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Deficit Reduction Measure Ushers in Tax Cuts Plus New Aid for Low-Income Populations in 1998

New tax cuts should encourage various activities, such as savings and investment, higher education, support for families, and environmental cleanup. Most new spending assists poor children and welfare populations, restoring some of last year's welfare program cuts. Although some new initiatives and tax breaks support development activities, most development program funding was steady or increased slightly. Meanwhile, the USDA Rural Development Mission Area and the Federal regulatory environment continue to evolve with important implications for rural America.

This Federal Programs issue of *Rural Conditions and Trends* (*RCaT*) describes Federal program and policy changes important for rural development, including most of the larger core development programs that assist rural infrastructure, housing, businesses, and general development (including planning and technical assistance), plus changes in tax and regulatory policy affecting rural areas. This issue examines budget, tax, and regulatory changes initiated in 1997 and taking effect in 1998. We also have two special articles: one covering the latest changes in welfare-related programs and the other describing USDA's evolving rural development mission.

Like other issues of *RCaT*, our analysis is primarily descriptive. In many of our maps and figures, we use the Census Bureau's Consolidated Federal Funds Reports data (also known as Federal Funds data) to reveal where individual Federal program allocations went in fiscal year 1996 (the latest available data), on the assumption that many of these same places will be affected by current policy changes affecting these same programs. We use various State and county typologies so we can describe how policy changes might affect specific types of places, such as farm States or poverty counties. A table showing the overall urban-rural distribution of major programs is presented in appendix A. Data sources and typologies are discussed in appendix B.

We are limited in the number of maps and other figures we can provide for any one issue, but over time we hope to present information on a wide variety of programs important to rural development. In earlier issues—particularly our first Federal Programs issue (Vol. 7, No. 2)—we covered a wider array of programs, including agriculture, health, defense, education, employment and training, environment and natural resources, and income support programs.

Some Major Themes of This Report Flow From the Deficit Reduction Legislation

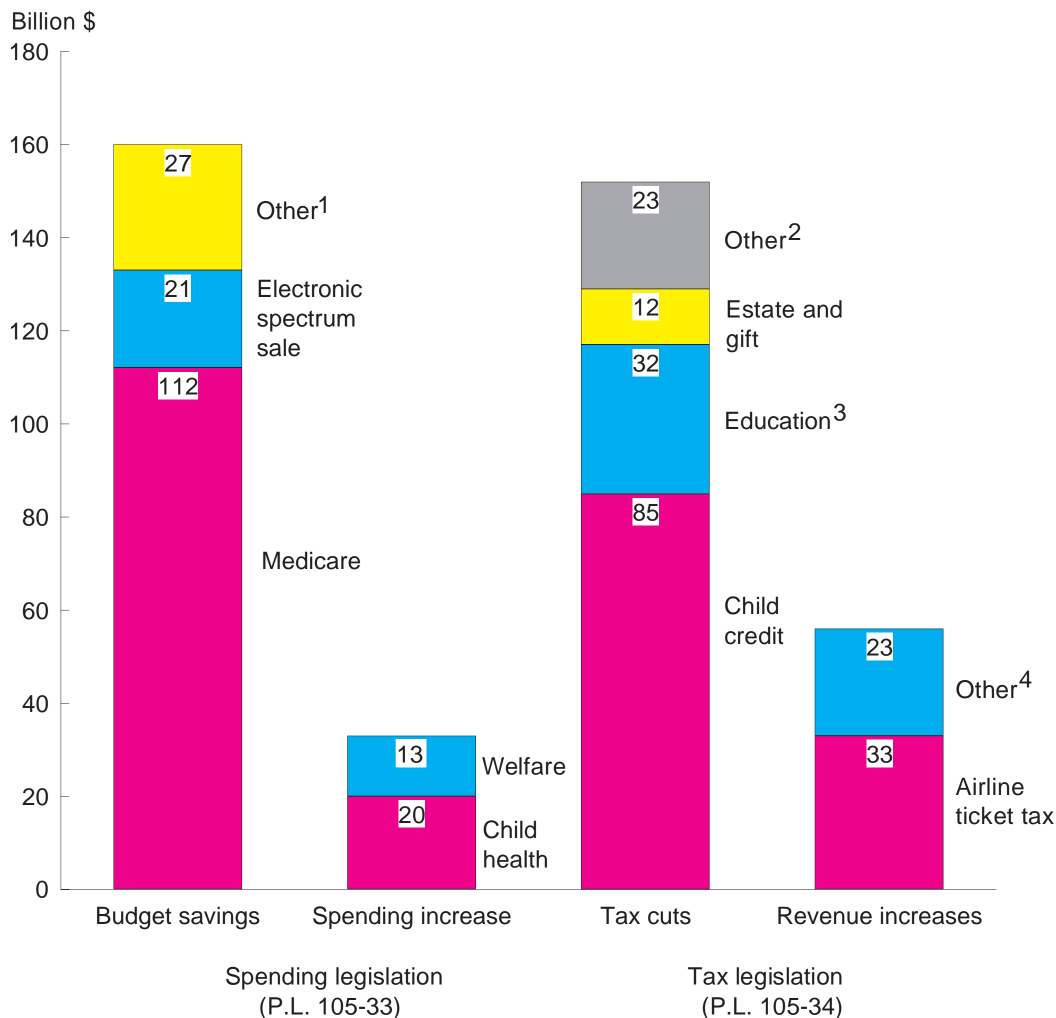
While charting a course to balance the budget, Congress and the Administration jointly found a way to cut taxes as well as increase spending. The deficit reduction legislation enacted in the summer of 1997 reconciled tax and spending plans with the resolution to balance the budget by the year 2002 (unless otherwise indicated, years cited in this article refer to Federal fiscal years, which begin October 1 of the previous year). Most of the anticipated deficit reduction derives from the assumption that economic growth will continue unabated, and from reduced growth in Medicare payments to hospitals and other health providers. Additional budget savings will come from Medicaid cuts, auctions of the electromagnetic spectrum, and revenues from the new segmented airplane ticket tax (which exempts flight segments to isolated rural airports) and from an increase in the cigarette tax. As a result, it was possible to actually increase Federal spending by $33 billion on programs mostly benefiting low-income children and welfare populations, while providing some $152 billion in new tax cuts over the coming 5 years (fig.1).

Although some rural development-related initiatives got a big boost from this legislation—particularly the welfare-to-work initiative—the 5-year budget plan allows little more than a 1-percent-per-year increase for most domestic discretionary programs, below that needed to keep up with expected inflation. Unless the economy performs better than anticipated or new sources of funds can be found, most of the major development programs appear to be facing stagnant funding levels in 1998 and in the coming 5 years. After the year 2002, more difficult budgetary adjustments may be needed as the cost of recently enacted tax reductions mounts. Another long-term concern involves the coming retirement of the baby boom generation, expected to cause rapid growth in the cost of Medicare and Social Security programs. The 1997 budget legislation accomplished no fundamental program changes to address this baby boom issue.

Figure 1

5-year changes in spending and taxes from the 1997 deficit reduction legislation

Deficit reduction was achieved through two pieces of legislation, one affecting mainly spending programs, the other affecting taxes



[1] Includes savings from Medicaid, cigarette tax increases, and miscellaneous spending cuts or tax increases.
[2] Includes new IRA's, capital gains, and other tax reductions.
[3] Includes only the hope and lifetime learning credits, excludes other, generally smaller education tax cuts.
[4] Includes extension of Federal unemployment surtax and miscellaneous revenue increases.
Source: ERS compilation, based on data from the Congressional Quarterly Weekly Report.

While long-term issues remain unresolved, the situation for rural development policy seems to have improved from 1 or 2 years ago. Among the most important development-related provisions to be implemented in 1998 are (1) the new tax cuts, some of which are targeted to development activities, (2) the creation of a new welfare-to-work grant program and the restoration of some welfare benefits that were cut in 1996, (3) the creation of a new State Child Health Insurance Program (SCHIP)—a block grant to address the needs of low-income children who lack health insurance, and (4) changes in Medicare and Medicaid programs that finance health services for the elderly, disabled, and low-income populations.

The changes affecting Medicare and Medicaid deserve note for their potentially disproportionate effects on rural areas. For example, the deficit reduction law significantly increases the minimum payment to managed care providers to $367 per month per beneficiary, resulting in narrower urban-rural differentials in plan payment rates. This should attract more health plans into rural markets, giving more residents access to managed care service that is preferable to fee-for-service for some kinds of health sevices. Because the new law did not increase payments for fee-for-service care, however, this could be a disadvantage for providers and beneficiaries who remain outside of managed care plans. Other significant health-related changes include (1) rising Medicare part-B premiums without compensatory increases in subsidies to low-income elderly beneficiaries, which over time could be problematic for the poor elderly that are more common in rural than urban areas; (2) increased State control over Medicaid, including the ability to cut Medicaid payment rates and end subsidies of Medicare out-of-pocket costs for low-income recipients, which some experts believe might hurt health care access for the poor; and (3) expanded coverage of benefits, including preventive health care and cancer screening, which would particularly benefit rural areas because of their relatively high proportions of elderly and disabled.

The new SCHIP child health insurance program is authorized to spend $20 billion over 5 years, the largest new program in the budget. It could particularly benefit rural communities because they tend to have a higher share of uninsured children than urban communities, but States have considerable flexibility in how the new child health money is used, so it is difficult to say exactly how this program will affect rural areas at this time.

Although these health program changes are important, in this report we focus on the tax- and welfare-related changes, including the new welfare-to-work program, because they are more closely associated and coordinated with rural development programs and strategies.

Tax Reduction Will Benefit Rural Areas

The Tax Relief Act of 1997 reduces taxes for various types of individuals and economic activities, potentially affecting all rural America. It includes tax relief for families (child tax credit and education tax incentives), incentives for savings and investments (individual retirement accounts and capital gains tax breaks) and various forms of tax relief for farmers and businesses (self-employed health insurance deduction, alternative minimum tax rate for small corporations, and capital gains, estate and gift tax reductions, and special tax provisions targeted to farmers). Although most of the tax savings benefit primarily middle-income people and places, some new tax cuts focus on problems of low-income people and places, including incentives to hire employees from targeted groups of disadvantaged individuals or places (work opportunity and welfare-to-work tax credits) or to encourage private enterprise development in high-poverty or distressed areas (new Empowerment Zones, Brownfields).

Welfare-Related Program Changes Also Significant

Besides the new welfare-to-work tax credit, a variety of program changes have occurred that should help welfare populations in adjusting to the welfare reform enacted in 1996. The most significant change was the creation of the new welfare-to-work block grant program providing $3 billion during 1998-99. This program includes both a formula grant to the States and competitive grants directly to local communities. Other welfare-related changes include the restoration of Supplemental Security Income (SSI) benefits to legal immigrants who were residents as of August 22,1996, and Medicaid coverage for disabled children who might have lost coverage because of welfare reform. States may now exempt some able-bodied food stamp recipients from work requirements. In addition, Job Training Partnership Act programs got funding increases, which should help with the training part of the welfare-to-work program.

Other Themes Involve General Assistance Initiatives, Increased Infrastructure Aid, Emphases on Small Business and Homeownership, and Regulatory Changes

The main general assistance programs (programs that provide multiple forms of development assistance) are minimally changed in 1998, but many of the smaller programs are getting funding increases, and several new multi-agency initiatives are expanding, including Empowerment Zones, Brownfields, and Community Development Financial Institutions. These expanding initiatives assist high-poverty urban and rural areas.

Highway aid, the Nation's largest infrastructure program, increases by 11 percent in 1998, with more substantial changes expected when the program is reauthorized. Some smaller transportation-related programs have also been given a boost, including the Appalachian Development Highway System, Amtrak, and the Airport Improvement program. The Essential Air Services program, which particularly assists small towns and rural areas, was given a larger and more stable revenue stream. Except for the water and waste disposal program, USDA's infrastructure programs are expected to increase their assistance in 1998, with the largest increases in telecommunications and community facilities.

Some business assistance programs, including USDA's Business and Industry program, are increasing their assistance levels in 1998. The Small Business Administration's Section 7(a) program, the Nation's largest business assistance program, is also expected to increase its loan guarantees, consistent with the recent Federal emphasis on stimulating development through small and minority business development. The larger business assistance programs continue to reinvent themselves to better serve nontraditional borrowers, while achieving efficiencies through greater use of private sector lenders to screen and monitor loan performance.

Housing assistance programs increasingly emphasize homeownership as more Americans are expected to buy their own homes. Homeownership program activity is expected to increase in 1998, as mortgage financing is made more available to those who would otherwise be unlikely to purchase a home. Families targeted for assistance include minorities and low-income individuals, which are now the populations with the most rapid homeownership gains. Public housing and rental assistance expenditures are fairly stable, but significant changes are expected soon for these programs.

The most significant regulatory changes involve telecommunications, electric power, pollution controls, public land management, and financial institutions. The telecommunications industry is going through turbulent adjustments to changes arising from the Telecommunications Act of 1996. New, more restrictive, air and water pollution regulations have been proposed which, over time, could significantly affect development in many rural and urban areas. New plans have been proposed for more effective management of natural resources on national forests and public rangeland in many parts of the country, and legislation was enacted to clarify and amend the mission of the National Wildlife Refuge System, recognizing both the interests of resource conservation as well as recreation on the 92 million acres of refuge areas nationwide. Meanwhile, regulations covering financial institutions, such as banks, credit unions, and the Farm Credit System, continue to evolve, with some significant implications for rural areas.

This Issue Highlights the USDA Rural Development Mission

USDA has primary responsibility for planning and coordinating Federal rural development efforts. It also operates most of the programs that target assistance in rural areas. The lead USDA entity for rural development is the Rural Development Mission Area. In earlier issues of *RCaT*, we mentioned some of the changes underway in this Mission and we have covered in some detail how some of its main programs are being reinvented. However, our coverage of this mission area has been fragmented due to the organization of our report into separate types of assistance, such as infrastructure, business, and

housing assistance. In this issue, in addition to our normal coverage of these programs, we provide a brief, comprehensive, description of this rural development agency's organization and programs, both large and small, including recent initiatives. *[Rick Reeder, 202-694-5360, rreeder@econ.ag.gov]*

Some New Initiatives Add to an Overall Stable Group of General Assistance Programs

Funding is steady for main general assistance programs, but the disaster aid law provides new money that will particularly help the upper Midwest and some recent initiatives grow in importance, including Empowerment Zones, Brownfields, and Community Development Financial Institutions, providing special assistance to low-income areas.

General assistance programs offer a variety of assistance, making them flexible enough to assist rural communities facing very diverse economic challenges, ranging from poverty problems to natural disasters. They also support comprehensive development strategies. Among the largest such programs are the extension activities funded by the Department of Agriculture (USDA), the Department of Commerce's economic adjustment assistance, the Department of Housing and Urban Development's (HUD) community development assistance, Federal Emergency Management Agency's (FEMA) disaster assistance, and the Bureau of Indian Affairs assistance programs. Some smaller programs, like the Appalachian Regional Commission's programs, focus on a particular region or type of place with special needs. Most of these programs, both large and small, have maintained stable funding in 1998 (references to years in this article refer to fiscal years). However, some new initiatives have begun that are worth noting.

Little Change in Funding in 1998 for Most Large General Assistance Programs

HUD's community development block grants (CDBG) will provide $1.25 billion general assistance to fund housing, infrastructure, and business development in small cities, rural areas, and some portions of metro areas in 1998—down only about 3 percent from 1997 (table 1). In addition to these amounts going to the State/small cities CDBG programs, CDBG includes some new set-aside funding for specific places or purposes. One set-aside provides $25 million for rural economic development. Few details of this set-aside program were specified, although it will provide for grants of up to $4 million for a variety of developmental activities and must include at least one grant in Iowa and Missouri and one for an Alaska native area. In addition to the $4.7 billion appropriated for 1998, $250 million in emergency appropriations will go for CDBG disaster relief financing (the same amount was provided for 1997).

HUD's section 108 loan guarantees, part of the CDBG program, helps communities finance housing rehabilitation, public facilities, and large-scale business development projects in both urban and rural areas. In 1998, the legal limit for these guarantees is about $1.3 billion; however, it is difficult to estimate how much will actually be obligated. In 1997, $189 million in loans were guaranteed, only a fraction of the $1.4-billion legal limit that year. Even so, this program is the largest for this kind of general purpose assistance.

Commerce Department's Economic Development Administration (EDA) provides planning, technical, and adjustment assistance. This is general assistance because it helps with a variety of projects aimed at job generation to adjust for local economic problems, such as persistent unemployment or underemployment. Unlike CDBG, it bypasses the States, going directly to local or regional governments. Funding for these programs remains stable in 1997, with $24 million for planning grants, $9 million for technical assistance, and $119 million for adjustment grants (including $89 million for defense adjustment). Additional funding goes to communities adjusting to natural disasters, including $40 million in 1998 for floods in the Midwest.

FEMA's disaster relief grants provide the lion's share of general assistance to places recovering from natural disasters. In 1997, FEMA's disaster relief totaled $4.3 billion. A good part of this assistance is headed for rural areas affected by the floods in the Midwest last spring. Current estimates for 1998 call for $3.2 billion, but the total could rise above 1997 levels if El Niño-related disasters require substantial supplemental funding.

