1988

Rural-Urban Linkages: An Assessment of State Government Revenue and Expenditure Patterns

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NEBRASKA POLICY CHOICES 1988, ed.Russell L. Smith
(Omaha, NE: Center for Applied Urban Research, 1988).

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Taxing and spending decisions made by Nebraska's policy makers have different impacts on Nebraska's metropolitan and nonmetropolitan counties, even though these impacts may be unintended. Furthermore, Nebraska's counties are linked through the operation of state government. Through their fiscal actions policy makers can strengthen these links or cause them to deteriorate. Policy makers should begin to incorporate the geographic dimensions of their decisions into their decision making processes, especially as they are faced with issues concerning property tax relief and rural development. A data set describing the geographic distribution of Nebraska state government taxes and expenditures is offered here for review.

Introduction

In carrying out its functions, Nebraska's state government shifts income and resources among regions in the state. It collects taxes from individuals and businesses, receives intergovernmental transfers from both the federal government and local governments, receives fees and charges from users of some services, and takes in other miscellaneous revenues. These revenues are then paid out as wages and salaries to state employees, operating expenditures, capital outlays, and transfers to individuals, businesses, and local governments.

It is important for Nebraska policy makers to recognize how spending and taxing decisions affect substate areas. It is unlikely that the impacts of taxing and spending will be equal around the state, although the differences may be unintentional.

This chapter provides information on how state government revenue and spending patterns vary across Nebraska. To highlight these patterns, four types of counties are defined according to the size of the largest city they contain. Analysis of the data indicates that there are indeed variations in the extent to which revenues are drawn from or expenditures accrue to certain

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The development of the data set used in this chapter was funded by the Urban Conditions Research Program, Center for Applied Urban Research, College of Public Affairs and Community Service, University of Nebraska at Omaha. Plans are to update and expand the data set annually as information becomes available. For further information contact the author at CAUR.

The author wishes to thank Tim Himberger and Dave Van Veldhuizen.

types of counties. Knowledge of how such changes will affect urban and rural Nebraska can help policy makers who are considering changes in Nebraska's tax or expenditure structure.

Past Studies

Nebraska's state government has recognized the need to study the geographic incidence of taxation; that is, how many tax dollars are paid by residents of the various regions in Nebraska. In 1979, the Nebraska Unicameral's Revenue Committee recommended that this aspect of taxation should be included in a broad tax incidence study to be "undertaken some time in the future" (Nebraska Legislative Council 1979). The recommended study, however, would not include the state's expenditure system.

In 1981, the Revenue Committee prepared a study that analyzed the tax and revenue structure data of Nebraska. The purpose was "to determine the most effective means of providing property tax relief by shifting the property tax burden to other forms of taxation" (Nebraska Legislative Council 1981). The study measured the county distribution of income, sales and property taxes and looked at the distribution of state funds to local governments. The study did not analyze the relationship between taxes and expenditures among the counties. It also ignored other types of state government expenditures, such as wages and salaries paid to state employees and public assistance payments that have impacts on local areas. Another weakness of the study was that sales taxes were allocated to the county where purchases were made, not where the income for those purchases originated.

Perhaps it is easier to recognize taxes paid than government spending. We are reminded of taxes each time we make purchases or look at our pay stubs.

The *Nebraska Comprehensive Tax Study* (Wasylenko and Yinger 1988) provides a detailed analysis of Nebraska's fiscal system. It contains sections on tax incidence for households and businesses, but it does not attempt to measure the geographic incidence of taxes. And despite its broad coverage of revenue, the study generally neglects expenditures.

Perhaps it is easier to recognize taxes paid than government spending. We are reminded of taxes each time we make purchases or look at our pay stubs. State government expenditures may not be as recognizable because they are usually less personal. However, expenditures also have differential impacts throughout the state.

State-operated facilities can be considered basic industries for some communities. State offices and installations provide jobs and income to local residents, attracting wages and salaries which bring back tax dollars that had been taxed away by a higher level of government. In Lincoln, the presence of the state capitol and the University of Nebraska-Lincoln makes state government obvious. But the state has a presence in every county in Nebraska; every county has at least one state employee. And virtually every county has residents who receive transfer payments and other types of public assistance.

The state also distributes funds to local governments. Some go to projects such as streets and highways, while some are in the form of direct aid to local subdivisions, such as school districts. For some communities, the amount of state funds received exceeds local property tax collections. But in general, state funds distributed to local governments average more than one-third the amount of property taxes collected (Nebraska Department of Revenue 1986).

Understanding the distribution of both taxes and expenditures is necessary in order to measure the impact of the state's fiscal system on the various substate areas. This understanding can then be used to help evaluate some of the state's policy options. State government's taxing and spending patterns can either support or undermine other state goals. For example, increasing sales taxes in order to reduce property taxes used for the support of local education may have varying impacts around the state. Likewise, increasing the income tax in order to pay for expanded income maintenance payments will have different impacts in substate areas. The effects would be different in terms of which areas pay the increased taxes as well as which areas benefit from the increased spending.

As another example, the research in this chapter shows that rural counties receive more state aid than do counties with large cities, relative to their population and income. If the state chose an economic development strategy which strengthened the economic capacities in some of the state's larger communities, it would probably require shifts in current taxing and/or spending patterns to ensure policies consistent with such a growth center strategy.

Urban-Rural Connections

Another current area of attention is the belief that Nebraska is disconnecting; that its urban and rural areas are becoming less interdependent. In its reports on Nebraska's future, SRI International has suggested that "Nebraska is increasingly becoming uncoupled — urban areas from rural areas— at a time when it can ill afford to fragment its resources" (1988; 38). According to the report, *New Seeds for Nebraska*, "Omaha and Lincoln have become less dependent on the rest of the state, and many rural areas in the west and north-central parts of the state have little interaction with the state's urban centers." It suggests that Nebraska's leadership must move to improve urban-rural relationships, or risk not achieving consensus on the state's future.

As discussed earlier, however, Nebraska's substate areas are connected through the state's tax and expenditure system. A primary purpose of this chapter, therefore, is to develop a method to measure the distribution of taxes paid and expenditures received between the state's urban and rural areas.

A major product of this study is a methodology which produces a set of data to examine the current distribution of state government taxes and expenditures.

Obviously, pecuniary measures provide an incomplete picture of how the state is linked by its government, but it is beyond the scope of this chapter to define all these links. In addition, this research is not intended to be a comprehensive analysis of the state's fiscal system, nor is it intended to enumerate all the costs and benefits associated with the operation of Nebraska's state government. Instead it focuses on several of the major tax and expenditure categories. Taxes included for discussion are sales and use tax, personal income tax, corporate income tax, sales tax on motor vehicles, and taxes on tobacco and alcohol. The expenditure categories include wages and salaries for state government employees, transfer payments and other assistance to individuals, and transfers to local governments.

A major product of this study is a methodology which produces a set of data to examine the current distribution of state government taxes and expenditures. This data set also can be used to evaluate future policy alternatives. Although the data in this chapter are for 1985, the methodology easily can be applied to other years.

Definition of County Groups

To better understand the distribution of taxes and expenditures in Nebraska, the state first must be divided into collections of counties. Counties are used as building blocks because they are a level of geography for which information generally is available.

Before dividing the state into its rural and urban components, urban and rural counties must be defined. The U.S. Bureau of the Census defines the urban population as all persons living in places of 2,500 or more inhabitants or in the closely settled areas, incorporated or unincorporated, which surround a large city (sometimes referred to as urban fringe). The remainder of the population is classified as rural. But because counties can have both urban and rural components, this definition does not allow an accurate classification of counties.

