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Contents

This month's cover shows four people's solution to the gas shortage.

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The Institute Has a New Director: Henry W. Lewis

HENRY WILKINS LEWIS sees the past, present, and future of the Institute of Government in terms of University service to the governments and people of North Carolina. That is important, for Henry Lewis, is the new director of the Institute of Government, an organization to which he has devoted twenty-seven years of his professional life.

In his view, the Institute of Government, a part of the University of North Carolina at Chapel Hill, reflects the University's long-held philosophy that it has a total educational mission, both *in* and *beyond* the classroom, to serve the people of this state. Lewis believes that nothing is nearer the heartbeat of the state or more determinative of the kind of society the state has than its government, at both state and local levels. He feels that the Institute's mission is to reach people now in governmental positions or who may come into governmental positions. This outreach—through teaching, consulting, and publishing—is designed to enhance the quality of public service in the state and to help individuals in developing their capacity for that service.

Henry Lewis does not see this as any change from the tradition or services of the Institute of Government. He believes it is imperative that the Institute of Government faculty remain sensitive to the needs of those in public office and retain a constant willingness to work directly with all categories of public officials and personnel. He hopes and believes that the Institute staff will also be able to communicate to non-officeholding citizens some better understanding of "whatever it is that government takes on and is charged with doing." In effect, this continues a long-established concept of Institute responsibility and role, for Henry Lewis says flatly: "This is no departure from what we are charged with doing."

Over the years Henry Lewis has come to have strong convictions about the relationship of the Institute of Government to the University at Chapel Hill. He states them succinctly: "The Institute of Government is fortunate to be University-based. I am confident that a major reason for the Institute's success is the kind of people we have been able to attract to our faculty. The reason we have been able to attract and hold them is that they are able to identify with the University as faculty members." Even so, he adds emphatically, "The objective for every Institute of Government faculty member is that he or she maintain close contact with people on the job in governmental service."

SINCE THESE OBSERVATIONS obviously reflect the views of an administrator, it is worth noting that Henry Lewis has never sought an administrative role. A native North Carolinian, Lewis was born and raised in the town of Jackson in Northampton County. Following his early education in Jackson public schools and at Virginia Episcopal School in Lynchburg, he received his A.B. degree from the University of North Carolina in 1937 and his J.D. degree from Harvard University in 1940. Admitted to the Bar in North Carolina in 1940, he engaged in private legal practice for a year and then served in the United States Army for five years. His principal affiliations during World War II were with the 99th Infantry Division, Headquarters, Third Army, and with Army Ground Forces Headquarters. He was separated from the Armed Services in 1946 as a captain and since then has served on the Institute of Government faculty, attaining the rank of Professor of Public Law and Government in 1958.

His major fields of research, teaching, and writing have been property taxation, organization of state tax agencies, legislative organization and procedure, and election law and procedure. Property taxation remains a continuing thread in his career. Even in November of this year, his first month as director of the Institute of Government, he presided over one of his regular schools for tax officials.

Through the years Lewis has served with three tax study commissions. He was consultant and draftsman for the Commission for the Study of the Revenue Structure of the State (1957–58), the Commission for the Study of the Local and Ad Valorem Tax Structure of the State (1969–70) (and drafted its Machinery Act of 1971), and the Commission for the Study of Property Tax Exemptions and Classifications (1971–72). For this last commission, he drafted its revisions of the statutes dealing with exemption, classification, and preferential tax treatment of property.

When working with the organization of state tax agencies, Lewis served as consultant and draftsman for the Commission on the Reorganization of State Government (1953–54), with emphasis on the Department of Revenue, the State Board of Assessment, the Tax Review Board, and the Department of Tax Research. In the study and reworking of legislative reorganization and procedure, he did research and analyzed the standing committee system of the North Carolina Senate for H. P. Taylor, Sr., who was then Lieutenant Governor; initiated proposals to decrease the size and number of Senate committees; and made comparable studies of committees in the State House of Representatives. His background in election law and procedure includes serving (1966–67) as consultant and draftsman for the Election Laws Revision Commission, recodifying the primary and general election laws of North Carolina.

His numerous publications include *Basic Legal Problems in the Taxation of Property* (1958); *Property Tax Collection in North Carolina* (two editions, 1951 and 1957); *In Rem Property Tax Foreclosure* (with Robert G. Byrd, 1959); *Judicial Review of Property Tax Appraisals in North Carolina* (with Donald A. Furtado and others, 1966); *Mandamus and the Octennial Revaluation of Real Property* (with William A. Campbell, 1967); *Property Tax Exemptions and Classifications* (1970); *The Annotated Machinery Act of 1971; The Property Tax: An Introduction* (1972); *Legislative Committees in North Carolina* (1952); *The General Assembly of North Carolina: Organization and Procedure* (1952); *Conducting Municipal Elections* (1961); *Report of the Election Laws Revision Commission* (1966); *Primary and General Election Law and Procedure: A Handbook for Election Officials* (eleven editions, through 1968); *An Introduction to County Government* (1963; revised 1968).

Although he has never actively sought a primary role as an administrator, Lewis has been called upon

to serve in administrative capacities before being appointed as director of the IOG. He was in charge of the Institute's Legislative Service in 1949, 1951, and 1953 and shared that responsibility with George Esser in the 1955 session. During Gordon Gray's administration as president of the Consolidated University of North Carolina, he served on a committee to investigate hazing at the University and wrote a report that became rather celebrated. He also served as chairman of the committee to inaugurate William B. Aycock as chancellor of the University.

More administrative challenge came when he consented to take leave from the Institute faculty to serve one year as vice-president of the Consolidated University. His principal responsibilities for the University's general administration included acting as liaison official between the Board of Trustees and the University administration and as legal counsel to the president of the University, the chancellor, and the Board of Trustees on matters affecting labor relations and student disruption and discipline. He also had supervision of the University's television system during that year.

[It is worth noting that Lewis has other administrative experience outside the University system. He is a director of the Bank of Northampton in Jackson and vice-president and a director of the Wilkins Texas Company, a Virginia corporation. Since 1950, he has often been a vestryman and three times senior warden of the Chapel of the Cross in Chapel Hill, a member of the Standing Committee of the Episcopal Diocese of North Carolina for three terms, and three times deputy to the Episcopalian general conventions. Since 1957 he has been a member of the Advisory Board of the Ackland Art Museum of the University of North Carolina, a president of the North Carolina Collectors, and twice a member of the executive committee of the State Literary and Historical Association. His memberships include Phi Beta Kappa, Alpha Tau Omega, Order of Gimghouls (University of North Carolina, Chapel Hill), Lincoln's Inn So-

What do others think of Henry W. Lewis, the new director of the Institute of Government? Here are some comments:

Henry Lewis represents to me the essence of what is truly good about North Carolina. He knows the state from end to end, is acquainted with vast numbers of its people, is related to many of them, and works for its welfare with devotion, energy, and skill. His interests are many and wide, but somehow they all come home to Carolina in the end. . . . He is the man who proved to me that one person really can be kin to a whole state.

—Joseph C. Sloane, Chairman
Department of Art
University of North Carolina at Chapel Hill

If I were to choose one thought or recollection concerning Henry, it would be his enthusiastic desire to help others and to discuss their problems. This, of course, has been reflected in the ad valorem tax field, since that is his specialty; but I believe it will be reflected in any aspect of his life.

—P. Eugene Price, Jr.
Forsyth County Attorney, Winston-Salem

I have high regard for [Henry Lewis] . . . especially for his penetrating mind and his keen attention to details. In the area of North Carolina tax law I doubt whether anyone exceeds him in knowledge, especially historic perspective.

—William D. Snider
Editor and Vice-President
Greensboro Daily News—Greensboro Record

I have a very high regard of Henry's ability and I am confident that the Institute will continue to flourish under his leadership.

—William A. Dees, Jr., Goldsboro
Attorney-at-Law and Chairman of the Board of Governors
University of North Carolina

Among other qualities, Henry Lewis's tenacious adherence to sound standards and his enormous capacity for hard work have made him a highly respected leader in the academic world and in the halls of government.

—William Friday
President, University of North Carolina

When I think about Henry Lewis, I come immediately to the thought that here is a man of many parts—able, learned, and effective professionally, with broad intellectual and cultural interests, notably in art and history, a good and responsible churchman, and a valuable University professor who can be counted on—with it all, a man who doesn't hesitate to speak his mind.

—J. Carlyle Sitterson
Kenan Professor of History
Former Chancellor, University of North Carolina at Chapel Hill

. . . [Henry Lewis] is a man of great dignity, of broad and deep cultural interests, of profound commitment to the state of North Carolina and its government, and of tact and personal grace. He is a devout churchman, and in an age when they are becoming distressingly few, he is in the truest and best sense a gentleman.

—C. Hugh Holman
Kenan Professor of English
Former Provost, University of North Carolina at Chapel Hill.

Although [Henry is the tax] "expert" from out of town, he never has taken adamant positions, but has always recognized the fact that there are problems to which there are no apparent answers, even in the statutes that he has so ably drafted. It has always been a pleasure to work with him.

—James C. Fox
New Hanover County Attorney

[Henry is] the most knowledgeable expert on ad valorem taxes I have ever had any contact with. He has always been willing to give me the benefit of his research on the many and varied county problems which I have plagued him with, and his guidance has been particularly helpful in the many areas in which statutes have not been interpreted by the courts.

I value his friendship highly, and admire him greatly.

—Clarence Kluttz
Rowan County Attorney

[Henry] has always sought to involve himself in things that were challenging to him and in the end productive.

—J. C. Eagles, Jr., Wilson
Former Vice-Chancellor for Finance
University of North Carolina at Chapel Hill

ciety (Harvard Law School), North Carolina Bar Association, and Torch Club.]

LEWIS NOTES THAT THE CHALLENGE facing any new Institute of Government administrator derives in part from the structure of the organization. He says: "The Institute administrator traditionally frees the staff from administrative responsibilities so that they can do the job for which they are hired. But he doesn't get any preparation or helpful experience as a faculty member and has to learn a great deal from scratch." Lewis lists budget, personnel, and building maintenance as three examples of administrative responsibility for which experience as a staff member does little to prepare the new administrator.

The new director sees space limitations and insufficient supporting services as primary Institute problems. Since the present Institute of Government building was constructed seventeen years ago, Institute services and personnel have outgrown the building's ability to house them. Says Lewis: "We are severely restricted with regard to classroom space and have had to encroach on needed dormitory space for offices." (Actually, the entire basement floor residence hall has, of necessity, been converted to office space. The first Institute building, completed in 1939, served, from the time the Institute moved into the present building in 1956 until recently, as the Administration building for the Consolidated University.)

The University and the state, as Lewis sees it, have been responsive in meeting the Institute needs for faculty. However, he observes: "We need funds for supporting services, secretarial and business. Further, the funds available to the Institute of Government for publications are too limited. Restricted state support for these purposes hurts. The effectiveness of an Institute of Government staff member is seriously restricted without adequate secretarial and research assistants, especially when funds for publications also are tight."

THE FULL-TIME NATURE of the administrator's job will leave Lewis little time for the teaching and writing he has so long cherished. He points to the new demands on his time in characteristic fashion: "The directorship requires so much consultation under the University's instrument of government, there is no way I can escape responsibility. I have no right to pass authority and responsibility to any faculty member. I can ask someone to act for me, but, if I should, I would still be responsible."

Lewis is only the third director of the Institute of Government in forty-three years. The founder and first director, Albert Coates, served from the inception of the Institute in 1931 until retirement in 1962. The second director, John L. Sanders, was Institute director from 1962 until November 1, 1973, when he assumed duties as Vice-President for Planning of the University of North Carolina. As it happens, all three directors call eastern North Carolina home. Both Coates and Sanders were born and raised in Johnston County.

Another common denominator is the legal background of each director. Coates, like Lewis, is a graduate of Harvard Law School. Saunders completed his law degree at the Law School of the University of North Carolina. This compatibility of geographical origins and personal backgrounds provides an interesting circumstance. Each of the three directors, however, is very much an individualist. That individuality has been and no doubt will be reflected in the administration of each man. For clues as to the personality, character, and qualifications of Henry Lewis, you may wish to read comments by others published in the box on page 3.

—Elmer R. Oettinger

SANDERS BECOMES VICE-PRESIDENT OF THE UNC SYSTEM

SAYING HELLO to Henry Lewis as director of the Institute of Government means saying goodbye to John Sanders. Sanders resigned the directorship last October to become Vice-President for Planning of the University of North Carolina system, which now comprises all of the state's institutions of higher education. He became the Institute's second director when its founder, Albert Coates, retired in 1962.

If it is true that an administrator's chief role is to expedite the work of his colleagues and bring out the best in them, then John Sanders was an unqualified success at the Institute. First of all, he had a strong concept of the Institute's mission in serving the people of North Carolina, and all of his leadership was directed toward that end. He was utterly fair with all who work at the Institute, and his colleagues knew that his comments and criticisms came from perceptive insights and were aimed at improving the Institute's service to the state. Members of the staff and faculty during his directorship did not work for John Sanders; they worked for the people of the state and their governments through the Institute and with Sanders.

In his vision for the Institute, he saw its work expanding steadily, but he had constant concern for its quality. He was not interested in empire-building—he sought the growth and well-being of the Institute solely in order that its mission might be better accomplished. He believed strongly in the Institute's operating principles of competence, objectivity, and nonadvocacy, and he saw the Institute as being in the service of all the people of the state, of all political factions and parties, and of all levels and units of government.

A remarkable thing about John Sanders is his sense of humor. He is a serious man, yet he has an abundance of wit that is quick, dry, and incisive. It is an extension of his personality; directed at himself, he uses it to maintain a modest attitude that is genuinely his. He also uses humor as an instrument of administration, as a tool to cut open the most difficult public and organizational problems. At the Institute, if the faculty began to take itself too seriously, he could suggest that the dust in the hallways probably reflected clay-footed traffic that had nothing to do with the number of visitors to the Institute. And in social situations no one has ever accused him of being puny at punning (to which he is mildly addicted).

Within the University of North Carolina at Chapel Hill and the larger University system, Sanders has made enormous contributions in special posts and committee assignments, assignments that came to him because of his knowledge of law and higher education and because of the respect for his judgment that other administrators hold. (And who can calculate the contributions he has made in simple conversations with those who have sought his opinion and counsel?) Few months have passed without his involvement in some significant general University activity in Chapel Hill. He served on the Chancellor's Advisory Council and on the Agenda Committee for the Faculty Council; he was chairman of various committees concerned with evaluating some aspect of the University's operation and a member of dozens of others; and he was the president of the first Faculty Assembly, composed of representatives from the sixteen institutions that make up the University of North Carolina system. Just before his resignation as Institute director, he served as chairman of the UNC-CH special Affirmative Action Committee that was charged with developing an affirmative action plan for the Chapel Hill campus. In addition, he often served on state and national committees as a representative of the Institute of Government or the University.

SANDERS HAD BEEN A MEMBER of the Institute staff for six years before he was appointed director by William B. Aycock, then Chancellor at Chapel Hill. During that time he had been in charge of the Institute's staff work for the Commission on Reorganization of State Government and had established himself as an authority on legislative apportionment and redistricting and on state constitutional development in North Carolina. His articles on legislative representation that appeared in *Popular Government* in 1961 and 1962 stand as the key work on the history of legislative representation in North Carolina. These were supplemented by other publications on representation and by extensive assistance to legislative committees concerned with reapportionment and redistricting after the 1960 and 1970 censuses.

The work on various revisions of the North Carolina Constitution during the past two decades provided Sanders with another opportunity to develop the narrative of North Carolina constitutional history and to contribute through staff support to the constitutional revision that occurred during this period. In these years he wrote an account of the several constitutional conventions and analyses of the proposals for revising the Constitution. When Governor Moore appointed the special constitutional study committee that produced the editorial revision of the Constitution and amendments that were ultimately approved by the voters in 1970, Sanders was the key member of the Institute staff that rendered professional support to the committee. Much of the research, drafting of texts, and final committee report were his work.

Almost from the beginning of his sojourn at the Institute Sanders had followed his interest in higher education. In the fourteen months immediately before he became director, he had been on leave to serve as secretary to the Governor's Commission on Education Beyond the High School. The work of that commission—which has been described as the most intensive and comprehensive study ever made of higher education in North Carolina until then—led to the establishment of the present system of community colleges and technical institutes. His assignment with that commission only began his extensive work in higher education. In 1966 he provided the principal staff assistance for the special commission studying the Board of Trustees of the Consolidated University of North Carolina. And throughout the 1960s he worked with University officials, members of the General Assembly, and Governors on the various reorganization actions that culminated in the establishment of the present statewide University of North Carolina system, of which he has become Vice-President.

Thus while for eleven years Sanders was an administrator by title and a distinguished one in fact, he continued his professional work in the areas of legislative representation, constitutional development, and higher education.

IN HIS UNDERGRADUATE DAYS (he was once a student at North Carolina State) Sanders had planned a career in architecture, though he received his undergraduate degree in history. Some of his close friends will fancy that they see him taking Frostian glances backward at the roads of architecture and history that were not taken when he later chose law and public service. They are probably correct, and in his avocation he has found a way to merge these interests in architecture, history, and law. He is the leading authority on North Carolina's state capitol building and has spent countless hours of research on its history. In the current capitol restoration, he has served as consultant to the architects and to the Division of Archives and History. It is characteristic of him that a private passion is also a public service, just as it was characteristic (and to be expected) that when he left a record of accomplishment at the Institute, it was to move to another post where service to the State and the University could continue.

—Jake Wicker

FINANCING PUBLIC EDUCATION
Recent Court Decisions

William A. Campbell

This article reviews a number of recent judicial decisions dealing with the financing of public education. Its primary focus is on the *Serrano*[1] and *Rodriguez*[2] cases and the principles to be derived therefrom, but it also discusses the school finance issues presented by recent decisions involving the education of mentally retarded children, metropolitan desegregation plans, and student fees.

IN 1971 AND 1972, great hopes were raised in some quarters and great consternation in others by a series of judicial decisions that sought to eliminate, on constitutional grounds, inequalities in financial resources among local school districts that resulted from differences in property valuations. The United States Supreme Court rejected the constitutional theory upon which these decisions were based in the case of *San Antonio Independent School District v. Rodriguez*,[3] and thus ended for a time hopes that the inequalities complained of—and admitted—would be declared invalid on federal constitutional grounds. That did not end the matter, however, because several of the judicial decisions following *Serrano* were based on state rather than federal constitutional grounds,[4] and other suits may yet be brought on state grounds. Furthermore, the *Serrano-Rodriguez* cases stirred an intense interest among governors and state legislatures in methods of alleviating some of the more egregious inequities in local school finance. The comments and observations in this article, therefore, are relevant to those states in which suits, based on language in the state constitution, have been or are being brought challenging the systems of school finance on *Serrano-Rodriguez* principles, and to those states that are not under judicial mandates to restructure their systems but whose governors or legislators wish to make changes in accordance with *Serrano-Rodriguez* principles.

This article is a revised version of a paper presented in Las Vegas, Nevada, March 28, 1973, at a Seminar on Financing Educational Opportunity, sponsored by the Regional Interstate Project Program. The paper has been published by the Colorado Department of Education in a report of the seminar. Most of the research for this article and the ideas presented in it were developed in the author's work on the *Report on North Carolina School Finance: Responses to Serrano-Rodriguez* (Institute of Government, November 1, 1972). Co-authors of the Report were Charles D. Liner, Assistant Professor of Public Law and Government and Economics, and Robert E. Phay, Associate Professor of Public Law and Government—both at the Institute of Government, University of North Carolina at Chapel Hill; and John M. Payne, Assistant Professor, Rutgers University School of Law.

1. Serrano v. Priest, 96 Cal. Rptr. 601, 487 P.2d 1241 (1971).

2. Rodriguez v. San Antonio Independent School District, 337 F. Supp. 280 (W.D. Texas 1971).

3. 411 U.S. 1 (1973).

4. *Serrano* itself is based in the alternative on state constitutional grounds. So also are *Robinson v. Cahill*, 118 N. J. Super. 223, 287 A.2d 187 (1972), *aff'd on state constitutional grounds*, 62 N.J. 473, 303 A.2d 273 (1973), and *Milliken v. Green*, 389 Mich. 1, 203 N.W.2d 456 (1972).

