Politics, Capacity, and Pass-Through Decisions in the American States: Evidence from the American Recovery and Reinvestment Act

Sean Nicholson-Crotty* and Jill Nicholson-Crotty†

*Indiana University; seanicho@indiana.edu
†Indiana University

State governments have considerable discretion regarding when they use federal grants to deliver goods and service themselves and when they pass those grants through to fund service delivery by local governments, nonprofit organizations, and other substate entities. This discretion influences the expenditure, and potentially the impact, of many billions of dollars every year. Unfortunately, we know very little about the decisions states make regarding the volume of federal grant aid they pass through, or about the types of subrecipients most likely to receive that money. Drawing on delegation theory, this study develops the argument that the amount and target of pass-through funding will be a function of the state's capacity to produce desired goods, shared policy preferences between state and local actors, and the relative capacity of substate actors to produce those same goods. We test these hypotheses in analyses of the pass-through of ARRA grants to subrecipients by state governments between 2009 and 2012. The results from those analyses suggest that delegation theory provides a useful way to understand both the volume of pass-through that states engage in as well as the target of those monies.

The Government Accountability Office estimates that in 2012, at least $79.6 billion of federal grants were "passed through" by states to subrecipients, including primarily local governments and nonprofit organizations. In some cases, a high rate of pass-through is mandated by the federal government. For example, the Homeland Security Grant Program requires that states distribute at least 80 percent of awarded funding to local governments. Many other grants, however, like those administered by U.S. Department of Energy (DOE) for the establishment of State Energy Plans or those offered by U.S. Department of Health and Human Services

Publius: The Journal of Federalism volume 45 number 3, pp. 475–494
doi:10.1093/publius/pjv018
Advance Access publication April 24, 2015

(HHS) for care of the aging,[1] do not have any pass-through requirement. The lack of such a requirement is, in fact, more typical. When President Reagan consolidated seventy-seven categorical grants into nine block grants under the 1981 Omnibus Budget Reconciliation Act, only two included a pass-through mandate.

Thus, in many programs, state governments have considerable discretion regarding when they use federal grants to deliver goods and service themselves and when they pass those grants through to fund service delivery by other entities. The use of that discretion creates significant variability in the ways in which federal dollars are spent once they arrive in a state. For example, South Dakota passed approximately 26 percent of the total funds it received from the American Recovery and Reinvestment Act (ARRA) programs through to subrecipients. Alternatively, North Dakota, which actually received considerably less ARRA funding, sent 44 percent of that money to local governments and nonprofit organizations. The targets of funding also varied dramatically. As an example, Virginia sent over 85 percent of its pass-through to local governments, while Arkansas sent over 60 percent to nonprofit organizations.[2]

If we look at specific types of funding, the differences are even starker. For example, Georgia passed through 25 percent of ARRA grants it received from HHS, while Mississippi sent almost 95 percent of its awards to subrecipients. Equally as interesting, the variability in pass-through behavior included not only how much money was awarded, but also the *types* of subrecipients that states chose. Georgia sent 72 percent of the HHS money it passed through to local governments. Mississippi sent only 2 percent of awards to local governments and, instead, chose to pass federal grants almost exclusively (96 percent) to nonprofit organizations within the state.

Despite the large amount of money at stake and the significant implications for fiscal federalism and state policy, very little work has sought to explain variation in the pass-through of federal grant funding. Decades of research have taught us a great deal about how federal actors design and distribute grants-in-aid. We also know much about the ways in which recipients use discretion when deciding how to spend those monies. We know almost nothing, however, about the decisions states make regarding the volume of federal grant aid they send to substate actors, or about the types of subrecipients most likely to receive that money. The work that exists is of high quality, but it has tended to be narrowly focused on the responsiveness of different levels of government to urban problems and the implications of pass-through decisions for local government finances.

This study offers a more comprehensive examination of the political economy of pass-through decisions in the American States. Drawing primarily on the delegation theory it develops the argument that the amount and target of delegated spending will be a function of shared policy preferences between state and local actors, the state's capacity to produce desired goods, and the relative capacity of substate

actors to produce those same goods. We test these hypotheses in analyses of the pass-through of ARRA grants to subrecipients by state governments between 2009 and 2012.

Findings from these analyses accord well with the expectations, drawn from delegation theory, that state actors are more likely to delegate the production of public goods via pass-through grants (i) when they have to due to limited capacity, (ii) when they have more allies among potential agents, and (iii) they will send such grants to the agent with the highest capacity for producing quality goods and services. Specifically, we find that the amount of grant aid passed through to substate entities is associated with the state's management capacity and the degree to which Governors and potential subrecipients share political preferences. We also find that the proportion of those funds targeted at nonprofit organizations versus local governments is in part a function of the relative capacity of those subrecipients to produce goods and services funded by pass-through.

Pass-through Funds in the Literature

As noted above, there is very little work on the award of federal grants to subrecipients by state governments. Even the federal government has given relatively little attention to the subject, focusing primarily on compliance with those pass-through requirements that exist and the reporting and accounting challenges that accompany subawards (see for example US, GAO 2013). The small amount of scholarly literature has typically approached the issue from the perspective of urban politics and policy.