A measure that does allow county classification, and one used in this chapter, is the Metropolitan Statistical Area (MSA). Briefly, an MSA is a county or a group of contiguous counties which contains at least one city of 50,000 or more residents. To be included in an MSA, contiguous counties must be socially and economically integrated with the central city. Nebraska contains three MSAs, two of which are shared with Iowa. The three MSAs and the Nebraska counties contained in each are: Omaha (Douglas, Sarpy and Washington counties); Lincoln (Lancaster County); and Sioux City (Dakota County). The remaining counties in the state are considered to be nonmetropolitan.

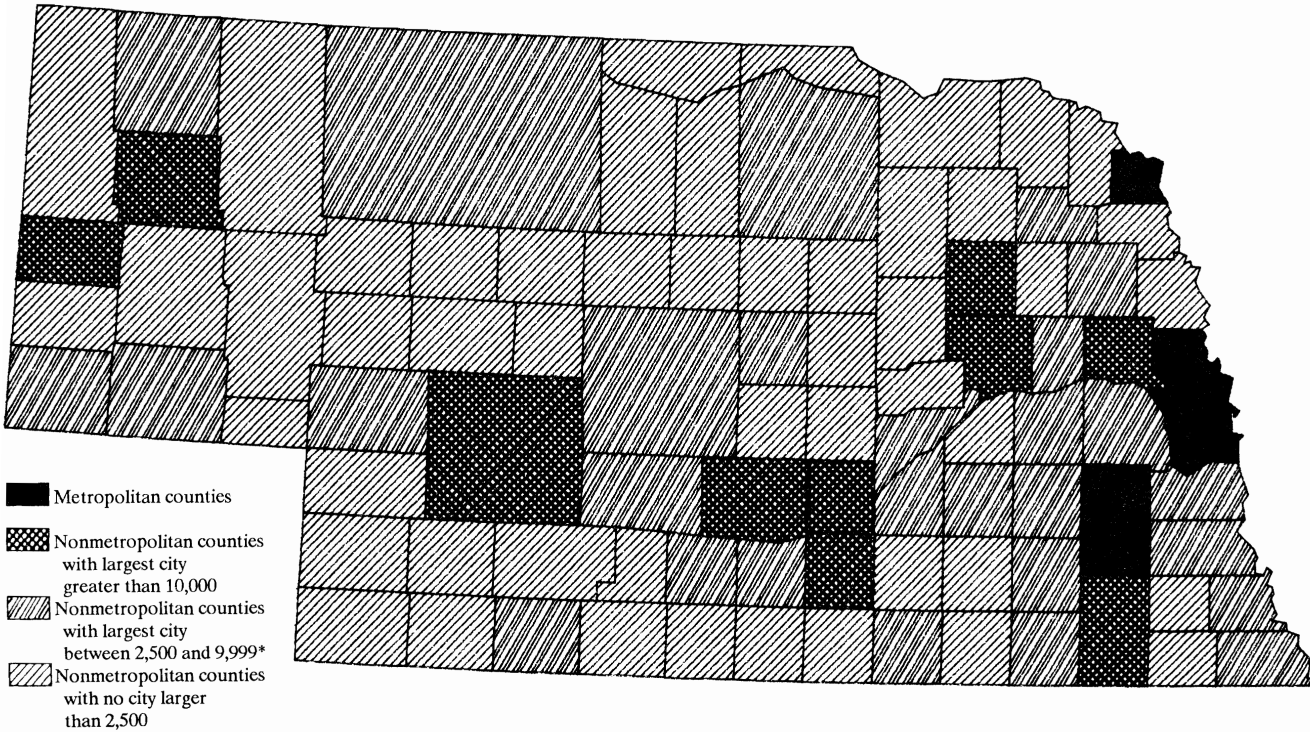
The metropolitan-nonmetropolitan classification scheme also has problems, because it ignores the vast differences among nonmetropolitan counties. To take these into account, the state's nonmetropolitan counties can be further divided by size of largest city. The divisions for the state, as shown in figure 1, then become:

1. Metropolitan counties;
2. Nonmetropolitan counties where the largest city has 10,000 or more persons (referred to as large-city counties);
3. Nonmetropolitan counties where the largest city has between 2,500 and 9,999 persons (referred to as small-city counties); and
4. Nonmetropolitan counties where the largest city has fewer than 2,500 persons (referred to as rural counties — they also meet the Census Bureau's definition of rural).

Overview of Nebraska's Fiscal Structure

Any discussion of the distribution of Nebraska state government taxes and expenditures should begin with a review of the major components of the state's fiscal structure. Table 1 presents expenditure and revenue data drawn from the U.S. Census Bureau's *State Government Finances, 1986.* As shown, Nebraska receives revenues from a variety of sources, with approximately one-half (forty-eight percent) coming from taxes. The remaining major sources include intergovernmental revenue (primarily from the federal government), 25.3 percent; current charges for provided services, 11.1 percent; miscellaneous revenue including interest earnings, 8.4 percent; and insurance trust revenue including employee retirement, 7.3 percent.

Figure 1 - Nebraska's Counties Grouped by Size of Largest City in 1985



***Includes Butler and Nuckolls counties, although David City and Superior dipped below 2,500 in 1985.**

For reference map with county names, see page xiii.

Table 1 - State Government Revenue and Expenditure in Nebraska and the United States, FY 1985-86

	-Nebraska-			-United States Total-	
	Amount (Thousand Dollars)	Percent of Total Revenue	Percent of Total Taxes	Percent of Total Revenue	Percent of Total Taxes
Total Revenue	2,334,204	100.0		100.0	
General revenue	2,164,881	92.7		81.8	
Intergovernmental revenue	590,242	25.3		20.5	
From federal government	561,408	24.1		19.3	
General revenue from own sources	1,574,639	67.5		61.3	
Taxes	1,119,382	48.0	100.0	47.4	100.0
General sales	349,884	15.0	31.3	15.5	32.8
Motor fuel	146,546	6.3	13.1	2.9	6.2
Motor vehicle license	49,381	2.1	4.4	1.6	3.4
Income	406,387	17.4	36.3	17.8	37.6
Individual	351,828	15.1	31.4	14.0	29.6
Corporation	54,559	2.3	4.9	3.8	8.1
Other taxes	167,184	7.2	14.9	9.5	20.0
Current charges	258,873	11.1		6.2	
Education	139,610	6.0		3.6	
Hospitals	81,468	3.5		1.3	
Miscellaneous revenue including interest earnings	196,384	8.4		7.7	
Insurance trust revenue, including employee retirement	169,323	7.3		17.0	
Other revenue	0	0.0		1.2	

	-Nebraska-			-United States Total-	
	Amount (Thousand Dollars)	Percent of Total Expenditure	Percent of Direct Expenditure	Percent of Total Expenditure	Percent of Direct Expenditure
Total expenditure	2,204,924	100.0		100.0	
Intergovernmental	537,476	24.4		31.1	
To local governments	536,133	24.3		30.6	
Current operation	1,149,610	52.1		43.9	
Capital outlay	248,500	11.3		8.1	
Other expenditures	269,338	12.2		16.9	
Exhibit: Expenditure for salaries and wages	601,469	27.3		17.9	
Total direct expenditure by function	1,667,448	75.6	100.0	68.9	100.0
General expenditure	1,584,446	71.9	95.0	57.6	83.7
Current expenditure	1,335,946	60.6	80.1	49.9	72.5
Capital outlay	248,500	11.3	14.9	7.7	11.2
Education services	412,580	18.7	24.7	13.8	20.0
Social services and income maintenance	524,997	23.8	31.5	19.9	28.9
Transportation	269,836	12.2	16.2	7.4	10.7
Public safety	83,324	3.8	5.0	3.7	5.4
Environment and housing	86,141	3.9	5.2	2.4	3.5
Governmental Administration	52,772	2.4	3.2	2.9	4.2
Other general expenditures	154,796	7.0	9.3	7.5	10.9
Insurance trust expenditure, including employee retirement	83,002	3.8	5.0	9.4	13.6
Other direct expenditure	0	0.0	0.0	1.9	2.7

Source: U.S. Bureau of the Census, *State Government Finances, 1986.*

Table 1 also presents the average revenue structure for state governments in the United States. It shows that Nebraska's state government receives relatively more revenues from intergovernmental sources, current charges, and miscellaneous revenue; and relatively less from insurance trust and other revenue sources, compared to other states. The percentage of the state's revenues coming from taxes is approximately the same as the national average.

