Federalism and Separation of Powers

Federal Aid to the States

*By Chris Edwards**

In recent years, members of Congress have inserted thousands of pork-barrel spending projects into bills to reward interests in their home states. But such parochial pork is only a small part of a broader problem of rising federal spending on traditional state and local activities.

Federal spending on aid to the states increased from $286 billion in fiscal 2000 to an estimated $449 billion in fiscal 2007. The number of different aid programs for the states soared from 463 in 1990 to 653 in 2000, 814 by 2006.

The theory behind aid to the states is that federal policymakers can design and operate programs in the national interest to efficiently solve local problems. In practice, most federal politicians are not inclined to pursue broad, national goals, but are consumed by the competitive scramble to secure subsidies for their states. At the same time, federal aid stimulates overspending by the states, requires large bureaucracies to administer, and comes with a web of complex regulations that limit state flexibility.

At all levels of the aid system, the focus is on spending and regulations, not delivering quality services. And by involving all levels of government in just about every policy area, the aid system creates a lack of accountability. When every government is responsible for an activity, no government is responsible, as was evident in the aftermath of Hurricane Katrina.

The failings of federal aid have long been recognized, but reforms and cuts have not been pursued for years. Aid has spawned a web of interlocking interests that block reform, including elected officials at three levels of government, armies of government employees, and thousands of trade associations representing the recipients of aid.

Yet the system desperately needs to be scaled back, not least because the rising costs of federal programs for the elderly are putting a squeeze on the federal budget. This article examines the growth of the aid system and describes its failings.[1] Congress should begin terminating activities that could be better performed by state and local governments and the private sector.

Historical Development

Prior to the Civil War, proposals to provide federal subsidies for state and local activities were occasionally introduced in Congress, but they were routinely voted down or vetoed by presidents for being unconstitutional. In 1817, President James Madison vetoed a bill that would have provided federal aid to construct roads and canals.[2] In 1830, President Andrew Jackson vetoed a bill to provide aid for a road project in Kentucky, arguing that it was of "purely local character," and that funding would be a "subversion of the federal system."[3] In 1854, President Franklin Pierce vetoed a bill that would have provided aid to the states for the indigent insane, also citing federalism reasons.

The federal government approved grants of land to the states for schools, roads, and canal projects. However, there were no grant programs that disbursed cash to the states for ongoing activities. That started to change toward the end of the nineteenth century. The Morrill Act of 1862 provided grants of federal land to the states for the establishment of colleges. In 1879, Congress provided funds to a private, non-profit group in order to distribute to the states educational materials for the blind. In 1887, the Hatch Act provided subsidies to the states for agriculture research, and was the first cash grant program.[4] An 1888 act provided aid to the states for veterans' homes.

Federal aid activity increased substantially in the early twentieth century. The "dual federalism" of the nineteenth century was being replaced by what came to be called "cooperative federalism." When the income tax was introduced in 1913, it provided the means for policymakers to finance a large range of new federal aid programs. Here are some of the early aid laws:[5]

- The Weeks Act of 1911 provided aid to the states for forest fire prevention.
- The Smith-Lever Act of 1914 provided subsidies to land-grant colleges.
- The Federal Aid Roads Act of 1916 provided aid to the states to build highways.
- The Smith-Hughes Act of 1917 created grants for vocational education.
- The Chamberlain-Kahn Act of 1918 provided aid to the states for combating venereal disease.
- The Fess-Kenyon Act of 1920 provided aid to the states for vocational rehabilitation.
- The Sheppard-Towner Act of 1921 provided aid to the states "for the promotion of the welfare and hygiene of maternity and infancy."

These seven early aid programs had similar features and similar faults as today's aid programs. All seven programs required the states to match federal funds on a dollar for dollar basis—federal aid was called the "fifty-fifty system." Matching requirements induce excess spending and divert state-source funds from other, perhaps higher, priorities of each state. If states are induced to spend more of their funds on farm subsidies, for example, they may have less to spend on their justice systems.

The new aid programs usually mandated an expansion in state and local bureaucracies. Aid programs required the states to set up new boards and agencies to oversee government spending in the prescribed activities. The 1916 Act required states to create highway departments; the 1917 Act required the states to establish vocational education boards; the 1921

** Chris Edwards is the Director of Tax Policy Studies at the Cato Institute, and author of Downsizing the Federal Government (2005).*

Act required states to create children's bureaus; and so on. The states had to create detailed plans, file regular reports to Washington, and subject themselves to inspection by federal officials. In order to receive aid, states were often required to pass legislation that regulated state and local activities in ways sought by Congress.