The first body of relevant work emerged during a larger debate over whether states or the federal government are more responsive to urban problems.[3] Comparing relative levels of direct federal and state aid to "distressed cities," including pass-through funds, made a convenient vehicle for testing responsiveness (see for example Morgan and England 1984; Morgan and Shih 1991). In one of the earlier pieces, Dye and Hurley (1978) rejected the long-held conclusion that the states were largely unresponsive to urban problems based on relatively stronger correlations between state aid and measures of need within the cities. The authors did not separate pass-through and own-source state aid, and acknowledged that the latter might explain the result. Ward (1981) sharply criticized Dye and Hurley's conclusions based on several operational decisions in their analysis, including the failure to separate federal funds from state aid, and suggested that this had likely caused the authors to dramatically overstate the relative responsiveness of state governments to urban problems. It is important to note, however, that he also did not separate the components of state aid or model the pass-through decision independently. The debate over responsiveness among the levels persisted for the better part of the next decade with scholars arguing that the distinction between

state aid and federal pass-through is unimportant because the impact relative to direct federal aid was so much larger (Tietlebaum 1981); that the choice of cities as the unit of analysis reduced the confounding influence of pass-through funds because most of those were targeted at counties and school districts (a questionable assertion, but see Pelissero 1984); or, at times, ignoring the potential impact of pass-through funds altogether (Schneider and Ji 1990).

Related to, but in some ways distinct from, the responsiveness literature is work suggesting that differences in the state-local fiscal context may affect state aid decisions. Key differences include the existence of revenue sharing arrangements, the proportion of total expenditures (particularly in health and education) provided by the different levels, differing mandates regarding service provision in areas such as welfare, and variation in the amount of local spending mandated by state governments, among others (see for example ACIR 1978, 1981, 1982 for examples). They also include differences in the degree to which states are willing to impose limits on the types and levels of taxes that local governments can levy (see Joyce and Mullins 1991; Mullins and Wallin 2004). These and other characteristics of the state-local fiscal context are important for this analysis because they affect the amount of aid, including pass-through, transferred from state to local governments (Ladd and Yinger 1989). Other work has shown that state characteristics influence the targeting of pass-through when states administer programs like the Community Development Block Grant (Rich 1993).

Pass-through funds again received explicit attention in the literature when scholars became interested in the effects of grant consolidation, devolution, and reduction during the Reagan Administration. Early descriptive accounts speculated that state-level decision making for programs like the CDBG small cities grant might result in community development efforts more attuned to local interests (instead of always favoring housing rehabilitation, which was HUDs preferred policy) (See for example Krane 1987). Later work confirmed that the focus changed when states began administering the program, but did not always move closer to local preferences. Interestingly, for our purposes, it also demonstrated that state implementation capacity was an important predictor of the way in which the grants were administered (Jennings et al. 1986).

Other empirical work during this period was concerned with the impact that cuts and consolidation would have on local finances. Luce and Pack (1984) found that mandated pass-through monies often displaced state aid at more than a $1 to $1 rate while grants not accompanied by a mandate actually had a small positive effect on local revenue. Because of supplantation, the authors suggested that local governments in about forty states would be worse off with 100 percent pass-through requirements and that those in a majority of states are better off with more state discretion, even controlling for a reduction in federal aid. Subsequent work confirmed the mechanism underlying this assertion, finding that state grants almost

completely offset cuts in direct federal aid between 1984 and 1987 (Ladd 1990). Interestingly, however, that research suggested that the offset came primarily from own-source rather than additional pass-through funds (Ladd 1991).

A Theory of Pass-through Decisions

The literature on pass-through funds has not only been relatively limited but also offered mixed conclusions regarding the use of these funds—with some work suggesting that states use pass-through monies to supplant own-source expenditures (Luce and Pack 1984) and other work finding that state aid responsiveness to local government is largely independent of pass-through (Ladd 1991). There also does not exist an accepted theoretical model of pass-through decisions. Ladd (1990, 1991) articulated and validated a model of state aid, which suggested that it is a function of state revenue, local revenue, and changes in federal direct aid to local governments. Because she finds that state aid is not dependent on pass-through decisions, however, that model does not allow us to generate specific hypotheses about the conditions under which states will use *federal* monies to fund public goods production by other levels of government, rather than providing those goods themselves. It also cannot tell us why a state might choose to target pass-through funds at third or public sector organizations.

In this study, we draw primarily on delegation theory in order to develop hypotheses about the conditions under which states will choose to pass grants through to subrecipients, as well as the types of organizations that are most likely to receive those funds. Delegation ''theory'' is actually a somewhat amorphous product of a massive and evolving literature (See Hammond, Glazer, and Bendor 2001 for a review and synthesis). At its core, delegation is concerned with when a person with decision authority will choose to give some of that authority to an agent, but authors have been interested in myriad elements and extensions of that key question (e.g., signaling, screening, credible commitment, etc.). For our purpose, however, the most basic model will suffice. In that model, a boss can either delegate or not and the subordinate can choose to work or not. Intuitively, the boss prefers and to the degree possible will choose an agent that works over one that shirks. The model assumes an ally principle, meaning that if the boss delegates, then she picks the agent whose ideal point is the closest to hers.

The boss is indifferent between getting the outcome she wants for sure by controlling the policy herself or by delegating. Hence, if there is an agent who can produce the outcome that the boss wants because he works and is ideologically similar to the boss then she delegates; if not, she does not. The value of delegation decreases when the boss has greater certainty about her ability to produce the desired outcome or greater uncertainty about the ideology of available agents or their willingness to work (Bawn 1995).

We begin with the assumption that state actors are interested in accomplishing policy goals and that they sometimes believe that delegating via pass-through grants is the best way to do this. If a state has the capacity to deliver public goods to constituents directly, then it is likely that it will do so. This is because direct provision, as opposed to delegation to some agent, ensures less policy drift (see Epstein and O'Halloran 1999) and maximizes electoral credit from voters (Peterson 1995; Volden 2007).

