Transition Year Brings Changes for Rural Development

Richard J. **Reeder**

The year 2001 was characterized by dramatic political, social, and economic transition. A new President and a new majority party in the Senate changed the Nation's domestic policy priorities, reducing income and estate taxes and expanding and reforming education programs. With the September 11 terrorist attack came a transition to a more security-minded society. The Federal Government responded with legislative and regulatory changes to improve "homeland security," with immediate effects on air travel in many rural areas. Meanwhile, the economy moved from slow economic growth to mild recession. While efforts to pass an economic stimulus package failed in 2001, Federal spending on the military, homeland security, and disaster assistance increased after September 11, as did funding for some important rural development programs. Farm and rural development legislation was reauthorized in May 2002.

This article describes the most important recent changes in Federal policy for rural development. It examines Federal tax, spending, and regulatory policy. Tables cover most of the major programs affecting rural development, along with recent changes in funding and an indication of the types of places affected most by these programs, based on recent geographic fund allocations.

The farm legislation that reauthorized most rural development programs through fiscal year 2007 and created some new programs was enacted in May 2002 and is covered briefly at the end of this article.

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Income and Estate Taxes Cut

The income tax cuts enacted in June 2001 are discussed in greater detail in the following article by Jim Monke and Ron Durst. Although not aimed at stimulating rural economic development, this legislation's importance for rural economies should not be understated. Income tax cuts increase disposable income and can stimulate the economy. In places where tax cuts provide relatively large increases in disposable income, local economies may particularly benefit.

As noted by Monke and Durst, people in rural areas may be more likely to benefit from provisions eliminating the marriage penalty, and farming areas will be major beneficiaries of the repeal of the estate tax. In addition, some poor rural communities may benefit from expanded eligibility for earned income tax credits and refundable child tax credits, and from reductions in tax rates for low-income individuals. However, it is hard to pinpoint the effect of the legislation on different types of rural areas because of the complexity of the tax system and lack of appropriate data.

One potentially negative impact of the tax legislation is that it reduced surplus Federal tax revenues that might otherwise be used to pay for rural development programs. The cost of the tax cut to the Federal treasury was estimated at $1.35 trillion over 10 years. At the time it was enacted, this left a considerable amount of surplus revenues available for other uses. Subsequent events—including the onset of the recession and the increased spending on education, defense, and homeland security after September 11—used up most surplus funds, raising the possibility that the Federal budget could end in deficit in fiscal 2002 and in subsequent years. This could jeopardize the future funding of some existing or proposed rural development programs.