Various sleights-of-hand were used to get around constitutional concerns about expanded federal power. Funding for the 1890 Morrill Act was supposed to come from the proceeds of federal land sales in the states, but in practice the funds came from regular appropriations. The 1916 road subsidy law aimed to fund "post roads," or those that were used for federal mail delivery, but Congress defined it extremely broadly.[6] The 1911 aid bill was supposed to fund state forest fire prevention only near navigable rivers, providing a constitutional pretence for these activities as being related to interstate commerce.[7]

Figure 1 shows the number of aid programs for the states beginning with the education program of 1879. By 1930 there were fifteen federal aid programs. It was getting harder to hold the line on federalism as politicians became increasingly activist and new lobby groups were established. Labor unions pushed for federal funding of vocational education and succeeded with the passage of the Smith-Hughes Act in 1917. The passage of the 1916 road bill was preceded by the introduction of at least sixty-two different road subsidy bills in Congress.[8] State highway officials had formed a national organization in 1914 with an office in Washington to press for aid, and highway lobby groups helped draft the 1916 bill.[9]

Nonetheless, there was resistance to the growth in aid, and the shortcomings of aid programs were already becoming evident.[10] President Calvin Coolidge was a frequent and pointed critic of the aid system. In his budget message for 1926, Coolidge declared:

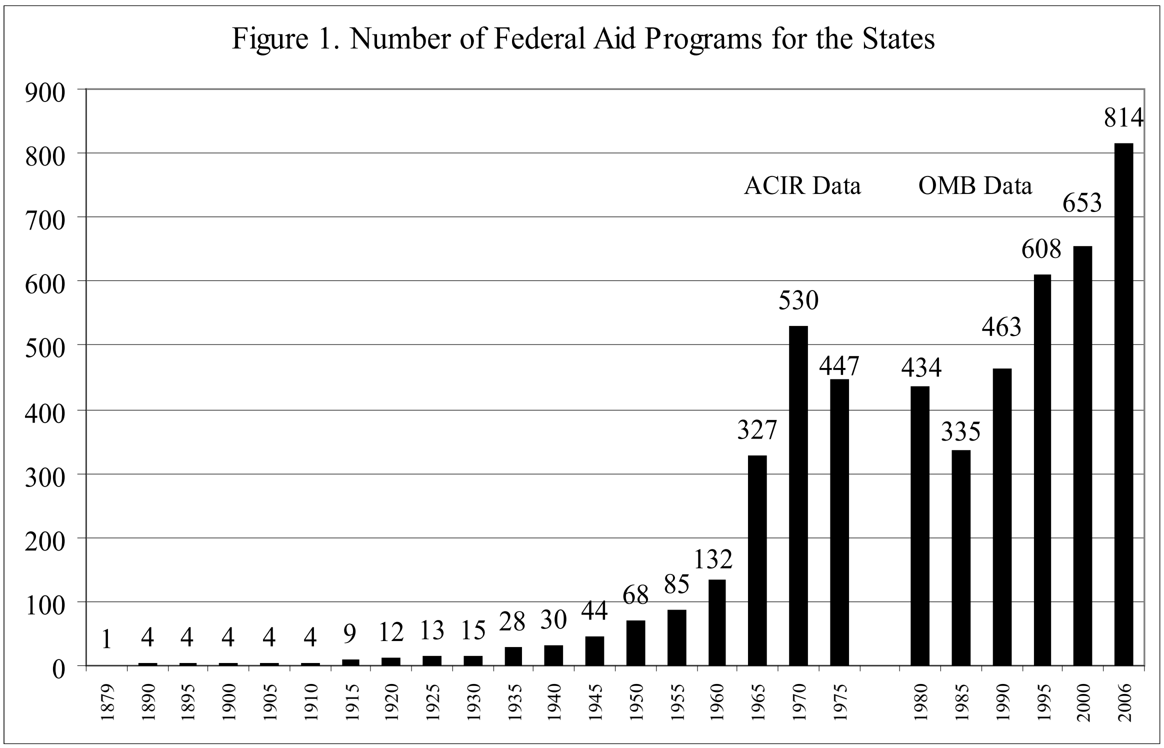
> I am convinced that the broadening of this field of activity is detrimental both to the federal and state governments. Efficiency of federal operations is impaired as their scope is unduly enlarged. Efficiency of state governments is impaired as they relinquish and turn over to the federal government responsibilities which are rightfully theirs. I am opposed to any expansion of these subsidies.[11]

Some leaders in the higher-income East Coast states strongly opposed expansions in aid. Governor Albert Ritchie of Maryland said that the "system ought to be abolished, root and branch" with the money "left in the states for the states to use for their own local needs and purposes."[12]