The state's two major taxes— general sales and income— have approximately the same relative importance for Nebraska as for the nation. Revenues from motor fuel taxes and motor vehicle license fees are higher in Nebraska, but other taxes generate proportionately less revenues here than the average of all states.

Table 1 also reviews the expenditure side of the Nebraska's fiscal system.[1] Slightly more than half of the state's expenditures go to support current operation, of which the largest amount goes to wages and salaries (27.3 percent of all expenditures). Intergovernmental transfers (mostly to local governments) comprise 24.4 percent of expenditures; capital outlay accounts for 11.3 percent; and other expenditures account for 12.2 percent.

Compared to the national average, the percentage of Nebraska's expenditures for current operation, especially wages and salaries, are higher. Nebraska's proportion of transfers to local governments is lower.

Looking at Nebraska's direct expenditures by function shows that social services account for 31.5 percent. This is followed by education services (24.7 percent) and transportation (16.2 percent).

Distribution of Taxes and Expenditures

A problem arises when trying to analyze the flow of revenues and expenditures among the various areas of the state, because much of the data lack county identification. Even for those data that are available on a county basis, the county of collection or activity may not be the county of origin or destination. For example, sales and use taxes are reported at the county where the sales took place, but some of the purchasers live in other counties. Thus, when a resident of St. Paul makes a purchase in Grand Island, the sales tax paid is reported by Hall County even though it was paid by a Howard County resident.

Clearly, some taxes reported by urban areas are actually paid by residents of rural areas. To the extent that a county attracts sales, its sales taxes reflect taxes paid both by its residents and by residents of other counties. Sales tax figures for the counties which lose sales understate taxes paid by their residents. Unless taxes can be allocated to the county of residence of the person or household that pays the taxes, there will be an inaccurate picture of the urban-rural distribution of taxes in Nebraska.

Other taxes, collected at the state level, are not reported by county. Taxes in this category include corporate income tax and many of the miscellaneous taxes, such as those on tobacco and liquor. In order to allocate these taxes to regions, indirect procedures must be used. These are outlined later in the chapter.

An Overview of the Data Set

Table 2 contains an estimate of Nebraska taxes collected, by county of origin; and expenditures, by county of destination. Each tax and expenditure category is analyzed separately in this section. Table 2 also expresses the substate-area tax and expenditure values as percentages of the respective state totals. For comparative purposes, total personal income and total population for each region are included with taxes and expenditures. When the data set was compiled, 1985 was the latest year for which some of the data were available. In order to maintain consistency, all data analyzed in this chapter are for calendar or fiscal year 1985.

The data in table 2 can be analyzed several ways. First, the distribution of a tax or expenditure item can be measured by reading across a row. For example, in the bottom half of the table, 51.6 percent of the sales tax on motor vehicles is collected in metropolitan areas; 48.4 percent is collected from nonmetropolitan counties; 19.1 percent comes from counties with large cities; counties with small cities provide 18.0 percent; and rural counties account for 11.2 percent.

Second, the shares of taxes or expenditures within a set of counties can be compared by reading down a column. This type of comparison shows that counties with small cities account for a low of 13.0 percent of the corporate income tax and a high of 21.6 percent of the state's tobacco tax.

Viewed in isolation, these percentages present an incomplete picture. Taxes paid and expenditures received by counties are also related to the areas' incomes and population sizes. A final method of comparison, therefore, views the area's share of taxes or expenditures in relation to its share of personal income or population. For example, rural counties account for 12.5 percent of Nebraska's personal income and 13.4 percent of its population but receive 26.5 percent of the state aid to counties and only 4.3 percent of the wages and salaries paid to state employees.

To facilitate comparisons of taxes or expenditures to income and population, table 3 shows each area's taxes generated and expenditures received as a ratio to its shares of income and population. For example, from table 2 we see that Nebraska's rural counties have individual income tax liabilities totaling 8.2 percent of the total for the state. Table 2 also shows that residents in the rural counties earn 12.5 percent of the state's personal income, and they account for 13.4 percent of the state's population. Compared to its share of

Table 2 - Selected Taxes and Expenditures for Groups of Counties in Nebraska, 1985

	Metropolitan Counties	-Nonmetropolitan Counties- Total	Large-City Counties	Small-City Counties	Rural Counties
		-Thousand Dollars-			
SELECTED TAXES					
Estimated sales tax	101,595	112,195	44,512	40,641	27,042
Sales tax on motor vehicles	19,076	17,898	7,080	6,666	4,152
Individual income tax liability	169,364	126,033	56,461	45,206	24,367
Estimated corporate income tax	41,585	26,000	13,180	8,805	4,014
Estimated tobacco sales tax	8,440	11,934	4,665	4,392	2,877
Estimated liquor sales tax	6,811	7,061	2,827	2,583	1,651
Total taxes	346,872	301,122	128,725	108,293	64,104
SELECTED EXPENDITURES					
Total state aid*	154,850	200,718	70,969	73,922	55,827
State aid to counties	16,600	47,596	11,701	18,885	17,010
State aid to cities and villages	34,723	38,820	15,957	14,182	8,681
State aid to townships	4	112	21	51	40
State aid to fire districts	22	52	12	24	15
State aid to misc. districts	245	132	42	58	32
State aid to school districts	96,907	102,341	39,918	36,662	25,761
Additional state aid	6,350	11,664	3,318	4,060	4,287
State government wages paid	367,849	142,150	81,566	38,558	22,026
Public assistance and related programs*	144,585	138,443	57,698	46,178	34,567
Aid to dependent children	36,980	25,128	12,589	7,215	5,324
State supplement	2,435	2,743	1,260	931	551
Food stamps	24,436	22,819	10,603	7,139	5,076
Medicaid	75,618	83,101	31,299	29,296	22,506
Adult & family contracted services	5,114	4,652	1,946	1,597	1,110
Total expenditures	667,283	481,310	210,233	158,658	112,419
Total personal income	10,327,000	10,579,000	3,996,000	3,970,000	2,613,000
		-Persons-			
Population	746,600	858,700	325,200	318,100	215,400
		-Percent of State Total-			
SELECTED TAXES					
Estimated sales tax	47.5	52.5	20.8	19.0	12.6
Sales tax on motor vehicles	51.6	48.4	19.1	18.0	11.2
Individual income tax liability	57.3	42.7	19.1	15.3	8.2
Estimated corporate income tax	61.5	38.5	19.5	13.0	5.9
Estimated tobacco sales tax	41.4	58.6	22.9	21.6	14.1
Estimated liquor sales tax	49.1	50.9	20.4	18.6	11.9
Total taxes	53.5	46.5	19.9	16.7	9.9
SELECTED EXPENDITURES					
Total state aid*	43.6	56.4	20.0	20.8	15.7
State aid to counties	25.9	74.1	18.2	29.4	26.5
State aid to cities and villages	47.2	52.8	21.7	19.3	11.8
State aid to townships	3.5	96.5	18.2	43.9	34.3
State aid to fire districts	29.5	70.5	16.4	33.3	20.9
State aid to misc. districts	64.9	35.1	11.2	15.3	8.5
State aid to school districts	48.6	51.4	20.0	18.4	12.9
Additional state aid	35.2	64.8	18.4	22.5	23.8
State government wages paid	72.1	27.9	16.0	7.6	4.3
Public assistance and related programs*	51.1	48.9	20.3	16.3	12.2
Aid to dependent children	59.5	40.5	20.3	11.6	8.6
State supplement	47.0	53.0	24.3	18.0	10.6
Food stamps	51.7	48.3	22.4	15.1	10.7
Medicaid	47.6	52.4	19.7	18.5	14.2
Adult & family contracted services	52.4	47.6	19.9	16.3	11.4
Total expenditures	58.1	41.9	18.3	13.8	9.8
Total personal income	49.4	50.6	19.1	19.0	12.5
Population	46.5	53.5	20.3	19.8	13.4

*State fiscal year 1985-86.

