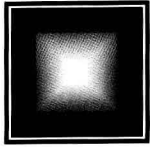


# PUBLIC FINANCE

and the American Economy



NEIL BRUCE



# PUBLIC FINANCE and the American Economy

*Neil Bruce*

*University of Washington*



**ADDISON-WESLEY**

---

An imprint of Addison Wesley Longman, Inc.

Reading, Massachusetts • Menlo Park, California • New York • Harlow, England  
Don Mills, Ontario • Sydney • Mexico City • Madrid • Amsterdam

---

---

Sponsoring Editor: Denise Clinton/John Greenman  
Production Supervisor: Heather Garrison  
Senior Marketing Manager: Quinn Perkson  
Production Services: Ruttle, Shaw & Wetherill, Inc.  
Cover Designer: Diana Coe  
Cover Illustration: Eileen Hoff

Copyright © 1998 by Addison-Wesley Educational Publishers, Inc.

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of the publisher.

### Library of Congress Cataloging-in-Publication Data

Bruce, Neil.

Public finance and the American economy / Neil Bruce.

p. cm.

Includes bibliographical references and index.

ISBN 0-321-01167-8

1. Finance, Public—United States. 2. Local finance—United States. 3. Government spending policy—United States. 4. Fiscal policy—United States. 5. Entitlement spending—United States. 6. Debts, Public—United States. 7. United States—Economic policy—1993— I. Title.

HJ257.2.B78 1997

336.73—dc21

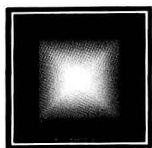
97-30044

CIP

*Reprinted with corrections, November 1998*

Printed in the United States of America.

2 3 4 5 6 7 8 9 10—MA—02 01 00 99 98



# *Preface*

Writing a textbook on American public finance at this time has been like reporting a horse race while it is still in progress. When I began, the track was crowded with entries, some of which—like Health Care Reform—hardly got out of the starting gate. Others, like Flat Tax, appeared as contenders in the heat of the presidential race but faded in the stretch. One two-year-old—Budget Impasse—practically stopped the race. Unlike a horse race, however, the contest among public policies has no finish line. We can be sure that none of the challengers named here is out of the race for good; the same issues that grabbed the headlines during the past few years will continue to absorb the nation's attention for years to come.

One of the main reasons I wrote this book is my conviction that a good understanding of public finance is essential for interpreting and understanding the profusion of fiscal events and proposals that occupy national attention, from cutting capital gains taxes to privatizing social security. These policies and proposals can affect our lives in important ways, yet because they frequently are poorly understood—even by knowledgeable people—they are easy to politicize and difficult to amend. To corroborate this, one need only look at the often acrimonious budget debates. Although current issues and policy debates motivate and illustrate the substance of public finance in this book, I also relate the issues and debates to the enduring questions of public finance: What is the appropriate role of government in a market economy? How do government programs affect the economy? How should the programs be financed? Who will benefit, and who will pay? These fundamentals provide the necessary background for putting the diverse array of policies in the right perspective.

Another reason for this textbook is my view that public finance is an excellent subject for students seeking to apply economic theory and methods to interesting real-world problems. Many of my own students, initially skept-

tical toward economic theory because they thought it too abstract and divorced from real-world issues, became enthusiastic about economics by taking public finance because it showed them how to think about and understand important issues—such as using pollution permits to reduce the cost of environmental protection and charging tolls to reduce highway congestion. Students learn economics best by applying it to practical issues, whether balancing the budget or reforming welfare. I wrote this book with the need to engage and motivate students utmost in mind.

The text is directed at seniors or juniors who have taken a course in intermediate microeconomics, or at least a solid principles course using analytic tools such as the indifference curve diagram. Nonetheless, I have aimed to make the book accessible to students with more limited backgrounds who are willing to do some preparation. Specifically, the text emphasizes intuitive and diagrammatic explanations wherever possible, and it avoids mathematical expressions unless necessary. Chapter appendixes cover the more difficult analytic material, and a main appendix reviews the core concepts of microeconomic theory used throughout the book.

