

State and Local  
Finance  
*in the*  
National Economy

BOOKS BY ALVIN H. HANSEN

FULL RECOVERY OR STAGNATION?  
FISCAL POLICY AND BUSINESS CYCLES

*with* HARVEY S. PERLOFF

STATE AND LOCAL FINANCE IN  
THE NATIONAL ECONOMY

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# State and Local Finance *in the* National Economy

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By

ALVIN H. HANSEN, Ph.D., LL.D.

*Littauer Professor of Political Economy,  
Harvard University, and Special Economic Adviser,  
Board of Governors of the Federal Reserve System*

AND

HARVEY S. PERLOFF, Ph.D.

*Formerly Economist, Board of Governors  
of the Federal Reserve System*



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## INTRODUCTION

IN THESE war years we have rediscovered our economic power. Throughout the thirties, the strength of the American industrial giant lay dormant. No one in 1940 dreamed that the Federal Reserve Index would reach 240 in 1943; that the Gross National Product would reach \$187 billion; that the national income would reach \$148 billion. These things were just not believed possible. But here they are. Our productive capacity has reached a level so high that if we now permitted our national income to fall to the level of 1929, we should have about 18 million unemployed.

Thus, our sights all along the line have been raised. Plans cast in terms of the old standards are obsolete. All these developments impinge in innumerable ways upon the problems of state and local governments.

The American people are citizens of a great unified nation. The tasks of the nation as a whole must, however, be carried forward under a federal system of government. A nation so large in geographic extent and so varied in its industrial and social development demands a large reliance upon local responsibility and local government.

The conflict between different levels of government is frequently posed in unrealistic terms. Too often it is assumed that a vigorous state government, for example, implies a diminution in the sphere and influence of local government, and, similarly, that enlarged activities of the federal government encroach upon the proper functioning of state governments. It can, however, be demonstrated, we think, that only when the higher levels of government play their appropriate role vigorously and efficiently are conditions created under which subordinate units of government can effectively carry out the functions appropriate to them. It is where state governments are strong and vigorous that efficient local government flourishes. Experiences of recent years have demonstrated that when problems which transcend the power of state and local governments are not vigorously attacked by the federal government, state and local government becomes unworkable.

The American people have continuously throughout their history set themselves new goals for the nation as a whole in terms of political,

social, and economic progress. These national goals can only be effected through the three levels of government, each playing its appropriate role, and not by any artificial departmentalization of the three governmental levels. Thus, despite the fact that we operate in a federal system, the programs which we seek to carry through are national in scope, involving appropriate action at each governmental level.

Fiscal policy has an important role to play in all this. Under modern conditions, many things must be done by collective action. Public finance underlies, of necessity, community action. It is, therefore, of the utmost importance that the financial machinery of government and the intergovernmental fiscal relations be geared to the requirements of present-day society.

Too often financial problems are treated within the pattern of a static system. Energies are expended upon patching up or plugging holes where they might better be directed toward ways and means of improving the economic base and developing a sound foundation upon which the various governmental fiscal structures may be built.

The main problems in intergovernmental relations center around shifts in financial responsibilities. Any realistic appraisal of the American governmental structure, and what is necessary to make its functioning effective, must take cognizance of this pivotal fact. At the same time, however, it is important to realize that while the federal government may rightly make contributions toward the support of essential social services, the major control of the actual administration will still, in the typical case, remain at the state or local level. Thus we approach our problem on the assumption that the values associated with local self-government are very real and important.

I wish to express my great obligation to the Graduate School of Public Administration, Harvard University, for the seminar and research facilities which it has made available. I am, moreover, deeply indebted to the Board of Governors of the Federal Reserve System for placing at my disposal the efficient services of its library and its ample research resources.

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Finally I wish to express my deep appreciation for the stimulation of frequent and continued discussion with Dean John H. Williams of Harvard on the broader aspects of fiscal policy and its relation to monetary policy.

The authors alone assume full responsibility for the opinions expressed and for errors which may inadvertently have escaped their attention.

Although one of the authors of this book is now a member of the Army of the United States, his work on the book was done before his entry into military service. The opinions expressed in this book are not to be taken as those of the War Department.

ALVIN H. HANSEN





# CONTENTS

INTRODUCTION	v
PART I. THE PROBLEMS AND DEFICIENCIES	
1 WARTIME AND POSTWAR PROBLEMS	1
2 SERVICE LEVELS AND RELATIVE RESOURCES	14
3 STATE AND LOCAL TAX DEFECTS	35
4 FISCAL PERVERSITY IN BOOM AND DEPRESSION	48
PART II. MEANS OF STRENGTHENING THE FISCAL BASE AND OF RAISING SERVICE STANDARDS	
5 MODERNIZING LOCAL GOVERNMENTS	70
6 RESOURCE DEVELOPMENT, URBAN REDEVELOPMENT, AND FISCAL CAPACITY	98
7 INTERGOVERNMENTAL CO-OPERATION	121
8 FEDERAL UNDERWRITING OF MINIMUM SERVICE STANDARDS	141
PART III. THE OVER-ALL BUDGET, FULL EMPLOYMENT, AND ECONOMIC STABILITY	
9 PUBLIC EXPENDITURES, INCOME CREATION, AND COSTS	181
10 FINANCIAL PLANNING, PUBLIC CREDIT, AND CYCLE POLICY	194
11 THE EXPENDITURE BUDGET IN A FEDERAL SYSTEM	223
12 A REORGANIZED OVER-ALL TAX STRUCTURE	243
APPENDIX A MOULTON'S "THE NEW PHILOSOPHY OF PUBLIC DEBT": A REPLY BY ALVIN H. HANSEN	285
APPENDIX B RECOMMENDATIONS OF THE ROYAL COMMISSION ON DOMINION PROVINCIAL RELATIONS IN CANADA	299
APPENDIX C STATE LEGISLATION NEEDED FOR URBAN REDEVELOPMENT BY ALFRED BETTMAN	303
INDEX	306