Sources: Nebraska Department of Labor, *1985 Nebraska Employment and Wages*; Nebraska Department of Revenue, *Annual Report 1985*, *Annual Report 1986*, and *State Funds Distributed to Local Government Subdivisions*; Nebraska Department of Social Services, *Annual Report 1986*; U.S. Bureau of Economic Analysis, *Local Area Personal Income*; U.S. Bureau of Labor Statistics, "Consumer Expenditure Survey."

Table 3 - Ratios of Income and Population to Selected Taxes and Expenditures for Groups of Counties in Nebraska, 1985

	Metropolitan Counties	-Nonmetropolitan Counties- Total	Large-City Counties	Small-City Counties	Rural Counties
			-Ratio to Income-		
SELECTED TAXES					
Estimated sales tax	0.96	1.04	1.09	1.00	1.01
Sales tax on motor vehicles	1.04	0.96	1.00	0.95	0.90
Individual income tax liability	1.16	0.84	1.00	0.81	0.66
Estimated corporate income tax	1.25	0.76	1.02	0.69	0.48
Estimated tobacco sales tax	0.84	1.16	1.20	1.14	1.13
Estimated liquor sales tax	0.99	1.01	1.07	0.98	0.95
Total taxes	1.08	0.92	1.04	0.88	0.79
SELECTED EXPENDITURES					
Total state aid*	0.88	1.12	1.04	1.09	1.26
State aid to counties	0.52	1.47	0.95	1.55	2.12
State aid to cities and villages	0.96	1.04	1.14	1.02	0.94
State aid to townships	0.07	1.91	0.95	2.31	2.75
State aid to fire districts	0.60	1.39	0.86	1.75	1.67
State aid to misc. districts	1.31	0.69	0.59	0.81	0.68
State aid to school districts	0.98	1.02	1.05	0.97	1.03
Additional state aid	0.71	1.28	0.96	1.19	1.90
State government wages paid	1.46	0.55	0.84	0.40	0.35
Public assistance and related programs*	1.03	0.97	1.06	0.86	0.98
Aid to dependent children	1.21	0.80	1.06	0.61	0.69
State supplement	0.95	1.05	1.27	0.95	0.85
Food stamps	1.05	0.95	1.17	0.80	0.86
Medicaid	0.96	1.03	1.03	0.97	1.13
Adult & family contracted services	1.06	0.94	1.04	0.86	0.91
Total expenditures	1.18	0.83	0.96	0.73	0.78
			-Ratio to Population-		
SELECTED TAXES					
Estimated sales tax	1.02	0.98	1.03	0.96	0.94
Sales tax on motor vehicles	1.11	0.90	0.95	0.91	0.84
Individual income tax liability	1.23	0.80	0.94	0.77	0.61
Estimated corporate income tax	1.32	0.72	0.96	0.66	0.44
Estimated tobacco sales tax	0.89	1.09	1.13	1.09	1.05
Estimated liquor sales tax	1.06	0.95	1.01	0.94	0.89
Total taxes	1.15	0.87	0.98	0.84	0.74
SELECTED EXPENDITURES					
Total state aid*	0.94	1.06	0.99	1.05	1.17
State aid to counties	0.56	1.39	0.90	1.48	1.97
State aid to cities and villages	1.02	0.99	1.07	0.97	0.88
State aid to townships	0.08	1.80	0.90	2.22	2.56
State aid to fire districts	0.63	1.32	0.81	1.68	1.55
State aid to misc. districts	1.40	0.66	0.55	0.77	0.64
State aid to school districts	1.05	0.96	0.99	0.93	0.96
Additional state aid	0.76	1.21	0.91	1.14	1.77
State government wages paid	1.55	0.52	0.79	0.38	0.32
Public assistance and related programs*	1.10	0.91	1.00	0.82	0.91
Aid to dependent children	1.28	0.76	1.00	0.59	0.64
State supplement	1.01	0.99	1.20	0.91	0.79
Food stamps	1.11	0.90	1.11	0.76	0.80
Medicaid	1.02	0.98	0.97	0.93	1.06
Adult & family contracted services	1.13	0.89	0.98	0.83	0.85
Total expenditures	1.25	0.78	0.90	0.70	0.73

*State fiscal year 1985-86.

Sources: *See* Table 2.

personal income, therefore, the rural counties' income tax liability is a ratio of 0.66 (8.2÷12.5). Compared to population the ratio is 0.61 (8.2÷ 12.5). To clarify the measure used:

1. If an area's share of taxes or expenditures is equal to its income or population share, then the ratio is 1.0.
2. If an area's share of taxes or expenditures is greater than its income or population share, then the ratio exceeds 1.0. Taxes are drawn from the area or expenditures are attracted to the area.
3. If an area's share of taxes or expenditures is less than its income or population share, then the ratio is less than 1.0. Residents of the area pay less taxes or receive less expenditures than its income or population suggests.

This method of comparing relative shares of taxes and expenditures to personal income or population allows for the analysis of individual categories and does not require a complete regional allocation of all taxes and expenditures. Therefore, an individual tax or expenditure category can be excluded without harming the analysis.

Selected Taxes

Taxes, which represent fifty percent of Nebraska's state revenues, are the only revenue source included in this analysis. Additional Nebraska state government revenues come from intergovernmental transfers, current charges, insurance trust, and miscellaneous sources. Taxes included here are individual income taxes, corporate income taxes, sales and use taxes, sales tax on motor vehicles, and liquor and tobacco taxes. These represent the majority of the taxes collected by the state government

Estimated Sales Tax. Sales taxes cannot be measured directly by county of origin, because the data are available only for county of purchase. To determine estimates of taxes paid by a county group, an allocation method based on income groups and taxable expenditures for those income groups was used. The income groups were the five groupings reported by the Nebraska Department of Revenue in its annual reports: less than \$6,000; \$6,000 to \$12,000; \$12,000 to \$18,000; \$18,000 to \$30,000; and \$30,000 and over. Taxable expenditures by income group were compiled from 1985 Consumer Expenditure Survey (CES) information, which is released by the U. S. Bureau of Labor Statistics and contains detailed expenditure and income data for a sample of households in the United States.

Household data from the CES are classified by size of community. Three groups of communities identified by the CES roughly conform to metropolitan counties, large- and small-city counties, and rural counties. Using the CES, taxable household expenditures were identified, summed, and averaged for each income group in each community group.

Nebraska's taxable spending for each set of counties in Nebraska was estimated by multiplying the average taxable household expenditures (calculated from the CES) by the actual number of households reported by the Nebraska Department of Revenue. There was one calculation for each income class within each county group.

To determine total taxable expenditures for a county group, the expenditures were summed over all income classes. County group totals were expressed as percentages of the state total, and Nebraska's 1985 sales and use tax was multiplied by the percentages. The result is an estimate of sales taxes paid by the residents of each county group in the state.