However, aid proponents were persistent, and as aid bills began to pass, new interest groups were formed and Congress was bombarded with requests for subsidies.[13] A few states initially refused to take part in some of the aid programs, but an observer at the time said that for most states "to get a few millions they shamelessly barter away their birthright" of reserved powers under the Constitution.[14]

By the time President Franklin Roosevelt came to office, many legal and political precedents had already been set for the large expansions in aid enacted under the New Deal. In the 1930s, aid programs were created for public housing, welfare, employment, and many other activities. The Federal Emergency Relief Act of 1933 provided more than $3 billion to the states over two years for work relief.

Federal aid expanded during the 1950s, with the number of aid programs almost doubling from 68 in 1950 to 132 by



Sources: Advisory Commission on Intergovernmental Relations (1879-1975), Office of Management and Budget (1980-2000), and author's estimate based on OMB methodology (2006).

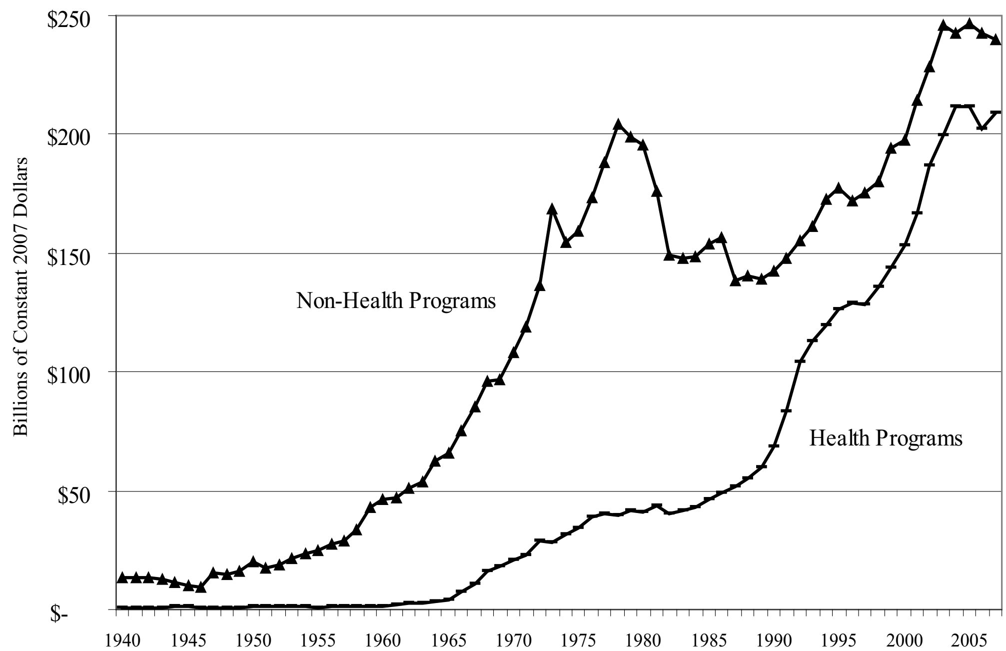
1960. That expansion occurred despite President Dwight Eisenhower's expressed concerns about federalism. Eisenhower had established a commission in 1953 to identify federal activities that could be returned to the states, but unfortunately no reforms were enacted.[15] The largest new grant program during this era was the Federal-Aid Highway Act of 1956.

The Highway Act provides an illustration of how federal regulatory controls started coming as a package deal with federal dollars. The Act imposed Davis-Bacon rules on all state highway projects that received federal money, which mandated that construction workers be paid "prevailing wages." That usually had the effect of increasing labor costs on projects at taxpayer expense. Because many states were already constructing their own highway systems in the mid-1950s, one effect of the 1956 Act was to increase the costs of many highways that would have been built anyway.

revenues available to individual states. Of course, the ultimate source of federal money distributed to the states is the taxpayers who live in the fifty states, but policymakers have always ignored this inconvenient truth.

In addition, aid advocates have been infused with a belief in the "public interest theory of government," which is the idea that policymakers act with the best interests of the broad general public in mind. In past decades, conventional wisdom held that the federal government could be effective and efficient at solving local problems. Are there poor people and blighted buildings in your city? Let us use the seemingly unlimited resources of the federal government to hire experts, bulldoze the blight, and build modern high-rises to solve the problem. That type of top-down thinking was behind the creation of aid programs for urban renewal, housing, education, and many other activities.

