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LAND TAX ISSUES

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BEFORE THE

SUBCOMMITTEE ON TAXATION AND IRS OVERSIGHT

OF THE

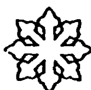
COMMITTEE ON FINANCE

UNITED STATES SENATE

ONE HUNDRED SIXTH CONGRESS

SECOND SESSION

JULY 25, 2000



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LAND TAX ISSUES

TUESDAY, JULY 25, 2000

U.S. SENATE,
SUBCOMMITTEE ON TAXATION AND IRS OVERSIGHT,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:10 a.m., Hon. Orrin G. Hatch (chairman of the subcommittee) presiding.

Also present: Senators Jeffords, Baucus, and Bryan.

OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM UTAH, CHAIRMAN, SUBCOMMITTEE ON TAXATION AND IRS OVERSIGHT

Senator Hatch. I am happy to welcome you all out here today to the Subcommittee on Taxation and IRS Oversight.

We will examine legislation before the committee that provides tax incentives for the conservation of land for environmental benefits.*

I would like to thank Chairman Roth for recognizing the importance of this issue and for his cooperation in scheduling this hearing this morning.

In my State of Utah are vast areas of public land. The good news is that these areas will remain open and will be there for the use and enjoyment of the American public into the foreseeable future.

However, even in Utah we are concerned about the loss of our open spaces, especially in connection with our agricultural lands and our urban open spaces.

The American Farmland Trust estimates that the U.S. has lost approximately 3,000 acres of farmland every day since 1970. Considering the central role that agriculture plays in our society, this is a matter that merits the attention of Congress.

Utahns are concerned about the loss of open spaces in our urban communities as well, and they are not alone. In 1998, there were more than 200 successful ballot initiatives by State legislatures throughout the U.S. aimed at preserving urban open spaces.

When we consider our great cities, we must also remember that there is much more that makes them livable than plenty of parking. Our urban parks contribute significantly to the ecology, not to mention the quality of life, in urban areas.

In response to this need, Senator Baucus and I have introduced S. 1558, the Community Open Space Bond Act. Our proposal

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*For more information on this subject, *see also*, Joint Commitee on Taxation document, Present Law and Description of Proposals Relating to Federal Income Tax Provisions That Impact Energy, Fuel, and Land Use Conservation and Preservation (JCX-84-00), July 24, 2000.

makes available up to $1.9 billion annually for 5 years in bonding authority to State, local, and tribal governments for the conservation of urban open spaces.

Unlike a similar proposal by the administration, our proposal puts the power into the hands of locally elected officials to determine how best to protect their lands. Under our proposal, the Federal Government provides the incentive, but local officials maintain the control.

Today we will also discuss a variety of proposals to protect lands outside of our urban areas. Senator Jeffords has a proposal to provide tax incentives for land sales for conservation purposes.

Senator Gregg has a bill to help preserve family-held forest lands. Senator Brownback has a proposal to provide additional incentives for farmers to use the Conservation Reserve program. Finally, Senator Baucus has a bill that provides incentives for the voluntary conservation of endangered species.

The land conservation bills we will review today create incentives for conservation activities rather than Federal mandates. Federal mandates tend to be expensive and ineffective, and too often they put government policy at odds with our citizens. Incentives, on the other hand, allow citizens to share in the credit for achieving a positive outcome for society.

The vast majority of Americans consider themselves environmentalists, and it is long past time that we promote policies that will tap into this good will and allow our citizens to share in the effort and the credit for conserving our planet.

Now, we will turn to Senator Baucus for any comments he would care to make at this time.

OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR FROM MONTANA

Senator BAUCUS. Thank you very much, Mr. Chairman.

First, I want to thank you for holding this hearing. I know how busy you are, and particularly how involved you are with some of the matters on the floor dealing with judicial nominations, and all the other things on your agenda. I want to thank you, Mr. Chairman, for holding this hearing.

Senator HATCH. Thank you.

Senator BAUCUS. The use of incentives to promote conservation, I think, is a very, very important carrot. There are a lot of sticks in land regulation. Conservation credits are very good carrots.

It is also critical, because too often conservation issues become very polarized. People take sides and stop listening to each other. It is my judgment that, by using incentives, we might be able to bring people a little more together and start to get at that polarization that otherwise occurs.

I was vividly reminded just a few weeks ago, I was holding a conference in Great Falls, MO basically to help prove our State's economy. People might think Montana's income per capita is all right, but I regret to say it is not. We are 51st in the Nation, including District of Columbia, in wage per capita income and we are about 47th in the Nation in total per capita income.

Also, we are not a low cost of living State. We are about 26th in the Nation. We are also first in the Nation in the number of jobs

that a household has to have to make ends meet. We have our work cut out for us.

But the point is this. The conference we held worked. There was so much energy there. One reason was because it was totally nonpartisan. I made it very clear from the beginning, this is nonpartisan. I do not care whether you are a Republican or a Democrat, I am going to cut you off when you are speaking if you get at all partisan. It has got to be totally nonpartisan.

Obviously, there were Democrats and Republicans there that are community leaders, but it was totally nonpartisan. It is clear that that went a long way in creating the confidence that maybe something is going to come out of this.

But one point kept coming across at that conference that over a thousand people attended. That is, as we work to improve our economy we clearly do not want to sacrifice that which makes our State special, that is, our clear skies, our clean water, and a timeless sense of space. We want to strike a balance so that we have, as the conference slogan put it, an economy to match our landscape, second to none.

Today's hearing gives us a chance to consider some tax incentives which I think will help us strike that balance. Let me mention four. The first, is a tax incentive to help communities use bonds to preserve open space, as provided in the legislation that Senator Hatch and I have introduced.

You might think that Montana is one place where open space would not be an issue. Well, that would not be correct. It is a big issue in Montana, for two reasons. First of all, open space defines us. It is why we call Montana the last, best place.

It is why the preamble of our State constitution begins by thanking God for the "quiet beauty of our State, the grandeur of our mountains, and the vastness of our rolling plains." But Montana is changing. It is growing, and in some places, growing quickly.

This decade, Montana's population has grown by more than 10 percent. In Flathead County in the northwestern part of our State, and Gallatin, the south central part, those counties are growing by more than 20 percent.

Growth does have benefits, but it also has costs in the form of sprawl, congestion, pollution, and an increased demand for services.

An editorial in the Billings Gazette, our largest paper, recently put it this way: "Something must be done or in time we will not have to lock the gate because the best parts of Montana will be ruined. Then no one will want to come here, let alone live here."

Our bill would address that. It provides a national incentive for communities to preserve open space, reduce water pollution, and protect the environment.

The second approach is tax incentives to help landowners conserve wildlife, especially through the Partners for Wildlife program. It is a great program, Partners for Wildlife. It brings landowners, State officials conservation groups, people from the local community together to conserve habitat.

A good example is something called Blackfoot Challenge, which is working in our State to preserve habitat for bull trout in West Slope Cutthroat.

As it now stands, landowners that receive payments under other conservation programs do not have to treat the payment as taxable income. On the other hand, because of a glitch in the Code, if a landowner receives payments under the Partners for Wildlife program, they do have to declare it as taxable income. I do not think that makes any sense. It discourages people from participating. I believe we should amend the Code to fix it.

The third approach is the better use of conservation easements. I am proud that this committee has been a leader on conservation easements. I am even more proud that the Montana Land Reliance has been a national leader on the ground. By encouraging easements rather than acquisition of fee title, we can avoid some of the Federal land grant debates that have proven so divisive.

A fourth approach is the State tax incentives. As we all know, we are in the midst of a big debate about how to reform estate tax. I believe, under either of the two major proposals that we have been debating here in the Senate, estate tax will continue to be a factor for years to come.

In light of this, we can build on the work begun in 1997 under the leadership of Senator John Chafee to create incentives for decedents to leave a conservation legacy. I have more to say as we get to other questions, and look forward to the testimony.

Senator HATCH. Thank you, Senator.

Our first witness today is Jon Talisman, who is a former Finance Committee Chief Tax Counsel under Senator Moynihan. He is the Acting Assistant Treasury Secretary for Tax Policy.

Mr. Talisman will be testifying both on the land tax issues that are the subject of the hearing today, and also on the energy tax issues on which this subcommittee held a hearing last Tuesday.

So we are happy to see you again, and we welcome you to the committee. We look forward to your testimony, Jon.

STATEMENT OF JON TALISMAN, ACTING ASSISTANT SECRETARY FOR TAX POLICY, DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Mr. TALISMAN. Thank you, Mr. Chairman.

Mr. Chairman, Senator Baucus, and distinguished members of the subcommittee, I welcome the opportunity to discuss with you today the administration's proposed tax incentives for encouraging the creation of open spaces in urban areas and the preservation and conservation of farm and other rural lands, and our incentives for lowering U.S. dependency on foreign oil.

The President proposed budget initiatives to help build livable communities for the 21st century. This initiative would provide communities with tools, information, and resources they can use to enhance the quality of life of their residents, strengthen their competitiveness, and build a stronger sense of community.

As part of that initiative, the administration proposed a new financing tool, Better America bonds, to help preserve green space and improve water quality for future generations.

The proposal would make available over 5 years a total of $10.75 billion in bond authority for investments by State, local, and tribal governments to preserve green space, create or restore urban

parks, protect water quality, and clean up abandoned industrial sites.

The administration has also proposed to make permanent the tax incentive to clean up brownfields in targeted low-income areas, which is scheduled to expire on December 31 of this year.

With respect to the environment and our dependency on foreign oil, the administration's budget also included an $8 billion program over 5 years to encourage energy efficiency, reduce greenhouse gas emissions, and develop renewable energy sources.

The package includes targeted tax incentives, increased funding for research and development, and energy efficient technology, a new Clean Air Partnership fund to boost State and local efforts to reduce air pollution, accelerated efforts to develop clean energy sources both here and abroad, and funding for global climate change research.

In addition to calling for steps to decrease our demand for oil through increased efficiency, the administration is proposing new steps to support domestic exploration and production and to help producers when oil prices are low.

The administration's proposals would simplify and reduce taxes attributable to geological and geophysical costs and delay rental payments.

In the interest of time, I will focus on two key aspects of our package: Better America bonds and the new tax incentives for highly efficient vehicles. My written testimony also discusses the other key elements of our program.

Americans are increasingly concerned that the quality of the environment surrounding their communities is threatened by sprawl, that scenic vistas are being lost, that watersheds are eroding and contaminated, and that public access to outdoor recreation is diminishing.

To address those concerns, the administration proposed the creation of a new financial tool called Better America bonds for use by State, local, and tribal governments, often in partnership with nonprofit organizations, to help the communities become more livable.

Better America bonds are modeled after the existing Qaulified Zone Academy bonds, which have been effective in stimulating critical investments in schools all over the country.

The Federal Government would, in effect, pay all the interest on Better America bonds for 15 years, thereby significantly lowering the cost of financing below that attainable by issuing traditional tax-exempt bonds.

I want to thank both the Chairman and the Ranking Member for your leadership in sponsoring S. 1558, which shares many aspects of our proposal.

The proceeds of Better America bonds could be used to acquire and improve open spaces, wetlands and public parks, and to assess and remediate brownfields and other damaged property.

The administration proposed $2.15 billion of authority to issue Better America bonds each year for 5 years, beginning in 2001, for a total of $10 75 billion of bond authority.

The EPA would administer an annual open competition among State, local, and tribal governments for bonds authority, subject to published guidelines.

Moving to our energy efficiency initiatives, the administration has proposed several designed to reduce energy consumption and greenhouse gas emissions by encouraging the deployment of technologies that are highly energy efficient and that use renewable and alternative energy sources.

The design of these incentives incorporates several criteria designed to minimize windfalls for investments that would have been made even absent the incentives and to facilitate tax administration.

Let me, briefly, just describe those criteria. First, the eligible items should meet higher standards for energy efficiency than conventional equipment or use renewable energy sources. This ensures that tax benefits promote energy efficiency and reduce greenhouse gas emissions.

Second, the energy efficiency standards should be sufficiently high so that eligible items presently account for a small share of the market. This, again, will minimize windfalls for purchases that would have been made absent the credit.

Third, the targeted technologies have significantly higher purchase prices than conventional equipment, and at current market prices have limited cost effectiveness. These high up-front costs are another reason relatively few items incorporating the targeted technologies would be purchased without a tax incentive.

Fourth, the items should be commercially available, or near commercialization. Fifth, the items must be defined precisely enough so that the IRS and taxpayers can administer and take the incentives.

The tax incentives the administration has proposed cover vehicles, buildings and homes, renewable energy, and industrial equipment.

Again, in the interest of time, and as an illustration, I will discuss only one aspect of our climate change package. Autos consume 40 percent of oil products in this country and the transportation sector accounts for one-third of carbon emissions.

The proposed tax credits for electric and hybrid vehicles will encourage the purchase of vehicles that incorporated advanced automotive technologies and will help to move energy efficient hybrid vehicles from the laboratory to the highway.

The proposal would extend the present tax credit for electric vehicles and fuel cell vehicles. This credit, which is currently 10 percent of the cost of qualified electric vehicles, up to a maximum credit of $4,000, is scheduled to phase down beginning in 2002 and to be phased out entirely in 2005. Our proposal would extend the credit at its $4,000 maximum level through 2006.

The proposal also would provide tax credits of $500 to $3,000 for certain hybrid vehicles, depending on requirements for the vehicle's design and performance. The credits would be available for all qualifying vehicles, including cars, minivans, sports utility vehicles, and pick-up trucks.

Hybrid vehicles, which have more than one source of power on board, and electric vehicles have the potential to reduce greenhouse gas emissions, air pollution, and petroleum consumption. These ve-

hicles can significantly reduce emissions of carbon dioxide, the most prevalent greenhouse gas. Hybrid vehicles eligible for the $3,000 credit would be 50 to 100 percent more fuel efficient than a conventional vehicle of the same size and power.

In conclusion, we believe that the administration's new initiatives represent sound policy that can produce significant environmental and energy security benefits for decades to come.

We look forward to working with the members of the subcommittee, the full committee, and the Congress on these initiatives.

Again, I want to thank both the Chairman and the Ranking Member for holding this hearing and for their leadership in this area.

This concludes my prepared testimony, and I will be happy to answer any questions that you may have.

[The prepared statement of Mr. Talisman appears in the appendix.]

Senator HATCH. Well, thank you so much, Mr. Talisman.

Last Tuesday, the subcommittee heard testimony from witnesses as diverse as the Union of Concerned Scientists and General Motors about the need for tax incentives to jump-start the alternative fuels industry. The Jeffords-Hatch bill was designed to do just that, with temporary market-based incentives.

Now, I know the administration shares our view that the Nation should move forward towards alternative fueled vehicles, but it appears that your proposal focuses solely on electric vehicles and hybrid electric vehicles.

Does the administration not believe that dedicated alternative fueled vehicles powered by fuels such as natural gas or propane should also be promoted?

Mr. TALISMAN. Senator Hatch, as you said, we do share your goals of promoting purchases of vehicles that use alternative fuels. We have a proposal with respect to hybrid vehicles, where certain uses of alternative fuels would qualify for that credit.

We certainly would like to work with you and your staff in developing other tax incentives regarding alternative fuels that meet the criteria that I set forth in my testimony.

Senator HATCH. Well, thank you. That would be great. We would like to make sure we have the best bill we can, and we would like to have both sides together on it and walk down the street together.

One of the major barriers to widespread use of alternative fueled vehicles is the lack of refueling infrastructure. Do you believe that tax incentives such as tax credits or immediate expensing of the cost of such facilities can be effective in attracting potential suppliers to this marketplace?

Mr. TALISMAN. I believe that, again, the issue will be whether there are economic inefficiencies that need to be overcome in attracting people to this marketplace. It is our belief that providing a credit, as we have for the hybrid vehicles, will enable us to encourage this marketplace and encourage suppliers.

There are also significant incentives already in the Code. For example, the excise tax on alternative fuels is lower than it is for, for example, gasoline, generally.

Senator HATCH. All right.

As you have noted, the administration's proposed Better America bond program is similar to the Baucus-Hatch Community Open Space bond bill. The principal difference is in the question of who makes the allocation decisions.

Now, we have been pretty careful in drafting our bill so that the incentive would be provided by the Federal Government, but local decision makers would be in the driver's seat.

Now, how effective do you think the credit approach taken by both proposals would be compared to a typical municipal bond which allows the bond purchasers to receive the interest on a tax-exempt basis?

Mr. TALISMAN. We believe that it would be a very efficient mechanism, that the local governments would be able to capture virtually the full amount of the tax incentive.

Under current tax-exempt bonds some of the tax subsidy is lost to the local government, so we believe it is a more efficient approach. We have used the tax credit bond mechanism and proposed it with respect to Qualified Zone Academy bonds, which have been proven to be an effective device for providing school construction.

Senator HATCH. Thank you.

Do you think that these bonds will be attractive to both individual investors as well as corporate investors?

Mr. TALISMAN. We believe, certainly, that it would be attractive to both individuals and corporate investors, and we believe, as more bonds become available to the marketplace as investors become educated, that will be evidenced.

Senator HATCH. Thank you.

I am going to turn to Senator Baucus, then to Senator Jeffords. I have to step out for a few minutes. I will be back, hopefully, at the end of both of your questions.

Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

Senator HATCH. Excuse me. I missed Senator Bryan. After Senator Jeffords, then Senator Bryan.

Senator BAUCUS. Secretary, do you have any concerns with what the Chairman referred to, namely, instead of the EPA making this allocation decision, a board makes it? Do you have any concerns about that?

Mr. TALISMAN. Well, the issue is whether we believe a special board needs to be established. We certainly want to work with you all to develop an appropriate allocation mechanism.

We believe the EPA is an appropriate device for allocating, and we do not necessarily believe that an 18-member board is necessary, but we would like to work with you all in coming up with a proposal to which we can all agree.

Senator BAUCUS. Well, I appreciate that because I, frankly, think we might need something like this board to get support in Congress to pass it. I think the thought that another government agency is going to be making this allocation is going to run into some significant resistance in the Congress. My main point is one of pragmatics, figuring out a way to get it passed and make it work, but I appreciate your response.

Some critics of this proposal say that somehow we reduce the capital available for the tax-exempt market. That is, these bonds would have that effect.

Do you have any reaction to that?

Mr. TALISMAN. We actually do not believe that that is the case. Again, this is a more efficient mechanism, we believe, and we will direct the subsidies to the local governments. However, we believe that the market can, given the allocation of these bonds, undertake both.

Senator BAUCUS. Do you foresee any potential—this is sort of a contradiction in terms—unforeseen consequences? I mean, if something might go wrong with the creation of this kind of an instrument in the capital markets, what might it be? That is, what dislocations might occur?

Mr. TALISMAN. We came out with the Qualified Zone Academy bonds in 1997 and we originally came up with a regulation that set the interest rate for the credit. The interest rate that we established was considered to be a below-market interest rate such that the bonds had to be issued at a discount. We subsequently amended our regulations to increase the credit rate.

We understand that those bonds now are trading substantially without a discount and that the interest rate we established by regulations is a market interest rate. I think that is the sort of item that you would have seen had you not already had a program out there, but I think that that issue has pretty much been resolved.

Senator BAUCUS. Have you had a chance to look at the provision I am suggesting with respect to the Partners for Wildlife program? Before I go back to the bonds, is the administration basically comfortable with the approach suggested by Senator Hatch and myself? Do you want to work with us, or is there a significant problem that we should be aware of right now?

Mr. TALISMAN. No. Our proposals are very much on the same order; you already noted the difference in the allocation mechanism. There is also a difference between the treatment of brownfields for a private purpose that we should discuss in the future, but nothing material other than the allocation formula.

Senator BAUCUS. All right.

With respect to the Partners of Wildlife program, as you know, the Fish and Wildlife Service set up this program and gives grants to persons who are working to improve wildlife habitat, et cetera, but they are treated as taxable income to the person receiving these grants, whereas, there are other programs essentially administered by the USDA, Sodbuster, Swampbuster, et cetera, which under 126 of the Code provide that those payments to farmers are not taxable income.

A lot of us believe that that is just basically a glitch because this is administered by Interior, not by USDA, and there really is no substantive difference between the two, so long as they are substantially the same kind of grant, and therefore the Code should be amended to include payments under the Partners of Wildlife program as non-taxable income. Would you agree with that?

Mr. TALISMAN. I share your interest in ensuring that similar payments are treated similarly under the Code. It does not seem to make any sense that the programs administered by Interior are

treated less favorably than programs administered by the Department of Agriculture.

We want to ensure also that Section 126 is working appropriately and ensure that certain safeguards be attached, but again, we share your interest in this issue.

Senator BAUCUS. I appreciate that.

I have a question on the estate tax mileage limitation, which I am certain you are aware of. I have got a chart here which sort of explains the situation. The green areas are areas that are within the 10-mile limitations in order to qualify, but there are a lot of people not in the green areas.

Basically, those are the parts of the country where land values are probably lower than they are in the colored areas because the colored areas are closer to the population centers, which tends to push up real estate values.

My view, frankly, is it does not make any sense to have this 10- or 25-mile limit, under Section 203(1)(c) of the Code. My guess, too, is it is not going to cost very much if that mileage limitation was eliminated, because we are talking about land that is probably a lot lower value on a per acre basis than the areas that are colored. Your thoughts?

Mr. TALISMAN. Well, the mileage limitation was designed to target the incentive to those areas that were under development pressure or near national parks. That targeting, we believe, is important because the tax incentive is designed to provide a conservation easement benefit to those areas that would otherwise be developed or not contributed to the national park.

On the issue of expanding, obviously, you point out on that chart that a fair amount of the country is qualified. We would like to discuss with your staff reasons for expanding it.

But there are other changes, I believe, at least in one of the bills before the Senate, and those changes would influence our decisions with respect to the targeting of this because the conservation easement benefits are already substantial under the Code, in that you can get sometimes more than 100 percent of the value of the easement as a deduction.

Senator BAUCUS. Well, I appreciate that. We do have to work on some solution here, because I think the current provisions are a bit discriminatory.

Mr. TALISMAN. And we did work, and will continue to work, with the Congress with respect to conservation easements, as we did in 1997. Thanks.

Senator BAUCUS. Thank you.

Senator HATCH. Thank you.

Senator Jeffords, then Senator Bryan.

Senator JEFFORDS. I think Senator Hatch may have already asked this question. The bill I have introduced provides the tax credits for dedicated vehicles, the administration bill is limited to hybrid vehicles or electric vehicles.

Do you think our energy policy should include dedicated vehicles as well?

Mr. TALISMAN. Senator, we, again, share the goals that you and Senator Hatch want, of ensuring that we have purchases of vehicles that use alternative fuels and encourage energy efficiency. We

have differences in approaches. As I said to the Chairman, we want to work with you all to develop an approach that would be mutually acceptable, but that would accomplish both our purposes.

In my testimony, which you missed, I articulated a series of criteria by which we judge our climate change package, designed to ensure that we are not providing windfall benefits to technologies that would already be brought to market and to ensure that the item could be administered, but that also encourage our goal of energy efficiency.

In applying those standards to our bill, we developed a different approach than the approach you took, but I would certainly be willing to work with you and your staff in trying to figure an approach that would mesh the two.

Senator JEFFORDS. Thank you.

That is all, Mr. Chairman.

Senator HATCH. Thank you, Senator Jeffords.

Senator Bryan?

Senator BRYAN. Thank you very much, Mr. Chairman.

With respect to the Better America bonds program, the issuer would be the local community or the State that would be involved, is that right? Are they the issuer of the bonds?

Mr. TALISMAN. That is correct.

Senator BRYAN. And in looking at this program, most States have some type of bonded indebtedness limitation fixed in their constitution by statute.

In terms of the practical application, would these bonds impact any statutory or constitutional limitations in terms of the amount of bonded indebtedness? And I ask that question because some States are pretty close to that cap. I think this is a good program, I do not mean to suggest to the contrary, but I am particularly interested in that aspect of it.

Mr. TALISMAN. Senator Bryan, it is our belief that States would, and have, amended their statutes to take into account these new Federal programs. For the Qualified Zone Academy bond program, for example, States have increased their authority to issue those.

We think one of the benefits of the Better America bonds, and also the administration's School Modernization bond proposal is that, as State governments and investors become more familiar with the tax credit bond mechanism, it will be more efficiently used than in the past and necessary changes to legislation will be made.

Senator BRYAN. Mr. Talisman, I am supportive of the concept. I am a co-sponsor. In our State, which is experiencing enormous urbanization pressures both in the Las Vegas area where 6,000 people arrive each month, and in areas in northern Nevada, particularly Douglas County, which is about 50 miles from Reno, which has historically been an agricultural or rural community which is experiencing growth pressures, which is transforming that community from an agricultural to a more urbanized base, that community has been very much interested in protecting its open spaces because, in effect, the character of the community is changing.

But I must say with great respect, you just do not amend the constitution of a State based upon a new program. That is going to involve something, in Nevada, that is a 1 percent limitation. So, maybe we can have a later conversation on that.

The next question I have, is one of the approaches being taken in Nevada is to, in effect, acquire development easements, retaining the private property in private ownership, but in effect compensating the landholder for his, her, or its development rights, keeping the property essentially in a rural setting and compensating the individual property owner for, in effect, giving up the development rights.

Would this bond be available for that purpose? I hope the answer is yes.

Mr. TALISMAN. I believe that it would, but I would like to look at what you are talking about and make sure that it meshes with the language of our statute. I believe that it would.

Senator BRYAN. Let me say, I think we are all on the same page here, Mr. Talisman.

Mr. TALISMAN. Right.

Senator BRYAN. We are all trying to acquire that. But in the west where you have a State like Nevada where 87 percent of the entire geography of the State is owned by the Federal Government, it injects an additional note of controversy when you remove it from the private property tax rolls.

There is a way to solve this problem to accomplish what I think the administration is trying to accomplish, which I am supportive and other members of the committee are trying to accomplish, by simplifying acquiring the development rights. There you have retained the property and private ownership, but you in effect keep the open space which I think is so important for communities.

Let me shift focus to the vehicle portion of this. The new Honda and one other Japanese manufacturer is coming out with an automobile that combines both electric and a small internal combustion engine. Would that vehicle qualify under the provisions of this proposal?

Mr. TALISMAN. The proposal is not currently effective, but yes, that would qualify under the proposal once it became effective. Yes.

Senator BRYAN. Under the new proposal.

Mr. TALISMAN. Yes.

Senator BRYAN. Let me be clear on that. You have got a current program which is, as you have described it, to scale down and phase out by 2005. You want to keep that at that level under this proposal, and I am supportive. Then there is a new credit of $500 to $3,000 for certain hybrid vehicles.

Explain to me whether or not it would be possible for an individual driving an automobile described under the terms of the proposals to qualify for both the old credit and the new credit, or are they mutually exclusive?

Mr. TALISMAN. They are mutually exclusive.

Senator BRYAN. Mutually exclusive.

Can you just, very briefly, and I do not want to take other members of the committee's time, explain what is the difference between the two?

What vehicle qualifies under the old system which we are extending, what kind of vehicles would qualify under the new tax credit?

Mr. TALISMAN. Again, for a vehicle to qualify as a hybrid vehicle it would have to meet certain standards.

Senator BRYAN. Without getting involved in a whole lot of the bureaucratic jargon, can you just kind of, in the idiom of the street, tell us what kind of vehicles would qualify?

Mr. TALISMAN. Well, the current law credit is only for electric and fuel cell vehicles, and that is a 10 percent credit up to $4,000.

Senator BRYAN. Only electric vehicles or vehicles that are powered by a fuel cell.

Mr. TALISMAN. Whereas, the new credit could draw power from other sources, including alternative fuels. Again, this is described in detail in my written testimony on pages 10 and 11. Again, the credit phases up depending on how much of the power is provided from rechargeable energy sources.

Senator BRYAN. So if I am understanding your answer, Mr. Talisman, you are saying that this new Honda vehicle would not qualify under the old credit, but would qualify under the new?

Mr. TALISMAN. That is correct. It would qualify under the hybrid credit.

Senator BRYAN. And you have expressed some flexibility in terms of doing some things that might expand that a bit in terms of making other types of fuel-efficient vehicles qualify for one or both of those credits.

Mr. TALISMAN. That is correct. We are interested in incentives that will improve energy efficiency that are targeted and, again, do not create the windfalls and meet the criteria, so we certainly would be willing to work with the members of the subcommittee and committee to address those issues.

Senator BRYAN. Well, I thank you for your answer. We will certainly hasten to inform the junior colleague of our acting chairman today that he qualifies under this new tax credit proposal. I do not know whether that becomes retroactive to the first of the year; we will talk about that as well.

Senator HATCH. Well, he is certainly proud of his vehicle, is all I can say. He has taken all of us for a ride in it. It is quite a car.

Senator BRYAN. Thank you very much, Mr. Chairman.

Mr. TALISMAN. Thank you.

Senator BRYAN. Thank you, Mr. Talisman.

Senator HATCH. Thank you, Mr. Talisman. We appreciate you taking the time to be with us today. It is good to see you back again.

Mr. TALISMAN. Thank you. Thank you very much.

Senator HATCH. Take care.

We will now hear from our second panel which will discuss tax incentives to create open spaces in urban areas.

I would like to welcome Hon. H. Brent Coles, Mayor of Boise and current chairman of the U.S. Conference of Mayors. We welcome you, Mayor Coles.

We also have Ms. Virginia Gorday, senior vice president for Portman Holdings, LP, representing the Real Estate Round Table; Mr. Sam Staley, director of the Urban Futures Program, at the Reason Public Policy Institute; and Mr. Alan Front, senior vice president for the Trust for Public Land.

I want to welcome each of you here today, and we will begin with you, Mr. Mayor.

STATEMENT OF HON. H. BRENT COLES, MAYOR OF BOISE, IDAHO, CHAIRMAN OF U.S. CONFERENCE OF MAYORS

Mayor COLES. Thank you very much, Mr. Chairman, Senator Baucus, Senator Bryan, Senator Jeffords. I appreciate the opportunity to be here today.

My name is Brent Coles, Mayor of the City of Boise, ID and President of The U.S. Conference of Mayors. I am here speaking on behalf of the mayors of America, strongly supporting the legislation before you.

We in Boise, ID, as many of the western communities, are growing very fast. The free enterprise system works very well. We are very proud of our private property rights.

At the same time, as businesses come into our community, as the technology industries grow, as the industries that we call the new economy businesses who seem to really have a conscience about their community and quality of life, they are asking us to do more and more in our community to preserve the small-town qualities, the open space, air quality, water quality.

Given that emphasis, 50 mayors met in Chicago last Friday to review this type of legislation, and we do come out in strong support of the Community Open Space Bonds Act. We recognize this as a tool, a partner that will help us in achieving the goals of our local communities.

We recognize also the need for continued support for incentives for brownfields in the clean-up and redevelopment of our brownfields that likewise will help us in preserving the greenfields space around our communities.

We support the Commercial Revitalization Tax Credit Act, which likewise will help us in our neighborhoods. We strongly believe that increased rail investment will make a real difference long-term in keeping open space. We call upon the leaders in our Nation's capital to develop a national rail policy which we think will make a major impact in investment in our communities.

As for Senate bill 1558, Mr. Chairman and Senator Baucus, we strongly support that approach. We want to see this tax-related legislation enacted. We recognize that tax-related incentives impact us in our neighborhoods, in our downtowns, and our communities. It impacts our families and our quality of life.

We recognize that we could be very successful in preserving open space and building parks and improving water quality and cleaning up brownfields with this particular piece of legislation. It will make a difference in my home town. It will make a difference for the families in our communities.

We have currently, as we grow and at the speed that we are growing, some local support. We use some impact fees to go out and purchase properties in advance of the development that is occurring, but we simply do not have the tax base to go out and develop and green up those spaces.

I have 240 acres of property, 10 soccer sites, 10-acre locations where we could build ball diamonds, where we could go with our families and throw a frisbee and have picnics, but I do not have the ability to build those parks.

We have done a good job in our community getting out in advance of growth, but we need a partner. The Federal Government would be a great partner for us in this case.

The establishment of a Community Open Space Bonds Board, we think is a great idea. It is a good piece of legislation. It enables local, business, and government officials alike to be involved in the discussion about open space and where these bonds should be used.

We recognize the sensitive land issues. Out west in Boise, ID, much like the communities in which you live, we have wonderful foothills and mountains as a backdrop. That gives us that green space. That gives us that backdrop. That gives us a definition, a boundary. Even though we are growing very rapidly and becoming very big and very large in our eyes, that helps us hold on to that small-town feel.

But, likewise, with our recognition of private property rights, those could be developed very quickly and go away as a beautiful backdrop and wonderful environment for us, unless we have something of a partner. These bonds would give us that partnership and ability to go out and leverage our local funds.

I would like, also, to comment on rail reinvestment in our Nation. We recognize that there are more than 200 rail projects in this country today, and 48 of those are in the top 50 metropolitan areas. We see that as a real plus. They are leading the way. They recognize that rail is important to them.

But in cities like Salt Lake City, Boise, ID, and others, I think that rail would likewise help us slow down the growth in the suburbanized areas, help us in our urban areas, provide us access, preserve open space. Preserving those corridors is very important to us.

We just purchased 18 miles of railroad right-of-way from Union Pacific in Boise, ID. They were going to abandon it and rip out the rails. I had no partner, I had no funds to access. We used property taxes from the good property taxpayers of the City of Boise to buy the rail corridor to begin the process of moving ahead. We continue to need partnerships.

We support the High-Speed Rail Investment Act. We see that as a plus. We see that as a movement. It will provide impetus and momentum in our Nation towards a national rail policy.

It would give us some momentum as we build our commuter rail systems within our communities where we could link to a national rail system and a high-speed system.

Senators Chafee and Jeffords have proposed legislation, Senate bill 2334, now pending before this committee, and likewise, we support that. We believe that will help us in the development of our brownfields. Every city in America has a brownfields, large or small, that could be developed with this kind of support, this kind of partnership.

I thank you very much for the opportunity to provide these remarks. You have my written testimony.

Senator HATCH. Thank you, Mayor. We will put all of the regular statements into the record as though fully delivered. We know we are only giving you 5 minutes each to summarize, but we appreciate having you all here.

[The prepared statement of Mayor Coles appears in the appendix.]

Senator HATCH. Ms. Gorday, we will take your testimony now.

