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Senate Energy and Natural Resources Committee Hearing on Secure Rural School and Community Self-Determination Act and Payments in Lieu of Taxes

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Thank you Chairman Murkowski, Ranking Member Cantwell, and members of the Committee. I am pleased to join you today to discuss the Secure Rural Schools and Community Self-Determination Act (SRS) and Payments in Lieu of Taxes (PILT) programs.

I work at Headwaters Economics, an independent, nonprofit research group based in Montana. We work to improve community development and land management decisions in the West.

As an economic geographer, my primary research and policy interest is in understanding why some counties that have federal lands and natural resources seem to do better than others. Working closely with county commissioners and collaborative groups, I appreciate the importance of federal county payments in shaping local government budgets and rural economic development opportunities.

I want to use my time to describe a potential solution for county payments: building an endowment for public land counties by investing commercial receipts into a newly established permanent trust fund. Such an endowment would fund a long-term reauthorization of SRS—eventually eliminating the need for appropriations altogether—and would guarantee all counties predictable, fair, and rising payments year over year.

It has become clear that asking Congress to reauthorize and appropriate funds for SRS and PILT each year without a funding plan in place is an untenable position for counties. An endowment offers a long-term funding solution.

A permanent trust funded by commercial receipts could benefit from increased revenue from federal lands, but it would stabilize these revenue streams over time and ensure all counties fair payments even in years and in places where generating historic levels of receipts isn't possible.

Before describing how an endowment would work and the ingredients for its success, I want to provide important context, including: the current budget proposals for PILT and SRS and their implications for counties; the economic contributions of federal lands in a changing economy; the important role of natural resource fiscal policy in local government budgets and economic development; and the limitations of revenue sharing payments as a solution to ensuring predictable and fair compensation to local governments for tax-exempt federal lands.

Current Budget Proposals Would Significantly Reduce Payments to Local Governments

Headwaters Economics recently generated projected payments for every county in the U.S. based on the most recent Forest Service 25 percent revenue sharing payments, Bureau of Land Management (BLM) O&C 50 percent revenue sharing payments, U.S. Fish and Wildlife Service Refuge Revenue Sharing (RRS) payments, and a projection of PILT for FY 2017 with the funding level capped at the most recent 10-year average of PILT payments. These projections are included as Attachment A.

Our projections show that if SRS is not reauthorized and if the Administration's recent budget proposal to limit PILT to the ten-year average is accepted by Congress, federal payments to counties will decline by 43 percent nationally. The hardest hit counties, primarily rural counties with large shares of federal lands, could see payments decline by more than 90 percent.

For example, I was in Central Idaho last week meeting with county commissioners, timber industry and agency employees, staff of environmental NGOs and others that are part of the Clearwater Basin Collaborative. The Collaborative set aside half a day to discuss the implications of losing SRS and PILT funding, and what solutions might be available.

We heard from Idaho County that it stands to lose $7 million, nearly 90 percent of the county's payment. Clearwater County could lose more than half its payment (57%), a decline of more than $1.1 million.

Declines Will Harm Rural Counties Already Struggling Economically and Fiscally

The potential sharp decline in payments comes at a time when rural counties across the U.S. like Idaho and Clearwater Counties are still struggling to recover from the Great Recession. The two counties together lost population between 2011 and 2015 (the latest year for which data are available) and have more than 500 fewer jobs in 2015 compared to 2007 before the start of the Great Recession.

It should be noted that not all counties with tax-exempt lands are struggling. Cities and some parts of the rural West connected to them by convenient air travel are growing, attracting people and businesses choosing to locate near federal lands. Places like Bozeman, Montana, where I live are grappling with rapid growth.

Still, some rural counties are not capturing these economic opportunities in part because of limitations they face in attracting high-wage services jobs being created in the new economy in places like Bozeman.