Figure 2. Federal Aid to the States, Constant 2007 Dollars



Federal aid exploded during the 1960s. Figure 1 shows that the number of aid programs quadrupled from 132 in 1960 to 530 by 1970. Under President Lyndon Johnson, new aid programs were added for housing, urban renewal, education, health care, environmental protection, and many other activities. Aid spending rose from $47 billion in 1960 to $129 billion by 1970, measured in constant 2007 dollars, as shown in Figure 2.

President Johnson called his policies "creative federalism," but his activism dealt a severe blow to the federalism of the nation's Founders. By the end of the 1960s, many policymakers believed that the federal government should spend money on just about any activity that it wanted, and questions regarding constitutional propriety were seldom considered anymore.

The huge growth in federal aid in the 1960s occurred for many reasons. Policymakers were fooled by the mirage that "federal resources" appeared to be limitless compared to the tax

We know today that the federal government is not very good at solving local problems. Even casual observation of Congress reveals that policymakers put the various narrow interests of their states above all else most of the time. Aid is the perfect tool to satisfy parochial special interests, and that is why the aid empire prospers today—not because experts believe that it works well.

Growing Aid, Growing Problems

The unchallenged optimism of the 1960s about the federal government's ability to solve state and local problems did not last. By the late 1960s, budget analysts were becoming alarmed at the growing complexity and overlap of federal grants. Two of President Johnson's top economic advisors and other experts began to push for consolidation of narrow "categorical" grants into broader and more flexible "block" grants.[16]

Categorical grants fund a narrow range of eligible activities based on detailed federal rules that state governments are required to follow. Until the 1960s, all grants were categorical grants; the vast majority still are. Categorical grants are very complex. As far back as the Hoover Commission in 1949 experts had proposed replacing them with block grants.[17] Congress passed the first block grant in 1966, which converted sixteen extant health care grants into a single broader program. A block grant for law enforcement was enacted in 1968. But these small reforms were overwhelmed by the avalanche of new categorical grants enacted in the late 1960s. The number of programs seems to have reached a temporary peak in the early 1970s, and then declined for a few years as the pace of program creation slowed and some existing programs were consolidated. While fewer new programs were added during the 1970s, the cost of aid programs soared as spending on all the programs created during the 1960s kicked into overdrive. President Richard Nixon took some modest steps toward consolidating the burgeoning aid system into block grants, arguing that federal aid had become a "terrible tangle" of overlap and inefficiency.[18] In his 1971 State of the Union address, Nixon lambasted "the idea that a bureaucratic elite in Washington knows what is best for the people."[19]

Nixon's reforms fell far short of his rhetoric, and just a few of his "new federalism" initiatives were enacted. Nixon succeeded in creating three block grants.[20] In addition, an extreme form of block grant, "revenue sharing," was begun in 1972 to give funding to the states with almost no strings attached. The problem was that revenue sharing did not substitute for existing grants—it was added on top. The program was abolished in 1986.

Consolidation of narrow grants into broader block grants made sense to budget experts, but members of Congress usually favored categorical grants because they could be better targeted toward special interests. The expansion of categorical grants was in sync with the increasingly fragmented committee structure in Congress in the mid-twentieth century. That is, the number of aid programs grew as the number of committees and subcommittees grew. Each committee and subcommittee wanted its own realm of programs over which to preside.

During the 1970s, concern grew over the complexity of the mushrooming federal aid system. When President Jimmy Carter came into office he proposed a "concentrated attack on red tape and confusion in the federal grant-in-aid system." [21] Carter pursued a number of modest reforms, but, like Nixon, he did a better job describing the aid problem than enacting solutions.

The bipartisan Advisory Commission on Intergovernmental Relations (ACIR) criticized many aspects of the federal aid system through the 1960s, 1970s, and 1980s. In 1980, ACIR published an eleven-volume study on federalism, which concluded that Washington's power had become "more pervasive, more intrusive, more unmanageable, more ineffective, more costly, and, above all, more unaccountable."[22] In an ironic twist, the ACIR, a rare government agency that criticized government programs, was one of the few agencies abolished by the Republicans in the 1990s.

The Government Accountability Office also criticized the federal aid system. In 1979 it found:

> The federal assistance system is an array of often conflicting activities and initiatives which defy understanding to all but the most serious students of the system … During the 1960s, the explosion in the number of federal programs made shortcomings in the [aid] system apparent. Studies showed that red tape, delays, and vast amounts of paperwork were characteristics common to most federal [aid] programs. [23]

President Ronald Reagan came into office promising to respond to such concerns and to revive federalism. He tried to cut aid spending, convert existing aid programs to block grants, and transfer some activities back to the states. The Omnibus Budget Reconciliation Act of 1981 eliminated fifty-nine grant programs and consolidated eighty categorical grants into nine block grants.[24]

In 1982, under his "new federalism" agenda, Reagan sought to re-sort federal and state priorities, such that each level of government would have full responsibility for certain activities. For example, Reagan proposed that welfare and food stamps be both financed and operated by the states.[25] Reagan also proposed "turnback" legislation to end about forty federal programs. Thus, he proposed that the federal government end most highway programs, while canceling the federal gasoline taxes that supported them.

