

Is the Federal "Branch Office" Ready for a Promotion? Managing Budget Cuts at the State Level

by Ferrel Guillory



In his campaign to reduce federal domestic spending, President Reagan has ridden on the coattail of a myth — that the enormous growth in social programs in the past two decades has been accompanied by an equally enormous expansion of the federal bureaucracy. In fact, the creation of hundreds of federal programs contributed to a substantial growth in bureaucracy in state and local governments, not in the federal bureaucracy. "Although federal programs, budgets, and regulations have grown markedly over the past 20 years, federal domestic employment — perhaps the best single indicator of the direct national role — has held almost steady," said a recent report of the Advisory Commission on Intergovernmental Relations (ACIR).¹

In 1962, the federal government had 160 grant-in-aid programs, costing about \$7 billion. The number of these programs had doubled by 1967 and tripled by 1978, with the cost rising to \$85 billion. Federal civilian employment rose from 2.5 million in 1962 to a peak of 3.0 million in 1967. During the 1970s the number went down, ending that decade at 2.9 million. The number of federal civilian employees actually declined during the 1970s.²

If the number of federal programs and dollars has increased, why hasn't federal civilian employment grown commensurately? "The federal government has sought to exert its increasing influence indirectly, through the carrot-and-stick of subsidy and regulation" explains the ACIR report. "State and local governments remain the dominant service providers in every domestic field — except social security, the postal service, money and banking, and certain regulatory areas." Consequently, the number of state and local government employees has more than doubled in the last 20 years, the period during which the number of federal grant-in-aid programs has exploded. In North Carolina in the last 15 years, the number of teachers and state employees grew by 69 percent, from 108,000 to 181,000.³

For 20 years, then, North Carolina and other states increasingly served as branch offices of the federal government. Policymaking centered more

and more in Washington, as the federal government sought to fight poverty and hunger, clean up the environment, train people for employment, and stimulate community development. State governments accepted federal money, matched it with their own, and operated federal programs according to federal directives.

But now the Reagan administration, with the assistance of Congress, has begun to change things. Most visibly, they have sent less money down the pipeline from Washington, which will adversely affect the everyday lives of millions of North Carolinians. As important as the amount of money, however, is the way the federal budget cuts are taking place. Using sweeping fiscal techniques — grouping individually-funded programs into "block grants" and changing eligibility requirements in social services programs — Reagan and the Congress have turned over to the states more responsibility for setting policy and priorities. In addition, they have simply ended the financing of programs like the public service jobs component of the Comprehensive Employment and Training Act (CETA). These federal actions have forced states to face a choice of no longer having a program or using state monies to carry on a particular task or service.

State governments, which had been happily handing out benefits paid for primarily by federal dollars, now have to hand out the news that benefits are being cut. Moreover, the promise of "federalism" — where states administer programs once run according to federal guidelines and mandates — is proving to be largely illusory. The major cuts are not in block grants, which the states can choose to administer, but in individually-funded programs — water and sewer construction, CETA jobs, university research grants, Medicaid — which cannot be administered at the state level with as much flexibility as can block grants. (See article on pages 36-42 for a full explanation of the

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main budget cuts in North Carolina and the method used for each cut.) State officials must now cope with the difficult task of determining new policy priorities and of meeting human needs with less money. "We're all sort of off balance," said an aide to Gov. James B. Hunt, Jr.

In August, President Reagan signed into law the Omnibus Budget Reconciliation Act, which set the maximum amount of money that Congress could appropriate for the 1981-82 federal fiscal year (Oct. 1, 1981-Sept. 30, 1982). This far-reaching piece of legislation grouped over 50 individually-funded programs into nine block grants, put federal budget ceilings on other programs not in block grants, and changed eligibility requirements and reimbursement mechanisms for "entitlement" programs such as Aid to Families with Dependent Children (AFDC) and Medicaid. While the Reconciliation Act is only an authorization bill and thus did not include final appropriation figures and provisions for many programs (these are to come late in 1981 and early 1982), it did indicate roughly how many federal dollars the state would lose.