STATEMENT OF VIRGINIA S. GORDAY, SENIOR VICE PRESIDENT FOR PORTMAN HOLDINGS, L.P., REPRESENTING THE REAL ESTATE ROUND TABLE, ATLANTA, GA

Ms. GORDAY. Good morning, Chairman Hatch, Senator Baucus, and members of the subcommittee.

My name is Virginia Gorday and I am senior vice president of Operations for Atlanta-based Portman Holdings. Portman Holdings owns, designs, manages, develops office, retail, residential and hotel properties.

I appreciate the opportunity to testify today on behalf of the Real Estate Round Table and in support of the Community Open Space bonds bill sponsored by Senators Hatch and Baucus.

Why are policies that promote open space and the re-use of previously developed property important to an organization that represents building owners, lenders, and developers?

It is quite simple. Successful real estate projects depend in large part on the health and vitality of the community to which they belong. Open space creation and the productive re-use of existing properties are major components of community health and vitality.

In all communities, new or old, suburban or urban, the existence of attractive, accessible, and usable open space is the keystone of community redevelopment. It promotes a sense of livability that is fundamental to any successful development or redevelopment project.

If an area is not livable, people will not be attracted to it as a place to work, live, shop, or play. Revitalization of central urban areas is a focus of Portman Holdings because its founder, John Portman, believes that the vitality and viability of America's cities is dependent upon their urban core.

This focus is not without risk. In fact, so pressing are these risks and challenges, many developers pass on redevelopment projects and opt instead to develop so-called green fields because they present fewer financial risks and development obstacles.

Not only does the community revitalization suffer as a result, but sprawl is encouraged. Portman Holdings, like several other members of the Real Estate Round Table, has a very proud history of revitalization projects.

Public-private partnerships were involved in many of the most notable Portman projects that include the Embarcadero Center in San Francisco, Renaissance Center in Detroit, Peachtree Center in Atlanta, and an excellent example of a public-private partnership is our own Centennial Olympic Park in Atlanta.

Important features to all these projects were open-space preservation and reclamation, brownfield clean-up, and building of public facilities. The Community Open Space bond will help foster the public-private partnerships needed to make future projects work through the flexible funding source it will provide, particularly at the local level.

Again, Mr. Chairman, on behalf of Portman Holdings and the Real Estate Round Table, I commend you and Senator Baucus for your efforts to enact the Community Open Space bond bill.

This is a good bill that will have positive impacts on not only the creation, preservation, and reclamation of open spaces, but on the redevelopment of communities and the control of sprawl.

In addition to this bill, Mr. Chairman, the Real Estate Round Table urges all members of the committee to enact other Federal policies designed to promote redevelopment, environmental clean-up, and building modernization.

Specifically, we encourage the enactment of S. 2700, which is legislation introduced by Senators Smith, Baucus, Chafee, and Lautenburg, to clarify the potential liability of prospective purchasers of mildly contaminated sites commonly known as brownfields, and to provide more certainty that clean-up decisions made at the State level will be recognized as final determinations under Federal law.

Over 400,000 brownfields exist throughout the country. This legislation has over 50 bipartisan co-sponsors and simply must be enacted if meaningful brownfield reclamation is to be achieved. We particularly thank Senator Baucus for his ardent and critical support of this bill.

S. 2438, legislation introduced by Senator Abraham that would allow the expensing of brownfield clean-up, currently expensing is limited to brownfields located in empowerment zones.

Last year, this committee approved a provision expanding the expensing provision for empowerment zones to any brownfield, wherever located. Unfortunately, it did not get enacted. We urge that enactment this year.

S. 879, legislation introduced by Senators Conrad, Nickles, Baucus, and Robb, and five other committee co-sponsors to allow leasehold improvements to be depreciated over 10 years, a period that more closely matches the economic life rather than 39 years, which is a disincentive to owners to keep the modernization process going on and upgrading tenant spaces.

Also, legislation is needed to allow demolition costs to be depreciated or amortized instead of capitalized and added to the basis of land. This is unfavorable tax treatment and is an impediment to redevelopment.

In conclusion, Portman Holdings and the Real Estate Round Table support the Community Open Space bonds bill because it will effectively promote the creation, preservation, and reclamation of open spaces. Open spaces improve community livability, and the greater the livability of communities, the more positive the impact on real estate in those communities.

Thank you again for this opportunity to testify. The Real Estate Round Table looks forward to working with the committee to preserve, protect, and reclaim our remaining open spaces. Thank you.

Senator HATCH. Thank you, Ms. Gorday.

[The prepared statement of Ms. Gorday appears in the appendix.]

Senator HATCH. Mr. Staley?

STATEMENT OF SAM STALEY, DIRECTOR, URBAN FUTURES PROGRAM, REASON PUBLIC POLICY INSTITUTE, LOS ANGELES, CA

Mr. STALEY. Thank you.

I am going to reorient my oral testimony a little bit based on what I have heard today, mainly because the written testimony stands as a separate statement.

But there are a couple of things that have been brought up in the conversation, as well as the questions, as it relates to land conversation and the Better America bonds that I would just like to raise and what I think are pretty important issues.

One, is that I think we need to be realistic about what land conservation that the Better America bonds or other open-space preservation bills can achieve in the context of land development and sprawl.

At the current levels of funding, I do not think we can expect to have a significant impact on sprawl or land use development because you are simply not going to be able to acquire the kind of land spaces that you need to affect land patterns.

I think, when we think about open-space preservation, while it makes sense to think about it in terms of parks and recreation areas, I think we have to think differently about issues when we are talking about issues of sprawl, which are really driven more by land density and land use patterns.

I will give you a quick illustration of this. What very often happens when we have open space preservation programs that are in place on the local and State level, is they typically go to preserve 200 acres here, 300 acres there, but very often we are talking about land development that occurs over tens of thousands of acres in a metropolitan area.

So when we are talking about congestion, we are talking about what is going to happen with the creation of new communities in managing growth, until we are looking at something on that scale, we are really not talking about having a significant impact. A good example of this is what is already happening in many of the local areas.

As a matter of fact, a recent study that was just produced for the Fannie Mae Foundation that looked at some of these local programs and were talking about land conservation, or preservation, if you will, where the land is permanently being pulled off of the market for future development. We are talking about maybe 1.5 percent, 2 percent, 3 percent, maybe in 4 percent in a region.

In a particular local case, we had a very successful effort in Ohio in a little town called Yellow Springs to preserve 930 acres from development, and it cost them $3 million to do that. It is really an extraordinary case. But in that county where that land preservation took place, there were over 170,000 acres of farmland.

So what is a real potential which I think has to be considered in the context of this program, is that you can encourage leapfrog development. In a sense, if you preserve 300 acres here, you are not preserving the 300 acres next to it, and particularly if it is not contiguous and integrated in an urban greenway. So that is one issue.

The other, is I have serious questions about, while these issues are very important on the local level and is something I have been working with for 3 years—actually, longer, since I have been working in the area of urban policy—it is not clear to me that there is a compelling reason for the Federal Government to become more involved in this, particularly at the State and local level.

Just a quick figure to put this in context. On average in the United States, State Governments have rainy day funds and surpluses that are 9.4 percent of their general revenue budgets.

There is a fair amount of discretionary income or money that could be reallocated at the State and local level to these types of issues if they want, and we are finding that State and local governments are doing it.

It is not clear to me that an increased Federal effort is going to significantly enhance those efforts beyond what is already happening, and also I think it runs the risk of encouraging open space when it is not thoroughly integrated into an open space or strategic plan for the local area. Again, that creates problems as well.

So we see a lot of State and local action on this initiative, but I think because of that interest, that does not necessarily mean that an increased Federal role or presence is necessary.

One of the things that does concern me, and it is something that has been brought up before, is the mechanism by which these funds will be allocated. Personally, I am very skeptical of the Environmental Protection Agency as the appropriate agency to be involved, because they tend to take a very proscriptive approach to land development.

There is a particular view of a city that they think policy should either encourage, which is a mixed-use, relatively high density, which does not fit in most of America. So I think the emphasis should be, to the extent possible, decentralizing and localizing the decision making as much as possible and to also recognize that it is the local communities that are going to know most effectively what kinds of land can be preserved, which is ultimately going to be very strategic parcels.

But again, the emphasis I want to put on this is I do not think we should be characterizing this as an anti-sprawl or a sprawl containment mechanism, because I just do not think that those are the impacts we are going to see, certainly not on the scale we are looking at now.

We really need to be looking at other things on the local level if we really want to affect land use patterns. A lot of these are regulatory, and some of them are federal, like the brownfield liability, which is critical for central city revitalization. But in terms of open space, this impact is going to be very, very small.

Thank you.

Senator HATCH. Thank you, Mr. Staley.

[The prepared statement of Mr. Staley appears in the appendix.]

Senator HATCH. Mr. Front, we will take your testimony.

STATEMENT OF ALAN FRONT, SENIOR VICE PRESIDENT, THE TRUST FOR PUBLIC LAND, WASHINGTON, DC

Mr. FRONT. Thank you, Mr. Chairman.

I am Alan Front, here representing the Trust for Public Land today, known to our friends as TPL, a national, nonprofit land conservation organization that works with local community partners in the public and private sectors to protect landscapes of significance for public use and enjoyment.

From that perspective, I appreciate the opportunity to share again with the committee the Trust for Public Land's strong support, and like at least two of my tablemates, optimistic support for the results that S. 1558, the Community Open Space Bond Act, could bring to those communities.

Because there has been a small parade of witnesses and because I have submitted written testimony, and because I also have for submittal for the record a letter from other groups that are supporting this legislation, I would like to use my time this morning just to make three brief points about the importance of S. 1558 and the Community Open Space bonds that it would authorize.

First, I want to thank you, Mr. Chairman, Senator Baucus, and Senator Roth for your leadership in recognizing the inextricable, indelible links between tax policy and open space protection between public financing and control of sprawl.

I want to thank you and recognize just as much your recognition that when it comes to the sort of Federal partnership dollars that the Community Open Space Bond Act would produce, that little things can, indeed, mean a lot.

I know many Senators have recently returned from Atlanta, where I have been gratified and my organization has been honored to work with Senator Coverdell and other members of the Georgia delegation to benefit from their leadership in the protection of the Chattahoochee River greenway, a long, thin, vital swatch of green space that runs through the very communities that make up the Atlanta metropolitan region.

That greenway vision involving 180 miles of river frontage, involving real estate values and easement and fee acquisition as well as private landowner agreements, amounting to far in excess of $100 million, a program that speaks to many of the same issues that the Community Open Space bond program would speak to, land protection, water quality preservation, redemption of environmentally challenged properties, that program was built on the basis of a vision from the delegation and from Senator Coverdell, your colleague, that seed money from the Federal Government, a bit of Federal support, could actually spark a prairie fire of local investment, investment on the part of local government, State government, and the philanthropic community. That is precisely what has happened in Atlanta.

That model, that underlying philosophy that has been replicated in so many places, Senator Hatch, is what we have been pleased to see happening along the Bonneville Shoreline Trail between Provo and Ogden, it is what we have seen on the Burlington waterfront, it is what we have seen at Lake Tahoe, it is what we have seen in the Upper Swan Valley of Montana.

All of these examples and all of this underlying philosophy is precisely the vision and the philosophy that underlies the Community Open Space bonds program.

Second, I would like to mention, from TPL's working experience, that there has never been a more important time for such a program. According to recent Federal Government figures, 400 acres or so of green space is absorbed or converted every hour, of every day, of every year. That means that an aquifer recharge area or a local park the size of this committee room vanishes, is lost to us, once every second somewhere in America.

Local communities have responded to that challenge and, over the last 3 years, have voted just in referenda to bond themselves to the tune of about $15 billion. But many of those funds, as you know, and as I know is one of the reasons for the Community Open Space bond, are absorbed by the cost of debt service.

There are other communities in other States, including the State of Georgia, which have been unable to pass meaningful funding for open space protection, in part because of the cost of financing. Community Open Space bonds would solve many of those problems.

Last, but not least, I want to mention that the Community Open Space bond program itself and the mechanisms contained within it are the appropriate ways to deal with those problems and to bring just the kind of Federal role that the Trust for Public Land believes at this point is wanting and, hopefully, is imminent.

With enactment of this program, Community Open Space bonds would provide not a regulatory solution, not an invisible hand or a guiding hand, but a helping hand to those communities, bringing resources to those communities in exactly the places that they need it and in exactly the ways that those communities explicitly provide.

The flexibility of this funding source is extremely valuable, as you have heard from Mayor Coles, you have heard from the Real Estate Round Table, as we have heard from all of the community partners that we work with around the country. This is vitally needed and it is just flexible enough, it is just right enough, and this is the time for it.

Thank you very much.

[The prepared statement of Mr. Front appears in the appendix.]

Senator HATCH. Thank you. We thank all four of you.

Mayor Coles, you speak of the importance of having the Federal Government as a partner in managing growth in our Nation's various cities. As we all know, Federal power can take on a life of its own. How do you think we can ensure that the Federal Government does not begin to take over local decision making?

Mayor COLES. Mr. Chairman, thank you for the question and for the opportunity. Within the legislation—and I believe you are one of the authors of this part of that legislation—the Community Open Space Bonds Board, I think, is one protection. That will include local elected officials on that board who will oversee the use of the bonds, the opportunity to use the bonds.

Likewise, local government always has the option to accept or reject the opportunities that the Federal Government extends to us. That is, at a community level we can accept or reject this opportunity.

Once we become a partner, we expect to be an equal partner. Our experience so far is that, when we have met at the table as equals, local government has done very well.

In this case, the example where local government would no doubt be using some of their own leverage, their own property tax base, they are using maybe impact fees. Local businesses participating, the real estate market participating where you have a lot of partners then looking at a piece of open space, a greenway, a green belt, a trail system, I think we have a great opportunity to work closely with the Federal Government and be one of the partners at the table, not be the only partner at the table, where in that case the Federal Government often then is heavy handed. But where there are many partners, we have always done very well.

Senator HATCH. It seems to me, Mayor, that Boise is very similar to many cities in Utah that have been transformed by the emergence of the so-called "new economy."

Yet at the same time, these high-tech businesses are neighbors to our traditional western businesses or livelihoods of mining, ranching, farming, and many other activities that have been around for many years. How can we ensure that we do not lose our unique way of life that is attracting so many to the West while embracing the best of the new economy at the same time?

Mayor COLES. Well, of course, that is the challenge. This piece of legislation helps us do that. Currently under private ownership, we have many farms, ranches, lands, open space contiguous to our city, and we have become used to that piece of property just being there and thinking that it would always be there.

At the same time, in Treasure Valley, we graduate 5,000 young people from high school every year. If we want to maintain the exact quality of life and the same environment that we have today, we have to tell those 5,000 young people, we appreciate the fact you came here and went to high school, but we are not going to develop any more open space, we are not going to allow any more industry, therefore, you must go live somewhere else in America today.

We must be able to develop some land and, at the same time, increase the density of our existing communities. We need to increase the density of our existing communities. We need to be able to develop the brownfields that exist everywhere in America, even in Boise, ID. The opportunity to expense in some of the legislation that is being talked about, that will help us and that will help all of the communities out in the west.

Likewise, this legislation using bonding authority, using the tax base that comes from the industry that is coming to us. The technology industries have a real conscience. They want the quality of life. The reason they come is that quality of life.

So to be able to increase density, to be able to use this kind of leverage to purchase open space and trail systems, to be able to use the open space more equitably, those are the kinds of things that we are doing.

The transit corridors are very important to us. They will also help us preserve our quality of life. We are jamming up our streets, our roads, our freeway system. If we can build rails in America, if we can build that alternative, it can be a great alternative to us and help us maintain our quality of life in America today.

Senator HATCH. Ms. Gorday, in looking at your biography, you have had a lot of experience in dealing with housing and real estate issues.

From your perspective, what is the level of need among our communities for the type of help the Community Open Space bond legislation would provide, and can these needs not be met with traditional tools at the disposal of local entities, such as municipal bonds?

Ms. GORDAY. I think the biggest issue, and the driving issue, is the financing that we as real estate people have to put together with banks and with other various entities, and the length of time it takes to put those together, whether you are looking at municipal bonding or not. Yes, that can work, but does it work, and what are the demands, and what is available, particularly in a State like Georgia or in Atlanta?

We look at the infrastructure expansion, how long can we keep it going, where is it going to go to, can the cities, can the tax base afford to take care of that? Our focus has always been on urban centers and the need for more development and more working of existing spaces.

That, to us, is critical. I think there are various and sundry financing arms out there. They are hard, often, to put together. I see this impact with these types of bonds being very helpful.

As Mayor Coles had mentioned, we have seen our local business community come together with the governmental community to look at different resources and answers. So, it is complex. For real estate developers, we often have the pressure of time. We have to get the deal done.

Senator HATCH. Thanks.

Senator Baucus?

Senator BAUCUS. Thank you, Mr. Chairman.

Ms. Gorday, I am just curious how this is going to help Atlanta. As I understand it, Atlanta's two main problems are water and congestion.

Ms. GORDAY. Amen.

Senator BAUCUS. So how will this help deal with congestion? I do not think we are going to create much water here out of this program, but how will Atlanta deal with this congestion problem and how will these measures that we are talking about, specifically brownfields as well as open space, help?

Ms. GORDAY. What has happened in Atlanta, and what is happening today in Atlanta, and how this could help, is with the development of open spaces. We have the Carter Center with the Presidential Parkway that was slated to be an interstate. It is not an interstate, it is a bike path. It is a greenway.

Centennial Park, which came out of public-private work and development with the Olympics has been a catalyst for redevelopment of really an abandoned area of Atlanta. This was really a brownfields area. Nobody wanted to touch it. Nobody wanted to get near it.

We have seen unbelievable return, people coming back to live in the city. It has changed our tax base. It has also helped, very honestly, with the relationships between different constituency groups.

You do not have just the poor living in the City of Atlanta now. This is bringing up everybody's lifestyle.

Senator BAUCUS. I wish you the best of luck, because I know it is a problem. I know a lot of people are working on it.

Mayor, I wonder if you could address some of the points that Mr. Staley made, namely, the proper role for the Federal Government. He also said that maybe the scale here is not large enough.

Your comments?

Mayor COLES. Thank you, Senator Baucus. I appreciate the opportunity to respond, and I think Mr. Front responded also in his comments, that these are partnerships. Ten acres is not going to do the job. These are not going to preserve the tens of thousands of acres of open space we would like to preserve.

For example, the City of Boise, and I think you could take the Wasatch Front, and you could take Billings, or some other communities around, particularly in the west where you have those fronts, those mountain ranges which have been natural barriers, natural green spaces that are now becoming developable.

As they develop, you look for partners. We talk about real estate and developers becoming a partner. The City of Boise become a partner, State government becomes a partner.

Mr. Staley indicated the surpluses that State governments have. I can tell you that Governors are very stingy with those surpluses, and very, very few of those dollars will come down to cities for greenway and open spaces, but maybe some will.

If some of those dollars come forward, if the Federal Government becomes a partner, the businesses today, the new economy businesses, we call them, have a conscience. They will go out and vote for bond elections. They will put matching funds up. They know, to attract the engineers to work in their businesses, they have got to have good education, good quality of life, et cetera.

So this piece of legislation becomes a leveraging tool. I can go out and do a bond election, which I will do this May, for $10 million. That is not enough to buy what I need along our front, but that $10 million, added to BLM land that is there, added to what I can leverage through this legislation and then through the private partnerships, I can make that thousands of acres.

Senator BAUCUS. I appreciate that. You might have heard me mention this Economic Development Conference I hosted in Montana. I sent two of my staff over to Boise to pick the brains of people in Boise to figure out how you did it.

Mayor COLES. Thank you.

Senator BAUCUS. We wanted to see how you were dealing with all of this, and it gave us a lot of good ideas for our conference.

One thing that came back, just as you mentioned, is the partnerships. Boise State has its own separate, private group that it works with, and lots of other entities like that. It seemed to be something that works and that we took from your good work in Boise.

I am curious, though. You mentioned there is not a huge tax base in Boise. I think you mentioned that, or there is not the revenue in Boise to do some of the things you want to do.

Over in Montana, we cast a little bit of an envious eye at Boise. It has got HP, it has got Micron, Simplot, and some big companies.

I am just a little curious, if there is not more private assistance here in developing something like open space.

Mayor COLES. Thank you, Senator Baucus. The answer to that is, yes, there is a strong property tax base, but the sales tax revenues within our city go to the State, the income tax revenues go to the State, and there is very little sales tax that comes back to us.

So in the City of Boise, we pay our way. All the services that we provide within the community, particularly the public safety, police and fire, and parks and planning, et cetera, are paid for by property taxes. That gives us very little room. You get so high in property taxes, suddenly I am not competing as I would like to because of the high rate of taxes.

So we have one tool that the State legislature has given us called a serial levy, where we can ask for an increase in property taxes for 2 years only. Yet it cannot be very high because it is going to be voted down. Property taxes people love to vote against them.

So I feel I can raise $5 million a year over two years. Well, $10 million is not going to buy that beautiful foothills front that I have up there, but it will provide leverage.

If I do that, if the Federal Government will be a partner, and then these businesses will step forward and say, people that own their single-family homes have been willing to vote yes. Larger businesses will then begin to come forward, some of the trusts will come forward, and then I can buy a large portion of that property.

Senator BAUCUS. How important is brownfields legislation to your work in Boise?

Mayor COLES. Actually, Senator Baucus, in our downtown area where we had the rail yards right in the heart of our downtown, we have done a good job redeveloping so far next to that. But we have a big open space down there where the rail yards have been that we have not been able to attract the investment to clean that up. Brownfields is very important to us.

Senator BAUCUS. Thank you. I appreciate that.

Mr. Chairman, I see my time is up. I would just urge, frankly, all of you to kind of keep talking to members of the Senate to get that brownfields legislation passed.

We have over 57 co-sponsors to that bill, Mr. Chairman, and it is a no-brainer. I mean, communities want this legislation passed to help develop and redevelop downtown areas. It is caught up in the Senate here, for reasons I will not go into at this moment.

But frankly, if we could find a way to kick that loose, we are going to provide a huge benefit to people locally, so they themselves can locally determine their own future and decide for themselves how to develop their own communities. I just urge all of us to do what we can to get that legislation passed.

Senator HATCH. Well, thank you, Senator Baucus.

Senator Bryan, we will turn to you.

Senator BRYAN. Well, thank you very much, Mr. Chairman. An interesting hearing. I thank each of our witnesses for their candid responses.

Mayor, the first question to you. How many local jurisdictions do you think will take advantage of this legislation if it is enacted?

Mayor COLES. The U.S. Conference of Mayors represents over 1,000 cities of 30,000 and more. I think many of those cities, literally hundreds of those cities, would be ready to compete for this bond leverage.

Senator BRYAN. And would you make any suggestions to us in terms of changes to the legislation that would make it easier for you and your other colleagues who represent municipalities to take advantage of?

Mayor COLES. Make the form one page long, two pages at the most. Otherwise, cities have to hire grant writers and many cities cannot. So, make it very simple.

Senator BRYAN. I could not agree more with you.

Mayor, you may know the answer to the question I was asking Mr. Talisman. The concern that I had, is I did not know to what extent, if you choose to avail yourself of this, particularly, to what extent that might impose or impact on any bond limitation provisions that may exist, either under your State constitution or local or State legislative enactments.

Do you happen to know whether that is a concern at all?

Mayor COLES. Thank you, Senator Bryan. I thought about that as you asked the question previously. I can only give my own personal response for my community. Being in a very conservative environment, we have not even bonded 10 percent of our revenues, so we have room for bonding. I am not sure that is in our State constitution or not.

We have just kept bonding at such a limit, paid off our bonds before we went and did the next bond. I think there are many communities in that situation where this would be available to them, where they have been very conservative with their bonding authority.

Senator BRYAN. I am not sure what, if anything, we can do. But in my own State, which has experienced such enormous growth, there have been bond issues for schools, for a whole host of essential services, the effect of which is it has, at least in some areas, have impacted what is left on that cap.

That becomes, again, a competing question of, do you bond to expand local law enforcement and public services, which as a mayor you are very much interested in, I know, or do you bond to provide for additional schools? Those are all, obviously, very important to a community. Or do you pass bonds for expansion of hospital and community health services?

So I would hope in drafting this thing that we do provide some flexibility. I am not sure exactly what the answer is, but that is a concern that I had, and I appreciate your comments.

Mayor COLES. Thank you.

Senator BRYAN. Ms. Gorday, Mr. Staley, Mr. Front, any suggestions to us in terms of the way this language is presented in this legislation that you would suggest that we change so that it might be made more usable?

I appreciate the Mayor's comment, make it a short-form application so we do not generate a new cottage industry here of people who have particular talents or aptitudes to fill out these applications because they are going to be competitive grants.

But any thoughts any of you have in terms of what we might do to improve this legislation, make it more workable?

Senator BRYAN. Mr. Front, you are about ready to respond.

Mr. FRONT. Thank you, sir. Senator, I suggest that many of the changes that folks have suggested have already been incorporated in this program, and so with respect to some of the magnitude issues that have been raised, it seems to be right with respect to some of the limitations as to who can buy and who can participate in the program.

The revisions in the QSAB program have been incorporated into this vehicle. So at least it strikes us that, because of crack draftsmanship to this point, the bill is ready to go, and we appreciate and support it.

Senator BRYAN. Mr. Front, you are satisfied that, as currently drafted, it would enable communities who want to acquire development rights to do so under the provisions?

Mr. FRONT. Yes, sir.

Senator BRYAN. I thank you very much.

Thank you very much, Mr. Chairman.

Senator HATCH. Thank you, Senator Bryan.

Senator Jeffords?

Senator JEFFORDS. Thank you, Mr. Chairman. Being one of the original proponents of brownfields, I am perhaps making more of a statement.

Senator Baucus brought up the problems of urban areas in large rural States. I would like to bring up the problem of urban problems in small rural States. Vermont has a history that left it with a lot of brownfields.

We were, I guess, the machine tool industry of America for many years. In every small community, practically, there was a little plant that had a lot of used oil and everything else that went in, so we are filled with brownfields. Yet, we have hopes that legislation that is passed will not prevent those areas that are plagued with brownfields are not eliminated.

I wondered if you would have any comments as to whether this legislation would seem to fairly treat those of us in these kinds of circumstances. Anyone want to comment?

Mayor COLES. Senator Jeffords, certainly I think this legislation points to the need for us to increase densities within our communities so that we can purchase the green fields around us, and build the greenway and green belt systems around us.

To increase those densities, just as you have indicated, those brownfields must be developed and we must move every piece of legislation that opens up the opportunity for investment in those brownfields. They are great locations. Cities have already invested in the sewer systems and in the streets, and the street lights, and all of that infrastructure is in place around those brownfields.

So when Senator Baucus was referring to, I think, S. 2700, it would likewise be another tool in helping us move forward in development of those brownfields. Some of them are just gas stations on the corner, a great piece of real estate abandoned that could provide great tax base to our community to pay for the other needs and services, but simply cannot be developed because of some of

the restrictive requirements and the costs of cleaning up the waste that is there.

Senator JEFFORDS. Thank you, Mr. Chairman.

Senator HATCH. Thank you.

We want to thank this panel. You have been very helpful to us, and we appreciate you taking time to be with us. Thank you so much.

We will now be pleased to hear from our third panel, which will discuss tax incentives designed to conserve land in rural areas.

Our witnesses for this panel are Mr. Guy Donaldson, president of the Pennsylvania Farm Bureau, who is representing the American Farm Bureau Federation; Ms. Elizabeth Thompson, the legislative director for Environmental Defense; Mr. Austin Cleaves, a dairy farmer from East Montpelier, VT, who is here representing the Nature Conservancy; and Mr. Jerry Townsend, a Montana rancher and vice president of the Montana Land Reliance.

We welcome each of you. We will begin with you, Mr. Donaldson.

Senator BAUCUS. Mr. Chairman, if I might, I would like to just say a word about Mr. Townsend to the panel. He is a rancher from Montana from Highwood.

Highwood is a very unique part of our State. It is what you would expect: the woods are a little bit higher up compared to other parts of our State. He has an operation of 300, close to 400, head of cattle and he is very interested in the local community of Highwood. It is near Great Falls, near Malsner Air Force Base. It is a wonderful, rolling-hills part of Montana.

He is on the board of the Montana Land Reliance, which I think is one of the most successful organizations in the country in this area, namely, working to help ranchers stay alive working with them through the use of easements, credits, and other tools to maintain open space in our country. But he is a real leader, and I am real happy you were able to make the trip, Jerry. Thanks for coming.

Mr. TOWNSEND. Thank you.

Senator HATCH. We are happy to have you here, Mr. Townsend. We will start with you, Mr. Donaldson.

STATEMENT OF GUY F. DONALDSON, PRESIDENT, PENNSYLVANIA FARM BUREAU, REPRESENTING THE AMERICAN FARM BUREAU FEDERATION, CAMP HILL, PA

Mr. DONALDSON. Good morning, Mr. Chairman and members of the committee.

As you have stated, my name is Guy Donaldson, president of the Pennsylvania Farm Bureau. My family and I grow 550 acres of apples, peaches, cherries, and vegetables in Adams County. There is a little town there by the name of Gettysburg that you may have heard of from time to time.

I am pleased to appear before you today to present the views of the American Farm Bureau Federation on several measures dealing with tax incentives and conservation.

First of all, I would like to comment on S. 2344, the Conservation Reserve Program Tax Fairness Act. Most farmers and ranchers are self-employed. Self-employment taxes of 15.3 percent apply to in-

come from labor and employment and are assessed in order to collect for Social Security and Medicare.

The self-employment tax does not ordinarily apply to income from cash rents because cash rental income represents equity value of ownership in the land.

USDA makes the Conservation Reserve Program, or CRP payments, to owners and operators of land who sign a rental agreement and agree to refrain from farming the enrolled property in order to conserve and improve the environmental resources of that land.

In 1966, a tax court ruled that CRP payments were considered rental payments and, therefore, would not be subject to self-employment tax.

But in March of this year, the Sixth Circuit Court reversed the Tax Court's opinion, placing an additional tax burden of 15.3 percent on farmers for their CRP payments and allowing the Internal Revenue Service to retroactively collect the taxes from the last 4 years on farmers participating in CPR.

The Farm Bureau believes that it is unfair to treat active farmers and ranchers differently from other taxpayers when imposing self-employment taxes on rental income.

Because of this particular case, the IRS now singles out farmers and ranchers as landlords liable for self-employment tax. For other taxpayers who receive CRP payments and are not materially participating in a farming operation, the payments are considered to be rental income that is not subject to self-employment tax.

This issue not only has impact on farmers and ranchers, but also on the environment. Self-employment tax on CRP payments may discourage a farmer from further participation in the program.

Environmentally sensitive acreage that has been taken out of production to protect its natural resources may very well be forced back into production if CRP payments are subject to self-employment tax.

Congress should pass legislation to restore equitable tax treatment for farmers and ranchers by making it clear that CRP payments are not subject to self-employment taxes. The Farm Bureau supports S. 2344, introduced by Senators Brownback and Daschle, to clarify that CRP payments are not subject to self-employment taxes.

The second issue I would like to comment briefly on is S. 1392, the Species Conservation Tax Act of 1999. The Farm Bureau supports this bill introduced by Senator Baucus. The bill provides incentives to landowners wishing to take active measures to provide species' habitat.

The Partners for Wildlife program is a popular program with landowners. The funding, often matched by the landowner, provides a means to enhance wildlife on private property. Senator Baucus has recognized the need to exclude from taxable income the funds received for this program.

Landowners, especially farmers and ranchers, gladly bear part of the costs for these projects, and taxing as income the funds that enable them to provide habitat is really a disincentive.

Lastly, I would offer this comment on S. 808, the Conservation Tax Incentive Programs of 1999. The Farm Bureau supports S.

808, which excludes from gross income 50 percent of the gain from the sale of land or an interest in land to an entity intending to put the land in a conservation use. For farmers and ranchers, the sale of capital assets of this type can trigger huge capital gains.

The effect of this legislation will provide further incentives to landowners to consider selling either the land or the development rights to that land for conservation purposes.

I thank you very much for the opportunity to make these comments, and I would welcome questions at a later time.

Senator HATCH. Thank you very much.

[The prepared statement of Mr. Donaldson appears in the appendix.]

Senator HATCH. Ms. Thompson, we will take your testimony.

STATEMENT OF ELIZABETH THOMPSON, LEGISLATIVE DIRECTOR, ENVIRONMENTAL DEFENSE, WASHINGTON, DC

Ms. THOMPSON. Thank you. First, I would like to thank the committee, in particular Senators Hatch and Baucus, for inviting Environmental Defense to speak on this topic.

Endangered species need a tax break, or more correctly, private landowners who provide habitat, or could provide habitat for endangered and rare wildlife, need a tax break.

Let me explain. When most people think of protecting endangered species, they think of protecting remote areas far away from human influence and leaving those areas in a natural state.

Yet, in terms of America's rarest species, such a view is largely a myth. In fact, most rare wildlife in the United States rely heavily on private lands, lands that are often used for ranching, agriculture, timber production, or other uses.

Moreover, most of our endangered species are threatened by habitat loss. Thus, if we are to recover such species, we need to restore and manage privately owned habitat.

Whether it is utilizing prescribed fire to improve grasslands for threatened Utah prairie dogs or restoring coastal prairies for Atwater's prairie chicken, restoring and managing habitat can be quite costly. Yet, nothing in the Endangered Species Act requires any landowner to proactively manage their lands for the benefit of endangered species.

Yes, the Act does prohibit destruction of an occupied habitat, but it does little to reward private landowners who manage their lands so as to improve conditions for endangered species. It is these landowners and the endangered species who depend upon their stewardship who need a tax break.

Many good ideas to reward and encourage conservation through tax changes have been suggested. We urge particular attention to the following three. First, defer that portion of the estate tax subject to a conservation agreement benefitting endangered species.

In 1995, the Keystone Center convened a diverse group to examine incentives for private landowners to conserve endangered species. The first of several unanimous recommendations agreed to was a change in the Federal estate tax.

Although Congress is currently considering other, more sweeping changes in the estate tax, the recommendation of the Keystone

Center report remains sound and remains one that can work with or without other changes in the estate tax.

The recommendation is intended to eliminate the perverse incentive that Federal estate taxes create for destroying endangered species' habitat. Heirs, as you know, can be forced to harvest timber, sell, or subdivide properties in order to pay estate tax. From the perspective of wildlife conservation, this can be devastating.

