see Hines and Thaler 1995).

For our purposes, this large empirical literature is important because it suggests that intergovernmental grant programs have had a substantial expansionary impact on the level of overall public spending. Additional federal taxes that are transformed into intergovernmental grants (even nonmatching grants) do not constitute a wash in terms of their impact on the size of the public sector. It is not easy to estimate the magnitude of this effect, as this would, in principle, require a detailed model of how these grants have influenced the growth over time of the state and local sectors. But we offer a simpler and admittedly crude calculation. If we take at face value the econometric estimates of the stimulative impact of intergovernmental grants, a conservative estimate would be that an average dollar of grants results in about 50 cents of additional state-local expenditure and about 50 cents of tax relief at the state and local levels.[18] Since federal grants account for about 20 percent of state-local revenues, this would suggest that state-local budgets in the aggregate are (at a minimum) about 10 percent larger than in the absence of these grant revenues. We do not intend this crude result to be taken as a serious effort to measure the effect of federal grants on state and local governments. Our intent is rather to make the point that in the process of transforming the character of the American federal system into one of cooperative federalism through an extensive reliance on intergovernmental grants, the New Deal also introduced a fiscal structure more conducive to overall growth of the public sector.

5.9 The Legacy of the New Deal

The New Deal has had a lasting impact on the structure of American government. As we have seen, one dimension of this impact was to create a much larger and more active role for the central government. To get a clearer sense of this, we see in figure 5.1 the federal, state, and local shares in public expenditure excluding national defense and interest on the federal debt. This measure of fiscal shares (as discussed earlier) avoids some of the disruptions produced by wartime and required payments on the national debt. It is interesting to subject these data to some simple econometric scrutiny. It is clear from looking at the graph that the federal share has risen over the course of the century. In fact, if we simply regress the federal share of public expenditures on time, we find that

18. See Hines and Thaler (1995) for a summary of these estimates. This is a conservative estimate in that it is based on the measured impact of nonmatching grants; the stimulative effect of matching grant programs is substantially higher.

$$(1) \quad \text{Federal share} = \underset{(6.3)}{-4.5} + \underset{(6.8)}{.0025}\text{Time}, \quad R^2 = .75,$$

where the numbers in parentheses are absolute values of the t-statistics. The estimated equation confirms the growth in the federal share and indicates that on average the federal share of the public budget has increased over this period by about 1 percentage point every four years.

But the path of the federal share in figure 5.1 also suggests that its growth has not been very regular. In fact, a large increase in this share seems to have occurred during the New Deal years. To account for this, we introduce into the equation a dummy variable that takes on a value of zero for those years before 1934 and a value of one for 1934 and thereafter. This yields

$$(2) \quad \text{Federal share} = \underset{(2.7)}{-2.5} + \underset{(2.9)}{.0014}\text{Time} + \underset{(2.9)}{.091}\text{Dummy}, \quad R^2 = .85.$$

We thus find that a "regime shift" took place during the New Deal period that increased the federal fiscal share by an estimated 9 percentage points. In addition, there remains a statistically significant trend over time toward greater fiscal centralization. But this effect is much smaller than in equation (1): the federal share now took about seven years to grow by 1 percentage point over the period under study. Moreover, if we return to figure 5.1, this process of continuing centralization appears to have its source in the New Deal years; there is no increase at all evident in the federal share prior to 1934. Thus, the data suggest that the New Deal programs both increased fiscal centralization and, at the same time, set in motion a process of further centralization.

The basic theory of fiscal federalism can provide a partial explanation for this trend toward greater fiscal centralization. The motivation behind the assignment of functions to local, state, and national governments is different for the allocative function of providing basic public goods and services (such as education, roads, and police and fire protection) than it is for the redistributive function of providing support for low-income households (Oates 1972, chap. 1; 1994). Decentralized levels of government have as their primary economic role the provision of levels of "local" public goods that are tailored to the particular preferences and circumstances of their own jurisdictions. In contrast, providing assistance to the poor requires a more substantial central presence. A local government, for example, that attempts to redistribute income aggressively from wealthy to poor households immediately creates incentives for resident high-income families to move elsewhere and for poorer families to migrate into the jurisdiction. It is easy to show that such mobility can readily undermine the achievement of local redistributive objectives and will, in general, result overall in suboptimal levels of support for the poor (see, e.g., Brown and Oates 1987). The implication is that in a federal system, the central government must play a major role in the design and financing of assistance to the poor.

