
INTERVIEWS

CITIES & STATES: CHALLENGES FOR THE NEXT CENTURY

The social, economic, and technological changes of the coming century present significant challenges with which states and cities will have to contend. Policy Perspectives engaged Donald Borut, Executive Director of the National League of Cities (NLC), and Raymond Scheppach, Executive Director of the National Governor's Association (NGA), in separate conversations to learn how they see these issues playing out for their member states and cities. Their answers expand on the nature of these issues, what strengths these levels of government bring to the task of addressing them, and in what areas collaboration can be enhanced. Both Borut and Scheppach agree that the changing economy is a central consideration for states and localities as they look to the future. Addressing federal preemption, in particular, seems an area ripe for further collaboration between the two levels of government.

Policy Perspectives: *As we face the next century, what are the major issues facing our cities?*

Borut: There are a number of issues—let me just put a context on it. Right now, cities are in better financial shape than they have ever been—the survey that we do, the fiscal survey of cities, has indicated that three-quarters of the cities claim that their fiscal condition is as strong than it has ever been and if we look over the past ten years when we've done that survey, the data affirms it. So financially cities are in better shape than they have ever been. But it seems to me that there are a number of issues that over the long term will have profound effects on cities. One of them is the global economy and, essentially, the changing nature of the economy. We're seeing an incredible interdependence between nations. Our methods of raising money are going to have to change, and we are seeing that presented through the Internet Tax Freedom Act—essentially, the issue of whether or not sales taxes can be collected by state and local government to assist cities. And so the first thing I would note in the long term is what is happening to the economy, and given that there are changes that are occurring, changes in the speed with which information gets transferred, changes in the accessibility of technology, changes in the financial world—these things are going to have a profound impact on cities.

A result of that will be the question of how cities are go-

Policy Perspectives: *What are the major issues facing the states?*

Scheppach: My personal view is that we are really at a watershed period, where we're seeing bigger changes in federal-state relationships than we've seen in the last two hundred years. I think the Constitution had an enormous amount of flexibility built in, so we've had periods where we've had the flow toward the federal government and the flow back. I'm of the view right now that the necessity for uniformity in terms of rules and regulations that is required by the international marketplace is having already and will have business more and more coming to the federal government to preempt state authority. We've already seen that over the last several years in telecommunications, Internet taxes. You're seeing it currently in the health care market with the Patient's Bill of Rights; you've got bills pending on electricity deregulation. You saw a bill on the right to die, where the federal government is trying to override Oregon's law, and I guess a couple of other states that are looking seriously at that. I think the pace of this is just going to continue.

If you shift from federal-state relations, and ask what challenges the states have, the New Economy is really bringing some huge challenges. Number one, the states have to do a much better job of educating and training the labor force. They've got to develop much more adaptable institutions

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ing to finance themselves. I mentioned that the Internet tax is something that we are dealing with, but that, it seems to me, is the short-term problem. The broader issue is how local governments are going to be able to raise revenue in a global economy. In the past, you had a physically-bound, place-bound situation, so you raised money within the place. But given that the economy is now porous, and the business that is done crosses borders so easily, the real question is how do you raise revenue to support places, and that is going to be the second issue.

A third issue that is clearly ever-present, and we deal with it when there is a crisis and avoid it when there isn't, has to do with the issue of race and racism and how we are engaging, or not engaging, across racial lines. It seems to me that one of the things that has happened, even though we are talking about globalization, is that in many ways we are isolating ourselves more and more in terms of living patterns and in terms of interactions. So how we deal with the historical burden of racism I think is something that we are going to have to figure out. It permeates the culture and it has a profound, often unstated, impact on the way we engage or don't engage. And while the presenting and most formidable element is black-white, there really are Asian, Hispanic, and interethnic racial issues that simply are going to have to be addressed.

So those would be what I would call the long-term issues. Now there are short-term issues that we are dealing with as well, and those have to deal mostly with the federal government, and how the federal government deals with local governments. That issue is framed mainly in terms of preemption—taking away the discretion of local government, just as in earlier years there were the federal mandates, when the federal government was requiring cities to perform certain functions, and continues to do this, without providing the funding. In terms of the federal system, preemption right now is really a defining issue. For our members, when they think about the federal government they don't think necessarily about the largesse that they can get, they think about the constraints or the limits that are being placed on them.