The Keystone recommendation would give landowners the opportunity to reduce the estate tax burden in return for voluntarily entering into revocable agreements to manage their lands in ways that benefit endangered species.

Second, allow for the deduction from income of expenses incurred in implementing measures to conserve endangered species. As noted above, management measures needed to aid in the conservation of imperiled wildlife are costly, often very costly.

They are, moreover, almost by definition measures that would not be ordinarily undertaken for economic reasons. Otherwise, the species that benefit from them would not be imperiled.

Congress can make it less costly for the landowner who wants to be a good steward and who is willing to do the sorts of things that are not ordinarily done for economic reasons. It can, for example, allow for the deduction from income of costs incurred in implementing measures to conserve endangered species.

The landowner will still bear most of the cost of such measures, but by allowing the deductibility of such expenses some of the costs will be shared with the general public who are the ultimate beneficiaries of such measures.

Finally, exclude cost share payments to landowners under the Partners for Fish and Wildlife program from taxable income. The Partners for Fish and Wildlife program is a small, but important U.S. Fish and Wildlife Service program that provides cost sharing assistance to private landowners for the restoration of wetlands, native prairie, and other wildlife habitats.

To date, over 21,000 landowners have participated voluntarily in the program, restoring more than 464,000 acres of wetlands and more than 447,000 acres of upland habitats.

In 1978, Congress added a provision to the Tax Code, Section 126, that makes a portion of the cost share payments to landowners under a variety of conservation programs eligible for exclusion from taxable income. The Partners for Wildlife program did not yet exist then, and thus it was not among the programs specifically enumerated under Section 126.

Because of the wide support for partners for the Fish and Wildlife program, its low cost, and the fact that payments under other conservation cost share programs can be excluded from income, Section 126 ought to be updated to include the Partners program.

The simplest and best way to do this is to add the Partners program to the list of programs specifically enumerated in Section 126. This recommendation enjoys virtually universal support among both environmental and landowner organizations.

Thank you again for the opportunity to testify before this subcommittee.

Senator HATCH. Well, thank you, Ms. Thompson.

[The prepared statement of Ms. Thompson appears in the appendix.]

Senator HATCH. Mr. Cleaves, we will take your testimony.

STATEMENT OF AUSTIN CLEAVES, DAIRY FARMER FROM EAST MONTPELIER, VT, REPRESENTING THE NATURE CONSERVANCY

Mr. CLEAVES. Thank you, Mr. Chairman, Mr. Baucus. I appreciate the opportunity to speak to you on behalf of the proposal that Mr. Jeffords has made in regards to land gains tax break for people who donate or sell easements.

I want to tell you, I am a dairy farmer. I live in East Montpelier, VT. On my way down here today in the plane, I thought, boy, am I out of my element, big-time. However, when my plane landed, there was no sun and immediately I was put in a line to wait for a cab, and I felt a good deal like one of my cows approaching the milking parlor. We are always in lines, we are always waiting, we are always waiting for gates to open, so I felt pretty much at home after all.

Senator HATCH. Well, you are not the first one to feel that way.

Mr. CLEAVES. I would expect. But I do appreciate all of the effort that you people put in in serving your constituencies from around the country. I know you leave some pretty beautiful areas back home, and I do appreciate that.

I am here on behalf of the Nature Conservancy and also on behalf of myself as a dairy farmer in central Vermont, where I farm approximately 1,400 acres and I maintain a herd of over 700 dairy cows.

I have been a town selectman and a planning commission member, and I have seen firsthand the consequences of a loss of farmland and rampant growth, even in a very rural State like Vermont.

We are just losing farmland and species' habitat faster than we can possibly hold it at bay. Flying down, today in my little turbo prop, or whatever it was, we only flew at 10,000 feet, so you pretty much get a sense of what is going on below you all the way down from where I started from. It is just amazing to see the amount of development and the infringing on open space that is occurring. It is happening everywhere.

I am personally committed to any effort to protect agricultural land in my State. I sold the development rights on my farm back in 1991, and also provided a recreational trail easement which is now part of about a six-mile trail system in our community, which has been done in perpetuity. I think it is a real model for other communities to benefit from.

I think, however, some of the earlier lands that have been conserved were the easier ones. These oftentimes were owned by people who could perhaps donate the rights to that land, and we certainly have appreciated and been the benefactors of that.

However, now I think we are seeing more and more people who would like to sell the development rights, but cannot afford to gift it. The one big issue in many of their minds is, oh boy, I am going to be hit with a major capital gains tax.

I know on my own farm, it has been in my family since 1788. When I took over the farm about 40 years ago, there was not even

a gift tax filed. So to determine my basis on the property, it was kind of a joke. I mean, we had to go back to what were values out there in 1960. That was tough. That is what a lot of people are facing.

They either have owned their land for a long time, and as you know how land values have appreciated, their basis does not amount to a whole lot so the capital gains steps in and really socks you. I think people who just cannot afford to make that gift are hesitant to do so. I think this would be an incentive to get us over that hump.

The Nature Conservancy supports this new tax initiative, and we certainly urge the passage of Senator Jeffords' proposal. I think there are many examples of this from around the country. I cite in my own written testimony a couple in Utah which you might be familiar with, Senator Hatch.

I think the one on a local level, my neighbor, who farms an adjoining farm, saw what I had done with my land and was interested, but was really sweating the capital gains tax that he was going to have to pay.

It took him about 3 years to finally come around to it, and there is another family farm that was passed down through the generations. I know that this would be a very important tool in helping us conserve more land.

Our Governor, Howard Dean, has asked me to convey to you his support for—am I that long-winded? Anyway, I will close by saying we certainly urge your support for this initiative, and hopefully it will be successful. Thank you.

Senator HATCH. Thank you. It is nice to have you here, Mr. Cleaves.

[The prepared statement of Mr. Cleaves appears in the appendix.]

Senator HATCH. Mr. Townsend, we will take your testimony.

STATEMENT OF JERRY TOWNSEND, VICE PRESIDENT, MONTANA LAND RELIANCE, HIGHWOOD, MO

Mr. TOWNSEND. Thank you, Mr. Chairman, distinguished committee members, and members of the staff.

It is a great personal honor for me to appear before you today on my own personal behalf and on that of the Montana Land Reliance, and especially on this most important subject of private lands conservation.

A special thank-you to Senator Baucus for inviting us to be here and a part of this today.

I am a director of the Montana Land Reliance. That is one of my community service functions. My real job is ranching. Or I should say, my paying job. My sometimes paying job is ranching.

I was born and raised in central Montana in the area of the Highwood Mountains, and have returned there in 1974 to buy the cattle ranch from my other family members. We run commercial beef cattle and provide some recreational big game hunting on the ranch.

In 1995, I donated a conservation easement on the ranch to the Montana Land Reliance. Senator Baucus has alluded to the fact that traditional farming and ranching is in trouble in this country.

It is a very important part of our cultural heritage in Montana and it is part of what makes it such a special place.

In the 25 years that I have been back on the ranch, it is estimated that we have lost over three million acres of Montana farm and ranch land to development. Lots of these places have been lost because of the cost price squeeze that goes on between ever lower commodity prices and ever and steadily increasing input costs.

It puts, often, these family ranchers in a position where they just cannot cash flow anymore, and one of the ways out is to sell for development. That is often the route that they choose in order to retire their outstanding debts.

So there are some signs of trouble on the horizon. Just last week, there was a headline that is all too common any more in Montana newspapers talking about a Texas firm buying a Butte, MO ranch.

They plan to make the Sterling Canyon Ranch, according to this release, into a luxury resort, complete with high-end homes. There goes another 1,100 acres.As I say, we see this happening all too often.

Today I would like to visit with you briefly about a policy initiative that Senator Baucus is working on, and we have been working with him on, that we think could have dramatic effect on the current laws regarding conservation easements.

We need to expand the conservation easement tax incentive program to make it beneficial to real, on-the-ground farm and ranch families. In our opinion it is working pretty well now for people with outside income. It does not work very well for people like myself who make their living from the land.

Before I give you an overview of the proposal, allow me to give you a little background on the Land Reliance. It is a private, nonprofit land trust that holds conservation easements only with the State of Montana. It was formed in 1978, and since that time, with the help of some 380 private landowners, we have been able to protect 365,000 acres of Montana from development.

Included in this acreage is some 700 miles of stream and riverfront property, 7,000 acres of wetlands, over 140,000 acres of elk habitat, and just over 142,000 acres in the Greater Yellowstone ecosystem alone, or that area north of the park.

All of this has been done with private conservation easements, typically with farmers and ranchers or those who have bought farms and ranches.

Right now, we see a problem on the horizon. Private landowners are in incredible economic distress and under pressure to develop their land because of these issues that I spoke of earlier.

We are often referred to as land rich and pauper poor. We have the paper assets, but unless you sell the ranch you do not have much for money. So we need to find some additional tools or modify the existing tools to make them work for the real ranchers.

Another problem, is that the average Montana rancher is my age, mid-50's. So from the estate viewpoint and the turnover to subsequent generations, time is certainly of the essence here. We must not delay.

So how do we propose to turn this around? We believe we can amend the current Tax Code in three simple ways. First, we would

propose—and I believe this is the most important—creation of a direct tax credit for the donation of an easement.

Now, under the current system, as most of you know, the credit is towards gross income. It is an adjustment down in gross income, then your tax is applied. The problem is, with on-the-ground farmers and ranchers, we do not have much in the way of net income or gross income. We have tremendous expenses, and oftentimes there is little or no income to be had.

So, while this works pretty well for outside folks who have an outside source of income and it continues to work well for them, it does not work very well for my colleagues, my neighbors, my farm and ranch friends.

The relatively small deduction that they can get under the current system does not equate to the potential income that they have forfeited by the donation of the easement and it really does not justify the value the public has gained from this donation.

I see I am already out of time. I have two other items, if I may continue a moment. Would that be all right?

Senator HATCH. Go ahead.

Mr. TOWNSEND. The second item, is we would like to see the playing field leveled for all types of entities. Right now, the C-type corporations are treated differently than all other businesses. Individual partnerships, limited liability companies, and so on all are able to deduct 30 percent of their gross income after a donation, where C corporations are limited to 10 percent. Now, that has affected me personally because I am a C corporation.

Many of the C corporations in Montana are like myself, one stockholder, sometimes four or five, but they are just a family operation as much as any of the others. We think if we could put them on a level playing field with the other entities, that would be a good thing.

Now, in my case, to give you an example of the inadequacy of the law as it stands, my donated value for my conservation easement was $524,000. In the subsequent 5 years, I have been able to save $1,858 in Federal taxes as a result of giving that away.

So what I did was give up the rights to half a million dollars and, in fact, it cost me about $600 to do it because my appraisal, which is required for the tax write-off, cost me $2,500. So, this is not a real attractant to get people like me to give an easement, and obviously that is not why I did it.

The Reliance knows of about 40,000 acres right now of C corporation ranchers like myself who have told us that the impediment to their donating an easement is this 10 percent factor. So, we need to level that playing field.

The third thing we would like to see, is the elimination of the 25-mile radius from the urban centers or national wild lands. The reason for that, is Montana is such a large State and very rural, that 25-mile exclusion pretty well precludes most people from partaking in that special tax incentive, which has mostly to do with estate taxes.

Now, the other thing it has, it includes a post mortem election which, to me, is the most important part of it. If we can broaden that to include all Montanans, especially the post mortem election part of that, that is, after a principal dies that the heirs, up to one

year, can donate an easement, I think that would have huge consequences on the amount of easement work that we can do in Montana.

We, as ranchers, are notoriously bad planners when it comes to estate planning. I would say that 90 percent of the ranchers that I have spoken with do not even understand that the IRS values their land differently than the county, so often they go to their graves thinking they do not have a problem. But, of course, they do have a problem when the IRS comes in and values it at the highest and best use.

This would give an opportunity for their heirs then to step in, make a donation, and keep this ranch in the family. There would be some ranches that would certainly be kept in the family as a result of it.

The Reliance has done, incidentally, two of these post mortem elections in the last year, even with the 25-mile restriction. So, I think that is very important.

But I would emphasize that the first issue is probably the most important; a direct tax credit, because ranchers just do not have the income to protect that will work under the current system. It is just minuscule, as in the case of my own example.

Thank you very much for the opportunity to speak with you today. I would be happy to answer any questions or anything that you might have.

Senator HATCH. Thank you, Mr. Townsend.

[The prepared statement of Mr. Townsend appears in the appendix.]

Senator HATCH. I will turn to Senator Baucus.

Senator BAUCUS. Thank you very much.

Jerry, that was a very good explanation of the economic bind that a lot of farmers and ranchers are in under current tax law.

Folks want to keep the place in the family, they are roughly your age, getting close to retirement and wondering what in the world they are going to do, and finding that the current laws with respect to easements and donation, whether it is under the Endangered Species Act or a conservation easement, or whether it is estate tax law provisions with respect to deductions, exclusions, just does not help very much and it basically is because there is just no cash. That is, the ranch may be worth something on paper, but the rate of return is usually close to or below zero. It is not making anything, therefore, the current provisions do not make any sense.

Could you maybe just give a little more flavor so people further understand the basic point, namely that there is no income and that a number of farmers and ranchers who do not have outside income cannot take advantage of the current deduction and, therefore, the need for credit. Just add a little more flavor to that so people will get an idea of what I am talking about.

Mr. TOWNSEND. I would be happy to, Senator. Thank you for that, and that opportunity.

It seems, and I have sat here today and listened to some talk about some pretty big money, what we are talking about here with this direct tax credit is not a lot of money, but remember, we are dealing with entities that do not generate a lot of money.

To be honest with you, the reason that people donate ranches, the reason I donated my conservation easement, comes from the heart. It is because we love the land. It is part of us. It is part of who we are, and we want to leave that legacy for future generations.

What we see has happened to this point, what we in the Land Reliance feel, is we have pretty much creamed the crop, so to speak, under the current legislation. People like myself who felt so motivated by it as to protect the land in spite of the fact that it was going to cost me $700 to give away a half a million, have already done it.

Now we are to some people who still—and I emphasize—have it in their heart, they want to protect the land, but they need an incentive, even a small incentive. If they do not pay much in the way of Federal tax, of course, it will be a small incentive. It is a great investment.

It would be a wonderful investment for the government. We can get protection of hundreds of thousands of dollars' worth of land at a very minimal cost, spread over a whole number of years as they generate taxable income. So, the cost-benefit ratio would be incredible with this.

But my main point is, there are so many of my colleagues, my neighbors, my friends who would tip over and go with an easement if they had a little incentive. This direct tax credit would do that, in my opinion.

Senator BAUCUS. I totally agree with you. I mean, in talking to farmers and ranchers, you could not have described it better. It is so important.

I might add, too, it is sort of interesting that the Farm Bureau and the Environmental Defense Fund are sitting next to each other here on the same panel in favor of the same set of proposals, which to me indicates that it is probably a pretty good idea that we go down this road.

Senator HATCH. Which indicates that Democrats ought to spend more time with some of us Republicans.

Senator BAUCUS. Right. [Laughter.] Also, it sort of indicates incentives, in terms of credits or other tax incentives, are probably a pretty good tool to find that common ground between farmers and ranchers on the one hand, and the conservation community on the other.

Mr. Chairman, I just thank the panelists. They have all been just terrific.

Senator HATCH. They sure have.

Senator BAUCUS. Thank you again, Jerry.

Senator HATCH. Thank you, Senator Baucus.

Senator Jeffords?

Senator JEFFORDS. Thank you, Mr. Chairman.

First, I want to express my appreciation for you having this hearing, and also for allowing me to participate.

Second, I want to welcome my good friend Austin Cleaves from East Montpelier, Vermont. Austin is too modest to mention this himself, but Austin was named Vermont's Farmer of the Year in 1989, and he has been a dairy farmer, as he pointed out, for 35 years and operates one of Vermont's largest and best farms. So, he

has a very strong background to really let us know how important this legislation is.

Also, he was going to, I am sure, introduce the letter of the Governor, and I would like to do that for him. I request your permission to submit for the record a letter from Vermont's Governor Howard Dean in support of S. 808, the Conservation Tax Incentives Act.

This bill reduces the amount of income landowners would have to report and pay tax on when they sell their land for conservation purposes.

Under the bill, when a landowner sells land for conservation purposes to a State or local government or to a conservation organization, only one-half gain would be excluded from the income. This would have the effect of reducing by half the capital gains that you would have to pay.

This is a fiscally conservative, market-based approach and one that certainly follows right along with your thinking, I believe.

Austin, how important is this to Vermonters? This is something that the Governor thinks is a great idea. Among the farmers, how important is this?

Mr. CLEAVES. I think it is very important. As I have said, we have had a land conservation effort going on in Vermont for a number of years, as you are well aware, and we have been very successful.

But I think we have done the easy parcels. We have done the ones that tended to be owned by people possibly with other sources of income, or even out of state owners who have really felt committed to donating easements.

Most farmers cannot afford to donate their easements, as the gentleman from Montana mentioned. Your whole life is wrapped up in this piece of real estate that you have worked on all those years, and to just walk away from it, much as your commitment to seeing it continue as undeveloped, even in the same family or available to another family to continue farming, you just cannot afford it. You may have debts that need to be taken care of before you move on, or if you would like to leave a little something, maybe, to your heirs.

I think it is very important, and I think this capital gains thing, we are seeing fly in the face of this more and more.

Senator JEFFORDS. Thank you, Mr. Chairman. I appreciate your holding this hearing very much. We will work with you on trying to get some good legislation out.

Senator HATCH. Thank you, Senator Jeffords.

I want to thank each one of you. Your testimonies have all been just excellent, and we are very appreciative to have the support that we have for these various bills, but especially this one here today.

Senator JEFFORDS. Mr. Chairman, I did want to present and have made a part of the record the Governor's letter.

Senator HATCH. Without objection, we will make Governor Dean's letter a part of the record.

[The letter appears in the appendix.]

Senator HATCH. I want to express my sincere thanks to each and every one of the witnesses today, especially those who have traveled such a long distance to get here. It means a lot to us.

I also wish to thank those who submitted written testimony for the hearing. We will keep the record of the hearing open through Thursday the 27th for additional comments.

Again, I want to express appreciation to Chairman Roth and his staff for their assistance.

Once again, thanks so much for being here, and with that we will adjourn the subcommittee. Thanks so much.

[Whereupon, at 12:08 p.m., the hearing was concluded.]

APPENDIX

Additional Material Submitted for the Record

Prepared Statement of Austin Cleaves

Mr. Chairman and members of the Committee, thank you for the opportunity to present testimony on the critically important issue of tax incentives for land conservation. I am speaking today on behalf of The Nature Conservancy, a private conservation organization that protects the land and water needed to protect the diversity of life on earth. For nearly half a century, the Conservancy has worked with the private sector, using the tools of the market place and the best available scientific information, to conserve the special places that ensure the survival of plant and animal species. To date, it has helped protect more than 11 million acres of land in the United States. The Conservancy's experience working hand-in-hand with landowners like me in diverse communities has led them to seek changes in the federal tax code that would more effectively encourage and reward private conservation actions.

I am here today as a member of the Conservancy to support the federal tax code changes that The Nature Conservancy recommends, and which would provide the most benefit for land conservation. I am a dairy farmer in East Montpelier, Vermont. I farm approximately 1,400 acres throughout central Vermont and I maintain a herd of some 700 dairy cows.

I come before you today as a former town selectman, former member of the town planning commission and former member of the Board of the Vermont Land Trust. I have seen firsthand the consequences of the loss of farmland and rampant growth even in a state as rural as Vermont. I am personally committed to efforts to protect agricultural land in my state, having sold the development rights and a recreational trail easement on my farm in 1991. However, many other landowners are not in the same position that I am, and in my opinion, if we are to succeed in preserving agricultural land and green spaces, we must find new incentives to keep farmers and others on working lands and to protect critical open spaces.

I am here specifically to support Senator Jeffords' proposal (S.808) to reduce the capital gains tax on sales of land and/or conservation easements, which would, from my experience, create a vital new incentive for farmers such as myself, who voluntarily choose to protect their lands. This bill would exclude 50% of any gains realized from private, voluntary sales of land or easements for conservation. Although every farmer's financial situation is unique, I believe that such an incentive would encourage more landowners to consider favorably a conservation option for their land because they would realize a higher return from such a sale after the taxes were paid than if this provision were not in place.

For example, I am aware of a project near Provo, Utah, where The Nature Conservancy is currently working with the owners of Cherry Hill Dairy to protect 170 acres of critical upland and wetland habitat on the shores of Utah Lake. Cherry Hill Dairy has been a well known farming operation and the property has been in the family for over 100 years. The family is eager to protect the land. But the property has a very low basis. Should the family sell an easement for the agreed upon price of $400,000, the capital gains taxes would be steep and has been a barrier to the owners' decision to sell. If Senator Jeffords' bill were enacted, the tax savings on such a sale would persuade the owners to protect the farm permanently.

There is another, larger example in Utah of how this proposal would help landowners. A Davis County family would like to sell to the Conservancy 228 acres of valuable upland and wetland habitat to help raise funds for retirement, family needs, an LDS Mission that they are planning, and to protect agricultural land that has been in the family for generations. The property is located in a fast-growing

area on the shores of the Great Salt Lake and provides critical habitat for thousands of shorebirds and waterfowl. The Nature Conservancy has offered over $3 million but the family has not accepted the offer as yet. They are worried that the tax burden on the sale will be so great that they will not be able to meet their family needs. Again, S. 808 would solve this dilemma for the family.

Finally, Governor Howard Dean has asked me to convey to you his support for Senator Jeffords' bill because it would have critical benefits for state conservation and farmland protection programs. As you may know, Vermont has a long and well-established track record of investing its own funds in farmland and open-space protection. This bill would help state and local governments leverage funds to accomplish even more with our tax dollars.

THE NATURE CONSERVANCY'S CONSERVATION TAX PROPOSALS

S. 808 is the Conservancy's and my top priority conservation tax incentive. As you will see, it is ranked first in the fairly comprehensive set of recommended changes for the committee's consideration below. These proposals are based on input from the Conservancy's field staff who work with landowners on a daily basis and understand the major obstacles to land conservation. The capital gains exclusion proposal reflects the interests of private landowners. This proposal, discussed in more detail below, was introduced in the House and Senate as the Conservation Tax Incentives Act of 1999 and enjoys bipartisan support, including the endorsement of both of the leading major party presidential candidates.

We also support the proposal of Chairman Hatch and Senator Baucus to create a new open space bond program and Senator Baucus' endangered species conservation bill.

The Conservation Problem: Preserving Quality of Life

Healthy communities are made up of complex systems of forests, wetlands, deserts, productive soils, rivers and other interdependent resources. The cumulative effect of seemingly unrelated activities such as deforestation, the paving over of agricultural land, the filling in of wetlands and urban sprawl has been to fragment the landscape and strain the fabric of wild and human habitat. The sustainability and quality of life in every region of the country is in danger. The rate of the development of land exceeds by far both the rate of population growth and the rate of open space conservation.

The Landowner's Problem: Safeguarding Financial and Environmental Assets

Federal and state environmental protection laws and regulations such as the Endangered Species Act, the Clean Water and Clean Air Acts, are important tools to help preserve the environmental quality of land, but they can place economic and regulatory burdens on individual landowners. Government cannot, and should not, have the sole responsibility for maintaining and preserving the public benefit of open spaces. If conservation efforts are to succeed, private landowners must be active and willing participants. In the United States, approximately 70% of the land is privately owned. Well over half of all imperiled species are found on private land, and many exclusively so. The species found on private lands are declining more rapidly than are those on publicly held lands.

Landowners have a stake in the quality of their community's environment. They also have a right to realize economic benefits of their investment in land. Tax incentives for conservation provide a mechanism for meeting both of these interests.

Solution: Tax Incentives

Two kinds of tax incentives for conservation currently exist in the federal tax code. One provides an income tax deduction for charitable contributions of partial interest in land for conservation purposes; the other provides an estate tax exclusion for gifts of conservation easements in certain geographic areas. These benefits can make it possible for landowners to meet both conservation and financial goals if they have an income sufficient to utilize the tax deduction. But there are many landowners with income too low, or land so valuable, that these provisions are not financially beneficial. For example, for many farmers near metropolitan areas the fair market value of their land is a primary financial asset that cannot be relinquished. Market conditions can mean that the sale of the land for development is the only viable choice in order to realize a full economic return.

Existing conservation tax incentives are important but, given the rate at which land is disappearing and species are lost, they are not sufficient. New tax incentives are needed to encourage the protection of additional private lands. To address this need, The Nature Conservancy supports a range of conservation tax incentives that fall into three general categories:

1. Incentives to encourage the sale, gift or exchange of land or easements for conservation;
2. Incentives to encourage private land to be managed for conservation benefits; and
3. Incentives to prevent the break-up of large land-holdings.

Within each of these categories, we have proposed specific tax changes that will provide benefits to both landowners and conservation. They are as follows:

(1) Incentives to Encourage the Sale, Gift or Exchange of Land or Easements for Conservation

(a) Capital Gains Reduction for Conservation Sales. This proposal, which would be implemented by S. 808, would reduce the amount of capital gains tax if land is sold for conservation purposes, thereby providing a landowner with a more attractive financial return from such sales.

S 808, sponsored by Senator James Jeffords, is The Nature Conservancy's top priority.

I would like to congratulate Senator Jeffords for his leadership on this issue. His legislation is a fiscally conservative, market-based approach to land conservation. It achieves environmental objectives without imposing new land use regulations. The provision is strictly voluntary, administratively simple, and uses definitions and tests for conservation purposes that are already contained in the tax code. It provides capital gains tax relief for sales of land for conservation to government agencies or qualified conservation nonprofits. The bill would allow landowners to preserve permanently their property's environmental value without foregoing its financial value. It would exclude 50% of any gain realized from private, voluntary sales of land or interests in land for conservation. The land must be used to protect fish, wildlife or plant habitat or open space for agriculture, outdoor recreation or scenic beauty.

Senator Jeffords' bill also helps state and local governments leverage funds and accomplish more with their tax dollars. Estimates indicate that, for every dollar of lost revenue from this tax provision, almost two dollars worth of land would be protected. Sales of land to state and local governments for conservation would qualify, in addition to such sales to federal agencies and conservation nonprofit organizations. Citizens who vote to increase their taxes to fund bonds for land conservation will benefit because the funds raised will go farther toward reaching the community's conservation goals.

(b) Increase the Value of Gifts of Land or Easements Made for Conservation. This proposal would change the individual and corporate charitable giving laws to make the tax value of conservation gifts more valuable, particularly for the "cash poor-land rich" landowner.

Senator Baucus' legislation, S. 1392, would promote this objective by increasing from 30% to 50% the amount of the taxpayer's adjusted gross income that could be offset by a threatened or endangered species conservation easement donation, and by allowing the unused deduction to be carried forward for twenty years. The Conservancy strongly supports this legislation as a critical new conservation incentive.

(c) Enable Conservation Transactions to Qualify for Low-Cost Financing. This provision would allow conservation organizations to qualify for tax-exempt financing or to issue tax-exempt installment obligations to a seller when purchasing land.

The Community Forestry and Agriculture Conservation Act of 1999 (S. 1085), sponsored by Senator Murray, would create a targeted version of this incentive. It would allow tax-exempt financing of working timber and agricultural lands by nonprofits, requiring permanent conservation easements to ensure sustainable use of the land. The Nature Conservancy endorses this proposal, and commends Senator Murray for her leadership in this legislation.

We recommend broadening the legislation with a slight modification so that it would apply not only to the acquisition of working lands, but also to the acquisition of other conservation lands. We would like to see this type of tax-exempt financing used for any conservation land acquisition made by qualified land trusts and conservation organizations. This change could be accomplished with small additions to S. 1085. The Conservancy would be happy to work with Senator Murray to develop such language.

(d) Encourage Private Capital to Make Investments in Conservation Land. The basic idea is to create incentives (greater deductions, tax credits or loan guarantees) for private, third party financing for conservation or open space transactions. For example, we believe that S.1558, The Community Open Space Bonds Act of 1999, would be an excellent vehicle to encourage private investment in environmental infrastructure projects, including open space acquisition, by providing a Federal tax credit on the debt service on state and local government bond obligations issued for

such purposes. We commend Senators Hatch and Baucus for their leadership in introducing and sponsoring this proposal.

(e) Change Corporate Liquidation Rules Where Conservation Lands are Involved. This proposal would allow small corporations whose primary asset is land to donate such land for conservation purposes without triggering a tax, as is the case under current law.

(f) Revise the Rules for Land Exchanges Where Conservation Lands are Involved. This revision would lengthen the time for qualifying exchanges and/or broaden the types of property that could qualify for treatment as a like-kind exchange involving conservation lands

(2) Incentives to Encourage Management of Private Land for Conservation

(a) Make Conservation Management Expenses More Valuable for Private Landowners. Provide tax credits for habitat management expenses such as prescribed burns, exotic species removal, riparian and habitat restoration. Again, the Conservancy applauds Senator Baucus for his leadership in introducing S. 1392 which would encourage private land to be managed for endangered species protection by providing a landowner with an estate tax deferral for such time as the land is subject to an endangered species conservation agreement.

(b) Provide Habitat Conservation and Management Insurance. Create a subsidized insurance program whereby landowners who agreed to manage land in furtherance of a conservation plan would be held harmless (using the insurance proceeds) from the potential loss in value of their land from implementation activities under the plan.

(c) Make Private Ownership of Conservation Land Affordable. Make property taxes paid on land subject to conservation easements eligible for treatment as a tax credit.

(3) Incentives to Prevent the Break-Up of Large Land-Holdings

(a) Provide Estate Tax Relief for Conservation Landowners and their Estates. Extend the geographic application and financial benefits of recent estate tax changes to encourage conservation. Allow estates with conservation lands to donate a conservation easement and use the value of such an easement to offset the estate tax that would otherwise be due.

The American Farm and Ranch Protection Act, now section 2031(c) of the federal tax code, passed in 1997 and was expanded in 1998. This legislation was the first new tax incentive for conservation since the enactment of the conservation easement donation incentive in 1976, and it has the potential to save a great deal of land that would otherwise have been subdivided and sold for development in order to pay estate taxes. We support efforts such as that included in Senator Baucus' legislation to perfect and strengthen 2031(c) so that it can realize this potential.

First, we have estimated that approximately one third of the continental U.S. is currently not covered by the statute. The current boundaries omit critically important areas with national natural resources. For example, National Wildlife Refuges, BLM designated lands of critical environmental concern, Wild and Scenic River designated areas, and other categories of Federal resource lands are excluded by the geographic restrictions. There is no clear rationale for omitting these lands from those included in the Act. In addition, land in or near state and local protected areas are not included even though they may be under severe pressures.

The land that is excluded from coverage under the Act is likely to have, on average, low fair market values because it is located in predominately rural areas. Therefore, the marginal cost of including such land under the statute should be small. This small cost to the public is greatly outweighed by the land conservation benefits to be derived.

Finally, the American Farm and Ranch Protection Act's effectiveness would be substantially improved if the financial limitations on its use were removed. With the caps in place, the provision has a limited ability to serve as a conservation incentive on large landholdings that may have values inflated by nearby development. These are the very resources that the original legislation intended to reach.

(b) Provide Incentives Against Habitat Fragmentation Actions. Create incentives to prevent open land from being converted or fragmented; reward landowners who refrain from habitat fragmentation causing actions and seek to remove existing incentives in the tax code that encourage landowners to subdivide and fragment their lands.

CONCLUSION

Land conservation is a growing national need. Private landowners hold the future of biodiversity in their hands. The tax incentives the Conservancy recommends

would provide interested landowners with the tools to conserve their land and contribute to the public interest in the preservation of the diversity of life.

We appreciate the leadership of Senators Jeffords, Hatch and Baucus and encourage the Committee and other members of Congress to support the innovative, voluntary tax proposals that we are discussing today.

The Conservancy is eager to work with the Chairman and other members of this committee in support of new tax incentives for conservation. Thank you for the opportunity to present testimony before you today.

PREPARED STATEMENT OF HON. H. BRENT COLES

Good morning. I am Brent Coles, Mayor of Boise, Idaho and The President of The United States Conference of Mayors.

I am pleased to appear before you today to share the perspectives of the nation's mayors on the importance of open space and how this Committee can support local efforts in this regard through federal policy actions, specifically changes to the Tax Code.

OVERVIEW OF BOISE AREA

Let me begin my remarks with a brief discussion of some of the many challenges before my city and region. Boise is Idaho's largest city and capital. The Boise region is the hub of our state's economy.

The City of Boise and its region is a fast growing and rapidly urbanizing area of the West. And, we are among the leading regions in high technology, placing us at the forefront of issues in meeting the challenges of the nation's "new economy."

Our area's manageable size and our citizens' strong connections to the natural beauty of our area make us keenly aware of the issues before this Committee today. As mayor, I can assure you that our citizens want the mayor and their other representatives to make smarter decisions on urban development. And foremost among them is a call to action on open space preservation, while simultaneously sustaining our economic progress. Our residents expect us to secure a future where the natural amenities that make our area such a special place to live are preserved. And, we have a strong and growing private sector, particularly those considered new economy businesses, that share this view.

Our experience in the Boise area is similar to what you will find in most areas of the country. Like our citizens, our new economy business leaders have consistent and forceful views on what they expect from the communities where they locate and conduct business. These businesses are placing increased value on our livability or those community amenities that make places unique and desirable.

They want communities and regions that can guarantee a higher quality of life for their employees, with the critical assets in place that anchor a modern economy. This means local commitments to sensible urban development patterns, rising workforce skills and the education capacities to make this happen, modern transportation and other infrastructures to link their local areas to the world and better serve their workers at home, and improving livability in their community.

In the Boise area, we have been fortunate that we are positioned to deliver on these demands. As a result, we have had great success recently in making our area a desirable location for new economy businesses.

Let me cite some data to support these claims. At the Conference of Mayors and in partnership with the National Association of Counties, we have been studying the emergence of the nation's city/county metropolitan areas, tracking their dominance in supporting U.S. economic growth.

In a new report released last month on the high-tech economy, we documented that the new economy is largely concentrated in the nation's 319 city/county metropolitan areas. It showed that the Boise area is among the nation's fastest-growing, high-tech economies, posting an annual growth rate of more than 18 percent growth from 1998–1999, placing it in the top 10 areas of the nation. And, we also reported on high-tech shares of each metropolitan area's output (or what is called 'gross metropolitan product' or GMP). Again, the Boise region ranked in the top ten in the nation in terms of the high-tech share of our GMP.