However, there are likely to be many cases in which state governments do not have the capacity to directly deliver the level of public goods desired by constituents. This lack of capacity might be structural, in that local entities control the mechanisms through which goods are delivered. For example, if citizens across a state demand higher quality teachers, a state could change continuing education requirements, but it could not mandate that districts hire more teachers with master's degrees. Alternatively, the lack of capacity might be functional. In other words, state government agencies may simply be too small, underfunded, or lacking in expertise to deliver the services citizens demand. Research suggests that such capacity shortfalls hurt performance and increase the incentives for contracting and outsourcing (See Howlett 2009 for a review); so it is reasonable to expect that they would also increase the reliance on pass-through funding. In the language of delegation theory, these factors increase uncertainty on the part of the boss, in our case the state's governor, regarding her ability to produce the desired policy outcome.

On the other side of the capacity coin is the ability of the *recipient jurisdiction* to handle public goods production delegated to them via a grant. When deciding to make awards, prime recipients of federal grants can typically choose between local governments and 501(c)(3) providers, though, at times, federal grants also authorize private businesses as subrecipients. Delegation theory suggests that states making subawards will attempt to select agents that are most likely to produce the outcome that they desire, which we assume is, in part at least, effective policy. There is significant variation across the states in the degree to which local governments and/or the third sector have the capacity necessary to be effective implementers of policy and relative effectiveness should help to explain the choice by state agencies of the target for pass-through grants. This capacity is analogous to the willingness/ability of the agent to work to produce the boss' goals in the simplified delegation model discussed above.[4]

Finally, we expect the ally principle to hold in the delegation of pass-through grants. As noted above, delegation theory suggests that if the boss delegates, she picks the agent whose ideal point is the closest to hers.[5] In the case of pass-through grants, the ally principle implies that Governors and agencies should pass more federal money along when there is a higher level of shared partisanship and, thus preference congruence, with substate actors. In cases where such congruence is low,

we would expect them to centralize, rather than delegate, production in order to minimize policy and credit drift.

In summary, delegation theory leads us to expect that Governors and state agencies will pass a greater volume of federal grants through to subrecipients when they lack sufficient capacity to deliver goods and services on their own, when there is a greater political (i.e., partisan) payoff for doing so, and when they have a higher degree of preference congruence with a state's citizenry. Additionally, we hypothesize that the target of pass-through funds will be, in part at least, a function of the relative capacity of local governments and third sector organizations within a state.

Pass-through under the Recovery Act

Testing the expectations outlined above, or any hypotheses regarding pass-through funds, is challenging both because of the difficulty in separating pass-through from state aid in many publicly available data and the even more daunting task of following that money to the subawardee. Fortunately, transparency and accountability requirements associated with the American Recovery and Reinvestment Act offer a unique opportunity to do both of these things for a large volume of grant aid.[6]

For this article, we look at all ARRA awards made to the states and subsequently to subrecipients between 2009 and 2012.[7] The key purposes of the ARRA were five-fold including: to promote economic recovery; to assist those most impacted citizens; to provide investments in technological advances in science and health; provide investments in transportation, environmental protection, and other infrastructure; and to stabilize State and local government budgets, in an attempt to avoid reductions in essential services and state and local tax increases.

To those ends, the ARRA designated roughly one-third to tax incentives for individuals and businesses. Of those, the payroll tax credit and the losses offset credit were the largest programs. The Act also dedicated a little less than half the total ($357 billion) to federal spending programs. Some of that money, like the $21 billion spent on energy infrastructure was directed exclusively at federal targets for projects like nuclear production site cleanup. Much of it, however, like the $27.2 billion set aside for Energy Efficiency and Renewable Energy Research and Investment was targeted at the states through mechanisms like the Energy Efficiency and Conservation Block Grant and the State Energy Programs. Those funds, along those sent to the states through the National Surface Transportation Discretionary Grants, Drinking Water Revolving Fund, and numerous other programs were eligible for pass-through to substate actors.

Finally, $144 billion, or about one-fifth of total Recovery Act aid was allocated to State and Local Fiscal Relief. About 60 percent of that went to Medicaid, but the

reminder was targeted at education via the State Fiscal Stabilization Fund. These funds were given to governors in order to incentivize policy changes (e.g., pre-K through college student data systems, school turnaround, etc.), help local schools avoid cuts and retain teachers, and support facilities modernization and repair. Obviously, these funds were also eligible for pass-through to subrecipients.

In addition to the unprecedented transparency of the awards, we believe that the large volume of aid eligible for pass through across numerous programs also makes the ARRA a good place to study this phenomenon because the amount of money and the number of transactions gives us the statistical power to draw reliable conclusions. Of course, those unique features of the recovery act, along with the financial conditions that precipitated the Act, might also jeopardize the external validity of our results. We believe that the results should generalize, at least in part, to other pass-through decisions because much of the funding was distributed through *existing* programs with *existing* pass through requirements. Nonetheless, we are cognizant of the threats to external validity and urge readers to interpret the results with caution until they can be validated in other settings.

From 2009 to 2012, the federal government made approximately 1,200 grants to state-level agencies and entities. Those actors, in turn, made approximately 120,000 awards to subrecipients within their states. Because we are interested in the delegation decisions that state governments make with grant dollars, we aggregate these transactions to the state year, which is the unit of analysis in models discussed below.[8] Average pass-through grants per capita, as well as the proportion of those funds that went to nonprofit organizations and local governments, between 2009 and 2012 are presented for each state in table 1.