In writing this book, I have also wanted to share with readers my interests in and enthusiasm for public finance. At a time when popular views about government seem divided between fanciful idealism and relentless cynicism, a subject that so clearly identifies the objectives good government can accomplish while recognizing the harm bad government can do is a much-needed corrective. My objective has been to present the subject in a manner that is comprehensive, balanced, up-to-date, and as interesting as possible. The main governmental spending and tax programs are described in what I hope is the optimal amount of detail: enough for interested readers to find what they need but not so much that they get lost in a sea of numbers. Description, however, has not been my main goal. Throughout the book, the economic ideas and concepts underlying the different programs are discussed, and the effects of the programs on the economy are analyzed.

I should mention also that I have aimed to write an honest book that conveys what economists know about the impact of government policies on the economy but does not gloss over the many defects and uncertainties in this knowledge. While I have not shied away from discussing unresolved differences on empirical and conceptual matters, I have avoided debates and controversies that are purely doctrinal or ideological. My guiding principle has been to present economics as a method of understanding the economic functions of government and the ways they can best be achieved.

---

## *Content and Organization*

Although the book is organized traditionally, with the chapters divided equally between spending programs and revenue policies, it features many new and useful approaches to public finance and some important differences in emphasis from other textbooks. Part I examines the economic roles that government plays in a market economy. Chapter 1 opens with a comprehen-

sive statistical overview of government and highlights the budget process; uncontrollable government spending; and “hidden” government spending, such as tax expenditures, loan guarantees, and regulations. In Chapter 2, welfare economics provides a coherent framework for understanding the choice between markets and government. The chapter explains economic efficiency in clear intuitive terms and illustrates the concept of market failure with several examples, including the problem of “orphan drugs.”

Part II focuses on government programs that reallocate the use of the economy’s resources. Chapter 3 presents an engaging example illustrating efficient outputs of public goods and introduces some novel aspects of public good theory, such as the free-rider problem as a type of prisoner’s dilemma problem, and the application of public good theory to policies regarding knowledge capital and technology. Recent developments in network externalities, as well as conventional forms of externalities, are covered in Chapter 4. An especially useful feature of this chapter is an extensive and up-to-date discussion of environmental policy alternatives. Given the importance of the “new federalism,” an entire chapter—Chapter 5—is dedicated to state and local spending. This chapter develops fiscal federalism as a framework for understanding the issues raised by the intense current interest in devolving federal programs to the states.

In Part III, public choice and benefit-cost analysis reveal different sides of the government decision-making process. A structured treatment of voting theory and of the incentives facing bureaucrats—topics of mounting importance in public finance—is found in Chapter 6. Chapter 7 offers an emphasis on benefit-cost analysis that is different from what is usually found in such chapters. Rather than stressing the mechanics of discounting, the chapter focuses on the methods of measuring benefits and costs, especially non-market goods. It includes a description of the property-value and travel-cost methods, as well as an evaluation of the controversial contingent valuation method.

The three chapters in Part IV describe the latest advances in the spending programs for welfare, social security, health, and education, which now constitute the bulk of government spending. The main poverty programs are described in Chapter 8, which also reports the latest developments in the welfare debate, including the far-reaching reforms of 1996. The analysis of the social security program in Chapter 9 includes a discussion of how the program redistributes income, and also evaluates recent proposals for reform, such as privatizing the program or investing the trust fund in stocks. This chapter also covers unemployment compensation programs. Chapter 10, on government programs that enhance human resources, gives equal weight to education and health care.

The remaining chapters cover the tax system and tax policy issues. The three chapters in Part V provide a solid foundation for understanding the tax system. Chapter 11 introduces students to the effects of taxes on the allocation of resources, using an excise tax as a model. Chapter 12 features an unusually detailed explanation of tax incidence. In addition to the standard analysis of forward and backward shifting, the chapter contains a step-by-

step calculation of the incidence of an excise tax across income groups and discusses new developments, such as lifetime incidence and generational accounting. Methods of evaluating tax policy, including an intuitive diagrammatic explanation of optimal tax theory, are highlighted in Chapter 13. The chapter stresses the criteria of equity and administrative costs, as well as economic efficiency, for determining desirable tax policies.

Part VI provides a comprehensive and up-to-date examination of the federal income tax system and its impact on household behavior. Chapter 14 describes the structure of personal income and payroll taxes using the Haig-Simons concept to identify the main selective features. The effects of these taxes on household behavior, including recent empirical results, are presented in Chapter 15, which also discusses the politically sensitive topic of tax expenditures, like the mortgage interest deduction. Chapter 16 covers business income taxes more thoroughly than usual by emphasizing the principles that define business income, as well as the details of the corporate income tax system.