So as I appear today, I can personally testify to my local experiences that have a strong connection to the future direction of the national economy. As such, Mr. Chairman, I want to emphasize how important it is to have a federal partner, with the policies in place that complements local efforts, particularly as we try to meet the rapidly changing demands of our new economy.

As we go forward in the Boise area, I believe that our future economic success hinges on a handful of key strategic decisions we are now making, as our region

dramatically transitions to a larger population and rising economic output. Among these are the decisions we make on regional economic development and how we manage and preserve our open space and land resources.

In short, we must reconcile how we sustain our growth and increase our prosperity, without degrading our unique and defining assets, like our very dramatic and natural open space, that so often underlies individual and businesses decisions to make the Boise area home.

CONFERENCE OF MAYORS' AGENDA

As President of the Conference of Mayors, a position I assumed last month from Denver Mayor Wellington E. Webb, I have been given the opportunity to set the agenda for the nation's mayors. I have already set forth an agenda that builds upon the work of Mayor Webb, with a particular focus on transitioning communities to the new economy.

This agenda will concentrate on policies to better deploy technology in our schools, in our workforce and in the many services cities deliver. It calls for actions that support local areas in their efforts to grow smarter, including preserving open space and increasing investment in parks. It emphasizes infrastructure investment, such as airport enhancements and reinvigorating rail services to improve the movement of people and goods within and among our nation's regional economies.

Mr. Chairman, we believe that the Tax Code can be a powerful ally in helping local areas move this agenda forward. This morning I focus my remarks on some pending tax proposals that mayors believe can further local efforts to preserve open space, including initiatives that will help local areas shape future urban development. Such measures will help us slow down or reduce pressures on open spaces, particularly within or in proximity to our metropolitan areas where these land resources are particularly at risk.

INITIATIVES/INCENTIVES ON OPEN SPACE

We have identified a number of federal tax initiatives that we believe will assist local effort to preserve open space. First, we support proposals, such as the "Community Open Space Bonds Act of 1999" (S. 1558), that directly supports local areas and their efforts to preserve and protect open space in their communities and regions.

We have also placed a high priority on incentives to stimulate private sector investment in brownfields cleanup and redevelopment, helping local areas reshape regional development patterns and overall reduce our appetite for greenfields as locations for new development.

We have also called for tax incentives to reinforce the assets of existing communities, by tapping the considerable value of infrastructures now in place and encouraging reinvestment in existing neighborhoods and communities.

Finally, we have consistently advocated for increased investment to expand our nation's rail capacities, both inter-city and local/regional rail systems. In the Washington, DC area, you can see powerful examples of how this investment can shape urban development, such as Metro's Orange Line in Arlington, Virginia.

COMMUNITY OPEN SPACE BONDS

Let me first begin by expressing our support for initiatives patterned after the Administration's "Better America Bonds" proposal that support local efforts to preserve open space and support park development, brownfields cleanup and water quality improvements. I want to commend you, Mr. Chairman, and Ranking Member Baucus, for your leadership in sponsoring the "Community Open Space Bonds Act of 1999" (S. 1558) to help communities address these priority needs.

At the Conference's Annual Meeting last year, the nation's mayors adopted a separate policy statement expressing our strong support for this approach, calling specifically for action during the 106th Congress when and if tax-related legislation moves forward.

Mr. Chairman, we urge you to include S. 1558 in any tax-related legislation which is likely to advance through the process in the closing weeks of this Congress. We have vetted this proposal with the mayors on several occasions, and we believe that the bond structure you have developed will be responsive to communities throughout the country. And, we believe it will enhance local efforts to preserve open space, build parks, improve water quality and cleanup brownfields.

What is particularly appealing about this approach is that it supports many pressing needs in our communities, at a relatively modest federal cost. Many communities are growing too quickly to have either the capacity or resources available at this time for investment in open space preservation, as they race to keep up with

pressing demands for basic services. And, of course, when they finally have the local resources to address what we call the "stewardship" issues, like open space preservation, land costs have risen dramatically and development patterns have limited their options.

Conversely, for other communities saddled with slow growth or declining industrial, commercial or housing bases, having access to these resources can really make a difference in tackling brownfields. The program would help them right now in making a more substantial investment in their future. And, we know that these communities, given their economic circumstances, can't generate a sufficiently larger pool of capital locally to accelerate their brownfield cleanup efforts so as to reinvigorate their tax base over the longer term.

There are many other examples of how making resources available today can make a big difference down the road. Speaking of roads, this is not a new idea. For example, the Federal Highway Administration used to provide below market interest loans for advance right-of-way acquisition for future road projects as a method of reducing future highway project costs.

We also believe that modifications you have made to earlier proposals will also improve the allocation of these resources through the establishment of the Community Open Space Bonds Board and other provisions that will help to ensure a balanced distribution of these resources. We believe that the Board and its inclusion of non-federal participants will help ensure a more responsive approach to meeting our local needs with these resources.

Mr. Chairman, I would like to ask you to consider making right-of-way acquisitions to support future rail investments one of the eligible activities under S. 1558. In Boise, we recently acquired a right-of-way from Union Pacific that we plan to use to anchor our future commuter rail system for the region. Through my work with local officials in my area, what is called the Treasure Valley Partnership, we are already making plans to funnel future commercial and residential development along this rail corridor. In the long run, the success of this effort will make a very powerful contribution to our region's long-term effort to grow smarter. We believe this is one of the most important actions we can take to lessen the pressure on open space in our region. Helping communities make these strategic investments early on in the process is very consistent with the intent of your legislation.

At last count, there are more than 200 such rail projects under development in virtually every part of this country. In fact, of the nation's top 50 metropolitan areas, 48 of them are now planning, engineering or constructing either a "new rail start" or adding to an existing rail system. Rail projects in just these 48 regions will serve more than 40 percent of the nation's population. Supporting these efforts in the early stages with resources for right-of-way acquisitions will save millions of dollars in future costs associated with these projects.

A couple of recent experiences have really impressed me on this issue. Earlier this month, I was in Charlotte to tour their plans for a new rail system and its relationship to future development in that region. Already, developers are constructing or in the process of constructing thousands of housing units in the downtown area of the city, with developers anticipating the region's investment in rail and other fixed guideway facilities in the region. In Dallas, following the introduction of light rail services in that community, there are nearly 14,000 housing units that are being constructed or planned within one mile of the downtown core over the past 18 months. This is equivalent to constructing a small city, without consuming any additional open space.

Mr. Chairman, I know that you are quite familiar with these issues, given your experience with the Salt Lake City's light rail project. These examples and others throughout the country underscore why I have made increased commitment to rail services, both intercity and intracity, a top item on my agenda. The Conference would be pleased to work with you to provide specific recommendations on how your legislation could help further early acquisition of rights-of-way for these rail projects.

As mayors, we consistently called for new partnerships with the federal government that don't tell us what to do, but help us do what our communities need and citizens want. S. 1558 is an excellent example of this type of partnership, and we would urge you to move forward and seek its enactment.

Mr. Chairman, since I have indicated our strong interest in the need for increased investment in rail services, I also wanted to discussed our support for another tax proposal, the High Speed Rail Investment Act (S. 1900), that is also pending before this Committee. Last week, I convened more than 50 mayors in Chicago for a leadership meeting on my agenda. Among the issues that we discussed was the need for this Congress to move forward with S. 1900 to help solidify the emerging and

broad-based efforts among the states for the development of high-speed rail corridors and services.

This fall Amtrak will introduce the Acela service on the Northeast Corridor, ushering in a 21st Century transportation system for America. As you know, the Acela train sets are the first high speed trains to be constructed and operated in North America. This revolution in intercity passenger train services has stimulated an incredible response among the states and communities, many of which are now seeking high speed rail services for their own regions. For mayors, we know that these systems will further anchor existing places as destinations for business investment and residential development, furthering our efforts to reduce outward pressures on open spaces.

Among the priority recommendations from this leadership session was a call upon Congress to enact S. 1900 during this Congress. Already, about half of the Senate is cosponsoring this legislation, which is largely patterned after your Community Open Space Bonds proposal. I raise this issue specifically in the context of our discussion this morning because of the strong connection between expanded passenger rail capacities and open space preservation. Mr. Chairman and Members of this Committee, I want to convey the mayors' strong support for S. 1900 and to urge your action on this priority legislation.

BROWNFIELDS/URBAN REINVESTMENT

Mr. Chairman, the mayors continue to assert that tax incentives are needed further the success they are having in attracting reinvestment in their cities. I wanted to note our support for several pending proposals before this Committee that will further reivestment in cities and challenged neighborhoods.

Among the biggest obstacles in urban development is the preponderance of brownfield sites that too often sit idle and underutilized, awaiting developers and other private sector interest to bring these sites back to productive use.

Last month, the Conference's membership adopted a policy statement urging the Congress to renew and expand the coverage of current law provisions that now only allow developers in certain targeted areas to "expense" their cleanup costs. Specifically, our policy calls upon Congress to simply eliminate the targeting provision, making expensing eligible at any brownfield property. If this broader eligibility can't be accomplished, the policy recommends expensing for areas defined as 'urbanized areas' as Senators Chafee and Jeffords have proposed in the legislation (S. 2334) now pending before this Committee.

Mr. Chairman, as you consider ways to move forward on tax incentives for open space preservation, we would also urge you to consider this proposal, given the vast potential of brownfield redevelopment to contribute substantially to the preservation of open space in virtually every part of the nation.

Mr. Chairman, among the other pending proposals that are applicable to this discussion, the Conference also urges support for tax credits to assist distressed communities that have not benefited from the strong growth of our nation's economy. Although our nation has experienced enormous economic growth over the last nine years, there are many rural and urban areas where unemployment remains exceptionally high, and where new job opportunities and business growth remains stagnant. In many instances, these areas are plagued by increasing numbers of brownfields that need to be cleaned up and restored to active use and abandoned homes and commercial buildings that need to be rehabilitated to promote occupancy and extend the life of these structures.

To address these concerns, the Conference is urging support for Commercial Revitalization Tax Credits, legislation sponsored by Senator Kay Bailey Hutchison. This proposal will provide tax credits to businesses to help defray the cost of construction, expansion and renovation in an estimated 1000 economically distressed communities.

The Conference is also urging support for the Administration's New Markets Tax Credits initiatives, which will provide numerous tax incentives to spur job growth and economic development in poor neighborhoods. Among these initiatives, tax credits would be provided to community development banks and similar institutions so they could generate venture capital that could be used to provide loans to business to revitalize poor neighborhoods.

CLOSING REMARKS

Mr. Chairman and Members of the Committee, I want to thank you for this opportunity to share our views on these important issues.

I would like to underscore the commitment of the mayors to support your efforts to move forward with legislation in this area. As President of the Conference of

Mayors, I can assure you that the nation's mayors will strongly support your efforts in this regard.

HOWARD DEAN, M.D.
Governor

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July 24, 2000

Senator Orrin G. Hatch
Chair, Subcommittee on Taxation and IRS Oversight
Committee on Finance
US Senate
Washington, DC 20510

Dear Senator Hatch,

Thank you for giving me this opportunity to submit testimony supporting S. 808, an act to amend the Internal Revenue Code of 1986 to provide tax incentives for land sales for conservation purposes.

Conserving open space, working farms and working forests continues to be one of my top priorities as Governor. Since 1991, the state has directly conserved, either through fee purchase or conservation easement, over 200,000 acres of forestland, wilderness and open spaces. Working with federal and private partners, Vermont has conserved such cherished lands as the Long Trail traversing the state and the 133,000 acres of the former Champion Lands in Vermont's Northeast Kingdom. Also since 1991, we have conserved 200 farms, or approximately 68,000 acres of farmland. For the farm conservation alone, the state has invested over $20 million. This is an investment in an essential segment of Vermont's economy and the backbone of Vermont's heritage and character. By conserving land through conservation easements we do not only protect irreplaceable natural resources and traditional settlement patterns and ways of life. The conservation of land through the use of working forest and working farm conservation easements has many additional public benefits.

The benefits flowing from a state's commitment to land conservation reach far and wide – they are not limited to the citizens of a particular state. Vermont today is within a five-hour drive of 65,000,000 people. Many of these neighbors benefit from the recreation opportunities presented by Vermont's rural nature. Conservation of the resource is therefore of national significance.

Senator Orrin G. Hatch
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The benefits of this conservation is also important to the nation's environment and economy. Management practices written into easements protect the nation's waters from non-point source pollution. Erosion controls, timber harvesting practices and buffer zones along rivers and other waterways help maintain the environment while at the same time encouraging private investment in land. Well designed conservation easements also ensure the growth of high quality timber to support a domestic value added woods product industry and a diversified, locally based agricultural community. The sale of conservation easements frees up capital to invest in the economy. Land conservation, in addition to keeping rural lands working lands, also prevents sprawl and focuses development into existing communities, promoting revitalization of downtowns and less need to drive from store to store or business to business. This effort to keep settlement patterns compact generates less air pollution from mobile sources, thereby helping to maintain the nation's air quality.

Many states, like Vermont, spend stand funds for land acquisition and the purchase of conservation easements. The federal government is a good partner in these efforts. Creative approaches such as the one offered by S.808 are greatly appreciated by states attempting to protect their heritage, economy and environment through conservation. Senate bill 808 provides a simple mechanism to stretch precious dollars thereby allowing states to conserve more acreage for the same amount of money. This proposal creates a new conservation tool that is simple, voluntary and uses mechanisms and terms already existing in the tax code. It provides an encouragement to "land rich, cash poor" landowners for whom tax incentives for donations and other tax benefits may not be practical.

In closing, I want to thank you and your colleagues for giving me the opportunity to express my strong support of this bill. I encourage the Senate to approve this measure and thereby contribute to the preservation of this nation's great open spaces, woodlands and farms.

Sincerely,

Howard Dean, M.D.
Governor

HD/dmr

PREPARED STATEMENT OF GUY F. DONALDSON

Good morning, Mr. Chairman and members of the committee. I am Guy Donaldson, President of the Pennsylvania Farm Bureau. My family and I farm 550 acres of apples, peaches, cherries and vegetables in Adams County, Pennsylvania. We also operate a farm market during the summer months. I am appearing before you today on behalf of the American Farm Bureau Federation, which represents more than 4.9 million member families in every state and Puerto Rico, to discuss various measures dealing with tax incentives and conservation.

S. 2344—CONSERVATION RESERVE PROGRAM TAX FAIRNESS ACT

Most farmers and ranchers are self-employed. Currently they pay a self-employment tax at the rate of 15.3 percent. Self-employment taxes apply to income from labor and employment and are assessed in order to collect for Social Security and Medicare. The self-employment tax does not ordinarily apply to income from cash rents, because cash rental income represents the equity value of ownership in land.

The U. S. Department of Agriculture (USDA) makes Conservation Reserve Program (CRP) payments to owners and operators of land who sign a rental agreement and agree to refrain from farming the enrolled property in order to conserve and improve the environmental resources of that land. CRP covers over 34 million acres of environmentally sensitive land. An estimated 270,000 farm families have enrolled land in CRP. USDA makes about $1.8 billion in CRP payments annually, an average of $5,000 per farm and $45.15 per acre.

In 1996 the Tax Court case, Wuebker vs. Commissioner, ruled that CRP payments were considered rental payments and therefore would not be subject to the self-employment tax. But in March 2000, the Sixth Circuit Court of Appeals reversed the Tax Court's opinion, placing an additional tax burden of 15.3 percent on farmers for their CRP payments and allowing the Internal Revenue Service to retroactively collect these taxes from the last four years on farmers participating in CRP.

It is unfair to treat active farmers and ranchers differently from other taxpayers when imposing self-employment taxes on rental income. Because of the Wuebker case, the IRS now singles out farmers and ranchers as landlords liable for the self-employment tax. For other taxpayers who receive CRP payments, and are not materially participating in a farming operation, the payments are considered to be rental income that is not subject to self-employment tax.

Farmers and ranchers are in a no-win situation concerning the application of self-employment taxes. Agriculture producers face confusion and uncertainty because it is not known if and when an appeal will be heard by the full Sixth Circuit Court.

Additional confusion arises over jurisdictional matters. The original case was brought before Tax Court. The Tax Court ruling, which said that self-employment taxes are not owed, has nationwide application. The appeals case was heard in the Sixth Circuit Court of Appeals which only has jurisdiction over Ohio, Tennessee, Michigan and Kentucky. This means that farmers in other states are not directly affected by the appellate court decision to require self-employment taxes on CRP payments. But because the IRS believes that the tax should be paid, it could audit farmers in other states with the intention of securing favorable court rulings to collect the tax. If farmers and ranchers are audited and fail to satisfy the IRS, they risk paying back taxes, interest, penalties and the cost of amending as many as four years' tax returns.

This issue not only has impact on farmers and ranchers, but also on the environment. Self-employment tax on CRP payments may discourage a farmer from future participation in this program. Environmentally sensitive acreage that has been taken out of production to protect its natural resources may be forced back into production if CRP payments are subject to self-employment taxes.

Tax policy should not single out farmland owners to pay the self-employment tax on cash rental receipts. The IRS should not be able to impose new taxes on farmers and ranchers without congressional approval.

Congress should pass legislation to restore equitable tax treatment for farmers and ranchers by making it clear that CRP payments are not subject to self-employment taxes.

Farm Bureau supports S. 2344 introduced by Sens. Brownback (R–KS) and Daschle (D–SD) to clarify that CRP payments are not subject to self-employment taxes.

S. 1392—SPECIES CONSERVATION TAX ACT OF 1999

Farm Bureau supports S. 1392 introduced by Senator Baucus (D–MT). The bill provides incentives to landowners wishing to take active measures to provide species habitat.

Every year, we receive calls from Farm Bureau members who are disappointed there is not enough funding for the Partners for Wildlife Program. This is a popular program with landowners. It is simple. The funding, often matched by the landowner, provides a means to enhance wildlife on private property. The funding is mostly in the form of small projects of less than $10,000. Senator Baucus has recognized the need to exclude from taxable income the funds received from this program. Landowners, especially farmers and ranchers, gladly bear part of the cost for these projects. Taxing as income the funds that enable them to provide habitat is a disincentive. We take this opportunity to ask members of the committee to support additional funding for this program in the future.

We support both Sections 4 and 5 of the bill. Tax incentives are an effective means of enhancing habitat conservation goals.

S. 808—THE CONSERVATION TAX INCENTIVES ACT OF 1999

Farm Bureau supports S. 808 which excludes from gross income 50 percent of gain from the sale of land, or an interest in land, to an entity intending to put the land in a conservation use. The effect of this legislation will provide further incentives to landowners to consider selling either the land or the development rights to that land. For farmers and ranchers, the sale of capital assets of this type can trigger a major taxable event. To minimize that tax liability puts these types of transactions on a more level playing field with acquisitions that do not provide conservation purposes.

Prepared Statement of Alan Front

Mr. Chairman, my name is Alan Front, and I am pleased to appear before the Subcommittee today to share the perspective of The Trust for Public Land, a national nonprofit land conservation organization, regarding the urgent need for renewed federal assistance—as provided by S. 1558, the Community Open Space Bond Act—for community-based open space protection. I appreciate this opportunity to discuss my organization's enthusiastic support for this important legislation.

First, I want to express my gratitude to Subcommittee Chairman Hatch and Ranking Member Baucus for introducing S. 1558 and convening this hearing. In doing so, the Subcommittee has recognized the powerful but often overlooked nexus between the tax code, sprawl and smart growth. This is a most appropriate forum for examining how community revitalization and land conservation can be accomplished with federal encouragement. Along these lines, the specific mechanisms of the Community Open Space Bond Act will harness the power of the tax code and bond markets to give local governments more opportunities to protect their human and natural environment, while at the same time allowing ordinary citizens to benefit from their investment into our Nation's future.

Since 1972, TPL has worked to protect land for people, helping government agencies, property owners, and local interests to establish and enhance public spaces for public use and enjoyment. By arranging conservation real estate transactions, TPL has facilitated the public protection of well over a million acres of park, forest, agricultural, and other resource lands. Through these "win-win" partnerships, many communities have woven an appropriate open-space thread into their overall land-use fabric. In the process, they have recognized the interdependence of the built environment and the natural one, and have reaped the benefits of balanced growth.

THE NEED FOR LAND CONSERVATION

Despite the best efforts of local, state and federal government conservation agencies, overwhelming development pressures are posing continued, imminent threats to some of our nation's most scenic and fragile landscapes, leading communities to search for new solutions. Let me cite just a few examples:

In Florida, Broward County Commissioners are considering bond issues to finance the hundreds of millions of dollars needed to set aside green spaces. In the Chesapeake Bay region, even as a landmark multi-state agreement is implemented to protect the Bay, a new report details that sprawl may eventually overwhelm that watershed. In Tampa, a massive brownfields redevelopment program is fostering new development on long-vacant lots, which in turn are costing less to develop than sub-

urban sites because infrastructure is already in place. Voters in Peoria, Arizona this fall will decide on a $30 million bond authorization to acquire land and build parks.

Land-use trends on a national scale are raising new concerns about whether the harmony between development and environmental protection can be maintained. We have seen the rate of open space conversion more than double in the past decade; according to recent Department of Agriculture statistics, farmland and other open space is yielding to development at an average rate of nearly 400 acres every hour. And from the wilderness to the inner city, even as these open spaces are being lost, Americans are more and more urgently expressing their need for more parks, greenways, wildlife areas, community gardens, and scenic protection.

The federal government, through the tax code as well as through direct aid programs, has long contributed to important local economic development. Regrettably, though, an unintended by-product of this local support has been the conversion of ranches, riverways, farms, wetlands and other open spaces. The time is right to harness those same financial incentives to provide options for our local governments to rehabilitate downtowns, create new community meeting places, encourage working landscapes, and protect our great scenic vistas so the next generation can enjoy these special places and irreplaceable resources.

LOCAL GOVERNMENT FUNDING MECHANISMS

Local governments have instituted different types of fees and taxes to protect their open spaces. The following examples demonstrate the breadth of these alternatives, as well as their limitations. In many of these cases, Community Open Space Bonds would make a pivotal difference in leveraging these efforts.

Park City, Utah

Sitting high in Utah's beautiful Wasatch Range, Park City is faced with sprawl pressure from two significant sources. A mecca for outdoor recreation and the site of several 2002 Winter Olympic events, the city finds its market for second homes and resort condos booming. And, located only 45 minutes from downtown Salt Lake City, Park City is being hit with suburban sprawl from one of the fastest-growing urban centers in the country.

Park City sits at the end of a narrow valley, almost completely surrounded by slopes owned by the United Park City Mines, ski resorts, and other private landowners. Over the last decade, the two entrances to the valley and open fields on the valley floor have filled with development. More recently this development has spread to many of the surrounding slopes. In response, the Park City Council has made vigorous efforts to protect as much open space as possible.

In the summer of 1998, city leaders concluded that they had exhausted even the most creative open space funding options within the city budget. Fearing that the most important open space parcels would be lost, the city began working to protect critical tracts of land, and the public finance staff began researching options for a public funding measure. Within three months, a $10 million parks, open space, and recreation bond was passed with 77 percent of the vote—a major step in protecting the city's valuable open space.

Community Open Space Bonds would further leverage these local bonds, allowing Park City residents to better manage growth and conserve the landscape and protect those recreational opportunities that are so important to the area's quality of life.

Montana's Resort Tax

Since 1985, visitors to Montana have helped some communities pay for parks and open space through a local-option resort tax. The state legislation allows designated resort communities, small communities with large numbers of tourists, to tax visitors for traveler-related infrastructure and services.

Once the state approves a community's resort status, voter approval must be won. The measure allows these resort towns to levy a sales tax of up to three percent on tourist-related goods and services such as restaurants, lodging, entertainment, and recreation.

More and more communities are turning to this tax as the number and impact of visitors increase. Montana voters have twice defeated a statewide sales tax but seem more willing to approve this local option. Voters in Whitefish, for example, recently approved the tax and will dedicate 5 percent of the $800,000 in first year revenues to a bike path.

S. 1558 would permit Montana's resort communities to leverage their resort tax receipts against Community Open Space Bonds, and use the local tax receipts to pay off the bond principal, while the federal government covers the interest in the form of federal tax credits.

Austin, Texas

An '80s boomtown, Austin's growth went virtually unchecked until a variety of citizen groups formed to protect the city's scenic beauty and natural resources. A $20 million land conservation measure—the Barton Creek Wilderness Park general obligation bond—was sponsored by Citizens for Open Space (COS), a 100-member local coalition that was focused on protecting the most urban section of the Barton Creek watershed.

The open space acquisition bond was joined on the ballot by a Save our Springs (SOS) water quality initiative—a regulatory measure designed to protect the Barton Creek watershed—and a $22 million bond to preserve habitat land. These measures were handily approved by Austin's voters.

Since the victory, 978 acres of the most environmentally sensitive land in Barton Creek Wilderness Park has been acquired—below budget and in less than half the time originally estimated.

Community Open Space Bonds could further leverage these local funds to protect additional acres in this key watershed.

Florida Forever

Ranked among the fastest-growing states in the country, Florida has responded to development pressures by launching aggressive land conservation and natural resource protection programs. Most recently, in April 1999, the state enacted Florida Forever, which builds upon an existing ten-year program known as Preservation 2000 (P2000).

P2000 was designed to raise $3 billion for land conservation over a ten-year period from 1990–2000, funded through the sale of state revenue bonds backed by receipts from the state's documentary stamp tax on real estate transfers. It has also served as a funding umbrella for several state programs whose goals are to acquire land for the purpose of conservation and outdoor recreation. Florida Forever will provide an additional $3 billion over the next ten years for the acquisition and improvement of community-based parks and urban green spaces.

Community Open Space Bonds could stretch the Florida Forever funds to protect an even greater number of ecologically sensitive areas around the state, and assist localities coping with incredible growth pressures.

These are but a few of the methods that states and local communities are utilizing to raise funds to conserve land. Other local funding techniques include property taxes, special assessment districts, impact fees, borrowing, and user fees.

BALLOT INITIATIVES

I have included as Appendix A of my testimony results from 102 local referenda from 1999 that propose using public funding to protect open space. Ninety-two of these referenda won approval (90%). In 1998, 124 of 148 (84%) of similar open space referenda were approved. These referenda do not include many of the legislature-passed initiatives to fund open space programs at the state and local level.

These results, from across the Nation, show the overwhelming desire of the American people to protect their open spaces and to grow smarter. But at the same time that many states are empowering municipal governments with the fiscal authority to issue bonds, others are tightening local purse strings by imposing tax limitations, super-majority requirements and other restrictive measures.

Local governments have stepped up to the plate. It is time for the federal government to become their partner by creating another tool to better leverage local funds.

USING COSBS TO LEVERAGE FUNDS FROM STATE AND LOCAL PROGRAMS

Community Open Space Bonds essentially provide local communities the opportunity to issue bonds without paying any interest. The community (issuer) would be responsible for paying off the principal in fifteen years. The federal government would be responsible for paying the issuer's interest on these bonds during the fifteen years, in the form of federal tax credits to the bondholder. That tax credit would be equal to the corporate average AA bond rating, as posted by the U.S. Department of the Treasury, multiplied by the face amount of the bond. The bond issuer would then use the proceeds from the sale of these bonds to fund the "qualified environmental infrastructure project[s]" permitted by this legislation.

These qualified environmental infrastructure projects include:

- acquisition of property for open space, wetlands, public parks and greenways;
- visitor facilities, including nature centers, campgrounds, hiking and biking trails;
- the enhancement of water quality by revitalizing the land along waterways and cleaning up toxic waste affecting water quality;

- easements to maintain working landscapes and for access to public land; and,
- brownfields remediation.

The COSB mechanism will allow local governments to recapture for programmatic use that portion of bond funding normally allocated to debt service. States and localities could use funds from the hundreds of ballot and legislative initiatives passed over the last few years purely to pay off principal, while the federal government would cover the interest in the form of tax credits. This would be a true partnership between states (by devolution of fiscal power to local governments), the federal government (by paying the interest on these bonds) and local governments (by coming up with the funds in the first place and by undertaking the projects).

The demand for community parks and open space is greater than ever. Yet federal and state aid often falls short. And while there are other federal programs that seek to preserve open spaces, there are none similar to COSBs that give communities the range of options with this type of financing mechanism, and unprecedented decision-making powers at the local level. Under S. 1558, localities determine the best course of action for their particular needs and situation. This legislation encourages local governments to revitalize their communities with the carrot of federal financial assistance—and not the stick of regulatory constraints.

Not only is S. 1558 a creative funding approach, it also is a substantial one. Under this legislation, local, state, and tribal governments will be able to make available up to $1.9 billion in bonding authority annually for five years. That is a total of $9.5 billion in bonding authority over a five-year period.

The Trust for Public Land is pleased by the breadth of options given to local governments under this legislation. The needs of local communities vary greatly, and oftentimes a one-size-fits-all federal approach does not work. Across the country, we have worked with local, state and federal partners in projects as diverse as the many landscapes they protect, from the scenic Bonneville Shoreline Trail in Utah to community gardens in New York City. (Attached for the record as Appendix B is a description of several other communities where TPL is assisting local entities with meeting their conservation needs, which I hope will help show the diversity of needs that a COSB-type proposal can meet.)

From conservation easements to protect working landscapes, to wetland and upland acquisition to help restore a degraded river, the methods and tools that local governments use to protect their special places often depends on their funding needs and the authority granted to them by the state government. While these projects vary greatly, one theme is consistent: local governments need additional tools and resources to reach their conservation goals.

S. 1558 would give local communities one more tool to enable them to implement their goals. TPL commends the Subcommittee for holding this hearing and looks forward to working with you to make Community Open Space Bonds a reality.

Thank you again for the opportunity to testify today.