Further, rural areas have seen a decline in manufacturing and natural resource sector jobs, and largely stagnant wages. These declines stem from productivity gains (fewer workers are required in plants, mills and in the forest), increased competition and trade, and continued uncertainty in commodity markets. It is in these rural communities where the impact of declining SRS and PILT payments will be felt most acutely.

There are opportunities in these rural communities, and we recently profiled gains in rural manufacturing. However

County Payments Support Rural Services Critical to Economic Development

Rural areas struggling economically also often face a declining tax base, reduced school enrollments and significant challenges in raising local levies and fees, in part due to constitutional and regulatory limits at the state level on local revenue and spending authority.

Local governments also are being asked to take on increasing responsibilities, including a growing role for counties in providing social services and coordinating economic development in addition to more traditional local government operations including public safety, education, roads, and infrastructure responsibilities.

More and more, counties and the services they provide are central to local and regional economic stability and growth. For example, good schools are central to attracting and retaining families and businesses in rural counties and education is correlated with higher wages and better employment opportunities for individuals.

Declining enrollment at Clearwater County, Idaho's schools and reduced budgets have jeopardized gifted and talented programs, shop, art, and music classes that are sometimes cut and are constantly threatened from limited budgets. The school district is now on a four-day week and cannot support day-long kindergarten classes. Losing SRS would require deeper cuts.

The county is working to retain and attract families and businesses, but this becomes increasingly difficult without good schools and other services.

Increasing Active Management on Federal Lands Will Not Replace SRS and PILT

Idaho and Clearwater Counties also are working collaboratively to address critical forest health challenges and trying to retain mill capacity and skilled workers to do the work. There is broad agreement among members of the Collaborative on many of these issues, and success stories are increasing.

Despite need and opportunity to increase the pace and scale of restoration activities, including timber harvest, active management is not a solution to county payments. Most projects on the national forests are conducted using stewardship contracts that allow receipts to be retained locally and reinvested in additional work on the forest. Even if stewardship receipts are made eligible for revenue sharing or if these projects are converted to commercial sales, receipts would not approach recent levels of SRS. Annual revenue sharing payments also would expose counties to volatility in commodity markets and continued political and legal uncertainty over time.

This is true in a large number of timber dependent counties where receipts are unlikely to return to historic levels. Last year, I travelled to California to attend the Rural County Representatives of California (RCRC) annual meeting. RCRC champions policies on behalf of California's rural counties which face the same forest health, economic development, and fiscal challenges as their peers across the U.S. These counties in California, like Idaho, are concerned about the loss of SRS and PILT funding.

Sierra County, California, for example, lost population and employment between 2000 and 2015. Historically mining and timber-dependent, the county is too remote to capture the high-wage high-tech jobs being created in the state's metro regions. The county also has lost its mill capacity, skilled workforce, and other infrastructure that would facilitate large annual commercial timber harvests.

Supervisor Lee Adams and his peers have closely watched discussions about reforming the process to harvest timber off National Forest lands, which, in turn, would boost payments to counties and schools. Supervisor Adams welcomes and encourages such reforms. But federal policymakers need to be aware that in Sierra County—and it can be assumed in a great number of California's forested counties—reverting back to 25 percent payments will not sustain local schools and road budgets. Even if the federal government finds a way to increase the pace and scale of forest management activity, Supervisor Adams worries the regulatory climate in California likely would not allow it to happen in Sierra County and many other rural California counties.

Building an Endowment to Benefit Rural Counties and Their Schools

Building an endowment to fund federal land payments to counties and schools by establishing a permanent trust offers a solution to these difficult issues related to county payments.

First, it offers a long-term funding solution that over time pays for permanent extensions of SRS. This hearing and recent letters from Congress, governors, and counties to the Administration indicate broad support for extending these programs while a longer-term funding solution is developed. Building an endowment would accomplish that goal.

A permanent trust would utilize commercial receipts as the funding mechanism for county payments. A key difference between the permanent trust model and annual revenue sharing is that a permanent trust stabilizes these revenue streams over time, insulating counties from the uncertainty of annual revenue sharing payments.