The extension activities, funded in part by USDA's Cooperative State Research, Education, and Extension Service (CSREES), provide valuable, research-based technical

Table 1
Main general assistance programs
Funding is relatively steady for most of the large general assistance programs

Program	Funding level by fiscal year[1] 1997 actual	1998 estimate	Change	Rural areas most affected by the program
	—Billion dollars—		Percent	
HUD State/small cities community development block grants	1.29	1.25	-3	Small towns and rural areas in farm and poverty States
HUD section 108 loan guarantees	.18	—[2]	—[2]	Same as above
EDA adjustment assistance, includes economic and defense adjustment, planning, and technical assistance	.15	.15	0	Low-income areas, vary from year to year
FEMA disaster relief[4]	4.34	3.26	-24	Earthquake- and flood-prone areas
USDA's extension activities	.43	.42	0[5]	Small towns and rural areas
BIA Native American assistance programs	1.64	1.70	4	Indian reservations

[1] Unless otherwise indicated, new budget authority is used for funding levels.
[2] The amount of section 108 loan guarantees is mostly a function of demand by communities; thus it is impossible to provide accurate estimates for 1998 or for change from 1997 to 1998.
[3] In 1995, these programs were concentrated in farming, totally rural, and midwestern counties, but in 1996, they focused on mining- and government-dependent, urban and metro adjacent, and rural West counties.
[4] FEMA funding amounts shown are for new obligations. The 1998 amount could rise when new national emergencies are declared and supplemental funding is supplied.
[5] Funding declined by $2 million.
Source: *Budget of the United States Government, Fiscal Year 1999*.

assistance to rural communities that otherwise lack the trained staff to formulate complex development strategies. Extension activities include agricultural as well as nonagricultural development. Federal funding for extension activities remains roughly constant at $424 million in 1998 ($430 million is provided for research related to these activities), down only slightly from $426 million in 1997.

The Interior Department's Bureau of Indian Affairs (BIA) provides general assistance to Native American tribes. Funding for BIA is increasing from $1.64 to $1.70 billion in 1998. The BIA programs provide assistance to Indian reservations, mostly located in rural areas.

Many Small Programs Get More Funding in 1998

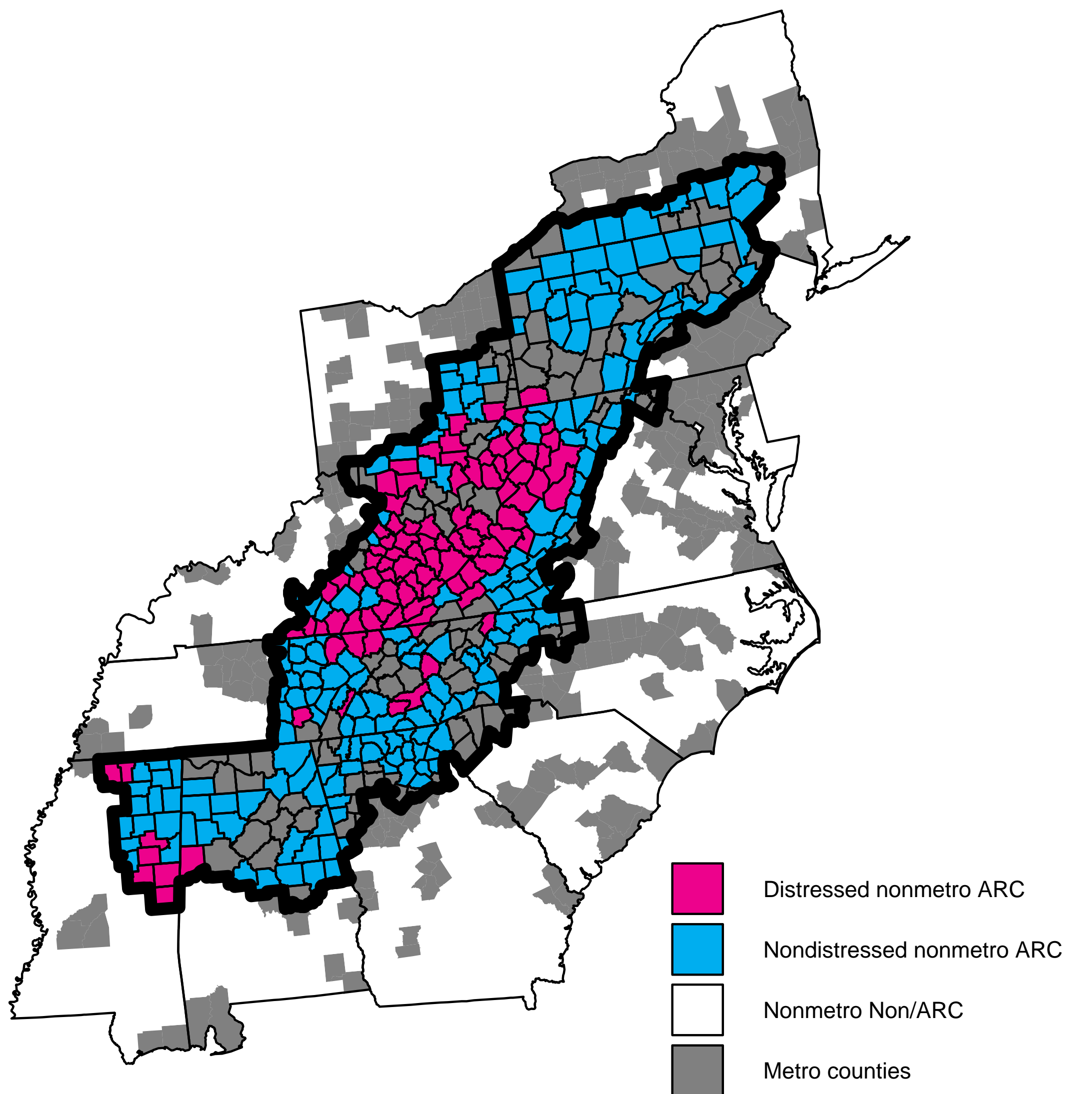
Small general assistance programs tend to help specific regions or places facing long-term economic challenges. Some of these programs are getting more funds this year than last. For example, the Appalachian Regional Commission's (ARC) programs will get $170 million in 1998, $10 million more than the year before. Included in the $170 million

is about $58 million for area development, $103 million for highways, and $6 million for local development districts and technical assistance. The ARC plans to spend $15 million over 3 years on its new entrepreneurship program to help create home-grown businesses. This program provides financial, technical, managerial, and entrepreneurial training assistance, and helps with technology transfer and the creation and expansion of entrepreneurial networks. The Appalachian region, particularly the more distressed counties that are targeted for particular assistance, benefit from ARC's programs (fig. 1). This region will also benefit from $300 million in additional highway funds from the Department of Transportation (see Infrastructure Assistance article).

Figure 1

Counties receiving assistance from the Appalachian Regional Commission (ARC)

Distressed counties receive particular assistance



Note: The Appalachian Regional Commission's boundaries are shown in bold black. Distressed counties have at least 150 percent of the U.S. unemployment rate (9.3 percent), 150 percent of the U.S. poverty rate (19.7 percent), and less than 67 percent of the U.S. per capita market income ($12,074) or 200 percent poverty and one other indicator.
Source: ERS calculation using data from the Appalachian Regional Commission.

Interior Department payments in lieu of taxes go to areas that must forego local taxes on Federal lands within their jurisdictions. Funding for this program, which primarily benefits the West with its substantial Federal land holdings, rises from $114 million to $120 million.

USDA's Forest Service helps distressed timber-dependent and persistent-poverty communities diversify their economies and build development capacity through its economic recovery and rural development programs. Funding for these programs falls from $10.5 million to $8.9 million in 1998. However, USDA's Resource Conservation and Development (RC&D) program, which provides assistance to 315 designated RC&D areas to address local environmental, economic, and social needs, gets an increase in funding, from $29 million to $34 million. USDA's rural economic development grants and loans, which cover project feasibility studies and startup costs, incubators, and other rural development activities, also see program funding rise in 1998: loans will rise from $12 million to $25 million; grant funding remains constant at $11 million.

Disaster Relief Legislation Provides Supplemental Funds Benefiting Many Distressed Rural Areas

The Disaster Relief Legislation Act of June 1997 provided $5.5 billion in supplemental funds for disaster relief. Much of the assistance went to flood-affected areas of the upper Midwest. The act provided the following supplemental funds: $3.5 billion for FEMA flood relief in the upper plains, the Ohio Valley, and the Pacific Northwest, $100 million for Community Development Block Grants (CDBG) that HUD is directing to the upper Midwest (and additional CDBG funding for other disaster areas), $650 million for emergency highway repairs, $390 million for the U.S. Army Corps of Engineers, $161 million for USDA's watershed and flood prevention programs, and $58 million for USDA's Women, Infants, and Children (WIC) nutrition aid. While most of this money went for assistance in 1997, some extends into 1998.

This emergency assistance was paid for out of rescissions (reductions) of other programs. In some cases, this resulted in reduced aid for general assistance programs. For example, USDA's new Fund for Rural America, which got its first $100 million in funding in January 1997, lost $20 million through rescission—half of the reduction came from research supporting rural development and half came from rural development project funding. This program will not receive the second of its three originally scheduled $100-million fund infusions until October 1, 1998. Consequently, for fiscal year 1998, the program has only $34 million in unobligated carryover funds for CSREES research.

Empowerment Zones and Brownfields Initiatives Expanded

The 1997 tax legislation authorized the creation of a second round of Empowerment Zones (EZ's), including 15 urban EZ's and 5 rural EZ's, to be designated by the end of 1998. Four of the new rural EZ's will go to rural areas with high poverty; communities with population outmigration are eligible for the fifth rural EZ. The new rural EZ's, which will be designated and administered by USDA, will be eligible for the following EZ tax incentives over a 10-year period: (1) up to $60 million in tax-exempt bonds for each zone, not subject to State volume caps, to be used on development projects, (2) additional section 179 expensing deduction for appreciable tangible property (not land) investments, (3) Brownfields deductions (see below), and (4) qualified zone academy bonds. The empowerment zones would also qualify for work opportunity tax credits covering 40 percent of first year earnings paid to special "target" groups of workers, though these credits are currently set to expire at the end of June 1998. The new zones do not receive the employer wage tax credits that the first round of EZ's got. Still to be decided is whether the new zones will receive social service block grant funds, as the Administration has proposed.

Meanwhile, the Empowerment Zone/Enterprise Community (EZ/EC) program continues to help the first round of rural EZ/EC's, which includes 3 rural EZ's and 30 rural EC's (which get substantially less funding than the EZ's). The new tax legislation liberalized the defini-

tions of zone businesses qualified to receive tax assistance, but otherwise will not affect the operation of this first round of rural EZ/EC's. The 33 rural EZ/EC's began receiving assistance in 1995. By January 1998, they had drawn down $62 million of their $208 million in Social Service Block Grants (SSBG) allocated to them as part of the program. These communities are also receiving increasing amounts of other assistance, resulting in an additional $617 million in public and private investment. For example, rural EZ/EC's got $55 million in earmarked USDA funds for infrastructure and business assistance in 1996 and $59 million in 1997. In addition, EZ/EC's qualify for priority points when competing for funds from many other Federal programs.

In 1997, a new multi-agency Brownfields National Partnership was announced, expanding the existing Brownfields initiative. When it began in 1993, this was an EPA initiative aimed at helping clean up polluted development sites so they could be redeveloped. As of 1997, about $20 million had been spent on this program. The new strategy involves more money—about $300 million has been proposed over 2 years—and coordinated assistance from other Federal agencies. For example, under the new plan, the Environmental Protection Agency (EPA) will fund assessment and cleanup operations and related training, HUD will provide community development and housing assistance, and EDA and the Small Business Administration (SBA) will provide economic development assistance. In total, 15 Federal agencies are involved in this new Brownfields National Partnership. To fund this initiative in 1998, EPA was authorized to spend about $85 million; HUD may spend $25 million from CDBG-set-aside funds and will target section 108 loan guarantee assistance to this effort.

To further the goals of this initiative, a new Brownfields tax incentive was created as part of the 1997 tax legislation. This tax incentive allows businesses to deduct environmental cleanup costs associated with Brownfield sites that are certified by States as having potentially hazardous substances. The tax benefits are limited to sites within EZ/EC's or any census tract with a 20-percent or greater poverty rate. While most Brownfields are located in urban areas, some high-poverty rural areas should benefit from this initiative, which should particularly benefit those places where land available for development is scarce (such as in mountainous areas like the Rockies or the Appalachians).

Other Initiatives Provide New or Additional Assistance

The Community Development Financial Institutions (CDFI) initiative also got an increase in funding, from $50 million in 1997 to $90 million in 1998. This initiative, which began providing assistance in 1996, revitalizes distressed urban and rural communities by enhancing the ability of selected financial organizations to extend credit and provide technical assistance to promote community development. CDFI's provide a wide range of financial products and services, including mortgage financing to first-time homebuyers, rental housing rehabilitation, startup business loans, and basic retail/consumer financial services for low-income residents. The 1998 funding includes $22 million for Bank Enterprise awards extending credit to distressed areas, $40 million for nonloan assistance to CDFI's, and $20 million for training and technical assistance.

A new American Heritage River Initiative will help restore and revitalize waterfront areas along outstanding stretches of America's rivers. Communities have nominated sites to be considered for this status. The President will select 10 of these American Heritage Rivers in 1998, the first year of this initiative. Partnerships will be created from the community up, through local, State, tribal, and Federal governments, rather than from the top down. Federal agencies will refocus resources from existing Federal programs to provide particular assistance to these areas.

The Northwest Economic Adjustment Initiative will increase its funding in its last year, 1998. This initiative committed $1.2 billion over 5 years, beginning in 1994, to assist businesses, workers, tribes, and communities hurt by reduced Federal timber harvests in California, Oregon, and Washington. Rural areas are the primary beneficiaries. Financial and technical assistance comes from various Federal agencies (USDA, Labor, EDA, EPA, HUD, Interior), allowing a comprehensive approach to revitalization, coordinated with

State and local efforts. Funding for the initiative began at $248 million in 1994, peaked at $268 million in 1995, dropped to $260 million in 1996 and $234 million in 1997. In 1998, the final year of the program, funding is expected to increase to $278 million. Much of this money comes from existing programs that are giving more priority to these places than before. *[Rick Reeder, 202-694-5360, rreeder@econ.ag.gov]*

Transportation Programs Received Largest Funding Increases

Funding increased or remained unchanged in 1998 for most Federal infrastructure programs. Important rural infrastructure activities include stopgap funding of the Nation's highway programs, rail freight merger issues, and increased funding for rural air service.

A wide array of infrastructure is supported by Federal assistance. Although a few changes were made in funding of environmental infrastructure, such as drinking water and wastewater systems, more significant changes affected transportation infrastructure in fiscal year 1998. Program activity generally is increasing for most other infrastructure programs important to rural areas, such as rural electric and telecommunications, community facilities loans, public works grants, and Forest Service payments for schools and roads.

Few Changes to Environmental Infrastructure Programs

The Environmental Protection Agency's (EPA) Drinking Water State Revolving Fund (SRF) program, which capitalizes State revolving loan funds to finance new and improved local drinking water systems, has received $725 million in Federal funding for fiscal year 1998 (references to years refer to fiscal years) (table 1). Another EPA program, the Hardship Grants Program for Rural Communities, which finances the construction of wastewater treatment facilities and complements the $1.35-billion (1998) Clean Water SRF program, continues to operate under a $50-million appropriation provided in fiscal year 1996. Under this program, small (fewer than 3,000 residents), disadvantaged (high unemployment, low income) rural communities are eligible for assistance in planning, designing, and constructing wastewater treatment facilities.

The largest USDA infrastructure program, the Water and Waste Disposal Program, provides loans and grants to small (not in excess of 10,000 residents) rural communities for establishing, expanding, and modernizing water treatment and waste disposal facilities. This program has received $1.27 billion for 1998, a 6-percent reduction from the prior year. This aid supports USDA's Water 2000 initiative, which targets Federal investment to rural communities having the most serious drinking water quality, quantity, and dependability problems. According to a 1995 estimate, more than 2.4 million rural Americans have deficiencies in their water supply, including 1 million rural residents that lack complete plumbing facilities. The highest levels of aid go to totally rural and persistant-poverty counties.

Funding Up Sharply for Most Transportation Programs

Authorization for the multiyear transportation act (the 1991 Intermodal Surface Transportation Efficiency Act, or ISTEA) expired at the end of September 1997 and funding for surface transportation programs began operating on a stop-gap basis, pending a final agreement on long-term reauthorization. The Department of Transportation's (DOT) Highway Planning and Construction Program, which provide grants for Federal-aid highways, is funded at a record $23.3 billion for 1998, up 11 percent from the 1997 funding level. This program is important in many nonmetro counties, especially in the West where per capita allocations are highest. The Nonurbanized Area Formula Program (section 5311), which provides money for rural public transportation, has received $134 million for 1998, a 6-percent increase, and is especially important in parts of the Northeast.