Policy Perspectives: *In terms of addressing these long-term problems like racism, what sorts of strengths do you think city governments bring to dealing with these issues, as compared to the other levels of government?*

Borut: There are a couple of things. Local governments are where people interact, where the face-to-face quality

of life issues occur. They are making decisions daily that affect how people live. Furthermore, local elected officials as leaders have an opportunity to be able to model and indeed affirm community values. So it seems to me that they are extremely well positioned, and they do this in many areas, like, for example, in this issue of racism. As everyone suggests, we ought to talk about it, but as you get close to the issue, it's like the same poles of a magnet: you come together and then you push away immediately because it's uncomfortable. It seems to me that those in leadership positions have a pulpit from which to operate. And it's not as though it's just bringing people together to talk. There is a whole host of ways that they can address, and increase the appreciation of, differences around race: in the appointments that are made to boards and commissions, in the way resources are allocated for the provision of services, and in thinking about where certain facilities are placed. I am reminded about one of the meetings we had when we brought together a team from Jackson, Tennessee. One of the real fundamental concerns that the African American community had was that the city, thinking that they were providing economic development, built a jail in a predominantly black neighborhood. So the mayor and council saw this as an economic development initiative and the citizens saw this as: "What are you doing? You are simply reaffirming a whole host of prejudices that are simply inappropriate." And so there are a variety of things that local elected officials can do. We have a significant report of our Advisory Council coming out that addresses this very set of issues.

Policy Perspectives: *How do you see cities' relationship with the states changing as some of these issues get addressed, and as both levels get significantly more responsibility?*

Borut: There are a couple of ways. One, as state and local governments look at the federal government, we have some shared concerns, namely about preemption. But you come down one level, and there are many at the local level that have the same concerns about the state, that the state is preempting. But the fact is that cities are creatures of the state—the Constitution doesn't address cities; their powers come through the state, and as economies change, and as state borders become less significant, cities are going to have to identify what it is that they have in common with the states, or what it is they are dependent on the states for. So it seems to me that over time there is the likelihood that there will be a necessity of trying to find ways of relating to and engaging with the states. Again, we are finding with the Internet tax issue, there are states that are trying to figure out how they can collect, and so they will have to work with cities to figure out how those

taxes will be distributed back to the cities.

As the economy changes, there is going to be more and more pressure for centralization, simply because there will be nation-states that are dealing with each other more and more business, which is going to be porous and able to move anywhere, is going to want standardization so that they don't have one set of rules in one place and one set in another. So there is going to be pressure to centralize. We are going to be resisting that, because we believe in home rule and local discretion. And then the same pressure is going to occur at the state level; so there will be a potential conflict between local governments and the states. But it seems to me that out of necessity we are going to have to figure out how to deal with that. Change in a global economy is not something you can turn on or off or say I don't like it. It's sort of like trying to resist the sun coming up in the morning. It will come up, and I would submit that what is happening to the global economy, as mobilized by changes in technology, information, finance, and the movement of capital, is going to force us to figure out not just how we are dealing with our own economies but also how we interact with the state and federal governments.

Policy Perspectives: *Are there certain areas in which you foresee better collaboration with the states?*

Borut: Yes. I think that the one where we have a lot in common has to do with how we are going to raise revenues to support public services. We are in the same boat with the states, and it seems to me that we have to figure out what relationship and role we expect them to play. In recent years we have assumed that if the federal government would just stay out of our way we'd be able to do things. But at the same time, because of this pressure towards centralization, we may have to think differently about how revenues are raised internationally in some way, and recognize a role that we may not like for the federal government. We will have to figure out together how to deal with the federal government. Rather than reacting to proposals in Congress or the Administration, one of the things that is essential is that local government groups, like NLC and state government groups, like the National Conference of State Legislatures and the governors, try and figure out what from our perspective would be most desirable and most appropriate, so that we are being proactive instead of reactive in the development of alternative or refined methods of revenue collection. Those are issues.