For counties like Sierra County, California where increasing receipts to historic levels is unlikely, SRS is needed to provide fair and equitable compensation for non-taxable federal lands.

For Idaho and Clearwater Counties, Idaho, extending SRS provides the predictability and flexibility for the counties to continue to work collaboratively on forest management reform with all the tools and creative leasing and partnership opportunities available to them. SRS payments mitigate the financial risks associated with national recessions and uncertain commodity markets.

For example, had Congress established a permanent trust in 2000 along with SRS, today it would be worth $1.2 billion and would be able to make annual distributions equal to or greater than current levels of annual commercial receipts. In other words, counties would already be better off with predictable and stable distributions from a trust that match or exceed current revenue sharing payments.

Permanent trusts are common among U.S. states that have timber, coal, oil and gas resources on state lands. For example, Alaska, Louisiana, New Mexico, North Dakota, Oklahoma, Texas, and Wyoming have state land royalty and severance tax trust funds with a combined value of more than $100 billion.

Currently, commercial receipts generated on federal lands are either shared directly with counties or are deposited in the U.S. Treasury to pay the first portion of appropriated programs.

If a permanent trust is established, receipts would instead be directed to the permanent trust and the principal balance would be invested to earn income. Congress also could make discretionary allocations to the permanent trust. For example, Congress could make a one-time deposit to capitalize the permanent trust up front or identify additional sources of commercial receipts that could be deposited into the permanent trust on a recurring basis.

For a permanent trust to work, the principal balance must be protected in perpetuity. One possible solution is to have in independent entity with a fiduciary responsibility to counties and the U.S. Treasury manage the permanent trust. Legislation establishing a permanent trust would require that the entity with fiduciary responsibility to counties manages the trust principal for the interest of the beneficiaries; that the management strategy ensures the preservation of the trust principal; and the trust is managed to provide a predictable source of revenue to the beneficiaries.

Congress and the Administration (for example through the office of the inspector generals of the Agriculture and Interior departments) would have to provide oversight.

In order to keep counties whole in the interim period while the endowment is growing, Congress must extend appropriations. Extending appropriations for SRS at current (2015) levels and investing receipts into a permanent trust would increase the cost of county payments to the U.S. treasury in the short term. The minimum level of appropriations required to establish a permanent trust is an amount equal to the value of receipts invested into the permanent trust each year so that counties are at least held whole with regard to current levels of revenue sharing payments. Congress will need to determine the funding level that is possible and appropriate.

If appropriations fall below the most recent levels of SRS (2015) and the authorized PILT payment, counties will receive lower payments in the short term. The existing PILT formula, with less than full funding, would also have the unintended effect of redistributing payments from rural counties to metropolitan counties. Metro counties would experience payment declines of 39 percent on average while non-metro counties would experience declines of 46 percent on average.

Essentially, rural counties most dependent on payments would bear the brunt of declines. The challenge, if appropriations levels are to fall, is to create a county payment system that does not overcompensate relatively wealthy urban and resort areas, and recognizes the relative importance of PILT in other counties where the compensation from federal lands can be a significant contributor to local governments and services they provide.

If lower funding levels (or no funding for SRS) are appropriated, Congress may consider reforming the PILT formula to reverse the urban bias and prioritize the allocation of lower funding levels to rural counties. Headwaters Economics has explored this idea, and a white paper describing possible reforms are included as Attachment B.

Conclusion

Finding a long-term solution to forest health, rural economic development, and county payments is critical and demands creativity and persistence.

Building an endowment from natural resource wealth is a well-established, transparent solution to the challenge of providing stable and predictable payments from natural resources on public and private land. A new permanent trust at the federal level would reshape the fiscal relationship between federal, states, and local governments. The benefits of permanent and increasing payments without the need for permanent appropriations make it an idea worth exploring.

I look forward to continued discussions and I am happy to answer any questions you may have.

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