The $1.7-billion (1998) Airport Improvement program, which provides grants for airport capital projects, such as runway repaving, control tower improvements, and aviation safety projects, has received a 16-percent increase in funding for 1998. The $50-million (1998) Essential Air Services program, which funds air service for small communities that lost it after deregulation, has received a nearly 100-percent funding increase for 1998. The increase was attributable to the development of new funding sources for this program, which provided for a more stable revenue stream. This program mostly benefits a small number of rural communities mainly in the Midwest, the Rocky Mountain States, and Alaska (fig. 1).

Table 1

Summary of selected rural infrastructure programs

Most infrastructure programs had funding increases in 1998

Program	Federal funding by fiscal year: 1997	1998 projected	Change	Rural areas most affected by the program
	Billion dollars	Billion dollars	Percent	
USDA rural water and waste disposal grants and loans	1.36	1.27	-6	Totally rural and persistent-poverty counties
USDA electric loans	.82	.93	12	Same as above
USDA Community Facilities Loans	.22	.36	63	Totally rural counties in the South
USDA Distance Learning and Telemedicine Loans and Grants	.16	.16	3	Rural areas in general
DOT Highway Planning and Construction Program	20.90	23.30	11	Counties in the West
DOT Airport Improvement Program	1.46	1.70	16	Services-dependent and Federal land counties
DOT Nonurbanized Area Formula Program	.12	.13	6	Counties in the Northeast
EPA clean water State revolving fund (SRF)	1.35	1.35	0	Government counties in the South
EPA drinking water SRF	1.28	.73	-43[1]	Disadvantaged communities with small water systems
EDA public works grants	.17	.18	8	Manufacturing counties

Note: USDA = U.S. Department of Agriculture. DOT= U.S. Department of Transportation. EPA = U.S. Environmental Protection Agency. EDA = Economic Development Administration, U.S. Department of Commerce.

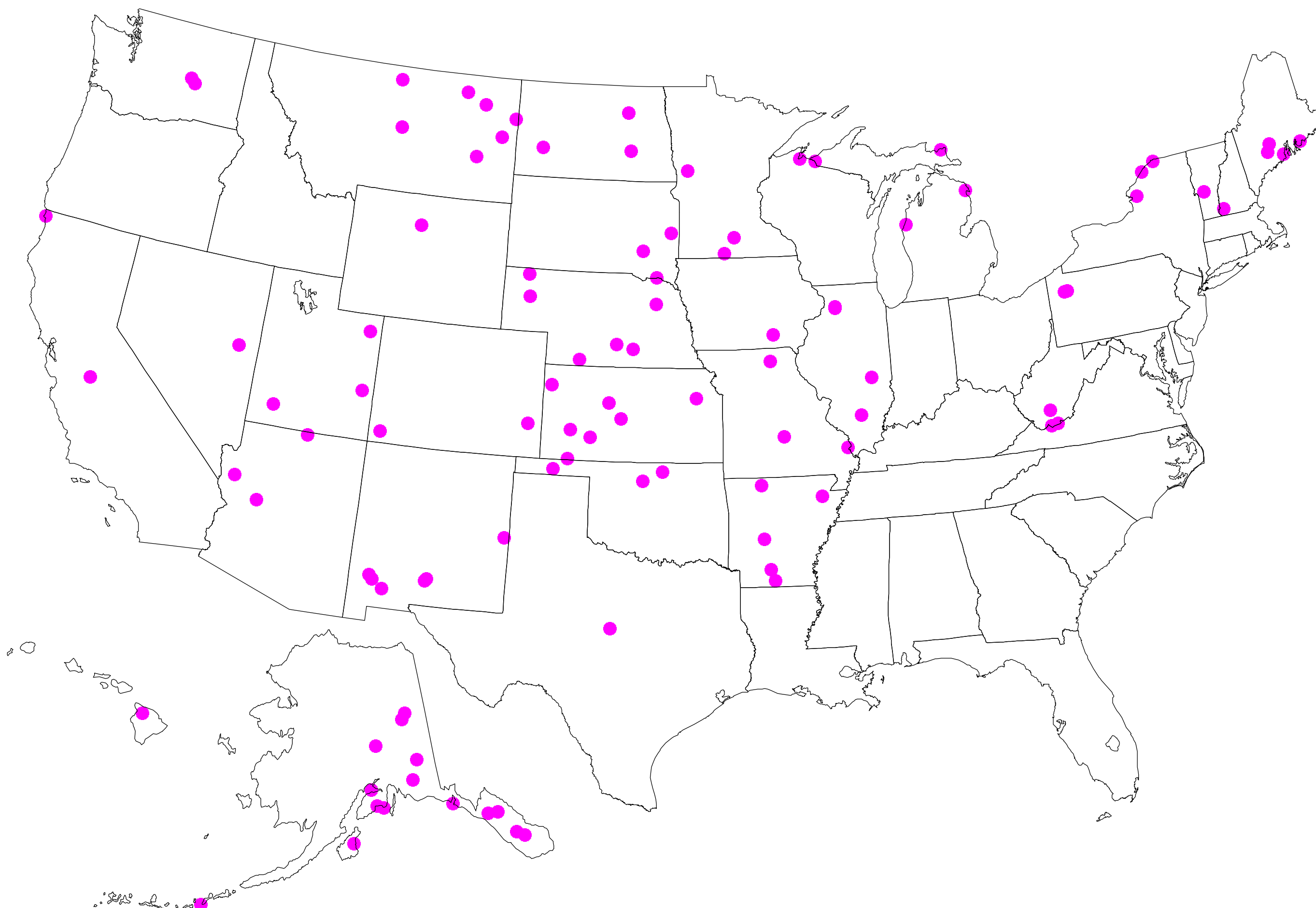
[1]Funding for the Drinking Water SRF in 1997 includes a transfer of money from 1996, resulting in what appears to be a decline for 1998.

Source: *Budget of the United States Government, Fiscal Year 1999*.

Amtrak took a 6-percent funding cut for 1998, making $793 million available for passenger rail activities this year. But Amtrak also received a $2.3-billion infusion for rail capital improvements, payable in two equal installments in fiscal years 1998 and 1999 (P.L. 105-34). While the impact of these added funds on rural passenger rail service is still unclear, most small towns will probably not be significantly affected because relatively few nonmetro communities have Amtrak service (fig. 2). The Local Rail Freight Assistance program, which provides money for track rehabilitation in primarily rural areas, received no new funding, but it continues to operate on carryover funds.

Figure 1
Communities served by Essential Air Services program, 1997

Most aid goes to communities in the Midwest, Rocky Mountain States, and Alaska



Source: Calculated by ERS using data from the U.S. Department of Transportation.

A big issue for 1998 is the proposed purchase of the Consolidated Rail Corporation (commonly referred to as Conrail) by Norfolk Southern and CSX railroads. The potential impact of such a merger on competition in rail freight service in the East will be an important issue for the Surface Transportation Board as it decides whether to approve the merger. This decision, expected sometime in 1998, may be influenced by severe rail freight congestion resulting from the recent merger between Union Pacific and Southern Pacific railroads.

The Appalachian Development Highway System (ADHS) of the Appalachian Regional Commission, whose stated objective is to provide Appalachia with a modern system of four-lane highways, received $94 million in fiscal year 1998, a slight decrease of 4 percent from 1997 levels. But funding for this program was also greatly boosted by an additional $300 million in supplemental money to be administered by the Department of Transportation (P.L. 105-66).

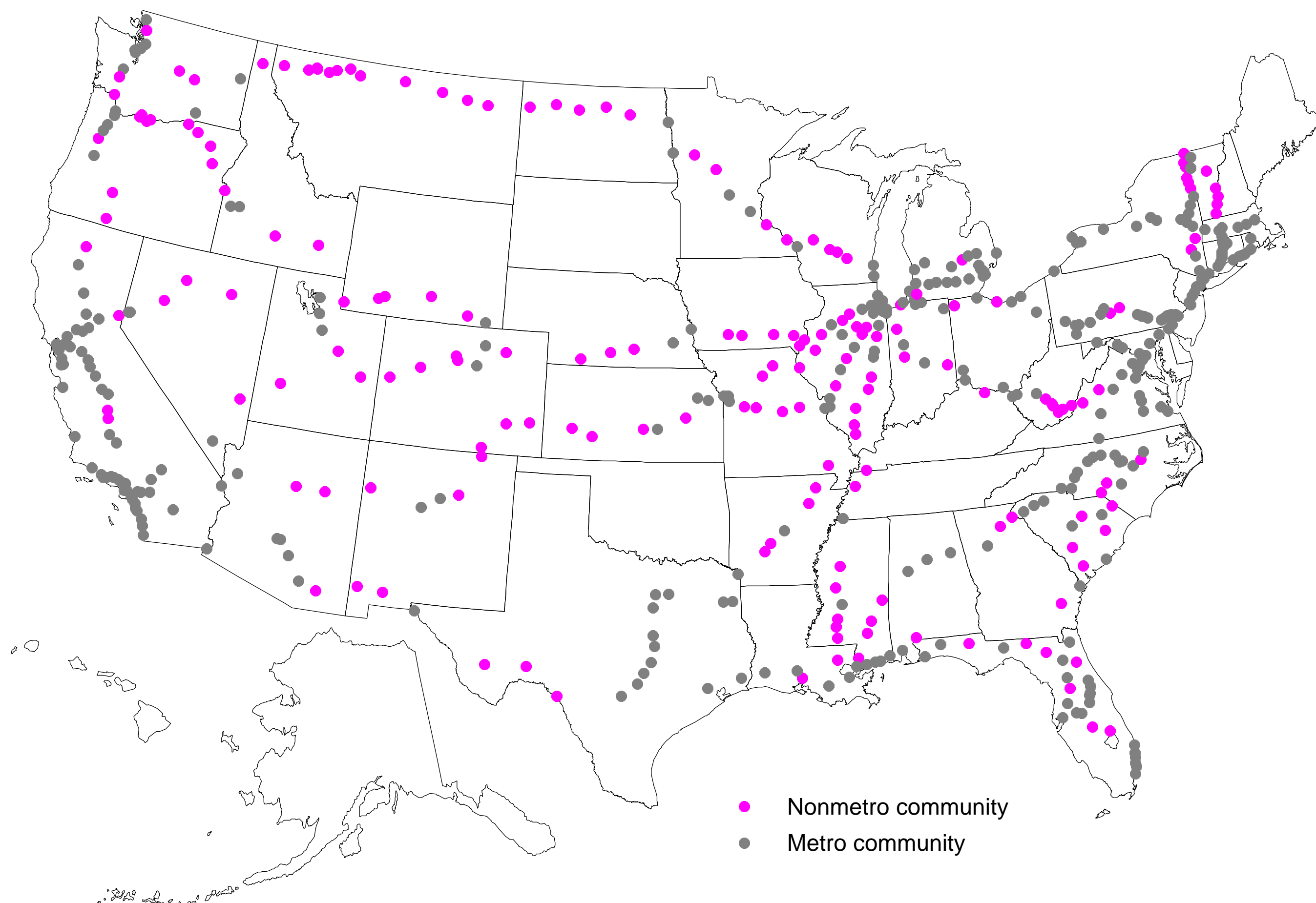
Other Infrastructure Programs

Except for the Water and Waste Disposal Program, USDA's infrastructure programs received funding increases for fiscal year 1998. For example, the Rural Housing

Figure 2

Communities served by Amtrak, June 1996

Although most towns lack passenger rail service, it remains important to those towns served



Note: Amtrak currently has no service in Alaska, Hawaii, Maine, Oklahoma, or South Dakota (although passenger rail service is available in Alaska through Alaska Rail). Map excludes Amtrak Thruway Bus service.

Source: Calculated by ERS using data from Amtrak.

Service's $359-million (1998) Community Facilities Loan program, which provides loans for essential community facilities in rural areas, got a 63-percent boost in funding compared with 1997. Funds are allocated to each State proportionately based on its rural population, with the program mainly assisting totally rural areas in the South in recent years. The Forest Service's $261-million (1998) Payments to States program, which provides grants for public schools and roads on national forest lands, grew by 12 percent.

Economic Development Administration (EDA) public works grants help distressed communities create jobs by attracting new industries, promoting business expansion, and diversifying local economies. This program particularly benefits rural manufacturing counties. EDA funds have been used for a variety of public facilities, such as water and sewer systems, industrial access roads, port and railroad facilities, schools, and business incubators. Funding for the EDA Public Works Grants program is increased 8 percent for 1998, to $178 million.

The Tennessee Valley Authority (TVA), the quasi-Federal agency that provides flood control, navigation, and electric power in the Tennessee Valley region, has received $70 million in Federal appropriations for 1998. This 34-percent decrease from 1997 funding levels is an attempt to eliminate Federal subsidies for TVA.

Funding for most telecommunication programs should increase in 1998. USDA's $495-million (1998) telecommunications loans are projected to grow sharply, by 76 percent, over 1997 levels, and the $175-million (1998) Rural Telephone Bank loans are projected to increase by 75 percent. These programs, important in totally rural counties, provide loans for upgrading and expanding telecommunications facilities that serve nonmetro residents. Funding for USDA's $163-million Distance Learning and Telemedicine program, which provides loans and grants to improve rural education and health care through telecommunications, grew by 3 percent in 1998. The Commerce Department's Information Infrastructure Grants program, which promotes the widespread use of telecommunications (the so-called Information Super Highway) to improve the quality and accessibility of various teleservices, such as health care and education, has received $18 million for 1998, a 14-percent cut.

Funding for USDA's $925-million (1998) Electric Loan program, which provides loans for upgrading and expanding electric services to rural residents, is projected to grow by 12 percent in 1998. This aid supplements money available from private credit sources and is most important to rural residents in totally rural areas and persistent-poverty counties. *[Dennis Brown, 202-694-5338, dennisb@econ.ag.gov]*

Strong Economy Energizes Commitment to Target Funding to Underserved

Federal agencies administering programs to assist small business continue to devise policies that better monitor program performance while increasing efficiencies to allow budget appropriations to accomplish more. As a part of the change in management style, agencies are requiring private sector participants to take on more risk and management responsibilities in exchange for Federal guarantees. Through this process, agencies are finding ways to cooperate with the private sector to better meet the social goals of these programs.

The importance of small business to the general economy is used to support the current Administration's budget increases for nearly all business assistance programs. According to data from the Commerce Department's Survey of Current Business that has been compiled by the Office of Advocacy, a division of the Small Business Administration, small businesses were central to the gross domestic product's strong 4.4-percent growth in 1996 and nonfarm employment rise of 2.5 percent. Nationwide, new firms rose by 2.8 percent over 1995, while business terminations decreased by 1.6 percent. Small-firm-dominated industries added 1.5 million net new jobs.

Other studies have shown that 3.5 million businesses are owned by minorities in the United States. However, if the percentage of minority businesses were equal to the percentage of minorities in the overall population, there would be 6.8 million such businesses. The apparent discrepancies in how minorities have participated in the current economic expansion has focused recent efforts to sharply increase Federal assistance to small and minority-owned businesses and to make more Federal capital available to minority entrepreneurs. In addition to increasing funding, agencies are establishing more rigorous methods of evaluating whether the targeted groups are being served. Secretary of Agriculture Dan Glickman established the National Office of Outreach to assure that small and minority businesses have full access to all USDA programs and services.