In his 1983 budget message, Reagan argued that "during the past 20 years, what had been a classic division of functions between the federal government and the states and localities has become a confused mess."[26] Reagan had some success in cutting federal aid. Both aid spending and the number of aid programs were cut substantially during the early 1980s. Data from the Office of Management and Budget show that the number of aid programs for the states was cut from 434 in 1980 to 303 in 1982, before beginning to rise again.[27]

Reagan's progress in cutting aid programs was reversed by President George H. W. Bush. Aid spending and the number of programs grew rapidly in the early 1990s. Then, in the mid-1990s, the new Republican congressional majority tried again to revive federalism. Their biggest success was welfare reform in 1996, which turned open-ended categorical welfare aid into a block grant.

Since the mid-1990s, there have been no serious efforts to reform or cut the federal aid system, even though it is larger and costlier than ever. The system's many failings, which were discussed often during the 1970s and 1980s, have only become more acute as hundreds of new programs have been added since then. The current Bush administration has expanded the aid system rather than trying to restrain it. Department of Education outlays have doubled since 2000, as President Bush has taken steps to further nationalize local public schools. In other areas, the Bush administration's faith-based and marriage initiatives have hooked thousands of private organizations on federal subsidies. Richard Nathan, an architect of Nixon's new federalism, opined that Bush's policies "have reflected a willingness to run roughshod over state governments that is out of character with previous Republican administrations."[28]

Federal Aid Today

The number of aid programs increased from 653 in 2000 to 814 in 2006.[29] Aid spending rose from $351 billion in fiscal

2000 to an estimated $449 billion in fiscal 2007, measured in constant 2007 dollars.[30] Federal aid to the states is the third-largest item in the federal budget after Social Security and national defense. The five largest federal aid programs are Medicaid, highway construction, Temporary Assistance for Needy Families, education for the disadvantaged, and Section 8 housing subsidies.[31]

The 814 federal aid programs for the states generally take the form of either "formula" or "project" grants.[32] While most aid programs are project grants, most aid spending is on formula grants. That is because many of the largest aid programs, including Medicaid, are formula grants.

Under formula grants, legislation spells out how much funding each state is to receive based on factors such as state income and population. Under project (or "discretionary") grants, federal agencies distribute thousands of individual grants on a competitive basis after an expert review of proposals, at least that is how it is supposed to work.

One form of "discretionary" aid is earmarking. That occurs when the grant process is hijacked by individual members of Congress seeking to divert funds to particular projects in their districts. Thus, while a federal agency might normally distribute cancer research grants based on an expert review of proposals, politicians can end-run around the agency and directly target funds to health facilities in their districts.

Earmarking has exploded in recent years, and numerous congressional scandals have stemmed from the practice. The number of earmarks in federal spending bills increased from under 2,000 per year in the mid-1990s to more than 15,000 per year recently.[33]

This article focuses on aid to state governments, but the federal government also has hundreds of programs that directly provide subsidies to businesses, non-profit groups, and individuals. A complete list of federal aid programs is the 2,437-page Catalog of Federal Domestic Assistance (CFDA).[34] In 2006, the CFDA listed 1,696 federal subsidy programs, of which 814 were for state and local governments, as noted.

Despite general agreement among experts that block grants are superior to narrow categorical grants, only about twenty of the more than 800 state aid programs are block grants.[35] The reason notes the GAO is that "legislation addressing a specific need holds far more political appeal than broader purpose block grant programs. Any effort to incorporate categorical programs into a broader purpose program is interpreted as an attack on the congressional committees who created the programs, the agencies who administer them, and the clientele groups who prosper."[36]

Thus, the federal aid system is not about financing and operating programs in the most efficient manner; it is about politics. Politicians, special interests, and aid recipients resist conversion of programs to block grants because that would reduce their control and make programs easier to cut. One can debate whether or not federal aid is a good idea in theory, but in practice the political system has locked the nation into the most complex and inefficient form of aid: categorical aid.