The chapters in Part VII explore topics that often receive too little attention. Taxes on consumption and wealth, including federal excise and estate taxes, state retail sales taxes, and local property taxes, receive special attention in Chapter 17. The chapter explains the technical and policy issues associated with taxing consumption under a VAT and a personal consumption tax, such as the recently proposed “USA tax.” Chapter 18 is unique to this book. It provides a full treatment of multijurisdictional tax issues, including state and local taxes, tax exporting and tax competition, formula apportionment and unitary taxation, and the taxation of multinational enterprises. Varying views on the dangers of deficit finance are explained in Chapter 19. This chapter highlights the latest developments in this area, including Ricardian equivalence, alternative ways of measuring the deficit, optimal deficit policy, the burden of government debt, and the merits of a balanced budget amendment.

---

## *Some Special Features*

In addition to presenting the most important and up-to-date developments in public finance, I have tried to preserve the traditional core of the subject and to place recent fiscal events in a historical perspective where appropriate. Several features, I believe, distinguish this book. Some of the most notable are described below.

### *Increased Attention to Issues of Fairness and Distribution*

Although economists are famous for stressing efficiency, in polls people express great concern about issues of fairness in public policy. In the policy sections of this book, I make an effort to pay more attention to equity criteria than is common in public finance textbooks. Some examples are the identification of equity principles, the use of the social welfare function and distri-



butional weights, the trade-off between efficiency and equity, and the interplay of equity and efficiency in setting desirable tax rates on different goods.

*Fuller  
Treatment of  
State and Local  
Public Finance  
Issues*

Given the growing importance of the “new federalism,” I was determined from the outset to write a textbook that gives more weight to the fascinating public finance issues facing state and local governments. There are two full chapters on these issues—one on spending and another on taxes—presented in the appropriate parts of the book. Readers can find topics on state and local governments in other chapters as well.

*Extensive Use  
of Examples*

The relative price of one picture is a thousand words, so I did my best to gather as many interesting and illuminating examples as I could find. Most chapters feature two boxes drawn from newspapers, journals, current research, or the World Wide Web that illustrate or offer an interesting perspective on the topics covered in the chapter. In the narrative itself, I use numerous other examples to clarify abstruse ideas and consolidate students’ understanding of the material.

*Summary of  
Recent  
Empirical  
Research*

Throughout the book, I have attempted to communicate what economists know about how government programs and policies affect the economy. To this end, I have drawn on the latest empirical results, including, for example, the effects of welfare programs on household behavior, the influence of the “marriage tax” on marital decisions, and the impact of IRAs on saving.

*Emphasis on  
Practical  
Applications*

Although the book contains a fair amount of intermediate microeconomic theory, including the labor-leisure model and the intertemporal choice model, I have avoided theory for theory’s sake. Rather, I have stressed the practical application of microeconomic theory as a tool for understanding the impacts of government policy, such as the effect of a tax credit on the labor supply and the effect of a deficit on household saving.

---

## *Instructional and Learning Aids*

In addition to the features already mentioned, such as the boxes on illustrative topics, the book offers several other instructional and learning aids.

- **Captioned diagrams.** The text contains more than 100 diagrams and figures accompanied by descriptive captions that enhance the text discussion and help students review the material.
- **Appendix on microeconomics.** As mentioned, the book is directed at students who have already taken a course in intermediate microeco-



nomics. To help students who lack this background or want to refresh their memories, I have included an appendix at the end of the book that reviews some of the most important elements of microeconomic theory.

- ***Conclusions and summaries.*** Following the text of each chapter, a concise conclusion recaps and ties together the chapter's main points and draws out larger ideas. A bulleted summary—a handy study aid for students—further reviews the essential chapter contents.
- ***Problems.*** Each chapter is followed by several carefully chosen Questions for Discussion and Review, designed to probe students' comprehension of the chapter material. These include factual questions, computational problems, and conceptual questions suitable for classroom discussion.
- ***Key terms and glossary.*** Important terms and expressions are introduced in boldface and are clearly explained or defined. For reference, the key terms and their definitions are collected in a Glossary at the end of the book.
- ***Selected and consolidated references.*** Each chapter concludes with a selection of references, with descriptions that are useful for readers who want to delve further into the topics presented. Numerous Internet sources are included. At the end of the text, a Consolidated References section provides detailed publishing information for these references.