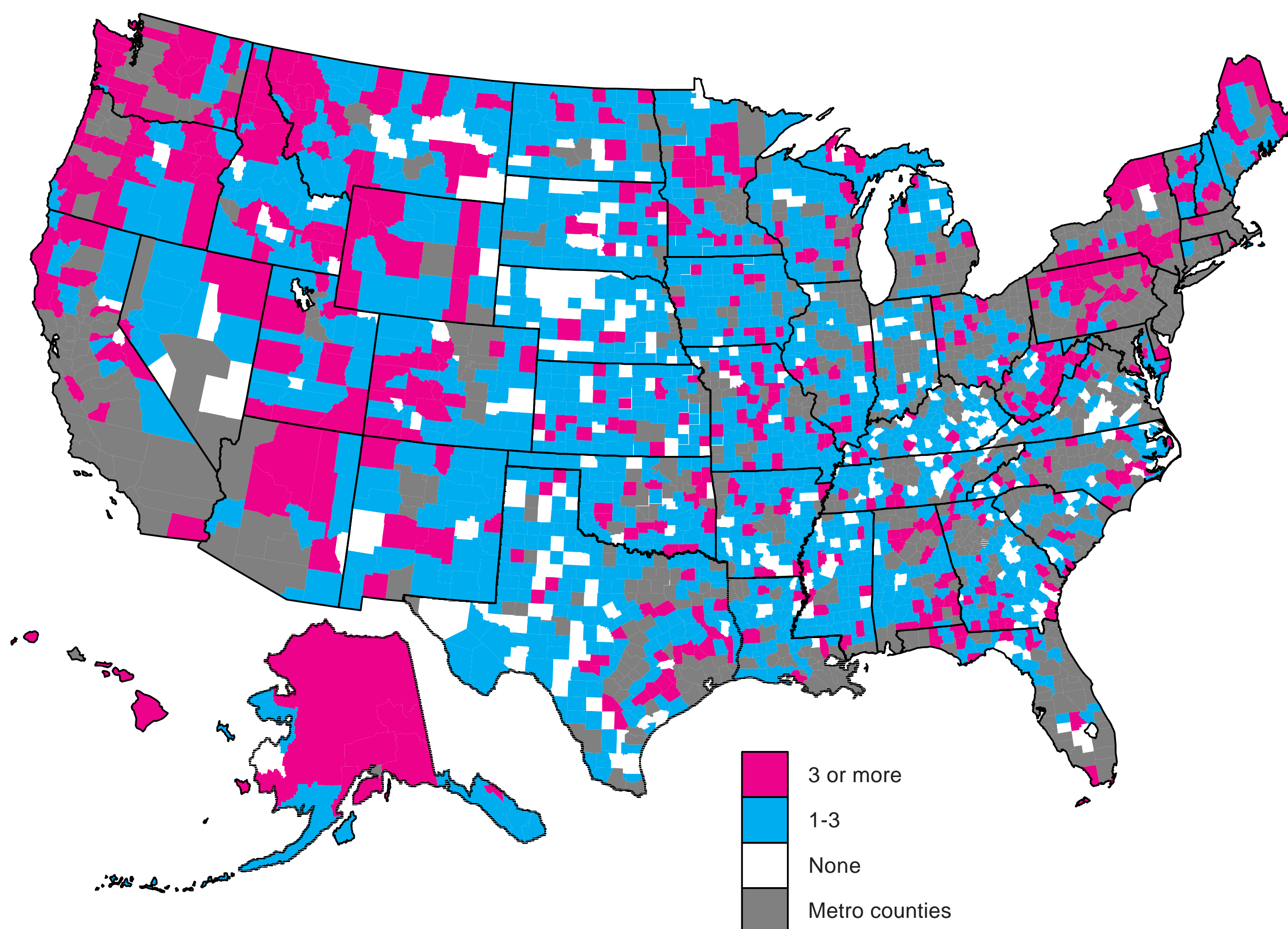
Of the 2,276 counties designated as nonmetro (or rural) in 1996, 320 received no business program assistance at all (fig. 1). By contrast, more than 400 counties received assistance from three or more programs. Those counties not receiving assistance were concentrated in the Great Plains and in various parts of the South. The location of these counties suggests that areas with little or no population growth or that are seriously underdeveloped may be less likely to generate demand for credit and, thus, may make less, or no, use of credit-market-enhancing programs. This assistance pattern may also reflect a possible need to better inform the public of what Federal small-business assistance is available.

Expansion in Program Activity Expected to Continue

Over the last 5 years, the level of funding for business assistance programs has steadily increased and the types of assistance offered have broadened. Over 20 programs are available to make capital more accessible at reduced interest rates; and many of these programs provide technical assistance to increase the small business borrower's probabilities of success. The largest programs are guaranteed loan programs that increasingly rely on private sector lenders to screen applicants and monitor loan performance. Beginning in the early 1990's and even more so in the last two budget cycles, agencies assisting small business development have energetically developed new programs to better target microbusinesses and those businesses not well suited to traditional borrower-lender relationships.

The Small Business Administration (SBA). SBA offers over 15 different programs to meet the varying financial needs of small business. SBA's largest business assistance program, the section 7(a) guaranteed loan program, is projected to increase its program level from $9 billion in 1997 to $9.2 billion in 1998 (all references to years refer to fiscal years). This program is available to both metro and nonmetro areas, but is of particular importance to nonmetro areas, many of which rely almost exclusively on small businesses for their employment growth. The number and volume of loans made under the 7(a) guarantee program have increased dramatically in recent years. In 1992, SBA made or guaranteed approximately 24,000 loans totaling about $5.9 billion. By 1997, that increased to approximately 45,000 loans totaling about $9.5 billion. As the number of loans and volume outstanding have increased, the average percentage of the loan that

Figure 1
Number of small business programs benefiting rural counties, fiscal year 1996
Many of the 320 nonmetro counties without small business assistance are in the Great Plains



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

was guaranteed has declined: 81 percent was guaranteed before 1992, while 73 percent was guaranteed in 1997. In 1996, nonmetro areas received $24 in per capita small business 7(a) guarantee assistance, somewhat less than the $27 received in metro areas; the nonmetro areas that benefited most were in counties in the West that were not adjacent to metro areas, and in counties specializing in services and farming.

The second largest SBA program, the section 504 Certified Development Loan Company program, is projected to increase its obligations from $1.4 billion to $2 billion in 1998. The section 504 program has also significantly grown. In 1992, the 504 program assisted about 290 Certified Development Companies (CDC's), making about 2,000 long-term loans totaling nearly $560 million. In 1997, about 6,900 loans were made through the same network of 290 or so CDC's totaling $1.4 billion. In 1996, nonmetro counties on average received just over $8 per capita in 504 loan guarantees compared with over $11 per capita for metro ones. Among nonmetro areas, nonadjacent nonmetro counties received more funding per capita than those adjacent to metro counties, and western counties and counties emphasizing service industries benefited the most (table 1).

USDA's Rural Business-Cooperative Service (RBS). RBS's main business assistance programs are the Business and Industry (B&I) program, the Intermediary Relending

Table 1
Selected business assistance programs
Most business loan guarantee programs are expected to increase or maintain steady loan activity in 1998

Program	Program level by fiscal year[1] 1997 actual	1998 estimate	Change	Rural areas most affected by the program
	—Billion dollars—		Percent	
SBA 7(a) business loan guarantees	9.00	9.20	2	Services, farming, and Federal lands counties in West
SBA Certified Development Loan Company guarantee (section 504)	1.42	2.00	41	Services counties in West
SBA disaster loans	.96	.79	-18	Place experiencing disasters
RBS Business and Industry loan guarantees (B&I)	.82	1.00	22	Service and mining counties in West
RBS Intermediary Relending Program	.04	.04	0	Farming, Government, nonadjacent, and Federal lands counties in West
RBS Rural Business Enterprise Grants (RBEG)	.05	.04	-20	Farming, service, and transfer counties in West and South
EDA Economic Adjustment[2] Grants	.03	.03	0	Farming and totally rural counties in West

Note: EDA = Economic Development Administration, U.S. Department of Commerce. RBS = Rural Business-Cooperative Service, U.S. Department of Agriculture. SBA = Small Business Administration.
[1] Budget authority used for grant programs; projected loan levels (obligations or program level) used for loan programs. Note that in some cases, budget authority may be falling at the same time that projected loan obligations are rising. 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] This represents just part of the larger EDAP program (see text); many of these grants are used to support revolving loan funds that issue loans to businesses; hence, a larger number of loans will result than indicated by this budget authority amount.
Source: *Budget of the United States Government, Fiscal Year 1998.*

Program (IRP), and the Rural Business Enterprise Grants (RBEG) program. Of the three agencies involved in providing direct financial assistance to small businesses, RBS is the only one to have program restrictions regarding size of community. RBS's programs are generally available to communities with less than 50,000 in population; in the case of the IRP, city populations are limited to 25,000.

The B&I program includes both guaranteed loans and direct loans. The larger guaranteed program created about $820 million in loan activity, through its guarantees, in 1997. The program is projected to create upwards of $1 billion in loan activity in 1998, for an

increase of 22 percent. The IRP is expected to remain steady and provide around $40 million in low interest-rate loans to capitalize revolving loan funds in rural areas. The RBEG program provided about $50 million in grants in 1997, but, due to budgetary constraints, is projected to decline in activity by about 20 percent for 1998.

Commerce Department's Economic Development Administration (EDA). EDA operates another program benefiting rural businesses, the Economic Adjustment Program (EAP). As the name implies, the EAP helps local areas make adjustments to severe changes in their economic situations. Funding for the EAP remains steady at about $31 million in 1998. Approximately 10 percent of this amount will be available to make grants to capitalize revolving loan funds. Through the revolving loan funds, EAP provides most of its assistance to small businesses.

Reinvention Efforts Continue to Improve Business Assistance Programs

Rapidly evolving financial markets are changing both the structure of intermediaries as well as the types of clients they are serving. Competition within and across business lines, along with changing regulatory structures and increasingly sophisticated analytical techniques, have lenders seeking out some borrowers previously thought to be uncreditworthy. In addition, funds are flowing more readily to their most productive uses, and information quality and quantity has increased as well. Together, these changes are affecting the roles, risks, and operations of Federal credit programs. If the main Federal role is to provide credit that private markets would not otherwise provide, then Federal credit programs must evolve as private credit markets evolve, and the success of these programs must be measured meaningfully. Implementation of the Government Performance and Results Act (GPRA) will help to assess whether programs are achieving their intended results in practice—and will improve the odds for success. The Federal Credit Reform Act of 1990 began to reconcile the tension between achieving social goals or purposes and "business-like" financial management. Implementation of GPRA is bringing the realization that a program's social success and financial success are two facets of the same goal.

SBA, RBS, and EDA have each become more efficient as a result of efforts to implement the requirements of GPRA. Portfolio performance has improved for the SBA's 7(a) guarantee program, and RBS's B&I loan portfolio loss rates have declined. Additional improvements have come as better loan information is gathered and other technical refinements have been made allowing subsidy rates on Federal credit assistance to be lowered. This results directly in lower cost to the agency per dollar of loan activity.

The Future of Small Business Credit Assistance

As more has been learned about how Federal credit programs can complement private markets, program outcomes have become more successful. Previous successes are resulting in an across-the-board refocusing of primary program missions. In keeping with the goal of making credit available where it otherwise would not be, each agency that administers a small business assistance program in 1998 is pushing program accessibility to the poorest and other neglected members of the economy.

The SBA Microloan Program is targeted to very small businesses with financing needs of $25,000 or less. This program was made permanent in December 1997 under P.L. 105-135. To date, over $65 million has been lent to almost 6,600 microborrowers. In addition to very small loans, the program offers business-based technical assistance to each microloan client.

In addition to the SBA Microloan Program, SBA will be focusing its programs, performance, and policy objectives on increasing small business opportunities by (1) concentrating on traditionally underserved small businesses; (2) offering specialized financing products, such as venture capital, export financing, and bonding opportunities; (3) improving methods of providing credit assistance through electronic lending, less documentation, centralized functions, and one-stop capital access points; (4) reducing costs

by maintaining a high-quality portfolio through an improved liquidation process; and (5) effectively implementing a loan asset sales program. Number four is an example of placing more responsibility for financial performance of a loan on the private sector lender. For the lenders to exercise the loan guarantee, they are now required to liquidate all relevant chattel, which secures the loan. This reduces the guarantee costs for the SBA.

USDA's RBS has implemented similar types of goals and is also requiring more financial responsibility of participating lenders. USDA will also be focusing on meeting the financing needs of persistent-poverty, declining-population, and minority rural areas. One example is the newly revised IRP program, which will be more directly targeted to the poorest rural areas. Also, loan applications will now be approved at the State office rather than the national office. *[George Wallace, 202-694-5369, gwallace@econ.ag.gov]*

Federal Housing Assistance Promotes Homeownership

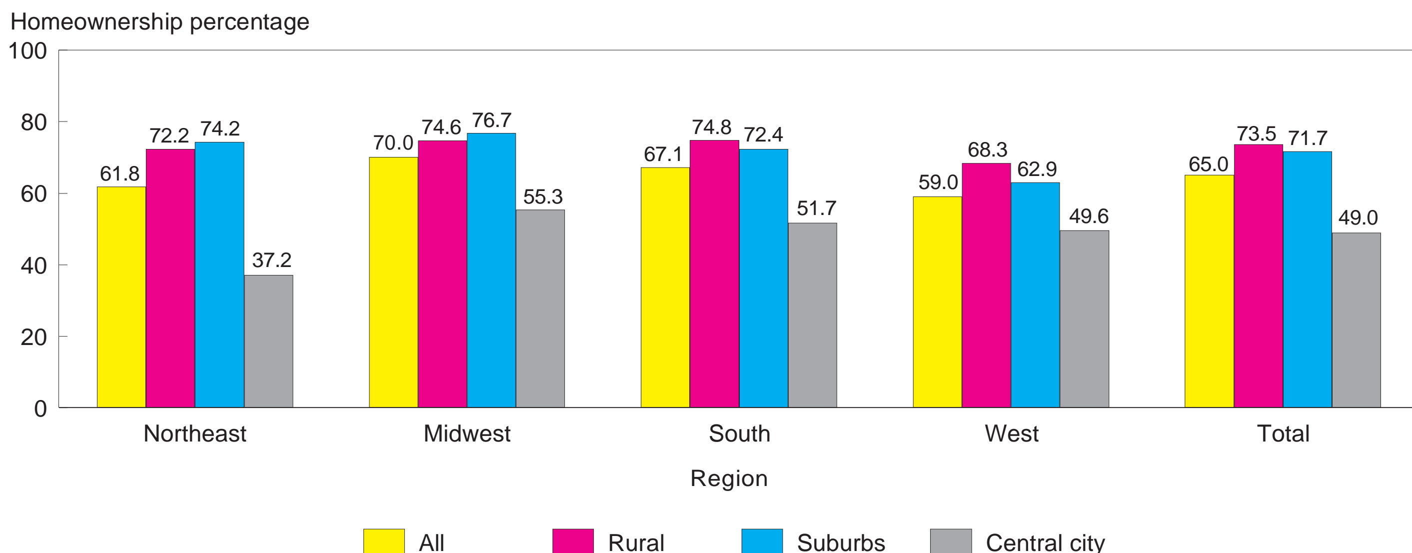
For several years, the rate of homeownership has increased, while the activities of Federal agencies have been targeted at promoting and supporting this trend. These trends are expected to continue, while major changes are proposed for public housing programs.

Most American families (65.7 percent) own their homes. Homeownership is highest in rural America, averaging 73.7 percent for 1997, compared with a similar 72.5 percent for metro suburbs and 49.9 percent in central cities. Homeownership for each of these areas is at its highest level in over a decade, with each up about 0.2 percent from 1996 levels. This is the third consecutive year for across-the-board increases in the homeownership rate. Regionally, rural homeownership rates are higher than those of suburbs in the South and West, but suburban rates were higher in the Northeast and Midwest (fig. 1). Homeownership is most typical for nonminority populations, those neither very young nor old, and families with higher incomes. As homeownership increases, the income gap between owners and renters widens, and the proportion of renters with low incomes increases. But in other ways, dissimilarities between owners and renters are narrowing. Although homeownership is less frequent among minorities, particularly Blacks and Hispanics, the rate of growth in homeowning is most rapid for these minority populations.

Federal housing programs are critical factors in advancing homeownership as the preferred housing alternative for most Americans. The long history of USDA programs that have provided home mortgages to low-income rural families may well have contributed to the particularly high level of homeownership in rural communities. In contrast, housing assistance for low-income urban families has historically relied more on rental assistance.

In both rural and urban America, as more of those who can afford homeownership leave rental housing, the already high share of renters that are low-income continues to grow. Welfare reform is beginning to affect the incomes and lives of many renters, particularly those receiving government housing assistance, including many of those in public housing. Against this background, a number of issues affect rental housing and complicate the debate about appropriate public policy. These issues include who would be assisted, the amount of that assistance, tenant requirements, appropriate local autonomy, and delivery methods (vouchers, public housing, low-income housing tax credits, low-cost construction loans, or rental subsidies).

Figure 1
Homeownership rates by region, 1995
Rural homeownership tops suburbs in South and West



Source: ERS tabulation from American Housing Survey for the United States in 1995.

The amount of direct mortgage lending by Federal agencies is now so small that annual fluctuations are unlikely to have much effect on the level of homeownership (table 1). However, such changes are still very important to the potential borrowers. Because of their low incomes they often have no other way to achieve homeownership. Most direct mortgage lending is done through USDA's section 502 program. Although lending under this program declined somewhat in 1997, higher levels are anticipated for 1998 and have been requested in the President's budget for 1999. This would interrupt a period when each year many of the more heavily subsidized Federal housing programs were reduced in size, and the subsidies provided to each program participant were often lowered. The much less costly USDA section 502 guarantee program has a clientele with relatively higher incomes and charges insurance fees that cover a substantial portion of loan losses and operating costs.

Unless restrained by regulatory ceilings, year-to-year changes in the volume of loan guarantees tend to reflect loan demand rather than the emphasis placed on such activities by the administrating agencies. USDA's section 502 guarantee program has grown each year since its inception, reaching its authorized limit each year. But both the Department of Housing and Urban Development's (HUD's) Federal Housing Administration (FHA) and the Department of Veterans Affairs (VA) insured fewer loans in 1997 than in 1996 and, as

Table 1
Summary of largest housing programs
Projected levels of some Federal housing loan programs are up in 1998, others are down

Program	Program levels by fiscal year: 1997 actual	Program levels by fiscal year: 1998 estimate	Change	Rural areas most affected by the program
	—Billion dollars—		Percent	
USDA/RHS:				
Single family (sec. 502)—				
Direct loans	0.71	1.00	4	Large metro fringe, South and Midwest, retirement and Federal lands counties[1]
Guarantees	2.03	3.02	49	Included above[1]
Multifamily (sec. 515)	.15	.13	-16	West, totally rural, and poverty
Rental assistance	.52	.54	5	West, all but the most urbanized
VA:				
Loan guarantees	24.30	24.80	2	West, urbanized nonmetro and adjacent
HUD:				
FHA single-family mortgage insurance	75.43	82.26	9	West, urbanized nonmetro
Public and Indian	24.08	23.68	-2	West, nonadjacent and high poverty

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

[1] Information on loan distribution combines direct and guaranteed loans in a single category.