1999 Open Space Acquisition Ballot Initiatives

102 Referenda in 22 states; 92 winning referenda (90%); 10 losing referenda (10%); total funds $1,832,993,000

State	Jurisdiction	Date	For	Against	Description	Tax Rate	Total Funds
AZ	Glendale	11/2	68%	32%	Bond issue for open space preservation and trails		$53,700,000
AZ	Phoenix	9/7	80%	20%	Increase sales tax for open space acquisition	1/10 cent	$256,000,000
AZ	Scottsdale	9/11	77%	23%	Bond issue for park acquisition		$200,000,000
CA	San Carlos	11/2	76%	24%	Property tax surcharge for parks $6/parcel		$1,200,000
CO	Adams Co.	11/2	60%	40%	Sales tax increase for open space acquisition	1/5th cent	$38,500,000
CO	Boulder Co.	11/2	69%	31%	Extend sales tax for open space for 10 years	1/4th cent	$123,500,000
CO	Clear Creek Co.	11/2	51%	49%	Open space bond for land acquisition		$1,500,000
CO	Clear Creek Co.	11/2	52%	48%	Property tax increase to establish open space fund	1 mill	
CO	Larimer Co.	11/2	60%	40%	Extend existing sales tax 15 years to support bonds for open space program	1/4th cent	$54,000,000
CO	Pitkin Co.	11/2	69%	31%	Extend and increase property tax, authorize bonding for open space and trails		$12,000,000
CO	Summit Co.	11/2	65%	35%	Property tax to fund bonds for open space purchases		$30,000,000
CO	Brighton	11/2	66%	34%	Reallocate sales tax for open space preservation, parks, and recreation		
CO	Erie	11/2	50%	50%	Increase sales tax and create $5 million bond authority for open space	1/4th cent	
CO	Louisville	11/2	77%	23%	Allow use of excess tax revenues for open space preservation		
CO	Lafayette	11/2	64%	36%	Increase sales and use tax for open space preservation	1/4th cent	$750,000
CO	Nederland	11/2	61%	39%	Authorize 309-acre open space acquisition		
CO	Nederland	11/2	71%	29%	Allow use of excess tax revenues for open space preservation		
CT	Cheshire	11/2	65%	35%	Open space acquisition bond		$500,000
CT	Danbury	11/2	79%	21%	Portion of larger bond devoted to open space and recreation investments		$2,800,000
CT	Glastonbury	11/2	74%	26%	Bond for acquisition of land and conservation easements		$3,000,000
CT	Rocky Hill	11/2	65%	35%	Bond for open space acquisition		$1,000,000
CT	Woodstock	5/3	100%	0%	Creates land acquisition fund (town meeting vote)		
DE	Newark	11/2	74%	26%	Property tax increase for open space acquisition	.05mill	$4,200,000
FL	Sarasota Co.	3/16	65%	35%	Dedicate property tax increase for land acquisition, protection, and management	0.025 mill	
FL	Sarasota Co.	3/16	68%	32%	Bond for land acquisition		$53,000,000
FL	Miami Beach	11/2	87%	13%	Bond issue for parks and public beaches		$24,000,000
GA	Clarke Co.	11/2	93%	47%	Portion of sales tax increase to be used for land acquisition	10% of 1 cent tax	$10,000,000
IO	Blaine Co.	5/27	50%	90%	Bond for purchase of conservation easements		
IL	Kane Co.	4/13	66%	34%	Bond issue for new Forest Preserve District		$70,000,000
IL	Lake Co.	4/13	66%	34%	Bond issue for new Forest Preserve District		$55,000,000
IL	Will Co.	4/13	57%	43%	Bond issue for new Forest Preserve District		$70,000,000
IL	Glen Ellyn	4/1	56%	44%	Bond issue to purchase a specific property		$3,500,000
IL	Homer Twp.	4/13	63%	37%	Bond issue for open space preservation		$8,000,000
IL	Libertyville	2/23	47%	53%	Bond issue for open space preservation		
MA	Northboro	4/26	46%	54%	Portion of additional real estate tax to finance open space purchases	1 per cent	
MA	Quincy	11/2	78%	22%	Acquire 67-acre parcel for open space preservation		
ME	Statewide	11/2	69%	31%	Bond issue to acquire lands and conservation easements		$50,000,000
MI	Ann Arbor	11/2	64%	36%	Property tax for park acquisition		$8,000,000
NC	Mecklenburg Co.	11/2	69%	31%	Bond issue for greenway acquisition and park improvement		$52,000,000
NC	Mecklenburg Co.	11/2	61%	39%	Portion of bond issue to be used for open space protection		$220,000,000
NC	Asheville	5/12	47%	53%	$18 million bond issue for parks and greenways		
NH	Northfield	8/31	87%	13%	Bond issue to acquire 85 acres		$375,000
NJ	Hunterdon Co.	11/2	67%	33%	Property tax increase to establish open space trust fund	0.3 mill	
NJ	Warren Co.	11/2	59%	41%	Property tax increase for open space trust fund	0.2 mill	
NJ	Allamuchy Twp.	11/2	73%	27%	Property tax increase for open space trust fund	0.2 mill	
NJ	Atlantic Highlands Bor.	11/2	72%	28%	Property tax increase for open space, parks and historic preservation	0.1 mill	$30,000
NJ	Berlin Twp.	11/2	57%	43%	Property tax increase for trust fund to purchase conservation easements	0.4 mill	
NJ	Bethlehem Twp.	11/2	61%	39%	Property tax increase for open space, farmland preservation, parks and recreation	0.2 mill	
NJ	Bordentown Twp.	11/2	56%	44%	Property tax increase for trust fund to purchase conservation easements	0.3 mill	
NJ	Byram Twp.	11/2	73%	27%	Property tax increase for open space fund	0.2 mill	
NJ	Chatham Twp.	11/2	59%	41%	Property tax increase for open space preservation and parks and recreation	0.1 mill	
NJ	Colts Neck	11/2	36%	64%	$2.5 million for land acquisition for open space and recreation		
NJ	Cranbury Twp.	11/2	84%	16%	Dedicate portion of property tax for open space and farmland preservation	0.3 mill	
NJ	Franklin Twp.	11/2	64%	36%	Property tax increase for open space/farmland preservation trust	0.1 mill	

State	Jurisdiction	Date	For	Against	Description	Tax Rate	Total Funds
NJ	FrelinghuysenTwp.	11/2	66%	34%	Property tax increase for farmland preservation	0.1 mill	
NJ	Green Brook Twp.	11/2	53%	47%	Property tax increase for open space, parks and historic preservation	0.15 mill	
NJ	Hanover Twp.	11/2	63%	37%	Dedicate portion of property tax for open space preservation and parks and recreation		
NJ	Hopatcong Twp.	11/2	51%	49%	Dedicate portion of property tax to create open space trust fund	0.1 mill	
NJ	Howell Twp.	11/2	80%	20%	Property tax increase to establish Open Space and Farmland Trust Fund	0 1 mill	
NJ	Lawrence Twp.	11/2	68%	32%	Property tax increase for trust fund to purchase conservation easements	0.1 mill	
NJ	Lincoln Park Bor.	11/2	48%	52%	Would dedicate property tax increase for an open space trust fund	0.2 mill	
NJ	Logan Twp.	11/2	65%	35%	Property tax increase for trust fund to purchase conservation easements	0.1 mill	
NJ	Lopatcong Twp.	11/2	75%	25%	Property tax increase for open space trust fund	0.1 mill	
NJ	Manalapan Twp.	11/2	57%	43%	Property tax increase for open space preservation and related projects	0.1 mill	
NJ	Millstone Twp.	11/2	62%	38%	Property tax increase for open space, farmland preservation, and parks	0.2 mill	
NJ	Montville Twp.	11/2	67%	33%	10-year increase in existing property tax for open space preservation	0.25 mill	$5,328,000
NJ	No. Brunswick Twp	11/2	71%	29%	Property tax increase for open space and farmland preservation	0 3 mill	
NJ	No. Hanover Twp.	11/2	75%	25%	Reallocate property tax for purchase of conservation easements	0 2 mill	
NJ	Oceanport Bor.	11/2	67%	33%	Dedicate portion of property tax to establish Open Space Preservation Fund		
NJ	Old Tappan Bor.	11/2	72%	28%	Property tax increase for open space acquisition and conservation projects	0.1 mill	$300,000
NJ	Pittsgrove Twp.	11/2	59%	41%	$15,000 for farmland preservation to be raised by 2000		$15,000
NJ	Plainsboro Twp	11/2	79%	21%	Dedicate portion of property tax for open space and farmland preservation	0 1 mill	
NJ	Pohatcong Twp	11/2	65%	35%	Property tax increase for open space and farmland preservation	0 3 mill	
NJ	Randolph Twp	11/2	78%	22%	Extend property tax for open space trust fund	0 2 mill	
NJ	Roseland Bor	11/2	62%	38%	Property tax increase for open space, historic preservation, and parks	0 2 mill	
NJ	Scotch Plains Twp	11/2	51%	49%	Property tax increase for open space preservation and parks and recreation	0.2 mill	
NJ	So. Orange Village Twp	11/2	76%	24%	Dedicate portion of property tax for for open space, historic preservation, and parks	0.1 mill	
NJ	Springfield Twp	11/2	78%	22%	Property tax increase for trust fund to purchase conservation easements	0 2 mill	
NJ	Tewksbury Twp.	11/2	66%	34%	Property tax increase for trust fund to purchase conservation easements	0 3 mill	
NJ	W Amwell Twp	11/2	63%	37%	Property tax increase for preservation of open space, farmland, and historic preservation	0.2 mill	$45,000
NJ	Westampton Twp.	11/2	62%	38%	Property tax increase for trust fund to purchase conservation easements	0 2 mill	
NY	Suffolk Co	11/2	55%	45%	Extend sales tax for protection of drinking water supplies	1/4th cent	$140,000,000
NY	Brookhaven	11/2	70%	30%	Bond issue for open space and drinking water protection		$10,000,000
NY	Southold	11/2	58%	42%	Bond issue for purchasing property and development rights		$2,000,000
OH	Franklin Co.	5/4	59%	41%	Property tax for prairie, forest, and wetland acquisition	0 65 mill	$125,000,000
OH	Columbus	11/2	68%	32%	Bond issue for parks and recreation		$59,400,000
OH	Symmes Twp.	11/2	63%	37%	Renew property tax increment for parks and green space	0.185 mill	
OH	Twinsburg	11/2	69%	31%	Bond issue for open space acquisition		$10,500,000
PA	Buckingham Twp	11/2	85%	15%	Bond issue for farmland/open space preservation		$9,500,000
PA	E Marlborough	11/2	67%	33%	Property tax increase to buy open space	0 2 mill	
PA	E. Rockhill Twp.	5/18	61%	39%	Income tax increase to fund open space acquisition	0 125 per cent	
PA	Half Moon Twp.	11/2	57%	43%	Property tax increase for farmland protection	2 mills	
PA	Logan	11/2	65%	35%	Property tax increase to establish open space trust fund	0 1 mill	
PA	Plumbstead	5/1	48%	52%	Dedicate income tax increment for open space preservation	0 5 per cent	
PA	Solebury Twp	11/2	90%	10%	Bond issue for open space acquisition		$10,000,000
PA	W Vincent Twp.	11/2	40%	60%	Property tax increase for open space preservation	0.56 mill	
PA	Willistown Twp.	11/2	80%	20%	Income tax increase to fund open space acquisition	0 125 per cent	$5,000,000
RI	Barrington	9/28	81%	19%	Bond issue for open space and recreation		$1,000,000
VT	Stowe	3/2	66%	34%	Bond issue for open space acquisition		$350,000
WA	San Juan Co	11/2	73%	27%	Extend real-estate excise tax for land acquisition and conservation	1 per cent	$18,000,000
WA	Lakewood	11/2	47%	53%	$9.9 million bond issue for parks, recreation, and land acquisition		
WI	Dane Co.	4/6	76%	24%	Bond issue to protect park lands		$30,000,000

Alan Front
Trust for Public Land
July 25, 2000

Appendix B

Special Places that Would be Further Enhanced by Community Open Space Bonds

Below are several locations where the Trust for Public Land is actively working as a partner with local government(s) to help them meet their conservation needs.

Chattahoochee Riverway, Georgia

With invaluable assistance from the late Senator Paul Coverdell of Georgia, the Trust for Public Land has worked with a group of active, eager partners in the acquisition, conservation and ongoing management of land to create a Chattahoochee Riverway. The goal of the campaign is to transform the Chattahoochee River from one of the nation's most threatened rivers into a vital center of community life for metro-Atlanta. The Chattahoochee provides drinking water for half of all Georgians and is Atlanta's most significant natural resource.

This 180-mile ribbon of green would stretch from the North Georgia mountains to Columbus, through seven counties and six cities – including Atlanta -- enhancing communities with recreational and natural lands.

From controlling erosion and run-off, and by creating buffer strips along the river, Community Open Space Bonds will allow for a flexible approach so different localities can use approaches best suited to their area to protect this treasure and to restore the Chattahoochee.

Bonneville Shoreline Trail, Utah

Piece by piece, Utah citizens want to preserve the Bonneville Shoreline Trail that runs 100 miles along the foothills of the Wasatch Mountains. From Santaquin in the south to Brigham City in the north, this trail will connect 40 communities and pass through such diverse settings as a university campus, Mormon temples, wilderness areas, and high tech research firms.

Salt Lake City has experienced rapid growth in the past several years and continued fast- paced growth is predicted. One recent projection triples the Wasatch Front population to five million by 2050.

Elected officials, land trusts, local governments and foundations support the creation of the Bonneville Shoreline Trail. Several communities including Salt Lake City, Draper, and Provo have already purchased and protected sections of land along the

trail. Currently, one-third of the Bonneville Shoreline Trail is protected and can be accessed in at least two-dozen places.

San Antonio, Texas
Edwards Aquifer

According to a 1990 Kansas State University study, population growth in Bexar County will skyrocket during the next 50 years. By 2050, an estimated 3,100,000 people will live in the county. Because the Edwards Aquifer is San Antonio's sole source of drinking water, the land within the aquifer's recharge zone must be protected to ensure clean water for future generations. The San Antonio Water System and the Edwards Aquifer Authority encouraged the creation of the Government Canyon State Natural Area.

Creeks and floodplains located in this area contribute recharge to the Edwards Aquifer, which in addition to providing drinking water also provides open space and protective corridors throughout the county.

Once completely assembled, the Government Canyon State Natural Area will total more than 6,500 acres and will be one of the largest urban parks in the country. Under TPWD's management, the public will be able to enjoy a variety of recreational opportunities at the park. Government Canyon provides important habitat for outstanding examples of animal and plant communities, including the golden-cheeked warbler and the black-capped vireo, oak-juniper savannahs and woodlands, live oak, and cedar elm.

Idaho County, Idaho, Burgdorf Meadows
Nez Perce Cultural Lands

The Trust for Public Land is attempting to acquire a conservation easement over 94 acres in the Salmon River watershed that is a culturally significant site to the Nez Perce Tribe, which has a history of using the watershed for hunting, fishing, and gathering. An easement prohibiting development of Burgdorf Meadows will also protect important big game foraging habitat for deer, elk, and moose and maintain one of the Secesh River's only remaining strongholds for spawning summer Chinook salmon. Once the easement is in place, TPL will convey it to the Idaho Department of Fish and Game and the Nez Perce Tribe.

Community Open Space Bonds would allow the Nez Perce to acquire additional easements and would further stretch their resources while accomplishing their conservation and cultural goals. S. 1558 permits tribes, as well as state and local governments, to utilize this funding mechanism.

Chattanooga, Tennessee
Reconnecting People with the River

The Trust for Public Land has been working with a broad range of neighborhood groups and public agencies to implement the 1987 greenway master plan for Chattanooga, Tennessee. The heart of the plan is the proposed Chattanooga Greenways and Tennessee Riverpark, which will link city neighborhoods to the Tennessee River with a network of walking and bike paths. The trails will benefit the neighborhoods while connecting Chattanooga's residents to one another and to the previously neglected natural areas through which the trails pass.

Miami, Florida
Miami River Greenway

An estimated 250,000 people live along the Miami River. This multicultural population physically interacts with the river landscape daily, and yet access to the beneficial landscapes has been systematically limited over time. Currently, few public gateways exist to encourage either visual or physical interaction with the river. A river greenway system would serve to reconnect the diverse cultural and ethnic neighborhoods adjacent to the river to the important community, economic and environmental asset. Important species of plants and animals still inhabit the river, with the manatee being a symbol of an ecosystem at risk. The Biscayne Bay is a direct recipient of freshwater flowing from the Miami River. Less than 15% of South Florida's rainwater reaches the Biscayne Bay Aquifer, the primary drinking water supply for the metro region. The remainder is evaporated by the sun or drained by canals to the sea.

Even though the river is polluted today, and supports a large industrial marine use, there is opportunity to ecologically revitalize this river while at the same time providing access to it for the people that live so close, yet have very little interaction with the Miami River.

A concept report put together by the Trust for Public Land and Greenways Incorporated offers a broad vision and set of goals for the Miami River Greenway. These goals include providing access to the River, supporting river-borne commerce, restoration of water quality and fostering stewardship of the River, among others.

Community Open Space Bonds would offer proponents of this vision another tool to reach their goals and to revitalize and turn the Miami River into a destination landscape in the metro area.

Tulsa, Oklahoma
Protecting Drinking Water Supplies

One of the most significant environmental concern facing Oklahoma today is the issue of drinking water contamination due to confined animal feeding operations CAFOs) -- a concern shared by many other regions of the country. Nowhere in the state is the problem more severe than northeast Oklahoma. This region, populated by 600,000 residents, draws its drinking water from Lake Eucha and Spavinaw Lake, in the Ozarks to the east of Tulsa.

Historically, Tulsa and its environs enjoyed bountiful, clean public water. But excessive amounts of poultry waste, disposed of too close to the small streams that eventually feed into Lake Eucha and Spavinaw Lake, are overwhelming the natural purifying ability of this system. Phosphate contamination has led to excessive algae growth, a foul odor and taste of drinking water, and escalating costs of water purification. As the problem grows, the long-term consequences -- though not always clearly understood -- could include serious health risks.

The outcry over the deterioration of the drinking water supply has placed enormous pressure on elected officials. The Oklahoma legislature has announced that drinking water contamination due to CAFOs is a priority issue to be addressed. Legislative options include a moratorium on new CAFOs and strict regulation of existing operations. Both steps are feared and ardently opposed by farmers and the poultry processing industry.

The City of Tulsa, and its partner the Trust for Public Land, are working to research and design a land conservation program that could obviate or at least mitigate the need for draconian and divisive regulatory controls, pitting urban against rural interests in the state. TPL's preliminary assessment indicates that a top priority should be the creation of buffer zones along streams in the watershed. In order to engage the cooperation of farmers and other landowners and avoid constitutional challenges of uncompensated "takings" of property rights, such a program must pay landowners for any loss in property value caused by creation of the buffer zones. In other words, easements need to be purchased by an appropriate municipal or regional agency, rather than creating buffers through regulation.

Community Open Space Bonds could be utilized to stretch state and local funding to implement the plan to protect Tulsa's drinking water supply by acquiring easements or other suitable methods.

PREPARED STATEMENT OF VIRGINIA S. GORDAY

Chairman Hatch, Senator Baucus and members of the Subcommittee, my name is Virgina Gorday. I am Senior Vice President of Operations for Atlanta-based Portman Holdings, L.P.

Portman Holdings is a group of companies founded by architect and developer John Portman that owns, designs, manages and develops office, retail, residential and hotel properties located in major urban centers throughout the United States and in several foreign countries.

I appreciate the opportunity to testify today on behalf of The Real Estate Roundtable. The Real Estate Roundtable is an organization comprised of the principals of the leading real estate companies as well as the elected leaders of many of the major real estate trade associations. Its members are public and private real estate owners, advisors, developers, investors, lenders and managers. The Roundtable is the vehicle for the leading real estate executives to identify, develop, analyze and advocate federal policy positions affecting real estate.

I am please to testify in support of the Community Open Space Bonds bill sponsored by Senators Hatch and Baucus. This legislation creates a tax credit bond instrument that provides communities with an opportunity to obtain zero-interest federal financing for the purchase of open space, cleanup and redevelopment of contaminated brownfields, construction of park facilities, public land access projects and water quality preservation. I am also pleased to have this opportunity to bring to your attention several additional federal policy initiatives that are consistent with the goals of the Community Open Space Bonds bill and urge their enactment.

Why are policies that promote open space and the re-use of previously developed property important to an organization that represents building owners, lenders and developers? It is quite simple. Successful real estate projects depend, in large part, on the health and vitality of the community to which they belong. Open space creation and the productive re-use of existing properties are major components of community health and vitality.

In all communities, new or old, suburban or urban, the existence of attractive accessible and usable open space is the keystone of community redevelopment. It promotes a sense of livability that is fundamental to any successful development or redevelopment project. If an area is not "livable," people will not be attracted to it as a place to work, live, shop or play. Certainly the developer, lenders and investors suffer as a result, but in no less measure the community does to.

Revitalization of central urban areas is a focus of Portman Holdings because John Portman believes that the vitality and viability of America's cities is dependent upon their urban cores. This focus is not without risk and seemingly endless challenges, however. In fact, so pressing are these risks and challenges that to many developers pass on redevelopment projects and opt instead to develop so-called "green fields" because they present fewer financial risks and development obstacles. Not only does community revitalization suffer as a result, but sprawl is encouraged. Public/private partnerships help share this risk burden and provide the resources and cooperation to work through the many challenges.

Portman Holdings has a proud history of revitalization projects. Several other members of The Real Estate Roundtable do as well. Public/private partnerships were involved in many of the most notable Portman projects that include:

- The Embarcadero Center, San Francisco
- The Renaissance Center, Detroit
- Peachtree Center, Atlanta
- Centennial Olympic Park, Atlanta

Important features to all these projects were open space preservation and reclamation, brownfield cleanup and building of park facilities. The Community Open Space Bond bill will help foster the public/private partnerships needed to make future projects work through the flexible funding source it will provide, particularly at the local level.

Neither communities nor private developers alone can assume the financial risk required to take action on so many needed projects. In a public/private partnership, however, more of these projects can go forward and be brought to fruition because it is more financially feasible for the developer and the local government to take the chance to do the right thing.

The Community Open Space Bond bill will provide communities with the additional financing they need for these projects that cannot be obtained from the federal government through spending programs. With the funds from the bond issues, local governments can make their own decisions about open space preservation, redevelop their own brownfields properties and address other environmental issues. Bond financing—whether locally or federally subsidized—is not only more cost effec-

tive but also more equitable than using current appropriations of tax dollars. This is because it allocates the cost of acquiring green space over the life of the bonds. In that way it ensures contributions from the current and the next generation.

Again, Mr. Chairman, on behalf of Portman Holdings and The Real Estate Roundtable, I commend you and Senator Baucus for your efforts to enact the Community Open Space Bond bill. This is a good bill that will have positive impacts not only on the creation, preservation and reclamation of open spaces, but on the redevelopment of communities and the control of sprawl.

In addition to this bill, Mr. Chairman, The Real Estate Roundtable urges all Members of the Committee to enact other federal policies designed to promote redevelopment, environmental cleanup and building modernization. These policies are consistent in objective with the Community Open Space Bond bill because they are a federal response to sprawl and promote environmental remediation. Logically, if redevelopment is promoted, there will be less pressure to develop new spaces thereby preserving more open space. Furthermore, these policies have the support and sponsorship of many Members of this Committee.

Specifically, The Real Estate Roundtable encourages the enactment of:

- S.2700, legislation introduced by Senators Smith, Baucus, Chafee and Lautenberg to clarify the potential liability of prospective purchasers of mildly contaminated sites commonly known as "brownfields" and to provide more certainty that cleanup decisions made at the state level are also recognized as final determinations under federal law.
- S. 2438, legislation introduced by Senator Abraham that would to provide for the expensing of costs incurred to cleanup brownfields.
- S. 879, legislation introduced by Senators Conrad, Nickles, Baucus and Robb to allow leasehold improvements to be depreciated separately from structures over a 10 years period instead of the 39 years currently required.
- Legislation to allow demolition costs to be depreciated or amortized instead of capitalized and added to the basis of the land.

S. 2700 BROWNFIELD PURCHASER LIABILITY PROTECTION

The U.S. Conference of Mayors estimates that there are over 400,000 brownfields sites across the country. These sites are the hulking warehouses, dormant smokestacks and abandoned shells of industrial plants we find throughout the country. They are monuments to the "old economy." Development of these sites would help restore many blighted areas, create jobs where unemployment is high and ease pressure to develop beyond the fringes of communities. Small, urban centered businesses often benefit most directly by this redevelopment.

Many brownfields properties are located in inner cities—precisely where many businesses want to be. The economics are often right. Critical infrastructure, including transportation, is already in place and the workforce is in close proximity.

Unfortunately, while many of these sites have great potential, they remain the province of federal policies, such as Superfund, that perpetuate a legacy of urban decay by inhibiting the very kinds of investments our company and many others are in business to make.

To that end, we urge Congress to swiftly enact the kinds of reforms contained in S. 2700—introduced by Senator Smith with over 50 bipartisan cosponsors. This bill would clarify the potential liability of prospective purchasers of brownfields and provide more certainty that cleanup decisions made at the state level are also recognized as final determinations under federal law. Real estate companies should not be asked to take the risk that, for example, a $500,000 investment could become a $10 million liability. Senator Baucus has been an ardent supporter of this legislation and we thank him for his individual efforts to enact this reasonable and overdue policy.

S. 2436, BROWNFIELD COST RECOVERY ACT

With respect to tax policies affecting redevelopment, it is important to focus on the current tax treatment of environmental cleanup costs particularly brownfields.

Current law generally requires that these clean up costs be capitalized and added to the basis of the asset—which in many cases is land. Since land is not depreciable, these costs cannot be recovered until the property is sold. This discourages long term ownership and investment—a common and often required feature of successful real estate projects. Changing the law to allow the immediate expensing of these cleanup costs would promote the re-use of existing property and reduce some of the pressure to consume open space by development.

We are pleased that Congress recognized this in 1997 and enacted an exception that allows the expensing of cleanup costs for contaminated sites —albeit only in

empowerment zones or certain targeted high poverty areas. Last year, this Committee, in reporting out the Taxpayer Refund and Relief Act of 1999 and the Tax Relief Extension Act of 1999, approved a provision removing those targeted geographic requirements. Unfortunately, it did not get enacted. Senator Spence Abraham this year has introduced S. 2436 to accomplish the same goal and we strongly urge you to enact this bill.

S. 879, 10 YEAR LEASEHOLD IMPROVEMENT DEPRECIATION

Another tax policy that would stimulate the preservation of open space is S. 879 introduced by Senator Kent Conrad. This bill would change the current 39 year depreciation treatment for leasehold improvements to 10 years—a depreciation treatment that more closely matches the true economic life of leasehold improvements. Over 9 billion square feet of leased space is in the marketplace. The added tax cost resulting from 39 year depreciation for leasehold improvements is a disincentive for owners to keep buildings modern by customizing and upgrading tenant space. If buildings are not modernized to meet tenant needs, tenants will look to lease space in newer buildings. The result is greater pressure to build new buildings and consume so-called "green fields."

We are pleased that several members of the Finance Committee have joined Senator Conrad in supporting S. 879. Particularly we thank Senators Hatch, Baucus, Nickles, Robb, Mack, Kerrey, Bryan, Breaux and Murkowski for cosponsoring this important legislation. We urge that the Committee enact this bill this year and achieve the dual result of helping modernize existing buildings and easing the pressure to develop new buildings because of outdated building stock.

RECOVERY OF DEMOLITION COSTS

Demolition can be an expensive cost component of a redevelopment project. Similar to environmental remediation costs, demolition costs must be capitalized to the land and this unfavorable tax treatment is an impediment to redevelopment. We believe demolition costs for non-historic structures costs should be amortized over a specified period of time or, at a minimum, be added to the basis of the building and depreciated. If the current tax law disincentive to re-invest in existing property that requires demolition is mitigated, more redevelopment will result and our valuable and cherished open spaces will benefit.

CONCLUSION

In conclusion, Portman Holdings and The Real Estate Roundtable support the Community Open Space Bonds bill because it will effectively promote the creation, preservation and reclamation of open spaces. Open spaces improve community livability. The greater the livability of communities, the more positive the impact on real estate in those communities. Open space bonds also would give local governments the flexible financing they need to embark on the public/private partnerships needed to bring about redevelopment and the promotion of open space.

Additionally, we urge the committee to enact the other federal policies discussed above designed to promote redevelopment, environmental cleanup and building modernization. These policies are consistent in objective with the Community Open Space Bond bill because they are a federal response to sprawl and promote environmental remediation. We believe that the promotion of redevelopment through tax incentives and Superfund liability protection will result in less pressure to develop new spaces lead to the preservation of more open space

Thank you again for this opportunity to testify. The Real Estate Roundtable looks forward to working with the Committee to preserve, protect and reclaim our remaining open space.

PREPARED STATEMENT OF SAMUEL R. STALEY, PH.D.

I would like to begin by thanking the committee for the opportunity to comment on the federal role in preserving open space and land conservation. Urban and suburban development issues have emerged as an important part of the policy debate in the United States, and these hearings provide an opportunity to broaden the parameters of this debate and provide some context for federal policy. Indeed, while some components of state, local, and federal growth-management strategies are controversial (e.g., growth boundaries, state mandates, etc.), almost everyone seems to agree that open-space preservation is a legitimate public-policy goal.

Unfortunately, relatively little time or resources have been spent understanding the dimensions of open-space preservation in a policy context. In particular, while

widespread public sentiment supports enhanced efforts to protect open space and farmland, the amount of open space, the specific strategies, and the role of the federal government in these efforts is unsettled. As I will discuss below, given the state of the current debate and our knowledge of land-use trends on the national and local levels, skepticism is warranted concerning significant increases in the federal role in these efforts.

THE FEDERAL ROLE IN LAND ACQUISITION AND OPEN SPACE

The key question before the committee is whether the federal government should dramatically expand its role in protecting open space and promoting land conservation by significantly increasing public expenditures for these activities. Both the Better America Bonds and CARA legislation attempt to expand this role, focusing primarily on using federal money to leverage state and local spending. Since the federal government is leveraging local initiatives, many people may view these efforts as benign. Poorly targeted federal spending and poorly designed strategies for open-space acquisition, however, may well do more harm than good, even in the area of land conservation. A central issues is whether a compelling federal interest exists in local land conservation efforts.

National Land Use, Farmland, and Open Space

As a matter of national policy, current urbanization trends do not threaten the amount of open space. Using preliminary data from the National Resources Inventory, only 5.4 percent of the nation's land is developed.[1] Less than 4 percent of that developed land is urbanized.[2] While the NRI data suggest the rate of land development has increased, the increase is only marginally impacting the amount of open-space overall.

In fact, developing a consistent federal response to open-space issues is problematic because states vary significantly in the amount of land developed. The most developed state in the nation is New Jersey where 35 percent of the state's land is developed. Less than 3 percent of many western states is developed. Already, the federal government owns more than 400,000 acres, almost four times the amount of land developed according to the preliminary NRI data. Some states have more than half their land locked up in federal and state wildlife preserves. In Utah, 64 percent of the state's land is permanently protected through federal ownership according to the Bureau of Land Management.[3] In fact, almost one-third of New Jersey is currently protected through a network of state and federal parks that includes the Pinelands National Reserve (the Pine Barrens).[4]

Not surprisingly, the greatest debates about open space occur at the local and regional level, not the national level. For example, Washtenaw County, Michigan was the focus of an intense fight to pass a property tax increase to fund a land preservation program. The county is home to Ann Arbor and part of the greater Detroit economic region, and the debate centered on farmland loss and the quality of life. Yet, more than half of Washtenaw County's land was still in rural and agricultural uses.[5] Similarly, debates over growth management and land development have proliferated in largely rural and suburban areas, from Portland, Oregon to Ventura

[1] This analysis relies on the preliminary NRI data recalled in March 2000 contained in *Summary Report, 1997 National Resources Inventory*, U.S. Department of Agriculture, Natural Resources Conservation Service, December 1999. All land-use data refer to this source unless otherwise noted. The recall was prompted by the discovery of a computer programming error that overestimated the amount of developed land, particularly in rural areas. The new data will not be released until September 2000 according to the U.S. Department of Agriculture. For a critique of the NRI data, see Steven Hayward, "The Suburbanization of America," in *A Guide to Smart Growth*, ed. Jane S. Shaw and Ronald D. Utt (Washington, D.C.: Heritage Foundation/The Political Economy Research Center, 2000), pp. 9–10. See also Samuel R. Staley, "An Overview of U.S. Urbanization and Land-use Trends," in *Smarter Growth: Market-based Strategies for Land-use Planning in the 21st Century*, ed. Randall G. Holcombe and Samuel R. Staley (Westport, CT: Greenwood Press, in press), available from the author.

[2] Historically, urbanized land accounts for between two-thirds and three-quarters of the developed land in the United States. See Samuel R. Staley, *The Sprawling of America: In Defense of the Dynamic City*, Policy Study No. 251 (Los Angeles: Reason Public Policy Institute, 1999), pp. 10–12 and the discussion in Staley, "An Overview of U.S. Urbanization and Land-use Trends."

[3] Daniel R. Simmons, Randy T. Simmons, and Samuel R. Staley, *Growth Issues in Utah: Facts, Fallacies, and Recommendations for Quality Growth* (Murray, UT: The Sutherland Institute, October 1999), pp. 51–52.

[4] Staley, "An Overview of U.S. Urbanization and Land-use Trends."

[5] Samuel R. Staley, *"Urban Sprawl" and the Michigan Landscape: A Market-oriented Perspective* (Midland, MI: The Mackinac Center for Public Policy, October 1998), pp. 9–10, Appendix C.

County, California to Lancaster County Pennsylvania. Many of these areas do not face a general threat to their open space. Rather, land conservation programs are the product of local quality of life issues and a fear of community change.

Defining Open Space

The type of open space people want to conserve is not well defined either. Most of the debate that motivates concerns about urban sprawl is localized: people are concerned about open space in their backyard, not hours away in a distant park or forest. Utah, for example, is initiating a statewide and regional growth-management strategy, focusing primarily on the Salt Lake City region. Yet, less than 2 percent of the Greater Wasatch Area (including Salt Lake City) is developed, and planners expect less than 4 percent to be developed by 2020 based on current trends.[6]

To the extent open space is an issue in rural areas, the debate revolves around the fragmentation of farmland. Even here, however, the fragmentation is most important in areas close to towns and cities. In rural Yellow Springs, Ohio, concern over development prompted the town and local residents to buy a 930-acre farm to prevent new development. Local residents, the local government, and antidevelopment organizations raised more than $3 million to buy the property.[7] Absent the open-space acquisition, the land would likely have been developed for housing. New housing, while taking decades to achieve build-out, had the potential to significantly increase the population in the village and the surrounding area. Many feared the loss of the rural-village atmosphere that this development would have prompted.[8]

Farmland Preservation

Importantly, while the Yellow Springs case is often used as an example of "farmland preservation," the real motivation was the protection of open space to prevent change in their community. The nation's agricultural industry is healthy, and the nation remains an exporter of key crops, including rice, wheat, cotton, soybeans, and corn.[9] Agricultural productivity is at all time highs in the United States and in the world. Ross Korves, Deputy Chief Economist for the American Farm Bureau Federation, observes that the world agricultural yield is expected to increase by about 1.5 percent per year while world population growth is expected to fall from 1.2 percent be year in 2005 to 1 percent by 2015. Thus, food security is not a sufficient reason for promoting farmland preservation on the national, state, or local levels.

Not surprisingly, a significant portion of the decline in farmland is attributed to lower demand for agricultural land. Luther Tweeten, an agricultural economist at Ohio State University, estimates that 74 percent of the decline in cropland nationwide can be explained by lower demand for agricultural products and uses.[10] These estimates are consistent with the preliminary data released by the NRI. From 1982 to 1997, 28.9 percent of the total land used for rural and urban development was converted cropland. The remainder came from pasture, range, forests, and other rural lands. More significantly, cropland fell by 45.9 million acres during this period, but development accounted for only 19.1 percent of this decline. The remaining cropland was converted to forest, pasture, range, wetlands, or other rural uses.

State Involvement in Open-space Preservation

State and local governments have been active in open space preservation for several years. In fact, as of June 2000, all states except North Dakota, South Dakota, Oklahoma, and Texas had land conservation or open-space programs on the books. More importantly, states and local governments have become increasingly active on this front.

The most heralded case is probably New Jersey's voter-approved commitment to spend more than $2 billion by 2010 on environmental protection and land conservation. More than $800 million will be dedicated to farmland preservation and $600

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[6] Simmons, Simmons, and Staley, *Growth Issues in Utah*, pp. 41–42.

[7] Samuel R. Staley, "The Political Economy of Land Conversion of the Urban Fringe," in *Agriculture and the Environment: Searching for Greener Pastures*, ed. Terry L. Anderson and Bruce Yandle (Palo Alto, CA: Hoover Institution Press, 2000).

[8] The Village of Yellow Springs has a population of about 4,000 and is the home to Antioch College, a nationally known liberal arts college.

[9] U.S. Department of Agriculture, Economic Research Service, *Foreign Agricultural Trade in the United States*, January–February issues.

[10] Luther Tweeten, "Competing for Scare Land: Food Security and Farm Preservation," paper presented to the American Agricultural Law Association, Minneapolis, Minnesota, October 17, 1997 and "Cropland Conversion and Urban Development in Ohio," Ohio State University Department of Agricultural Environment, and Development Economics, unpublished manuscript.

million to open-space acquisition and growth management.[11] Some analysts estimate this initiative could place as much as half of the state's remaining privately-owned land off limits to future development. Other notable state initiatives include Arizona's commitment to spend $20 million per year on open space.[12] Minnesota is dedicating $12 million to open-space acquisition, Oregon is committing $45 million per year to its program.[13] Pennsylvania has also committed more than $100 million per year over five years to land conservation, and Ohio will be placing a $200 million proposal to fund open space on its ballot in November.[14]

On the local level, several counties have initiated open-space programs. One of the more heralded examples is Lancaster County, Pennsylvania, where two programs have combined to save more than 30,000 acres. Moreover, despite the failure in Washtenaw County, Michigan, open-space and parks programs tend to receive substantial public support at the ballot box.[15] In addition to public initiatives, more than 1,213 local land trust protect almost five million acres of land.[16] National conservation organizations such as the Nature Conservancy and Audubon Society protect another 10 million acres.

Federal Efforts to Promote Land Acquisition Could be Counter Productive

Despite the apparent popularity of these programs, several reasons exist for adopting a cautionary policy stance at the federal level. Significant increases in federal involvement could be counter productive, particularly if they reinforce politically motivated attempts to put as much land off limits to development as possible as quickly as possible.