The Serrano-Rodriguez Principles

Serrano v. Priest, decided in 1971 by the California Supreme Court, was the first judicial decision invalidating, on equal protection grounds, a state system of school finance. In reviewing the school finance system under attack, the court found that, in fiscal year 1968–69, 55.7 per cent of educational revenue in California came from the local property tax, 35.5 per cent from state aid, and 6.1 per cent from federal funds. The amount of local funds available depended on the appraised property values in the local school district, and these values varied across the state. California employed a foundation plan of state aid with which it tried to ensure that each district received a minimum amount of money per pupil, regardless of its property values. Despite this program, wide disparities existed in per-pupil expenditures among the local school districts.

The court found that the state's system of financing public education brought about a denial of equal protection of the laws under the Fourteenth Amendment to the United States Constitution and similar clauses of the California constitution. In so finding, the court declared that education was a fundamental constitutional interest and that any wealth classification affecting education must be strictly scrutinized. The legal principle to be derived from *Serrano* may be summarized as follows: a system of financial support for public education in which the major determinant of funds per pupil is the appraised valuation of property within a district creates a classification based on wealth affecting a fundamental constitutional interest unsupported by a compelling state interest; that system is therefore in contravention of the equal protection clause of the Fourteenth Amendment. This principle is more succinctly stated by Coons, Clune, and Sugarman in *Private Wealth and Public Education* in the now-famous Proposition I: "The quality of public education may not be a function of wealth other than the total wealth of the state."[5]

Following *Serrano*, there were decisions in Minnesota, Texas, New Jersey, Arizona, Wyoming, Kansas, and Michigan that invalidated on equal protection grounds the systems of school finance in those states. The Texas case, *Rodriguez v. San Antonio Independent School District*, is of special interest because it was appealed to the United States Supreme Court, where it was reversed. A three-judge federal district court reviewed the Texas school finance system in *Rodriguez* and found the same types of inequalities that the California court had found in *Serrano*. Texas also employed a foundation plan, but the local districts had to use funds raised from the local property tax to finance capital expenditures and to finance all operating expenditures above the foundation level. As a result, wide disparities existed in per-pupil expenditures among the local districts.

The district court essentially followed the reasoning of the *Serrano* case and held the Texas system unconstitutional as a denial of equal protection of the laws in violation of the Fourteenth Amendment. Both *Serrano* and *Rodriguez*—*Serrano* explicitly, *Rodriguez* implicitly—rest on the assumption that there is a significant and demonstrable correlation between the level of expenditure and the quality of education. Common wisdom tells us that this is so up to a certain point; but beyond that point, common wisdom is not helpful, and several recent studies made by social scientists indicate that there is no significant correlation—beyond some difficult-to-define threshold.[6]

It should be emphasized that neither *Serrano* nor *Rodriguez*, nor any of the cases following them, declared that the property tax may not be used for the financing of schools; a properly structured and equalized property tax appears to be constitutional. Further, it should be emphasized that the cases do not require the affected states to implement any particular type of financing system; rather, they tell the states what they cannot do. Finally, the cases do not require equal per-pupil expenditures across the state, although they do appear to permit such equal expenditures.

The United States Supreme Court reversed the district court in *Rodriguez*. The Court, in an opinion by Justice Powell, first stated that the Texas financing system, although leaving local school districts dependent on widely disparate property tax bases, did not create a wealth classification in the way that other classifications had done that had been struck down as "suspect." To support this position, the Court reasoned that the Texas financing system discriminated not on the basis of personal wealth but on the basis of district wealth, and in previous cases declaring wealth classifications invalid, the discrimination had been on the basis of personal wealth. Second, the Court stated that the wealth discrimination complained of did not cause an absolute deprivation of education, but only diminished the quality of the education in some uncertain degree. The Court further refused to accept the argument that education is a fundamental constitutional interest. It did not deny the importance of education to society, but stated that social importance alone is not enough to elevate an interest to the status requiring special constitutional protection. There is no right to education

5. See Private Wealth and Public Education 304 (1970).

6. See Office of Education, U.S. Department of Health, Education and Welfare, Equality of Educational Opportunity (1966), [The Coleman Report]; Mosteller and Moynihan, eds., On Equality of Educational Opportunity (1972); and Picariello, *Report for Fiscal Year 1967*, in How Effective Is Schooling? (Averch ed. 1971).

7. San Antonio Independent School District v. Rodriguez, 411 U.S. 1 (1973).

"explicitly or implicitly guaranteed by the Constitution." The Court thus declined to accept the two supporting arguments that would have required that the finance system be measured by the more exacting "strict scrutiny" test under the equal protection clause, and instead measured the system by the traditional "rational relationship" test. The Court accepted the state's contention that the objective of the classification was to preserve some amount of local control over school financing and that there was a rational relationship between the system and the objective.

The majority opinion was joined by five of the nine Justices. Justice Stewart wrote a brief concurring opinion that stressed the presumption of the validity of state legislative classifications when no "suspect" classification is involved. Justices Brennan and White, joined by Justice Douglas, dissented on the grounds that the Texas system of finance is invalid even when measured by the rational relationship test. Justice White's point is a telling one. He reasoned that it is not enough that the system seeks to achieve a constitutionally valid objective; the means chosen to reach that objective (the classification) must be rationally related to the objective. "Requiring the State to establish only that unequal treatment is in furtherance of a permissible goal, without also requiring the State to show that the means chosen to effectuate that goal are rationally related to its achievement, makes equal protection analysis no more than an empty gesture." The Texas system was simply not a rational means of achieving the goal of local financial control.

Justice Marshall, in a powerful dissent joined by Justice Douglas, stated that the Court's recently adopted practice of measuring equal protection cases by either a "strict scrutiny" or "rational relationship" test was simplistic and not supported by precedent. Justice Marshall stated, however, that some classifications did merit closer examination than others, and he would include classifications impinging on educational opportunity as among those requiring careful examination. He disagreed with the majority opinion that only discriminations against rights explicitly or implicitly guaranteed by the Constitution merited close scrutiny. The test should be, he said, the closeness of the connection between constitutional rights and nonconstitutional interests that make the effective exercise of those rights possible. If the connection is sufficiently close and strong, then any discrimination against the supporting interests must be carefully examined. In support of this position Justice Marshall cited *Skinner v. Oklahoma ex rel. Williamson*,[8] *Reynolds v. Sims*,[9] and *Griffin v. Illinois*.[10] He then pointed out that the quality of a citizen's education strongly influences the effectiveness with which he exercises his constitutionally guaranteed rights of free speech and participation in federal elections; the connection is sufficiently close to warrant a careful examination of any wealth classifications affecting educational opportunity. Justice Marshall further pointed out that not all of the wealth-classification cases have involved absolute denial of rights because of poverty. In *Griffin v. Illinois*, poor persons convicted of crimes could appeal their convictions, but the effectiveness of their appeals was diminished because they could not afford a copy of the trial transcript. Furthermore, contrary to the interpretation given in the majority opinion, the Court has struck down discriminations against districts and other political subdivisions when such discrimination affected the citizens living in those districts; see, for example, *Baker v. Carr*.[11]

8. 316 U.S. 535 (1942).
9. 377 U.S. 533 (1964).
10. 351 U.S. 12 (1956).

Alternative Responses

There are many alternative approaches—at least in theory—that a state might take in responding to *Serrano-Rodriguez* principles. Among them are three approaches that illustrate the basic methods of altering a system of school finance: district power equalizing; full state funding; and full state funding with 10 per cent local option.

District Power Equalizing. The essence of all district power equalizing[12] schemes is that each local school district is guaranteed that for a given tax rate, it will receive a given amount of money per student, regardless of its appraised property valuations. For example, the state might determine that for a tax rate of $0.60 per $100 appraised valuation per student, a district shall receive $360 per student; for a rate of $0.50, a district shall receive $300 per student; and for a rate of $0.40, $240 per student. In District A, if the $0.60 rate produces only $250 per student, the state must equalize District A in the amount of $110 per student.

In some district power equalizing models, wealthier units would be required to remit locally raised revenues to the state treasury. To continue our illustration, District A, for example, with a tax rate of $0.60 may actually produce $400 per student, $40 more than the state-mandated amount. Under *Serrano-Rodriguez* principles, District A may not retain this excess because that would recreate the wealth-based inequalities struck down in those cases. The logical procedure would be to remit this excess to the state treasury, from which it could be distributed to the poorer districts. In North Carolina, and prob-

11. 369 U.S. 186 (1962).
12. This model is thoroughly explained and illustrated in Coons, Clune, and Sugarman, *supra* note 5, beginning at page 201.

ably in several other states, this sort of arrangement for disposing of the excess is very likely unconstitutional. It appears to be in contravention of a fairly widely accepted principle of constitutional law that to tax one unit of local government for the benefit of another unit is a deprivation of property without due process of law. As a consequence, in states that follow this constitutional principle, district power equalizing schemes must be structured so that no district is required to give up any funds. One means of doing this is to select as the model unit for purposes of establishing the equalization scale a hypothetical district that is wealthier than the wealthiest unit in the state. For example, if the appraised valuation per student of the wealthiest unit is $100,000, the hypothetical unit on which the equalization scale is based could be set at $110,000 per student. The result of using this hypothetical, "super rich" unit as the guide unit is that all districts retain all locally raised funds.

A second problem with district power equalizing is that in the first years of establishment, it is very likely to create uncertainty in the state budgeting process. The state must know what tax rates each local district will choose before it can know the total amount of equalization funds that will be necessary, and it must have some idea of the amount of funds that will be available to equalize local units before it can set the maximum and minimum rates that the districts may charge. Hence, at least initially, there will be something of a circularity problem.

Furthermore, if a district power equalizing system is to be based on the property tax, there will need to be a thorough statewide equalization of property valuations for tax purposes. In every state with which I am familiar, the law requires property to be appraised at its market, or true, value. The unit doing the appraising is usually the county, or school district, or sometimes the township. Most states then permit the local taxing unit to apply to the market value an assessment ratio of anywhere from 20 to 100 per cent, so that the resulting *tax value* of property—or assessed valuation, as it is sometimes called—is only a fraction of market value. To speak of equalizing property values does not mean correcting different assessment ratios; that is a relatively easy matter. It refers, rather, to correcting for differences in the accuracy of appraisals in the local taxing units. For example, in unit A an appraisal survey might find that farm land is actually appraised at only 40 per cent of market value and residential property is appraised at only 65 per cent, while in unit B farm land is appraised at 60 per cent of market value, but residential property is appraised at 80 per cent. To implement a district equalizing scheme in such circumstances without first equalizing appraised property values would be to penalize those units with appraisals most nearly approaching market value and give a windfall to those units with appraisals at a low percentage of market value; such a system would quite likely be subject to attack on both due process and equal protection grounds.

In those states where district property wealth is not correlated with personal income, a way of avoiding the property valuation problem that has much to recommend it is to base the district power equalization scheme on an income tax rather than on the traditional property tax. This would require, however, either a multitude of local income taxes, with the many complexities that accompany an income tax, or some type of local surcharge or percentage checkoff on the state income tax in those states that have income taxes.

Full State Funding. In the response model that calls for full state funding, the state assumes responsibility for funding all educational expenditures. In this model, it will not do for the state simply to assume the share in each district now being funded from local sources, and thereby preserve existing inequalities. True, in such a situation, the funds available to each district would be a function of the wealth of the state as a whole, but it would be constitutionally indefensible for a state to perpetuate existing inequalities among the local units. Therefore, as a state begins to assume responsibility for all expenditures, it must begin equalizing those expenditures among the local units. This equalization entails serious political and fiscal problems. A state could, in theory, equalize down to the average district in terms of per pupil expenditures, or even down to the lowest spending unit. Such a leveling down would be politically impossible in most states, and it would certainly be educationally unsound. This leaves the possibility of equalizing up to some expenditure level. Leveling up of course means that the state will spend more on education than it has, and this will probably require an increase in some state taxes or the imposition of new taxes, especially in those states that do not now impose sales and income taxes. While these tax and expenditure increases are likely to be unpopular, keep in mind that there will be a concomitant decrease in local property taxes. The expenditure level to which a state will equalize will largely be a function of two factors, the disparity between the highest- and the lowest-spending districts, and the political feasibility of tapping new revenue sources. The New York State Commission on School Finance (Fleischmann Commission Report) recommended a leveling up to the sixtieth percentile for that state. A study done for North Carolina suggested that it would be feasible for North Carolina to equalize up to the ninetieth percentile.[13]

13. See Report on North Carolina School Finance: Responses to Serrano-Rodriguez 119–20 (Institute of Government, November, 1972).

A question related to the equalization problem is what should be done concerning the districts at or above the target level. One possibility is that they be frozen at their per-pupil expenditure levels for a selected base year, plus an annual increment of from 3 to 6 per cent to compensate for inflation, while the other districts are being leveled up to the target level and new allocation systems are being devised.

A second, related problem concerns the time period during which the equalization process is to take place. I believe that in most states a minimum of four years should be allowed, and in some states as much as six years may be needed. This time period is necessary to allow the gradual increase in taxes for the needed revenues, to allow the low-spending units time to work out means for effectively absorbing the increased funds, and to permit the state department of education or comparable agency time for planning and for working out new allocation formulas and cost adjustments.

Ten Per Cent Local Option. The third model for responding to *Serrano-Rodriguez* is really a variant of full state funding: full state funding with a 10 per cent local option. This model is exactly like full state funding except that local districts are permitted to supplement the state grant in an amount not to exceed 10 per cent of that grant. This local supplement would have to be raised entirely from local taxes and would not be equalized. This is the model recommended by the President's Commission on School Finance (the McElroy Commission). A note of caution is in order here. If the *Serrano-Rodriguez* principles are strictly applied, full state funding with an unequalized local option in any amount would be unconstitutional, for the funds available for education in each district would be a function of something other than the wealth of the state as a whole.

Cost Adjustments in State School Finance

Whatever model and variations are chosen for responding to *Serrano-Rodriguez*, a group of issues must be dealt with that may, for the sake of convenience, be grouped under the heading of cost adjustments. Cost adjustments are essentially techniques for recognizing the differences in the costs of educating various categories of children in different geographical locations across a state. A system of school finance will probably pass muster under *Serrano-Rodriguez* principles if it is not cost adjusted—that is, if it distributes funds equally on a per capita basis. But a system will not move toward the achievement of real equality, as distinguished from constitutionally measurable equality, until it takes account of the cost differentials of educating different types of students in different locations.

The Problem of Cost Adjusting. There are two sides to the cost adjustment problem—the cost side and the need side. On the cost side are the relatively easy to quantify cost differentials such as transportation, heating, and maintenance. The remaining cost differentials are more difficult to measure. There is, for example, the municipal overburden problem. This is usually defined as the problem created by the higher tax loads carried by municipalities for public services other than education. This extra load would probably need to be taken into account in any sort of district power equalization model where local revenue sources are to be used; I am uncertain about its relevance to a full state funding model. On the other hand, the municipal overburden problem may be an economic smokescreen for what is really a political issue. City dwellers who are paying higher taxes for fire and police services, for municipal auditoriums and public housing, and for paved streets and city parks are getting what they pay for. Non-city dwellers are not paying equivalent amounts for non-school services, but neither are they receiving those services. I mention this only to indicate that the question of municipal overburden deserves a great deal more analysis than it has heretofore received.

There can be no question that the cost of living varies from place to place, and that generally it is higher in urban than in rural areas. We need much more information on this matter than we now have. Furthermore, even the information we have, the standard cost of living indexes, is given by SMSA (Standard Metropolitan Statistical Area), so that it is of no help in measuring living costs for two or more school districts in the same SMSA. A third cost differential related in some ways to the cost of living problem is that school districts differ in attractiveness to teachers and administrative personnel. As a consequence, District B, for example, must pay more to hire a teacher with the qualifications it desires than District A. These attractiveness differences are extremely difficult to measure with any precision, but they certainly exist.

Turning to the need side of the picture, we see again that certain categories of students have educational needs that are relatively easy to quantify in terms of expenditure differentials. In this first group may be included students with speech and hearing problems and mentally retarded children. With regard to the education of retarded children, another judicial decision of which account must be taken is *Pennsylvania Association for Retarded Children v. Pennsylvania*.[14] In that case, the plaintiff alleged that Pennsylvania's public education system, to the extent that it did not provide access to a free public education for every educable and trainable retarded child in the Commonwealth, was a denial of equal protection of the laws under the Fourteenth Amendment. In a consent decree entered in the case, Pennsylvania agreed to provide a free public education

14. 334 F. Supp. 1257 (E.D. Pa. 1971).

for all educable and trainable retarded children between the ages of 6 and 21, and to provide an education to retarded children under 6 years of age in those districts offering free pre-school programs to other children.

A case from the District of Columbia, *Mills v. District of Columbia Board of Education*,[15] has made a similar order for the District schools. The *Mills* case contains a much fuller discussion of the constitutional principles involved than does the Pennsylvania case. Although it did not expressly articulate this view, the court seems to have held that education is a fundamental constitutional interest and that the exclusion of retarded children from educational offerings is an individious classification.

Suits making similar allegations have been filed in North Carolina and in other states. Should the principles announced in the Pennsylvania and District of Columbia cases become generally applicable in a state through either a federal or state court decision, more money would have to be made available for the education of retarded children. These additional funds would very likely have to come from state sources and would probably be allocated to regional centers in those areas with small numbers of eligible children. Since the Supreme Court has declined to accept the theory that education is a fundamental constitutional interest, the future of these cases, at least insofar as they are based on the Fourteenth Amendment, is very uncertain.

Other differences in expenditures to satisfy educational needs that are less easy to calculate than those discussed above are the varying costs of educating children in different grade levels and culturally deprived or disadvantaged children. Vocational education and music and studio art programs present a different set of problems. It should not be too difficult to calculate what such projects cost; instead, the problem in full state funding systems and in some types of district power equalization is how to determine which school districts are to get these programs and the level of funding for them.

Techniques for Cost Adjusting. The method of cost adjustment that has probably been most discussed is **pupil weighting.** In a pupil-weighting scheme, a weight of 1 is assigned to represent the "average" or "basic" child. Children in various grades, children in vocational programs, handicapped children, and educationally or culturally deprived children are then assigned weights indicating their degree of variance from the "basic" child. At least two pupil-weighting indexes are available as guides: the one devised by the National Educational Finance Project, and the one contained in New Jersey Assembly Bill 1271. A few examples will show some of the differences between these two indexes. For pre-school children, the N.E.F.P. index assigns a weight of 1.3; the New Jersey index assigns a weight of 0.75. For vocational students, N.E.F.P. assigns a weight of 1.8; New Jersey, a weight of 2.0. For disadvantaged children, N.E.F.P. assigns a weight of 2.0 (using a family income of $4,000 or less a year as the measure of disadvantage); New Jersey adds 0.75 for any student in disadvantaged circumstances (using receipt of aid to families with dependent children as the measure of disadvantage). The effect of the pupil-weighting scheme, of course, is to channel twice as much money for the education of the child with a weight of 2.0 as for the child with a weight of 1.0.

One advantage of pupil weighting, besides permitting cost adjustment, is said to be its respect for subsidiarity—local control of education. Through the use of weighting, full state funding of education should be possible without complete state control of the decision-making mechanism. A weighting index, if derived from actual cost and need data, should be reasonably objective, and it can be applied in a fashion that avoids substantial interference by state officials in the local budgetary process. All that needs to be done is to count the students in each of the weighting categories and compute a weighted total.

A disadvantage of the student-weighting scheme is that the weight to be assigned to each group of students is open to subjective bias and perhaps political tinkering. One can seldom be fully confident, for example, that the proper weight for factor X is 1.7 and not either 1.5 or 1.9, yet those small variations may significantly alter the distribution of funds. Before a pupil-weighting scheme is undertaken, careful thought should be given to the possibility that the weights could acquire, intentionally or otherwise, a subjective bias that would be very difficult to detect, much less rebut. There would be a substantial risk that important policy decisions might be hidden in the abstract weighting numbers, numbers that in themselves are not very informative, especially since the weights would have to be reviewed periodically to achieve needed flexibility and to reflect changed conditions affecting needs and costs.