Since the New Deal had poor relief as one of its major objectives, it is not surprising to find that the introduction of needed redistributive programs involved an increased degree of centralization of the public sector. The New Deal, as we have seen, introduced a variety of major welfare programs including social security and categorical assistance programs such as OAA, aid to the blind, and ADC (the predecessor to AFDC). As programs like AFDC grew in importance in later years, we find that the increased public role in income redistribution manifests itself in part in an increased degree of fiscal centralization.

Income maintenance programs could, in principle, be wholly centralized, with a centrally designed set of rules and benefits administered uniformly across jurisdictions. But, as we have seen, the New Deal took another course. The political setting for these programs was such that state and local officials demanded and got an active role in the specification of various key parameters for these programs (e.g., support levels) and for their administration, while the central government set up general guidelines and provided the bulk of the funds in the form of matching grants. The political economy of the new redistributive programs took the form of a cooperative enterprise between the various levels of government that has proved quite durable.[19]

The New Deal, however, was not the progenitor of all the changes in government structure since 1940. The New Deal was financed through national borrowing as much as through tax revenues. As a result, the changes in fiscal structure occurred largely on the expenditure side at the national level; it was at the state and local levels that new forms of taxation emerged in the 1930s. Not until World War II with the advent of income tax withholding did the national revenue structure take new shape.

A whole range of grant programs was begun in the 1960s that did not follow the New Deal pattern. These varied in their intent and structure, but typically the national government assumed much more direct control over the administration of the programs. The War on Poverty programs that cut state and even local governments out of the process are, by and large, gone now. The general revenue-sharing program is also gone. Although there was a move to consolidate conditional project grants into looser block grants for general purposes, block grants today are a relatively modest part of the fiscal system. For the most part, experiments in intergovernmental programs over the past 30 years that have not followed the New Deal pattern have not stood the test of time.

We have argued that the New Deal pattern of intergovernmental relations was the result of the struggle between state and national governments, and also between the president and Congress, for control over these programs. Ever since the New Deal, Congress has shown less inclination to locate either ad-

19. However, certain recent changes in the structure of welfare programs aim at shifting more of the responsibility for poor relief back to the states and changing the form of federal support from matching to bloc grants. It remains to be seen how all this will work out.

ministrative or financial control at the state level. As a result, the national government has continued to experiment with a wide range of intergovernmental forms. State and local governments, however, still want the substantial autonomy they were given in the New Deal programs. And they have effectively lobbied for a continuation of New Deal programs, albeit with growing complaints about unfunded mandates, and kept those programs in existence.

A widely misunderstood result of all that happened during and since the New Deal is the notion that it was only the federal government that grew during the 1930s. In 1927, state own revenues were 2.1 percent of GNP, and local own revenues were 6 percent of GNP. In 1940, state own revenues were 5 percent of GNP, and local own revenues were 5.8 percent of GNP. During the 1930s neither state nor local governments became smaller relative to the economy, and state governments grew. In 1992, state revenues were 7 percent of GNP, and local revenues were 6.1 percent.

Although the share of total fiscal activity at the local level declined sharply during the New Deal, the share at the state level actually rose. State expenditures were 13 percent of all government expenditures in 1927 and 17.5 percent in 1940. Rather than displacing state governments, the expansion of national government activity actually created incentives for state governments to expand their roles. The New Deal legacy has arguably been stronger governments at all levels, not just the central government. This is the result of national government programs that encourage, even demand, state and local participation in nationally funded programs.

Even local governments, whose fiscal share has declined so sharply, continue to play the major role in the actual delivery of most major domestic public services (see figure 5.1). The New Deal was clearly the time during which the national government came into prominence in the domestic sphere, but the way in which this took place has led to a cooperative form of federalism involving active roles for all three levels of government. The relative importance of the three levels may have varied at times over the past 50 years, but as we approach the close of the century, all three seem well entrenched in an active, if sometimes contentious, public partnership.

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