Now there is another issue, and it is all connected, which has to do with the environment. The language of the day is

sustainable development. The fact is that as a globe we are consuming enormous amounts of resources and the dilemma is how can local governments deal with these types of issues that cross boundaries. We have economic pressures to try and provide economic development—the question is, how do you provide a balance? That kind of issue requires that local governments work collaboratively on a regional basis—to find ways to avoid economic competition in the region and to create an appropriate balance between economic development and utilization of resources and pollution.

Policy Perspectives: *What kind of factors need to be in place for that kind of regional collaboration to happen? It certainly seems to be a big focus in much of today's policy discussion.*

Borut: I think that there needs to be a recognition about that interdependence. There is in some areas, but not in others. It is hard to see the consequence of individual behavior. For example, the coolant in my air conditioner leaks out, and someone says, you are going to hurt the ozone layer. OK, I can't get someone to come in and fix it so it will be two weeks. The fact is that for everyone who does that, the ozone layer is damaged that much further. But how do I relate to the ozone layer in Antarctica? We have to find ways of seeing and appreciating the consequences. It is hard on a global level, but it seems that there is a much greater possibility of seeing some of this on a regional basis. One of the things that is happening is that school kids have become part of the discussion. It becomes part of the discussion in school and then kids tell their parents, and there is more pressure created. It seems to me that there is a real issue of the tradeoffs and costs and there has to be a willingness to pay those costs. One of the ways is to be able to demonstrate, and I don't have the answer for how, that if you don't deal with these issues now, the costs will be far greater in the future. The economies of our cities are better than they have ever been—that might be a good time to reallocate resources or think about ways of changing the way we collect revenues because things are so good we can afford to make adjustments. But this won't happen unless there is a pressure. Without a crisis, people don't react. To wit, members of Congress want to do a tax cut at the very time we know we still have problems. I don't have the answer.

Policy Perspectives: *You talked about some of the strengths that city government brings to the table, in terms of being at the level where people are and being able to model behaviors. Are there things you think city government does best, in this atmosphere of being expected to provide more and more? Are there some things they are better*

equipped to do than others?

Borut: One of the things they do, and this is more general, is being able to hear what priorities are, what citizens feel is important, and respond to them. It seems to me that they are able to make choices that are in sync with the concerns of the citizens. They're also able to respond quicker to expectations and changes in those expectations. Now there is a whole range of services that cities can provide—often the kind that citizens don't think about unless they aren't working. You don't think about water unless you don't have it; you don't think about sewers until they back up; and you don't think about tree trimming until you find the branches are falling down because they haven't been cared for or the trees fall over when the land gets saturated. So in many ways what citizens expect is what they have and they get upset when local government isn't responsive. One thing local governments do is to respond to citizen concerns through service provision.

There is more and more pressure to find ways of providing services in collaborative ways, or contracting with other cities to increase the productivity. There was a governor of Maine several years ago who noted to local officials in the state that they had done a great deal to improve productivity, and he was prepared in return to try and restructure the tax system in their favor but not raise the overall amount of taxes. Therefore, if they couldn't raise more money, and they squeezed as much as possible out of services, the only thing he saw as an option was trying to either consolidate services, or, within a metropolitan area, for one unit of government to contract with another so that you don't have multiple overhead, so that, for example, you don't have a command structure or department in every city no matter what the size but rather you contract. So there is going to be more and more interest, pressure, and need to find alternative ways of delivering service but at the same time be able to respect and keep a sense of city community that comes with lots of municipalities in metropolitan areas.