The federal budget cuts hit North Carolina particularly hard in two areas that Gov. Hunt has set as high state priorities — economic growth and human development. Major grant reductions came in funds for water and sewer facilities and for job-training, areas which affect North Carolina's drive for economic diversification. Substantial federal cutbacks also came in AFDC, child nutrition, the Title XX grants that pay for child day care and other social services, and Medicaid — all significant in a state where about 15 percent of the population lives below the poverty level. Among the 860,000 North Carolinians who live in poverty, females head 58 percent of those households, and the heads of 30 percent of the households work but do not earn sufficient wages to raise the household above the poverty line. "They are hitting us in the very areas where we can't afford to lose if we are to grow," said Hunt, in an interview for this article.

State government has only just begun regaining its balance and looking ahead to the time when it must make some fundamental choices in response to the federal budget cuts. As a preliminary step, North Carolina has already informed the federal government that it would accept administration of six of the nine block grants: maternal and child health, social services, low income energy assistance, community services, preventive health, and alcohol, drug abuse and mental health.⁴ Hence, the state will decide how to distribute the federal funds available for programs in these

blocks. About 75 percent of the total formerly allocated for the individual programs grouped in the block grants are available to the states for the 1981-82 fiscal year.

A recent survey by the National Governors' Association found that, like North Carolina, most states were moving immediately to assume control of the block grants that were available for state takeover. If a state does not accept a block grant, the federal government will continue to administer the programs as categorical grants but at the reduced budget levels.

When the General Assembly returned to Raleigh in October for a "budget session," neither Gov. Hunt nor legislative leaders had developed a programmatic reaction to the federal cuts. Hunt said that his administration had not had time to make decisions about which programs to pick up: "It was a question of the time required to do it in a fair way." In addition, the Governor and legislators had a major political hurdle to surmount in enacting a salary increase for teachers and state employees. Legislators focused their attention on establishing future state revenues so as to permit the pay raise and finance special local projects rather than concentrating on how to provide a state cushioning of federal cuts. Consequently, during the October session, the Governor and the General Assembly took a hodge-podge of actions, mostly of a stop-gap nature:

1) In most cases, cuts were simply "passed

The Senate power structure huddles during the October budget session. From left: Sen. Kenneth Royall, Lt. Gov. Jimmy Green, Sen. Craig Lawing, and Sen. Harold Hardison.

Photo by Paul Cooper



through." Programs administered at the state level were scaled back by the approximate amount of money reduced in Washington. If the federal government cut a program by 25 percent, the legislature passed on that 25 percent cut at the state and local levels. The General Assembly did not offset the reductions, either by appropriating additional state funds or by raising taxes.

2) The legislature took some remedial action. In a variety of small, yet important, ways, it managed to help ease the transition to a slowed flow of federal funds. The legislature raised the standard of need for welfare, thus allowing some 450 families to keep AFDC, Medicaid, and Title XX social services.⁵ It also raised the payment for foster care and extended Medicaid to unborn children so that a poor woman with her first pregnancy could qualify for prenatal care. But the General Assembly did not appropriate an additional \$8 million for the Medicaid program, an amount which would have avoided some \$25 million in total Medicaid program cutbacks resulting from the new state-federal funding formula under the Reconciliation Act (see article on pages 43-48 for a full explanation of the Medicaid issue).

3) An expanded clean water bond issue was authorized. The legislature took this action in part to offset a \$34 million federal reduction in construction grants for water and sewer facilities and in part because the Governor promoted the issue as part of his campaign to recruit new industry. In early 1981, before the federal cuts, Hunt had sought a \$220 million bond issue, but he enlarged his proposal to \$300 million in response to the federal action. Before general obligation bonds can be issued in North Carolina, they must be approved in a statewide referendum. Even if voters approve the action, the uncertain condition of the national bond market may make it difficult to raise capital through bond sales. Although the bond legislation did not require an immediate outlay of state money, by authorizing the water and sewer bonds, the legislature made its first large step toward offsetting a substantial federal cut-back.

4) The legislature sought to give itself some power over block grants. Legislative leaders established a special mechanism for coping with the block grants with the intent to give itself added leverage in the priority-setting process. In

Legislators and Governor Clash over Budget Provisions

— The Legal Issues at Stake

by Ran Coble

"The legislative, executive, and supreme judicial powers of the State government shall be forever separate and distinct from each other."

— Article I, Section 6, the N.C. Constitution

"The Governor shall prepare and recommend to the General Assembly a comprehensive budget of the anticipated revenue and proposed expenditures of the State for the ensuing fiscal period. The budget as enacted by the General Assembly shall be administered by the Governor. . . ."