Land Acquisition Can Not Curb Urban Sprawl

First, federal efforts could simply encourage piecemeal land acquisition that promotes urban sprawl. As much as the efforts of states, local governments, and local citizens may be lauded for their concern about protecting open space, these efforts rarely impact land-development patterns significantly.

Ohio provides a useful example. Yellow Springs was able to protect 930 acres. But this parcel is surrounded by thousands of acres of farmland that could be developed for housing. Greene County, home Yellow Springs, has more than 178,000 acres of farmland according to the 1997 Census of Agriculture. Nearby Clark County has another 172,000 acres. In fact, based on current land prices in urban areas, the $200 million current law makers want to dedicate to land conservation could effectively impact less than 1 percent of the state's open space and farmland.[17]

An analysis of other open-space acquisition programs reveals similarly small impacts. After twenty years, Lancaster County's open-space acquisition programs have protected 7.7 percent of the county's farmland.[18] Maricopa County expects to preserve more than 90,000 acres in the Phoenix region by 2010, but this represents just 1.5 percent of the total acreage in the area.[19] Along the Treasure Cost of Florida, just north of Miami, 54,558 acres are targeted for preservation, but this represents just 2.4 percent of the land in the region.[20] Even if federal dollars significantly increased the ability of these programs to preserve open space, the impact on overall land use and development will be minor.

Significantly boosting land purchases across the board, a likely effect of federal initiatives, is likely to spur land acquisition in ways that encourage leapfrog development. Preserving patches of several hundred acres in different spots in metropolitan areas can help create parks, but also encourage the development of noncontiguous urban areas that still must be served by roads, water, sewer, and other urban

[11] Linda E. Hollis, Douglas R. Porter and Paul S. Tischler, *Livability and Affordability: Open Space Preservation and Land Supply* (Chevy Chase, MD: The Growth Management Institute, June 2000).

[12] Ibid.

[13] Ibid.

[14] Ibid.

[15] Phyllis Meyers, "Livability at the Ballot Box: State and Local Referenda on Parks, Conservation, and Smarter Growth, Election Day 1998," Discussion Paper prepared for The Brookings Institution, Center on Urban and Metropolitan Policy, January 1999.

[16] 1998 National Land Trust Census, Land Trust Alliance, Washington, D.C., http://www.lta.org. See also the discussion in Staley, *The 'Vanishing Farmland' Myth*, pp. 10–12.

[17] Samuel R. Staley, "Ohio Farmland Preservation Efforts Trivial, Off Target, and May Encourage Urban Sprawl," *Perspective on Current Issues* (Columbus, Ohio: The Buckeye Institute for Public Policy Solutions, July 2000).

[18] Samuel R. Staley, Jefferson G. Edgens, Gerard C.S. Mildner, *A Line in the Land: Urban-growth Boundaries, Smart Growth, and Housing Affordability*, Policy Study No. 263 (Los Angeles: Reason Public Policy Institute, October 1999), p. 30f.

[19] Hollis, Porter, and Tischler, "Livability and Affordability," p. 17.

[20] Ibid., p. 21.

infrastructure. Similarly, these efforts can encourage current trends toward lower densities.

Public Land Purchases are Inflexible

A second issue is the inflexibility of public land-acquisition programs. Almost all open-space programs presume that any land purchased will be kept permanently from development. Land, however, is a resource and can serve a variety of different uses. To exclude some uses (e.g., housing, offices, or shopping centers) ignores productive alternatives that could enhance community welfare. Private land trusts, in contrast, have the flexibility to be more strategic in land acquisition and sales. Many trusts swap land they consider more valuable for environmental purposes for land that is less desirable, permitting land development and urbanization more efficiently and economically. Public land programs, in contrast, are often driven by political goals to prevent any future development, regardless of its economic efficacy.

Lack of Local Knowledge

An additional problem posed by federal efforts to promote land acquisition is the tendency to promote porkbarrel projects. At current levels of funding, open-space and farmland protection programs must be strategic. Parcels of land need to be selected and identified for their strategic, aesthetic, and amenity value. Federal initiatives are likely to make this strategic thinking difficult. States and localities, much like transportation funding, will make efforts to acquire the funds without a full assessment of the costs and benefits of land acquisition. Currently, in many states, land acquisition programs rarely consider the potential costs of land acquisition, including noncontiguous urbanization, reductions in land supply, maintenance costs for parks and recreation areas, traffic congestion impacts, or the economic viability of land for agricultural purposes.

Most state budgets are generating fiscal surpluses, providing opportunities to increase funding for land conservation programs. The states have sufficient revenues to fully fund existing open-space protection programs without federal involvement. In Ohio, for example, the state is expected to run a $600 million fiscal surplus. Since 1996, the state has run cumulative surpluses in excess of $1.6 billion.[21] For Fiscal Year 1999, state governments in the United States had rainy day funds averaging 9.4 percent of their general revenue funds.[22]

Unintended Consequences

Finally, the federal government runs the risk of encouraging land development regulation and growth-management experiments with potentially significant unintended consequences. Under the Conservation and Reinvestment Act (CARA), for example, planning mandates could encourage a largescale reclassification of private property without mechanisms for reversing poor strategic decisionmaking.[23] Similarly, local governments are experimenting with growth-control techniques such as urban-growth boundaries, ignoring potential side effects such as higher housing prices and lower housing affordability.

CONCLUSION

In sum, little evidence suggests the federal government has a compelling justification for promoting further local open-space acquisition or farmland protection beyond existing efforts on the state and local levels. Open-space and farmland concerns are distinctly local issues. The nation is not faced with the prospect of losing significant amounts of open space or farmland. Urbanization, in particular does not pose a significant threat on a national or state level. Most states remain largely undeveloped and current trends in land use do not suggest a significant change.

More importantly, the private sector, state governments, and local governments are already responding to the public desire to preserve more open space. State and local governments have authorized hundreds of millions of dollars in new spending for open-space acquisition and farmland protection. Indeed, most states are running fiscal surpluses and have the ability to significantly increase spending for land conservation if they want to.

Federal involvement at this time, however, does have the potential to reinforce poor policymaking and decisionmaking on the state and local level. By reinforcing

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[21] Data provided by The Buckeye Institute for Public Policy Solutions, Columbus, Ohio.

[22] Ibid. and survey of states by the Ohio Legislative Budget Office. See the budget office's publication *Budget Footnotes* (June–July 1999), p. 246.

[23] For a critique of CARA, see Greg VanHelmond and Angela Antonelli, "Why CARA is Fiscally Irresponsible and a Threat to Local Use Decisions," *Backgrounder No. 1370* (Washington, D.C.: Heritage Foundation, May 9, 2000).

the perception that development is encroaching on open space and farm productivity, federal efforts could encourage inefficient and damaging growth-management policies while, paradoxically, encouraging leapfrog development and urban sprawl.

Thank you for your attention and interest.

PREPARED STATEMENT OF JONATHAN TALISMAN

Mr. Chairman, Senator Baucus, and distinguished Members of the Subcommittee: I appreciate the opportunity to discuss with you today the Federal income tax issues relating to proposals to encourage the creation of public open spaces in urban areas and the preservation of farm and other rural lands for conservation purposes as well as Federal income tax issues relating to proposals to lower U.S. dependency on foreign oil used in transportation fuels (including tax incentives to promote the use of alternative fuel vehicles and to increase domestic oil production). The first part of my testimony will focus on the Administration's proposed tax incentives to help build livable communities. I will then discuss the Administration's proposals for lowering U.S. dependency on foreign oil. I would like to begin by thanking the Chairman and Senator Baucus for their leadership on these issues.

Earlier this year, in the Administration's budget for FY 2001, the President proposed initiatives to help build livable communities for the 21st century. These initiatives aim to provide communities with tools, information, and resources they can use to enhance the quality of life of their residents, enhance their economic competitiveness, and build a stronger sense of community. For example, the Administration proposed a new financing tool—Better America Bonds—to help preserve green space, improve water quality, and revitalize communities for future generations. The Administration proposal would make available a total of $10.75 billion in bond authority over 5 years for investments by State, local, and tribal governments to preserve green space, create or restore urban parks, protect water quality, and clean up abandoned industrial sites. The revenue cost of the Better America Bonds proposal is estimated to be $690 million over 5 years. The Administration also proposed to make permanent the tax incentive to clean up brownfields in low-income communities and other targeted areas, which is scheduled to expire on December 31, 2000. The revenue cost of the brownfields proposal is estimated to be $600 million over five years.

The Administration's budget also included a $4 billion package of tax incentives over 5 years to encourage energy efficiency, reduce greenhouse gas emissions, and develop renewable energy sources. The tax incentives are part of a larger package of complementary initiatives.

In addition to the tax incentives, the Administration's budget includes a $337 million increase in funding for research and development in energy-efficient technology and renewable energy, a new $85 million Clean Air Partnership Fund to boost State and local efforts to reduce air pollution and greenhouse gases, almost $500 million to accelerate efforts to develop clean energy sources both here and abroad, and $1.7 billion in funding for global climate change research. The President's package of research and development funding and tax incentives to address the challenge of climate change totals over $4.1 billion for fiscal year 2001.

In addition to calling for steps to decrease our demand for oil through increased efficiency and increased development of renewable energy resources, the Administration is proposing new steps to support domestic exploration and production, and to lower the business costs of producers when oil prices are low. The Administration's proposals include favorable tax treatment for geological and geophysical costs and delay rental payments. The revenue cost of these tax proposals is estimated to be $750 million over 5 years.

My comments today will focus on an explanation of the Administration's tax initiatives for improving the environment and reducing our dependence on foreign oil.

ENCOURAGING PROSPERITY, IMPROVING THE ENVIRONMENT

Better America Bonds

Americans are concerned that the quality of the environment surrounding their communities is threatened by sprawl, that scenic vistas are being lost, that watersheds are eroding and contaminated, and that public access to outdoor recreation is diminishing.

To address these concerns, the Administration proposed the creation of a new financial tool—referred to as "Better America Bonds"—for use by State, local, and tribal governments, often in partnership with nonprofit organizations, to make their communities more livable. Better America Bonds are a tax-credit bond program,

similar to the current-law provision for Qualified Zone Academy Bonds. Through the provision of tax credits, the Federal government would, in effect, pay all the interest on Better America Bonds for fifteen years, thereby significantly lowering the cost of financing below that attainable by State, local, and tribal governments issuing traditional tax-exempt bonds. S. 1558, introduced by the Chairman and ranking member of this subcommittee, contains many significant aspects of the Better America Bonds proposal. In fact, the bonds proposed by S. 1558 would be very similar to Better America Bonds, except that under S. 1558 the authority to issue bonds would be allocated by a newly created board, whereas the authority to issue Better America Bonds would be allocated by the Environmental Protection Agency (EPA), as described below. In addition, Mr. Matsui and others have introduced a proposal for Better America Bonds in H.R. 2446. The Administration looks forward to working with Congress to resolve the differences between these bills and the Administration's proposal.

Interest would effectively be paid to holders of Better America Bonds in the form of a credit that could be claimed by the bondholder against Federal income taxes otherwise due. The credit rate would be set by the Treasury Department on a daily basis based on aa corporate yields of comparable maturity. The credit rate set for the day on which the bonds were sold would apply for the life of the bonds. (This method of setting credit rates was established by Treasury regulations for Qualified Zone Academy Bonds sold on or after July 1, 1999.) Issuers of Better America Bonds would pay no interest for the 15-year term of the bonds; their only obligation would be for repayment of principal after 15 years.

The Administration's proposal is designed to enhance the marketability of Better America Bonds by allowing buyers of the bonds to strip the "coupons," in the form of the tax credits, from the obligation to repay principal and sell the two pieces separately, much the same way that Treasury obligations are stripped. This would permit non-taxable entities, such as pension funds and endowments, to benefit from the difference between the current value of the stripped principal and the repayment of principal at par upon redemption, while a taxable investor claims the tax credit.

The proceeds of Better America Bonds could be used for the following purposes:

1. Acquisition of land by State, local, or tribal governments for open space, wetlands, parks, or greenways. Acquired land would be owned by a government or a tax-exempt entity whose exempt purposes include environmental protection.
2. Construction of public access facilities such as campgrounds and hiking or biking trails on publicly owned land or land owned by a tax-exempt entity whose exempt purposes include environmental protection.
3. Improvement of water quality by planting trees or other vegetation, creating settling ponds to control runoff, or remediating conditions caused by the prior disposal of toxic or other waste.
4. Acquisition of permanent easements on privately owned open land that prevent commercial development and any substantial change in the character or use of the land. Such easements could be held by governments or tax-exempt entities.
5. Environmental assessment and remediation of brownfields owned by State or local governments under certain circumstances.
6. Environmental assessment and remediation of property damaged by anthracite coal mining and owned by a State, local, or tribal government or qualifying tax-exempt entity under certain circumstances.

For example, the City of Lewistown, Montana could use Better America Bonds to acquire land for parks, open space, and trail systems. Other Montana municipalities could issue Better America Bonds to acquire land along rivers, such as the Missouri and the Yellowstone, in order to preserve the natural structure, reduce erosion, and protect the water quality. In Utah, Better America Bonds could be used to preserve the Bonneville Shoreline Trail in the Wasatch Mountains. In addition, Salt Lake City could use Better America Bonds in its Park Blocks development, in furtherance of its plan to create green space, pathways and park facilities to support significant economic development.

In general, property acquired with the proceeds of Better America Bonds would be available only for public use and use by tax-exempt entities, but not private use. The one exception is with respect to remediated brownfields and certain property damaged by coal mining, which could be sold to a private entity for private development, with the sale proceeds made available to repay principal.

Owners of property financed with Better America Bond proceeds generally would be required to covenant not to convert the property to a nonqualifying use without first offering the property for sale to tax-exempt entities at a price that does not

exceed the original value of the property. A tax-exempt purchaser would be required to hold the property in its qualifying use in perpetuity.

The Administration proposes $2.15 billion of authority to issue Better America Bonds each year for 5 years beginning in 2001 (i.e., a total of $10.75 billion of bond authority). Of the total authorization, $50 million per year would be available with respect to property damaged by anthracite coal mining under special allocation rules. The EPA would administer an annual, open competition among State, local, and tribal governments for authority to issue these bonds, subject to published EPA guidelines.

Projects qualifying for Better America Bonds, with the exception of remediated brownfields and damaged coal property converted to private use, could be financed by tax-exempt bonds under current Federal tax law. Indeed, States and localities occasionally use tax-exempt bonds for these purposes. But more needs to be done. Benefits from environmental projects are often so diffused over time and distance that taxpayers within particular local jurisdictions are reluctant to finance such projects with conventional tax-exempt bonds. Better America Bonds would provide a deeper subsidy than tax-exempt bonds in order to induce State and local governments to undertake beneficial environmental infrastructure projects. The revenue cost of the proposal is estimated to be $690 million for FY 2001–2005.

Compared to traditional tax-exempt bonds, Better America Bonds would significantly reduce the financing costs to local taxpayers of environmental projects. For example, annual payments of principal and interest on a traditional 30-year, 6 percent, $10 million tax-exempt bond issue would be about $726,000. In comparison, the annual payments into a sinking fund earning 6.5 percent that would repay after 15 years the $10 million principal of an issue of Better America Bonds would be about $414,000. A State or local government issuing the bonds would thus save about $312,000 per year over the initial 15 years, and $726,000 per year over the remaining 15 years of a 30-year issue's term. Better America Bonds would cost state and local governments only about half of what a tax-exempt bond would (in present value terms). This is a powerful tool for financing investments to make our communities better.

Better America Bonds not only would provide a deeper subsidy to State and local governments than tax-exempt bonds, they also would be more efficient. With Better America Bonds, the Federal government would pay the issuer's interest costs in the form of a tax credit to the bondholders. The issuer would receive the full benefit of the Federal subsidy.

By contrast, the revenue loss to the Federal government from tax-exempt bonds exceeds the amount of the subsidy to State and local governments. The subsidy from a tax-exempt bond depends on market factors, and is equal to the debt service savings a State or local government realizes by borrowing at a tax-exempt, rather than a taxable, interest rate. The large volume of outstanding tax-exempt bonds has increased tax-exempt interest rates generally, which has reduced the subsidy provided by tax-exempt bonds to amounts significantly below the cost to the Federal government.

BROWNFIELDS REMEDIATION COSTS

Brownfields are abandoned or underutilized properties where redevelopment is complicated by known or suspected contamination. Because lenders, investors, and developers fear the high and uncertain costs of cleanup, they avoid developing contaminated sites. Blighted areas of brownfields hinder the redevelopment of affected communities and create safety and health risks for residents. The obstacles in cleaning these sites, such as regulatory barriers, lack of private investment, and contamination and remediation issues, are being addressed through a wide range of Federal programs that includes the tax incentive for brownfields remediation.

To encourage the cleanup of contaminated sites, the Administration proposed, and the Congress enacted in the Taxpayer Relief Act of 1997, a brownfields tax incentive that permits the current deduction of certain environmental remediation costs. Environmental remediation expenditures qualify for current deduction if the expenditures would otherwise be capitalized and are paid or incurred in connection with the abatement or control of hazardous substances at a qualified contaminated site. A qualified contaminated site must be located within a targeted area, i.e., census tracts with at least 20-percent poverty rates (and certain contiguous industrial or commercial tracts), designated Empowerment Zones and Enterprise Communities, and the 76 EPA brownfields pilot projects designated before February 1997. In order to claim a current deduction, the taxpayer must obtain a statement from a designated State environmental agency that the qualified contaminated site satisfies the statutory geographic and contamination criteria of a brownfield. The provision

applies to qualified environmental remediation expenditures paid or incurred in taxable years ending after August 5, 1997, and before January 1, 2002.

Many taxpayers are unable or unwilling to undertake long-term remediation projects based on the current-law, temporary incentive because environmental remediation often extends over a number of years. For that reason, the Administration's budget proposed a permanent extension of the brownfields tax incentive. That proposal was introduced by Mr. Coyne and several cosponsors as H.R. 1630.

Reclaiming brownfields would encourage the redevelopment of targeted communities by making unused or underutilized land productive again. Extending the special current-law rule on a permanent basis would eliminate uncertainty regarding the future availability of the incentive and encourage long-range investment in the targeted areas. The revenue cost of the proposal is estimated to be approximately $536 million for FY 2001 2005. Treasury estimates that the tax incentive would induce an additional $7 billion in private investment to return 18,000 brownfields to productive use over the next ten years.

ENERGY SECURITY

Oil is an internationally traded commodity with its domestic price set by world supply and demand. Domestic exploration and production activity is affected by the world price of crude oil. Historically, world oil prices have fluctuated substantially. From 1970 to the early 1980s, there was a fivefold increase in real oil prices. World oil prices were relatively more stable from 1986 through 1997. During that period, average annual refiner acquisition cost (composite) ranged from $14.83 to $23.74 per barrel in real 1992 dollars. In 1998, however, oil prices declined to about $11.15 per barrel at the refiner in real 1992 dollars, their lowest level in 25 years in real terms. Since 1998, the decline has reversed with refiner acquisition costs (in nominal dollars) rising to about $17.50 per barrel in 1999 and to over $28 per barrel in March 2000. Although March is the latest month for which composite figures are available, the price of West Texas intermediate crude on the spot market was nearly $31 per barrel on July 20, 2000.

Domestic oil production has been on the decline since the mid-1980s. From the late 1970s to the mid 1980s, oil consumption in the United States also declined, but in the last decade oil consumption has risen by nearly 12 percent. The decline in oil production and increase in consumption have led to an increase in oil imports. Net petroleum imports have risen from approximately 42 percent of petroleum products supplied in 1989 to 51 percent in 1999. The volatility of crude oil prices over the past year has focused attention on the economic condition of the oil and gas industry, the increasing U.S. dependence on foreign oil supplies, and the prospects for reducing reliance on oil imports.

The strong performance of our economy over the past year, despite oil price rises, underscores the dramatic improvements in energy efficiency we have achieved over the past quarter century. While past oil shortages have taken a significant toll on the U.S. economy, the recent increases in oil prices have yet to have a major impact on the economy. Increased energy efficiency in cars, homes, and manufacturing has helped insulate the economy from these short-term market fluctuations. In 1974, we consumed 15 barrels of oil for every $10,000 of gross domestic product. Today, we consume only 8 barrels of oil for the same amount of economic output.

We can, however, do more to minimize the effect of future energy price increases and reduce our dependence on foreign oil. One essential element of national energy security is a comprehensive and balanced program of tax incentives. These must include both support for domestic oil producers to reduce our reliance on oil imports and incentives for energy efficiency and renewable and alternative energy sources. While current law provides substantial tax incentives for domestic oil and gas production and some incentives for energy efficiency and renewable and alternative energy, the Administration proposes to do more in both areas.

ENERGY EFFICIENCY AND ALTERNATIVE ENERGY SOURCES

Individuals and businesses do not invest enough in energy-saving technologies that produce benefits to society in excess of their private returns. If a new technology reduces pollution or emissions of greenhouse gases, those "external benefits" should be included in the decision about whether to undertake the investment. But potential investors have an incentive to consider only the private benefits in making decisions Thus, they avoid technologies that are not profitable even though their benefits to society exceed their costs. Tax incentives can offset the failure of market prices to signal the desirable level of investment in energy-saving technologies because they increase the private return from the investment by reducing its after-

tax cost. The increase in private return encourages additional investment in energy-saving technologies.

CURRENT LAW TAX INCENTIVES FOR ENERGY EFFICIENCY AND ALTERNATIVE ENERGY SOURCES

Tax incentives currently provide a limited amount of support for energy-efficiency improvements and increased use of renewable and alternative fuels. Current incentives in the form of tax expenditures are estimated to total $5.8 billion for fiscal years 2001 through 2005. They include a tax credit for electric vehicles and expensing for clean-fuel vehicles and clean-fuel refueling property ($460 million), a tax credit for the production of electricity produced from wind or biomass and a tax credit for certain solar energy property ($625 million), an exclusion from gross income for certain energy conservation subsidies provided by public utilities to their customers ($560 million), and an income tax credit or partial excise tax exemption for ethanol and renewable source methanol used as automobile fuel ($4.2 billion).[1]

Electric and clean-fuel vehicles and clean-fuel vehicle refueling property

A 10-percent tax credit is provided for the cost of a qualified electric vehicle, up to a maximum credit of $4,000. A qualified electric vehicle is a motor vehicle that is powered primarily by an electric motor drawing current from rechargeable batteries, fuel cells, or other portable sources of electric current, the original use of which commences with the taxpayer, and that is acquired for use by the taxpayer and not for resale. The full amount of the credit is available for purchases prior to 2002. The credit begins to phase down in 2002 and does not apply to vehicles placed in service after 2004.

Certain costs of qualified clean-fuel vehicles and clean-fuel vehicle refueling property may be deducted when such property is placed in service. Qualified electric vehicles do not qualify for the clean-fuel vehicle deduction. The deduction begins to phase down in 2002 and does not apply to property placed in service after 2004.

Energy from wind or biomass

A 1.5-cent-per-kilowatt-hour tax credit is provided for electricity produced from wind, "closed-loop" biomass (organic material from a plant that is planted exclusively for purposes of being used at a qualified facility to produce electricity), and poultry waste. The electricity must be sold to an unrelated third party and the credit is limited to the first 10 years of production. The credit applies only to facilities placed in service before January 1, 2002. The credit amount is indexed for inflation after 1992.

Solar energy

A 10-percent investment tax credit is provided to businesses for qualifying equipment that uses solar energy to generate electricity, to heat or cool or provide hot water for use in a structure, or to provide solar process heat.

Energy conservation subsidies

Subsidies provided by public utilities to their customers for the purchase or installation of energy conservation measures are excluded from the customers' gross income. An energy conservation measure is any installation or modification primarily designed to reduce consumption of electricity or natural gas or to improve the management of energy demand with respect to a dwelling unit.

Ethanol

Ethanol and renewable source methanol used as a highway fuel may qualify for either an income tax credit or a partial exemption from the excise tax on highway fuel. The income tax credit is generally 54 cents per gallon for ethanol and 60 cents per gallon for renewable source methanol. As an alternative to the income tax credit, gasohol blenders may claim a gasoline tax exemption of 54 cents for each gallon of ethanol and 60 cents for each gallon of renewable source methanol that is blended into qualifying gasohol. Slightly lower credits and exemptions apply in years after 2000 and both the credit and the exemption are scheduled to expire in 2005. The favorable tax treatment of ethanol increases national energy security by reducing the demand for imported oil and U.S. dependence on foreign oil sources.

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[1] *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2001*, U.S. Government Printing Office, Washington, DC, 2000, p. 120. These estimates are measured on an outlay-equivalent basis. They show the amount of outlay that would be required to provide the taxpayer the same after-tax income as would be received through the tax preference. This outlay-equivalent measure allows a comparison of the cost of the tax expenditure with that of a direct Federal outlay.

Gas-guzzler tax

In addition to the tax incentives described above, a tax ranging from $1,000 to $7,700 per vehicle is imposed on gas-guzzling automobiles (automobile models with a fuel economy of less than 22.5 miles per gallon).

ADMINISTRATION PROPOSALS TO PROMOTE ENERGY EFFICIENCY AND ALTERNATIVE ENERGY SOURCES

The Administration has proposed tax incentives designed to reduce energy consumption and greenhouse gas emissions by encouraging the deployment of technologies that are highly energy efficient and that use renewable and alternative energy sources. The proposed incentives also are designed to minimize windfalls for investments that would have been made even absent the incentives and to facilitate tax administration. The design of the tax incentives incorporates the following considerations:

Superior energy efficiency compared to conventional equipment. The eligible items should meet higher standards for energy efficiency than conventional equipment or use renewable energy sources. This ensures that tax benefits promote energy efficiency and reduce greenhouse gas emissions.

High threshold for eligibility. The energy-efficiency standards should be set sufficiently high so that eligible items presently account for a small share of the market. This minimizes windfalls for purchases that would have been made absent the credit.

High up-front costs compared to conventional equipment. The targeted technologies have significantly higher purchase prices than conventional equipment and, at current market prices, may have limited cost effectiveness. These high up-front costs are another reason relatively few items incorporating the targeted technologies would be purchased without a tax incentive.

Commercially available. The items should be commercially available or near commercialization. This ensures that the incentives encourage the deployment of new technologies that private markets have already developed.

Ease of administration. The items must be defined precisely enough that taxpayers can take advantage of, and the IRS can administer, the incentives. This helps to ensure that tax benefits are claimed for the items for which they are intended.

The tax incentives the Administration has proposed cover vehicles, buildings and homes, renewable energy, and industrial equipment. The proposed incentives will encourage businesses and consumers to increase their investment in energy-efficient items, new technologies, and renewable and alternative energy sources. The investments induced by the credits would be long-lived and, therefore, would produce energy savings and greenhouse gas reductions for many years after the investment is undertaken. The induced increase in the market penetration of energy-efficient technologies, new technologies, and renewable energy sources may lead to lower cost production and increased awareness of the benefits of such technologies that could have lasting effects.

Reductions in greenhouse gas emissions, however, are not the only benefits that will be realized from these incentives. The incentives will also reduce local air pollution. In addition, the proposals will produce private benefits, such as energy savings for consumers and businesses.

Vehicles

Cars and light trucks (including minivans, sport utility vehicles, and pickups) currently account for 20 percent of greenhouse gas emissions. Those vehicles also account for about 20 to 40 percent of urban smog-forming emissions and 40 percent of total U.S. petroleum consumption. Almost all cars and light trucks use a single gasoline-fueled engine.

Hybrid vehicles, which have more than one source of power on board, and electric vehicles have the potential to reduce greenhouse gas emissions, air pollution, and petroleum consumption. The proposed credits will encourage the purchase of vehicles that incorporate advanced automotive technologies and will help to move advanced hybrid vehicles currently under development from the laboratory to the highway. These vehicles can significantly reduce emissions of carbon dioxide, the most prevalent greenhouse gas.

The proposal would extend the present tax credit for electric vehicles and fuel cell vehicles. Under current law, a 10-percent credit is provided for the cost of qualified electric vehicles and fuel cell vehicles up to a maximum credit of $4,000. The maximum amount of the credit is scheduled to phase down in 2002 and be phased out

in 2005. The President's proposal would extend the tax credit at its $4,000 maximum level through 2006.

The proposal also would provide new tax credits of $500 to $3,000 for certain hybrid vehicles, depending upon requirements for the vehicle's design and performance. A qualifying hybrid vehicle is a road vehicle that can draw propulsion energy from both of the following on-board sources of stored energy: (1) a consumable fuel, and (2) a rechargeable energy storage system. The tax credits would be available for vehicles purchased during the period 2003 through 2006. The credit amounts—available for all qualifying vehicles, including cars, minivans, sport utility vehicles, and pickup trucks—would be:

- $500 if the rechargeable energy storage system provides at least 5 percent but less than 10 percent of the maximum available power;
- $1,000 if the rechargeable energy storage system provides at least 10 percent but less than 20 percent of the maximum available power;
- $1,500 if the rechargeable energy storage system provides at least 20 percent but less than 30 percent of the maximum available power; and
- $2,000 if the rechargeable energy storage system provides 30 percent or more of the maximum available power.

If the vehicle actively employs a regenerative braking system, the amount of the credit shown above would be increased by:

- $250 if the regenerative braking system supplies to the rechargeable energy storage system at least 20 percent but less than 40 percent of the energy available from braking in a typical 60 miles per hour (mph) to 0 mph braking event;
- $500 if the regenerative braking system supplies at least 40 percent but less than 60 percent of such energy to the storage system; and
- $1,000 if the regenerative braking system supplies 60 percent or more of such energy to the storage system.

Hybrid vehicles eligible for the largest credit would be 50 percent to 100 percent more fuel efficient than a conventional vehicle of the same size and power. Doubling a car's fuel economy reduces its emissions of carbon dioxide by about 50 percent. The revenue cost of this initiative is estimated to be about $2.1 billion for FY 2001–2005. These credits are estimated to result in purchases of 17 million electric and hybrid vehicles through 2010.

Buildings and homes

This sector currently accounts for about one-third of energy consumption and the related greenhouse gases. The proposed tax incentives would encourage investment in highly energy-efficient building equipment and new homes, and solar energy systems.

Tax credit for energy-efficient building equipment

A tax credit of 20 percent would be provided for energy-efficient equipment that will improve the energy efficiency of both residential and commercial buildings. The items covered are electric heat pump water heaters, natural gas heat pumps, and fuel cells. The credit would be 20 percent of the cost of the equipment, subject to a cap. It would be available for the period 2001 through 2004.

Items eligible for the credit are top-tier technologies that are much more energy efficient than conventional equipment. For example, compared to typical units on the market, the eligible electric heat pump water heaters and natural gas heat pumps are about twice as efficient. Items eligible for this credit embody new, cutting-edge technologies that have substantial purchase prices and that are limited in their cost effectiveness. They generally account for less than one percent of market sales. Therefore, the credits would benefit very few purchases that would have been made absent the credit. Some makes and models of qualifying items are currently available. Existing energy efficiency standards for the designated heat pump water heaters and natural gas heat pumps have been used to define eligible items precisely enough for IRS to administer the credit.

The revenue cost of this incentive is estimated to be $201 million for FY 2001–2005. The credit is estimated to result in purchases of nearly 2 million items of highly energy-efficient building equipment through 2010.

Tax credit for energy-efficient new homes

Residences account for about one-sixth of U.S. greenhouse gases and offer one of the largest sources of energy saving potential. Over one million new homes and manufactured homes are built and sold each year. Some States and certain Federal programs require new houses to meet certain energy code standards for insulation and related construction standards, and for heating, cooling and hot water equipment. However, the energy efficiency of new homes could be improved significantly

through the use of more energy-efficient building practices and more efficient heating and cooling equipment that exceed current efficiency standards.

A tax credit equal to $1,000 to $2,000 (depending upon the home's energy efficiency) would be provided to encourage consumers to purchase energy-efficient new homes. The tax credit would be: (1) $1,000 for homes that use at least 30 percent less energy than the standard under the 1998 International Energy Conservation Code (IECC)—this credit would be available for homes purchased during the period 2001 through 2003; and (2) $2,000 for homes that use 50 percent less energy than the IECC standard this credit would be available for homes purchased during the period 2001 through 2005.

Homes qualifying for the credit would use 75 percent to 85 percent less energy than existing housing and as much as 50 percent less energy than typical new housing. The revenue cost is estimated to be $633 million for FY 2001–2005. The credit is estimated to result in purchases of over 400 thousand new energy-efficient homes through 2010.

Tax credit for solar energy systems

Solar energy systems accounted for 0.025 percent of electricity generation in 1998. These systems produce no greenhouse gas emissions. To encourage use of these systems, a tax credit would be provided for the purchase of rooftop photovoltaic (PV) systems and solar water heating systems equal to 15 percent of the cost up to a maximum credit of $2,000 for PV systems and $1,000 for solar water heating systems. The tax credit for PV systems would be available for the period 2001 through 2007 and the tax credit for solar water heating systems would be available for the period 2001 through 2005.

The revenue cost of this incentive is estimated to be $132 million for FY 2001–2005. This incentive will help to achieve the President's goal of one million solar energy roofs by 2010. The credit is estimated to reduce electricity demand from nonsolar sources by 3 billion kilowatt hours through 2010.

Renewable and alternative energy sources

Wind and biomass currently account for about 2 percent of electricity generation from renewable sources. These renewable energy sources produce virtually no greenhouse gas emissions. Methane gas, which has approximately 21 times the greenhouse gas effect as carbon dioxide, accounts for about 10 percent of the warming caused by U.S. emissions. Methane from landfills, the single largest source of methane emissions, accounted for 37 percent of total U.S. methane emissions in 1997. To make electricity produced from wind and biomass price competitive with other forms of electricity generation, the proposal would extend the current-law tax credit for wind and biomass, expand eligible biomass sources and facilities, and allow a credit for electricity produced from cofiring biomass with coal. The proposal also would provide a tax credit for electricity produced from methane from landfills.