Source: ERS calculations based on the Budget and Census's Federal Funds data.

usual, were below their maximum levels. FHA and VA loan guarantees are projected to increase in 1998 because of greater anticipated demand for this assistance.

In addition, two government-sponsored enterprises (GSE's)—the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac)—are major players in home mortgage financing through their secondary-mortgage market activities. They purchase home mortgages made by other lenders and in turn sell securities backed by the assets and income represented by those loans or on occasion hold mortgages as their own investments. Both GSE's have initiatives to increase their purchases of certain categories of mortgages, including those on rural properties.

Fewer Rural Home Buyers Receive Government-Assisted Mortgages

While a substantial minority of both rural and urban households benefit from Federal housing programs, these programs reach a smaller share of rural households. The 1995 American Housing Survey found that 14.6 percent of nonmetro and 24.0 percent of metro home mortgages were either from, or insured by, a Federal government agency (fig. 2).

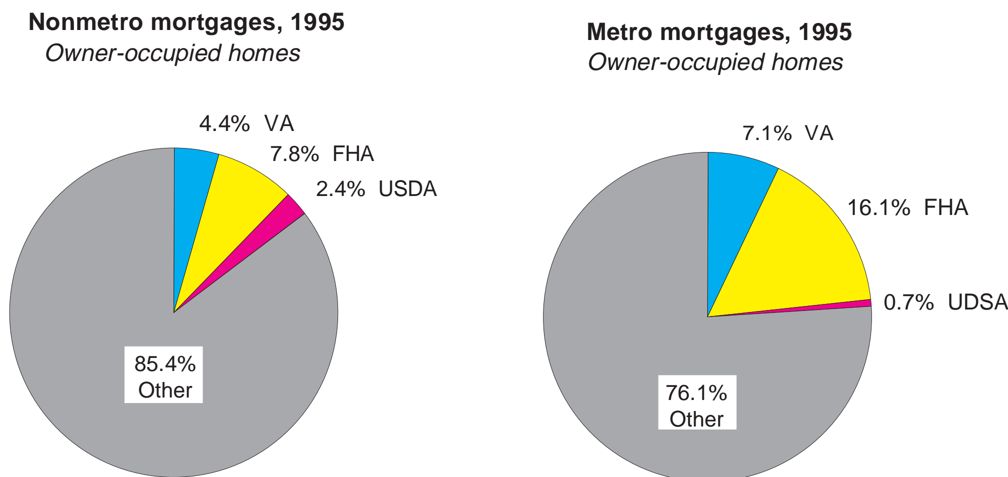
HUD is primarily responsible for housing assistance and, consequently, through the FHA, provides the largest amount of home mortgage assistance, both in urban and rural areas. However, USDA's section 502 direct and guaranteed program, administered by the Rural Housing Service (RHS), also plays an important role. In particular, the section 502 direct loan activity is the only mortgage program targeted to low-income households that otherwise could not afford to be homeowners.

Section 502 loan guarantees are increasing in importance in rural areas. Since its start in fiscal year 1992, the volume of loan guarantees has increased each year, a trend that is expected to continue in fiscal year 1998. From 1992 through 1997 the amount of section 502 direct lending has been declining. As a result, section 502 guarantees are now about three times the dollar amount of direct loans. The 1997 level of direct lending was below that anticipated when the budget was passed, because higher than expected market interest rates in turn raised the amount of subsidy associated with each direct loan. However, both direct and guaranteed lending are expected to rise in 1998.

Figure 2

Use of Federal government mortgage insurance programs, 1995

Rural mortgages are less often Government-insured

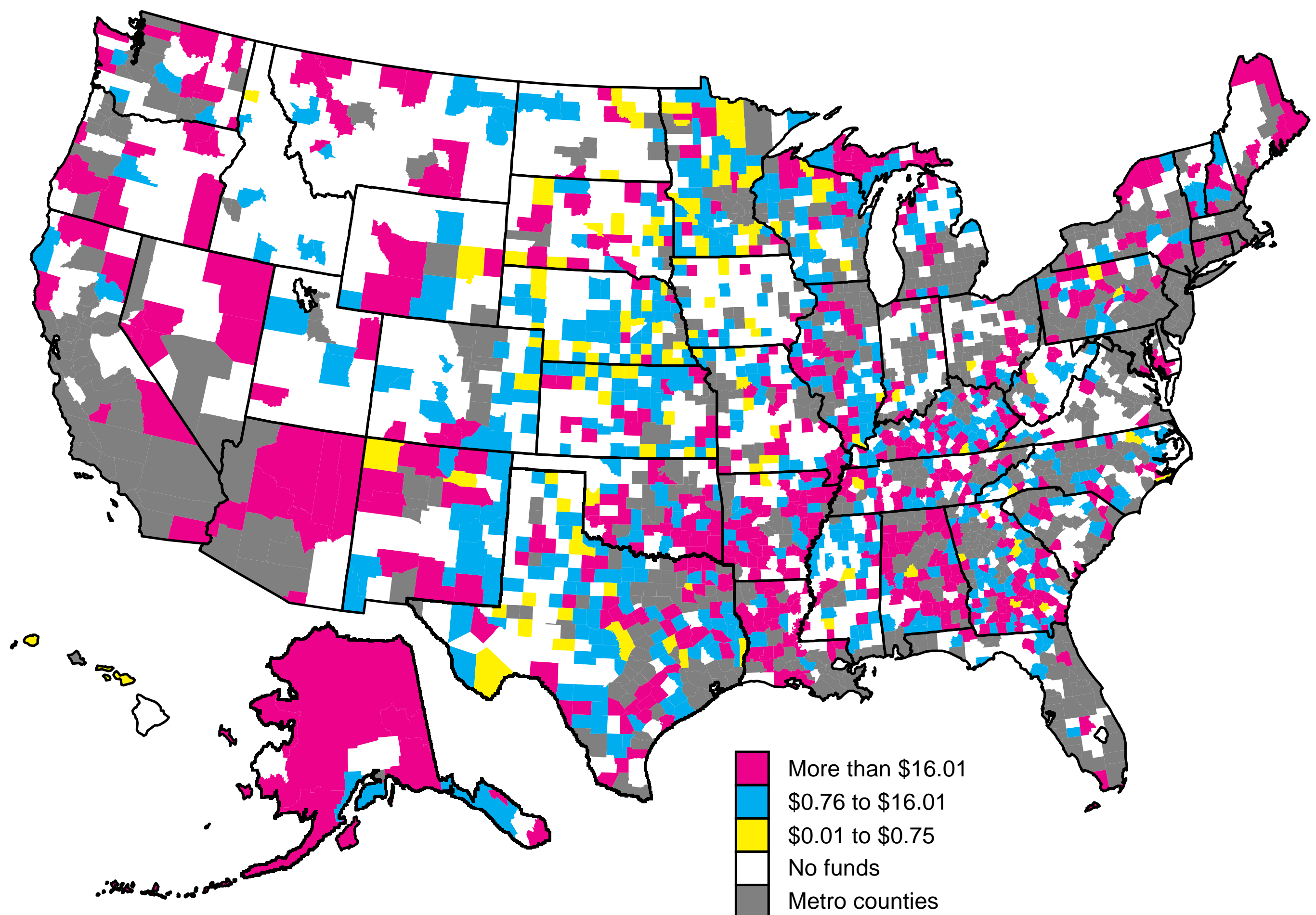


Source: ERS tabulations from American Housing Survey for the United States in 1995.

Government Rental Programs Changing

Rental housing assistance takes many forms. Low-income housing tax credits (LIHTC's) allow developers of low-income housing to borrow funds at below-market interest rates by providing an annual Federal tax credit to investors in limited partnerships that make these loans. The property owner can use the funds for purchase, construction, or rehabilitation, and in turn is obligated to rent a portion of those units to low-income tenants at below-market rates. Each State is allowed a limited number of credits each year, based on its population. The President's 1999 budget proposes an increase in the amount of these credits. Subsidized loans usually provide low-interest financing to a nonprofit, limited-profit, or governmental entity that, in exchange, agrees to certain requirements for providing low-income housing. Rental assistance payments are often used in conjunction with the previously mentioned subsidies to bridge any gap between the rent-paying ability of low-income tenants and the rent payments that are due property owners. Programs providing such assistance to rural tenants are operated by the USDA and HUD. Certificates and vouchers are issued to qualified families for use in paying for qualified housing, which is generally rental and privately owned. Vouchers are quite similar to certificates, but

Figure 3
Per capita HUD public and Indian housing assistance, fiscal year 1996
Higher amounts are in the South and counties with Indian reservations



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

allow recipients to choose from a wider selection of housing units, potentially at a higher tenant cost. Many feel that vouchers' greater flexibility in location will be important for assisting many welfare recipients in their transition to employment. This part of HUD's section 8 program has recently become one of the major rental subsidy activities. Public housing provides 1.3 million publicly owned housing units operated by public housing authorities. While little, if any, new public housing is being built, except to replace demolished units, considerable funding is needed to operate and maintain this housing for those least able to pay rent.

While urban areas receive more Federal funds for rental housing than do rural areas, the difference is much less than that for homeowner programs. In fiscal year 1996, the largest programs for rental housing provided about $95 per capita nationally and $70 per capita in rural areas. Higher rural levels seemed to be in parts of the South, the Appalachian region, and Indian reservations (fig. 3). By comparison, the major homeownership programs provided per capita amounts of $273 nationally and $106 in rural areas.

Owner programs have a clientele base that includes many moderate-income families.Renter programs are almost exclusively focused on the low-income population. Renter programs operate either by subsidizing rents for those unable to afford adequate housing or by promoting an increased supply of low-cost rental housing. Both approaches can be found in a single program, such as the RHS section 515 program where financing costs are subsidized in return for an agreement that units be rented to program participants at reduced rates. HUD's rental assistance is shifting away from such long-term subsidies tied to particular rental units and into more flexible tenant assistance, which gives greater attention to housing vouchers, local control, and homeownership options.

The future direction of Federal government rental assistance is far from clear, though there have been a number of recent changes and more are quite likely. Since the 1970's, the poorest families have been given priority for public housing and tenant rent could not exceed 30 percent of adjusted income (which was often zero). Beginning in 1995, public housing authorities have had more flexibility to set their own rules, including charging a minimum rent (up to $50) and selecting tenants on a basis other than lowest income. But many housing authorities have been hesitant to make changes because this authority must be renewed each year. Various proposals for more permanent changes have been in the legislative process for over a year, and there is some optimism that an agreement will be reached soon. Points of contention include the degree of autonomy given local housing authorities (or governments), minimum and maximum rents, and the allowable income mix of tenants.

More permanent change has come to one segment of public housing, that for American Indians and Alaska Native tribes. New rules, established by 1996 legislation, will give tribal housing authorities more authority, providing $600 million of public housing funds as block grants. While there are still guidelines for the use of these funds, local authorities have much more flexibility than in the past.

Rental Assistance Is USDA's Major Expenditure on Housing Programs

USDA's housing programs, administered by the Rural Housing Service (RHS), provide assistance in rural portions of both nonmetro and metro counties. The section 502 single-family housing program comprised over three-fourths of the agency's total housing loan and grant activity. Most of this amount was related mortgage lending, not the government cost of providing that assistance. In contrast, expenditures for rental subsidies consumed the bulk of RHS's budget.

As discussed earlier, over the last 4 years, the direct lending share of the section 502 program fell, while the number and amount of guarantees grew rapidly. In turn, per borrower program costs have fallen, since only direct loans carry a significant subsidy. Subsidy expenses on new loans were also lowered by changes in program regulations

that increased the effective interest rate on most direct loans. Subsidies on direct loans also rise and fall in tandem with movements in market interest rates. This is because the effective interest rates on most new direct loans are determined by borrower income, without consideration of market interest rates. A major change implemented in fiscal year 1998 provides further cost savings to the Government, mostly through lowering administrative expenses.

RHS is using loan leveraging to reach more low-income borrowers with its limited funds for direct lending. In conjunction with the primary loan from another lender, the RHS makes a reduced-interest loan for the remainder of the total financed amount. RHS has an agreement with Fannie Mae and Freddie Mac that they will purchase the non-RHS portion of such loans. RHS often makes loan-sharing agreements directly with various public, private, and nonprofit entities. Although this increases the number of people that can be assisted, unless the companion loan also carries a greatly reduced interest rate, this program cannot reach RHS's lowest income clientele. In addition, because RHS takes essentially all of the risk exposure for the combined loan, RHS's future loss rate may be higher than if RHS were the sole lender, because it is involved in more loans.

The RHS administers other housing programs for the same rural areas eligible for the section 502 program. The largest of these activities in fiscal year 1996 provided rental assistance for low-income tenants in RHS-financed rental housing. The $520 million in estimated fiscal year 1998 budget authority for rental assistance is two-thirds of the total for all RHS loan and grant programs, exclusive of costs for salaries and expenses. Additionally, RHS's section 515 multifamily housing program provides financing for the construction, purchase, rehabilitation, or repair of low-income rental housing. Over two-thirds of such RHS rental housing assistance, both loan and grant, went to nonmetro areas. Additional RHS programs include such activities as very-low-income home repair, self-help housing, and farm-labor housing. After doubling to $26 million in fiscal year 1997, funding for mutual self-help grants is expected to remain steady in 1998.

FHA Insurance Expands Dominant Role in HUD Housing Programs

HUD's main housing activity is FHA's single-family home mortgage insurance program, which provided over $75 billion of mortgage insurance in fiscal year 1997 and is projected to exceed $82 billion in 1998. Only 6 percent of the amount insured in fiscal year 1996 was in nonmetro areas. These nonmetro loans were concentrated in the West and in counties that were more urbanized. The nonmetro aid distribution of FHA and RHS programs were quite different, with the RHS section 502 program varying little by rurality level and FHA assistance considerably lower in the more rural counties. Totally rural counties not adjacent to a metro area had only $25.29 of FHA loans per capita compared with $98.58 for the most urbanized adjacent counties and the metro average of $263.54.

HUD's multifamily programs receive the bulk of all housing grant funds. In fiscal year 1996, expenditures on the major public housing programs were about $6.2 billion, which was $23.22 per capita nationally and $18.95 in rural areas. On a per capita basis, rural counties with higher funding levels were more often in the West, were isolated from metro centers, or contained Indian reservations.

Major changes have already been made in HUD programs, and others are in the works. HUD programs seem destined to be far fewer in number and much more flexible in how they are used. State and local governments and housing authorities will have greater control over the use of Federal housing assistance. And many program recipients will have a choice in how that assistance is used, including where they will live, and even whether they will rent or purchase a home. Commitment is strong to expand the opportunity for homeownership to a wider audience, reduce the role of large-scale housing projects for the low-income, and respond to changing needs, such as those introduced by welfare reform. As an agency, the future HUD will also be quite different. The total number of HUD employees will drop over 20 percent, with many of these in a few locations

with specialized functions, and far fewer assigned to local offices. Many HUD activities will be consolidated or modified in other ways. While the dust has not yet settled, changes at HUD are underway, significant, and happening quickly.

VA Mortgage Insurance Concentrates in Urban Areas

VA housing loans are expected to total about $25 billion in fiscal year 1998, a nominal increase from 1997. In fiscal year 1996, about 11 percent of VA's housing program activity was in nonmetro areas. Nearly all of that is in the form of guaranteed loans. Rural areas received over $21 per capita of such VA loans, slightly more than half of that received by urban areas. VA nonmetro loan levels were highest in the most urban and adjacent counties ($33.93) and lowest in the most rural and nonadjacent counties ($10.09). By region, nonmetro lending was highest in the West ($36.28) and lowest in the Midwest ($15.24)

Most VA borrowers pay a loan guarantee fee that is a percentage of the loan amount. Fees are higher for certain loans, including those with smaller downpayments. Some special borrowers can receive the loan guarantee at no cost. The only direct loans that VA makes are a very few to finance specially adapted housing for a few disabled veterans. Still outstanding are a number of direct loans made by VA when they also targeted "rural areas where availability of private mortgage funds was limited." *[Jim Mikesell, 202-694-5432, mikesell@econ.ag.gov]*

New Welfare-to-Work Program Helps Adjustment to Welfare Reform

Congress enacted major welfare reform legislation in 1996, devolving much of the responsibility upon the States. In 1997, Congress and the Administration restored certain benefits to legal immigrants and to disabled children. Medical assistance to children of low-income families was extended, and job training programs received additional funding. A Welfare-to-Work program was created in a bold experiment to bring welfare recipients with the most difficult circumstances into the productive labor force.