Dependent Variables

We utilize three dependent variables to test the hypotheses outlined in the last section. First, we examine the ARRA dollars per capita passed through to subawardees by each state between 2009 and 2012. Recognizing that the total amount of pass-through is in part a function of the amount of grant funding that flows into the state, this model controls for the total ARRA funding per capita received by the state government in each year. We are compelled to use this method of ''normalizing'' the pass-through amounts, rather than simply modeling the proportion of funds passed through, because of way in which the data on the timing of awards and subawards are recorded by the federal government. A grant may be received by the state in year t, but awarded to a subrecipient in year t and $t+1$, or only in year $t+1$. We cannot observe this timing perfectly, which leads to unrealistic figures in some cases when we try to calculate a *yearly* pass-through rate. Putting total ARRA grants per capita in a model of pass-through per capita allows us to control relatively comprehensively for the amount of money a state has to

Table 1 ARRA pass-through in the American states, 2009–2012

State	Pass-through PC	Proportion local	Proportion NPO	State	Pass-through PC	Proportion local	Proportion NPO
Alabama	19.81	0.97	0.03	Montana	37.41	0.4	0.56
Alaska	62.56	0.75	0.22	Nebraska	21.56	0.36	0.57
Arizona	7.73	0.74	0.18	Nevada	88.40	0.53	0.44
Arkansas	15.86	0.28	0.59	New Hampshire	43.76	0.51	0.37
California	3.66	0.84	0.15	New Jersey	9.59	0.95	0.02
Colorado	25.42	0.86	0.11	New Mexico	31.83	0.76	0.06
Connecticut	18.63	0.59	0.35	New York	4.24	0.89	0.07
Delaware	109.30	0.78	0.18	North Carolina	13.31	0.37	0.56
Florida	7.91	0.73	0.27	North Dakota	53.15	0.89	0.06
Georgia	12.63	0.77	0.12	Ohio	6.86	0.67	0.24
Hawaii	159.93	0.08	0.72	Oklahoma	7.76	0.79	0.11
Idaho	38.52	0.41	0.63	Oregon	15.48	0.82	0.21
Illinois	7.55	0.88	0.05	Pennsylvania	8.73	0.51	0.44
Indiana	13.04	0.55	0.35	Rhode Island	76.89	0.31	0.65
Iowa	20.30	0.54	0.22	South Carolina	16.12	0.74	0.06
Kansas	19.18	0.48	0.44	South Dakota	27.49	0.66	0.09
Kentucky	18.74	0.47	0.4	Tennessee	8.27	0.45	0.47
Louisiana	21.44	0.37	0.45	Texas	3.53	0.54	0.42
Maine	30.12	0.92	0.07	Utah	31.54	0.77	0.09
Maryland	24.41	0.63	0.31	Vermont	37.05	0.37	0.57
Massachusetts	10.97	0.37	0.58	Virginia	14.11	0.85	0.1
Michigan	8.58	0.83	0.17	Washington	6.11	0.76	0.12
Minnesota	12.25	0.78	0.12	West Virginia	40.59	0.71	0.13
Mississippi	21.40	0.28	0.64	Wisconsin	7.90	0.94	0.05
Missouri	11.03	0.3	0.6	Wyoming	83.40	0.73	0.17

Note. Pass-through calculated from grants awarded to state agencies and offices as the prime recipient. Proportions do not always sum to 1 because states also pass a limited amount of grant funding through to private businesses and to other state agencies.

work with when considering delegation, without creating unrealistic values in the data.

Because of the range on the variable, and the resulting possibility undue influence for outliers, we model the natural log of pass-through per capita. In order to ease interpretation and keep the presentation of results consistent, we also log all other dependent and independent variables discussed below.

The second set of dependent variables captures the proportion of ARRA pass-through funds awarded to local governments and nonprofit organizations between

2009 and 2012. Here we can calculate proportions because the data on allocation by the state and the receipt by a subawardee are matched by year. For this study, 501(c)(3) and (c)(6) organizations were coded as "nonprofit." Counties, municipalities, single purpose governments, special districts, and councils or taskforces made up of exclusively local government representatives were coded as "local government." These were the primary categories of subrecipient and, not surprisingly, the two variables are highly negatively correlated ($p = -0.71$). However, they are not perfect inverses of each other because states also passed money through to private firms and other state agencies.

Independent Variables

Our key independent variables measure the primary explanations for delegation suggested by the theory, including the state's capacity to produce goods on its own, the degree to which potential agents are allies of the state government, and the ability of different types of agent to produce the outcomes desired by the state. We measure state capacity as both financial ability and management acumen. For the first, we include an indicator of the proportion of total expenditures made up by state funds. This captures the degree to which the state, rather than local governments is responsible for providing goods and services demanded by citizens.[9] We expect that states which pay a smaller share of total expenditures with own-source dollars have a lower ability to deliver goods and services directly and will, therefore, pass more money through to other entities.

We measure the state's ability to manage dollars and programs more directly with the 2008 Government Performance Project management grade for each state. Theoretically, the variable ranges from 1(F) to 12(A), though the states were actually assigned values of 4 through 11 in 2008. The measure assesses the quality and innovativeness of state government management on multiple dimensions including: Information, Human resources, Finances, and Infrastructure. We expect that states that received a higher grade will have greater capacity to use federal grants to deliver goods directly and will, therefore, pass a smaller proportion through to subawardees.