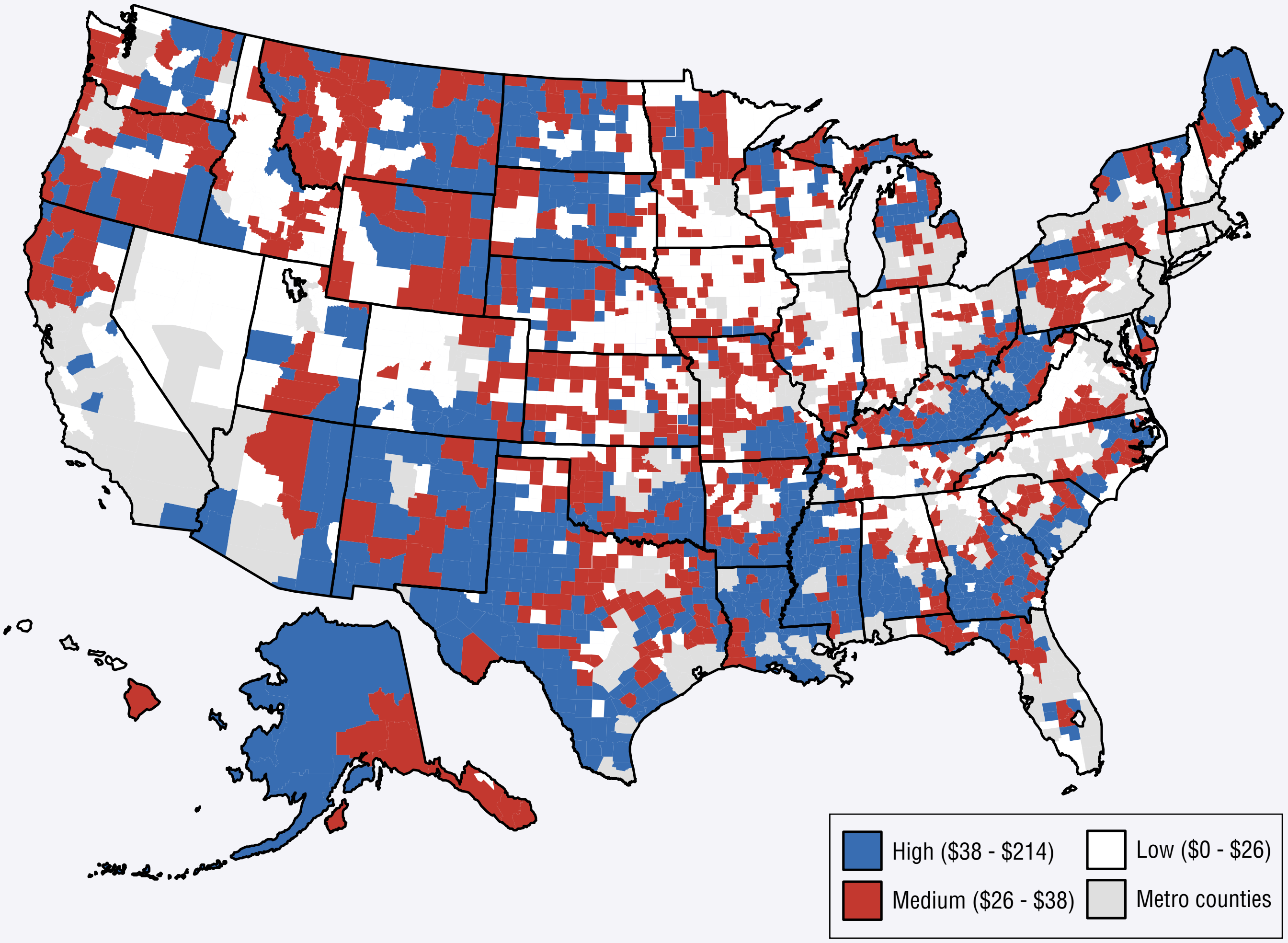
Education Reform

In December 2001, Congress reformed and expanded the Nation's education programs, authorizing over $26 billion in spending on elementary and secondary education in fiscal year 2002, an increase of $8 billion from 2001. The actual increase in spending is only about half that much, as Congress appropriated

Figure 1

Title 1 per capita education aid in nonmetro counties, fiscal year 1999

Low-income areas benefit; many are in the South



Source: Calculated by ERS using Federal Funds data from the Bureau of the Census.

only $22 billion for 2002 (from here on, 2002 refers to fiscal year 2002 unless otherwise stated). Much of the increase is in Title I aid to schools with disadvantaged students. This funding increase, together with new rules designed to target funds more effectively to these disadvantaged students, could particularly benefit rural communities with high concentrations of these students, many of which are located in the South (fig. 1). New money is also provided for specific initiatives, such as charter schools, school partnerships with colleges for math and science education, and $1 billion per year for reading instruction.

Although schools receive more money and States and localities can use it more flexibly, the money comes with new responsibilities. Over the next 12 years, all students must become "proficient" in reading and math skills and disadvantaged students must improve relative to advantaged students. Annual tests will measure student progress, and teachers must become qualified in their subjects. Meeting these worthwhile objectives could challenge some hard-pressed rural schools and localities. Schools that fail to meet these standards (after a trial period when they would first get additional funds and technical assistance) would be penalized.