A second cost-adjustment technique, **bloc weighting,** is a variant of pupil weighting that avoids some of the complexities of pupil weighting by compromising the accuracy of the cost adjustment. Rather than focusing on a set of often incalculable socio-economic characteristics, as pupil weighting does, the state might develop a mutually exclusive set of cost categories such that each school district could be assigned to a single bloc that roughly identified the magnitude of its cost problems. For example, categories might be established for urban districts with populations of 150,000 and over and for urban districts under 150,000. Similarly, suburban and rural school districts could be classified and weighted. The advantage of bloc weighting is, as stated, that it avoids the complexities of a more accurate student-

15. 348 F. Supp. 866 (D.C. 1972). This case is noted in 52 B.U.L. Rev. 884 (1972).

weighting plan. The categories selected are fully objective and not open to dispute. It oversimplifies the cost variables, but at the same time it emphasizes the policy content of the allocation decision. The disadvantage is the converse of the advantage: actual costs may be compensated in only a haphazard and partial fashion.

A third cost-adjustment technique is **budget approval**. In this method, actual school costs are justified to the state authorities, and approved actual costs are then reimbursed. Budget approval has the advantage of eliminating complex weight calculations and focuses attention instead on actual, justifiable costs. Under the budgetary approach, the state could establish guidelines and reimburse any amounts that fall within them. Budget approval would appear to be very useful in dealing with costs that can be easily and readily measured and do not vary greatly from year to year. Transportation and heating are examples. Once the budgetary approach is taken beyond these and similar items, however, it will involve the state much more heavily in the local budget process than might otherwise be thought necessary.

A fourth cost-adjustment technique that is responsive to the problem of differential needs is the **categorical grant** approach. This approach closely resembles the one taken by the federal government in its various categorical grants under the Elementary and Secondary Education Act of 1965. Grants could be made to local school districts for culturally disadvantaged children, for vocational education, for music and art programs, for children with learning disabilities, for gifted children, and so on. Presumably some sort of accounting system would have to be devised to ensure that the grants were being spent within state guidelines for the use of the beneficiary children.

Considerations in Responding to Serrano-Rodriguez Principles

Capital Expenditures, Debt Service, Federal Funds. In most discussions of *Serrano-Rodriguez*, attention centers on funds for current operating expenditures, because that is where most of the money goes. Nothing in the *Serrano* and *Rodriguez* opinions, however, indicates that capital expenditures are to be excluded from consideration. Also, a realistic look at school operations leads to the conclusion that the level of funds available for buildings and equipment substantially affects the quality of educational offerings. Therefore, it is a good assumption that any system of school finance purporting to respond to *Serrano-Rodriguez*—whether it be full state funding, district power equalizing, or some other method—must include funds for capital outlay as well as for current operating expenditures. The matter of local bonded indebtedness is more uncertain. The cases make no mention of what must be done concerning debt service, and unless the decisions are to be given retroactive effect, it seems likely that a state may leave outstanding bonded indebtedness to be paid off by the local districts with unequalized local revenues. Of course a state could pay off the bonds of local districts with some type of grant system, or it could equalize the local funds for this purpose through a district power equalizing system.

In most states the largest portions of federal funds have come to the local units either through Title I of the Elementary and Secondary Education Act of 1965 or through impacted-area programs. The continuation of some of these programs is in considerable question, but in any event, both the Title I[16] and the impacted-area statutes[17] require that federal funds be excluded from consideration in allocating state aid to local school districts. Thus, for purposes of devising a response to *Serrano-Rodriguez,* a state must not give weight to federal funds going to the local districts through the major federal programs.

On the matter of federal funds, the pending suit of *Downs v. Marlin,* No. 7396–B, in the federal district court for the Western District of Kentucky, requires mention. The plaintiffs in that case are challenging the constitutionality of the Title I allocation formula whereby for disadvantaged children the state may elect to receive amounts based on either the state average per-pupil expenditure or the national average, whichever is higher. The result of this formula is that states with per-pupil expenditures above the national average have more to spend than those below it, which latter group includes the Commonwealth of Kentucky. The challenge in *Downs* seems to be based on two theories. First, the plaintiffs allege that 33 per cent of the funds available for education in Kentucky are from local sources, primarily the local property tax. Thus the allocation of federal funds is tied in part to the wealth of the state, wealth measured in terms of appraised property values. The plaintiffs allege (1) that this link to property values is similar to the wealth classification impinging upon a fundamental constitutional interest—education—that was struck down in *Serrano,* and (2) that the incorporation of such a classification in a federal statute violates the due process clause of the Fifth Amendment (in the Fifth Amendment, the equal protection guarantee is not expressed, but has been implied in the due process language).

The second theory of attack is that the purpose of Title I is to improve the education of disadvantaged children wherever they happen to live; a system that gives more money to some disadvantaged children based on the average per-pupil expenditure in the state is simply irrational.

16. See 20 U.S.C. sec. 241g(c)(1).
17. See 20 U.S.C. sec. 240(d)(2).

Both contentions appear to have merit. In view of the reversal of *Rodriguez*, the plaintiffs' chances of success in *Downs* seem quite dim. The consequences of a victory for the plaintiffs—should they win—are anyone's guess. It may be that in the near future categorical grants will be largely replaced by revenue-sharing, which will not be tied to an allocation formula similar to that in Title I.

School Desegregation. Several other recent judicial decisions and trends that bear on school finance will need to be taken into account in devising new financing systems. Two of these cases involve school desegregation decisions affecting more than one political subdivision of the state, with the enormous financing problems attendant thereon. The two series of decisions on this point involve the school systems in Richmond, Virginia, and Detroit, Michigan. In the Richmond case, *Bradley v. School Board of Richmond*,[18] the federal district court ordered the consolidation of the Richmond school system with that of two suburban counties for the purpose of achieving better racial balance throughout the consolidated system. The Fourth Circuit Court of Appeals reversed this decision, and the Supreme Court, in a 4–4 decision, affirmed the reversal.[19] In the Detroit case, *Bradley v. Milliken*,[20] the federal district court found that the schools of Detroit were segregated and that the segregation was *de jure* (that is, that it resulted from official action) rather than *de facto*.

This is a critical finding and is of great importance to northern and western states that have not had segregated school systems deliberately created by statute. The court further ruled that the Detroit metropolitan area—including Detroit and two suburban counties, involving 86 school districts—was the appropriate geographical area for the development of a desegregation plan. Thus, the court did not go as far as the Virginia court in actually ordering consolidation. This decision was affirmed by the Sixth Circuit Court of Appeals.

The financing problems created by these decisions are not difficult to imagine. The following quotation from the Court of Appeals decision in the Richmond case contains a good summary:

> But even if we were to ignore Virginia law, as we are urged to do, there are practicalities of budgeting and finance that boggle the mind. Each of the three political subdivisions involved here has a separate tax base and a separate and distinct electorate. The school board of the consolidated district would have to look to three separate governing bodies for approval and support of school budgets.[21]

The problem of several different tax bases and assessment practices within a single school district would very likely create serious inequalities; furthermore, in the Richmond case, as would be true in North Carolina, the school board did not have tax-levying authority and would have had to look to several different governing boards for tax levies.

In these desegregation cases, if the local property tax is to be relied on as an element in the school finance system, it would appear that at least two steps must be taken to solve the budgeting and finance problems. First, a complete reappraisal of property throughout the school district would be necessary. Second, the district would have to be given tax-levying authority for all property in the district. Under existing finance systems and under district power equalizing schemes these actions would be necessary; under full state funding, of course, different tax bases would not be significant and tax-levying authority would be unnecessary.

Student Fees. Another group of judicial decisions affecting school finance are those regarding payment of fees by students for certain materials and services. These decisions turn on language in state constitutions that typically requires the legislature to provide a "free and uniform" system of public education, or a "thorough, efficient, and free" system of public schools. In at least three cases decided in the past three years many of these fees have been struck down as unconstitutional.

In an Idaho case, *Paulson v. Minidoka County School District*,[22] the Idaho Supreme Court held that under Article IX, section 1, of the Idaho constitution, which required the legislature to establish and maintain "a general, uniform and thorough system of public, free common schools," a school district could not withhold a student's transcript because he had not paid his textbook fees. The court stated that the use of textbooks was an essential part of a "free" public school system, and that fees could not properly be charged for books. The court also stated, however, that fees charged for various extracurricular activities were constitutional.

In a Michigan case, *Bond v. Ann Arbor School District*,[23] the Michigan Supreme Court found that the following student fees violated a Michigan constitutional provision requiring the legislature to "maintain and support a system of free public elementary and secondary schools:" general activity fees; fees for textbooks and supplies; fees for materials in shop, home economics, and art courses; and interscholastic

18. 338 F. Supp. 67 (E.D. Va. 1972), *rev'd* 462 F.2d 1058 (4th Cir. 1972).

19. School Board v. State Board of Education, 36 L.Ed.2d 771 (1973).

20. 345 F. Supp. 914 (E.D. Mich. 1972), *aff'd* 42 U.S.L.W. 2022, June 12, 1973 (6th Cir.), *cert. granted*, 42 U.S.L.W. 3306 (Nov. 19, 1973).

21. 492 F.2d 1058 at 1068.

22. 93 Idaho 469, 463 P.2d 935 (1970).

23. 383 Mich. 693, 178 N.W.2d 484 (1970).

athletic fees. The court stated that as a general rule a school district may not charge fees for any programs that are "necessary elements of any school's activity."

In the most recent case, *Granger v. Cascade County School District*,[24] from Montana, the principles of the *Paulson* and *Bond* cases have been broadened to a certain extent. In *Granger*, the plaintiff had challenged the imposition of student fees by the defendant school district on the ground that such fees violated Article X, section 1, of the Montana constitution, which required the legislature to maintain a "general, uniform and thorough system of public, free, common schools." The trial court held that in those situations involving fees for required courses—such as workbooks, towel fees for physical education, field trip fees, and fees for current events magazines—the charges were constitutionally invalid. The court further held, however, that reasonable fees could be charged for elective courses and extracurricular activities—such as rental of musical instruments, typing fees, and fees for shop materials. The Montana Supreme Court stated that the trial court had incorrectly formulated the legal test to be employed in fee cases in that its test did not adequately deal with high school courses that, though not required, counted toward credit for graduation. The supreme court phrased the applicable test as follows: "Is a given course or activity reasonably related to a recognized academic and educational goal of the particular school system?" If it is, no fees may be charged. The court stated that the initial determination of educational goals should be made by the school district.

A case related to the student fee cases is *Johnson v. New York State Education Department*.[25] In that case, suit was brought challenging New York's practice of furnishing free textbooks to children in grades 7–12, but leaving children in grades 1–6 to furnish their own textbooks unless the local school district vote to provide the books. The plaintiffs alleged that this arrangement denied children in grades 1–6 equal protection of the laws as guaranteed by the Fourteenth Amendment. The Court of Appeals for the Second Circuit upheld dismissal of the suit. The Supreme Court granted certiorari and then remanded the case to the district court after learning that the school district involved in the case had voted to provide free textbooks to students in grades 1–6. Thus, we still have no definitive answer on whether schemes like New York's, offering certain services to children in some grades but not in others, are constitutional.

The trend in the student fee cases, if there is one, is toward striking down fees for courses that are "necessary elements of a school's activity"—or, in the words of the Montana Court, "reasonably related to an educational goal of the school system." In states that are engaged in devising responses to *Serrano-Rodriguez*, or that may soon be so engaged, a careful examination should be made of all student fees with a view to removing those that do not clearly fall in the nonessential educational activity category.

In summary, the following trends and developments seem evident in the judicial decisions discussed in this article, in legislative proposals, and in several recent commission reports. First, education is increasingly regarded as a state rather than a local function. Second, educational opportunities should be made available on a reasonably equal basis to all who can benefit from them. Third, no child should be denied educational opportunities available to other children in the state because of the relative poverty of his family or school district. Finally, an effort is under way to sever the connection between funds available for education and the local property tax.

24. 499 P.2d 780 (Mont. 1972).

25. 449 F.2d 871 (2nd Cir. 1971), *vacated and remanded*, 34 L.Ed2d 290 (1972).

Geographic Distribution of Political Party Strength, 1972 General Election

H. Rutherford Turnbull, III, and James C. Drennan

The November 1972 general election statistics are presented in detail in the December 1972 issue of *Popular Government*. With these statistics as a starting point, this article will attempt to show, by the use of maps illustrating the results of the more important races, the geographic distribution of political party strength in North Carolina in the general election of November 1972. All maps are based on figures contained in the certified results as published in *North Carolina Elections, 1972*, issued by the Secretary of State.

While the caveats about the use of statistics issued in the December 1972 issue of *Popular Government* apply with equal force to this article, several other more specific limitations about the use of political maps should also be mentioned here.

First, many State Senate and House of Representatives districts are multi-membered. That is, more than one representative is elected from the same legislative district, and, typically, representatives are elected in those districts from both parties. The maps showing the geographic distribution of members of the present General Assembly have legends and shadings indicating the various combinations represented. The split delegations, however, may vary within the same category (Split Delegation: Democratic Majority) from 5 Democrats–1 Republican (15th House District) to 2 Democrats–1 Republican (33rd House District). As the example indicates, the relative strength of a political party within one particular category can vary greatly from place to place and still be portrayed as uniform on the map.

Second, the map showing areas represented by the Republicans and Democrats in the U. S. House of Representatives also can be misleading if it is not properly explained. The fact that a man represents a certain county in the House does not necessarily mean that the county gave him a majority of its votes; congressional districts represent another type of district that can also be misleading in determining geographic strength of a party—the multi-county, single-member district. An example of the misleading features inherent in mapping the election result in this type of district occurs in the Fourth Congressional District. Both Wake and Randolph counties gave the Republican congressional candidate significant majorities, yet the Democratic candidate was elected because he received slightly higher Democratic majorities in Chatham and Durham counties. The map does not distinguish this situation from the situation found in the Third Congressional District, where the Democratic candidate was unopposed. This imprecision can be abated by the use of the chart on page 17, indicating which party received a majority in each county in the 1972 congressional elections.

Third, and most important, the maps do not show the size of the majorities in any particular county. Many of the counties gave a statewide candidate an extremely narrow margin of victory (e.g., Montgomery County, where gubernatorial candidate Bowles received 3,382 votes and his opponent, Holshouser, received 3,353, a difference of 29 votes). In contrast, the Orange County vote for Democratic senatorial candidate Galifianakis was 16,348 while Republican candidate Helms received 7,759. On the map, both examples are simply shown as a Democratic majority in the particular county, but the disparity is apparent and cannot be avoided. The nu-

Chart of How Counties Voted in 1972 by Party

	% Registered		President		U.S. Senate		U.S. House of Rep.		Governor		N.C. Senate		N.C. House of Rep.	
	D	R	D	R	D	R	D	R	D	R	D	R	D	R
Alamance	75	19		X		X	X			X	X		X	
Alexander	52	40		X		X		X		X		X	X	X
Alleghany	67	31		X		X		X		X	X			X
Anson	92	6	X		X		X		X		X		X	
Ashe	54	43		X		X		X		X	X			X
Avery	25	74		X		X		X		X		X		X
Beaufort	87	11		X		X	X		X		X		X	
Bertie	96	3	X		X		X		X		X		X	
Bladen	93	6		X		X	X		X		X		X	
Brunswick	78	21		X		X	X			X	X			X
Buncombe	71	26	X		X		X			X	X		X	
Burke	62	33		X		X		X		X		X		X
Cabarrus	68	29		X		X		X		X	X		X	
Caldwell	54	40		X		X		X		X		X		X
Camden	95	4	X		X		X		X		X		X	
Carteret	68	28		X		X	X		X		X		X	
Caswell	93	6		X	X		X		X		X		X	
Catawba	58	34		X		X		X		X		X		X
Chatham	76	23		X	X		X		X		X		X	
Cherokee	53	41		X	X		X		X		X		X	
Chowan	92	7		X	X		X		X		X		X	
Clay	53	42		X		X		X		X		X		X
Cleveland	83	14		X		X		X	X		X		X	
Columbus	91	8		X	X		X		X		X		X	
Craven	85	13		X		X	X		X		X		X	
Cumberland	80	14		X		X	X		X		X		X	
Currituck	95	3		X	X		X		X		X		X	
Dare	83	15		X		X	X		X		X		X	
Davidson	60	35		X		X		X		X		X		X
Davie	43	53		X		X		X		X		X		X
Duplin	88	10		X		X	X		X		X		X	
Durham	81	15		X	X		X		X		X		X	
Edgecombe	88	10		X	X		X		X		X		X	
Forsyth	72	26		X	X			X		X		X		X
Franklin	92	7		X		X	X		X		X		X	
Gaston	71	24		X		X		X		X	X		X	
Gates	97	2		X	X		X		X		X		X	
Graham	57	39		X		X	X			X		X		X
Granville	95	4		X		X	X		X		X		X	
Greene	90	9		X		X	X		X		X		X	
Guilford	69	25		X	X		X		X		X		X	
Halifax	95	4		X		X	X		X		X		X	
Harnett	80	18		X		X	X			X	X		X	
Haywood	76	22		X	X		X		X			X	X	
Henderson	49	47		X		X	X			X		X		X
Hertford	95	4		X	X		X		X		X		X	
Hoke	92	6		X	X		X		X		X		X	
Hyde	91	7		X		X	X		X		X		X	
Iredell	72	24		X		X		X		X		X	X	X
Jackson	65	31		X	X		X		X			X	X	

	% Registered		President		U.S. Senate		U.S. House of Rep.		Governor		N.C. Senate		N.C. House of Rep.	
	D	R	D	R	D	R	D	R	D	R	D	R	D	R
Johnston	84	15		x		x	x			x		x	x	
Jones	91	7		x	x		x		x		x		x	
Lee	85	12		x		x	x		x		x		x	
Lenoir	85	13		x		x	x		x		x		x	
Lincoln	66	29		x		x		x		x	x		x	
Macon	63	34		x		x	x			x		x		x
Madison	62	36		x	x		x		x		x		x	
Martin	95	4		x		x	x		x		x		x	
McDowell	71	26		x		x	x			x	x		x	
Mecklenburg	67	28		x		x		x		x	x			x
Mitchell	29	71		x		x		x		x		x		x
Montgomery	71	26		x		x		x	x		x		x	
Moore	64	32		x		x		x		x	x		x	
Nash	83	14		x		x	x		x		x		x	
New Hanover	72	24		x		x	x			x	x	x	x	x
Northampton	99	1	x		x		x		x		x		x	
Onslow	82	14		x		x	x		x		x		x	
Orange	79	14	x		x		x		x		x		x	
Pamlico	87	12		x	x		x		x		x		x	
Pasquotank	89	8		x	x		x		x		x		x	
Pender	89	9		x		x	x		x			x		x
Perquimans	88	11		x	x		x		x		x		x	
Person	91	8		x		x	x		x		x		x	
Pitt	84	13		x		x	x		x		x		x	
Polk	59	35		x		x	x			x		x	x	
Randolph	49	46		x		x		x		x	x			x
Richmond	94	5		x	x			x	x		x		x	
Robeson	95	4		x	x		x		x		x		x	
Rockingham	80	16		x	x		x			x	x		x	
Rowan	62	34		x		x		x		x		x		x
Rutherford	75	24		x		x	x			x	x		x	
Sampson	62	36		x		x	x			x		x	x	
Scotland	91	6		x	x			x	x		x		x	
Stanly	58	36		x		x		x		x	x		x	
Stokes	60	38		x		x		x		x	x			x
Surry	62	35		x		x		x		x	x			x
Swain	70	28		x	x		x		x			x	x	
Transylvania	59	33		x		x	x			x		x	x	
Tyrrell	96	4		x	x		x		x		x		x	
Union	82	16		x		x	x		x		x		x	
Vance	91	7		x		x	x		x		x		x	
Wake	76	19		x		x		x		x	x		x	
Warren	92	7		x		x	x		x		x		x	
Washington	92	7		x	x		x		x		x		x	
Watauga	55	39		x		x		x		x		x		x
Wayne	82	16		x		x	x		x		x		x	
Wilkes	41	56		x		x		x		x		x		x
Wilson	85	14		x		x	x		x		x		x	
Yadkin	38	57		x		x		x		x		x		x
Yancey	60	37		x	x		x		x		x		x	
TOTALS	95	5	2	98	33	67	69	31	57	43	74	27	76	27

The North Carolina General Assembly (Senate and House of Representatives) is largely composed of multi-member districts. As a result, it is difficult to graph the vote by party and county. Thus, with respect to the N. C. Senate and House, the chart represents the party of the representative(s) from the district of which the county may be only a part. Where the delegation is split, but one party has a majority, only the majority party is checked. Where the split is even, both parties are checked.