---

## *Supplements*

An Instructor's Manual is available to adopters of the text. It contains chapter summaries, lecture suggestions, answers to the problems presented in the text, and questions and problems suitable for tests and examinations. The Instructor's Manual draws on my experience in teaching public finance to undergraduate students over the past twenty years.

---

## *Acknowledgments*

As an economist, I find it a special irony to acknowledge the enormous help given me by others. In a discipline that expounds theories of self-interested individuals, it is heartening to recognize the unselfish acts of others. I have been particularly fortunate in this regard, having received valuable contributions from several editors, numerous reviewers, generous colleagues, helpful students, and concerned relatives.

I would like to thank the staff at HarperCollins for helping to get the book off the ground, especially Jack Greenman, the acquisitions editor who talked me into writing it; Lisa Pinto, who gave me wonderful advice on a first clumsy attempt; and project editor Arlene Bessenoff for coordinating the early chapters. I am even more grateful to the staff at Addison Wesley Longman for helping me finish the book: notably Jack Greenman, whose as-

sociation with the project continued, to my delight; senior editor Denise Clinton; and senior development manager Sylvia Mallory, my project editor, whose judgment, advice, and deadline reminders were essential to my completing the project. I owe special thanks to my development editor Elisa Adams, whose friendly but incisive critiques on all chapters were indispensable, and whose timely encouragement was much appreciated. Thanks also to Peg Markow and the production staff at Ruttle, Shaw and Wetherill for an outstanding job.

The content of the book was greatly improved by comments and suggestions from my colleagues Gregory Ellis, Robert Halvorsen, Shelly Lundberg, and Cindy Madden at the University of Washington, who read various chapters. Helpful comments on the chapter about public goods were provided by Todd Sandler at Iowa State University. I want to thank my many students in public finance who acted as unwitting guinea pigs for my class-testing of chapter ideas, especially Michelle Dior, public finance student *extraordinaire*, who read all the draft chapters and gave me invaluable feedback from a student's perspective. I owe a special debt of gratitude to Janis Bruce, who not only helped me with the manuscript but provided unswerving patience and support.

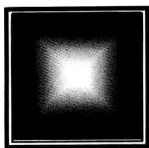
I would also like to thank my terrific reviewers, many of whom served well beyond the call of duty. Scores of their fine suggestions are reflected in the final product, and dozens more are not because I wasn't smart enough to do it. They are:

Jim Alm, University of Colorado, Boulder  
 Gary Anderson, California State University, Northridge  
 John H. Beck, Gonzaga University  
 Robert A. Blewett, St. Lawrence University  
 Robert T. Bray, California State Polytechnical University, Pomona  
 Paul Farnham, Georgia State University  
 Robert Fischer, California State University, Chico  
 Mary N. Gade, Oklahoma State University  
 Gary M. Galles, Pepperdine University  
 Fred Giertz, University of Illinois, Urbana  
 Timothy Gronberg, Texas A&M  
 Jonathan Hamilton, University of Florida  
 Charles Hawkins, Lamar University  
 Thomas Ireland, University of Missouri, St. Louis  
 Alan Kessler, Providence College  
 David Kiefer, University of Utah  
 Bruce R. Kingma, State University of New York, Albany  
 Gary D. Lemon, De Pauw University  
 Stephen E. Lile, Western Kentucky University  
 Jerry Miner, Syracuse University  
 Susan Parks, University of Wisconsin, Whitewater  
 George Plesko, Northeastern University

Thomas Pogue, University of Iowa  
Esther Redmount, Colorado College  
Paul Rothstein, Washington University  
Jeffrey Rubin, Rutgers University  
Daniel G. Rupp, Fort Hays State University  
Bernard Saffran, Swarthmore College  
Kathleen Segerson, University of Connecticut  
Wendell Sweetser, Marshall University  
David Terkla, University of Massachusetts, Boston  
Richard Tresch, Boston College  
Nancy White, Bucknell University  
Nancy Williams, Loyola College

Finally, I must make the obligatory disclaimer. I, and not the aforementioned individuals, am to blame for any remaining errors or shortcomings.