Both block and categorical grants involve top-down control of state and local activities from Washington. Both types of grant lead to the creation of large bureaucracies. Nevertheless, converting categorical grants to block grants would represent progress because it would make federal costs more controllable and aid spending easier to cut. A good first step toward restraining Medicaid's explosive spending growth, for example, would be to convert it to a block grant.

Today's federal aid structure is massive and complex. The three layers of government in the United States no longer resemble the tidy layer cake that existed in the 19th century, but a jumbled marble cake. Federal expansion into policy areas traditionally reserved to the states has proven to be a wasteful and bureaucratic way of governing the nation.

One problem is that Congress provides nowhere near enough oversight for aid programs. Members get a political payoff from setting up aid programs and pushing to increase spending, not from pruning those that do not work. The Bush administration has performed detailed reviews of 257 federal aid programs and found that 109 of them were "ineffective" or could not "demonstrate results."[37] Yet Congress has shown little interest in cutting or terminating those programs.

Federal Aid and Politicians

Over the decades, policymakers have argued that various state, local, and private activities needed federal intervention because they had become "national priorities." A fact sheet from the Secretary of Education, Margaret Spellings, begins:

> The responsibility for K-12 education rests with the states under the Constitution. There is also a compelling national interest in the quality of the nation's public schools. Therefore, the federal government… provides assistance to the states and schools in an effort to supplement, not supplant, state support.[38]

The flaw in logic here is that there are few activities the federal government performs that are not also priorities of individuals, businesses, and state and local governments. One can call education a "national" priority, but that does not mean that the federal government has to get involved. That is because education is also a high priority of local governments and families. Local governments are free to learn schooling techniques from each other, but there is no compelling interest for top-down control from Washington.

President Ronald Reagan made the following observation in his 1987 executive order on federalism:

> It is important to recognize the distinction between problems of national scope (which may justify federal action) and problems that are merely common to the states (which will not justify federal action because individual states, acting individually or together, can effectively deal with them).[39]

The confusion between problems that are truly national in scope and those that are merely common to the states even extends to homeland security. When you look at the details of federal aid to the states for homeland security, you find that much is going toward items that would be better funded locally, such as bulletproof vests and radio systems for first responders. When this sort of local spending is federalized, members of Congress play a game of tug-of-war over funding for their states, and put less emphasis on taxpayer value for money in their decisions.

The idea that aid to the states can be designed in the "national interest" is a theory that does not match political reality. The concern of members of Congress for their states and districts almost always trumps any other policy considerations. Members may convince themselves that spending on aid projects in their hometowns is good for the country, but that is only because the resulting tax burdens are spread over the rest of the nation and invisible to them. Aid proponents say that it is in the national interest to help those people and regions of the country with the greatest needs. But in practice, the aid system has never operated in that fashion. A 1940 article in *Congressional Quarterly* lamented that "the grants-in-aid system in the United States has developed in a haphazard fashion. Particular services have been singled out for subsidy at the behest of pressure groups, and little attention has been given to national and state interests as a whole."[40] Forty years later, the ACIR concluded essentially the same thing: "Regarding *national purpose,* the record indicates that federal grant-in-aid programs have never reflected any consistent or coherent interpretation of national needs."[41]

In the operation of the aid system, political and parochial concerns are far more important than national priorities. The problem is not that members are not patriots, it is that they are also activists and—like most people—they have emotional and community ties to their hometowns. Of course, even before the modern grants-in-aid system, federal politicians championed spending activities that benefited their home states. Legislators with navy bases in their states have always supported navy spending, for example. But the expansion of the aid system in recent decades has magnified the age-old regional battles in Congress.

The recent explosion in the "earmarking" of federal aid and procurement has taken geographic political competition one step further.[42] Some earmarking misallocates resources for properly federal activities such as defense. But most earmarking is for federal spending on properly state, local, and private activities. By opening the floodgates to earmarking, Congress has encouraged a stampede of local interests to beat a path to Capitol Hill. Local governments and local organizations are increasingly making end-runs around state officials and going straight to Congress whenever they need a new parking lot, museum, or airport terminal.[43]

Earmarking is tied to recent corruption scandals. Disgraced lobbyist Jack Abramoff famously called the appropriations committees in Congress "favor factories." Indeed, they are. Politicians trade earmarks for campaign assistance, trips, sweetheart business deals, and general political support. Total fees paid to registered lobbyists in Washington have increased from $100 million in 1975 to $2.5 billion in 2006, with a substantial share of those fees related to earmark lobbying.[44] Recent scandals have shown that federal politicians cannot keep their hands out of the cookie jar, but the fundamental problem is that the federal cookie jar has grown so large. With 814 state aid programs and 1,696 federal subsidy programs overall, it is not surprising that the number of earmarks has soared because each program is a delivery vehicle for favors to home-state interests. The earmarking explosion was a scandal waiting to happen.