The proposal would extend and expand the tax credit for electricity produced from wind and biomass. It would:

- Extend the current wind and biomass credit for 2.5 years to cover facilities placed in service before July 1, 2004.
- Expand the definition of eligible biomass for the present credit beyond closed-loop biomass to include certain forest-related resources and agricultural and certain other sources. This change would apply to facilities placed in service after December 31, 2000, and before January 1, 2006.
- Expand eligible biomass for existing facilities. The proposal adds a 1-cent-per-kilowatt-hour credit for electricity produced from the newly eligible sources for biomass facilities that were placed in service before January 1, 2001. The credit would be available for electricity produced from biomass after December 31, 2000, and before January 1, 2003.
- Allow cofiring biomass with coal. This proposal adds a 0.5-cent-per-kilowatt-hour tax credit for electricity produced by cofiring biomass in coal plants after the date of enactment and before July 1, 2004. This credit would be adjusted for inflation after 2000. Only the portion of electricity associated with biomass would be eligible for the credit.
- Allow methane from landfills. The proposal adds a tax credit for electricity produced from landfill methane for the first ten years of production if the facility is placed in service after December 31, 2000, and before January 1, 2006. The credit would equal 1.5 cents per kilowatt hour for facilities at landfills that are not subject to EPA's 1996 New Source Performance Standards/Emissions Guidelines (NSPS/EG) and 1 cent per kilowatt hour for facilities at landfills that are subject to NSPS/EG. These credits would be adjusted for inflation after 2000.

The revenue cost of this incentive is estimated to be $976 million over FY 2001–2005. This incentive is estimated to increase electricity production from renewable energy sources and methane by 80 billion kilowatt hours through 2010.

Industry

Distributed power technologies have made it possible to place electrical generation assets in or adjacent to commercial establishments and residential rental properties, as well as in industrial establishments. These technologies can be more energy efficient and generate fewer greenhouse gases than conventional electrical generation methods. Under current law, distributed power assets used in a commercial or residential building are likely to be depreciated over much longer lives than are similar assets used to produce process energy in an industrial setting. Also, because the current asset classification system predates the development of these technologies and the era of electricity deregulation, there are ambiguities regarding the proper classification of distributed power property. The proposal would simplify current law by clarifying and rationalizing the assignment of recovery periods to distributed power property, including property used to produce both electricity and useful heat and mechanical power. It would reduce taxpayer uncertainty and controversy in this area, and would promote the use of these more efficient technologies.

Distributed power property placed in service after the date of enactment would be assigned a 15-year depreciation recovery period and a 22-year class life. For this purpose, distributed power property would include only (1) property used in the generation of electricity for primary use in nonresidential real property or residential rental property used in the taxpayer's trade or business, and (2) property with a rated total capacity in excess of 500 kilowatts that is used in the generation of electricity for primary use in a taxpayer's industrial manufacturing process or plant activity. It must be reasonably expected that no more than 50 percent of the electricity produced from distributed power assets would be sold to, or used by, unrelated persons. Distributed power property may also be used to produce usable thermal energy or mechanical power for use in a heating or cooling application, subject to certain restrictions.

The revenue cost of this provision is estimated to be $10 million for FY 2001–2005.

INCREASED DOMESTIC PRODUCTION OF OIL AND GAS

The importance of maintaining a strong domestic energy industry has been long recognized and the Internal Revenue Code includes a variety of measures to stimulate domestic exploration and production. The tax incentives contained in present law address the drop in domestic exploratory drilling that has occurred since the mid-1950s and the continuing loss of production from mature fields and marginal properties.

The current tax incentives for oil and gas are intended to encourage exploration and production. They are generally justified on the ground that they reduce vulnerability to an oil supply disruption through increases in production, reserves, and exploration and production capacity. U.S. vulnerability to oil supply disruptions also has been reduced by the growth of oil production outside the Middle East, the establishment of the Strategic Petroleum Reserve, and measures that promote energy conservation and alternative energy sources. In addition, major technological advances in oil exploration, such as three? and four?dimensional seismic drilling, are helping domestic producers find more oil, at greater depths, on and off?shore. At the same time, these technologies have reduced the environmental footprint left by exploration and production to 1/10th the size it was 25 years ago.

Current law tax incentives for oil and gas production

Preferential tax treatment is an important source of assistance provided by the Federal government to the domestic oil and gas industry. Incentives for oil and gas production in the form of tax expenditures are estimated to total $8.3 billion for fiscal years 2000 through 2005.[2] They include the nonconventional fuels (i.e., oil produced from shale and tar sands, gas produced from geopressured brine, Devonian shale, coal seams, tight formations, or biomass, and synthetic fuel produced from coal) production credit ($3.7 billion), the enhanced oil recovery credit ($2.8 billion), the allowance of percentage depletion for independent producers and royalty owners, including increased percentage depletion for stripper wells ($1.7 billion), the exception from the passive loss limitation for working interests in oil and gas properties ($125 million), and the expensing of intangible drilling and development costs ($5 million). In addition to those tax expenditures, oil and gas activities have largely

[2] *Ibid.*

been eliminated from the alternative minimum tax. These provisions are described in detail below.

Percentage Depletion

Certain costs incurred prior to drilling an oil- or gas-producing property are recovered through the depletion deduction. These include costs of acquiring the lease or other interest in the property, and geological and geophysical costs (in advance of actual drilling). Any taxpayer having an economic interest in a producing property may use the cost depletion method. Under this method, the basis recovery for a taxable year is proportional to the exhaustion of the property during the year. The cost depletion method does not permit cost recovery deductions that exceed the taxpayer's basis in the property or that are allowable on an accelerated basis. Thus, the deduction for cost depletion is not generally viewed as a tax incentive.

Independent producers and royalty owners (as contrasted to integrated oil companies)[3] may qualify for percentage depletion. A qualifying taxpayer determines the depletion deduction for each oil or gas property under both the percentage depletion method and the cost depletion method and deducts the larger of the two amounts. Under the percentage depletion method, generally 15 percent of the taxpayer's gross income from an oil- or gas-producing property is allowed as a deduction in each taxable year. The amount deducted may not exceed 100 percent of the net income from that property in any year (the "net-income limitation").[4] Additionally, the percentage depletion deduction for all oil and gas properties may not exceed 65 percent of the taxpayer's overall taxable income (determined before such deduction and adjusted for certain loss carrybacks and trust distributions).[5]

A taxpayer may claim percentage depletion with respect to up to 1,000 barrels of average daily production of domestic crude oil or an equivalent amount of domestic natural gas. For producers of both oil and natural gas, this limitation applies on a combined basis. All production owned by businesses under common control and members of the same family must be aggregated; each group is then treated as one producer for application of the 1,000-barrel limitation.

Special percentage depletion provisions apply to oil and gas production from marginal properties. The statutory percentage depletion rate is increased (from the general rate of 15 percent) by one percentage point for each whole dollar that the average price of crude oil (as determined under the provisions of the nonconventional fuels production credit of section 29) for the immediately preceding calendar year is less than $20 per barrel. In no event may the rate of percentage depletion under this provision exceed 25 percent for any taxable year. The increased rate applies for the taxpayer's taxable year which immediately follows a calendar year for which the average crude oil price falls below the $20 floor. To illustrate the application of this provision, the average price of a barrel of crude oil for calendar year 1997 was $17.24; thus, the percentage depletion rate for production from marginal wells was increased by two percent (to 17 percent) for taxable years beginning in 1998. In addition, the 100-percent-of-net-income limitation has been suspended for marginal wells for taxable years beginning after December 31, 1997, and before December 31, 2000.

Marginal production is defined for this purpose as domestic crude oil or domestic natural gas which is produced during any taxable year from a property which (1) is a stripper well property for the calendar year in which the taxable year begins, or (2) is a property substantially all of the production from which during such calendar year is heavy oil (i.e., oil that has a weighted average gravity of 20 degrees API or less corrected to 60 degrees Fahrenheit). A stripper well property is any oil

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[3] An independent producer is any producer who is not a "retailer" or "refiner." A retailer is any person who directly, or through a related person, sells oil or natural gas or any product derived therefrom (1) through any retail outlet operated by the taxpayer or related person, or (2) to any person that is obligated to market or distribute such oil or natural gas (or product derived therefrom) under the name of the taxpayer or the related person, or that has the authority to occupy any retail outlet owned by the taxpayer or a related person. Bulk sales of crude oil and natural gas to commercial or industrial users, and bulk sales of aviation fuel to the Department of Defense, are not treated as retail sales for this purpose. Further, a person is not a retailer within the meaning of this provision if the combined gross receipts of that person and all related persons from the retail sale of oil, natural gas, or any product derived therefrom do not exceed $5 million for the taxable year. A refiner is any person who directly or through a related person engages in the refining of crude oil, but only if such person or related person has a refinery run in excess of 50,000 barrels per day on any day during the taxable year.

[4] By contrast, for any other mineral qualifying for the percentage depletion deduction, the deduction may not exceed 50 percent of the taxpayer's taxable income from the depletable property.

[5] Amounts disallowed as a result of this rule may be carried forward and deducted in subsequent taxable years, subject to the 65-percent-of-taxable-income limitation for those years.

or gas property for which daily average production per producing oil or gas well is not more than 15 barrel equivalents in the calendar year during which the taxpayer's taxable year begins.[6] A property qualifies as a stripper well property for a calendar year only if the wells on such property were producing during that period at their maximum efficient rate of flow.

If a taxpayer's property consists of a partial interest in one or more oil- or gas-producing wells, the determination of whether the property is a stripper well property or a heavy oil property is made with respect to total production from such wells, including the portion of total production attributable to ownership interests other than the taxpayer's. If the property satisfies the requirements of a stripper well property, then that person receives the benefits of this provision with respect to its allocable share of the production from the property for its taxable year that begins during the calendar year in which the property so qualifies.

The allowance for percentage depletion on production from marginal oil and gas properties is subject to the 1,000-barrel-per-day limitation discussed above. Unless a taxpayer elects otherwise, marginal production is given priority over other production for purposes of utilization of that limitation.

Because percentage depletion, unlike cost depletion, is computed without regard to the taxpayer's basis in the depletable property, cumulative depletion deductions may be greater than the amount expended by the taxpayer to acquire or develop the property. The excess of the percentage depletion deduction over the deduction for cost depletion is generally viewed as a tax expenditure.

Intangible Drilling and Development Costs

In general, costs that benefit future periods must be capitalized and recovered over such periods for income tax purposes, rather than being expensed in the period the costs are incurred. In addition, the uniform capitalization rules require certain direct and indirect costs allocable to property to be included in inventory or capitalized as part of the basis of such property. In general, the uniform capitalization rules apply to real and tangible personal property produced by the taxpayer or acquired for resale.

Special rules apply to intangible drilling and development costs ("IDCs").[7] Under these special rules, an operator (i.e., a person who holds a working or operating interest in any tract or parcel of land either as a fee owner or under a lease or any other form of contract granting working or operating rights) who pays or incurs IDCs in the development of an oil or gas property located in the United States may elect either to expense or capitalize those costs. The uniform capitalization rules do not apply to otherwise deductible IDCs.

If a taxpayer elects to expense IDCs, the amount of the IDCs is deductible as an expense in the taxable year the cost is paid or incurred. Generally, IDCs that a taxpayer elects to capitalize may be recovered through depletion or depreciation, as appropriate; or in the case of a nonproductive well ("dry hole"), the operator may elect to deduct the costs. In the case of an integrated oil company (i.e., a company that engages, either directly or though a related enterprise, in substantial retailing or refining activities) that has elected to expense IDCs, 30 percent of the IDCs on productive wells must be capitalized and amortized over a 60-month period.[8]

A taxpayer that has elected to deduct IDCs may, nevertheless, elect to capitalize and amortize certain IDCs over a 60-month period beginning with the month the expenditure was paid or incurred. This rule applies on an expenditure-by-expendi-

[6] Equivalent barrels is computed as the sum of (1) the number of barrels of crude oil produced, and (2) the number of cubic feet of natural gas produced divided by 6,000. If a well produced 10 barrels of crude oil and 12,000 cubic feet of natural gas, its equivalent barrels produced would equal 12 (i.e., 10 + (12,000/6,000)).

[7] IDCs include all expenditures made by an operator for wages, fuel, repairs, hauling, supplies, etc., incident to and necessary for the drilling of wells and the preparation of wells for the production of oil and gas. In addition, IDCs include the cost to operators of any drilling or development work (excluding amounts payable only out of production or gross or net proceeds from production, if the amounts are depletable income to the recipient, and amounts properly allocable to the cost of depreciable property) done by contractors under any form of contract (including a turnkey contract). Such work includes labor, fuel, repairs, hauling, and supplies which are used in the drilling, shooting, and cleaning of wells; in such clearing of ground, draining, road making, surveying, and geological works as are necessary in preparation for the drilling of wells; and in the construction of such derricks, tanks, pipelines, and other physical structures as are necessary for the drilling of wells and the preparation of wells for the production of oil and gas. Generally, IDCs do not include expenses for items which have a salvage value (such as pipes and casings) or items which are part of the acquisition price of an interest in the property.

[8] The IRS has ruled that if an integrated oil company ceases to be an integrated oil company, it may not immediately write off the unamortized portion of the IDCs capitalized under this rule, but instead must continue to amortize those IDCs over the 60-month amortization period.

ture basis; that is, for any particular taxable year, a taxpayer may deduct some portion of its IDCs and capitalize the rest under this provision. This allows the taxpayer to reduce or eliminate IDC adjustments or preferences under the alternative minimum tax.

The election to deduct IDCs applies only to those IDCs associated with domestic properties.[9] For this purpose, the United States includes certain wells drilled offshore.[10]

Intangible drilling costs are a major portion of the costs necessary to locate and develop oil and gas reserves. Because the benefits obtained from these expenditures are of value throughout the life of the project, these costs would be capitalized and recovered over the period of production under generally applicable accounting principles. The acceleration of the deduction for IDCs is viewed as a tax expenditure.

Nonconventional fuels production credit

Taxpayers that produce certain qualifying fuels from nonconventional sources are eligible for a tax credit ("the section 29 credit") equal to $3 per barrel or barrel-of-oil equivalent.[11] Fuels qualifying for the credit must be produced domestically from a well drilled, or a facility treated as placed in service, before January 1, 1993.[12] The section 29 credit generally is available for qualified fuels sold to unrelated persons before January 1, 2003.[13]

For purposes of the credit, qualified fuels include: (1) oil produced from shale and tar sands; (2) gas produced from geopressured brine, Devonian shale, coal seams, a tight formation, or biomass (i.e., any organic material other than oil, natural gas, or coal (or any product thereof)); and (3) liquid, gaseous, or solid synthetic fuels produced from coal (including lignite), including such fuels when used as feedstocks. The amount of the credit is determined without regard to any production attributable to a property from which gas from Devonian shale, coal seams, geopressured brine, or a tight formation was produced in marketable quantities before 1980.

The amount of the section 29 credit generally is adjusted by an inflation adjustment factor for the calendar year in which the sale occurs.[14] There is no adjustment for inflation in the case of the credit for sales of natural gas produced from a tight formation. The credit begins to phase out if the annual average unregulated wellhead price per barrel of domestic crude oil exceeds $23.50 multiplied by the inflation adjustment factor.[15]

The amount of the section 29 credit allowable with respect to a project is reduced by any unrecaptured business energy tax credit or enhanced oil recovery credit claimed with respect to such project.

As with most other credits, the section 29 credit may not be used to offset alternative minimum tax liability. Any unused section 29 credit generally may not be carried back or forward to another taxable year; however, a taxpayer receives a credit for prior year minimum tax liability to the extent that a section 29 credit is disallowed as a result of the operation of the alternative minimum tax. The credit is limited to what would have been the regular tax liability but for the alternative minimum tax.

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[9] In the case of IDCs paid or incurred with respect to an oil or gas well located outside of the United States, the costs, at the election of the taxpayer, are either (1) included in adjusted basis for purposes of computing the amount of any deduction allowable for cost depletion or (2) capitalized and amortized ratably over a 10-year period beginning with the taxable year such costs were paid or incurred.

[10] The term "United States" for this purpose includes the seabed and subsoil of those submerged lands that are adjacent to the territorial waters of the United States and over which the United States has exclusive rights, in accordance with international law, with respect to the exploration and exploitation of natural resources (i.e., the Continental Shelf area).

[11] A barrel-of-oil equivalent generally means that amount of the qualifying fuel which has a Btu (British thermal unit) content of 5.8 million.

[12] A facility that produces gas from biomass or produces liquid, gaseous, or solid synthetic fuels from coal (including lignite) generally will be treated as being placed in service before January 1, 1993, if it is placed in service by the taxpayer before July 1, 1998, pursuant to a written binding contract in effect before January 1, 1997. In the case of a facility that produces coke or coke gas, however, this provision applies only if the original use of the facility commence with the taxpayer. Also, the IRS has ruled that production from certain post-1992 "recompletions" of wells that were originally drilled prior to the expiration date of the credit would qualify for the section 29 credit.

[13] If a facility that qualifies for the binding contract rule is originally placed in service after December 31, 1992, production from the facility may qualify for the credit if sold to an unrelated person before January 1, 2008.

[14] The inflation adjustment factor for the 1999 taxable year 2.0013. Therefore, the inflation-adjusted amount of the credit for that year was $6.00 per barrel or barrel equivalent.

[15] For 1999, the inflation adjusted threshold for one set of the phaseout of $47.03 ($23.50 x 2.0013) and the average wellhead price for that year was $15.56.

This provision provides a significant tax incentive (currently about $6 per barrel of oil equivalent or $1 per thousand cubic feet of natural gas, or roughly half the wellhead price of gas) for production of nonconventional fuels. Coalbed methane and gas from tight formations currently account for most of the credit.

Enhanced oil recovery credit

Taxpayers are permitted to claim a general business credit, which consists of several different components. One component of the general business credit is the enhanced oil recovery credit. The general business credit for a taxable year may not exceed the excess (if any) of the taxpayer's net income over the greater of (1) the tentative minimum tax, or (2) 25 percent of so much of the taxpayer's net regular tax liability as exceeds $25,000. Any unused general business credit generally may be carried back three taxable years and carried forward 15 taxable years.

The enhanced oil recovery credit for a taxable year is equal to 15 percent of certain costs attributable to qualified enhanced oil recovery ("EOR") projects undertaken by the taxpayer in the United States during the taxable year. To the extent that a credit is allowed for such costs, the taxpayer must reduce the amount otherwise deductible or required to be capitalized and recovered through depreciation, depletion, or amortization, as appropriate, with respect to the costs. A taxpayer may elect not to have the enhanced oil recovery credit apply for a taxable year.

The amount of the enhanced oil recovery credit is reduced in a taxable year following a calendar year during which the annual average unregulated wellhead price per barrel of domestic crude oil exceeds $28 (adjusted for inflation since 1990).[16] In such a case, the credit would be reduced ratably over a $6 phaseout range.

For purposes of the credit, qualified enhanced oil recovery costs include the following costs which are paid or incurred with respect to a qualified EOR project: (1) the cost of tangible property which is an integral part of the project and with respect to which depreciation or amortization is allowable; (2) IDCs that the taxpayer may elect to deduct;[17] and (3) the cost of tertiary injectants with respect to which a deduction is allowable, whether or not chargeable to capital account.

A qualified EOR project means any project that is located within the United States and involves the application (in accordance with sound engineering principles) of one or more qualifying tertiary recovery methods which can reasonably be expected to result in more than an insignificant increase in the amount of crude oil which ultimately will be recovered. The qualifying tertiary recovery methods generally include the following nine methods: miscible fluid displacement, steam-drive injection, microemulsion flooding, in situ combustion, polymer-augmented water flooding, cyclic-steam injection, alkaline flooding, carbonated water flooding, and immiscible non-hydrocarbon gas displacement, or any other method approved by the IRS. In addition, for purposes of the enhanced oil recovery credit, immiscible non-hydrocarbon gas displacement generally is considered a qualifying tertiary recovery method, even if the gas injected is not carbon dioxide.

A project is not considered a qualified EOR project unless the project's operator submits to the IRS a certification from a petroleum engineer that the project meets the requirements set forth in the preceding paragraph.

The enhanced oil recovery credit is effective for taxable years beginning after December 31, 1990, with respect to costs paid or incurred in EOR projects begun or significantly expanded after that date.

Conventional oil recovery methods do not recover all of a well's oil. Some of the remaining oil can be extracted by unconventional methods, but these methods are generally more costly and uneconomic at current world oil prices. In this environment, the EOR credit can increase recoverable reserves. Although recovering oil using EOR methods is more expensive than recovering it using conventional methods, it may be less expensive than producing oil from new reservoirs. Although the credit could phase out at higher oil prices, it is fully effective at present world oil prices.

Alternative minimum tax

A taxpayer is subject to an alternative minimum tax ("AMT") to the extent that its tentative minimum tax exceeds its regular income tax liability. A corporate taxpayer's tentative minimum tax generally equals 20 percent of its alternative minimum taxable income in excess of an exemption amount. (The marginal AMT rate for a noncorporate taxpayer is 26 or 28 percent, depending on the amount of its al-

[16] The average per-barrel price of crude oil for this purpose is determined in the same manner as for purposes of the section 29 credit.

[17] In the case of an integrated oil company, the credit base includes those IDCs which the taxpayer is required to capitalize.

ternative minimum taxable income above an exemption amount.) Alternative minimum taxable income ("AMTI") is the taxpayer's taxable income increased by certain tax preferences and adjusted by determining the tax treatment of certain items in a manner which negates the deferral of income resulting from the regular tax treatment of those items.

As a general rule, percentage depletion deductions claimed in excess of the basis of the depletable property constitute an item of tax preference in determining the AMT. In addition, the AMTI of a corporation is increased by an amount equal to 75 percent of the amount by which adjusted current earnings ("ACE") of the corporation exceed AMTI (as determined before this adjustment). In general, ACE means AMTI with additional adjustments that generally follow the rules presently applicable to corporations in computing their earnings and profits. As a general rule a corporation must use the cost depletion method in computing its ACE adjustment. Thus, the difference between a corporation's percentage depletion deduction (if any) claimed for regular tax purposes and its allowable deduction determined under the cost depletion method is factored into its overall ACE adjustment.

Excess percentage depletion deductions related to crude oil and natural gas production are not items of tax preference for AMT purposes. In addition, corporations that are independent oil and gas producers and royalty owners may determine depletion deductions using the percentage depletion method in computing their ACE adjustments.

The difference between the amount of a taxpayer's IDC deductions and the amount which would have been currently deductible had IDCs been capitalized and recovered over a 10-year period may constitute an item of tax preference for the AMT to the extent that this amount exceeds 65 percent of the taxpayer's net income from oil and gas properties for the taxable year (the "excess IDC preference"). In addition, for purposes of computing a corporation's ACE adjustment to the AMT, IDCs are capitalized and amortized over the 60-month period beginning with the month in which they are paid or incurred. The preference does not apply if the taxpayer elects to capitalize and amortize IDCs over a 60-month period for regular tax purposes.

IDCs related to oil and gas wells are generally not taken into account in computing the excess IDC preference of taxpayers that are not integrated oil companies. This treatment does not apply, however, to the extent it would reduce the amount of the taxpayer's AMTI by more than 40 percent of the amount that the taxpayer's AMTI would have been if those IDCs had been taken into account.

In addition, for corporations other than integrated oil companies, there is no ACE adjustment for IDCs with respect to oil and gas wells. That is, such a taxpayer is permitted to use its regular tax method of writing off those IDCs for purposes of computing its adjusted current earnings.

Absent these rules, the incentive effect of the special provisions for oil and gas would be reduced for firms subject to the AMT. These rules, however, effectively eliminate AMT concerns for independent producers.

Passive activity loss and credit rules

A taxpayer's deductions from passive trade or business activities, to the extent they exceed income from all such passive activities of the taxpayer (exclusive of portfolio income), generally may not be deducted against other income.[18] Thus, for example, an individual taxpayer may not deduct losses from a passive activity against income from wages. Losses suspended under this "passive activity loss" limitation are carried forward and treated as deductions from passive activities in the following year, and thus may offset any income from passive activities generated in that later year. Losses from a passive activity may be deducted in full when the taxpayer disposes of its entire interest in that activity to an unrelated party in a transaction in which all realized gain or loss is recognized.

An activity generally is treated as passive if the taxpayer does not materially participate in it. A taxpayer is treated as materially participating in an activity only if the taxpayer is involved in the operations of the activity on a basis which is regular, continuous, and substantial.

A working interest in an oil or gas property generally is not treated as a passive activity, whether or not the taxpayer materially participates in the activities related to that property. This exception from the passive activity rules does not apply if the taxpayer holds the working interest through an entity which limits the liability of the taxpayer with respect to the interest. In addition, if a taxpayer has any loss for any taxable year from a working interest in an oil or gas property which is treated

[18] This provision applies to individuals, estates, trusts, personal service corporations, and closely held C corporations.

pursuant to this working interest exception as a loss which is not from a passive activity, then any net income from such property (or any property the basis of which is determined in whole or in part by reference to the basis of such property) for any succeeding taxable year is treated as income of the taxpayer which is not from a passive activity.

Similar limitations apply to the utilization of tax credits attributable to passive activities. Thus, for example, the passive activity rules (and, consequently, the oil and gas working interest exception to those rules) apply to the nonconventional fuels production credit and the enhanced oil recovery credit. However, if a taxpayer has net income from a working interest in an oil and gas property which is treated as not arising from a passive activity, then any tax credits attributable to the interest in that property would be treated as credits not from a passive activity (and, thus, not subject to the passive activity credit limitation) to the extent that the amount of the credits does not exceed the regular tax liability which is allocable to such net income.

As a result of this exception from the passive loss limitations, owners of working interests in oil and gas properties may use losses from such interests to offset income from other sources.

Tertiary injectants

Taxpayers are allowed to deduct the cost of qualified tertiary injectant expenses for the taxable year. Qualified tertiary injectant expenses are amounts paid or incurred for any tertiary injectant (other than recoverable hydrocarbon injectants) which is used as a part of a tertiary recovery method.

The provision allowing the deduction for qualified tertiary injectant expenses resolves a disagreement between taxpayers (who considered such costs to be IDCs or operating expenses) and the IRS (which considered such costs to be subject to capitalization).

Administration proposals to support domestic oil and gas production

In order to insulate the economy from the effects of future energy price increases, the President announced, on March 18, 2000, a comprehensive and balanced energy strategy that included tax incentives. This comprehensive approach includes, in addition to tax incentives for energy efficiency and renewable and alternative energy sources, support for domestic oil producers to reduce our reliance on oil imports.

Expensing of Geological and Geophysical Costs. The Administration is proposing to support domestic exploration and production by adjusting the tax treatment of the costs of exploration and development 68 geological and geophysical (G&G) costs. Under current law, geological and geophysical costs may be deducted in the year in which they are paid or incurred if exploration activity was unsuccessful, but must be capitalized if the exploration activity was successful. By allowing the industry to expense these costs, we will be encouraging the discovery of new reserves. The Department of Energy estimates that this G&G provision will add 230 million barrels of oil to domestic reserves. The revenue cost of expensing G&G costs is estimated to be $380 million over FY 2001–2005.

Allowing Expensing of Delay Rental Payments. A delay rental payment is an amount paid by a lessee to the lessor of a petroleum resource when the lessee does not begin producing commercial quantities of oil or natural gas as soon as was agreed to. The delay rental payment is intended to compensate the lessor for the royalties he does not receive while production is delayed. Currently, the uniform capitalization rules of section 263A would appear to require delay rental expenses to be capitalized to the depletable basis of the property to which they relate if the property is being held for development. Allowing producers to expense delay rental payments will lower the cost of doing business on Federal lands. The revenue cost of expensing delay rental payments is estimated to be $370 million over FY 2001–2005.

CONCLUSION

The Administration strongly supports the proposed tax credits for holders of Better America Bonds, a permanent extension of the current deduction of brownfields remediation expenses, the proposed tax incentives to improve energy efficiency and the environment, and the proposed tax incentives to support domestic oil and gas production.

The proposed Better America Bonds provide a new financing tool that will enable State, local, and tribal governments to preserve green spaces, create and restore urban parks, protect water quality and clean up brownfields. Those governments would be authorized to issue a total of $10.75 billion of Better America Bonds to finance environmental and conservation projects. The proposed permanent extension

of the current deduction of brownfields remediation costs will help return industrial and commercial sites in targeted areas to productive use. The proposal is estimated to induce an additional $7 billion in private investment and return an additional 18,000 brownfields to productive use over the next ten years. Together, these initiatives will help to preserve our environmental heritage and make our communities more livable in the 21st century.

The Administration's proposed package of tax incentives for energy efficiency and the environment is designed to improve energy efficiency by encouraging purchases of items that offer superior energy efficiency or that use renewable or alternative energy sources. The investments induced by the tax incentives would produce energy savings for many years after the investments are undertaken. The benefits of the proposal should increase significantly in the years beyond the ten-year budget window, through the transformation of markets after the credits are no longer in effect. Moreover, the proposed incentives also may generate other benefits to society, such as cleaner air.

The proposed tax incentives to support domestic oil and gas production will reduce tax burdens on domestic producers and encourage the discovery and exploitation of additional domestic oil and gas reserves.

In conclusion, Mr. Chairman, we believe that the Administration's proposed tax initiatives represent sound policy that can produce significant environmental and energy security benefits over the next ten years and for decades to come. The proposals represent investments that will generate long-term benefits for the Nation. We look forward to working with the Congress on these initiatives.

Mr. Chairman, this concludes my prepared testimony. I will be pleased to answer any questions you or other members of the Subcommittee may have.

Prepared Statement of Jerry Townsend

Mr. Chairman and Senator Baucus it is indeed an honor for me to appear before you today to talk about private land conservation. On behalf of the Montana Land Reliance, I thank you for taking up this important issue and add special thanks to Senator Baucus for the invitation to be here today.

I am a rancher. I was born and raised on my family's ranch in the Highwood mountains of North Central Montana. I have been operating the ranch since purchasing it from my parents in 1974. On the Elk Run Ranch we raise commercial beef cattle and provide recreational hunting. I donated a conservation easement to the Montana Land Reliance in 1995.

Farming and ranching is a critical part of the cultural heritage that makes Montana such a special place to live. And it's in trouble.

Over the past twenty-five years, over 3 million acres of agricultural land have been lost to development in Montana alone. Many of these acres were lost when family farms, hit hard by tough times, chose to give-up their generations old farming operations and sold to developers in order to pay their outstanding debts.

Just this past Friday, the following headline appeared in daily newspapers across Montana. It read: "Texas firm plans buying Butte [Montana] ranch."

According to the article, the 1,135-acre Sterling Canyon Ranch will become the property of Tex-Star Development and Building Inc. It will be turned into luxury resort complete with high-end homes.

Today, I want to visit with you briefly about a policy initiative we've been working on with Senator Baucus, that could have a dramatic, positive impact on protecting open space, conserving private land and enriching the farm and ranch heritage that is such an important part of who we are as a people.

The measure will expand the current conservation easement tax incentive program with an eye toward making the system work better for the bulk of real, working farmers and ranchers who would like to preserve their land for future generations but for whom the current system does not provide any meaningful incentive.

Before I give you an overview of the proposal, I'd like to give you some background on the work of the Montana Land Reliance.

The Montana Land Reliance is a private, non-profit land trust that utilizes conservation easements to permanently protect Montana's private lands. Founded in 1978, The Montana Land Reliance has been able, with the help of over 380 landowners, to protect just over 365,000 acres in Montana. This represents roughly 20 percent of all protected land by local or regional land trusts across the entire United States. This protected land includes 700 miles of stream and river frontage, over 140,000 acres of elk habitat, over 7,000 acres of wetlands and nearly 142,000 acres in the Greater Yellowstone Ecosystem (land that surrounds Yellowstone National Park).

All of this protection has been done with private conservation easements, typically with ranchers and farmers. At this point in The Montana Land Reliance's existence, we're finding that Montana's private landowners are facing incredible economic, estate and social pressures to develop their land. A vast majority are what we like to call "land rich, but cash poor." They typically hold a tremendous resource that they can't afford to keep. We need to find additional tools to help them keep their land in agricultural production and enable them to pass it on to their children. The average Montana farmer and rancher is my age, mid 50's, so time is of the essence.

So, how do we turn this around?

We believe the current tax code can be amended in a simple but meaningful way to significantly enhance private conservation efforts in Montana.

First, we proposed the creation of a tax credit to allow qualified farm and ranch filers to get a tax credit for donating a conservation easement to a qualified land trust. Put simply, the current system of deduction from gross income provides little real incentive for working farm and ranch households to place a conservation easement on their property. The issue is income. Too often, farmers and ranchers do not have an income level that allows them to use the current statutory deduction.

The relatively small deduction they can currently obtain by donating a conservation easement does not in any way equate to either the potential income they have forfeited or the value the public has gained from the donation. As a result, fewer and fewer farmers and ranchers are donating conservation easements and protecting their land for future generations. We've already creamed the crop, so to speak, under current law.

In our view, a tax credit would turn this around in short order. By providing a non-refundable tax credit to qualified farm and ranch filers we can more adequately provide fair treatment of their donation and can significantly enhance efforts to conserve critical farm and ranch lands.

By the way, to protect against abuse, the current legislation provides for a cap on the total tax credit available under the program and has a requirement that only filers with a majority of their income from farm and ranch operations would qualify for the credit.

Second, we believe it is important to level the playing field for all types of corporations. As you know, many farm and ranch operators do business as C-Corporations. Current law only allows C-Corps to deduct 10 percent of their income compared to the 30% allowed for other business types including Limited Liability Companies, Sole Proprietorships and Limited Liability Partnerships.

This affected me personally as my ranch operates as a C-Corporation. To give you an idea of the inadequacy of current law, my donative value was $524,000. In five years, I have only been able to save $1,858 in federal taxes. This savings does not even cover the cost of my appraisal which was about $2,500.

The Montana Land Reliance estimates that in Montana alone there are 40,000 acres of land in the hands of operators using the C-Corp structure who have already identified to us that the 10% limit is a barrier to their contributing an easement.

Third, we propose Congress eliminate the 25 mile radius provision that provides additional estate tax relief to landowners only within a 25 mile radius of a metropolitan area.

Current law provides that if a landowner entering into a conservation easement for land within 25 miles of a statistical metropolitan area or designated wilderness area, or within 10 miles of an urban national park, is eligible to receive an additional $300,000 in estate tax relief in the year 2000, increasing by increments of $100,000 each year to a cap of $500,000 per landowner in 2002.

Estate tax is a significant issue for many farm and ranch households. However, because of our sparse population, particularly in Eastern Montana, few Montana ranchers qualify under the 25-mile radius provision.

Elimination of the radius will be a significant improvement to current law and will at the same time enable many rural farmers and ranchers to pass along their heritage to future generations and protect the land from development forever.