Infrastructure Funding Mostly Increased

Funding for most major infrastructure programs either rose or remained constant in 2002

Table 1

Federal funding for selected infrastructure programs by fiscal year

Funding has increased or remained unchanged for most infrastructure programs in 2002

Program	2001 actual	2002 estimate	Change[1]	Rural areas most affected by the program[2]
	Billion dollars		*Percent*	
DOT Highway Planning and Construction Program	29.39	32.40	10	Totally rural and farming counties, and counties in the West
DOT Nonurbanized Area Formula Transit Grants Program	0.21	0.22	5	Rural, farm, and poverty States
DOT Airport Improvement	3.29	3.48	6	Rural and farm States, in the West
EPA Drinking Water SRF Capitalization Grants	0.82	0.85	3	Disadvantaged communities with small water systems
EPA Clean Water SRF Capitalization Grants	1.35	1.35	0	Urban States, in the Northeast
USDA Water and Waste Disposal Programs[3]	1.41	1.56	10	Transfer-dependent, totally rural, and nonadjacent counties
USDA Community Facility Loan and Grant Program	0.53	0.69[4]	30	Totally rural, nonadjacent counties
EDA public works grants	0.28	0.25	-12	Mining and transfer-dependent counties
RUS telecommunication loans[5]	0.50	0.50	0	Rural areas in general
RUS broadband grants	0.00	0.24	-----	Rural areas in general
RUS Distance Learning and Telemedicine Program	0.13	[6]	[6]	Rural areas in general
RUS Electric Loan Program	2.61	4.07	56	Rural areas in general

Note: DOT = U.S. Department of Transportation; EPA = U.S. Environmental Protection Agency; SRF = State Revolving Fund; RUS = Rural Utility Service, U.S. Department of Agriculture; EDA = Economic Development Administration, U.S. Department of Commerce.

1 Change is computed using actual amounts in millions of dollars, rather than rounded amounts shown in table.

2 When possible, program receipts per capita were computed for fiscal year 1999 to indicate the types of counties or States affected most. County and State types are defined in the appendix of *Rural Conditions and Trends,* Vol. 11, No. 1, 2000.

3 Includes both grants and loans, plus emergency community water assistance grants and solid waste management grants.

4 Includes economic initiative impact grants, hazardous weather early warning grants, and rural community development initiative grants.

5 Excludes Rural Telephone Bank loans.

6 Loan levels are expected to increase, but they cannot be estimated reliably.

Source: Budget of the United States Government, Appendix, Fiscal Year 2003.

Table 2
Federal funding for selected business assistance programs by fiscal year[1]
Most business loan guarantee programs are expected to have reduced loan activity in 2002

Program	2001 actual	2002 estimate	Change	Rural areas most affected by the program[2]
	Billion dollars		*Percent[3]*	
SBA 7(a) business loan guarantees	9.12	7.29[4]	-20[4]	Federal lands counties and counties in the West
SBA Certified Development Company guarantees (section 504)	2.27	[5]	[5]	Federal lands counties and counties in the West
SBA disaster loans	0.87	0.59[6]	-30[6]	Places experiencing disasters
SBA New Markets Venture Capital (NMVC)	0	0.15	---	High-poverty and low-income areas
Treasury Department Community Development Financial Institutions (CDFI)	0.11	0.08	-28	Low-income and minority areas
RBS Business and Industry loan guarantees (B&I)	1.09	1.15	5	Federal lands counties and counties in the West
RBS Intermediary Relending Program	0.04	0.04	0	Totally rural, farming, services, Federal lands, and poverty counties and counties in the West
RBS Rural Business Enterprise Grants (RBEG)	0.05	0.04	-16	Totally rural and farming counties and counties in the South[7]
EDA Economic Adjustment Grants	0.05	0.04	-18	Mining and government counties

Note: SBA = Small Business Administration; RBS = Rural Business-Cooperative Service, U.S. Department of Agriculture; EDA = Economic Development Administration, U.S. Department of Commerce.

[1]Budget authority used for grant programs; projected loan levels (obligations or program level) used for loan programs. In some cases, budget authority may be falling at the same time that projected loan obligations are rising (or vice versa due to subsidy use changes). This can happen for any number of reasons, including making use of greater efficiencies, reducing subsidies, charging fees, and using unobligated balances of funds from prior years.

[2]When possible, program receipts per capita were computed for fiscal year 1999 to indicate the types of counties or States affected most. County and State types are defined in the appendix of *Rural Conditions and Trends*, Vol. 11, No. 1, 2000.

[3]Calculated on actual expenditures and estimated expenditures. Does not correspond to table entries due to rounding.