Approximately 75 percent of Nebraska's sales taxes are paid by households; the remainder are paid by businesses (Due and Fairchild 1988). Therefore, the sales and use tax numbers reported in table 2 are 75 percent of the actual sales and use taxes reported in the Nebraska Department of Revenue's *Annual Report 1986.*

From table 2 it can be seen that the shares of sales taxes for metropolitan and nonmetropolitan areas are roughly the same as their shares of income and population. This fact is borne out by table 3, which shows that the ratios are all close to 1.0, with the exception of large-city counties. When sales taxes are compared to personal income, large-city counties have the highest ratio (1.09), followed by rural counties (1.01), small-city counties (1.00), and metro counties (0.96). Comparing sales taxes to population, large-city counties again lead the way with a ratio of 1.03, and they are followed by metro counties, small-city counties, and rural counties.

Sales Tax on Motor Vehicles. Because motor vehicle sales taxes are collected at the county of registration, they can be measured directly. These data are also available from the *Annual Report 1985.* Table 3 illustrates that the motor vehicle tax ratio is related directly to the size of the largest city in an area: as the largest city gets smaller, the ratio diminishes. The ratio of motor vehicle sales taxes to income for metro Nebraska is 1.04; relative to population it is 1.11. For counties with large cities, the ratios are 1.00 and 0.95; for counties with small cities they are 0.95 and 0.91; and for rural counties they are 0.90 and 0.84.

Individual Income Tax. Individual income tax is reported by county of residence of the person or household filing the tax, although the incomes may have been earned elsewhere. These data, therefore, were used as reported in the Department of Revenue's *Annual Report 1986.*

Table 3 shows that residents of metropolitan areas of the state pay a higher percentage of income tax than their shares of personal income and population would suggest. The ratio to income is 1.16, and the ratio to population is 1.23. The ratios decline as the size of the largest city in each county group gets smaller. The ratios for counties with large cities are 1.00 and 0.94; for counties with small cities the ratios drop to 0.81 and 0.77; and for rural counties the ratios are 0.66 and 0.61.

Corporate Income Tax. Corporate income tax cannot be measured directly by the area where the income was earned. Instead it must be estimated. Nonfarm private earnings, as reported in the U.S. Bureau of Economic Analysis' *Local Area Personal Income* (1988), was used to estimate corporate income tax. To illustrate, if an area accounts for ten percent of the state's nonfarm private earnings, it is assumed that the area accounts for ten percent of the state's corporate income tax as reported in the *Annual Report 1986* of the Department of Revenue. Not all corporations that pay corporate income taxes in Nebraska have employees in Nebraska, however, so this allocation method may overstate the actual amount of corporate income taxes originating in Nebraska.

Figures based on this allocation scheme show that a disproportionate share of corporate income tax is drawn from metropolitan counties. The ratio to income is 1.25, and the ratio to population is 1.32. Counties with large cities pay taxes roughly equal to their shares of income and population, with ratios of 1.02 and 0.96. The ratios for counties with small cities are 0.69 and 0.66. For rural counties the ratios fall to 0.48 and 0.44. This is a reflection of the employment base in the state's regions, as businesses in small-city counties and rural counties are more likely to be smaller and operated as proprietorships rather than corporations.

Other Sales-Related Taxes. Two other sales-related taxes are included in the analysis: tobacco and liquor taxes. These taxes were allocated to the sets of counties using a method similar to that for the sales tax.

From table 3, we can see that the ratios for the tobacco tax are higher for nonmetropolitan counties than they are for metropolitan counties. Within the nonmetropolitan grouping, counties with large cities recorded the highest ratios and were followed by small-city counties and rural counties. All three of the nonmetro regions recorded ratios larger than 1.0.

Liquor taxes are also reviewed in table 3. When compared to income, the liquor tax ratios show little variation among areas. Compared to population, however, we can see that the range of ratios begins to widen, from a high of 1.06 for metro counties to a low of 0.89 for rural counties.

Expenditures

To analyze the pattern of Nebraska state government expenditures, three classes of state spending were used: state aid to local governments, wages and salaries paid to state government employees, and public assistance and related payments. Together these categories account for the majority of state expenditures.

State Aid to Local Governments. State aid to local governments is reported annually by the Nebraska Department of Revenue in a report series titled *State Funds Distributed to Local Government Subdivisions*. Because some funds are not distributed to individual counties, they could not be aggregated into the county groups used in this chapter. The data in tables 2 and 3, therefore, do not include funds allocated to governmental subdivisions that are comprised of multi-county areas (for example, natural resource districts, educational service units, and Nebraska technical colleges).

Table 3 shows that state aid goes disproportionately to nonmetropolitan areas, while metropolitan areas receive less than their income and population shares. Within the nonmetropolitan counties, the ratios of aid to personal income and population increase as the size of the largest city in the county decreases. Large-city counties have ratios close to 1.0, while rural counties have the highest ratios (1.26 and 1.17).

State aid is received by various types of local governments. Table 3 indicates that the ratios differ by governmental subdivision and by county grouping. State aid to counties, townships, and fire districts and additional state aid goes disproportionately to nonmetropolitan counties; but state aid to miscellaneous districts goes more heavily to metropolitan areas. State aid to cities and villages and to school districts all have ratios close to 1.0 for each group of counties.

Large-city counties receive a percentage of state aid that is closest to their shares of personal income and population. Compared to income the ratio is 1.04, and compared to population it is 0.99. The highest relative shares of aid in large-city counties go to cities and villages and to school districts, where these counties have the highest ratios of all nonmetropolitan counties. The lowest shares of state aid in large-city counties accrue to fire districts and miscellaneous districts.

Small-city counties generally fit in the middle of the nonmetropolitan counties. Their ratio of state aid to income is 1.09 and to population is 1.05. Almost all categories of state aid for this group of counties have ratios close to or exceeding 1.0. The highest relative share of aid is for townships, and this is followed by fire districts, counties, and additional state aid. The lowest share of aid for small-city counties goes to miscellaneous districts.

Rural counties receive relatively more state aid than any other group of counties, when compared to income and population. The ratio to income is 1.26 and to population is 1.17. In rural counties, state aid to counties, townships, fire districts, and additional state aid all have ratios that greatly exceed 1.0 and are usually higher than any other county grouping. On the other hand, state aid for cities in rural areas falls below the other area ratios.

Wages and Salaries. The second category of expenditures consists of wages and salaries paid to state government workers. These data come from the Nebraska Department of Labor's *1985 Nebraska Employment and Wages*. As might be expected, given the location of the state capitol in Lincoln and the University of Nebraska in Lincoln and Omaha, metropolitan areas receive the highest proportion of wages and salaries paid by the state. The ratios for metropolitan counties are 1.46 compared to income and 1.55 compared to population. For nonmetropolitan areas the respective ratios are 0.55 and 0.52.

Within the nonmetropolitan counties, the ratios decline as the size of the largest city declines. Counties with large cities have a greater presence of state government, as some departments maintain offices and other facilities in these counties. The ratios for these counties are 0.84 compared to personal income and 0.79 compared to population.

Small-city and rural counties receive a much smaller relative share of the wages and salaries paid out by the state government, but they do receive some benefit from the operation of state government. The ratios for these two regions fall between 0.40 and 0.32.

Public Assistance and Related Programs. Another way state money is disseminated throughout Nebraska is through public assistance and related programs. Although many of these programs are funded, in part or in whole, by the federal government, they are administered by state agencies and reflected in the state government budget. Public assistance expenditures are reported annually by the Nebraska Department of Social Services.

Table 3 shows that public assistance expenditures are slightly more likely to accrue to the state's metropolitan counties. The ratio to income is 1.03 and to population is 1.10. For nonmetro counties, large-city counties record the highest ratios, with a ratio of 1.06 compared to income and 1.00 compared to population. Small-city counties receive the lowest relative share of public assistance, with respective ratios of 0.86 and 0.82.

Expenditures for the Aid to Dependent Children (ADC) program show the most variation among regions and are dominated by the metropolitan counties. For metro counties the ratio to personal income is 1.21 and to population is 1.28. The share of ADC expenditures received by counties with large cities is roughly equal to the shares of income and population. For the two remaining nonmetropolitan area categories, however, the ratios fall below 1.0, to 0.59 and 0.64.