Policy Perspectives: *That seems to fit with the idea of regionalism. In a related area, do you see a trend in how citizens are relating to or participating in local government?*

Borut: Yes. Certainly groups like the National Civic League espouse the fact that there is more and more citizen involvement. I think there is still a real problem that comes as a result of personal economic pressures. People are working harder and longer. Couples who are married and have kids are under pressure to balance their personal lives with

the expectation of work, and so sometimes it is harder to get involved. There was a piece written by Bob Putnam called "Bowling Alone." There are those who disagree with it, but Putnam's argument is that because people are working longer, there is more pressure, their ability to engage collectively or in community activities is reduced, and instead of participating actively in PTAs, for example, people tend to participate by writing checks. So they are not as involved; they don't interact as much; and they don't have the same kind of sense of community. Some argue with that and say that "soccer moms" are replacing that – in terms of participation in sporting activities. I think Putnam's argument has merit, and there is a real difficulty simply with the pressures that folks have. We do see more participation in inner city and lower income neighborhoods, not in more affluent neighborhoods. I think there is more citizen participation and engagement in communities where things are tough and there is a desire to make improvements.

Policy Perspectives: *On a related note, do you see a trend in people's views of government in the coming years? It seems to go in cycles. What trend do you see developing?*

Borut: There is no question that the attitude toward government has been going down, and a measure of that is the low voting turnout. The question is, do you think that your vote, and your involvement in government, is going to make a difference? People can say what they want, but if they don't vote, that is an indication of a lack of confidence in the governmental system. Four or five years ago the National Civic League did a study and found confidence in most institutions lacking, whether it was the business community, the religious community, or government—federal, state, and local. Local government had higher confidence than the other levels, and it looked like local government was improving. However, all the numbers were lousy. I think that when there is a diminution or cynicism about what happens in the federal government, regrettably that colors people's view of local government. At the same time, there is another survey that was done that looks at all sorts of trends and attitudes. One of the things that that survey showed was that the perception of local government was getting better, that instead of the "me focus" of the thirtysomething generation, that there is a change in focus with this generation. I need to see that data before I affirm it, but maybe there is a trend. Everything up to now is going the other way, but I hope that something is on the horizon.

Policy Perspectives: *A last and related question—in light of all*

of these economic and social changes, what do you see as the role of municipal government in the future?

Borut: I think there is going to be a real reshaping of what local government does and how people think about it. Because of the change in the economy and because of the change in how revenues are raised—and I don't know how that's going to come out—there is by necessity going to be a change in what expectations are for local government. Having said that, those of us who live in a community still want to be able, if we have a problem, to talk to someone; we don't want to talk to a voicemail system. We are not going to call Washington, so we want to talk to someone and know that there is a capacity to respond to our needs locally, so that isn't going to change. It is simply how local governments provide the service and where they get their money. So for example, will cities be providing all the services or will they be managing contracts for services to be provided? Will they be collecting taxes at the local level or will they be receiving reimbursements, collected at a higher level and then distributed? I think those are the kinds of changes that can be expected, and the challenges they present are real.

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to meet those needs. The new models are going to be privatization and partnerships with the business community. Rather than funding training through a technical school, you're going to find states providing money directly to the private sector, so that the state funds it but the private sector trains it. Then the private sector hires it and then the state moves on to the next challenge, rather than completely refunding everything through their current institutions.

States don't do a very good job of buying technology: they're eight to ten years behind the private sector. Because you have to protect the integrity of the procurement process, there is such a high premium on preventing fraud, that by the time states buy technology, it's often obsolete. So it's another reason why I think you're going to have to not hire the private sector to come in and build the management system, but contract out the entire service that requires the management system. You're going to have states have to go to the Web across-the-board in terms of information, letting people pay taxes, get driver's licenses, registrations, hunting licenses, fishing licenses, small business places where they can go and find out what kind of licenses they need. So you're going to have enormous challenges to really reinvent state government so that it's adaptable, flexible, much more customer-oriented, and has regulations that are not command and control, but are worked out with the business community. Really across the board in terms of all of the services that states provide, you're going to have to have a significant shift there as well.