Parochial politics feeds on itself and has created a dynamic response from the states. The more aid programs and earmarking, the more federal lobbying state and local officials and interest groups will do. Highway contractors, school teachers, and policemen have learned that the payoff from the one-stop-subsidy-shop in Washington is higher than the payoff from lobbying each state separately.

Earmarks represent just a part of the regional skirmishing in Congress. The formulas used for distributing aid are a bigger battleground. Consider the ongoing fights over the formulas used to distribute homeland security aid. Homeland security aid has often gone to regions that don't need it in order to buy expensive items that are little used. Members of Congress also battle over health care grants. A *Washington Post* story profiled Senator Hillary Clinton's (D-NY) fight to tweak the formula that distributes federal grants for HIV/AIDS so that a little more flows to New York.[45] By engaging in such a fight, Clinton is signaling to her constituents that she is a champion for their interests. The efficiency of programs and their positive or negative effects are not politically important. It is spending that generates the favorable media coverage.

The States: America's Biggest Lobby?

Governors and other state leaders are putting increasing efforts into securing federal aid spending. The Republican Governor of Texas, Rick Perry, is considered to be a conservative, but his official webpage is chock full of press releases touting his hand-outs of federal subsidies such as "Gov. Perry Announces $1.6 Million in Grants to Juvenile Offender Accountability Programs."[46] As federal aid has increased, governors have become less like chief executives and more like regional deputies for the federal government. Since the explosion of federal aid in the 1960s, state and local governments have become major lobbyists in Washington. The ACIR reported in 1967 that "grantsmanship has become a popular new game in Washington."[47] The *Wall Street Journal* published a story in 1966 about the new profession of "grantsman."[48] Grantsmen were the high-paid middlemen who benefited from the maze of President Johnson's new state aid programs.

Many state and local interest groups were organized, or greatly expanded their Washington offices, during the 1960s. By 1967, thirteen states and twenty-four cities and counties had established Washington offices to lobby for aid.[49] Today there are 88,000 state and local government entities in the United States, including cities, counties, towns, school districts, and special districts.[51] Most receive—and many actively solicit—federal funding. All these governmental units, and their 16 million employees, represent a powerful lobby in support of aid programs and the vast federal welfare state.

As the number of aid programs has grown, state and local officials have put increasing efforts into federal lobbying. For example, it is routine for local groups across the country to organize "fly-ins" to Washington for personal arm-twisting on Capitol Hill. One recent news article profiled fly-ins by officials from California counties.[51] Local groups pay Washington lobbying firms to organize their meetings and strategies, and each group comes equipped with a wish list of local projects that they want funded.

Who can blame today's state and local officials putting so much effort into lobbying? There are winners and losers in the federal fiscal roulette. An analysis of federal aid to the states for 2004 found large variations between jurisdictions.[52] The biggest recipients of aid on a per-capita basis were the District of Columbia ($7,445), Alaska ($4,972), and Wyoming ($3,268), while the smallest recipients were Nevada ($1,045), Virginia ($1,085), and Florida ($1,158). State governments treat federal aid like a goldmine, and they use a multi-pronged strategy to secure their share of aid nuggets. Texas, for example, has an Office of State-Federal Relations that provides news from Congress on aid programs and works with Texas agencies to maximize federal funding.[53] Maryland has a sophisticated grants agency that was created to tackle the "increasing competition with other states" for federal aid.[54] The agency seeks to increase Maryland's "market share" of aid through activities such as "relationship building" with federal aid decisionmakers. In California, a major performance review of state government under Governor Arnold Schwarzenegger found that the state "does not receive its fair share of federal grant funds."[55] The report examined the issue in detail and proposed that the state "develop aggressive strategies" for "maximizing" federal aid, including creating a new office to better coordinate aid efforts.[56]

Many states have created "think tanks" to research how to increase federal aid. California has the California Institute for Federal Policy Research in Washington D.C., which operates a sophisticated tracking system for federal legislation.[57] This organization has a corporate board stacked with California politicians and business leaders. California also has the Public Policy Institute of California based in San Francisco, which provides frequent reports regarding California's share of federal aid funding.[58] The Northeast-Midwest Institute represents a group of eighteen states stretching from Vermont to Minnesota. The Institute's website says that it publishes the "most detailed analysis of the flow of federal funds to the states, demonstrating the persistent federal disinvestment in Northeastern and Midwestern states."[59] The website notes that the Institute helped "protect Amtrak routes in the region," "altered the food stamp program's criteria to take into account higher costs of living in cold climates," "defeated persistent attempts by southern lawmakers to change the match rate for Medicaid and welfare payments to the detriment of the Northeast-Midwest," and "established a dual Community Development Block Grant (CDBG) funding formula that helps rebuild older communities."[60] The CDBG program illustrates how technical the battles over aid can be. One item in the formula that distributes CDBG funding is "housing built before 1940." How did this obscure item get into the CDBG formula? The Northeast-Midwest Institute got a member of Congress to insert it into legislation in 1977 in order to tilt aid toward older cities.