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merical totals by counties for all statewide elections are found in the December, 1972 issue of *Popular Government*.

Thus forewarned, the reader is invited to examine the following maps (in addition to a chart showing how each county voted in the presidential, senatorial, congressional, gubernatorial, and General Assembly races) to determine where and for what reasons the geographic strength of each party lies. The first two maps show the county, by party, of the candidate who received the majority votes in the races for office of Governor and United States senator. The other three maps illustrate—by legislative districts and thus by geographic area—the distribution of political party strength in the U. S. House of Representatives and the North Carolina Senate and House of Representatives. No map illustrating the presidential election in North Carolina is included because of the extreme onesidedness of the results. Only Orange and Northampton gave the Democratic candidate, Senator McGovern, a majority, while President Nixon received a majority in the remaining 98 counties.

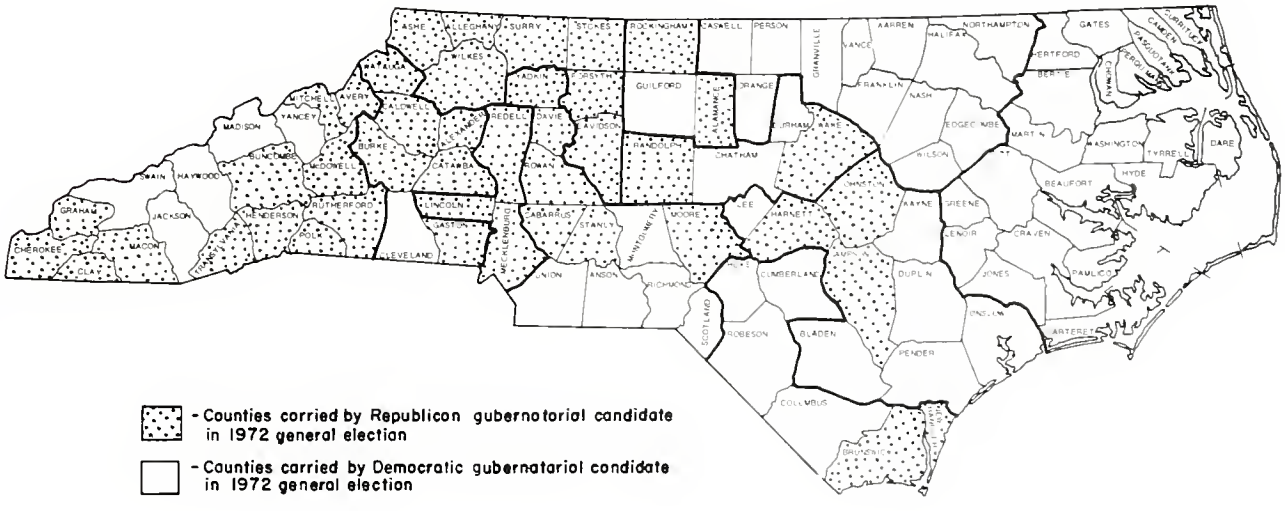
Drawing inferences from these maps is a risky intellectual endeavor in light of all the variables involved in any election. One of the more obvious problems in determining where party strength lies is the difficulty in separating votes cast for the party and votes cast for the candidate of the party.

In 1973, a United States senator and a Governor were elected from the Republican party for the first time since 1896. The degree of support for each Republican victor ranged from 98 county Republican majorities in the Presidential election, to 67 in the senatorial race, to 43 in the gubernatorial election. The evident difference is that Senator Helms fared much better as a Republican in the eastern half of the state than did Governor Holshouser, while Holshouser did slightly better in terms of the number of western and central counties in which he received a majority. This fact must be considered in any attempt to evaluate the maps in terms of whether an area is "Democratic" or "Republican."

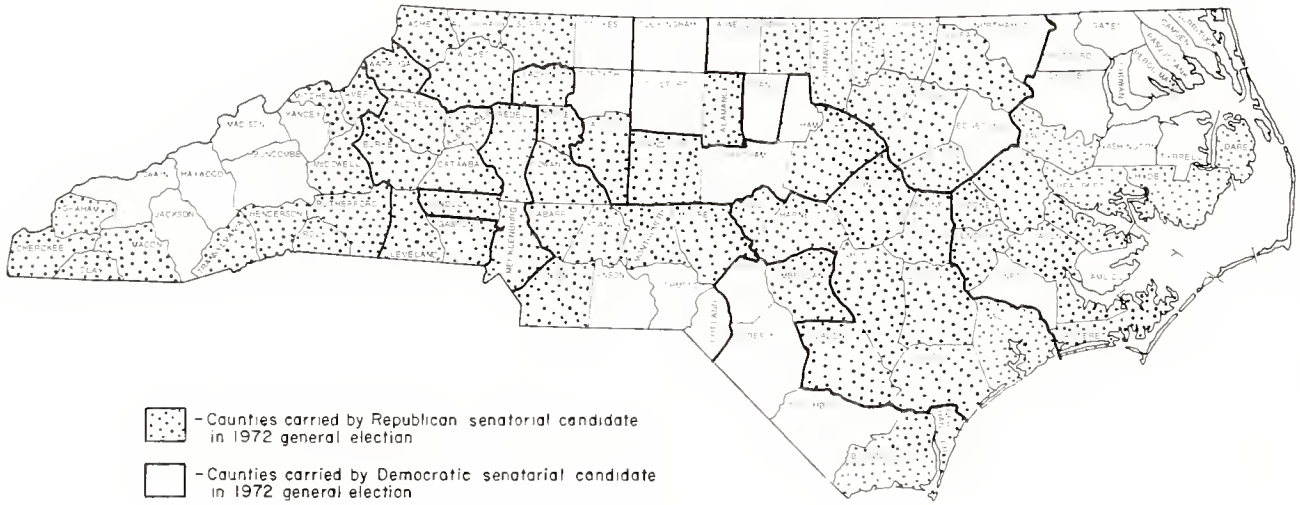
Nevertheless, an obvious conclusion to be drawn from the maps is the presence of Democratic strength in the eastern counties and the presence of Republican strength in the northwest portion of the state. These two facts are easily verified by the cumulative results of all the maps.

Finally, the maps illustrate that the urban areas of the state, at least in 1972, all had some element of two-party politics. All the larger counties in the state except Durham, which appears solidly Democratic on all the maps, appear in at least one of the maps as having voted for or being represented by Republicans. Similarly, all the larger cities appear on one or more of the maps as being represented by or giving a majority vote to Democrats. The larger cities include Charlotte (Mecklenburg), Winston-Salem (Forsyth), Greensboro (Guilford), Wilmington (New Hanover), Asheville (Buncombe), and Durham (Durham).

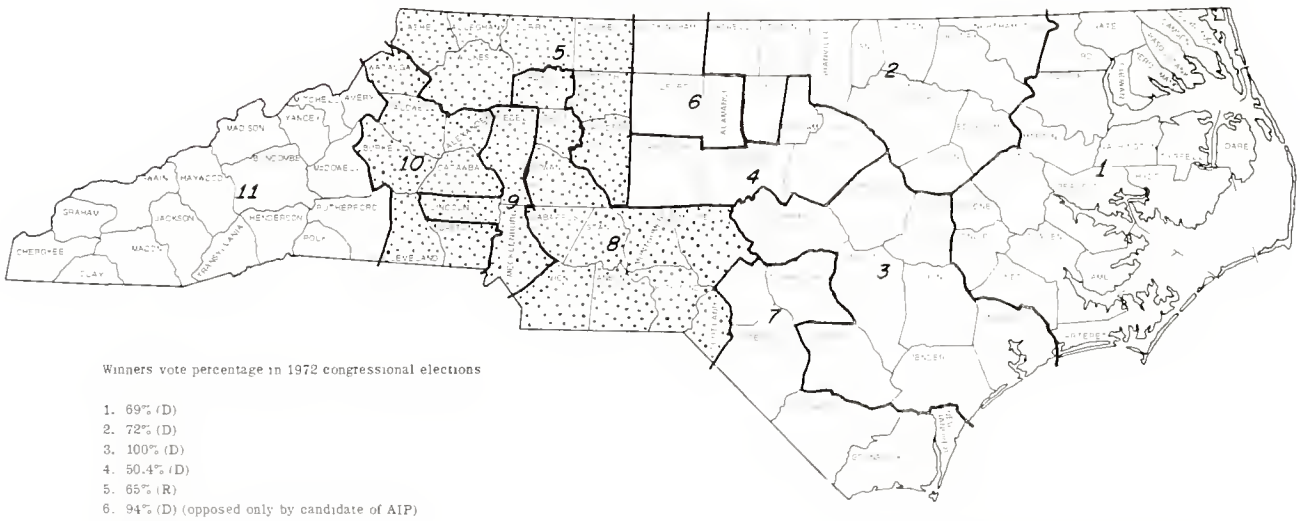
Geographic Distribution of Political Party Strength as Reflected in the 1972 Gubernatorial Election



Geographic Distribution of Political Party Strength in North Carolina
as Reflected in the 1972 United States Senatorial Election



GEOGRAPHIC DISTRIBUTION OF POLITICAL PARTY
STRENGTH AS REFLECTED IN NORTH CAROLINA CONGRESSIONAL DISTRICTS

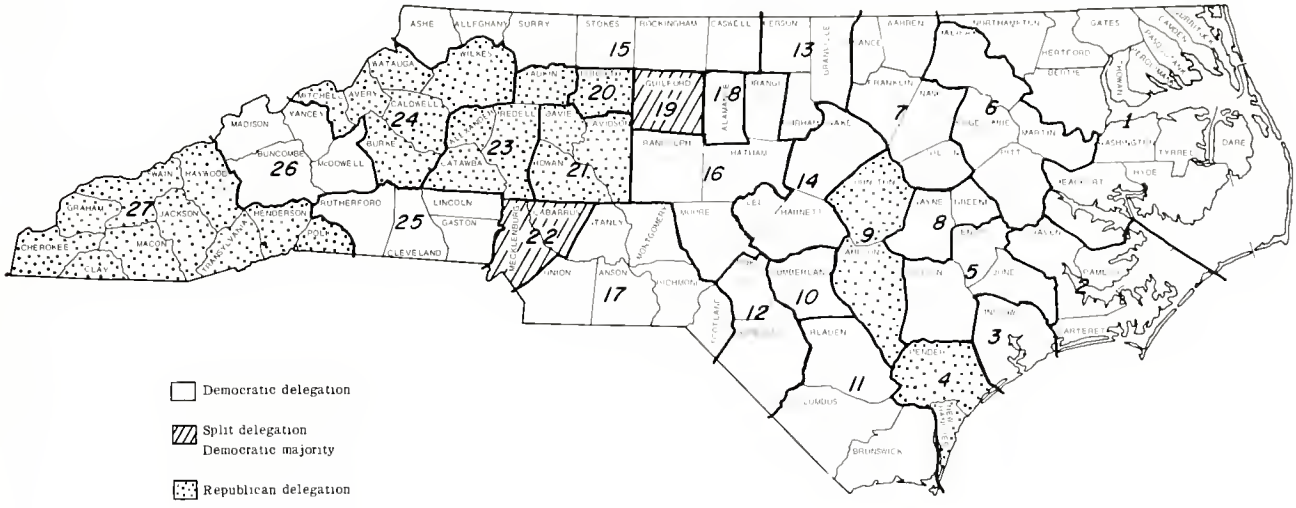


Winners vote percentage in 1972 congressional elections

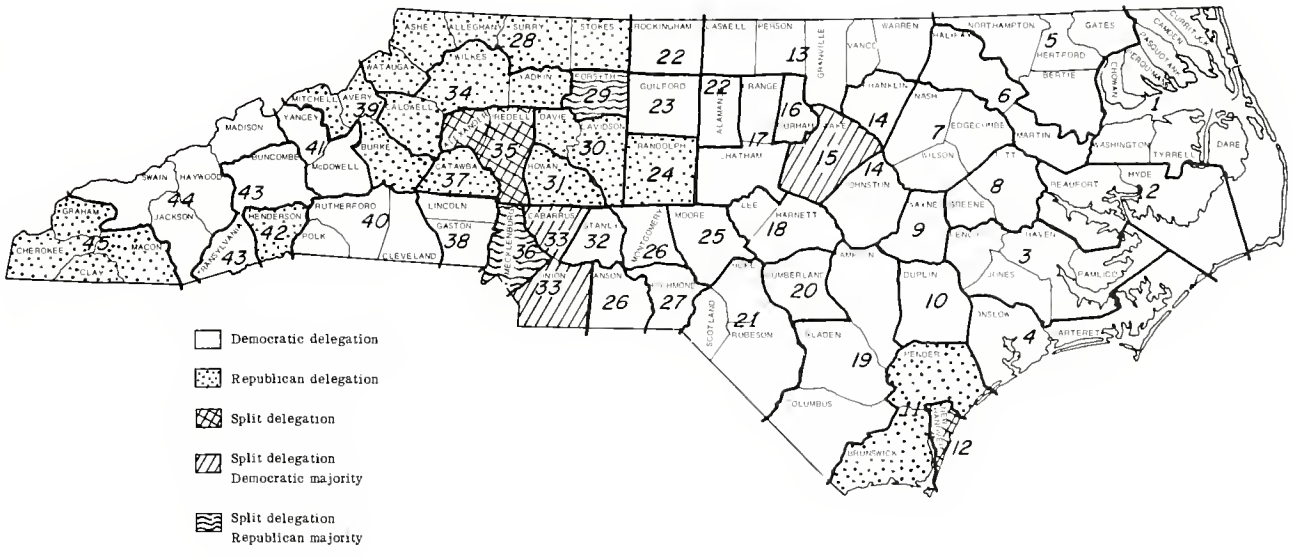
1. 69% (D)
2. 72% (D)
3. 100% (D)
4. 50.4% (D)
5. 65% (R)
6. 94% (D) (opposed only by candidate of AIP)
7. 60% (D)
8. 60% (R)
9. 59% (R)
10. 73% (R)
11. 59% (D)

- Area represented by democratic congressman
- Area represented by republican congressman

GEOGRAPHIC DISTRIBUTION OF POLITICAL PARTY
REPRESENTATION IN NORTH CAROLINA SENATE



GEOGRAPHIC DISTRIBUTION OF POLITICAL PARTY
REPRESENTATION IN NORTH CAROLINA HOUSE OF REPRESENTATIVES



THE RECURRING

For many years the state's General Fund reve amounts. Why do these surpluses occur each or legal requirements? Are they necessary for

C. Donald Liner, who is a member of the Institute of Government faculty and holds a Ph.D. in Economics from Washington University in St. Louis, argues that large perennial surpluses are not required for sound fiscal management and that budget policies should be made more flexible in order to permit full use of the state's resources.

THE EXECUTIVE BUDGET ACT, which establishes specific procedures for preparation, review, adoption, and execution of the North Carolina state budget, was designed to insure that no deficit will occur in the state's current operating budget. During the past four decades the Act has served this purpose very well: the state has not had a biennial operating deficit in the General Fund since the depression years of the early 1930s. On the contrary, in most biennia the state has collected much more revenue than necessary to cover expenditures for current operations.

The record of annual current operating surpluses and deficits appears in Table 1 (p. 27). A current operating surplus is the excess of revenues collected in any one year over the operating expenditures during the same year. A current operating deficit, which means that the state spent more for operations in a given year than it collected in revenue, does not indicate that the state was "living beyond its means," but rather that surplus funds collected in previous years were spent. When surplus funds are expended in the following biennium for operations and capital improvements, the current deficits can be quite large. The last column of Table 1 gives some indication of current surpluses and deficits after capital improvements appropriations are accounted for, but the figures shown are not the exact amounts, since not all capital improvement appropriations are expended during the first year of the biennium.

Despite the fact that current surpluses are spent partly for operations in subsequent years, the current operating surpluses have been large in most years, consistently so since 1961–62. For example, even the relatively small surplus of 1967–68 was larger than the combined amounts spent in 1967–68 for the judiciary system, public safety and regulation, and the corrections system. For the past ten years the current operating surpluses have averaged 5.2 per cent of revenues collected. In the fiscal year 1972–73 the surplus equaled 7.4 per cent of revenues collected, and an additional $58 million was received in federal revenue-sharing funds.

Surplus funds that have accumulated during each biennium have been invested in interest-bearing securities by the State Treasurer and have been appropriated by the General Assembly in the following biennium. In earlier years surplus funds were usually appropriated for operating expenses, but since the early 1960s there has been a tendency to appropriate a large proportion of surplus funds for capital improvements. Since 1960 the operating surpluses have financed more than a third of a billion dollars in capital improvements. The remainder of the surplus funds has been appropriated for current operations in the following biennia.

The estimated General Fund surplus of $323,104,000 that had accumulated by the end of the

(Continued on Page 27)

STATE SURPLUS

ues have exceeded expenditures by significant ear? Are they necessary to meet constitutional ound fiscal management?

Edwin Gill, the State Treasurer, points out that North Carolina's fiscal policies arose as a means of re-establishing a sound financial position during the Great Depression. He explains that the surpluses have resulted from an expanded economy and cannot necessarily be counted on. He maintains that in view of today's economic uncertainities, to change the state's budgeting practices would jeopardize its fiscal integrity.

I AM INDEBTED to the editor of *Popular Government* for the invitation to comment on an article by Dr. C. D. Liner, which is published elsewhere in this issue. With due deference to Dr. Liner, who has written well on various phases of State government, I must dissent from some of his assumptions and the opinions that he has expressed in this article. And, although I may differ sharply with Dr. Liner's views, I wish to make it clear that the differences between us are philosophical and not personal.

While I do not look upon this invitation as a forum for an exhaustive debate on the subject of State finance, I am always pleased to express my views on sound fiscal management in State and local government and, in passing, to reaffirm my contention that *In North Carolina, we have made a habit of good government.*

The State Treasurer is not officially a part of the budget process. Like other agencies, his office furnishes information requested by the Advisory Budget Commission and the Finance Committees of the House and Senate. On the other hand, the office of the Treasurer is an excellent vantage point to observe first hand the workings of the budget process. Being human, those who make revenue and expenditure estimates often make mistakes, and sometimes these errors are substantial. But, by and large, I admire the skill and the high motive with which this phase of the budget has been executed, and I believe that, notwithstanding the element of human error, the men who have constructed our budgets through the years have done a magnificent job. Their slogan could well be "Progress with Integrity."

FIRST OF ALL, I think that Dr. Liner has misunderstood the meaning of our Constitution, which must be read and construed as a whole. For instance, our Constitution clearly admonishes us against budget deficits. If there is one thing that our organic law is clear on, it is that our fiscal policy is based upon a balanced budget. Because the Constitution contains a provision for funding a deficit, Dr. Liner cites this provision as recognition of the *propriety* of deficits. The particular section of the Constitution that he cites, however, is intended to furnish a mechanism for funding a deficit that was not expected and for which the Advisory Budget Commission, the Appropriation Committees, or the General Assembly itself had not planned. Funding as used here means to borrow through the issuance of bonds or notes.

Our organic law contains not the slightest approval of deficit financing. In other words, it is unconstitutional to plan for a deficit. All the Constitution says is that, if the economy of the State should go into a sharp decline, despite whatever cuts may

be applied by the Governor as Chief Executive Officer of the State, and if it becomes necessary, a deficit may be funded. But nowhere does the Constitution *condone* the spirit of deficit financing.