[4]Excludes $4.5 billion in terrorist response loans in 2002.

[5]The fiscal 2002 amounts are impossible to estimate with any degree of reliability.

[6]Excludes $324 million in terrorist response loans in 2002.

[7]Also, farming, nonspecialized, Federal lands, and transfer-dependent counties were particularly affected by this program.

Source: Budget of the United States, Appendix, Fiscal Year 2003.

(table 1). For example, highway funds rose by $3 billion, from $29.4 billion in 2001 to $32.4 billion in 2002, and funding for most of the transit programs, including the nonurbanized area formula grant program, also rose. In addition, about $1 billion from excess trust fund revenues (called revenue-alignment budget authority or RABA funds) was earmarked to specific transportation infrastructure projects. This includes $247 million for the Transportation and Community and System Preservation program and $334 million for the borders and corridors programs.

The Environmental Protection Agency's (EPA) main infrastructure programs were funded at about the same levels as in 2001, though the Safe Drinking Water Program got a $25-million increase to $850 million. In addition, $1.1 billion went to State and tribal categorical grants, with much earmarked for specific water projects. This $1.1 billion also includes $40 million for rural Alaska and $75 million for the U.S.-Mexico border area.

Rural areas should benefit from increased rural electric loans from USDA's Rural Utilities Service (RUS) and from $24 million in RUS grants for broadband telecommunications (table 1). In addition, rural communities will benefit from increased loans and grants from USDA's community facilities programs, funded at $693 million in 2002, up from $535 million in 2001.

Funding dropped for the public works program of the Economic Development Administration (EDA)—from $286 million to $250 million—and for the technology opportunities program of the National Telecommunications and Information Administration (NTIA)—from $45 million to $15 million. For the latter program, the funding is already committed for continuing projects and no new projects will be funded. For each of these Commerce Department programs, the 2002 funding reduction followed a significant funding boost in 2001.

Business Assistance Programs Did Not Fare As Well

Interestingly, Federal funding was reduced for many business assistance programs at a time when the economy was moving into recession (table 2). Funding was cut in 2002 for the group of newly established programs operated by the Small Business Administration (SBA) as part of its New Markets initiative. This includes the Busiess LINK mentorship/technical assistance program, the Program for Investment in Microenterprise (PRIME), and HUBZones. Funding for one-stop-capital-shops was ended. In addition, funding was cut for the Community Development Financial Institutions (CDFI) program, which assists banks and other institutions that finance private sector development in underserved areas. EDA's main business assistance programs also received budget cuts for 2002. This includes economic adjustment grants, reduced from $50 to $41 million. EDA's defense adjustment assistance ($31 million in 2001) was eliminated because the time limit expired for the last military base closures eligible to receive such assistance. While these cutbacks mainly affect distressed areas, the estimated $2-billion reduction in SBA's 7(a) regular business loan guarantee program in 2002 affects rural and urban areas nationwide.

Most of USDA's business assistance programs, operated by the Rural Business-Cooperative Service (RBS), did not receive budget cuts. Funding for rural business opportunity grants fell from $8 million to $5 million in 2002, and rural business enterprise grants dropped by less than $1 million. However, funding either increased slightly or remained constant for rural cooperative development grants, rural economic development loans, and the intermediary relending program (table 2). RBS's business and industry loan guarantees, which are to a certain extent demand-driven, are expected to rise from $1.09 billion in 2001 to $1.15 billion in 2002.

Less Change Expected in Housing and General Assistance

Assistance will rise for most of USDA's main housing programs. Funding increased only slightly, from $686 million in 2001 to $701 million in 2002, for USDA's rental assistance program, run by the Rural Housing Service (RHS) (table 3). Funding also increased for the much smaller very low-income housing repair loan program, rising from $31 million to $46 million, and RHS's mutual/self-help grants will rise from $18 million to $56 million. An increase in activity may also occur in RHS's section 502 single-family housing loan guarantee program, but this is another demand-driven program and loan levels are difficult to estimate for 2002. Similar demand-driven uncertainties may occur in the much larger home mortgage and loan programs operated by the Federal Housing Administration (FHA) and the Department of Veterans Affairs. Meanwhile, the Department of Housing and Urban Development's (HUD) subsidized housing assistance should rise about 6 percent, and HUD's home investment assistance should rise 8 percent.