Our next set of independent variables capture the ally principle, which suggests that states should be more willing to delegate to agents that share their preferences. First, we measure the partisanship of state policymaking institutions. Because federal grants are almost always passed through executive agencies we focus on the preferences of the Governors that "control" those agencies. Specifically, we create a variable coded 1 for Republican governor and 0 otherwise. Next we capture the preferences of potential agents with the expressed preferences of the citizenry in the last presidential election. Specifically, we use the percent vote for the Republican presidential candidate in the last election. Finally, we explicitly measure the degree

to which the governor and the citizenry that make up local governments and nonprofits are likely to be allies by interacting the indicator of Republican governor with the presidential vote. We expect the interaction to be positive, suggesting that the willingness of Republicans to delegate policy authority to subnational agents increases when those agents are more likely to share their preferences.

The final set of independent variables measures the ability of different types of agents that might receive pass-through dollars to produce desired policy outcomes. For nonprofits within a state, we use the density of available targets as well as their wealth as a proxy for capacity. The assumption is that available partners who have the means to manage programming are a prerequisite for grant-related delegation. These data are gathered from the Form 990s submitted by NPOs to the Internal Revenue Service.[10] Specifically, we use the number of tax exempt entities per capita within the state and average beginning year revenue for those organizations. We expect each of these to be positively correlated with the proportion of pass-through grants awarded to nonprofits.

For local governments we have data that allow for slightly better measures of ability or capacity. In that case, we use the average own-source revenue per capita across those units as a measure of wealth and local government personnel per capita as a measure of management capacity. Again, each of these should positively correlate with the amount of pass-through to this type of agent. In order to avoid endogeneity between ARRA pass-through decisions and the density and wealth of the various sectors, we use data from 2008 to 2009 to construct measures of NPO and local government capacity.

Control Variables

The models discussed below also include several variables to account for alternative reasons why state governments might pass more federal grants through, or target those funds at different types of agents. Recognizing that legislatures also have a say in the expenditure of grant funds, especially through their role authorizing (or failing to authorize) expenditure in the state's budget, we account for legislative partisanship with a measure of the percent of legislative seats controlled by Democrats. The next control measures relative state size and population density, which may have an influence on how grants are spent once they enter a state. Specifically, we use the relative population formula used in many federal awards.[11]

We also control for differences in the state-local fiscal context, which may influence pass-through. Our most general proxy for this concept is total state aid to local governments. Previous work has offered mixed conclusions regarding whether or not pass-through decisions are related to own-source aid. Nonetheless, it seems reasonable to expect that the total amount of aid, including pass-through, in other program areas might reflect some latent or structural characteristic that would also

affect the pass-through of ARRA funds, independent of our variables of interest. We also include an indicator for Tax and Expenditure limits which captures the restrictiveness of limits on both state and local governments (see Stallman et al. 2012). These could encourage pass-through by structurally limiting the state government's ability to absorb and expend new revenue. Additionally, they could reduce the ability of local governments to produce desired outcomes and, thus, make nonprofits a more attractive agent for delegation via pass-through.

Finally, we measure one additional feature of the economic landscape that may have influenced the pass-through of recovery act dollars. Specifically, all models include a measure of the unemployment rate based on the assumption that states with higher levels of unemployment may have worked to get more "stimulus" dollars into local economies.

Results and Discussion

Results from the analyses outlined above are presented in tables 2 and 3. The first contains the model of the ARRA grants per capita awarded by a state to subrecipients, while the second presents the findings from models of proportion passed through to local governments and nonprofit organizations respectively. In all three cases, we estimate cross-sectional time series regressions with fixed effects for year and standard errors clustered at the state level.

Before getting to the variables of interest in our model of overall pass-through in table 2, we can note that the measure of total ARRA funds per capita is significant and positively correlated to pass-through, as we would expect. Alternatively, the percent of seats in the state legislature controlled by Democrats, state and local tax-and-expenditure limits, unemployment rate, and state population density relative to the remainder of the nation were negatively associated with the dependent variable. The amount of state aid per capita to local governments was not significantly correlated with the amount of pass-through.

Turning now to the variables of interest, the results regarding the impact of state capacity on pass-through decisions are mixed. On the one hand, the Government Performance Project measure of overall capacity is negative and significant, suggesting that states with greater management acumen passed less ARRA funding through to subrecipients. Substantively, the coefficient suggests that a 10 percent increase in capacity decreases pass-through by 2.2 percent. Alternatively, the findings suggest that the proportion of total expenditures provided by state rather than local governments is not significantly associated with the amount of pass-through.

The findings also provide evidence for the ally principle and the hypothesis that pass-through amounts are greater when more citizens have preferences that match those of the governor. Indeed, the results suggest that each 10 percent increase in

Table 2 Pass-through of recovery act grants by state governments, 2009–2012

Variables	Coefficients
Total ARRA Awards per capita	0.056**
	(0.026)
Republican Governor	–2.638
	(1.946)
GOP Presidential Vote	0.143
	(0.408)
Rep. Gov. X GOP Vote	0.847*
	(0.591)
Management Capacity	–0.220**
	(0.111)
Proportion State Expenditures	0.858
	(0.522)
Nonprofits per capita	0.861***
	(0.277)
Local Gov. Employment per capita	0.263**
	(0.110)
Percent Dem. Legislature	–0.01*
	(0.004)
Tax/Expenditure Limits	–0.016*
	(0.009)
Unemployment	–0.764**
	(0.304)
State Aid to Local Governments	–0.020
	(0.178)
Relative Population Density	–0.294**
	(0.077)
Intercept	8.572**
	(1.968)
$N = 196$	
$R^2 = 0.48$	

Notes. Model includes year fixed effects. Numbers in parentheses are robust standard errors. $^{*}p < 0.1$, $^{**}p < 0.05$, $^{***}p < 0.01$.

the percent vote for the Republican presidential candidate increases the amount passed through by Republican governors by 8.4 percent. A graph of the marginal effects in Figure 1 suggests, however, that the interaction between Republican governor and presidential vote only becomes significant in cases where more than 37 percent of citizens cast ballots for the Republican candidate.