The relative distribution of state supplement expenditures is similar for the state's metropolitan and nonmetropolitan counties, but within nonmetro counties, large-city counties record the highest ratios (1.27 to income and 1.20 to population).

Food stamps is an assistance category where metropolitan counties and large-city counties receive a large portion of expenditures relative to income and population. Large-city counties record the largest ratios.

The ratios for Medicaid are similar across regions (close to 1) with the exception of rural counties. Medicaid is the only public assistance category where rural counties receive a larger portion of expenditures than their income and population. This is likely to indicate a high proportion of older residents.

The final category of public assistance is adult and family contracted services. It also favors metropolitan counties with a ratio to income of 1.06 and to population of 1.13. The respective ratios for nonmetro counties are 0.94 and 0.89. As is the case for most of the other assistance categories, large-city counties have larger ratios than the other two nonmetro county groups.

Reviewing public assistance expenditures also points out an apparent inconsistency. Residents of nonmetropolitan counties have lower per capita incomes than do metropolitan county residents, and within nonmetropolitan areas, per capita incomes decline as the size of the largest city gets smaller. Even though public assistance payments are based on need, nonmetropolitan counties, especially rural counties and counties with small cities, account for a disproportionately smaller share of public assistance expenditures.

Summary of Patterns

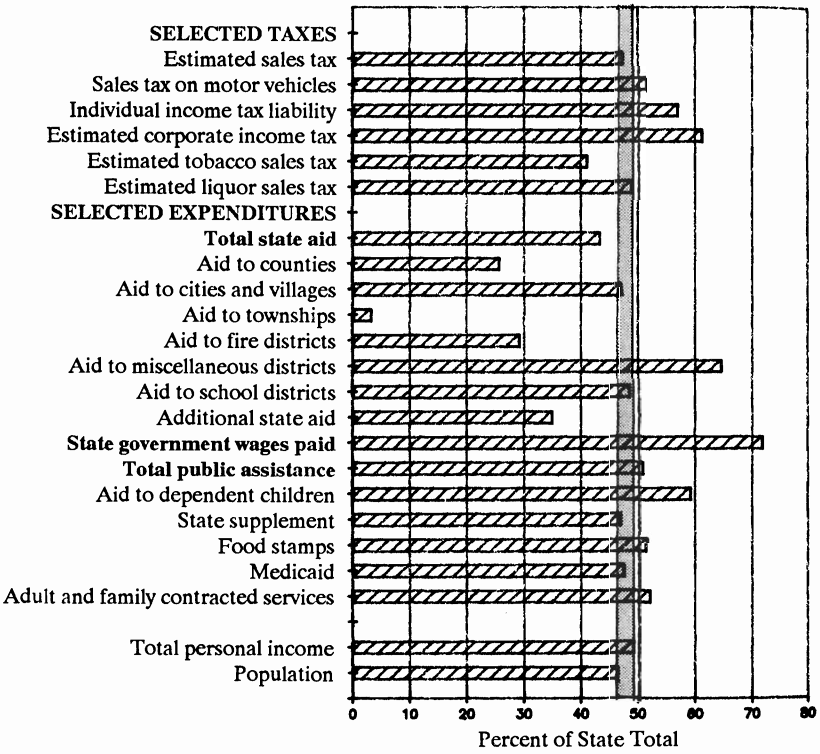
After reviewing each tax and expenditure category separately, it is easy to lose sight of the relative distribution within a set of counties. This section summarizes the relationship of taxes and expenditures for each set of counties. Figures 2 through 5 in this section provide visual comparisons of each group's percentage of taxes paid, expenditures received, and personal income and population represented. The figures are equivalent to reading down a column in table 2.

The vertical bar on each graph represents the range between the proportion of total state population and personal income that the county group accounts for. Any tax or expenditure item to the left of the bar represents less than the group's share of population and income. Any tax or expenditure item to the right of the vertical bar represents a greater share than the group's population and income.

Metropolitan Counties. As shown in figure 2, metropolitan counties account for 49.4 percent of the personal income and 46.5 percent of the population in Nebraska. Such counties generally account for a higher share of taxes than their population or income suggests. The biggest discrepancies occur for individual and corporate income taxes. Sales-related taxes, on the other hand, are comparable to income and population. The percentage of taxes paid by these counties range from a low of 41.4 percent for the tobacco tax to a high of 61.5 percent for corporate income tax.

Metropolitan counties also receive a larger share of the state's expenditures. This is primarily due to the large state government presence in Lincoln. Among the four county groupings, metropolitan counties receive

Figure 2 - Selected Taxes and Expenditures for Nebraska's Metropolitan Counties, 1985



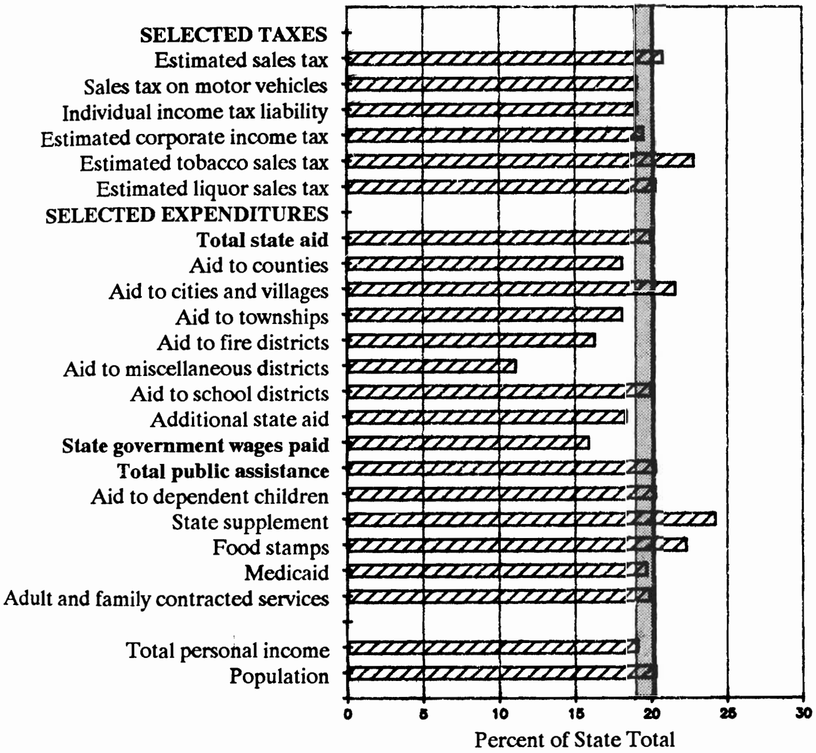
Source: Table 2.

the smallest ratios of state aid to income and to population. Governmental subdivisions in these counties receive 43.6 percent of total state aid. State aid expenditures range from a low of 3.5 percent of the aid for townships (Washington County is the only metropolitan county that has active townships) to a high of 64.9 percent for miscellaneous aid.

Metropolitan counties receive 51.1 percent of the state's public assistance payments, ranging from a high of 59.5 percent of the ADC payments to a low of 47.0 percent of state supplement.

Large-City Counties. Figure 3 shows that counties with large cities generally account for taxes and expenditures proportionate to their income and population. They earn 19.1 percent of Nebraska's personal income and hold 20.3 percent of its population.

Figure 3 - Selected Taxes and Expenditures for Nebraska's Large-City Counties, 1985



Source: Table 2.

There is little variation in the percentages of taxes paid by this group of counties. With the exception of tobacco taxes, the share of taxes paid is in the 19 to 21 percent range.