Table 3

Federal funding for selected housing programs by fiscal year

The largest percentage increase is expected for USDA's single-family guaranteed loan program

Program	2001 actual	2002 estimate	Change	Rural areas most affected by the program[1]
	Billion dollars		*Percent*[2]	
USDA/RHS:				
Single-family (sec. 502) direct loans	1.07	1.08[3]	1	West, retirement and Federal lands counties
Guarantees	2.34	3.13[3]	34[3]	Retirement and Federal lands counties, in the Midwest and West
Multifamily (sec. 515)	0.12	0.14[3]	21[3]	West, South, mining, poverty, commuting, retirement, Federal lands, and adjacent counties
Rental assistance	0.69	0.70	1	Totally rural, transfer-dependent, and poverty counties
VA:				
Loan guarantees	31.13	[4]	[4]	West, government, and Federal lands counties
HUD:				
FHA single-family mortgage insurance	107.45	[4]	[4]	West, South, retirement, and nonadjacent counties
Subsidized housing assistance[5]	20.94	22.10	6	West, urbanized adjacent, and poverty counties
Home Investment (HOME)	1.71	1.84	8	Northeast, urbanized adjacent, and government counties

Note: HUD = Housing and Urban Development; RHS = Rural Housing Service, USDA; VA = U.S. Department of Veterans Affairs; FHA = Federal Housing Administration.

[1]When possible, program receipts per capita were computed for fiscal year 1999 to indicate the types of counties or States affected most. County and State types are defined in the appendix of *Rural Conditions and Trends*, Vol. 11, No. 1, 2000.

[2]Calculated on the actual and estimated expenditures. Does not correspond to the table entries due to rounding.

[3]These estimates may overstate the increase in 2002. For example, last year's budget estimated increases of over 30 percent for these two programs; the actual increases were closer to 10 percent.

[4]The fiscal 2002 amounts are impossible to estimate with any degree of reliability.

[5]Includes Section 8 low-income housing assistance.

Source: Budget of the United States, Appendix, Fiscal Year 2003.

Of the main general assistance programs important for rural development, funding changed little for HUD's State/small cities portion of the community development block grant program and section 108 loan guarantee program, or for USDA's extension activities run by the Cooperative State Research, Education and Extension Service (table 4). HUD's $25-million rural housing and economic development program is also funded at the same level as in 2001. However, funding for the Bureau of Indian Affairs programs will increase 13 percent in 2002 (table 4), and even excluding supplemental funding for the September 11 crisis response, disaster assistance from the Federal Emergency Management Agency (FEMA) may increase, depending on what disasters occur in the remainder of the year. In contrast, funding for EDA's adjustment programs (which can be viewed both as business and general assistance) was reduced, while funding for EDA's planning and technical assistance programs was unchanged.

Funding for EPA's brownfields redevelopment program increased $6 million to $98 million in 2002. New legislation authorizes EPA to spend up to $200 million per year on the program through 2006, plus $50 million per year for State and tribal response programs. USDA's Fund for Rural America, which provided flexible money for rural development programs and research, was prohibited from new spending in 2002 and was later repealed as part of the 2002 farm legislation.

Regional Development Programs Gain Momentum

Last year's *Rural America* article on rural development policy (Vol. 16, No. 2) reported on the emergence of the Delta Regional Authority (DRA) and the Denali Commission, which joined the Appalachian Regional Commission (ARC) as large-scale regional development authorities. Both of these new authorities made progress in the last year. The DRA, which covers the lower Mississippi River region, is just beginning operations.