President Clinton signed into law the Personal Responsibility and Work Opportunity Reconciliation Act (P.L. 104-193) on August 22, 1996. It provided the most significant changes in welfare programs in 60 years (see *Rural Conditions and Trends*, Vol. 8, No. 1). It replaced a host of earlier programs, such as Aid to Families with Dependent Children (AFDC), Job Opportunities and Basic Skills Program (JOBS), and Emergency Assistance (EA), with the new Temporary Assistance for Needy Families (TANF) block grants to States. After decades of complaints about second- and third-generation welfare families and occasional scandals, the new program aimed to move away from cash assistance to families and toward integrating them into the productive work force.

Although most Americans probably visualize the poverty in the stricken center cities of this largely urbanized Nation, around 20 percent of welfare cases live in rural areas. Most of the case load is rural in 14 States—Alaska, Arkansas, Idaho, Kentucky, Mississippi, Montana, New Mexico, North Carolina, North Dakota, South Carolina, South Dakota, Vermont, West Virginia, and Wyoming. A considerable number of other States had rural areas of high welfare dependence. Central Appalachia, the Black Belt in the Southeast, the Mississippi Delta, and portions of the Southwest, Northern California, Washington, Montana, and Maine, and various Indian reservations across the country stand out in particular (fig. 1).

With the support of sustained economic growth, TANF surprised even many of its early supporters with its first-year success in reducing welfare cases between August 1996 and April 1997. The number of TANF recipients in Arkansas, for example, dropped by 5 percent, in Kentucky by 9 percent, in South Carolina by 24 percent, and in Tennessee by an amazing 27 percent. An ongoing concern, however, is the group of hardest-to-employ welfare cases, many of them in isolated rural areas. The Balanced Budget Act of 1997, signed by President Clinton on August 5, empowered the Department of Labor to give Welfare-to-Work grants to States and local communities. These funds were aimed at making it possible for even the hardest cases among TANF recipients to find and hold employment (see “Welfare-to-Work Grants”).

Provisions for Funding Welfare-to-Work

Congress voted $3 billion for the new Welfare-to-Work program, to be divided between fiscal years 1998 and 1999. A small amount was set aside for participating Indian tribes (1.0 percent), evaluation (0.8 percent), and performance bonuses to be distributed in fiscal year 2000 to successful States ($100 million). The remainder was to be divided between formula grants to the States and competitive grants to local communities.

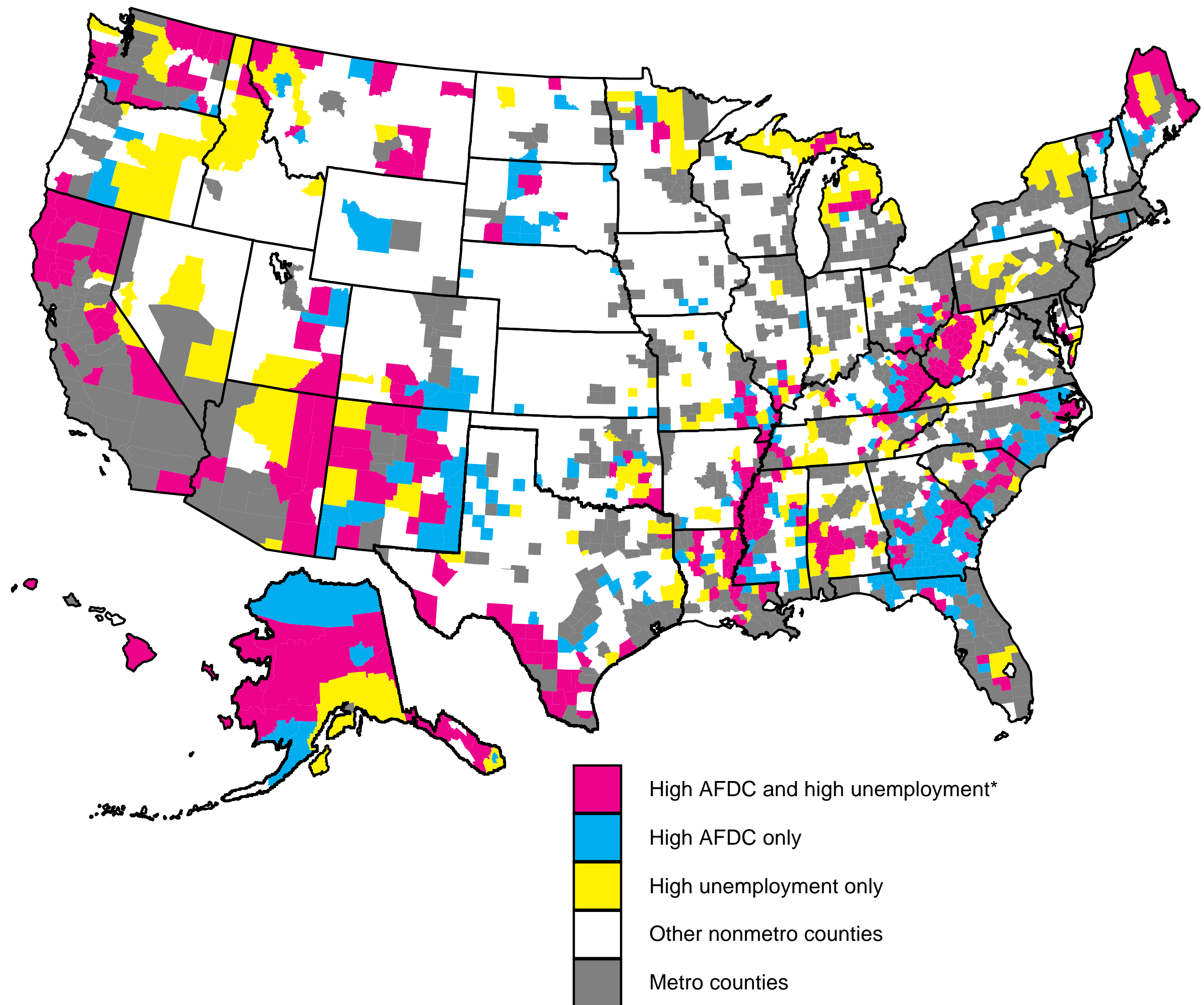
Seventy-five percent of these remaining funds will go to the individual States, Commonwealths, Territories, and the District of Columbia. Allocations will be made according to a formula that gives equal consideration to a State’s share of the total number of poor people nationally and the number of adult recipients of TANF assistance (fig. 2). Each State must submit a plan for administering the Welfare-to-Work grant for approval by the Secretary of Labor and must provide $1 of non-Federal funding for every $2 of Federal funds. Governors are responsible for administration and for coordinating with the separate TANF block grants.

The States must direct 85 percent of the grants to local private industry councils (established under the Job Training Partnership Act and called workforce development boards in some places). These councils, in combination with the chief elected officials, are responsible for overseeing or administrating programs within geographical jurisdictions known as service delivery areas. At least 50 percent of the allocations to these delivery areas must be distributed to areas of high poverty. The other half is parceled out according to num-

Figure 1

Rural counties with high AFDC dependency and high unemployment rates, 1995

Over 60 percent of high welfare-dependent counties also have high unemployment rates



* High equals top 25 percent of U.S. counties.
Source: Estimated by ERS using data from 1990 Census, Bureau of Labor Statistics, Bureau of Economic Analysis, and Social Security Administration.

bers of adults receiving TANF assistance for 30 months or more and the number of unemployed.

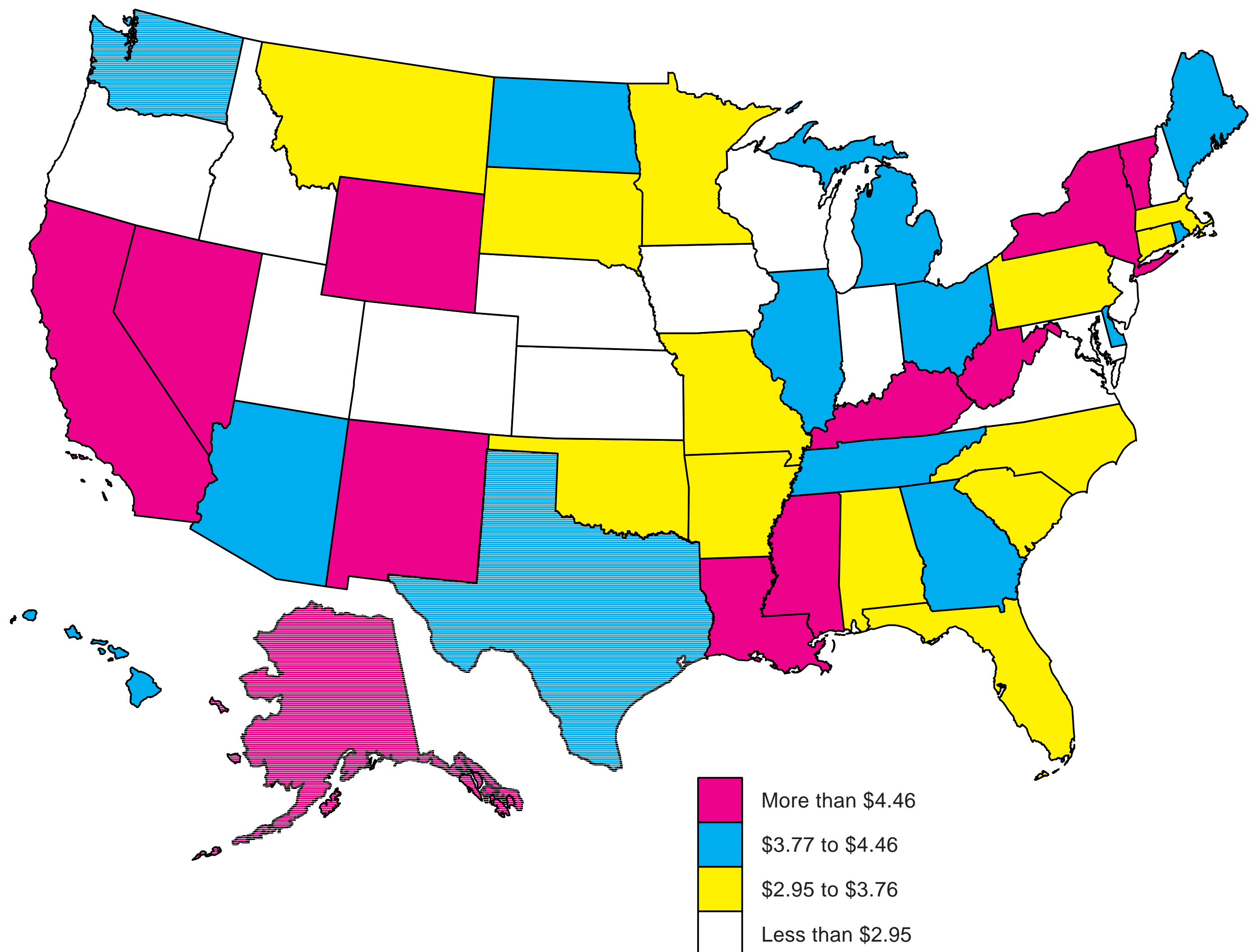
The Secretary of Labor, in consultation with the Secretary of Health and Human Services, the National Governors' Association, and the American Public Welfare Association, will develop performance measurements on the basis of job placement, duration of that placement, increase in earnings, and similar factors which will be used to distribute the performance bonuses to States in fiscal year 2000, if the program funding is extended.

Local governments, private industry councils, community action agencies, and other private entities may compete for grants from the 25 percent of funds not allocated by formu-

Figure 2

Welfare-to-Work State formula grants, per capita, fiscal year 1998

Largest per capita grants go to States in Appalachia, the gulf coast, and the western regions



Source: Calculated by ERS using 1998 funding estimates from the U.S. Department of Labor and 1996 population estimates from the Bureau of the Census.

la to the States. Areas with high concentrations of poverty will be given special consideration by the Secretary of Labor.

Welfare-to-Work Grants Should Help Welfare Recipients Find and Retain Jobs

Welfare-to-Work grants are directed toward the very core of the unemployed and welfare recipients. A minimum of 70 percent of any grant—whether State formula or competitive—must target individuals who are long-term welfare recipients, who will lose TANF benefits within a year, or who are noncustodial parents of minors whose custodial parent meets these criteria. In addition, the individual who fulfills one of those requirements must also face two out of three additional barriers: (1) lack of high school diploma or GED and low reading or math skills, (2) require substance abuse treatment for employment, and (3) poor work history. The other 30 percent of the grant may be used to help individ-

uals, such as recent recipients of TANF who have characteristics of long-term dependency, such as school dropout, teen pregnancy, or poor work history.

Many residents of rural areas—whether "up the hollow" in Appalachia, in the rickety shacks of the Black Belt or Mississippi Delta, or in migrant labor camps—meet these criteria. The problem faced by States, private industry councils, and other entities is how to use Welfare-to-Work grant funds. Initiative and imagination can be rewarded. The goal is to create jobs and to place welfare recipients in those jobs. This may require public- or private-sector wage subsidies, teaching good work habits, on-the-job training, placement and post-employment services, community service jobs if necessary, and counseling support for job retention.

Welfare-to-Work grants may well be considered a lifeline thrown out to those individuals on whom most of society has given up. States are moving to qualify for these grants.

Other Welfare Modifications

The Personal Responsibility and Work Reconciliation Act of 1996 (P.L. 104-193) did not specifically address whether Federal labor laws covered welfare recipients who entered the workplace. Early in 1997, the *Washington Post* wrote of instances of hotel workers who received $30 a week in wages, in addition to welfare benefits of $410 a month. Employers argued that they could not otherwise take on the burden of unskilled new employees without this monetary advantage. Their opponents responded that this system created two classes of workers and provided employers with the temptation to fire regular employees and replace them with welfare recipients. To remove any confusion, the Department of Labor issued a guideline on May 22 which said that labor legislation did indeed apply to welfare recipients entering the workplace. These included the Fair Labor Standards Act—covering minimum wages and child labor for example—the Occupational Safety and Health Act, unemployment insurance coverage, and the various antidiscrimination acts.

Recognizing the financial problems of many families with children whose income was too high to qualify for assistance but too low to be able to afford medical insurance, the Federal Government moved to give the States $20 billion over 5 years to expand Medicaid coverage, buy private insurance policies, or as New York and seven other States had already done, set up their own programs.

The Balanced Budget Act of 1997, along with establishing the Welfare-to-Work program, also modified sections of P.L. 104-193. It restored Supplemental Security Income (SSI) cash benefits to legal immigrants resident in the United States on August 22, 1996, who were disabled at that time or became so later. It decreed that Medicaid coverage would be continued for disabled children who might have lost SSI benefits as a result of eligibility changes under P.L. 104-193. It permitted States to exempt from work requirements up to 15 percent of able-bodied food stamp recipients ages 18 to 50 who have no dependents. It also forbade States from assigning to private entities the responsibility of deciding who is eligible for food stamps or Medicaid.

Funding for Job Training Partnership Act (JTPA) programs has been increased by $518 million above last year's total. JTPA programs include Adult Job Training ($955 million), Youth Training ($130 million), Summer Youth Employment ($871 million), Dislocated Workers ($1.4 billion), and Job Corps ($1.2 billion). Although they are not welfare programs, these programs should complement the new welfare-to-work program since they provide valuable training and job experience to help economically disadvantaged individuals, including welfare recipients. Also complementing the welfare-to-work transition are the tax changes benefiting low-income populations (see article on Tax Policy). *[Lowell Dyson, 202-694-5348, lkdyson@econ.ag.gov]*

Welfare-to-Work Grants as Contained in Balanced Budget Act of 1997
Key Provisions

Supplements to TANF for the hardest-to-employ welfare recipients

Target the estimated 20 percent of welfare recipients most at risk of long-term dependency.

Provide a "Work First" approach, including employment activities such as work experience, on-the-job training, and subsidized employment.

Provide supportive service such as child care, substance abuse treatment, emergency or short-term housing assistance, and transportation assistance.

Provide subsidized transitional work.

Funding

$1.5 billion earmarked in each fiscal year 1998 and 1999.

Nearly 75 percent of total goes to States by formula.

Nearly 25 percent goes as competitive grants directly to local governments, private industry councils, and private entities.

One percent set aside for Indian tribes, 0.8 percent for evaluation, $100 million for performance bonuses to successful States.

The Changing Face of Rural Development Assistance in USDA

USDA's rural development program has changed significantly as a result of the National Performance Review, the Government Performance and Results Act of 1993, USDA's reorganization in 1994, and major farm legislation of 1996. The new Rural Development Mission Area more efficiently uses State and local input and coordinates new initiatives and reforms to target more funds to pressing problems.

While not alone among Federal Departments in having responsibility for assisting rural areas, USDA provides a significant amount of aid, and its assistance tends to be more targeted to rural areas than that of other Federal Departments. Moreover, USDA is, by law, charged with leading and coordinating Federal rural development assistance. Over time, the ways in which USDA has assisted rural America have changed. Earlier in this century, "rural development" was roughly equal to "agricultural development." No more. Today, rural America's diversity of resources and needs requires a much more holistic response. Likewise, the public's expectations of what government should do, how it should do it, and how much it should cost also require a different response. Together, changes in the rural and governmental contexts are causing USDA to evolve its philosophy and organization for delivering rural assistance.