In my opinion, the most significant action taken by the General Assembly in our time was the passage of the Executive Budget Act in 1925. Until then, the State's finances had not required very large sums of money; the State had not at that time become involved in such wide-ranging objectives as maintaining all state highways and also the public schools. As the financial problems of the State grew and became more complex, a more efficient means to deal with financial affairs was clearly necessary—hence, the Executive Budget Act of 1925, which introduced sound business principles into the handling of public funds.

Beginning in 1925, the idea of a balanced budget became a part of the thinking of the people of North Carolina. From then on, our legislature began to act in a practical and knowledgeable manner within the context of sound budget procedures.

In 1929, the crash came and the Governor at that time was faced with an unprecedented decline in the economy, with a consequent sharp decline in revenue. In short, we ran up substantial deficits in 1930, 1931, and 1932; and, despite the Governor's action in cutting appropriations, we were faced with a substantial deficit. *But this deficit was not planned nor in any way foreseen.* It arose because no one anticipated a depression; as revenues declined, tax anticipation notes were issued to meet current expenses, which were later funded under the emergency provision in the Constitution that gives us the right to fund a "casual deficit."

From 1933, our economy began to improve, and since 1939, when we adopted the permanent revenue act, our economy has grown and expanded far beyond the dreams of those who had merely predicted recovery. As a result of the growing economy, which has also been tinged with inflation, we have had a series of credit balances, which are popularly called surpluses. Some have been modest and others have been very substantial, and the General Assembly has appropriated these quite unexpected surplus funds to help meet the growing and expanded needs of the people of North Carolina. Part of these funds have been used in providing for current demands (such as increases in the salaries of teachers and state employees) and part for funding much-needed permanent improvements, thus avoiding the cost of borrowing in order to finance the improvements.

Let me emphasize, it is the changing economy, often growing beyond expectation, and the increased demands of public service, due in part to inflation, that have resulted in our surpluses and the uses to which they have been put.

I WANT TO MAKE one thing clear: I know of no Governor and no member of the Council of State or of the Advisory Budget Commission or of the General Assembly who has believed in taxing the people in order to build up large surplus funds. But I believe that once the surpluses have occurred, we have acted wisely in applying these unexpected funds for the benefit of our people.

The point I wish to underscore is that whatever mistakes have been made in estimating revenue were not intentional but were made in the context of a growing and expanding State, which was making a desperate effort to keep in step with the needs of all North Carolinians, as interpreted by the people, by the communications media, and by the General Assembly itself.

I MUST NOW COMMENT on Dr. Liner's use of the word *deficit*. He considers any year in the State's history in which the budget is balanced by bringing forward a credit balance from the previous year as a deficit year. To use this word in such a way, it seems to me, is inconsistent with sound finance and accounting. How can there be a deficit when the State has sufficient funds to meet every obligation involved in the budget?

Also, he speaks of a bond issue as being a *planned deficit*. He would consider that the recent authorization of our $300 million school plant construction bonds pushed the State into a deficit status. In my opinion, this completely distorts the word deficit as used in state and local financing throughout the nation.

What is deficit financing as generally understood in state and local finance? It means that a budget is *deliberately* constructed so that it will require spending beyond available revenues—which, of course, is forbidden by our Constitution.

Dr. Liner's article contains some rather confusing and contradictory terms. For instance, it says in one place that we have had surpluses every year since the depression, but then elsewhere that we have experienced many deficits in recent years. Manifestly, the State cannot have both a surplus and a deficit at the same time. Upon closer examination, we find that Dr. Liner has assigned deficit status to certain years because the budget was balanced in those years by carrying forward surpluses from the previous year. The methods used in thus balancing the budget are, in my opinion, entirely appropriate. Would he have us not use these extra funds, but levy additional taxes to cover expenses? Or, to put it another way, would he have us cut taxes and fail to meet current needs? Of course not. So when he talks of recent deficits, we know that he is simply applying a standard to certain years that does not conform to the accepted language of public finance. As Treasurer of North Carolina, I have emphasized over and over

again that we have had no deficits in the budget of North Carolina since the depression.

In his article, Dr. Liner uses the word *surplus* rather generally without particular definition. I think it might be wise, in discussing his statement, to point out that the word *surplus* does not appear upon the balance sheet of the State; its equivalent is what we term a *credit balance.*

IT IS A FAIR INFERENCE that Dr. Liner feels that often we have given too much emphasis to a good credit rating, and not enough to providing for the needs of our people. On behalf of all of the Governors that I have known and all the legislators that I have worked with, I beg to differ. Dr. Liner suggests that we may have deliberately built up surpluses purely for the benefit of a credit rating. On the contrary, the building up of the large surpluses has been unexpected; furthermore, we have used our good credit rating to save millions of dollars for taxpayers in the favorable interest rates that we have secured in a large program of bond financing over the years. We may not on occasion have done as much for our people as we would like to do, but I think we have made a sincere effort to aid them within the availability of funds. *No, we have not sacrificed the welfare of our people for a good credit rating; we have used that credit rating as a tool in the service of our people.*

Dr. Liner seems to question the earnings that the Treasurer receives from the investment of surplus funds. Apparently he feels that the people could better use these funds themselves. If his facts were correct, I would agree with him heartily, but he overlooked the fact that only a very small portion of the funds invested are surplus funds. What he refers to are "temporarily idle funds," meaning funds on hand to meet appropriation requirements previously committed by the General Assembly. In no way would it be correct to classify moneys appropriated as surplus funds.

The question naturally arises: Why not reduce taxes and thereby do away with so-called surpluses? The answer is that at the time the budget is constructed, we do not know how our economy will behave, and therefore we do not know whether there will be surplus funds. For many years we have had surpluses, *but now it seems that the wave may have reached its crest.* And in view of many disconcerting elements in our economy connected with the energy crisis, we may for the first time since the depression be faced with some decline in our revenue.

I think all informed people will agree with the famous statement *Ours is a government of laws and not of men*—which simply means that no public official can go about the people's business except in terms of existing laws. So, when surpluses begin to build up, the Governor cannot simply allocate these funds for this or that purpose. He must await the sitting of the General Assembly, which alone has the power, under our law, to appropriate these funds. It is the very nature of our government that we cannot take executive action in regard to any matter unless provision has been made by law.

The General Assembly, realizing that there may be unexpected developments between sessions, has created what is known as the Contingency and Emergency Fund ($2 million in 1973–74), from which the Governor and Council of State may make allocations for unexpected and unanticipated needs. But neither the Governor nor the Council of State has any authority between sessions to tamper with this thing that has been called a *surplus* in the General Fund.

IT IS HEALTHY from time to time for people like Dr. Liner to criticize us and take us to task. But still, I would like to point out that in his criticism, Dr. Liner occupies the enviable role of Monday-morning quarterback! He did not have to make decisions in the stress and strain of the day, but has had the advantage of studying all that we have done through the years. In other words, he has had the wonderful advantage of hindsight.

I recognize in the opinions of Dr. Liner the hallmark of a man steeped in the classical viewpoint of the economist, and I respect him as a scholar, but we who deal with the practical affairs of balancing the budget believe that we should conform to the precepts and practices that are customary in financial circles and validated by tradition. We think it would be wrong for the State to depart from this traditional viewpoint. For us to vary from the generally accepted practices would shock the financial world and leave the impression that we look with favor on the philosophy of deficit financing, which flourishes in Washington but not yet in Raleigh.

BEFORE CLOSING THIS PAPER, I would like to describe in simple language how the budget process has been practiced for many years here in North Carolina.

What do we mean by the balanced budget? The principle is so simple as to require no complex interpretation. We mean that the availability of funds and outgo are approximately the same, and that the only acceptable variation from this would be for availability to exceed outgo, so that there will at all times be a *margin of safety.*

Balancing the budget is not an exact science. It is very difficult to know just how the tax structure will react to the economic conditions of the year, or biennium, with which we are concerned. But it is interesting that, in line with our careful policy, we have had a credit balance, or surplus, in the General Fund at the end of every biennium since the depression of the 1930s. Some years this so-called surplus has been modest, but in others, it has been substantial.

These credit balances have been used by the General Assembly to balance the budget for the ensuing biennium. A good deal of it has gone into capital improvements that would otherwise have been delayed or built with borrowed money.

The recurrence of a substantial surplus in the various biennia of the last twenty years often leads to a demand for tax reductions, and on occasion some reduction has been given. In this connection, I think we should keep in mind that a credit balance of $150 million is not a large sum of money when set against our recent biennial budget, which exceeded $4 billion.

In fairness to members of the General Assembly, it could be said that when the budget is balanced, they do not anticipate that the credit balance will be as large as we have recently experienced. To be sure that we do not have a deficit, they think in terms of a reasonable *cushion*. A credit balance, for instance, that approaches $100 million or $200 million is quite unexpected—something of a windfall, resulting from an unexpected expansion and growth of the economy.

What to do with a substantial credit balance such as we are now expecting will provoke a lot of debate. But how much better it is to be worried about a surplus than for North Carolina to be worried about an imminent deficit. Those who remember the days of the Great Depression, when deficits were the order of the day, will testify that any trouble in deciding on what to do with extra funds is nothing compared with the stark tragedy of being forced to increase taxes on people who are already on the brink of disaster, as we were compelled to do in 1931, 1932, and 1933.

Last but not least, this is no time to experiment in fiscal policy. After a long period of prosperity, we now face a crisis that is closely related to the shortage of energy. There are predictions that in the immediate future, cutbacks will be made in industrial production—with some rise in unemployment and lower profits. If our economy should produce less revenue in the future, then this is a doubtful time in which to strike off in a new direction, attempting new and untried policies. If the General Assembly that convened in January should feel that some tax reduction can be given, that is within its prerogative, but I wish to emphasize that today is a difficult time to attempt fiscal prophecy. No man can predict with any degree of accuracy how our economy will behave in the next few years or, for that matter, for the next twelve months. Certainly this is a time for the people of North Carolina to assert the virtues of moderation, reason, and restraint for which they are justly famous.

Is it necessary to maintain a budget surplus? *(Continued from Page 22)*

1971–73 biennium was by far the largest biennial surplus in history, although about $58.4 million of the surplus came from federal revenue-sharing funds that could not have been anticipated by the 1971 General Assembly. The size of the 1971–73 biennial surplus is best demonstrated in Table 2, which shows biennial rather than annual surpluses for the General Fund since the 1961–63 biennium and also includes both operating and capital expenditures of the General Fund. Even without revenue-sharing funds, the 1971–73 surplus of $264,700,000 was much greater than the 1965–67 surplus of $172,680,000.

In view of the magnitude of the surpluses, several questions should be asked. Is a perennial budget surplus required by law? Is a surplus required for prudent fiscal management? How does it come about that an operating surplus occurs almost every year? Finally, what are the consequences of surpluses? The purpose of this article is to address these questions.

THE NORTH CAROLINA CONSTITUTION specifically provides for incurring debt in order "to supply an unforeseen deficiency in the revenue" (before July 1, 1973, the language was "to supply a casual deficit"). The Constitution, in addition to providing for unforeseen deficits, also provides for planned deficits through bond financing or other forms of indebtedness. These planned deficits must be used for specific public purposes that are approved by the General Assembly and usually also by a majority vote of the people. Public debt can be used "to suppress riots or insurrections, or to repel invasions," "to meet emergencies immediately threatening the public health or safety, as conclusively determined in writing by the Governor," or "for any other lawful purpose, to the extent of two-thirds of the amount by which the state's outstanding indebtedness shall have been reduced during the next preceding biennium."[1] If the debt should exceed two-thirds the debt reduction in the previous biennium, approval of a majority of voters is required before it may be incurred. The Constitution thus provides for debt financing of specific operating expenditures, roads, schools, and other capital improvements.

1. N.C. Const., art V, § 3.

Table 1

North Carolina State Operating Surplus and Capital Improvement Appropriations, Fiscal Years 1951–52 to 1972–73 (thousands of dollars)

Year	State Revenues[a]	Expenditures from State Revenues for Operations	Current Operating Surplus (Deficit) (Revenues less Expenditures)	Current Operating Surplus (Deficit) as Per Cent of Revenues	Capital Improvements Appropriations[b]	Current Operating Surplus (Deficit) less Capital Improvements Appropriations[c]
1951–52	$ 273,104	$ 261,315	$ 11,789	4.3%	3,635	$ 8,154
1952–53	280,671	279,266	1,405	0.5	—	1,405
1953–54	286,988	289,068	(–2,080)	(0.7)	5,166	(–7,240)
1954–55	297,659	311,823	(–14,164)	(4.8)	—	(–14,164)
1955–56	342,122	311,354	30,768	9.0	400	30,368
1956–57	359,714	343,145	16,569	4.6	—	16,569
1957–58	364,024	368,678	(–4,654)	(1.3)	29,953	(–34,607)
1958–59	382,205	379,494	2,711	0.7	—	2,711
1959–60	444,141	414,203	29,938	6.7	65	29,873
1960–61	465,421	435,300	30,121	6.5	—	30,121
1961–62	521,516	522,896	(–1,380)	(0.3)	3,968	(–5,348)
1962–63	570,535	525,232	45,303	7.9	—	45,303
1963–64	603,462	594,028	9,434	1.6	66,350	(–56,916)
1964–65	667,290	631,373	35,917	5.4	—	35,917
1965–66	760,863	699,794	61,069	8.0	45,333	15,736
1966–67	825,264	755,534	69,730	8.4	—	69,730
1967–68	893,629	855,704	37,925	4.2	116,702	(–78,777)
1968–69	1,006,994	950,834	56,160	5.6	—	56,160
1969–70	1,183,602	1,137,343	46,259	3.9	76,669	(–30,410)
1970–71	1,294,568	1,243,723	50,845	3.9	—	50,845
1971–72	1,442,397	1,383,531	58,866	4.1	69,794	(–10,928)
1972–73	1,631,831	1,510,463	121,368	7.4	—	121,368

Notes: a. Tax and non-tax revenues of the General Fund and Highway Fund. Does not include federal funds, bond proceeds, revenues of self-supporting activities, federal revenue sharing funds, or revenues of the Agricultural Fund, which was discontinued in 1965.

b. Excludes appropriations of bond proceeds and self-liquidating appropriations.

c. Since capital improvement appropriations are not necessarily expended during the year of appropriation, the figures in this column do not represent the actual current surplus or deficit.

Table 2

General Fund Revenues and Expenditures, 1961–63 Biennium to 1971–73 Biennium
(thousands of dollars)

Biennium	Beginning Surplus	Revenues	Surplus Plus Revenues	Operating and Capital Improvements Expenditures	Ending Surplus
1961–63	$ 74,356	$ 790,165	$ 864,521	$ 752,847	$111,674
1963–65	111,674	941,557a	1,053,231	953,552	99,679
1965–67	99,679	1,196,959	1,296,638	1,123,958	172,680
1967–69	172,680	1,455,265	1,627,945	1,474,609	153,336
1969–71	153,336	1,846,186	1,999,522	1,852,305	147,217
1971–73	147,217	2,411,632c	2,558,849	2,235,745b	323,104b, c 264,700b, d

Notes: a. Includes $12,007,219 transfer from a reserve for refund of income tax withheld.
b. Estimated.
c. Includes $58.4 million in federal revenue sharing funds received for 1971–73.
d. Excludes $58.4 million in federal revenue sharing funds received for 1971–73.

Between 1925 and 1946, the state paid for capital improvements almost entirely through incurrence of debt approved by the General Assembly under the two-thirds rule (so-called legislative bonds). Only $75,000 of $22.7 million spent for capital improvements was appropriated from current tax revenues during this period. From 1947 to 1970 the state made relatively less use of debt financing for capital improvements, preferring instead to finance such outlays from current revenue. During this period, of $790 million of capital improvement authorizations (excluding reappropriations, self-liquidations, and receipt-supported projects), about 60 per cent was financed by direct appropriations of current revenue. Since 1970 the state has increased its use of debt by authorizing a $150,000,000 issue of Clean Water bonds and a $300,000,000 issue of school bonds plus other issues totaling $48 million. However, the state has continued to use record amounts of current revenue to finance capital improvements. During the period 1971 to 1973, more than $258 million of current revenue was appropriated for capital improvements. This was far more than for any comparable period in the state's history.

The State Constitution provides that the Governor shall prepare and recommend to the General Assembly a comprehensive budget of anticipated revenue and proposed expenditures and that the budget as enacted by the General Assembly shall be administered by the Governor.[2] As mentioned above, the Executive Budget Act[3] establishes the specific procedures for preparation, review, adoption, and execution of the budget.[4] Whereas the Constitution provides for meeting an unforeseen deficit through the issuance of debt, the Executive Budget Act calls for rather drastic action to avoid a deficit. It declares that all "maintenance" (operating) appropriations are conditional upon having sufficient revenues "collected and available" to finance all operating appropriations.[5] If the Director of the Budget determines that revenue collections are insufficient, he may, with the advice and consent of a majority of the Advisory Budget Commission, reduce the amounts to be allocated to the various appropriations or reduce all appropriations on a pro rata basis in order "to prevent an overdraft or deficit."[6] The law is very clear in its intent:

> The purpose and policy of this act are to provide and insure that there shall be no overdraft or deficit in the general fund of the State at the end of the fiscal period growing out of appropriations for maintenance, and the Director of the Budget is directed and required to so administer this act as to prevent any such overdraft or deficit.[7]

Thus the Executive Budget Act, unlike the Constitution, requires a balanced operating budget. However, the General Assembly could, under the Constitution, provide for debt-financing of some operating expenditures. In its effect, the Executive Budget Act tends to result in budget surpluses, since the strong medicine prescribed to prevent deficits encourages overly cautious revenue estimates and lowered spending proposals. But the Executive Budget Act, despite its strong language, does not provide a justification for the large current operating surpluses that have occurred, and it is possible to provide more flexibility in state budgeting so that large surpluses and deficits could be avoided.

First, the provisions that call for reductions in appropriations in the event of insufficient revenue collections apply only to current operating ("maintenance") appropriations, not to capital appropria-

2. N.C. Const., art. III, § 5(3).
3. N.C. Gen. Stat. §§ 143–1 through –34.1.
4. Cf. J. Sanders, The North Carolina Executive Budget Act Topically Arranged (5th ed. Chapel Hill: Institute of Government, 1973).
5. N.C. Gen. Stat. § 143–25.
6. *Id.*
7. *Id.*

tions. In recent years, capital improvements appropriations financed by current revenues have been large enough to serve as an effective buffer if actual revenue collections should fall below projected revenue collections.[8] Capital improvement appropriations can be made on the basis of revenue projections, perhaps on a priority basis, and then the expenditure of funds can be made contingent on receipt of adequate revenue. Low-priority projects that must be delayed can be funded as soon as sufficient funds become available. In this way there would be less danger of having to cut back operating funds if revenue collections fall short of projections. Second, the operating appropriations that are not spent also serve as a buffer should revenue collections be lower than expected. These so-called reversions average 3.8 per cent of total General Fund appropriations. As a result of these operating appropriations that are not spent and the normal lag of expenditures (particularly capital expenditures) behind appropriations, the State Treasurer would usually be able to finance an unforeseen deficit from "collected and available" revenues. For example, on June 30, 1972, the State Treasurer held about $229 million in General Fund cash. Third, some operating appropriations can be made contingent on receipt of revenue collections. The General Assembly used this method in the 1950s, making increases in teachers' salaries contingent on receipt of a certain amount of revenues. These three measures—flexible capital expenditures timing, reliance on reversions as a buffer, and selected use of contingent operating appropriations—would provide flexibility in budgeting so that the total financial resources of the state could be used each year to provide needed public services.

HOW DOES IT COME ABOUT that large budget surpluses occur almost every year? There are two main reasons:

1. The legislature makes very cautious estimates of anticipated revenues, and the amount of appropriations approved by the General Assembly is determined by the amount of anticipated revenues. The estimates are cautious so that if economic recession or lower than anticipated economic growth rates should occur, the appropriations would not have to be reduced as called for by the Executive Budget Act.

2. The amount of appropriations that is not spent becomes surplus funds. In the 1971–73 biennium, for example, these reversions amounted to $89.9 million.