Table 4

Federal funding for selected general assistance programs by fiscal year[1]

Little change in funding for most of the main general assistance programs in 2002

Program	2001 actual	2002 estimate	Change	Rural areas most affected by the program[2]
	Billion dollars		*Percent*	
HUD State/small cities community development block grants	1.27	1.30	2	Small towns and rural areas, particularly in poverty States.
HUD section 108 loan guarantees	0.34	---[3]	---[3]	Same as above
EDA adjustment assistance, includes economic and defense adjustment, planning, and technical assistance	0.11	0.07	-35[4]	Low-income areas, varies from year to year[5]
FEMA disaster relief[6]	3.17[6]	---[3]	---[3]	Earthquake,- storm-, floodprone areas
USDA extension activities	0.43	0.44	2	Small towns and rural areas
BIA Native American assistance programs	1.92	2.18	13	Indian reservations

Note: HUD = Housing and Urban Development; EDA = Economic Development Administration; FEMA = Federal Emergency Management Agency; BIA = Bureau of Indian Affairs.

[1]Unless otherwise indicated, new budget authority is used for funding levels.

[2]When possible, program receipts per capita were computed for fiscal year 1999 to indicate the types of counties or States affected most. County and State types are defined in the appendix of *Rural Conditions and Trends*, Vol. 11, No. 1, 2000.

[3]The fiscal year 2002 amounts are impossible to estimate with any accuracy.

[4]Most of the decline ($31 million) was from the elimination of defense adjustment aid.

[5]In fiscal year 1999, these programs provided the most assistance, per capita, to mining and government-dependent counties and to those adjacent to metro areas. Nonmetro areas got higher per capita payments in the Northeast and West than in other regions.

[6]FEMA funding amounts are for new obligations and exclude terrorism response aid.

Source: Budget of the United States, Appendix, Fiscal Year 2003.

It now has $30 million (including $20 million carried over from 2001) to work with in 2002. The Denali Commission, which covers Alaska and began in 1998, is beginning to pick up steam. In 2002, it has a direct appropriation of $30 million, plus $25 million in earmarked funding from other agencies (including $15 million from USDA's RUS to fund rural power system upgrades and $10 million in Health and Human Services funding for job training). Denali will also get $11 million from the Trans-Alaska Pipeline Liability Fund. Meanwhile, funds for the ARC's highway program (funded through the Department of Transportation) will rise significantly in 2002, while funds for ARC's nonhighway programs will remain at $78 million.

Some other distressed rural regions may soon benefit from similar programs. The 2002 farm legislation authorizes the establishment of a Northern Great Plains Regional Authority covering 399 counties in 5 States (Iowa, Minnesota, Nebraska, North Dakota, and South Dakota). In addition, 2002 appropriations included $250,000 for the University of Georgia to undertake a study of the need for a similar regional authority for the crescent-shaped portion of the Black Belt in the Southeast.

Several programs that target assistance to distressed communities, including in some cases multicounty regions, have recently designated new places to receive assistance, including 12 rural renewal communities (RCs), 2 rural empowerment zones (EZs), and 20 new resource conservation and development (RC&D) areas in 16 States and American Samoa (fig. 2). The 2002 farm legislation authorizes new programs to help small-scale regional entities plan and implement development in rural areas.

Competition for HUD's new renewal community program took place in 2001, and HUD announced its 40 designated RCs in January 2002. The 12 rural RCs, which receive various tax incentives, were Green-Sumter Counties, AL; southern Alabama (9 counties); Orange Cove, CA; Parlier, CA; northern Louisiana (14 parishes); central Louisiana (11 parishes); west-central Mississippi (13 counties); eastern Kentucky (4 counties); El Paso County, TX; Turtle Mountain Band, ND; Jamestown, NY; and Burlington, VT.

USDA's two new rural empowerment zones will get tax incentives, but so far, unlike the other eight rural empowerment zones, no grants have been awarded them. They are Aroostook County in Maine and the Futuro EZ (four counties along the middle Rio Grande in Texas).

The 20 new RC&D areas receive technical assistance from USDA's Resource Conservation and Development program, operated by the Natural Resources Conservation Service. This brings the total number of RC&Ds to 368. The designated areas cover about 85 percent of U.S. counties and 77 percent of U.S. population.

About the Federal Funding Tables

These tables contain budgetary information from the Budget of the United States and the Budget Appendix for fiscal year 2002, and from summary information obtained directly from USDA and other Federal agencies. Unless otherwise indicated, the amounts cited refer to obligations of budget authority or new loans or loan guarantees. The amount for fiscal year 2001 is the actual amount, while the amount for fiscal year 2002 is estimated. These 2002 estimates can be inaccurate at times, particularly for credit programs. The last column, indicating the types of areas most affected by the program, is based on our analysis of the geographic distribution of funds in fiscal year 1999, using the Consolidated Federal Funds Data from the Census Bureau. Note, however, that a program's geographic distribution can change from year to year.