Forces of Change

USDA Reorganization. Following the recommendations from Vice President Al Gore's National Performance Review, Mike Espy—then Secretary of Agriculture—established four key principles for USDA's reorganization: (1) improve the delivery of service to customers, (2) remain consistent with mandated missions, (3) make a better place for employees, and (4) save the taxpayers money. These principles were embedded in the subsequent reorganization, established by the Federal Crop Insurance Reform and Agriculture Reorganization Act. Signed into law in October 1994, this act restructured USDA and established seven "mission areas" based on the Department's primary missions. The act also realigned many programs and reduced the number of USDA agencies. Agencies such as the Farmers Home Administration, the Rural Electrification Administration, the Rural Development Administration, and the Agricultural Cooperative Service were renamed and reorganized as part of the new Rural Development Mission Area.

The act also affects the field presence of USDA rural development agencies. Since the 1930's, USDA has had field staff in every rural county, usually with separate offices for credit, conservation, and farm programs. Consistent with the reorganization, some 1,300 county offices have been closed or moved for consolidation. The goal is to have 2,550 consolidated "service centers" (colocations of the Farm Service Agency, the Natural Resources Conservation Service, and Rural Development) by 2002 (all years in this article are fiscal years, unless otherwise indicated).

Following the reorganization, staffs in USDA's rural development agencies have been significantly reduced. As of 1998, the staff levels for the programs making up USDA's three main rural development agencies—the Rural Utilities Service (RUS), the Rural Housing Service (RHS), and the Rural Business-Cooperative Service (RBS)—will have decreased by about 24 percent overall from their 1993 ceilings, with most of the decline coming from the Rural Housing Service, which accounts for about 85 percent of the combined staff of these agencies.

1996 Farm Legislation. Title VII—Rural Development—of the Federal Agriculture Improvement and Reform Act of 1996 authorized several significant changes to the rural development efforts of USDA. The most significant are described below.

First, it created the Rural Community Advancement Program (RCAP). The objectives of RCAP identified in the legislation are to "promote strategic development activities and collaborative efforts...to maximize the impact of Federal assistance," optimize resources, provide assistance in a way that recognizes the complexity of rural needs, design unique responses to address unique needs, and adopt flexible and innovative approaches to resolving rural problems. The legislation also gives priority to the smallest and poorest communities. The Rural Development Mission Area is supporting these objectives by

stressing leveraging, targeting, outreach, and partnerships in the mission area's strategic plan and in the State/tribal plans.

RCAP allows State Rural Development Directors to mix, to a degree, the funding streams for community facilities, utilities, and business and cooperative development, to provide a more flexible package of assistance aimed at meeting local needs that vary over time and across the country. For the programs covered by RCAP, State Directors may transfer up to 25 percent from one account to another, as long as the amount transferred nationally does not exceed 10 percent of total RCAP funds allocated. In the past, these programs were funded on an individual basis and unused money could not be transferred from one program to another. The rationale for the more flexible approach is to allow funds that were traditionally bound by "stove-pipe" allocations to be used more effectively.

Under this program, Rural Development State Directors are required to prepare individual State strategic plans that outline the use of USDA Rural Development resources in the State as well as plans for each Federally recognized Indian tribe in the State. In preparing the plans, Directors are required to actively seek out and involve public and private institutions and individuals. The objective of the planning is to develop a 5-year strategic plan and include a reasonable set of strategies and actions for the effective delivery of USDA rural development resources, singularly and in partnership with others. The plan is to focus on improving the physical, social and economic conditions of the rural and small towns in the State. Priority is to be given to communities and areas of greatest need. Assistance provided under RCAP must be consistent with the plans.

Second, the act created the Fund for Rural America, which provides a significant amount of funds ($100 million annually for 3 years initially) for a wide range of rural development assistance and research. The fund is divided into thirds, with one-third going respectively to rural development programs, rural development research, and rural development programs or research at the Secretary's discretion. The first of the 3 years' worth of funding became available January 1, 1997, minus $20 million in rescissions that provided supplemental disaster aid. The next two $100 million infusions are scheduled to be received on October 1, 1998, and 1999, respectively. (See article on General Assistance.)

Finally, the act requires the Secretary of Agriculture to establish and chair a Rural Development Interagency Working Group for the purpose of establishing rural policy, coordinating assistance, and evaluating performance of Federal rural assistance. The group will meet in fiscal year 1998.

Government Performance and Results Act. The Government Performance and Results Act of 1993 (GPRA) is another force affecting USDA's rural assistance efforts. The act, which requires agencies to measure and account for the results of their efforts, is the stimulus for USDA's new strategic plan and various reinventing efforts throughout the Department, including rural development efforts.

The New Face of Rural Development

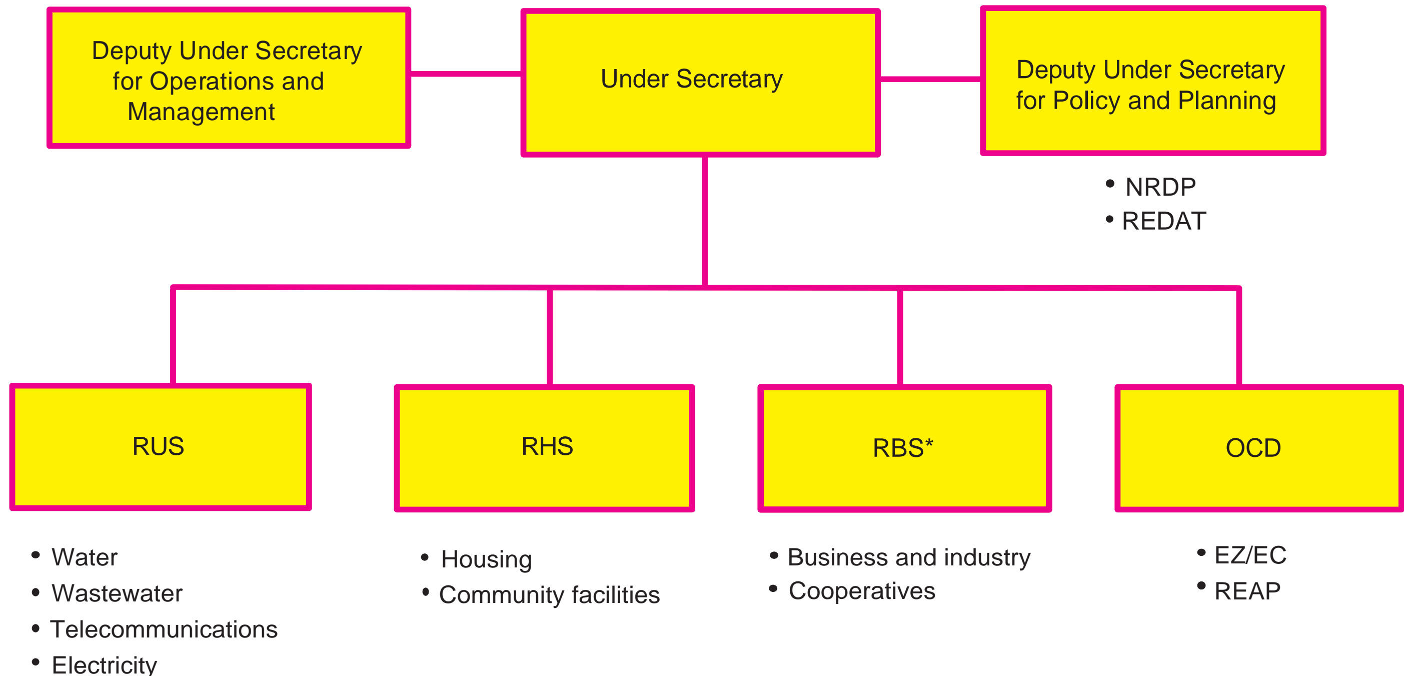
The Rural Development Mission Area's goal, as stated in its mission statement, is to "Enhance the ability of rural communities to develop, to grow, and to improve their quality of life by targeting financial and technical resources in areas of greatest need with activities of greatest potential." In addition to the three main agencies within the Rural Development Mission Area, there is a newly created Office of Community Development (fig. 1).

Rural Utilities Service. The Rural Utilities Service (RUS) administers electric, telecommunications, and water and waste programs formerly operated by the Rural Electrification Administration and the Rural Development Administration. These programs provide technical assistance, grants, loans, and loan guarantees for the infrastructure necessary to improve the quality of life and promote economic development in rural America. (A detailed list of these and other USDA rural development programs is provided at the end

Figure 1

Organization chart for the Rural Development Mission Area

The three main program agencies (RUS, RHS, and RBS) are complemented by activities of the two Deputy Under Secretaries and the new Office of Community Development



Note: RUS = Rural Utilities Service, RHS = Rural Housing Service, RBS = Rural Business-Cooperative Service, OCD = Office of Community Development, EZ/EC = Empowerment Zones/Enterprise Communities, REAP = Rural Economic Area Partnership, NRDP = National Rural Development Partnership, REDAT = Rural Economic Development Action Team.

*Not shown is the Alternative Agricultural Research and Commercialization Corporation, which is essentially an autonomous entity.

Source: Rural Development Mission Area.

of this article.) The RUS also coordinates the Water 2000 initiative, which has a goal of providing clean, safe, and affordable drinking water to all rural homes by the year 2000.

Rural Housing Service. The Rural Housing Service (RHS) administers community facilities and housing programs formerly operated by the Rural Development Administration and the Farmers Home Administration. These programs help finance new or improved housing for over 65,000 moderate-, low-, and very-low-income families each year. The programs also help rural communities finance, construct, enlarge, or improve fire stations, libraries, hospitals, medical clinics, industrial parks, and other community facilities. The RHS also plays a key role in the National Partnership for Homeownership initiative.

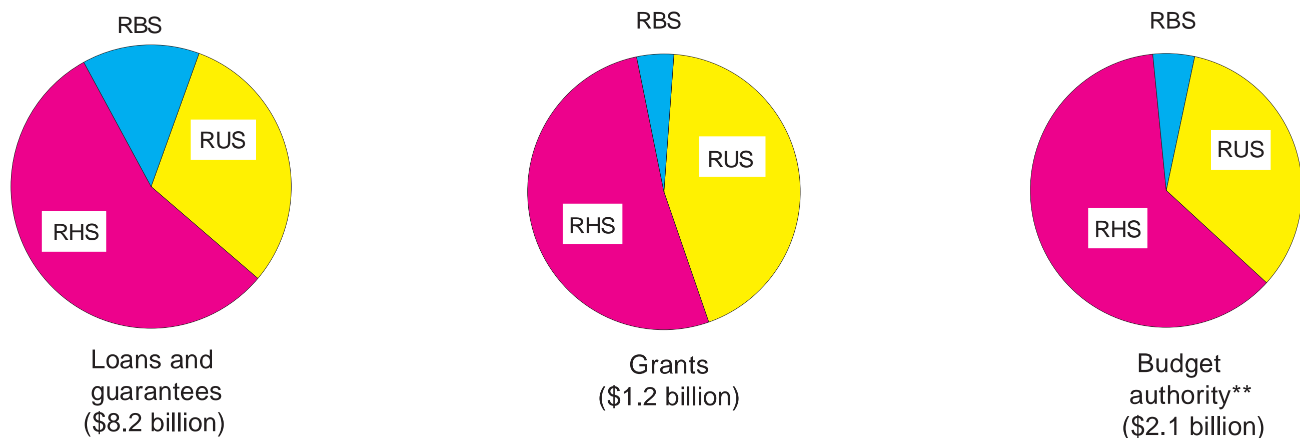
Rural Business-Cooperative Service. The Rural Business-Cooperative Service (RBS) administers programs, formerly administered by the Rural Development Administration, the Rural Electrification Administration, and the Agricultural Cooperative Service, that provide credit and assistance to rural businesses and cooperatives. The RBS partners with the private sector and community-based organizations to provide financial assistance and business planning. It also provides technical assistance to rural businesses and cooperatives and helps fund projects that create or preserve jobs in rural areas.

In 1998, the budget authority for these three agencies' (RUS, RHS, and RBS) programs, combined, was $1.6 billion. However, because many of their programs provide loans and guarantees, the total program assistance level is estimated to be about $9.9 billion. The Rural Housing Service accounts for the majority of the Rural Development budget (fig. 2).

Figure 2

Rural Development Mission Area budget by agency and type of assistance, fiscal year 1998*

The Rural Housing Service accounts for the majority of the rural development budget



Note: RUS = Rural Utilities Service, RHS = Rural Housing Service, RBS = Rural Business-Cooperative Service.
*Excludes the Alternative Agricultural Research and Commercialization Corporation.
**Includes $509 million in salaries and expenses of RUS, RBS, and RHS.
Source: 1999 Budget Summary, U.S. Department of Agriculture.

Office of Community Development. The mission of the Office of Community Development (OCD) is "to create self-sustaining, long-term economic development in areas of pervasive poverty, unemployment, and general distress, and to demonstrate how distressed communities can achieve self-sufficiency through innovative and comprehensive strategic plans developed and implemented by alliances among private, public, and nonprofit entities." OCD's primary activity is administering USDA's portion of the Empowerment Zone/Enterprise Community program. The EZ/EC program, a presidential initiative, provides technical assistance, block grants, tax credits, and priority consideration for Federal programs to specially designated high-poverty communities. OCD also works with Champion Communities (communities that were eligible and applied for EZ/EC designation but were not selected) to assist them in implementing their strategic plans that were developed when applying for designation.

In addition, OCD oversees the Rural Economic Area Partnership (REAP), an initiative assisting distressed multicounty areas in the Northern Great Plains, and several other initiatives that help communities in distressed regions, including the Southwest Border and the Lower Mississippi Delta initiatives.

Other Activities and Initiatives

In addition to these agencies and programs, the Rural Development Mission Area carries out other important activities and initiatives.

Rural Economic Development Action Team. The Rural Economic Development Action Team (REDAT) comprises representatives from the Rural Development; Research, Education, and Economics; and Natural Resources and Conservation mission areas of USDA. Its purpose is to coordinate activities and improve the effectiveness of the Department's rural assistance.

National Rural Development Partnership. The goals of the National Rural Development Partnership (NRDP), begun in 1990 by presidential initiative, are to improve the coordination of rural development programs, to serve as a catalyst in promoting rural interests, and to be a broker among the multisector interests and institutions involved in effecting rural development projects. The partnership works through State Rural Development Councils (established now in 38 States), which are composed of Federal,

State, tribal, and local government officials and private sector representatives. The National Rural Development Council is composed of representatives of Federal agencies and non-profit organizations and serves as an advisory board to the partnership, providing national expertise and assistance with regulations, legislation, program advocacy, national linkage, and coordination.

Northwest Timber Adjustment Initiative. This initiative provides funding and technical assistance to timber-dependent communities in the Pacific Northwest. It is part of a larger presidential initiative that coordinates efforts across Federal agencies and targets communities affected by changes in Federal land use regulations.

Water 2000. This initiative targets basic drinking water improvements to lower income families in distressed rural communities. About $1.3 billion in loans and grants have been committed to 1,000 high priority safe drinking water projects over the last 3 fiscal years.

President's National Partnership for Homeownership. The goal of this interdepartmental initiative is to help 8 million new families become homeowners by the year 2000. A major focus is to help more rural women become homeowners.

Bringing the Information Superhighway to Rural America. As part of the Administration's efforts to help create the Information Superhighway, USDA (primarily through the Rural Utilities Service) is taking steps to ensure that rural areas are "connected" to advanced telecommunications technologies and the information they bring.

Alternative Agricultural Research and Commercialization Corporation. This corporation operates essentially as an autonomous organization, making equity investments in rural businesses to assist in technological development and commercialization of industrial (nonfood, nonfeed) uses for agricultural and forestry materials and animal byproducts. It received $7 million in Federal funds in 1998.

North American Development Bank (NADBank)/Community Adjustment and Investment Program (CAIP). Through the Business and Industry Guaranteed Loan Program, the CAIP provides credit to businesses in communities in the United States that are evidencing significant job losses due to changes in trade patterns with Canada or Mexico after passage of the North American Free Trade Agreement. The goals of the CAIP are to assist private companies in creating and retaining job opportunities in impacted areas, leverage private sector business lending, and focus resources into the most significantly affected areas.

Armament Retooling and Manufacturing Support (ARMS) Initiative. Through a Memorandum of Understanding with the United States Army, the Business and Industry Guaranteed Loan Program is providing financial assistance to facilitate commercial firms' use of specified ammunition manufacturing facilities. RBS provides the programming and administrative services necessary and convenient to process applications for loan guarantees, the guaranteed repayment of the loans, and provides other services required to administer the ARMS Initiative Loan Guarantee program.