Initially revenue estimates are made as the budget is being prepared. During the legislative review and adoption process, the estimates are revised, usually upward, to reflect more recent and complete information on revenue collections and trends. These final estimates are added to the surplus that is expected to exist at the end of the current biennium to determine the total amount of revenues that will be available. There is a tendency for the General Assembly to regard unanticipated revenues as nonrecurring revenues and therefore to use them for so-called nonrecurring, mostly capital, expenditures.[9]

As Table 3 shows, since fiscal year 1951–52 revenues have exceeded estimates every year except 1953–54 and 1954–55, when estimated revenues exceeded actual revenues by relatively small amounts. Before 1953–55, revenues were underestimated only in 1935–36 and 1938–39, and then only by small amounts. In most other years estimates were substantially below revenues. The exceptions seem to occur as a result of economic recessions, as in 1953–54, 1954–55, 1957–58, 1958–59, 1969–70, and 1970–71. In 12 of the 22 years shown in Table 3, the difference exceeded 5 per cent of actual revenues; in six years it exceeded 10 per cent of actual revenues. Although in recent years the differences have not always been big relative to revenues, in absolute terms they were still large.

There are good reasons for being cautious in estimating revenues. With biennial budgets, revenues must be projected more than two years ahead. Growth in tax collections depends largely on the performance of the national economy, which cannot be predicted accurately. On the other hand, revenue collections have grown consistently over the years; revenue collections have not declined since 1949–50, and even then, actual revenue exceeded projected revenue. The main point to be made here is that revenue estimates used by the General Assembly should not be lower than can reasonably be anticipated in order to guard against a budget deficit. As discussed above, the annual appropriations reversions are large enough to provide a buffer should actual revenues be less than anticipated, and if capital improvements expenditures and perhaps some operating expenditures were made contingent on revenue collections, the state could make fuller use of its available resources without having to risk cutting back on-going programs.

The role played by official budget estimates in the budgeting and appropriations process deserves to

8. However, see pages 31–32 for a criticism of the practice of using current revenues to finance capital improvements.

9. The following table compares unanticipated revenues for each biennium with direct capital improvements appropriations for the following biennium (in thousands of dollars).

Biennium	Excess of General Fund Revenues over Anticipated General Fund Revenues	Capital Improvements Appropriations for Following Biennium
1953–55	$(—5,633)	0
1955–57	44,701	24,587
1957–59	9,387	5,340
1959–61	69,748	1,860
1961–63	82,604	63,074
1963–65	61,214	41,640
1965–67	124,864	112,357
1967–69	160,977	75,589
1969–71	66,086	64,891
1971–73	174,840	191,822

Table 3

Comparison of Official Estimates of General Fund Revenues with Actual Revenues, Fiscal Years 1951–52 to 1972–73

(thousands of dollars)

Year	Official Budget Estimate	Estimate As Revised During Legislative Session	Actual Revenues	Difference between Actual and Revised Estimates	
				Amount	As Percentage of Actual Revenues
1951–52	$ 146,002	$ 162,439	$ 178,888	$ 16,449	9.2%
1952–53	146,752	180,333	180,978	645	.04
1953–54	188,249	186,819	184,710	—2,109	1.1
1954–55	195,781	192,635	189,111	—3,524	1.9
1955–56	184,931	205,503	224,614	19,111	8.5
1956–57	184,918	208,178	237,768	29,590	12.4
1957–58	237,844	239,305	242,112	2,807	1.2
1958–59	245,628	247,090	253,670	6,580	2.6
1959–60	275,234	283,234	310,208	26,974	8.7
1960–61	272,213	283,213	325,987	42,774	13.1
1961–62	315,000	347,577	374,837	27,260	7.3
1962–63	325,000	359,984	415,328	55,434	13.3
1963–64	413,455	424,918	437,850	12,932	3.0
1964–65	427,370	443,418	491,700	48,282	9.8
1965–66	496,590	525,414	573,249	47,835	8.3
1966–67	525,487	546,680	623,709	77,029	12.4
1967–68	658,476	659,050	679,199	20,149	3.0
1968–69	697,278	695,238	776,066	80,828	10.4
1969–70	797,900	842,900	878,550	35,650	4.1
1970–71	887,700	937,200	967,636	30,436	3.1
1971–72	1,024,910	1,044,665	1,093,909	49,244	4.5
1972–73	1,115,075	1,133,820	1,259,416a	125,596	10.0

Source: Division of Tax Research.

Notes: a. Excluding federal revenue-sharing funds.

be reconsidered. Those who make official revenue estimates should not bear the responsibility for avoiding deficits. Rather, the objective of official revenue estimates should be accuracy, and they should be judged on their record for accuracy rather than on their record for avoiding deficits. If the General Assembly can have confidence in the accuracy of revenue estimates, it can more effectively take steps to make full use of the state's resources and at the same time take necessary measures to avoid deficits. One important step in improving accuracy of revenue estimates is to change the present policy of keeping official budget estimates confidential until the recommended budget is announced. Making the estimates public would serve as a check on their accuracy since economists and others could then examine them. Another step would be to bring outside consultants directly into the process of estimating revenues rather than having revenue estimates made solely within the Department of Revenue.

WHAT ARE THE CONSEQUENCES of these perennial budget surpluses? First, large surpluses ensure that appropriations will not have to be cut back as prescribed by the Executive Budget Act if an unforeseen reduction in revenues should occur. But, as we have seen, large surpluses are not necessary to meet provisions of this act.

Second, large surpluses presumably help North Carolina maintain the highest bond credit rating, which means that the state can borrow money at a slightly lower rate of interest. However, the state would probably be able to maintain its good credit rating without large surpluses since it has a broad-based and responsive tax structure, a history of fiscal responsibility, and a small outstanding debt compared with that of many other states.[10] In any event, the value of having the highest credit rating should be weighed against the cost of the budget surpluses. It might be preferable to pay a slightly higher rate of interest on debt than to forego the public programs and personal income that could be maintained from the surpluses. Debt service is a relatively small state expenditure, accounting for less than 2 per cent of General Fund expenditures, and, as we have seen, the state has in the last two decades financed most of its capital improvements programs not through debt financing but by use of current revenues.

A third advantage of budget surpluses is that they swell the amount of funds held by the State Treasurer, who collects considerable revenue from interest on the funds when they are invested (about $38 million in 1972–73 from General Fund and Highway

10. At the end of fiscal year 1971, twenty-two states had more state bonds outstanding than did North Carolina.

Fund investments). Although it is wise for the Treasurer to invest funds that are not needed immediately, it is another matter to levy taxes with the intention of using the revenues to generate interest income through investments. After all, taxpayers could put that money in their own savings accounts or spend it. As we will see below, withdrawing from the economy tax revenues that are not spent probably results in a loss of total personal income that is greater than the amount withdrawn and not spent.

The economic effect of not spending part of tax revenues deserves further elaboration. When a resident receives a dollar of personal income and spends it at the local grocery store, the end result is more than one dollar of income to North Carolina residents. For example, part of the dollar spent becomes income to grocery clerks, and part becomes income to North Carolina farmers who sell products to the grocery store. So a dollar added to the North Carolina economy may generate more than one dollar of income to state residents. Economists refer to this as a "multiplier" effect. The multiplier process also works in reverse. If a person suffers a reduction in income, and therefore spends less at the grocery store, the incomes of the grocer and the farmer with whom he trades will tend to fall. When the state taxes its citizens and spends the revenues to purchase goods and services, there are two separate effects. First, the taxes reduce the disposable income of citizens, which sets off the negative multiplier effect. If the state then hires North Carolinians or purchases goods and services from North Carolinians, an even greater multiplier effect will occur, and there will be a net increase in income of residents. If the state fails to spend tax dollars, the only effect is negative. The cost of the failure to spend the tax dollars that have been collected is the difference between the income of citizens after the tax is collected and the income they would have been receiving if the state had spent the tax dollars. This cost will be greater than the amount of unspent tax revenues. In addition, the state will have lost tax revenues from the foregone income.[11] As Table 1 shows, because accumulated operating surpluses are eventually appropriated, the total state budget does not produce a budget surplus every year. In many years a sizable current budget deficit occurs after capital expenditures are accounted for. Thus, although there is a perennial current operating surplus, the net effect is alternating current surpluses and deficits, and the economic effect is probably to lower state income in surplus years and to increase state income in deficit years. These fluctuations would be eliminated and the effect of the state budget on state income would be made consistently positive if large current operating surpluses were eliminated and capital improvements authorizations were made on a more regular basis.

Surpluses may also have a deleterious effect on the allocation of state revenues. Overly cautious revenue projections can lead legislators and the public to believe that revenues will not be adequate to finance on-going or proposed programs, so that needed programs are not funded or unneeded new taxes or tax increases are enacted. Since the surplus funds are treated as if they were a surprise at the end of each biennium, legislators and state officials may fail to plan adequately for new and improved programs. The three new taxes that have been enacted since the 1930s—the sales tax on food, effective in 1961, and the cigarette and soft-drink taxes, effective in 1969—apparently resulted from a belief that tax revenues would not be sufficient to cover on-going and proposed state programs. However, the operating surpluses that have occurred since the sales tax on food was enacted have exceeded revenues from these taxes.[12] Similarly, even without the soft-drink and cigarette taxes, there would have been annual operating surpluses in the General Fund.[13]

If surplus revenues had been used for current needs, capital improvements that would have been funded from surpluses would have required other means of financing. Several justifications can be provided for **not** funding capital improvements from surpluses. Capital improvements usually last many years. If they are financed through debt, they are paid for from tax revenues that are collected from those citizens who are then enjoying the benefits of the capital projects. The irony of spending surpluses on capital improvements is made even greater when incomes are rising, as they are in North Carolina. If tax revenues collected during a previous biennium are used to pay for capital improvements, today's citizens are being taxed to pay for projects that will

11. Some argue that the investment of unspent funds by the State Treasurer causes personal income to increase in the state as businesses borrow these additional funds to make investments. However, this argument ignores the fact that most of the unspent funds are invested in U.S. government securities, and the additional funds loaned to the U.S. government would benefit the entire nation, not just North Carolinians.

12. The following table shows estimated additional revenue from the sales tax on food for each subsequent biennium compared with ending General Fund surpluses.

Biennium	Additional Revenue from the Sales Tax on Food (millions of dollars)	Ending General Fund Surplus (millions of dollars)
1961–63	$ 61.0	$111.7
1963–65	70.2	99.7
1965–67	81.0	172.7
1967–69	93.3	153.3
1969–71	111.0	147.2

13. This is shown in the following table:

Fiscal Year	Additional Revenue from the Soft Drink and Cigarette Taxes	Ending General Fund (millions of dollars)
1969–70	$24.7	$ 46.3
1970–71	34.9	50.8
1971–72	38.1	58.9
1972–73	40.0	119.9

be used in the future by citizens who will have more income and can more easily afford to pay for those projects.

THERE ARE OTHER PRACTICAL REASONS why capital improvements should not be financed from surpluses. First, the notion that surpluses are nonrecurring is likely to distort budget decisions. Many people believe that nonrecurring revenues should be spent only on capital improvements rather than on operating programs. When the revenues are in fact continuing rather than nonrecurring, spending is biased toward capital projects and away from operating programs. Further, most capital improvements require maintenance expenditures and operating personnel for many years into the future. Rather than budgeting operating and capital expenditures independently, as under present practice, it would be sounder to consider operating programs and their associated capital requirements together as single programs.

The practice of funding capital improvements from surpluses tends to let the amount of capital improvements appropriations be determined by the ability to forecast revenues or by unforeseen economic circumstances that affect revenues rather than by the budget process on the basis of need. Should a project that will be needed for many years fail to be funded because of a temporary reduction in tax revenues? Under present practice, it is possible that high-priority capital projects will not be funded if a surplus does not exist whereas a low-priority operating program will be funded. Again, it would be sounder to consider operating and capital appropriations on the same basis.

If the General Assembly changes permanently to annual sessions, the budget surpluses are likely to become much smaller, especially if the budget is also put on an annual basis. Instead of having to project revenues more than two years in advance, the legislature will need to project revenues for only fifteen to eighteen months in advance. Economic changes that may affect tax revenues will be much easier to foresee. But annual sessions alone will not solve the problems discussed here.

STIPE GIVEN HISTORIC PRESERVATION AWARD

The North Carolina Historic Preservation Society has awarded Robert E. Stipe the Ruth Coltrane Cannon Cup for his contributions to preservation on the local, state, national, and international levels. Stipe is Professor of Public Law and Government and Assistant Director of the Institute of Government. The award is given annually for outstanding contributions to historic preservation. Stipe has drafted state legislation on historic properties, districts, zoning, and has advised on legislation dealing with history for the past ten years.

Stipe has lectured at conferences throughout the United States and abroad and organized the successful biennial course in Historic Preservation Planning, co-sponsored by the Institute of Government and the Division of Archives and History and attended by people from across the nation.

He was the principal organizer, guide, and translator for the first "Workshop in England," when county officials from two Virginia counties spent a week in England comparing American and British approaches to preservation.

On the local level, Stipe helped to establish both the Chapel Hill Historical Society and the Chapel Hill Preservation Society. The constitution and bylaws he drafted for these groups have served as models for many similar organizations.

In addition to teaching, Stipe has written, compiled, and edited numerous articles and books about historic preservation and has earned a reputation as a national and international scholar of preservation law. He was elected to the Board of Trustees of the National Trust for Historic Preservation and is a member of more than a dozen professional societies.

Stipe was a Senior Fulbright Research Fellow at the University of London in 1968–69 and did research in the legal, financial, political, and administrative aspects of historic preservation and townscape conservation.

THE EFFECT OF TAXES ON INDUSTRIAL LOCATION

C. Donald Liner

IT IS WIDELY BELIEVED that business firms can be induced to locate their plants in states or communities that have low business taxes or offer special tax concessions or financial subsidies to industry. This belief has led many states to make their tax systems favorable to business and to be reluctant to increase business taxes as much as other taxes.[1] Other states have made tax concessions designed to make their states more attractive to industry.[2] For example, some states partially or fully exempt inventories of raw materials or finished products from the property tax.[3] Other states have "freeport" laws, which provide a property tax exemption on inventories held in storage for shipment to other states. Other states give tax concessions to new or expanded plants; thus in some states new or expanded plants can be exempted from property taxes (usually not including school levies) for a specified period of time.[4] In some states, communities are permitted to issue public, tax-exempt bonds to finance construction of industrial buildings for use by private firms.[5] Many tax administration practices are designed to influence industrial location decisions and to maintain a "favorable business climate." Among these practices are low property tax appraisals, constant or negotiated tax appraisals, and liberal apportionment formulas for corporate and franchise taxes. Public or private agencies have been organized in many states to offer low-interest loans or to guarantee private loans for new firms.[6] Communities in some states may provide direct inducements in the form of cash donations, payment of moving expenses, sales or rentals of land or buildings at low prices, advance agreement on utility rates, construction of industrial parks, and free installation of sewer, water, and electricity lines.

Favorable tax treatment and special inducements to attract industry can be costly in terms of reduced state and local tax revenues and perhaps in terms of reduced tax equity. Do these measures benefit the public enough to cover their costs? A precise estimate

1. Business tax revenues have tended to fall as a proportion of total state and local tax revenues. In estimates made by the Advisory Commission on Intergovernmental Relations, of 48 states and the District of Columbia, between 1957 and 1967 taxes on business (excluding sales taxes) fell as a percentage of total state and local taxes in all but six states. Advisory Commission on Intergovernmental Relations, *State-Local Finances: Significant Features and Suggested Legislation* (Washington, D.C.: U.S. Government Printing Office, 1972), Table 76.

2. Property tax inducements in the United States date from 1649, when a property tax exemption was granted in Connecticut. For a short history of these inducements and a survey of their uses as of about 1967, see Paul E. Alyea, "Property Tax Inducements to Attract Industry," in Richard W. Lindholm (ed.), *Property Taxation USA* (Madison: University of Wisconsin Press, 1967), pp. 140–41.

3. As of January 1, 1972, in six states inventories were exempted because all personal property was exempt. Of the other states, 21 had provided relief from property taxes on inventories by low official assessment rates, by partially or fully exempting at least some kinds of inventories, or (in Wisconsin) by giving an income tax credit for inventory property taxes. A few states provided exemptions for special kinds of inventories such as textile or new cars. Cf., Advisory Commission on Intergovernmental Relations, *State-Local Finances,* Table 110.

4. For a description of these programs, see Benjamin Bridges, Jr., "State and Local Inducements for Industry, Part I," *National Tax Journal* 18 (March 1965), 8–9.

5. See *ibid.,* pp. 6–8, for a survey of the use of bond financing.

6. See *ibid.,* pp. 2–6 and 9–14, for a description of state loan guarantee programs, statewide development credit corporations, and local development corporations.

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of benefits and costs would be difficult, if not impossible.[7] Estimating benefits and costs may not be necessary, however, because a simpler question may suffice: How successful are tax and nontax inducements in influencing a firm's location decision.[8] The purpose of this article is to provide at least partial answers to this question by examining the role and importance of taxes in the plant-location decision and by reviewing the results of certain studies and surveys conducted for this purpose.

Public Services Also Attract Industry

Before examining the efficacy of tax inducements, it would be good to recall that taxes are collected in order to provide public services and that the quantity and quality of public services are likely to be at least as important to industry as taxes. Thus low tax rates may repel, rather than attract, industry if they produce inadequacy in such services as police and fire protection, water supply, schools, and health services.

Industry may demand adequate or even exceptional public services for several reasons. If such services as police and fire protection are not available, firms will have to provide them, which may be costly. Industry may be concerned that public services or facilities are available and adequate for the benefit of their employees—for example, schools, libraries, and recreation. Finally, industry may be concerned about the general quality of local government, especially the quality of local officials.

The quantity and quality of public services necessary to attract industry may require high rather than low tax rates. Among the 50 states, both state and local taxes and public expenditures are correlated with measures of economic development.[9] This does not mean that high taxes and public expenditures cause economic development to occur; it means, that high taxes and public expenditures at least do not impede economic development, and it contradicts the common belief that low taxes are associated with economic development. Furthermore, as industry moves into a state or community, the demand for public services is likely to increase. New residents require new housing and related public services as well as enlarged schools and other public facilities. Enlarged local payrolls also lead to higher demand for public services. In areas that are in transition from an agricultural to an industrial economy, the increased demand for public services is likely to be especially significant.

However, a common argument is that low taxes will attract industry and thus expand the local tax base so that more public services can be financed. This takes us back to the basic question: Are low taxes successful in attracting new industry?

How the Decision is Made

To evaluate the importance of taxes in influencing industrial location, it is necessary to understand how firms make location decisions and how taxes enter into these decisions.

It is the differences in tax levels rather than the absolute level of taxes that are relevant to the location decision. Taxes that must be paid regardless of location will not affect the location decision. For example, federal taxes will not affect location within the United States. Differences in state taxes may affect the choice of state but not location within a state. Moreover, tax differences among states have become less important in determining location because in recent years state tax structures have become more uniform and business tax rate differentials have become narrower. Today most states have retail sales taxes, corporate and personal income taxes, gasoline, alcoholic beverage, and cigarette excise taxes, and, of course, property taxes at the local level. As Table 1 shows, variation in rates of the retail sales, corporate income, and gasoline tax rates among states are not large, and differences in one tax are often offset by differences in other taxes.

Tax differentials may not be so important in location decisions as simple comparisons make them seem—for two reasons. First, the effect of tax differentials is reduced by about half because state and local taxes reduce a firm's federal corporation income tax liabilities, and local taxes reduce its state corporation income tax liabilities. For example, the difference between a 5 per cent and a 6 per cent state corporation income tax may not greatly influence a firm's location decision because the higher rate in one state will reduce the firm's federal corporation income taxes by about half the difference that would be exacted by the varying rates of the two states.

Second, tax differentials will not affect a firm's location decision if they do not affect profits. If a firm can offset tax differentials by increasing prices or by reducing payments to factors of production,

7. Bridges discusses measuring benefits and costs, but notes that the result is inconclusive. See Benjamin Bridges, Jr., "State and Local Inducements for Industry, Part II," *National Tax Journal* 18 (June 1965), 185–92.

8. To be judged accurately, the inducements must be shown to have caused firms to locate at places where they would not have located without the inducements. It is not sufficient merely to show that states or communities with light business taxes are being chosen as locations for new plants.