— Article III, Section 5(3), the N.C. Constitution

When the voters of North Carolina ratified Article III, Section 5 of the Constitution of 1971, neither they nor the legislature had any way of

knowing that only 10 years later federal block grant funds would be a part of subsequent state budgets. The budget administered by the governor in 1971 consisted of mostly state funds, and the federal funds that were available were tightly targeted by Congress. By 1981, the "Reagan revolution" had occurred, bringing with it a new system of federal funding.

In response to the federal initiatives, the 1981 General Assembly in its October session took two actions in House Bill 1392 that raise constitutional questions. First, it created a new Joint Legislative Committee to Review Federal Block Grant Funds (G.S. 120-80). Second, it gave the Joint Legislative Commission on Governmental Operations the power to review and approve any executive branch transfer of more than 10 percent of the money from one budget line to another (G.S. 143-23[b]). Various legal experts, as well as the Hunt administration, have questioned these provisions, thinking they may violate both the separation-of-powers clause of the state Constitution and the clause giving the governor the responsibility for administering the budget. Hunt has gotten an informal (and hence unavailable for publication) opinion from the Attorney General's Office on the issue, and he may eventually ask the N.C. Supreme Court for an advisory opinion.

The new provisions passed by the legislature

the revised appropriations legislation enacted in October, the General Assembly established a Joint Legislative Committee to Review Federal Block Grant Funds, with six House members appointed by the Speaker and six senators appointed by the Lieutenant Governor. The legislation gives the committee power to "review all aspects of the acceptance and use of federal block grant funds" and prohibited the executive branch from taking certain actions with regard to block grants without the prior approval of this committee of the General Assembly.

Gov. Hunt expressed concern about this special provision of the appropriations bill, along with another provision that requires the approval of the Legislative Commission on Governmental Operations for the executive branch to transfer funds over a certain amount from one line item to another. Although Hunt kept his objections low-key, the question arose as to whether these provisions violated the constitutional separation of the executive and legislative branches. One fallout of the Reagan budget cuts, therefore, may be a test of the constitutional balance between the legislature and the governor in North Carolina. (See box

on this page for an explanation of the legal issues involved.)

Whatever the outcome of this constitutional issue, the question remains: Are the General Assembly and the Governor prepared to cope with the new demands imposed by the federal cutbacks? There is hardly any doubt that state governments, including North Carolina's, are more sensitive to human needs and better prepared bureaucratically to run programs than they were when the federal government stepped in with its expansion of grants-in-aid 20 years ago. The state bureaucracy has ballooned in the last two decades and so has its ability to handle new administrative demands. But many federal social programs came about for the very reason that state legislatures failed to respond to human needs, so people turned to Washington. Having modernized itself with staff, computers, and new facilities, the N.C. General Assembly must now demonstrate its creativity and sensitivity — and its maturity as an institution — in reacting to federal cutbacks. Because the political-legislative process demands leadership in order to function well, the Governor,

raise two primary legal questions. Is the General Assembly interfering with the governor's power to administer the budget? And, can the General Assembly delegate budgetary review and approval powers to an interim committee for final action? The answers to these questions lie in the legal interpretations of G.S. 143-23(b), the restriction of funds provision, and the four subsections of G.S. 120-84(b) regarding block grants cited below, which forbid the executive branch from taking the following actions without prior legislative approval:

"(4) transfer of funds between block grants,
(5) intradepartmental transfer of block grant funds,

...
(7) adoption of departmental rules relating to federal block grant funds,

(8) contracting between State departments involving block grant funds,

..."

The North Carolina courts have interpreted the state Constitution to give the legislature the power both to appropriate funds for the public health, safety, and welfare and to oversee and review the executive branch. But in the new provisions enacted in 1981, the functions claimed by the legislature may clash with the constitutional power of the governor to *administer* the budget. Moreover, the legislature has vested

these extensive new budgetary powers in the hands of a few of its members — the 12 on the Joint Legislative Committee to Review Federal Block Grant Funds and the 13 on the Joint Legislative Commission on Governmental Operations.

While the legislative actions may appear to be an attempt to gain control of the new fiscal powers available to the states under "Reagan's revolution," political realities may prevent the constitutional questions from ever reaching a court of law. What matters ultimately is not what the new laws say but what the legislature and Gov. Hunt actually do. The Governor may refuse to comply with the new provisions which could force the legislators to sue him. Conversely, if the General Assembly exercises its new budgetary powers, the Governor may have to sue the legislators. But resorting to legal avenues for a resolution of the issues outlined above is not palatable to either side. "We really don't want to fight about it," an aide to Hunt told *The News and Observer*. "They're Democrats like us and they're friends we need to work with." Friends or not, the tension between the legislative and executive branches has increased, clouding the clear separation of powers called for by the Constitution.