Table 3 Targets of recovery act pass-through by state governments, 2009–2012

Variables	Local governments	Nonprofits
Nonprofits per capita	–0.819***	0.483
	(0.254)	(0.489)
Nonprofit Wealth	–0.087	0.800**
	(0.173)	(0.333)
Local Government Employ.	–0.105	0.017
	(0.254)	(0.489)
Local Government Revenue	0.428*	–1.023**
	(0.469)	(0.08)
Republican Governor	–0.285*	–0.212
	(0.121)	(0.234)
Percent Dem. Legislature	–0.009*	–0.005
	(0.004)	(0.009)
Management Capacity	–0.222	0.689**
	(0.137)	(0.263)
Tax/Expenditure Limits	–0.021**	0.044**
	(0.009)	(0.017)
Unemployment	–0.241	0.153
	(0.269)	(0.518)
State Aid	0.223	0.066
	(0.191)	(0.369)
Relative Pop. Density	0.185*	–0.094
	(0.102)	(0.196)
Intercept	–0.968	–13.465**
	(2.714)	(5.222)
$N =$	196	196
$R^2 =$	0.27	0.22

Notes. Models include year fixed effects. Numbers in parentheses are robust standard errors. $^{*}p<0.1$, $^{**}p<0.05$, $^{***}p<0.01$.

The findings in table 3 provide support for our expectations regarding the types of organizations most likely to receive pass-through funds. Turning first to the model of pass-through to local governments (Column 1), the results suggest that delegation via pass-through is, in part at least, a function of the agent's ability to produce the desired outcome. Tax revenue collected by those governments has a positive and significant amount of funding that they receive in pass-through funds. It is important to remember that the measure is constructed using own-source revenue and, is not, therefore influenced by state aid or pass-through.

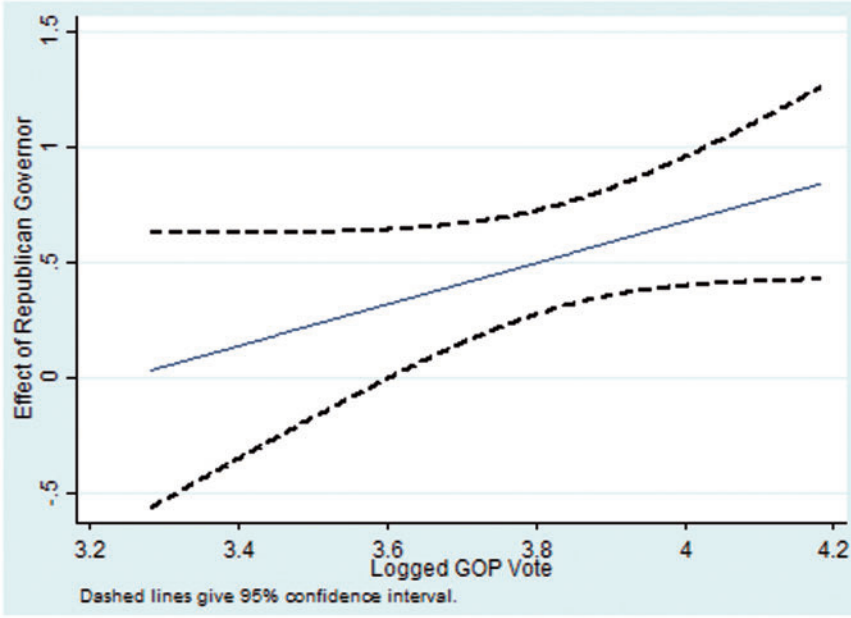

Figure 1 Moderating impact of citizen partisanship on the relationship between gubernatorial partisanship and ARRA pass-through.

Substantively, the results suggest that a 10 percent increase in local government revenue per capita increases the percent of pass-through funds going to local governments by 4.8 percent. The measure of local employees per capita is also positive and significant suggesting that higher capacity is associated with more pass-through to local government agents. The coefficient suggests that a 10 percent increase in local employment correlates with a 2.5 percent increase in the amount of pass-through targeted at local governments.

The findings also suggest that pass-through to local governments is associated with the relative availability of the other primary type of subrecipients—nonprofit organizations. The measure of NPO density is negative and significant and suggests that a 10 percent increase in the density of nonprofits correlates with a 10 percent decrease in the proportion of pass-through funding to local governments. Before moving on, it is interesting to note that the presence of tax and expenditure limits on local governments is also negatively associated with pass-through to this type of agent, though the substantive impact is relatively small. We include this measure to control for an important element of the state-fiscal context, but it can also be interpreted as a good proxy for the ability of local governments to produce desired policy outcomes.

The model of pass-through to nonprofit organizations (Column 2) also suggests that the relative capacity of the available agents affects delegation via pass-through.

The average wealth of third sector recipients is significant and positively related to the proportion passed through, with a 10 percent increase in average NPOs assets associated with a 8.9 percent increase in the proportion of ARRA sent to that type of organization. The percentage of pass-through funds targeted at nonprofit organizations was also associated with the capacity of potential local government recipients of those funds. A 10 percent increase in local government revenue is associated with a decrease of 10 percent in ARRA pass-through to nonprofit organizations. The measure of tax and expenditure limits on local governments is positive and significant in this case, suggesting that state governments are more likely to delegate to nonprofits when other available agents are financially constrained in their ability to produce services. Interestingly, the results also suggest that higher management capacity at the state level is associated with a higher percentage of pass-through to nonprofits rather than local governments.