Tax and financial inducements may possibly increase the amount of investment in new and expanded plants. However, in this article we will consider only location decisions rather than the size of plants.

9. Alan K. Campbell, "State and Local Taxes, Expenditures, and Economic Development," in *State and Local Taxes on Business* (Princeton: Tax Institute of America, 1965), pp. 206–7.

Table 1

State Rates on Corporate Income Tax, State Retail Sales Tax, and Gasoline Tax[1]
(Effective October, 1973, Unless Otherwise Noted)

	Corporate Income Tax (rate on taxable income exceeding $25,000) Percentage	State Retail Sales Tax (rate on general sales) Percentage	Gasoline Excise Tax, Cents Per Gallon
Alabama	5%[2]	4%	7
Alaska	—[3]	—	8
Arizona	8	3	7
Arkansas	6	3	8½
California	9	3¾[4]	7
Colorado	5	3	7
Connecticut	8	6.5	10
Delaware	7.2	—	9
Florida	5	4	8
Georgia	6	3	7½
Hawaii	6.4	4[5]	8–11[6]
Idaho	6.5	3	8½
Illinois	4	4	7½
Indiana	5	4	8
Iowa	8–10[7]	3	7
Kansas	6.75	3	7
Kentucky	5.8	5	9
Louisiana	4	3	8
Maine	7	5	9
Maryland	7	4	9
Massachusetts	7.5 plus 14% surtax	3	7½
Michigan	7.88	4	9
Minnesota	12	4	7
Mississippi	4	5[9]	9
Missouri	5	3	7
Montana	6.75	—	7
Nebraska	3.25	2.5	8½
Nevada	—	2	6
New Hampshire	7	—	9
New Jersey	7¼[10]	5	8
New Mexico	5[11]	4	7
New York	9	4	8
North Carolina	6	3	9
North Dakota	6	4	7
Ohio	8	4	7
Oklahoma	4	2	6.58
Oregon	6[12]	—	7
Pennsylvania	11	6	8
Rhode Island	8	5	8
South Carolina	6	4	8
South Dakota	5.5	4	7
Tennessee	6	3.5	7
Texas	—	4	5
Utah	6	4	7
Vermont	6	3	9
Virginia	5	3	9
Washington	—	4.5	9
West Virginia	6	3	8½
Wisconsin	7.9	4	7
Wyoming	—	3	7
Dist. Columbia	8[13]	5	8

1. See source for detailed rate schedules
2. 6% for financial institutions
3. 18% of federal income tax
4. 4¾% beginning April 1, 1974
5. Gross income tax varies from ½% to 4% of the value of products, gross proceeds, or gross income according to type of business
6. Varies by county
7. 10% for net income over $100,000
8. 9.7% for financial institutions
9. ⅛ of 1% to 5% of gross income, depending on type of business
10. Effective 1/1/74
11. 6% for banks and financial firms
12. 8% for financial businesses
13. Effective 1/1/74

Source: Commerce Clearing House, *State Tax Handbook* (as of October 1, 1973).

profits will not be adversely affected, and it may ignore tax differentials in deciding location.

Let us assume, however, that tax differences do affect a firm's profits and therefore must be considered in making a location decision. We then must ask: How important are taxes in the decision?

Other things being equal, a firm will logically choose a location where total costs are lowest—not the location where only tax costs are lowest. Taxes are only one of many costs of business and only a minor cost compared with total costs.[10] How tax differences influence location decisions depends on how those differences compare with combined differences in other costs.

In most cases, location decisions will hinge on more important and fundamental differences than tax differences. For example, the basic considerations of a market-oriented firm will be proximity to markets and transportation costs. Differences between alternative locations with respect to these considerations will usually outweigh benefits from low taxes. Similarly, firms that must rely on raw materials supplies will not usually be persuaded to locate away from supplies because additional transportation costs would outweigh lower tax costs. Labor-oriented firms will usually find that wage rates and availability of labor are more important than tax differentials.

While it is logical for a firm to consider total costs in all alternative sites, it is difficult, if not im-

10. Bridges estimated that if Wisconsin manufacturers were exempted from all local property taxes, firms' state-local tax costs would be reduced an average of 0.68 per cent of value of shipments. The estimates ranged from a low of 0.37 per cent for the food products industry to 1.10 per cent for the primary metals industry. However, the reduced state-local tax costs would be offset significantly by increased federal income taxes. Bridges, "State and Local Inducements, Part II," Table V, p. 178.

possible, to obtain complete information on costs at all alternative sites, and location decisions are probably made by a process of elimination. A firm first chooses a few primary criteria based on major considerations such as proximity to markets, raw materials supplies, transportation costs, and labor availability. Then it narrows the list of potential sites to a few sites or to a geographical area in which these criteria are met. Once the list is limited, the firm begins to consider secondary criteria such as taxes, cost of land, local public services, the desirability of the community as a place to live, and so on.

Thus, although the general area or the list of potential locations may be decided on the basis of market access, raw materials supply, labor supply, or transportation costs, the choice of a specific community, the choice of a particular state within an area, or the choice of an actual site may be determined by factors of secondary importance. Of course, to the communities involved in the final choice, these factors will seem to be the critical ones. It is thus conceivable that tax inducements, while affecting a minor cost and representing a minor location factor, could determine the choice in the end.

Labor-oriented firms are more likely than other firms to choose their locations on the basis of secondary factors because labor conditions do not vary as much within limited areas as they do between areas; raw materials supplies and market conditions are likely to vary more within an area than labor conditions. For example, many apparel firms are indifferent about location within an area that has low wages and abundant labor supply. For these firms, such factors as low land prices or tax inducements may determine specific location even though labor supply is basically a more important factor.

If inducements affect only the specific site but not the area in which firms locate, any tax or financial inducement that causes a plant to locate at a particular site may benefit that community, but it will not increase the benefits to the entire area. One community's gain is another community's loss. Therefore, as a matter of statewide or regional policy, tax or financial inducements may not be advisable even if they are shown to be successful in influencing firms' decisions to choose a particular community. Accordingly, southern states that have tax-exemption programs may be competing against other southern states for firms that want to locate somewhere in the South; as a region, the South probably gains little from these programs.

Given that in some cases taxes could be the decisive factor in choosing a specific location, are taxes important enough as a location factor for us to conclude that taxes will often decide industrial location? While it is difficult to assess the importance of taxes when so many factors are involved, there are several reasons for believing that taxes will seldom be the decisive factor. First, of course, taxes are not a primary location factor and only one of many secondary location factors. To be the determining factor, they must offset not only differences in primary factors but also differences in all other secondary factors. Second, as mentioned earlier, since a firm may be able to pass tax costs on to its customers, it may choose a particular state or community despite its higher taxes. Third, also mentioned earlier, the attraction of tax differences is reduced considerably by compensating changes in corporate income tax liability. Fourth, within geographical areas tax differentials tend to be small, and even among states tax structures are becoming more uniform. Fifth, a firm that is making a location decision will not have complete information about tax costs and therefore cannot make a decision on the basis of taxes alone, since complete tax information about alternative locations would be available only if the plant were built in the alternative locations. Finally, firms may be less concerned about the amount of taxes they will have to pay than about the fairness of taxes, the administrative red tape and reporting costs, and the stability of tax rates and administration.

ALTHOUGH THIS DISCUSSION seems to indicate that tax and financial inducements cannot be expected to be of major importance in industrial development, still the feeling persists very strongly that these inducements should pay off. After all, states and communities have continued to use inducements for many decades, and businessmen and industrial development specialists continue to urge their use. The following section contains evidence from studies and surveys of businesses that may shed some light on the efficacy of inducements.

Studies and Surveys

Over several decades, numerous studies have been made of the effect of taxes and financial inducements on industrial location decisions. Many of them have been based on surveys, usually by written questionnaire, of businessmen in firms that had made a location decision; other studies have used personal interviews of such businessmen. The consistency of their findings provides strong corroboration for the hypothesis that taxes are only a minor location factor. The following materials (including Table 2) summarizes the primary findings of 17 surveys based on questionnaires distributed that have been surveyed by another writer.[11] Markets, labor, raw materials,

11. William E. Morgan, "The Effects of State and Local Tax and Financial Inducements on Industrial Location" (Ph.D. diss., University of Colorado, 1964). Findings of surveys based on personal interviews, which also were reviewed by Morgan, were similar to those based on questionnaires, except that "personal factors" ranked higher in the interview surveys. See page 24 for a discussion of general weaknesses of the survey approach. Other studies are reviewed in John F. Due, "Studies of State-Local Tax Influences on Location of Industry" *National Tax Journal* 14, No. 2 (June 1961), pp. 163–73.

and transportation were the prime factors, while taxes were of little significance in all the surveys. However, textile, apparel, and shoe manufacturers considered taxes to be more important than did other types of firms.

• *Colorado Survey.* Taxes ranked twenty-seventh out of thirty factors. Only 12.7 per cent of the firms indicated that any consideration had been given to Colorado's state and local taxes. Less than 1 per cent of the new firms placed any importance on availability of community financial subsidies; subsidies ranked next to last in importance. The most important factors were "availability of markets," "availability of future markets," and "over all growth of the state or area."[12]

• *Florida Survey.* "State and/or municipal tax structures" was ranked fifteenth out of twenty-three factors; only one out of 752 firms listed it as a primary location factor. Taxes were mentioned by only 41 firms. "Community attitudes and aid" was ranked last; only two firms mentioned this factor, and they listed it third.[13]

• *Georgia Survey.* Although 36 of the 130 firms surveyed had received some form of assistance from the state or community, when asked "What could Georgia do to attract more industry," only three of the 102 comments received indicated that tax concessions would attract industry to the state.[14]

• *Maryland Survey.* Taxes ranked eighteenth out of 21 factors; only four firms out of 118 considered them significant. "Financial aid," mentioned by only five firms, ranked sixteenth. The most important factors were "labor," "markets," "available factory buildings," and "location of productive materials."[15]

• *Minnesota Survey.* "Personal and property taxes" and "real property taxes" ranked sixth and seventh out of 24 factors. "Work attitudes of individual workers" was considered most important, which may be explained by the fact that a large part of the sample hired primarily unskilled labor.[16]

• *New Jersey Survey.* "Reasonable state and municipal business taxes" and reasonable state and municipal personal taxes were ranked third and sixth, respectively, among twelve factors. Business taxes were considered to be "very important" by 34 per cent of the firms and "of some importance" by 41 per cent.[17]

• *New York Area Survey.* When asked to list the most favorable and the most unfavorable factors in their plant location decisions, businessmen listed "municipal taxes," "wages" and "taxes in general" as most significant unfavorable items. The most important favorable factors were "access to markets," "factory buildings," and "room for expansion."[18]

• *Oregon Survey.* "Favorable state and local taxes" ranked sixteenth out of 18 factors. Only 3 per cent of the firms were "strongly influenced" by state and local taxes.[19]

• *Seven Southern States Survey.* "Favorable tax structure" ranked fifteenth out of 16 factors, and financial aid ranked sixteenth. Favorable taxes were mentioned as being most important by less than 1 per cent of the firms.[20]

• *Southwest Survey.* Among 34 factors, taxes were ranked twenty-fourth by large firms and twenty-second by small firms in Oklahoma, Texas, Louisiana, Arkansas, Kansas, and Mississippi. "Subsidies or other incentives by state or local groups" was ranked last. The most important factors were "availability of product markets," "wages and salaries," and "abundance of general labor supply."[21]

• *Texas Survey—University of Texas.* Taxes were ranked eleventh among 15 factors most often mentioned. Subsidies were not mentioned as an important reason for selecting Texas as a location. The reason most often cited was the expanding southwestern market and the potential industrial development in population growth in the area.[22]

• *Texas Survey—Texas A & M.* Taxes ranked fourteenth among 16 factors in importance. Only five firms (approximately 1.5 per cent of the total) considered taxes to be of primary importance, and only 49 (15 per cent of the total) mentioned taxes as one

12. L. J. Crampon and Paul W. DeGood, Jr., *Industrial Location Survey*, (Boulder, Colorado: Bureau of Economic Research, University of Colorado, 1957).

13. Melvin L. Greenhut, "An Empirical Model and a Survey: New Plant Locations in Florida," *Review of Economics and Statistics* 41 (1959), 433–38.

14. A. Lee Cobb, "Factors Affecting Industrial Location in Georgia," *Georgia Business* 16, no. 2 (May 1957), 1–9.

15. *Location Factors in Establishing New Manufacturing Firms in Maryland* (Baltimore: Maryland State Planning Commission, 1951).

16. Business Executives' Research Committee and School of Business Administration, *Industrial Location and the Minnesota Economy* (Minneapolis: University of Minnesota, 1955).

17. Solomon J. Flink, et al., "The Attractiveness of New Jersey as a Manufacturing Location," *The Economy of New Jersey* (New Brunswick, N. J.: Rutgers University, 1958), pp. 243–61.

18. John L. Griffin, *Industrial Location in the New York Area* (New York: The City College Press, 1956).

19. Wesley C. Ballaine, *Why Business Firms Located in Oregon 1948–1957*, (Eugene, Oregon: Bureau of Business Research, University of Oregon, 1958).

20. Thomas P. Bergin and William F. Eagan, "Economic Role and Community Facilities," *Municipal Finance* 33, no. 4, (May 1961), 146–50.

21. Francis R. Cella, et al., *Factors Affecting Industrial Location in the Southwest* (Norman, Oklahoma: Bureau of Business Research, University of Oklahoma, 1954).

22. Florence Escott, *Why 122 Manufacturers Located Plants in Texas* (Austin, Texas: Bureau of Economic Research, University of Texas, 1954).

of their five reasons for locating in Texas. "Financial help" ranked thirteenth: only eight firms considered it an important factor and only 34 firms (less than 10 per cent of the total) considered it one of the five reasons for their location decision. The most important factors were markets, labor, and raw materials.[23]

- *West Virginia Survey.* Taxes ranked twelfth among 16 factors. "Community financial aid" was ranked last: 82 per cent of the firms stated that financial assistance "did not enter into the location choice." The most important factors were "adequacy of labor supply," "transportation facilities," and "location with regard to markets."[24]

- *Wisconsin Survey.* The most significant factors reported were "wages," "markets," "materials," and taxes."[25]

- *United States and Canada Survey.* This survey included 10,267 firms and 2,084 communities in the United States and Canada during the period 1926–27. Taxes were ranked twelfth and financial aid eleventh among 16 factors. Markets, labor, and transportation were the most significant factors.[26]

- *Business Week Survey.* Taxes ranked fifth among 13 factors; only 14 per cent of the firms considered taxes important in some degree in selecting a new plant location. The most important factors were markets, labor, transportation, and raw materials.[27]

- *Dun's Review Survey.* Twenty-two of 107 firms said they preferred rural areas for their new plants because these areas offered lower labor costs, better employee relations, and lower taxes and operating costs.[28]

One study not covered by Morgan's review shows taxes to be somewhat more important than other surveys did.[29] Conducted in 1963 in South Carolina, the survey showed that while labor conditions ("labor relations," "history of work stoppages," and "extent of unionization") were most important in the location decisions of the 32 firms in the survey, tax considerations ("assessment bases," "property tax rates and fees," "trends in tax legislation," and "special inducements to industry") were more significant than other factors. The findings of this study perhaps support the hypothesis that labor-oriented firms are more likely than other types of firms to make their choice of specific location on the basis of secondary factors. On the other hand, in an earlier South Carolina survey, none of the officials of 49 new manufacturing plants mentioned taxes as a significant factor even though South Carolina had a five-year exemption in most counties; raw materials and local markets were listed as most important.[30]

Table 2

Significance of Location Factors According to Business Opinion, As Revealed by 17 Questionnaire Surveys

Factor	Primary	Some	Little
Markets	16	1	—
Labor	10	7	—
Raw Materials	10	6	—
Transportation	7	10	—
Taxes	1	3	13
Financial Inducements	—	—	13

Source: Seventeen questionnaire surveys reviewed in William F. Morgan, "The Effects of State and Local Tax and Financial Inducements on Industrial Location" (Ph.D. diss., University of Colorado, 1964).

Tax and Financial Inducements as Instruments of Public Policy

In light of evidence from these surveys, one is tempted to dismiss tax and financial inducements as ineffective in all but marginal cases and therefore unworthy of use as instruments of public policy. But how then can we explain the persistent support of inducements? Why do the business community and industrial development specialists continue to insist that the tax structure be used to speed industrial development?

One possible explanation, of course, is that the business community is merely looking for a tax break, and the best chance for getting it is to convince the public or legislators that the tax break is in the public interest because it will draw new industry and increase employment and payrolls.

A less cynical explanation is that, of all the factors that determine location of industry, only taxes can easily be controlled. The large benefits often believed to accrue from new industry make many communities willing to go to great lengths to attract industry. But

23. L. S. Paine, *An Evaluation of Plant Location Factors in Texas,* Research Report 49 (College Station, Texas: Texas Engineering Experiment Station, Texas A & M College, 1954).

24. James H. Thompson and Thomas S. Isaack, *Factors Influencing Plant Location in West Virginia, 1945–1956* (Morgantown, W. Va.: Bureau of Business Research, West Virginia University 1956).

25. Wisconsin Business Research Council, *Industrial Development in Wisconsin,* Wisconsin Commerce Series, 5, no. 1 (Madison: The University of Wisconsin, 1957).

26. *Industrial Development in the United States and Canada, 1926–1927* (New York: Policy Holders Service, Bureau of the Metropolitan Life Insurance Company and the Civic Development Committee of the National Electric Light Association, 1928).

27. *The Plant-Site Preferences of Industry, and the Factors of Selection,* Business Week Research Report (August, 1958).

28. "New Light on Site-Seeking," *Dun's Review of Modern Industry* (March 1959), 90–91, 104–11.

29. A. C. Flora, Jr., "Industrial Location in South Carolina," *The University of South Carolina Business and Economic Review,* 10, no. 4 (January 1964), cited in Alvea, "Property Tax Inducements," pp. 149–50.

30. "Activating Motives of Industry Location Since 1939," *Is New Industry Tax Exemption Effective?* South Carolina State Planning Board pamphlet no. 9, (Columbia, S. C., March 1943), pp. 11–13.

fundamental changes that would encourage industrial development, such as establishing labor-force training programs or improving transportation facilities, are too costly and usually beyond the capabilities of single communities.

Tax and financial inducements are often supported on the grounds that benefits to a community from a new plant, in the form of increased employment and income, will far exceed their cost in reduced tax revenues. This would probably be true for the single plant that locates in a community or state as a result of a tax concession. Unfortunately, tax and financial inducements usually cannot be offered on a selective basis. Usually they must extend to all firms, and therefore they will benefit firms that would have made the same location decision even if an inducement had not been offered.[31] For example, in states that exempt inventories from property taxes in order to become more attractive to industry, revenue from all firms that previously paid taxes on inventories is lost, as well as revenue from all firms that subsequently locate plants in the state; this large revenue loss is offset only by the additional corporate and franchise taxes paid by the relatively few firms that will locate in the state as a direct result of the exemption. Thus, when we evaluate inducements as public policy instruments, we must weigh the benefits against total costs of the inducements. The only benefits that should be counted are benefits that accrue from plants that would not have made the same location decision if the tax or financial inducements had not been offered.[32] At the same time, all costs and financial inducements, including the cost of inducements that are not responsible for new plants, must be counted. When this is done, it seems unlikely that, given the evidence cited earlier, benefits will exceed costs.[33]

Even if inducements were found to be effective in influencing location decisions, their use tends to be self-defeating because other states or communities soon learn to use the same inducements, and thereafter the inducements become ineffective. As mentioned earlier, inducements are also self-defeating to a state or region because new industry in one community may be lost to other communities in the state or region.