Rural Air Travel Affected by New Security Rules

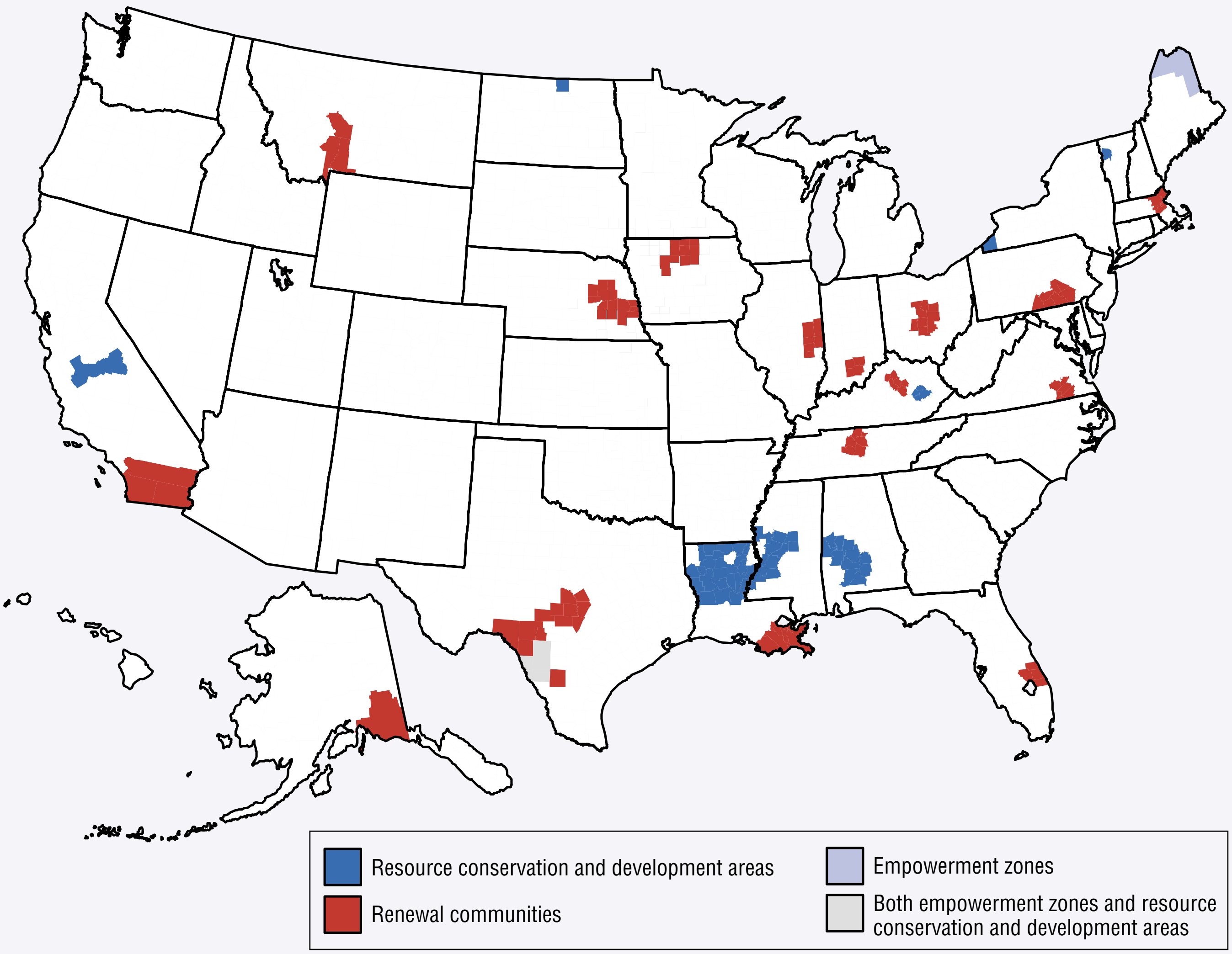
Following the September 11 attack, air travel was halted nationwide for a short period of time, then it resumed with new requirements aimed at making air travel more secure. With attention focused on the larger hubs in the air transportation system, the challenges these new restrictions posed to small regional and general aviation airports garnered less national attention. In fact, their challenge is in many ways more difficult, because they typically lack economies of scale and the financial resources to meet the new requirements. In addition, some rural airports experienced significant cutbacks in regular air service when principal airlines cut service.