Conclusion

An enormous amount of federal money flows into states and is then sent on to local governments, nonprofit organizations and, in a small percentage of cases, to private businesses. In most cases, the amount of funding that is passed through is not mandated by the grant. Previous research has told us very little about the factors that influence this decision, or about choices regarding the types of organizations targeted by pass-through funds.

This study suggests that such decisions can be understood, in part at least, through the lens of delegation theory. The amount of grant aid passed through to substate entities is associated with the state's capacity to produce the goods and services and the degree to which Governors and potential subrecipients share political preferences. The relative capacity of potential subrecipients to produce goods and services funded by pass-through is a consistent predictor of the type of organization—nonprofit or public—that is most likely to receive those funds. These findings accord well with our theoretical expectation that state actors are more likely to delegate the production of public goods via pass-through grants (i) when they have to due to limited capacity, (ii) when they have more allies among potential agents, and (iii) to the agent with the highest capacity for producing quality goods and services.

We believe our results are significant for both the study of fiscal federalism and the state policy. Chubb (1985) and others have suggested that grants-in-aid are a two tiered delegation problem involving Congress and the grantor agency and then the agency and the recipient jurisdiction. Our results suggest that, in some cases, it is in fact a three-tiered process, where the state governments that receive federal grants then choose to delegate some public goods production to another level via pass-through grants. As at the other transfer points, this delegation introduces the

possibility for policy drift. Our results indicate that states take steps to overcome moral hazard and adverse selection problems, but it is unlikely that these steps are sufficient to ensure that subrecipients spend grants exactly as the state agency would. This suggests that ''fly-paper'' studies and other work which looks at the correspondence between federal grants and subnational spending and policy outcomes probably need to account for pass-through activity and the consequences it may have for the achievement of federal goals via the grant-in-aid system.

The findings also have implications for state policy and state-local relations. Pass-through funds are an important intergovernmental policy tool used by states. Even after controlling for the capacity and availability of potential subrecipients, it appears that states pass more grant money through when there are more copartisans to receive it. Interestingly, there is not a great deal of research on the political use of aid by state governments, but this result accords well with studies of CDBG competitions and grant expenditure by Governors in state legislative districts. Coupled with the increasing number of state imposed local tax and expenditure limits, the strategic targeting of grant aid suggests a centralization of policy authority by state governments that is worthy of continued research.

As is often the case, our results raise as many questions as they answer. One of these turns on the amount of pass through that was *not* explained by delegation theory. The individual predictors suggested by the theory appear to have a meaningful impact on pass-through decisions. However, goodness of fit statistics suggest that a model based on delegation theory explains about 50 percent of the variation in total pass-through and about 25 percent of the choice of target between 2009 and 2012. This, of course, begs the question of what other theoretical stories can help us to understand this process. One likely explanation is a type of ''picket-fence'' intergovernmental relations. In places where local administrators and/or executive directors have long-standing relationships with state agencies, federal grants may flow through to those entities regardless of politics or relative capacity. Another probable explanation for pass-through variation may be interest group politics. States where potential subrecipients are more active advocates at the state-level may have higher levels of pass-through. Similarly, if municipalities or NPOs have louder voice in the state capital, it could easily change the balance of pass-through dollars flowing to the respective sectors. Though it is beyond the scope of this study, each of these alternative theoretical approaches to the question of pass-through deserves additional empirical attention.

Another key question is the direction of the relationship between pass-through grants and subrecipient capacity and activities. Because we only have a relatively short snapshot of time in our data, we cannot determine if subrecipient capacity is truly exogenous to state pass-through decisions. In reality, we assume that the relative availability and capacity of nonprofit organizations and local governments is in part a product of the fact that the state government has systematically favored

one sector with pass-through and other state aid over time. We cannot determine the degree to which pass-through and capacity are reciprocal, which is why we avoid causal claims in this study, but it is obviously important to disentangle this relationship in future research.

Notes

1 See for example CFDA 93.044, 93.045, 93.053.
2 Calculations made by the authors using data from fedspending.org.
3 This in turn was part of an even larger debate regarding the degree to which increases in state government professionalism and capacity leading up to the 1980s justified a rejection of the ''weak sister'' and ''fallen arches'' of federalism labels that had been placed on them in the 1960s.
4 The assumption that pass-through to different sectors is exclusively a function of granting agency preferences is, at best, incomplete because it ignores research suggesting that demand side factors have a significant impact on grant distribution patterns (Rich 1989). Specifically, this work suggests that (i) some entities have more experience and are better at applying for grants and (ii) differences in grantsmanship capacity influences patterns of aid distribution. Despite the fact that it suggests a different underlying mechanism, this insight actually leads to the same expectation discussed above. In states where local governments have greater capacity, more funds will flow down to public sector organizations and the opposite will be true in states where the third sector has relatively greater grant related capacity.
5 This insight from delegation theory comports well with competitive federalism theory, which suggests grants inherently confer some electoral advantage on the recipient jurisdiction because voters will only give credit to actors from a particular level for the actual share of an intergovernmental good that they produce (See Peterson 1995; Volden 2007). With this in mind, grantors should prefer to cede electoral advantage to those with whom they share preferences and alliances. This expectation also accords well with the literature on federal grant distribution, which suggests that grants are more likely to be awarded to states and congressional districts controlled by copartisans (Bickers and Stein 2000; Balla et al. 2002).
6 The Coburn-Obama Act of 2006 was supposed to ensure the creation of a searchable database of all federal grants and contracts. The database, named USASpending was created, but was deactivated during the sequester in 2011. The Federal Procurement Data Service did track and make publicly available both awards and subawards for grants associated with ARRA. For this article, we use fedspending.org's (formerly OMB Watch) interface with the FPDS data, which is significantly more user friendly.
7 Available data actually run through the second quarter of 2012.
8 Fedspending.org organizes data by calendar, rather than fiscal year and, thus, the unit of analysis is the state-calendar year.
9 In addition to capturing capacity, this measure also serves as a proxy for important features of the state-local fiscal context. Key results do not change if we use state

own-source revenue per capita as proxy for capacity (see for example Brown and Potoski 2006; Cogburn and Schneider 2003).