Policy Perspectives: *How much of the demand for those changes is a reaction to how well the economy is doing, and people's perception that there is not as big a role for government because there are other more responsive entities?*

Scheppach: I think it is true that the private sector is getting more involved in traditional government activities, as are independent sector foundations and so on. But also a lot of the pressure comes from the fact that the private sector is becoming very efficient, and so people look at what is working in their environment and have an expectation that when they turn to government services, it will be as responsive. People just don't have patience anymore for going and waiting in line at a state office for three hours to get a driver's license. They want to go on the Internet at nine o'clock at night and do it. So I think it's people seeing the efficiency of their day-to-day operations and saying, "I want government to be the same." I'm one who believes, because productivity will be up in the future over the levels

we've seen in the last twenty years, that real wages are going to go up. We've had a period over the last fifteen or twenty years of declining real wages. I think real wages are going to go up. Therefore this antitax sentiment is going to be reduced and shifted from antitax across-the-board much more toward efficiency of specific types of programs. That's the kind of shift we're going to see.

Policy Perspectives: *As we move into the next century, we have a twenty-first century economy based on knowledge services but a nineteenth century tax system based on manufacturing. What problems does that pose for the states?*

Scheppach: Our state tax systems are completely out of line with respect to economic activity. Almost in all areas. The sales tax, which represents almost 40 percent of states' revenues, by and large doesn't tax services—that's where all the growth in the economy is. If you look at what's happened over the last twenty years, we've had increasing rates on a shrinking base as opposed to a reduction in rates applied to a broader base. The sales tax as a base is eroding, and that is a problem. Second, on the corporate income tax side, corporations are getting much more sophisticated in taking their corporate profits to states that have low taxes or offshore. So I really question the long run viability of the corporate tax at the state level. One could make an argument for or against it, but I think if you can't make it fair and if you can't get a legitimate distribution, it's going to erode. So there are significant problems there.

I would suggest that the only tax that probably does in fact track economic activity pretty well is the income tax, but that represents less than 40 percent of state revenues. We have huge problems. The other issue is that some states have taxes on property, but it's normally physical property. The taxes of General Motors, because it's heavily infrastructure, are probably ten to fifteen times those of Microsoft because we don't really tax knowledge industries. I would say that we really have to do a complete revamping of our tax system, which politically is very difficult.

Policy Perspectives: *If people want government to be more responsive, how do you convince them that now is the time for a shift in the structures needed to pay for it?*

Scheppach: It's very hard. Governors and legislators are going to have to come together and provide the leadership and I think the business community is going to have to stop fighting all the taxes and really get together with government and talk about fairer distribution. I'll be honest, I don't think that unless the business community comes for-

ward and is part of that discussion, that we're not going to get it done in the states. The governors get a bit tired of the business community saying, "We don't want to pay any taxes, but we want you to pay more for the education and training of the labor force." A good 40 percent of states' money now is in education. They agree they have to do a better job of that. But if the business community wants that in the long run, it has to be willing to come forward and negotiate a fairer tax system.

Policy Perspectives: *You've discussed the relationship between the states and the federal government. What is the relationship between the states and the localities within them? It can sometimes be as contentious as state-federal relations.*

Scheppach: One of the things that's happened with some of the devolvement that we've seen over the last four or five years as the federal government has devolved some decisionmaking in the programs—the states have received more responsibility, but in their regulatory authority, they've been preempted. But as you've seen that trend from the feds to the states, there's also been a second trend which is from the states to the locals. And I think that makes sense. I think when there is not scale to the economies in decisionmaking, it should be shifted to the locals, so they can run the programs because they are more responsive to their voters. If you look at most polls, there is more faith in state and local government and that's where we need to shift decisionmaking.

Policy Perspectives: *As we move into the future, are the states as they now exist as political entities the most efficient units, or are there other more relevant commonalities?*

Scheppach: Our sense is we are approaching a world without borders—both internationally and within nations. That gets back to preemption and federal standards. But my sense is that if you were going to change your political borders to reflect homogeneity, you'd be doing that all the time, so that doesn't make a lot of sense. My view is that what you need is probably more regional planning, where you have groups of states getting together, so that even though you've got political boundaries, you have states looking at problems in a common way. I think we'll move in that way. My sense is that we'll retain the political borders, but have an increase in the federal standards setting, and perhaps more regionalism with groups of states getting together over certain issues. The trend of partnerships and privatization is going to increase. Particularly in some of the smaller states, I can see joint bidding on health care and certain types of other services so you can use the market power.