Most of the expenditures received fall in this same range: state aid is 20.0 percent and public assistance is 20.3 percent. Wages and salaries of state employees, on the other hand, are 16.0 percent. Within the state aid category, these counties receive a high of 21.7 percent of the aid to cities and villages and a low of 11.2 percent of the aid to miscellaneous districts. Their shares of public assistance spending range from 19.7 percent for Medicaid to 24.3 percent for state supplement payments.

Small-City Counties. These counties are close in population and income shares to large-city counties, but they generate less taxes and receive less state spending. Small-city counties account for 19.0 percent of Nebraska's total personal income and 19.8 percent of its population.

Figure 4 shows that other than state aid, most small-city county tax and expenditure categories account for smaller percentages of the respective state totals. Taxes range from 21.6 percent for tobacco tax to 13.0 percent for corporate income tax. The tobacco tax is the only tax where small-city counties are responsible for more than their percentages of the state's population and income.

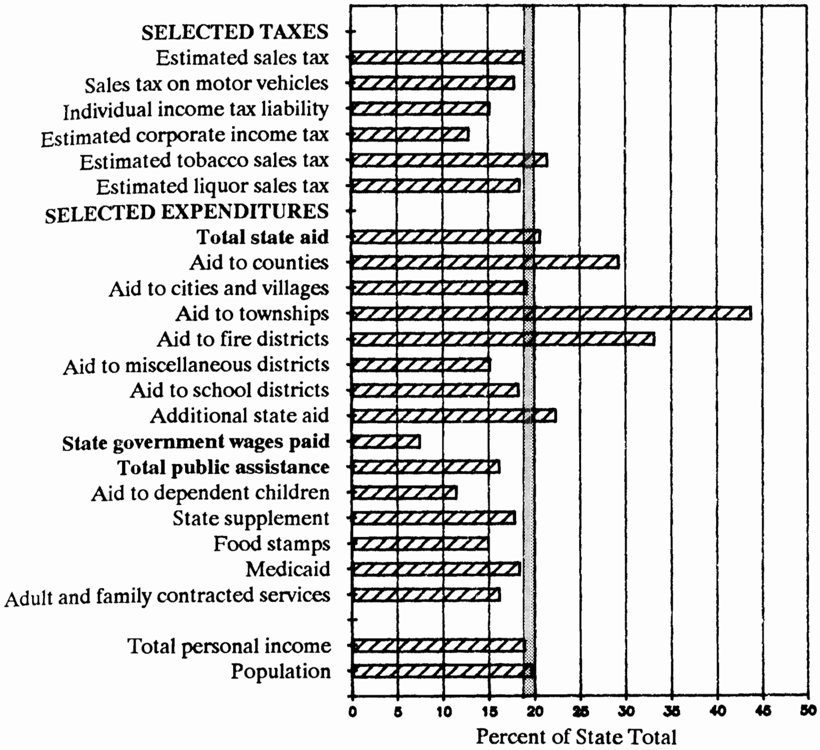
On the expenditure side, these counties receive 20.8 percent of the state aid and 16.3 percent of public assistance expenditures, but only 7.6 percent of state government wages and salaries. Except for state aid to school districts and miscellaneous districts, state aid for small-city counties is near or above 20 percent of the state total. At 43.9 percent, state aid to townships accounts for the largest share of an individual aid category. The largest percentage of public assistance expenditures comes from Medicaid at 18.5 percent, and the smallest comes from ADC at 11.6 percent.

Rural Counties. Figure 5 shows that rural counties exhibit a pattern similar to small-city counties. They account for a lower percentage of state taxes and also receive a lower percentage of many state expenditures, especially state government wages and salaries. This group of counties receives 12.5 percent of the state's personal income and contains 13.4 percent of the state's population.

Rural counties account for 5.9 percent of the corporate income taxes paid and 14.1 percent of the tobacco taxes. The percentages of income taxes paid fall far below population and income percentages, while sales-based taxes are comparable or slightly below.

State aid to rural counties amounts to 15.7 percent of the Nebraska total, while public assistance is 12.2 percent and wages and salaries only come to 4.3 percent. Within the state aid category, aid to townships accounts for 34.3

Figure 4 - Selected Taxes and Expenditures for Nebraska's Small-City Counties, 1985



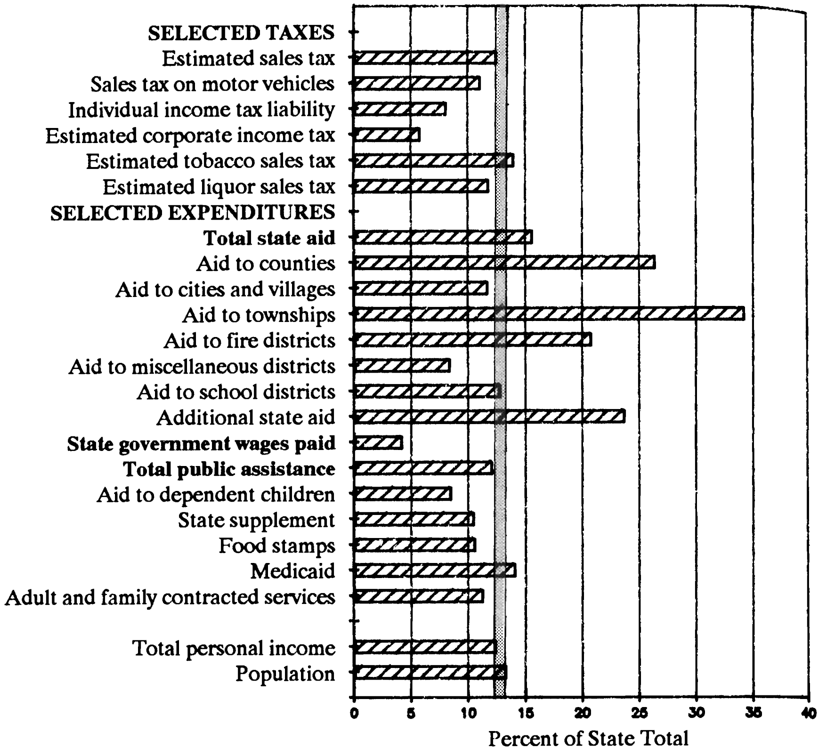
Source: Table 2.

percent of the state total, and aid to county governments accounts for 26.5 percent. The largest relative share of public assistance expenditures comes from Medicaid (14.2 percent) and the smallest from ADC (8.6 percent).

Lincoln MSA

Because of the major presence of state government activities in the Lincoln area, tax and expenditure information was also tabulated for the state without Lancaster County. This affected totals for the metropolitan counties, which then included Douglas, Sarpy, Washington, and Dakota counties. Because there was little change in most of the ratios, tables containing the adjusted data can be found in Appendix A at the end of this chapter. As expected, the largest change occurred for the ratios relating to wages and salaries.

Figure 5 - Selected Taxes and Expenditures for Nebraska's Rural Counties, 1985



Source: Table 2.

With Lancaster County removed, the state wages ratios for the remaining metropolitan counties dropped significantly but remained above 1.0 (1.13 to personal income and 1.23 to population). All nonmetropolitan regions showed gains, but large-city counties made the biggest jump, overtaking even the metro ratios. Their ratio of state wages to income is 1.37, and to population it is 1.30. This suggests that large-city counties have a sizable presence of state government facilities that is overshadowed when Lancaster County is included in the analysis.

Policy Choices and Recommendations

The information presented in this chapter indicates that geographic differences in the state's taxing and spending actions, though they may be unintentional, do occur. Furthermore, impacts vary across tax and expenditure categories. This chapter has shown that it is unlikely that county groups will receive and generate the same proportions of expenditures and taxes. Unless these impacts were intended, state policy makers must pay closer attention to the geographic distribution of their revenue and expenditure decisions.

As the Nebraska Unicameral continues with its New Horizons for Nebraska program, it should begin to incorporate an explicit regional perspective into its information base and decision-making process.