N. B.



# *Contents in Brief*

*Preface* xxiii

## **PART ONE**

---

### ***The Role of Government in a Market Economy* 1**

- 1 Sizing Up the Government 3
- 2 Understanding the Economic Role of Government 30

## **PART TWO**

---

### ***Government and the Allocation of Resources* 63**

- 3 Public Goods in Theory and Practice 65
- 4 Externalities and Public Policy 98
- 5 Spending by State and Local Governments 132

## **PART THREE**

---

### ***The Government Decision-Making Process* 171**

- 6 Voting and Public Choice 173
- 7 Evaluating Programs Using Benefit-Cost Analysis 215

## PART FOUR

---

### *Government and the Distribution of Income*    253

- 8   Spending on Programs to Alleviate Poverty    255
- 9   Social Security and Unemployment Compensation    294
- 10   Health Care and Education    333

## PART FIVE

---

### *The Basic Theory of Taxation*    367

- 11   Taxation and the Allocation of Resources    369
- 12   Tax Incidence Analysis: Who Bears the Tax Burden?    406
- 13   Elements of Tax Policy Analysis    441

## PART SIX

---

### *Income Taxation in the United States*    479

- 14   The Structure of Taxes on Personal Incomes    481
- 15   How Income Taxes Affect Household Behavior    514
- 16   Taxes on Business Income    555

## PART SEVEN

---

### *Topics on the Government Revenue Structure*    593

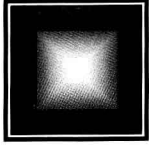
- 17   Taxes on Consumption and Wealth    595
- 18   State, Local, and Multijurisdictional Tax Issues    633
- 19   Deficit Finance    658

*Appendix*    A-1

*Glossary*    A-18

*References*    A-30

*Index*    A-37



# Contents

*Preface* xxiii

## PART ONE

---

### *The Role of Government in a Market Economy* 1

#### **1** *Sizing Up the Government* 3

What Is the Government? 4

The Size and Growth of Government 5

Government Spending in Other Countries 7

The Growth of Government 8

The Composition of Government Spending 9

Government Spending by Function 10

Government Spending by Jurisdiction 11

Financing Government Spending 12

Accounting for Government 14

The Unified Budget 17

Controllable and Uncontrollable Spending 18

BOX 1.1 When Is an Increase in Spending a Spending Cut? 19

Governing Without Spending 19

*Tax Expenditures* 20

*Loans and Loan Guarantees* 21

*Regulations and Mandates* 22

BOX 1.2 How the Visibility of Spending Can Perversely Affect

Government Incentives 23

<b>The Impact of Government on the Economy</b>	<b>24</b>
The Impact on Allocation of Resources	24
The Impact on Distribution of Economic Well-Being	26
The Impact on Prices and Factor Rewards	27
<b>Conclusion and Summary</b>	<b>27</b>
<b>Questions for Discussion and Review</b>	<b>28</b>
<b>Selected References</b>	<b>29</b>

## **2**     *Understanding the Economic Role of Government*     **30**

<b>Positive and Normative Economics</b>	<b>30</b>
<b>The Definition of Social Welfare</b>	<b>31</b>
Economic Efficiency and Pareto's Criterion	32
Distributional Equity and Efficiency	33
<b>The Efficient Economy</b>	<b>35</b>
Marginal and Total Willingness to Pay	36
Conditions for Economic Efficiency	38
<i>Conditions for Efficiency in Production</i>	40
<i>Measuring the Cost of Inefficiency</i>	41
<b>Economic Efficiency, Markets, and Government</b>	<b>42</b>
Adam Smith's Invisible Hand	43
Market Failure and the Functions of Government	44
<i>Orphan Drugs</i>	45
<i>Public Goods</i>	47
<i>Market Externalities</i>	47
<i>Insurance Market Failure</i>	48
<b>Introducing Distributional Equity into Welfare Economics</b>	<b>49</b>
Four Principles of Equity	49
Expressing Equity in a Social Welfare Function	50
The Distributional Weights Approach	53
<b>In Search of the "Second-Best"</b>	<b>54</b>
Why Not the Best?	55
Illustrating the Equity-Efficiency Trade-Off	55
<b>Conclusion and Summary</b>	<b>56</b>
<b>Questions for Discussion and Review</b>	<b>57</b>
<b>Selected References</b>	<b>58</b>
<b>Appendix: Illustrating Economic Efficiency with the Box Diagram</b>	<b>59</b>

## **PART TWO**

---

### *Government and the Allocation of Resources*     **63**

<b>3</b> <i>Public Goods in Theory and Practice</i>	<b>65</b>
Nonrival and Nonexcludable Goods	65