Congressional action is helping to alleviate some of these problems. In addition to federalizing baggage inspection, Congress has allowed grant funding from the Airport Improvement Program (AIP) to be used for security activities mandated by the new security rules, with no local match funds required. In addition, some special provisions help smaller airports. For example, some smaller (nonprimary) airports can now use AIP funding to meet debt service payments to avoid

Figure 2

Newly designated rural places receiving special assistance

Most regions received assistance



Source: Economic Research Service.

default on the debt. A new small community air service development program was funded at $20 million (part of the increase in funding for AIP), and the essential air service program that subsidizes air service in some rural areas got a funding boost from $50 million in 2001 to $113 million in 2002.

Other Regulatory Changes

Aside from security issues, the Bush administration has generally argued for less Federal regulation, providing States, localities, and the private market with more flexibility. This is evident in policy changes associated with economic regulation (antitrust and corporate mergers), electric regulation, and environmental regulation. For example, the Army Corp of Engineers announced in January 2002 that it is revising 11 "general permits" that allow construction on wetlands. The new permits would provide more flexibility to developers and leave local and State governments with more responsibility to see that wetlands are protected. Changes in EPA's main water infrastructure programs allow each State to shift funding between the Clean Water and the Drinking Water programs to address the most pressing priorities.

Not all recent regulatory changes have moved toward less Federal regulation. For instance, in lifting the moratorium on railroad mergers in June 2001, the Surface Transportation Board issued new, stricter rules for future railroad mergers. Another example—one of the most significant regulatory decisions during 2001 for rural development—was EPA's decision to uphold its earlier proposal to tighten restrictions on arsenic in drinking water. The new rule reduces the allowable levels by a factor of 5 (from 50 parts per billion to 10 parts per billion). EPA requires compliance by 2006 and plans to undertake research and development of more cost-effective technologies to help small water systems comply with the new standards. The increased rural water system grants authorized by the 2002 farm legislation would help rural communities meet the costs of complying with this new water standard.

Another important regulatory issue for rural development—one that still needs to be resolved—concerns rural consultation in transportation (highway) planning. The Transportation Equity Act for the 21st Century contained provisions requiring rural local officials' input into the State transportation planning decisions. However, the Department of Transportation's efforts to issue regulations to implement these TEA-21 provisions have been caught up in controversy over regulations concerning environmental planning. This has left States without clear guidelines on how to consult with rural communities when making important planning decisions.

The 2002 Farm Legislation

The Farm Security and Rural Investment Act of 2002 (P.L. 107-171) contained many provisions authorizing new or expanded rural development programs. With regard to infrastructure, several new USDA programs were authorized to improve rural water and waste disposal systems, and $360 million was authorized to reduce the backlog of pending applications for water and waste disposal and community water system grant applications. The act also included various telecommunications provisions, covering broadband, telework, local television broadcasting, and e-commerce. With regard to business development, a new program would provide equity capital and operational assistance to small businesses, and the level of assistance to value-added agriculture would be increased. Various new general assistance programs were authorized, covering a wide range of activities, including fire fighters and emergency personnel, community facilities grants benefiting rural seniors and Tribal colleges, and a program to preserve historic barns. In addition, several new programs would promote regional planning and comprehensive, strategic development. These include the Rural Strategic Investment Program, the Multijurisdictional Regional Planning Organizations program, and the Northern Great Plains Regional Authority. However, the Fund for Rural America was repealed.

If Congress appropriates funding for these programs, most authorized over the next 5 years, they could have a significant impact on rural development. For more information on these and other provisions in the 2002 farm legislation, see the ERS web page covering the legislation (http://www.ers.usda.gov/Features/FarmBill/). RA