Or consider the Public Policy Forum of Southeastern Wisconsin. It argues that this region of the country is at a "competitive disadvantage" because of a "failure to take full advantage of federal grants."[61] The government and business leaders of this group are taking an aggressive strategy to fix the problem. A recent report says that "competitive federal dollars drive economic growth... federal funding is a diverse source of capital that fuels discovery and wealth creation."[62] The report urges that local leaders hire staff and raise money for efforts to maximize inflows of federal dollars. Wisconsin groups should hire grant experts, travel to Washington two to four times per year, and phone federal agencies weekly. And they should raise private money to hire the experts needed to grab federal grants. Clearly, federalism has descended into a highly professionalized competitive battle between the states—and against federal taxpayers. The number of state and local governments that have hired high-priced Washington lobbyists has doubled since 1998.[63] One lobbying firm, Alcade & Fay, has a dedicated "Municipalities Practice Group," which generates $4 million annually in fees. Such firms typically charge their state and local government clients $10,000 to $20,000 per month. Alcade & Fay boasts that it has "secured billions of dollars in earmarked appropriations and federal grants."[64]

Because the federal budget is a goldmine for the states, it is not surprising that state and local officials invest in high-priced prospectors. Perhaps the most successful prospector is Gerald Cassidy, co-founder of the Washington lobbying firm Cassidy and Associates. The firm has been the focus of a recent series of articles in the *Washington Post*.[65] Cassidy and his firm pioneered the now-common practice of earmarking money for state and local spending projects in the federal budget. Cassidy's efforts have enabled him to amass a personal fortune of $125 million. The *Washington Post* series reveals that the expansion of federal spending on state and local activities has not just been driven by activist politicians on Capitol Hill. Entrepreneurial lobbyists, such as Cassidy, have played a key role in advancing the process by pro-actively selling their services to universities and other local institutions across the country. These days, state and local officials know that Washington lobbyists are helping most other jurisdictions secure federal cash, so if they sit on their hands or are squeamish about paying for lobbyists, they will lose out.

The time has long passed when state policymakers would jealously guard the independence of state activities and resist federal encroachment. These days, the priority of the states is to use every means available to squeeze more money from federal taxpayers. State officials have complained about the onerous rules of the No Child Left Behind law of 2002, and thirty state legislatures passed resolutions attacking NCLB for undermining states' rights. But the states did not call for repeal of the education law, they simply demanded more federal aid money to spend on NCLB implementation.

CONCLUSION

Under the federal aid system, about $500 billion flows into Washington each year from taxpayers in the fifty states. The funds are allocated by power brokers in Congress and routed through the federal bureaucracies. Then, somewhat depleted, the funds are sent back down to the states coupled with thousands of pages of federal regulations to comply with. It is a roundabout funding system that serves no important economic purpose. If it was shut down, state governments and the private sector would step in and fund those activities they think are worthwhile. During the 1970s and 1980s, government auditors, official commissions, and many analysts determined that the aid system needed major reforms. Ronald Reagan put the system on a diet for a few years, but the core pathologies were not addressed. Since then, hundreds more programs have been added to the system, the costs have grown higher, and the parochial battles over aid are bigger than ever.

The top-down micromanagement that comes with aid smothers policy diversity in the states. Aid mutes beneficial tax competition between the states. Aid destroys political accountability—when programs fail, politicians usually point fingers of blame at other levels of government. The federal aid system has been called a "the triumph of expenditure without responsibility." With the coming federal budget crunch from rising costs in Social Security and Medicare, the aid system is an ideal place to find budget savings. Initial reform steps should include converting Medicaid to a block grant to control costs and terminating hundreds of lower-priority aid programs. Cutting the aid system will require heavy political lifting, because the system is deeply entrenched. There are tens of thousands of state and local governments, unions, trade associations, and other groups addicted to the flows of dollars from Washington, and they will try to block any reforms. Ronald Reagan showed that aid can be cut, but it will take a fundamental challenge from another determined and reform-minded president.

Endnotes

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