<b>Efficient Output of a Public Good</b>	<b>67</b>
An Illustration: Planning a Party	67
Comparing Efficiency Conditions for Public and Private Goods	69
<b>Market Failure with Public Goods</b>	<b>73</b>
Nonexcludability and the Free-Rider Problem	73
The Inefficiency of Using Prices to Ration Public Goods	76
Problems in Providing Public Goods	78
<b>Mixed Public Goods</b>	<b>79</b>
Congestible Public Goods	79
Local Public Goods	80
<b>Applications of Public Good Theory</b>	<b>81</b>
Defense Spending in the United States	81
<i>Does the United States Spend “Too Much” on National Defense?</i>	82
<b>BOX 3.1 The Changing Rationale for Defense Spending</b>	<b>84</b>
<i>Cost Efficiency in National Defense</i>	85
The National Highway System	88
Technology Policy: Patents Versus Government R&D Spending	90
<b>BOX 3.2 Variable Tolls on a California Highway</b>	<b>91</b>
<b>Conclusion and Summary</b>	<b>92</b>
<b>Questions for Discussion and Review</b>	<b>93</b>
<b>Selected References</b>	<b>94</b>
<b>Appendix: Efficiency Conditions in a Production Economy with a Public Good</b>	<b>94</b>

**4**

***Externalities and Public Policy* 98**

<b>Types of Externalities</b>	<b>99</b>
Cost and Benefit Externalities	99
Consumption and Production Externalities	99
Network Externalities	100
<b>Externalities and the Efficiency of Markets</b>	<b>100</b>
Relevant and Irrelevant Externalities	104
Market Inefficiency and Network Externalities	107
<b>Externalities and Property Rights</b>	<b>108</b>
The Tragedy of the Commons	108
<b>BOX 4.1 Network Externalities and Efficiency: “The Fable of the Keys”</b>	<b>109</b>
The Reciprocal Nature of Externalities	111
Bargaining and the Coase Theorem	112
<b>Environmental Pollution as a Cost Externality</b>	<b>113</b>
<b>BOX 4.2 Coase Goes to Hollywood</b>	<b>114</b>

<b>Government Policies for Controlling Externalities</b>	<b>117</b>
Command and Control Policies	118
Variable and Tradable Permits	119
Effluent Charges and Corrective Taxes	123
Assigning Property Rights	127
<b>Conclusion and Summary</b>	<b>128</b>
<b>Questions for Discussion and Review</b>	<b>130</b>
<b>Selected References</b>	<b>131</b>

## **5**     *Spending by State and Local Governments*     **132**

<b>How State and Local Governments Differ from the National Government</b>	<b>132</b>
<b>State and Local Government Spending</b>	<b>133</b>
Composition of State and Local Spending	134
Demand for Local Government Spending	135
<b>The Theory of Local Public Goods</b>	<b>138</b>
Jurisdictional Spillovers	138
Local Public Goods and Community Size	139
Accommodating Different Tastes for Public Goods	139
The Tiebout Hypothesis: “Voting with One’s Feet”	142
<i>Assumptions Needed for Tiebout Hypothesis</i>	142
<i>Limits of the Tiebout Hypothesis</i>	143
<i>Jurisdictional Spillovers: Charles Tiebout Meets Ronald Coase</i>	145
<b>BOX 5.1 Loan-a-Cop</b>	<b>146</b>
<b>The Economic Theory of Federalism</b>	<b>147</b>
Benefits of Decentralization	148
<i>Greater Voice</i>	148
<i>Greater Choice</i>	149
<i>Competition and Innovation</i>	150
<i>Benefit Principle of Equity</i>	150
The Benefits of Centralization	151
<i>Internalizing Jurisdictional Spillovers</i>	151
<i>Avoiding Beggar-Thy-Neighbor Policies</i>	151
<i>Economies of Scale</i>	152
<i>Horizontal and Vertical Equity</i>	152
<b>Intergovernmental Grants</b>	<b>153</b>
Effects of Different Types of Grants	154
<i>Noncategorical Grants</i>	154
<i>Categorical Grants</i>	157
<i>The Flypaper Effect</i>	161
<i>Equalizing Grants in Education</i>	163
Tax Expenditures for State and Local Government	164
Intergovernmental Grant Policy	165
<b>Conclusion and Summary</b>	<b>167</b>