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too, faces a critical challenge. As he seeks to show that a second term can be fruitful (Hunt is the first N.C. governor allowed to succeed himself) and as he looks ahead to a possible 1984 campaign against U.S. Senator Jesse Helms, will Hunt be a strong enough leader to get state government to ease some of the human pain enacted by the federal budget cuts?

Actually, state officials are not completely to blame for the heavy burden they are now forced to bear. To be sure, Gov. Hunt and the legislature once, by formal resolution, called upon the federal government to operate within a balanced budget. So they share some of the responsibility for fostering the political sentiment that led to budget-cutting. But this is Ronald Reagan's revolution. It is his agenda of budget cuts — not the state's agenda — which was finally enacted.

Further, economic and political circumstances are working against a state's being able to pick up a substantial part of the federal cutbacks. The nation has fallen into a recession, and an economic downturn causes a fall-off in state revenue collections. As the Reagan administration has pointed out, states could raise their own taxes, but the President, through his own tax-cut package, has stirred an anti-tax psychology that makes it politically difficult for legislators and county commissioners to increase taxes at the state and county levels.

The legislature, moreover, has already passed a biennial budget effective through September 1983. To alter significantly an already-enacted budget could require not only a strong push from the Governor's office but also an enormous, well-orchestrated lobbying effort by an array of interest groups. But the people most affected by the budget cuts — the poor and working people with modest incomes — have the least organized lobbies.

So far, state officials have made few specific commitments for long-term responses to federal cuts. But if Gov. Hunt genuinely believes what he has been saying about how much state government has improved itself in the past 20 years, he can hardly brush the whole thing off and blame Reagan. Similarly, if Hunt is moved by his own words about the extent of poverty in North Carolina and its consequences for children, he cannot long let budget cuts simply be passed through, across-the-board.

The Governor has said he planned to develop proposals to offset federal actions according to his priorities of economic growth and development programs for people, especially children. For instance, he said, "I can easily see us putting less funds into maintenance type things and putting more into day care." But Hunt doesn't foresee

fundamental budget changes for several years. "We probably won't see the full redirection of some of these funds until the next biennial (1983-85) budget."

No one expects the state to offset everything cut in the federal budget. Private actions by businesses, churches, and civic organizations can help fill some gaps, but non-governmental agencies do not have the capacity to take up all the slack created by more than \$200 million in federal cuts. Government action is essential.

The benefits of the Medicaid program, for example, will have to be measured against the need for a new government building or a tax measure. It may not be necessary to continue a program precisely as the federal government has been having it run, but certain tasks remain to be accomplished by some method. If the federal government is going to reduce Title XX funds available for day care, then what other options should there be for working mothers who want to see that their young children are adequately cared for? If there are to be no federal grants for the CETA program, then what other job-training arrangement could be designed by state officials?

In human terms, the burden of the federal cutbacks falls particularly on the working poor. In governmental terms, the budget-cutting does not strike principally at the Washington bureaucracy, even though the perception of a "bloated federal bureaucracy" has helped the President get his program through Congress. Budget-cutting places the burdens of trying to manage the program reductions on the state bureaucracy. After a generation of serving as a conduit for federal social programs, the state and its bureaucracy now have to soften the blow of federal budget cuts on the low and middle income people of North Carolina. □

FOOTNOTES

¹*An Agenda for American Federalism: Restoring Confidence and Competence*, Advisory Commission on Intergovernmental Relations, June 1981, p. 34.

²*A Crisis in Confidence and Competence*, Advisory Commission on Intergovernmental Relations, July 1980, Table on p. 149.

³*Summary of the Recommended State Budget 1981-83 Biennium*, Submitted by the Governor and the Advisory Budget Commission to the General Assembly, p. 79.

⁴Primary care and education block grants are not available for state takeover until FY 1983. North Carolina has not picked up the community development block grant at this writing.

⁵Welfare eligibility is now limited to families with incomes not exceeding 150 percent of "standard of need." When the standard was raised, an income level which had not fallen under the old standards did fall under the new standard. Therefore, the increase in the standard of need resulted in fewer persons losing their eligibility for AFDC.