Taken as a whole, we believe this set of policy initiatives would increase participation in voluntary conservation easement programs in Montana by perhaps 100% within the first year of enactment.

All of these tools can be added to the current conservation easement law. These ideas are simple, private enterprise solutions that we believe will have an immediate, positive impact on private land conservation in Montana.

We believe encouraging private land conservation efforts is the right thing to do, and we sincerely thank you for taking a leadership role on this important issue. Here we have an opportunity to provide landowners and the land trust community with the tools needed to take a meaningful step forward in preserving the very heart of America.

COMMUNICATIONS

STATEMENT OF THE BOND MARKET ASSOCIATION

The Bond Market Association appreciates the opportunity to comment on the impact of tax laws on land use, conservation, and preservation, and in particular, on issues related to innovative financing for public projects. The Bond Market Association represents approximately 200 securities firms and banks that underwrite, trade, and sell debt securities both domestically and internationally.

We are pleased Chairman Hatch has chosen to explore ways to encourage land conservation and preservation using innovative financing solutions. The Community Open Space Bonds Act (S.1558) authored by Sen. Max Baucus and Chairman Hatch is one such example. The legislation would authorize issuance of tax-credit bonds, a new public financing structure that seeks to substitute tax credits for interest payments.

The Bond Market Association generally supports policy initiatives designed to leverage private capital and provide innovative financing solutions to policy issues. In this statement we focus on the structure of tax-credit bonds from a capital markets perspective, including for Community Open Space Bonds (COSB) and for other tax-credit bond proposals.

THE BACKGROUND OF TAX CREDIT BONDS

In a traditional debt financing, bond investors (lenders) earn periodic interest income paid by bond issuers (borrowers). In contrast, buyers of tax-credit bonds earn the ability to claim federal income tax credits which are designed to be in lieu of interest payments by bond issuers. The amount of the credit is equal to a credit rate set daily by the Treasury Department times the amount of tax-credit bonds an investor holds. If tax-credit bonds work as designed, issuers should receive zero-cost financing on their borrowing. Theoretically, all the return earned by investors results from the tax credit. The Taxpayer Relief Act of 1997 authorized $800 million of tax-credit bonds over two years in the form of Qualified Zone Academy Bonds (QZABs). Congress later reauthorized and extended the program through 2001. QZABs are designed to subsidize borrowing by targeted public school districts to finance improvements to school infrastructure.

Tax-credit bonds, despite their limitations, have the potential to provide deep subsidies to state and local government borrowers. Although in most instances tax-credit bonds have not lived up to their promise of offering zero-cost financing, they provide a lower cost of capital for states and localities than any other available source except for direct grants. Still, the structure could be improved significantly by adopting several targeted changes.

PROBLEMS WITH CURRENT QZABS

In order to be successful and offer states and localities the lowest possible cost of borrowing, tax-credit bonds for land conservation or greenspace preservation should be appealing to investors and other capital markets participants. The success of QZABs under current law has been hampered by several elements of their structure.

The timing of tax-credits may be mismatched. A QZAB investor earns the ability to take an annual credit on the anniversary date of a bond's issuance. However, the credit becomes economically valuable to the investor only when it has the effect of reducing a tax payment, and that occurs only on a day when an investor is required to make a federal tax payment. For some investors, tax payment dates occur only once per year. The mismatch in timing between the time a credit is earned and the time it generates a cash flow for the investor can significantly reduce the value of the credit.

The program is small. Congress has authorized only $400 million of QZAB issuance per year for four years, only a small portion of which has actually been used. This $1.6 billion amount is allocated among all the states, so any one state receives a relatively small allocation. The small size and short term of the program results in several problems. First, it is difficult for bond issuers, attorneys, underwriters, investors and others associated with municipal bond transactions to commit resources to developing expertise on a new and unknown financing vehicle when very little issuance will be permitted to take place. Second, the small issuance volume has resulted in no significant secondary market for QZABs. A lack of market liquidity discourages investors and raises costs for issuers.

Investors are limited. Only three classes of investors are permitted to earn federal income tax credits by holding QZABs: banks, insurance companies and "corporations actively engaged in the business of lending money." Individual investors, a potentially strong source of demand for tax-preferred investments, are excluded as QZAB investors. Recently proposed changes to the program would open the market for QZABs to other investors, including individuals.

CHANGES TO THE STRUCTURE OF TAX-CREDIT BONDS IN S. 1558

The structure of the tax-credit bonds provided for in the Community Open Space Bonds Act include a number of positive changes from the original QZABs program. Some key improvements in S.1558 include:

Strippability. Under S. 1558, it would be possible to strip the tax credit from the underlying debt instrument and market the tax credit separately. This change would help ensure that those investors who bought and held the credit would be those most likely to actually incur a tax liability over the term of the credit, and would help ensure that the credit is priced more efficiently. It would also permit the debt portions of tax-credit bonds to be sold to tax-exempt investors such as pension funds. A similar stripping provision applied to traditional tax-exempt bonds would improve pricing and efficiency in that market, as well.

Quarterly credit dates. Under S. 1558, credit accrual dates would be quarterly and would be timed to match quarterly estimated tax payment dates. This would help minimize a mismatch in timing between when a tax credit accrues and when it generates a cash flow for an investor. S. 1558 also allows the credits to be carried forward up to five years.

Transferability. Under S. 1558, there would be no limit on the transferability of the credit through sale and repurchase. Moreover, an investor would need to hold a bond only on the allowances date in order to qualify for the credit that quarter. This would permit an investor who had no tax liability in a given period to "repo out" a tax-credit bond—sell the bond temporarily to another investor at a price that reflects the value of the tax credit—and still benefit from the credit.

Exemption from "arbitrage" restrictions. Under S. 1558, COSB issuers generally would not be required to limit the return on the investment of bond proceeds if invested in Treasury securities and spent within 36 months or, in the case of sinking fund balances, invested in state and local government securities. Issuers would not be required to rebate arbitrage earnings to the federal government if the COSBs are invested this way for no more than 36 months. This would substantially reduce the costs of projects financed with tax-credit bonds. Arbitrage restrictions applied to traditional municipal bonds have resulted in uneconomic incentives and have imposed significant compliance costs on states and localities.

No Limit on Investors: S. 1558 places no restrictions on who is able to hold a COSB and claim the corresponding credit, thus effectively expanding the market for the bonds compared to other current law.

ADDITIONAL ISSUES AND RECOMMENDATIONS

Despite these significant improvements to the tax-credit bond structure in the Community Open Space Bonds Act, there remain significant limitations that would erode the value of tax-credit bonds and increase costs to school districts and other issuers. These include:

Consequences of issuer violations. The bill includes a provision for cases where an issuer fails to comply with the conditions of the program while bonds remain outstanding. The only remedy in such a case would be to rescind the ability of investors to claim credits for the bonds in question.

This provision would impose risks on investors and would hamper the success of tax-credit bonds. Similar risks exist for investors in tax-exempt municipal bonds. The tax risk for tax-credit bond investors, however, is greater than for tax-exempt bonds. With a tax-exempt bond, only a portion of an investor's after-tax return results from the tax preference. If the tax-exemption on a municipal bond issue were

repealed, investors would still earn a cash flow from the bond's issuer, albeit at a much lower after-tax return than originally anticipated. For tax-credit bonds, all the return earned by investors results from the tax preference. If the tax preference were rescinded, investors' rates of return would fall to zero.

It is unreasonable to impose a penalty—the loss of tax credits—on investors who have no control over issuer compliance with the terms of the program. The tax-credit bond structure should be amended so that in cases of issuer violations of the terms of the program, the government's only course of remedy would be against bond issuers. Investors should not be subject to penalties for violations they did not commit.

A credit-recapture provision in S.1558 requires issuers whose bonds fall out of compliance with the terms of the Community Open Space Bonds Act to repay the tax credit amount for the three preceding years. Investors would face potential liability to reimburse tax credits under the Community Open Space Bonds Act, but they would still see their return fall to zero.

Secondary market. The overall size of the COSB program would result in relatively small and illiquid secondary markets. ("Secondary market" refers to the buying and selling of securities after they are issued. "Liquidity" refers to the ease with which an investor can buy or sell a bond on the secondary market.) The bill would authorize $1.9 billion of COSB issuance per year for five years. In the context of the capital markets overall, however, this is a relatively small volume of issuance, especially given the novelty of the financing structure.

In contrast, there are approximately $1.5 trillion of traditional municipal bonds currently outstanding. As in any market with a small total outstanding volume of securities, the relatively small size of the tax-credit bond market would ensure that little secondary market trading took place. Tax-credit bonds would be illiquid instruments. As a result, investors would demand a liquidity premium, or a higher rate of return from bond issuers to compensate for the risk and cost of illiquidity. Short of authorizing substantially higher levels of tax-credit bond issuance—an impractical policy—the ability to mitigate this effect is limited. One possible remedy would be to encourage states and localities to employ pooled financing arrangements in order to generate larger bond issue sizes.

Federal Role in Local Financing. Tax-credit bonds would impose a significantly greater degree of federal control over the state and local financing process than bond issuers currently face. In the case of COSBs, a federally appointed board would be required to approve each and every project proposal before the project could receive tax-credit bond issuance authorization. This is not currently a federal requirement for state and local projects receiving tax-exempt financing. This requirement would add significant complexity and cost to the financing process. COSBs would also be subject to restrictions on issuance volume, which would obviously limit their value to states and localities that do not receive issuance authorization sufficient to meet financing needs. If the COSB proposal is enacted, we urge Congress to include broad guidelines as to the types of projects eligible for financing, but to strike requirements that federal agencies be required to approve financing plans.

Arbitrage limitations. As stated above, COSBs would be generally exempt from arbitrage restrictions that apply to traditional tax-exempt bonds as long as bond proceeds were invested in government securities or sinking funds were invested in special Treasury securities known as State and Local Government Series (SLGS). While this type of exemption certainly improves the attractiveness of tax-credit bonds to issuers, tax-credit bond proposals are vague with respect to the application of certain aspects of the arbitrage exemptions. For example, S. 1558 would require that issuers spend at least 95 percent of the proceeds of a tax-credit bond issue on qualified projects. However, the proposal does not directly address the question of whether the other five percent of the proceeds could be invested in SLGS as the nucleus of a sinking fund used to retire the principal on the bonds when due. The proposal is also vague regarding the question of whether a state or local government could combine a COSB issue with a traditional tax-exempt bond issue and use the proceeds of the tax-exempt bond to invest in SLGS and defease the COSB when it is issued. The COSB proposal would be strengthened if both of these structures were explicitly permitted.

Additional issues. Market participants have identified other limitations of pending tax-credit bond proposals that COSBs share. The features would tend to limit their attractiveness to bond issuers. Many of these appear to be purposeful limitations designed to restrict or target the level of subsidy associated with tax-credit bonds. The following are three examples:

- The credit rate for COSBs would be set monthly and would be based on yields on corporate bonds rather than taxable municipal bonds. The interest rate

should be continuously set to reflect as best as possible current conditions in the credit markets.

- The maximum maturity for COSBs would be limited to 15 years, whereas many public infrastructure projects currently are financed with debt up to 30 years in maturity and sometimes even longer.
- The tax-credit itself would be treated as taxable income, which would make the instruments less attractive to targeted investors.

RELATED LEGISLATION

Bills introduced in the House (H.R. 1863) and Senate (S. 1085) propose an additional innovative financing techniques to facilitate access to capital markets for land conservation. The Senate included this legislation as part of the Taxpayer Relief Act of 1999, though it was not in the conference report ultimately vetoed by President Clinton. Under the bill, tax-exempt revenue bonds could be issued to finance the purchase of forest and agricultural lands by non-profit 501(c)(3) organizations. Government entities would issue the bonds on behalf of the non-profit organization, and the non-profit would typically obtain the ownership rights to the property. The benefits of this innovative approach would be several. First, local communities will be able to ensure that renewable resources will be protected by partnering with non-profit entities to acquire land that would otherwise be too expensive to finance. Second, non-profit entities could manage the renewal process of the land and collect revenues from the harvesting of the resources to pay for bonds issued to finance the land acquisition, thereby ensuring the conservation of the land for the long term. Meanwhile, original landowners would be compensated for the sale of their land at fair market values. Finally, the federal government would not take ownership of the land, so ownership would stay in the private sector.

CONCLUSIONS AND RECOMMENDATIONS

The Bond Market Association supports the use of creative financing mechanisms that allow states and localities to leverage the capital markets to address policy issues. In this respect, we believe that tax-credit bonds could potentially provide an attractive form of federal assistance to states and localities to help finance capital investment. Most important, tax-credit bonds could potentially give issuers a lower cost of capital than they could achieve with any other instrument. However, a key element of the proposal—the ability of the IRS to rescind the tax credit in cases of issuer violations—would impose undue risks on tax-credit bondholders. If Congress considers tax-credit bonds, we urge the adoption of an amendment to hold bondholders harmless in cases of issuer violations. In addition, we recommend that the proposal be amended with respect to the treatment of sinking funds under arbitrage limitations as specified above.

STATEMENT OF ENVIRONMENTAL DEFENSE ON TAX INCENTIVES FOR CONSERVATION

Endangered species need a tax break. Or, more correctly, private landowners who provide habitat or who could provide habitat for endangered and rare wildlife need a tax break. Let me explain.

When most people think of protecting endangered species, they think of protecting remote areas, far away from human influence, and leaving those areas in a natural state. Yet, in terms of America's rarest species, such a view is largely a myth. In fact, most rare wildlife in the United States rely heavily on private lands—lands that are often used for ranching, agriculture, timber production, or other uses. Moreover, most of our endangered species are threatened by habitat loss. Thus, if we are to recover such species, we need to restore and manage privately owned habitat.

Whether it's utilizing prescribed fire to improve grasslands for threatened Utah prairie dogs, drilling artificial nest cavities for endangered red-cockaded woodpeckers, or restoring coastal prairies for Attwater's prairie chicken, restoring and managing habitat can be quite costly. Yet, nothing in the Endangered Species Act requires any landowner to proactively manage their lands for the benefit of endangered species. Yes, the Act does prohibit destruction of occupied habitat. But, it does little to reward private landowners who manage their lands so as to improve conditions for endangered species. And, it is these landowners and the endangered species who depend upon their stewardship who need a tax break.

Many good ideas to reward and encourage conservation through tax changes have been suggested. We urge particular attention to the following three:

Defer that Portion of the Estate Tax Subject to a Conservation Agreement Benefiting Endangered Species

In 1995, the Keystone Center convened a diverse group to examine incentives for private landowners to conserve endangered species. The group included people from environmental organizations, the forest products industry, agriculture, mining, and other interests. The first of several unanimous recommendations agreed to was a change in the federal estate tax. Although Congress is currently considering other, more sweeping changes in the estate tax, the recommendation of the Keystone Center Report remains sound, and remains one that can work with or without other changes in the estate tax.

The recommendation is intended to eliminate the perverse incentive that federal estate taxes create for destroying endangered species habitat. Heirs, as you know, can be forced to harvest timber, sell or subdivide properties in order to pay estate tax. From the perspective of wildlife conservation, this can be devastating. The Keystone recommendation would give landowners the opportunity to reduce the estate tax burden in return for voluntarily entering into revocable agreements to manage their lands in ways that benefit endangered species. To qualify, the owner (prior to death) or the executor (after the owner's death) would have to enter into a written agreement with the Secretary of the Interior (or a state fish and game agency if a suitable agreement between the Secretary and the state agency existed) to manage land in a way that provided significant benefits to endangered species. Such management could include lengthened timber rotations, improved grazing practices, restoration of native plant species, or other measures beneficial to rare wildlife and not otherwise required by law. If the heirs subsequently cease to honor the conservation agreement or dispose of the property without securing the agreement of the new owners to continue the conservation agreement, then they are liable for the taxes due.. In this manner, heirs can effectively defer for as long as they wish the estate tax otherwise due on a parcel of land. By maintaining the conservation agreement indefinitely, landowners could escape the estate tax on the property altogether.

Former Senators Chafee and Kempthorne urged enactment of the foregoing idea in 1997. It was a sound recommendation then and it remains so today.

Allow for the Deduction from Income of Expenses Incurred in Implementing Measures to Conserve Endangered Species

As noted above, management measures needed to aid in the conservation of imperiled wildlife are costly, often very costly. They are, moreover, almost by definition measures that would not ordinarily be undertaken for economic reasons—otherwise the species that benefit from them would not be imperiled. Aldo Leopold's observation of more than half a century ago is as true today as when he made it: "the private owner who today undertakes to conserve beauty on his land, does so in defiance of all man-made economic forces from taxes down—or up." But it does not have to be that way. Congress can make it less costly for the landowner who wants to be a good steward, and who is willing to do the sorts of things that are not ordinarily done for economic reasons. It can, for example, allow for the deduction from income of costs incurred in implementing measures to conserve endangered species. The landowner will still bear most of the cost of such measures, but by allowing the deductibility of such expenses, some of the cost will be shared with the general public, who are the ultimate beneficiaries of such measures.

This too is a recommendation unanimously made by the diverse participants in the 1995 Keystone Center report. Congress ought to embrace it.

Exclude Cost-Share Payments to Landowners Under the Partners for Fish and Wildlife Program from Taxable Income

The "Partners for Fish and Wildlife Program" is a small, but important U.S. Fish and Wildlife Service program that provides cost-sharing assistance to private landowners for the restoration of wetlands, riparian areas, native prairie, and other wildlife habitats. To date, over 21,000 landowners have participated voluntarily in the program, restoring more than 464,000 acres of wetlands and more than 447,000 acres of upland habitats. The Partners program enjoys the enthusiastic support of farmers, other rural landowners and the environmental community. In fiscal year 2000, about $31 million is available through the program.

In 1978, Congress added a provision to the tax code (section 126) that makes a portion of cost-share payments to landowners under a variety of conservation programs eligible for exclusion from taxable income. The Partners for Wildlife Program did not yet exist then, and thus it was not among the programs specifically enumerated in section 126. In addition to the specifically enumerated programs, however, section 126(a)(10) authorized the exclusion from income of a portion of cost-share payments made pursuant to "substantially similar" programs administered by the

Secretary of Agriculture. Under that authority, various programs not specifically enumerated in section 126 have been determined to be: within the scope of section 126 (e.g., WRP, EQIP, and WHIP, and the Forest Service's Stewardship Incentive Program). Although the Partners for Fish and Wildlife Program is substantially similar to many of the programs eligible for the exclusion, it does not qualify for the exclusion because it is administered by the Secretary of Interior rather than the Secretary of Agriculture.

Because of the wide support for the Partners for Fish and Wildlife Program, its low cost, and the fact that payments under other conservation cost-share programs can be excluded from income, section 126 ought to be updated to include the Partners Program. The simplest and best way to do this is to add the Partners Program to the list of programs specifically enumerated in section 126. This recommendation enjoys virtually universal support among both environmental and landowner organizations, including the American Farm Bureau Federation, the National Cattlemen's Beef Association and the National Woodland Owners Association. Because the Partners Program is quite small, the cost to the Treasury of this change is miniscule.

STATEMENT OF ART HARWOOD, PRESIDENT & CEO OF HARWOOD LUMBER PRODUCTS

RE. S. 1085

Mr. Chairman and members of the Subcommittee. My name is Art Harwood. I am the President and CEO of Harwood Products, a family owned sawmill located in Branscomb, Mendocino County, California. Harwood Products employs 270 people and has annual sales of $70,000,000. The last sentence of the Harwood Vision Statement states; "We are creating a system of sustained development, which fosters equilibrium with our people, resources and environment." The fact that this legislation furthers our companies vision of communities and the environment while helping to protect private property rights is why I am supportive in tax exempt forestry bonds.

S. 1085 is an opportunity to create real conservation gains on private working forests without requiring further governmental regulation while at the same time protecting private property rights. This will put more productive timberland into sustainable production in perpetuity helping to sustain rural employment. It will also help to mitigate the contentious public debate over how to manage our forestlands, bring diverse community groups together for a common goal and ease the government's financial burden in dealing with these issues.

One only need to look at the acquisition last week of The Timber Company (Georgia Pacific Timberlands) by Plumb Creek to recognize that there are millions of acres of timberland changing hands every year. This divestiture of forestland is likely going to accelerate as large integrated companies look to put their assets into more growth-oriented investments. This will put pressure on acquiring companies to cut the resource faster to pay down the debt. It will also lead to fragmentation of the timberland as buyers look for ways to increase value and cash flow from their investment by splitting it up for its real estate value. None of this is good for the environment or local communities.

S. 1085 is a way to help make sure that these working forests remain sustainable working forests in perpetuity without government interference and without infringing on anybody's property rights. It will require a willing seller and a willing buyer with the big winners being the local community and the environment.

Through the use of conservation easements and adherence to high environmental standards, the public can be assured that this land will be managed in a manner that protects all of the ecological assets that the public deems appropriate. This is doubly important because a lot of timberland changing hands is the subject of much public debate (remember the Headwaters Forest) leading to the divestiture of a lot of the government's time and money to deal with. One of the things that I like best about S. 1985 is that it will keep some of this contentious land in timber production instead of being bought up by government and private entities and set aside as parks or wilderness. Best of all, it has the support of industry, environmentalists and communities alike.

Rural communities will be big winners as they see a stable timber supply far into the future that is not being fought over by diverse interest groups. As a local employer who has been in the middle of the environmental wars for decades, I can tell that this will be a great relief for me.

S. 1085 truly creates a win/win situation for all parties involved. The modest costs to government in terms of tax revenue loss will more that be offset by less spending elsewhere. I urge you to look favorably on S. 1085.

STATEMENT OF PETER C. PASSOF, VICE PRESIDENT, REDWOOD FOREST FOUNDATION, INC.

Mr. Chairman and members of the Subcommittee, my name is Pete Passof and I am the Vice President of the Redwood Forest Foundation, Inc. (RFFI). The following statement has been authorized and approved by unanimous consent of the Board of Directors of RFFI. Our Board currently includes many of the diverse interests that characterize our community, i.e., environmentalists, saw mill owners, public officials, forest consultants, and small forest landowners.

By way of background, the Redwood Forest Foundation, Inc., is a Section 501(c)(3) private non-profit organization, organized January 8, 1998, to promote the public benefit and the general welfare. It's important to note that when the IRS finally approved our application in January of this year, we became the first nonprofit to receive authorization to purchase, own and manage timberland (including timber harvesting).

Our purpose is to acquire, protect, manage and restore the once great forests that surround communities in northern California, for the benefit of all citizens in perpetuity. Our goal is to create a model of "working community forests" by purchasing and sustainably managing these lands. To achieve this goal, RFFI is committed to maximizing: individual empowerment through public participation in managing resources for their optimal benefit and returning net profits directly back to the community; forest management practices that demonstrate respect for the integrity of forest ecosystems through the protection and conservation of biological productivity, ecological functions and environmental health; long-term community well-being through stable and rewarding employment, continuous infrastructure investment and financial integrity.

Please allow me to explain why the Board of Directors is offering its support for S. 1085, *The Community Forestry and Agriculture Conservation Act*.

We are currently witnessing the sale of millions of acres of industrial lands within the United States. Until now, many of these timberlands have been managed to provide short term economic gain to the owners. This has resulted in depleted forest ecosystems leading to a contentious public debate. Within Mendocino County, California, an important timberproducing county within the Redwood Region, more than 400,000 acres of forest land have sold in the last two years. We tried in vain to purchase these forested tracts to break the cycle of depletion and to restore economic stability to our local timberdependent communities.

We have come to the realization that cutover forestland does not have the appeal for preservation like old-growth. However, it is just as important in terms of large landscapescale protection and restoration of habitat. We believe that the income derived from active forest management and recreational opportunities will enable us to buy large and small forest tracts for conservation and open space values and pay back the incurred debt.

Since its inception more than 30 months ago, RFFI's Board of Directors have been closely working with the principals of US Forest Capital to seek out prospective willing sellers of industrial forest lands. We have also participated in their coordinated efforts to provide clarifying legislative language in the IRS code that will allow us, as a qualified California Nonprofit Public Benefit Corporation, to utilize tax-exempt revenue bond financing. We firmly believe that once the provisions of the Community Forestry and Agriculture Conservation Act become law, we will be in a extremely favorable position to meet our stated mission and goals. In the interim, we are confident that potential sellers and funders will see our community-based organization as a viable purchaser thus allowing us access to short-term taxable financing opportunities.

By allowing private, non-profit entities, such as RFFI, to access the tax-exempt debt markets by selling Community Forestry Bonds, the Federal government can achieve the conservation benefit that people are demanding, while doing so at a fraction of the cost. No other financial vehicle provides the public leveraging of private investment like taxexempt bonds. Once the tax-exempt funding is in place, we believe our organization can serve as a model for other timber-dependent communities to take a similar action.

In return for the ability to issue Community Forestry Bonds, we are fully prepared to:

- Place a permanent conservation easement on the property;

- Exceed relevant environmental laws;
- Complete a multi-resource management plan;
- Provide for a qualified third-party to hold the easement; and,
- Provide the third-party easement holder with adequate funds to monitor and enforce the easement.

Mr. Chairman, and members of the Subcommittee, on behalf of the Board of Directors of the Redwood Forest Foundation, Inc. and the many timber-dependent communities around the country who are seeking to keep their forests productive and working on a truly sustainable basis, I urge you to consider S. 1085, The Community Forestry and Agriculture Conservation Act as important legislative tool for the 21st century.

STATEMENT OF ROB MCKENNA, COUNCILMEMBER, KING COUNTY COUNCIL, WASHINGTON

Mr. Chairman and members of the Subcommittee, my name is Rob McKenna. I represent the Sixth District on the Metropolitan King County Council in Washington State. Thank you for holding this hearing on the relationship between tax law and conservation. I would like to submit this statement for the record in support of S. 1085—The Community Forestry and Agriculture Conservation Act.

King County is located in northwest Washington and includes both metropolitan Seattle and "edge cities" like Bellevue and Redmond which are home to hundreds of high tech companies such as Microsoft. At 2,200 square miles in area and with a population of 1.7 million, King County is one of the nation's largest counties. The eastern parts of the county include many rural and mountainous forestlands. My constituents care deeply about those forests. King County is a crossroads of traditional manufacturing industries such as Boeing and PACCAR alongside software, biotechnology and other high-tech companies. This powerful combination has resulted in explosive economic growth that has produced a high standard of living. King County also features an abundance of natural resources that provide a quality of life that continues to attract new residents. From Puget Sound in the west to the Cascade Mountains in the east, King County residents love their natural resources and environment.

But, as recognized more and more in the press, this explosive growth has not come without its challenges. In the Seattle area, forestland has been reduced by approximately 107,000 acres in the last 25 years. As the County continues to grow, the King County Council has worked to develop new tools that will continue to provide jobs for our constituents while managing growth in such a way that our quality-of-life is maintained. These tools have included a nationally recognized forestland, habitat and open space conservation program that has invested over $200 million in land acquisitions over the past three decades. These programs, coupled with philanthropic and state and federal technical and financial assistance, have helped us achieve some real gains in open space protection.

Yet, so much more needs to be done, especially given the increased rate of growth in forested areas. The tougher challenges we face in the years ahead are driven by four primary factors.

First, there are increasing pressures to convert working corporate forestlands to nonforest uses. These corporate forestlands sit between the Mount Baker-Snoqualmie National Forest to the East and the City of Seattle to the West. These lands have long served as an economic buffer for small rural forest-dependent communities and as an environmental buffer between the Cascade uplands and Puget Sound lowlands. However, as our population and the wealth of that population grows, we are seeing increasing development on the urban boundary and increasing fragmentation in rural areas as more and more citizens are interested in rural forest residences. We need to provide both green space and expansion in a mutually acceptable manner.

Second, King County is facing unprecedented pressures to enhance water quality standards in response to the listing of anadromous fish under the Endangered Species Act. We are working hard to do this without the divisiveness that has occurred among various parties in the past. And we have, in fact, made some progress, adopting a Sensitive Areas Ordinance to govern development standards and Best Management Practices for our roads maintenance program, among other measures. Yet again, one of the keys to our success will be assuring that non-point water sources flowing from the county, state and national forests through our cities will meet water quality standards. The working forests buffer I just spoke about, with the right management regime, provide a very attractive environmental means to

achieve our endangered species goals under the listings without creating stricter regulatory mandates or impacting private property rights.

Third, the current policy climate, notwithstanding my explanation above, has been less than cooperative, especially when it comes to forestry issues. This has made it difficult to bring people together, especially when one party or another has a stake in the issue, but may not be in a decision-making role.

Fourth, all levels of government and the philanthropic community just do not have the kind of funding that is needed, given other public policy needs, to achieve the level of conservation that so many of my constituents support. I know we are not alone and that local, state and federal entities share this challenge.

So what do we do about it? Time is running out in King County. Mr. Chairman, and members of the Subcommittee, we desperately need you to support S. 1085—The Community Forestry and Agriculture Conservation Act because it is the only tool that will address the challenges above in a manner that is doable today.

Community forestry and agriculture bonds will allow private non-profit entities to issue taxexempt revenue bonds for conservation purposes if the forestland they buy will have a permanent conservation easement placed on it and if the management plan they approve exceeds relevant environmental laws. While the transactions are complex and must be professionally managed, the concept is simple and responds to the challenges I outlined above in the following ways:

- For the first time an ownership category—private non-profit—provides an alternative to outright preservation, intensive timber production, and development. A private non-profit entity will have the philosophical and financial wherewithal to acquire large forested ownerships in an unfragmented state.
- The private non-profit will be required to exceed relevant environmental statutes and will have the board make-up and financial flexibility to not only meet the standards for anadromous fish protection, but exceed them if community economic objectives are met.
- For the fist time, environmentalists, industry, financial and local opinion leaders will have the opportunity to make decisions together regarding a large forested ownership.
- For the first time, a conservation entity will be able to leverage scarce taxpayer dollars with private investment to generate the large sums—tens to hundreds of millions of dollars—that are needed for large scale working forest protection.

King County is so supportive of this concept that we have been working for the last two years to test its feasibility and to create a financially sound and environmentally worthy non-profit in anticipation of using this tool.

The feasibility analysis was completed by the County's Department of Natural Resources and tested both the financial and policy effectiveness of the tool. From a financial standpoint, we took actual data from corporate timberlands and applied three different forest management scenarios to those lands. Then we applied both tax-exempt and commercial lending rates to those scenarios to see if we could generate the cash flow to pay off the principal and interest on the bonds. We could, even under the lightest forest harvest. We also tested this tool with a wide range of constituents as well. While they stressed the need for accountability, they also were supportive of moving forward with forestland acquisitions.

Last year the King County Council passed a resolution in support of Senator Gorton and Murray's Community Forestry and Agriculture Conservation Act. My colleague Councilmember Larry Phillips and I—as private citizens—joined two prominent conservationists and the University of Washington's forestry dean to create a non-profit in anticipation of taking advantage of community forestry bonds. We are working to identify an individual with financial experience to join the board and we are keeping a seat open in case a forestland seller would like a seat on the board. This will be quite a group, with conservationists and landowners—reflecting an array of philosophical and political beliefs—joined together to manage forestlands. We eagerly wait for the time when we can move forward with a transaction.

And time is running out. In the two years we have been working on this concept, more and more forestland has been converted and those lands that have not been converted are seeing their land values skyrocket. Even with tax-exempt rates, we still need to be able to service bond debt through sustainable forest harvests and the longer we wait, the more difficult it will be for us to achieve our goals. More importantly, the more pressing the challenges outlined earlier will become and the more costly those resolutions will become.

Mr. Chairman and members of the Subcommittee, we have had enough fighting about our forests. I urge you and your colleagues to provide us with a market-based conservation vehicle that doesn't require landowners or investors to leave money on the table to protect the environment. Please help us bring people together in support of our working forests. If not, I am afraid that we will be back in a more con-

tentious setting that in the end will cost a lot more money and cause a lot more divisions.

Thank you holding this hearing on this important subject.

STATEMENT OF JOHN M. ROSE, PRESIDENT AND CEO, SEATTLE-NORTHWEST SECURITIES CORPORATION

Mr. Chairman and members of the Subcommittee, my name is John Rose. I am President and Chief Executive Officer of Seattle-Northwest Securities Corporation, headquartered in Seattle and with offices in Portland, Oregon; Boise, Idaho; and Salt Lake City, Utah.

Thank you for holding this hearing on the relationship between tax law and conservation. I would also like to extend a special thank you to Congresswoman Dunn with whom I have had the pleasure of working on H.R. 1863—The Community Forestry and Agriculture Conservation Act which I testify in support of today.

Our firm is the leading underwriter of tax-exempt bonds in the Northwest. We have led recent bond financings for a diverse set of clients including the City of Seattle, the City of Boise, the University of Portland, Issaquah School District, and many others.

The purpose of my testimony is to describe why I believe that The Community Forestry and Agriculture Conservation Act will be an effective tool for use in promoting conservation.

The tax-exempt bond market has proven to be an effective vehicle for accomplishing public goals in the Northwest. Public goals including

- school construction,
- single family mortgages for lower-income families, and
- cleaner waters through the construction of sewage treatment plants

have all been achieved at a reduced cost because of the special qualities of the tax-exempt bond market.

Tax-exempt bonds can lower costs because lenders can accept lower interest rates while still achieving their investment goals. Today's tax-exempt market offers a highly rated borrower an interest rate of approximately 4.80 % for a 10 year loan, while a comparable taxable bond would require a rate of approximately 7.50 %. In addition, the tax exempt bond market is more accustomed to longer term borrowings; 20 and 30 year loans are quite common. These longer term tax-exempt bonds find a ready market with the buyers of those bonds including insurance companies, mutual funds and individual investors.

The Community Forestry and Agriculture Conservation Act will bring the powerful tools of the tax-exempt bond market to bear on the problems of encouraging a conservation management for threatened natural resource lands. Tax-exempt debt will allow the landowners to take a more patient view in managing their lands. Land management will be able to achieve higher environmental standards because the financing tool allows for longer time frames and requires less burdensome annual cash flows.

We are confident that the proposed structure will allow us to work with non-profit agencies, land owners and the investor community to complete transactions that will preserve working forests while at the same time achieving higher environmental standards. We have been working on several potential projects, and we are quite pleased with the results of our analyses. The new legislation will give us a tool that we can use to achieve important public goals. Thank you for providing me with this opportunity to testify today. I would be pleased to answer any questions or provide further information.

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