Several other arguments can be made against inducements. Firms may interpret low tax rates or tax inducements as an indication that public services are inadequate. Low taxes on industry may imply high taxes for other taxpayers in the community who will not benefit from the new plants. Existing industry may suffer a competitive disadvantage from special tax concessions to a plant; moreover, existing plants may expect to receive equivalent concessions. When property tax exemptions are granted, local governments may face higher public service costs while it is state government that receives the additional revenue in the form of corporate income, franchise, and sales taxes. Firms that are attracted to a community because of tax considerations are likely to have few other strong reasons for locating there. With weak ties to the community, these firms are likely to leave when tax concessions expire or when another community offers more attractive inducements. Finally, labor-oriented firms, which are most likely to be attracted by inducements, are more likely to be low-wage industries, which may not substantially improve the economic welfare of the community.

31. Morgan found that, while few plants' location decisions were made to obtain tax concessions, most plants applied for tax concessions when concessions were allowed. *Effects of Inducements,* p. 152.

32. Benefits should be "net benefits." That is, from the benefits in the form of increased income and employment, one should subtract "negative benefits" of industrial plants such as higher costs of local government and congestion and pollution costs.

33. Morgan concluded from his analysis of tax-exemption programs in five southern and two northeastern states that 90 to 93 per cent of total industrial investment during a four-year period would have been undertaken even if tax exemptions had not been available. The gain from the 7 to 10 per cent that located because of the inducement was found not to cover the direct cost of the exemptions. *Effects of Inducements,* pp. 156–58.

Book Reviews

PRISONERS IN AMERICA, edited by Lloyd E. Ohlin. Englewood Cliffs, N.J.: Prentice Hall, 1973. $2.45 (paperback).

This book provides an overview of problems confronting the American correctional system and offers guidelines for coping more effectively with prisoner rehabilitation. The author is professor of criminology at Harvard Law School, and this volume was used as background reading for conferees attending the Forty-second American Assembly held at Arden House, Harriman, New York, in December 1972. It includes an extensive list of the principal sources and suggested references that would be useful to a researcher interested in correctional reform.

THE ECOLOGY OF STRAY DOGS, by Alan Beck. Baltimore: York Press, 1972. 98 pp. $9.50.

In his movement to the city, man has brought his age-old companion—the dog. One authority estimates that half the nation's approximately 25 million dogs live in the city. Unfortunately, the large urban dog population causes problems for both man and dog.

The Ecology of Stray Dogs studies free-ranging urban dogs and their impact on the urban environment. With extensive field work in Baltimore, the author analyzes the source and distribution of free-ranging dogs, their behavior patterns, their mortality, and their social organization. He then discusses the impact of the urban dog population on public health and the quality of urban life. Going beyond the matter of dog bites, the discussion also raises the interrelatedness of rat control and dog control, the problems of large amounts of dog excrements in the city, and other environmental impacts such as noise and the destruction of trees and shrubs. The book concludes with strong recommendations for better-managed and stricter control of free-roving dogs in the city.

The value of the book will be determined by its use. To the urban planner, city manager, or legislator it may provide helpful background information for decision-making. For example, the study shows that dogs are more active and present in larger numbers around 6 a.m. Therefore, if dog wardens were on the streets at that time, they could pick up more dogs with less effort.

But despite the book's merits, it has drawbacks. The reader must endure a heavy dose of statistics and scientific language. Nor can he expect a comprehensive and scientific language. Furthermore, the book does not give a comprehensive program for dog control; the practical recommendations at the end of the book are few and directed largely at the Baltimore dog control program.

To the academician, the book offers data and observations that may be helpful in studying dogs generally or in studying the impact of the urban setting on dogs and other animals, including man. However, the book does not present a systematic theory of the ecology of stray dogs or of their behavior. Rather, it follows the narrow scope of the graduate thesis on which it was based. It simply recites by topic statistics and observations from the field study followed by a short discussion, presenting no conclusions or theories —save some practical recommendations for stricter dog control. Indeed, the book fails to explore the larger issues and implications of an urban dog study suggested in the introduction. In short, the book represents a novel and interesting study but is not a comprehensive or complete treatment of the ecology of free-ranging urban dogs.

Alan M. Beck, the author, is the Urban Ecology Task Force chairman with the Center for the Biology of Natural Systems at Washington University in St. Louis.

—Kenneth Davidson

NORTH CAROLINA, THE HISTORY OF A SOUTHERN STATE, by Hugh Talmage Lefler and Albert Ray Newsome, third edition. Chapel Hill: University of North Carolina Press, 1973. $11.95.

In this edition, Dr. Lefler has rewritten considerable amounts of text to include new information and to develop and give added prominence to areas such as the position and influence of the Negro in North Carolina. Updated appendixes of 1970 statistics, additional maps and charts, and bibliographies of recent books about North Carolina are bonus features for the general reader and the student who want a comprehensive history of the state through the decade of the 1960s.

REORGANIZATION OF HUMAN SERVICES —THE CATAWBA COUNTY APPROACH

T. Cass Ballenger and David G. Hunscher

Mr. Ballenger is the chairman of the Catawba County Board of Commissioners and Mr. Hunscher is the county manager.

IN NORTH CAROLINA, HUMAN SERVICES are rendered primarily at the county level. These include welfare (social services), health, mental health, alcoholic rehabilitation, and veterans' services. These programs generally result from both state and federal law; often the state law has come about to implement federal legislation that offers matching funds if the state and county governments will appropriate funds to finance the programs.

Responsibility for human services is shared through various organizational units in the three levels of government. At the federal level, it lies primarily within the U.S. Department of Health, Education and Welfare. The reorganization of North Carolina state government that has been under way since 1969 has centered most state-level activities in the field of human services in a single umbrella department called the Department of Human Resources, headed by the Secretary of Human Resources. The Secretary has all management functions in this area, which are specified by the legislation that created the Department to include "planning, organizing, staffing, directing, coordinating, reporting, and budgeting." Responsibility for policy matters is shared by the Secretary with a fifteen-member Board of Human Resources and with separate commissions in the various fields (social services, health, mental health, etc.) that govern policy. The fifteen-member Board advises the Secretary on matters referred to it by him, helps the Secretary develop major programs, and recommends priorities for programs within the Department of Human Resources.

Within the Department of Human Resources are the Divisions of Social Services, Health, Mental Health, and others, each headed by a director. For each division, there is a commission appointed by the Governor. Generally, the separate commissions are charged with responsibility for policy and the administration of the programs under their supervision, subject to the management authority of the Secretary. Each commission replaces a state policy board that formerly held the powers and duties now shared by the Secretary, the Board of Human Resources, and the director and commission of the division. Most important, the commissions no longer control personnel policies and practices, nor do they make independent budget presentations to the General Assembly. The general thrust of state reorganization has been to centralize general administration and budget making in the Secretary and Board of Human Resources and to permit the Secretary and the Governor to organize and reorganize the programs within the Department in any manner that seems likely to result in more efficient and effective provisions of services. For instance, the Secretary may establish or abolish any division of the Department with the approval of the Governor, and he may establish or abolish other administrative units or positions, transfer personnel between positions, and change duties, titles, and salaries without the Governor's approval.

ON THE COUNTY LEVEL, most major areas of human services are administered in a local department or agency by a county administrator, who implements policy set forth by a county board, following guidelines laid down by state and federal policy. The composition of these county boards is established by law, and their members are appointed in a variety of ways. For example, the board of social services is appointed partly by the State Board and partly by the county commissioners; the board of health is appointed by the commissioners, but must include certain professionals and public officials such as a licensed physician and the chairman of the board of county commissioners. Historically, each human services department within a county has operated independently of the others and in relative isolation. Some results of this separate approach are that:

(1) Each service agency is responsible for preparing, presenting and justifying its own budget requests to the county commissioners in isolation from other agencies.

(2) The independence of service agencies from each other discourages such efficiency measures as central referral, consolidated files, duplication of administrative operations, etc.

(3) The perspective of each agency on the total needs of the citizens of the county is limited to the relatively narrow program that each undertakes.

(4) Gaps in service are created when the total human resources needs of a person are not met by one of the existing county services. For example, an alcoholic appealing to an alcoholic rehabilitation agency may also need public assistance, mental health treatment, or other social services. The present fragmentation limits the help that a single agency can offer even though this person's total needs might not have been met.

(5) Service agencies are often located in widely separated parts of a city and may even be located in different cities. This physical separation presents two other impediments to helping the person in need—travel and distance. To receive the appropriate services he may need, a citizen may have to travel some distance to other agencies. In some instances, that distance and the necessary travel may become insurmountable obstacles in his effort to obtain further help; he may not have a car or money for a taxi, and there may not be adequate public transportation available.

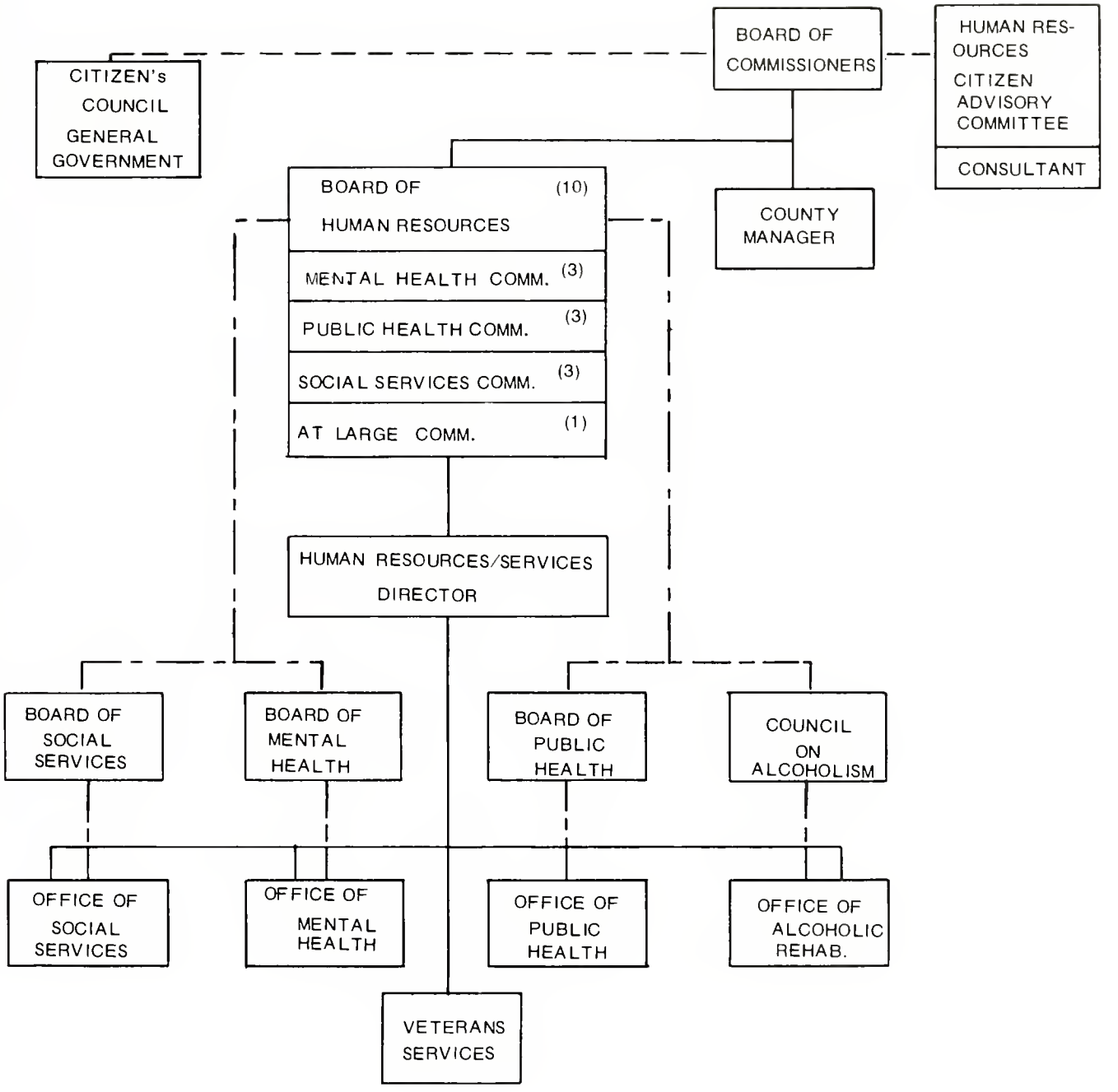
(6) The dissociation of these various services makes it difficult for county managers and county commissioners to evaluate the work of a single agency and its impact on the human needs of the community. With this inability to evaluate the adequacy of a program, the commissioners have little real basis for making funding judgments on existing programs or evaluating agency requests for new or expanded services.

For these reasons, the need for reorganizing the human services delivery system to achieve greater coordination becomes clear, and there is widespread interest at both the local and state levels in finding the best way to provide for more effective delivery of human services through new organizational approaches.

IN GENERAL, HUMAN SERVICES are administered within the boundaries of a single county, but some health and mental health programs have been developed on a regional basis that involve several counties. Though the General Assembly has authorized the provision of social services on a regional basis, this authority has not yet been used, and each county has its own social services program. Still, because of the problems just pointed out, several counties have begun to plan ways to unify their human resources programs. Their planning activities are based upon legislation enacted by the 1973 General Assembly that permits county boards of commissioners to reorganize county government as they see fit within the existing law, except that this blanket authority does not extend to certain extant boards—primarily those associated with human resources. A county may plan for reorganization of human services within its boundaries in several ways. One approach is to seek more effective coordination of delivery of human services within the existing legal framework. Another is to secure legislative authority—by special legislation or changes in the general laws applicable to local governments—to authorize local governments to reorganize existing local boards and departments that provide human services.

Two counties have each adopted one of these alternatives. Mecklenburg secured legislation in 1973 applicable in counties with a population over 325,000 (thus it apparently applies only in Mecklenburg) that authorizes the county commissioners to assume direct control over programs previously conducted through separate county boards and to have all the powers and duties of these boards. Mecklenburg has held the required public hearings and is planning a building to serve as a central intake or access point to the various human services provided by the county. The separate, independent local boards of social services and health will become advisory.

CATAWBA TOOK THE OTHER ROUTE. It chose to work within the existing law and began a planning process with the local boards and administrators affected. Over a two-year period, it has devised a program to work toward coordinating and improving the delivery of human services. The following material is



The Human Resource Director is appointed in conformance with the personnel regulations of Catawba County by the Board of Commissioners upon recommendation of the Human Resources Board.

Fiscal, administrative policies, and approvals are directed through the Director.

The Board of Human Resources provides state and federal policy coordination and local program development and review.

The Board of Human Resources consists of ten members from present policy boards, three from the public health board, three from the mental health board, and one at large member.

The chairman is chosen by the respective members and does not serve more than two terms.

Within the Human Resources Board, four subcommittees, consisting of not more than three members each, co-ordinate with each of the three main activities and boards under the Human resources Department.

The citizens council is called in as needed to provide lay input. This arrangement is as flexible as circumstances require.

an account of what the Catawba County Board of Commissioners has done to bring about this desired result through local leadership.

THE PLAN THAT HAS BEEN devised for Catawba calls for a Human Resources Program Area concept, in which areas of human need are defined and the resources of all human services departments are brought together as required to offer a program of help in each area. To serve as a coordinating and liaison agency among the various departments, a Human Resources Board has been proposed, to be appointed by the county commissioners. County commissioners have authority under existing law to create and appoint such a board.

In the projected implementation of the plan, the Human Resources Board will be composed of members of the county boards of the present independent human services departments. On an interim basis, the board is to be advisory—assuming no operational activity in the special areas of the present boards but encouraging and fostering cooperation at the policy level. Eventually, if a general law is enacted authorizing local governments to reorganize existing local boards over all human resources programs and departments that provide human services, the board will be given responsibility over human resources in the county and the present individual boards will be abolished or become citizen advisory boards. The board, by use of subcommittees, will deal with the specific problems faced by the individual agencies. Even in the interim period, such a board, representing all of the human services agencies will be a unified, knowledgeable body with a total perspective of human resources in its dealings with the county commissioners in regard to administrative, policy, and fiscal matters. It will serve a liaison function among the various agencies, and it will permit a single budget for the entire area of human resources to be proposed and presented to the commissioners for a unified program approach.

The county commissioners are also empowered to appoint or cause to be created a citizens' council, which is another element in the plan for coordinated human services delivery. This body would serve as a lay advisory group to county government in general. It would be broadly based, reflecting the geographic, demographic, political, and socioeconomic make-up of the county, and would include members of those public and private community service programs that know what the community resources and needs are.

Ideally, the structure of such a citizens' council would be kept as flexible as possible. A subgroup of the council might be designated to act in an advisory capacity in the area of human resources, defining the existing problems and pointing out other needs in the county not now being met through either public or private sources.

Its present authority also permits the Board of Commissioners to hire a human resources director, and it is this person who would be the key figure in bringing all of the efforts together for a total human resources program for the county. His job would require that he be alert in all areas under the human resources designation and accountable for the results of their activities. The director would be appointed by the Board of Commissioners upon recommendation of the Human Resources Board, to work closely with all people responsible for human services policy and administration. As planned, he would coordinate both the administrative and program actions of each agency, with the help of the administrator of that agency. This coordination would be accomplished by placing administrative responsibilities (such as intake records, bookkeeping, and state and federal program coordination) in the director's office. The director would also be empowered to contract with private agencies to expand service capabilities within the county. He would also be responsible for program area planning. This refers to the process by which a many-faceted human services program is devised that uses resources from each of the various human services agencies.

THE WORK THAT RESULTED in this plan for coordinating Catawba human services delivery system was done by the Catawba County Board of Commissioners and responsible officials in the human resources field over a period of two years. To date, the following actions have been taken to implement the plan.

1. On July 2, 1973, the commissioners adopted the reorganization plan that includes the concept of a county Department of Human Resources (see the diagram on page 43).

2. The Board of Commissioners has discussed the proposals with all of the independent boards involved and has been well received. These boards have expressed a willingness to move toward such a program.

3. The Board of Commissioners has already consolidated the personnel functions of the county-level human services agencies (screening, interviewing, etc.) into its own central personnel department, leaving the final decision in employment of new personnel to the appropriate agency director.

4. The Board has appointed a Human Resources Study Committee to study the needs of the community; the level of financial commitment of county, public, and private organizations; the level of proficiency and efficiency of the human resource agencies involved; and where changes could and should occur in the present human services delivery system. After these areas have been studied, the committee's findings will serve as important input into the commis-

sioners' decision-making activities. The study committee's function, then, is continuously to assess community needs. At all times, however, the commissioners retain complete freedom in electing to pursue structural changes in the way human services are provided, including hiring a director, seeking special legislation, or generally coordinating in other ways to improve services. In addition to the legal fact that certain of the commissioners' duties cannot be delegated, the reason for stipulating this freedom is that sometimes action must be taken in parallel rather than in sequence. Decisions must sometimes be made in conjunction with events that may be outside the planning and study efforts.

5. The Board of Commissioners has directed the county manager to retain a consultant for the county to serve as staff to the study committee.

6. The Board has directed that the architect hired to draw up plans for the county's new Mental Health Center include in his plans a scheme to include facilities for public health, social services, and other related services on the same site, thus providing physically for a central place of intake in human services. This entire facility would be built on the site of the county's hospital, which is centrally located and easily accessible from all points in the county.

7. The Board has directed that a public hearing be held with members present from all the boards and agencies involved to discuss the initial movement toward this concept of coordinated human services and to answer questions from the public.

Catawba County is clearly actively involved in developing a program for improving its human services delivery system, and it foresees that the other human service areas like alcoholic rehabilitation, veterans' service, and job counseling will quite logically be brought into the total plan.

The county feels that at a minimum it will have improved its human services by taking a thorough inventory of needs and available resources and by involving a number of interested citizens in the decision-making and information-gathering processes.

In summation, Catawba's aim is to improve the efficiency of present services in the area of human resources and avoid future costs through coordination. This coordination can be achieved under a system that uses a leadership concept to draw all of the county's human services resources together in a coordinated program and a single board strong enough and knowledgeable enough to be of advisory service to the commissioners and, ultimately, the citizens of the county. Such a reorganization and restructuring of services will produce a basis for evaluating the worth of these human service programs.

Those who have been involved in planning for this project freely admit that they will be feeling their way for a time in implementing the plan, but they believe that the very process of considering the services and analyzing their problems will make it possible to improve those services and lead to explorations for even better ways of coordinating and delivering help to those who need it.

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