10 In 2008, organizations that reported more than $25,000 in revenue were required to file the 990.

11 The formula is 0.5 (state population/national population) + 0.5 (state area/national area).

References

Advisory Commission on Intergovernmental Relations. 1978. *State mandating of local expenditures*. Washington, DC: U.S. Government Printing Office.

———. 1981. *State local roles in the federal system*. Washington, DC: U.S. Government Printing Office.

———. 1982. *State local roles in the federal system*. Washington, DC: U.S. Government Printing Office.

Balla, Steven J., Eric D. Lawrence, Forrest Maltzman, and Lee Sigelman. 2002. Partisanship, blame avoidance, and the distribution of legislative pork. *American Journal of Political Science* 46 (3): 515–25.

Bawn, K. 1995. Political control versus expertise: Congressional choices about administrative procedures. *American Political Science Review* 89 (01): 62–73.

Bickers, K. N., and R. M. Stein. 2000. The congressional pork barrel in a Republican era. *Journal of Politics* 62 (4): 1070–86.

Chubb, J. E. 1985. The political economy of federalism. *American Political Science Review* 79 (04): 994–1015.

Dye, T. R., and T. L. Hurley. 1978. The responsiveness of federal and state governments to urban problems. *The Journal of Politics* 40 (01): 196–207.

Epstein, D., and S. O'Halloran. 1999. *Delegating powers: A transaction cost politics approach to policy making under separate powers*. New York: Cambridge University Press.

Howlett, Michael. 2009. Policy analytical capacity and evidence-based policy-making: Lessons from Canada. *Canadian Public Administration* 52: 153–75.

Jennings, Edward, Dale Krane, Alex Pattakos and B. J. Reed, eds. 1986. *From nation to states: The small cities community development block grant program*. Albany, NY: State University of New York Press.

Joyce, P. G., and D. R. Mullins. 1991. The changing fiscal structure of the state and local public sector: The impact of tax and expenditure limitations. *Public Administration Review* 240–53.

Krane, D. 1987. Devolution of the small cities CDBG program in Mississippi. *Publius: The Journal of Federalism* 17 (4): 81–96.

Ladd, H. F. 1990. State assistance to local governments: Changes during the 1980s. *The American Economic Review* 171–75.

———. 1991. The state aid decision: Changes in state aid to local governments, 1982–87. *National tax Journal* 477–96.

Ladd, H. F., and J. Yinger. 1991. *America's ailing cities: Fiscal health and the design of urban policy*. Baltimore, MD: John's Hopkins University Press.

Luce, T., and J. R. Pack. 1984. State support under the new federalism. *Journal of Policy Analysis and Management* 3 (3): 339–58.

Lyons, W. E., D. Lowery and R. H. DeHoog. 1992. *The politics of dissatisfaction*. Armonk, NY: ME Sharpe.

Morgan, D. R., and R. E. England. 1984. State aid to cities: A causal inquiry. *Publius: The Journal of Federalism* 14 (2): 67–82.

Morgan, D. R., and M. C. Shih. 1991. Targeting state and federal aid to city needs. *State & Local Government Review* 21: 60–68.

Mullins, D. R., and B. A. Wallin. 2004. Tax and expenditure limitations: Introduction and overview. *Public Budgeting & Finance* 24 (4): 2–15.

Nicholson-Crotty, S., and N. Theobald. 2011. Claiming credit in the US federal system: Testing a model of competitive federalism. *Publius: The Journal of Federalism* 41 (2): 232–56.

Pelissero, J. P. 1984. State aid and city needs: An examination of residual state aid to large cities. *The Journal of Politics* 46 (03): 916–35.

Peterson, P. E. 1995. *The price of federalism*. Washington, DC: Brookings Institution Press.

Rich, M. J. 1989. Distributive politics and the allocation of federal grants. *The American Political Science Review* 83: 193–213.

Rich, M. J. 1993. *Federal policymaking and the poor*. Princeton, NJ: Princeton University Press.

Schneider, M., and B. M. Ji. 1990. The political economy of intergovernmental grant seeking: Targeting and suburbs, 1977 and 1982. *American Journal of Political Science* 34: 408–20.

Stallmann, J. I., S. Deller, L. Amiel, and C. Maher. 2012. Tax and expenditure limitations and state credit ratings. *Public Finance Review* 40 (5): 643–669.

Teitelbaum, F. 1981. The relative responsiveness of state and federal aid to distressed cities. *Review of Policy Research* 1 (2): 309–22.

U.S. Government Accountability Office. 2013. *Oversight of Selected States' Disbursement of Federal Funds Addresses Timeliness and Administrative Allowances GAO-13-392*. Washington, D.C.

Volden, C. 2007. Intergovernmental grants: A formal model of interrelated national and subnational political decisions. *Publius: The Journal of Federalism* 37 (2): 209–43.

Ward, Peter D. 1981. The measurement of federal and state responsiveness to urban problems. *Journal of Politics* 43: 83–101.