Although the geographic dimensions of state government taxing and spending decisions are rarely visible as a public issue, the current discussion surrounding LB775, the Employment and Investment Growth Act, illustrates how the benefits and costs of a particular program can have, or be perceived to have, differential geographic impacts. Another issue that Nebraska's policy makers will face in the near future is whether Nebraska should have a set of policies or strategies that focus on rural areas in general, and local governments in particular. Regardless of the choices made, policy makers must have information about and be aware of the potential geographic impacts of their decisions. As the Nebraska Unicameral continues with its New Horizons for Nebraska program, it should begin to incorporate an explicit regional perspective into its information base and decision-making process.

While the analysis presented in this chapter does not suggest any policy choices directly, it serves as an aid for evaluating alternative policies and strategies. Although a number of policy issues have dimensions that can be analyzed using a geographic approach, many of them can be highlighted under two broad themes: property tax relief and rural development.

Property Tax Relief

Property tax relief has been a popular topic in Nebraska for many years. Studies have shown that Nebraska's local governments are highly dependent on property taxes and that they receive proportionately less state aid than most other states' local governments do. Moreover, some county subdivisions are approaching their constitutional limit for property taxes.

Property tax relief can take many forms, but in the United States it generally has involved raising other taxes at the state level. These added revenues are then used to provide increased state aid to local governments, which can, in turn, decrease their reliance on property taxes. Using this perspective, property tax relief can also be viewed as increased state aid to local governments.

Once a decision is made to provide property tax relief, many inter-related questions remain. First it must be decided which tax or combination of taxes will be used to raise the necessary revenue, and which units of local government will be supported through increased state aid. In addition, it must be decided whether income is to be redistributed from one area of the state to another area as part of the process. Each of these goals requires different taxing and spending strategies and possibly redesigned state aid formulas. These strategies can provide comparable changes in taxes and spending for all counties (although the base to which the additional aid is added may be unequal); can redistribute income to a group of counties; or can provide aid to a governmental subdivision without regard to the geographic impacts.

Earlier in this chapter it was shown that income-related taxes usually have a greater relative impact on metropolitan counties and counties with large cities, and a much smaller impact on rural counties and counties with small cities. On the other hand, sales-based taxes such as the sales and use tax and cigarette and liquor taxes have a somewhat greater impact on nonmetropolitan counties, especially those with larger cities. In other words, increasing income-related taxes will generate relatively more revenues from metropolitan counties, while increasing sales-related taxes will generate relatively more revenues from nonmetropolitan counties (compared to population and personal income).

Regardless of the actions policy makers take, they must have some concept of the redistribution they wish to achieve.

For an example on the expenditure side, the state might decide to provide property tax relief for rural counties. Because these counties receive proportionately more aid than would be expected, given their population and income, even an across-the-board increase in state aid would have the effect of targeting aid to rural counties. If state policy makers chose to further increase the share of state aid accruing to rural counties, they could either create an additional category of aid (such as critical rural infrastructure assistance), change the allocation formulas currently used in order to emphasize factors characteristic of rural counties, or provide more aid directly to county governments (the county subdivision with the highest ratios of expenditures to income and population for rural counties).

Other reallocation strategies would entail changes in both taxes and expenditures. If policy makers chose to raise the sales tax in order to provide increased state aid to schools, the geographic effect would likely be neutral: both sales tax and aid to school districts are relatively even across Nebraska's four groups of counties. On the other hand, raising the income tax in order to increase aid to education would draw more taxes, proportionately, from metropolitan counties and would cause a redistribution of income from metropolitan to nonmetropolitan (primarily rural) counties.

Regardless of the actions policy makers take, they must have some concept of the redistribution they wish to achieve. This can then be compared to current distribution patterns to help determine which actions will attain the desired distribution.

Rural Development

By most indications, Nebraska's nonmetropolitan counties have suffered losses of income and jobs and an erosion of their tax base during the 1980s. Many states have developed policies and programs to address the development needs of rural areas. It seems likely that Nebraska policy makers, too, will have to address rural issues in the future. It appears that state government activities have approximately equivalent tax and expenditure impacts on rural counties. These counties generate less taxes than their share of income and population, and the share of state government expenditures going to these counties is also less than their share of income and population. If Nebraska's policy makers decide to develop a set of strategies or policies focusing explicitly on rural areas, they will face a number of policy choices with differing regional impacts that may augment or hinder their efforts.

People or Places. The state can focus its policies on people or places. According to Smith (1988):

> Advocates of people strategies argue that the needs of rural people can best be met when location factors are isolated from strategies; in other words, place is secondary . . . . For example . . . individual assistance programs, whether they be income maintenance or basic education programs to help the rural poor, need not be much different from programs for the urban poor.
>
> Advocates of place strategies, on the other hand, argue that people should be able to stay where they currently live; thus, efforts to meet human needs must focus on rural communities. Place-oriented advocates also argue that it is more efficient to use existing infrastructure investments than to relocate people. (Smith 1988)

Regardless of the strategy used, there is a geographic dimension. Expenditures for current people-oriented programs, such as public assistance, would tend to favor metropolitan counties and counties with large cities.

Place-oriented strategies that use existing state aid programs would tend to provide more dollars directly to rural counties and counties with small cities.

Growth Centers. Another basic choice that can be addressed in fashioning a rural strategy is whether to focus resources on communities or areas that are most distressed, or on growth centers in order to enhance their performance. SRI (1988) advocated building economic capacity in Nebraska's regional centers, which will cause the economies of those areas to grow, providing job opportunities for the surrounding areas. This strategy would develop not only the mid-sized communities, but many of the smaller communities as well. SRI's definition of growth centers included all of the large-city counties and several of the small-city counties described above.

Deichert and Smith (1988) also reviewed growth center strategies for Nebraska. They indicated that state government could differentiate among several sizes of growth centers. Most, however, conformed to the descriptions of large- and small-city counties used in this chapter.

One action consistent with a growth center strategy would be to increase state aid to large- and small-counties by changing allocation formulas or developing new categories of aid. However, another policy option would be to move some state government operations to these counties.

If state policy makers decide to pursue a growth center policy, they should focus state resources and programs on large- and small-city counties. Currently it appears that the opposite of a growth center strategy is being pursued. Large-city counties receive proportionately less of the state's expenditures but generate taxes comparable to their population and income base. Although these counties receive a share of state aid close to their income and population shares and account for a slightly higher share of public assistance, the lower proportion of state government wages and salaries, as compared to metropolitan counties, results in a lower level of expenditures.

Small-city counties exhibit a wider discrepancy than large-city counties. Taxes accounted for by this group of counties are proportionately lower and state aid is proportionately higher, but public assistance payments and state government wages and salaries received are much lower than for large-city counties. The net result is that their share of expenditures generally is lower than their share of taxes.

One action consistent with a growth center strategy would be to increase state aid to these counties by changing allocation formulas or developing new categories of aid. However, another policy option would be to move some state government operations to these counties, thereby adding to their wages, salaries, and service base. Given current and future changes in communications technology, it is likely that state government activities could be decentralized without losing efficiency or incurring additional costs. Obviously, any effort in this direction would have to be thoroughly evaluated on an agency-by-agency and program-by-program basis.

Conclusion

It has been argued that Nebraska is disconnecting, with urban and rural areas growing further apart. These areas, however, are linked through the operations of Nebraska's state government. Because policy decisions have differential impacts upon areas of the state, policy makers should try to identify these impacts. Decisions made by Nebraska's policy makers can rebuild linkages between the state's rural and urban areas, or they can intensify the rural-urban split.

Endnote

1. While the specific source of funds for individual expenditure categories cannot be identified, it should be remembered that many revenue sources are earmarked for specific spending activities. For example, much of the intergovernmental revenue received from the federal government goes for income maintenance and other social service payments.

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