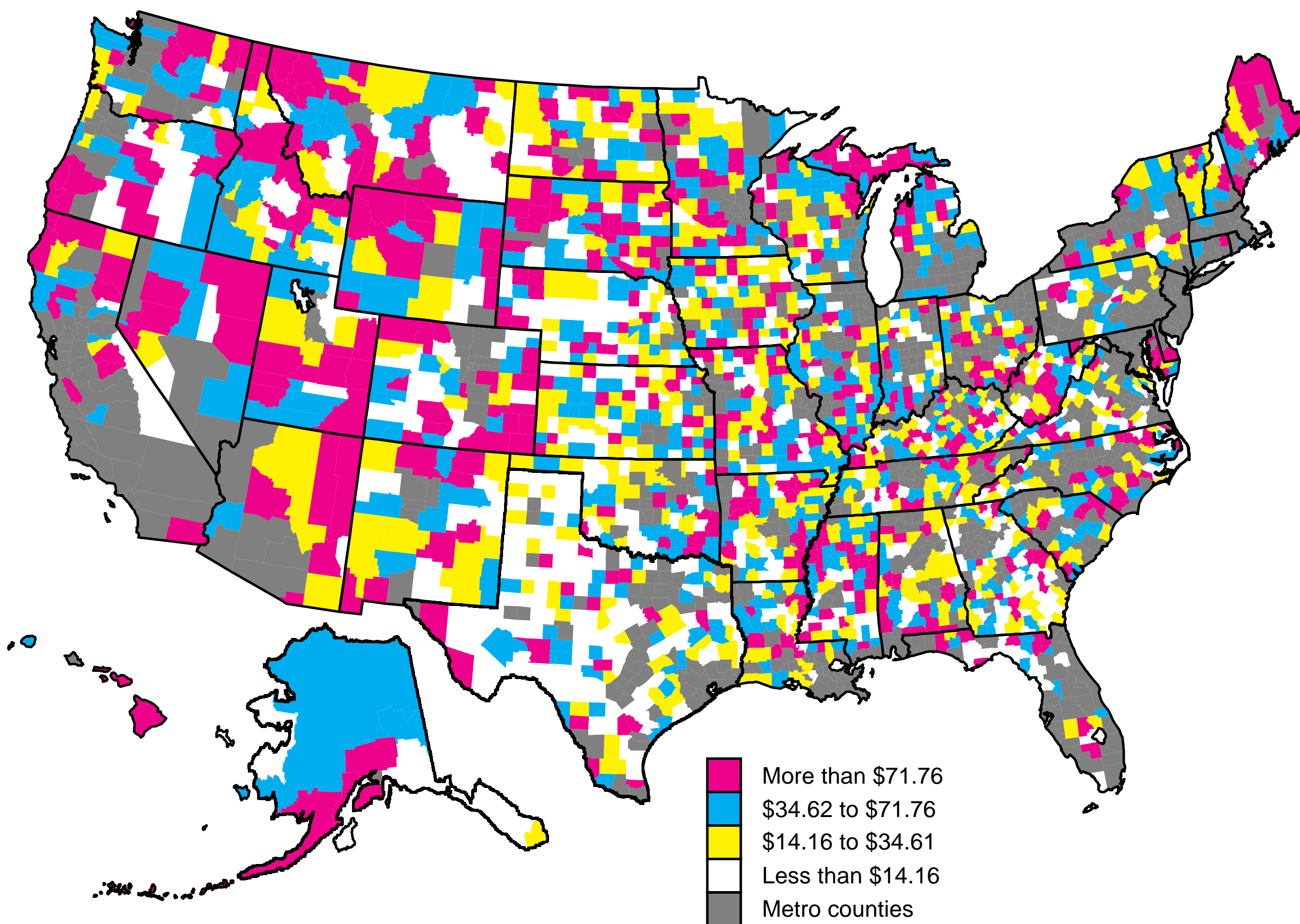
Delta Initiative. In 1996, the Rural Development Mission Area began this initiative to help address the needs of communities in the Lower Mississippi Delta region, one of the poorest areas in the United States. USDA awarded a contract for $200,000 to the Housing Assistance Council (HAC) to work with the communities in the area to develop a strategy that (1) identifies successful projects building on existing plans and community efforts, (2) strengthens the capacity of nonprofit organizations to undertake community-based development work in the region, and (3) leverages capital to facilitate a long-term regional collaborative effort. With input from town meetings and consultations, HAC developed a strategic plan identifying barriers to economic growth and recommending actions that might overtake those barriers. A "Delta Compact" has been drafted as a living document committing resources of several Delta institutions to the priority projects identified in the strategic plan. To date, 12 organizations have committed resources to the region under the "Delta Compact."

Colonias Initiative. Through a collaboration of USDA's Rural Development Mission Area, the Bank of America, and the Ford Foundation, this initiative will provide assistance to extremely poor individuals with poor housing and lacking running water and sewer who live along the Mexican border. The primary objective is to design and implement two resident-led community development models that hold promise for producing lasting improvements in five selected Colonias in New Mexico, Texas, and Arizona. Secondary objectives include simplifying access to technical and financial services for comprehensive development strategies and identifying ways in which the Bank of America's regular, profit-oriented activities can be mobilized to encourage development in these communities. The partners have committed $250,000 ($50,000 per Colonia) for the first year, contracting with two intermediaries (the Housing Assistance Council, a national housing organization, and Valley Interfaith, a community-based organization in the region) to implement the demonstration.

Geographic Distribution of Program Benefits

Various factors affect the distribution of rural development program benefits, including eligibility and selection criteria, which may vary from program to program, and priorities,

Figure 3
USDA Rural Development mission program funding, per capita, fiscal year 1996
Most rural counties received some assistance from USDA's rural development programs



Note: Includes Rural Development mission programs with more than $10 million funding in 1996; excludes electric and telecommunications programs.
Source: Calculated by ERS using Federal Funds data from the Bureau of the Census.

which may vary from State to State. Conditions and priorities will also change from year to year, affecting the geographic distribution. Although we do not have accurate county-level data for all of USDA's rural development programs, we do have data for most of the large programs belonging to the Rural Development mission area, including the main housing and business assistance programs and the water and waste disposal program (electric and telephone programs are excluded). When these are added together for allocations in 1996, including loans, guarantees, and grants, we see that much of rural America received at least some assistance, but the assistance varies significantly across the country (fig. 3).

Rural Development Efforts Elsewhere in USDA

The Rural Development Mission Area is not the only entity within USDA with rural development responsibilities and programs. Other agencies, including the Forest Service, the Natural Resources Conservation Service, and the Cooperative State Research, Education, and Extension Service, have rural development programs. These programs are discussed elsewhere in this report (see General Assistance). Other USDA agencies, such as the Economic Research Service, have programs of research or assistance that support rural development activities.

Finally, the recent USDA-wide sustainable development effort stands to significantly affect rural development. Sustainable development requires that short-term economic growth be consistent with long-term economic, institutional, and environmental developments so that it can be sustained over the long run. In September 1996, Secretary Glickman took steps to formalize the pursuit of sustainable development within USDA by appointing a Director of Sustainable Development and creating the USDA Sustainable Development Council. The director is charged with leading and coordinating cross-mission area work in sustainable development and representing the Department in both domestic and international arenas on sustainable development issues. The council, comprising representatives from each of the agencies and chaired by the director, serves as a forum for policy and program development, implementation, and evaluation on issues relating to sustainable development. It also provides a framework and mechanism for integrating across mission areas and program activities.

USDA Rural Development Mission Programs

Rural Utilities Service Programs

Water and Waste Disposal Loans

Purpose: To develop water and waste disposal (including solid waste disposal and storm drainage) systems in rural areas and towns with populations not in excess of 10,000. The funds are available to public entities, such as municipalities, counties, special-purpose districts, Indian tribes, and corporations not operated for profit. RUS also guarantees water and waste disposal loans made by banks and other eligible lenders.

Water and Waste Disposal Grants

Purpose: To reduce water and waste disposal costs to a reasonable level for rural users. Grants may be made for up to 75 percent of eligible project costs in some cases. The same types of applicants are eligible for grants as they are for loans.

Technical Assistance and Training Grants

Purpose: To make grants to nonprofit organizations to provide technical assistance and training to associations on a wide range of issues relating to the delivery of water and waste disposal service.

Solid Waste Management Grants

Purpose: To make grants to public and private nonprofit organizations for providing technical assistance and training to associations to reduce or eliminate pollution of water resources and improve planning and management of solid waste facilities. This assistance is available in rural areas and towns with a population not in excess of 10,000.

Emergency Community Water Assistance Grants

Purpose: To assist rural communities that have had a significant decline in quantity or quality of drinking water. Grants can be made in rural areas and cities or towns with a population not in excess of 5,000 and a median household income not in excess of 100 percent of a State's nonmetro median household income. Grants may be made for 100 percent of project costs. The maximum grant is $500,000 when quantity or quality of water significantly declined within 2 years or $75,000 to make emergency repairs and replacement of facilities on existing systems.

Rural Water Circuit Rider Technical Assistance

Purpose: To provide technical assistance for the operation of rural water systems. The RUS, through contracting, has assisted rural water systems with day-to-day operational, financial, and management problems. The assistance may be requested by officials of rural water systems or the RUS. The program complements RUS's loan supervision responsibilities.

Rural Electric Loans and Loan Guarantees

Purpose: To make insured loans and guarantees of loans to nonprofit and cooperative associations, public bodies, and other utilities. Insured loans primarily finance the construction of facilities for the distribution of electric power in rural areas. Guaranteed loans primarily finance generation and bulk transmission facilities for power supply borrowers.

Rural Telephone Loans and Loan Guarantees

Purpose: To make long-term direct loans to qualified organizations for the purpose of financing the improvement, expansion, construction, acquisition, and operation of telephone lines, facilities, or systems to furnish and improve telephone service in rural areas.

Rural Telephone Bank Loans

Purpose: To provide supplemental financing to extend and improve telephone service in rural areas.

Distance Learning and Medical Link Grants

Purpose: To encourage, improve, and make affordable the use of telecommunications, computer networks, and related technology for rural communities to improve access to educational and/or medical services. Maximum amount of grant is $350,000.

Deferment on Loan Payments for Rural Development Projects

Purpose: To promote economic or community development by allowing RUS electric or telecommunications borrowers to defer insured or direct RUS loan payments equal to eligible investments.

Rural Housing Service Programs

Community Facilities Loans

Purpose: To construct, enlarge, extend, or otherwise improve community facilities providing essential services in rural areas and towns with a population of 20,000 or less. The funds are available to public entities, such as municipalities, counties, special-purpose

districts, Indian tribes, and corporations not operated for profit. RHS also guarantees community facility loans made by banks or other eligible lenders.

Homeownership Loans

Purpose: To aid low- and moderate-income rural residents to purchase, construct, repair, or relocate a dwelling and related facilities.

Rural Rental Housing Loans

Purpose: To allow individuals or organizations to build or rehabilitate rental units for low-income and moderate-income residents in rural areas.

Rental Assistance

Purpose: To reduce out-of-pocket cash that very-low-income and low-income families pay for rent, including utilities.

Home Improvement and Repair Loans and Grants

Purpose: To enable very-low-income rural homeowners to remove health and safety hazards in their homes and to make homes accessible for people with disabilities. Grants are available for people 62 years old and older who cannot afford to repay a loan.

Self-Help Housing Loans

Purpose: To assist groups of six to eight low-income families in helping each other build homes by providing materials, site, and the skilled labor they cannot furnish. The families must agree to work together until all homes are finished.

Rural Housing Site Loans

Purpose: To buy adequate building sites for development into a desirable community by private or public nonprofit organizations.

Farm Labor Housing Loans and Grants

Purpose: To enable farmers, public or private nonprofit organizations, and units of State and local governments to build, buy, or repair farm labor housing in either dormitory or multifamily apartment style.

Congregate Housing and Group Homes

Purpose: To provide living units for persons with low incomes and moderate incomes and for those age 62 or older.

Housing Preservation Grants

Purpose: To provide qualified public nonprofit organizations and public agencies with grant funds for effective programs to assist very-low- and low-income homeowners to repair and rehabilitate their homes in rural areas and to help rental property owners and co-ops repair and rehabilitate their units if they agree to make such units available to low- and very-low-income persons.

Rural Business-Cooperative Service Programs

Business and Industry Guaranteed Loan Program

Purpose: To improve, develop, or finance business, industry, and employment and improve the economic and environmental climate in rural communities, including pollution abatement and control. This purpose is achieved through bolstering the existing private credit structure through guarantee of quality loans that will provide lasting community benefits. The guarantee authority is not intended to be used for marginal or substandard

loans or to “bail out” lenders having such loans. This type of assistance is available only to businesses located in rural areas. The terms ‘rural’ and ‘rural area’ mean a city, town, or unincorporated area that has a population of 50,000 inhabitants or less, other than an urbanized area immediately adjacent to a city, town, or unincorporated area that has a population in excess of 50,000 inhabitants.

Business and Industry Direct Loan Program

Purpose: To improve, develop, or finance business, industry, and employment and improve the economic and environmental climate in rural communities, including pollution abatement and control. This purpose is achieved through loans that will provide lasting community benefits. Although there is a requirement that borrowers are not able to obtain credit from other lenders at reasonable rates and terms, it is not intended that the B&I Direct Loan authority will be used for marginal or substandard loans. This type of assistance is available only to businesses located in rural areas. The terms ‘rural’ and ‘rural area’ mean a city, town, or unincorporated area that has a population of 50,000 inhabitants or less, other than an urbanized area immediately adjacent to a city, town, or unincorporated area that has a population in excess of 50,000 inhabitants.

Intermediary Relending Program Loans

Purpose: To finance business facilities and community development projects not within the outer boundary of any city having a population 25,000 or more. This is achieved through loans made by RBS to intermediaries that provide loans to ultimate recipients for business facilities and community development projects in rural areas.

Rural Business Enterprise Grants

Purpose: To assist public bodies and nonprofit corporations to finance and facilitate development of small and emerging private business enterprises located in rural areas. The terms ‘rural’ and ‘rural area’ mean a city, town, or unincorporated area that has a population of 50,000 inhabitants or less, other than an urbanized area immediately adjacent to a city, town, or unincorporated area that has a population in excess of 50,000 inhabitants.

Rural Business Opportunity Grants

Purpose: To assist public bodies, nonprofit corporations, Indian tribes, and cooperatives for planning, technical assistance, entrepreneurial training and leadership, and the creation of business support centers. A proposed rule defining program eligibility criteria was published in the Federal Register on February 3, 1998.

Rural Economic Development Loans and Grants

Purpose: To promote rural economic development and job creation projects through loans to RUS electric and telecommunication borrowers, including funding for project feasibility studies, startup costs, incubator projects, and other reasonable expenses for the purpose of fostering rural development. Maximum amount of grant or loan is $375,000 and $750,000, respectively. Maximum term of loan is 10 years at zero-interest rate.

Cooperative Service

Purpose: To promote the understanding and use of the cooperative form of business as a viable option for agricultural producers and other rural residents. To foster and support the cooperative business form. To provide knowledge to improve the effectiveness and performance of the Nation’s cooperative business.

Rural Cooperative Development Grant Program

Purpose: To establish and operate centers for rural cooperative development. To improve economic conditions of rural areas by promoting development and commercialization of new services, products, processes, and enterprises.

Office of Community Development Programs

Rural Empowerment Zones/Enterprise Communities

Purpose: To revitalize rural communities in a manner that attracts private-sector investment and thereby provides self-sustaining community and economic development. A total of 33 Round I rural Empowerment Zones (EZ's) and Enterprise Communities (EC's) were designated in December 1994 and their benefits consisted of tax incentives and title XX Social Service Block Grants. Five Round II rural EZ's will be designated in 1998. To date, benefits include tax incentives, but no grants have yet been allocated. *[Tom Rowley, formerly with ERS; and Rick Reeder, 202-694-5360, rreeder@econ.ag.gov]*

The Taxpayer Relief Act of 1997 Provides Significant Tax Relief to Rural America

The Taxpayer Relief Act of 1997, perhaps the most important tax legislation in the last decade, is expected to significantly reduce Federal taxes for farmers and other rural taxpayers. While much of the tax relief is provided to middle-income families through a new child tax credit and education incentives, lower income rural taxpayers will also benefit from expanded Empowerment Zones and increased incentives to hire economically disadvantaged individuals.

In August 1997, President Clinton signed into law the Taxpayer Relief Act of 1997, the tax portion of the agreement to balance the Federal budget. This legislation, perhaps the most significant tax legislation in over a decade, will provide a total net tax reduction of about $95 billion over the next 5 years. The act contained a number of general and targeted tax relief provisions that will significantly reduce Federal taxes for rural taxpayers. It provides tax relief for families through a new child tax credit and several new tax incentives for education. Savings and investment are encouraged through expanded opportunities to contribute to individual retirement accounts and reduced capital gains taxation. The act also provides substantial estate and gift tax relief, especially to farmers and other small rural business owners. Finally, the act contains provisions that promote rural development through new rural Empowerment Zones and incentives to hire certain economically disadvantaged individuals.

Tax Relief for Families

Child Tax Credit. The act increases tax benefits for dependent children by providing a $500 ($400 for 1998) tax credit for each qualifying child under the age of 17. The child credit is phased out at a rate of $50 for each $1,000 of modified adjusted gross income in excess of $110,000 for married taxpayers filing a joint return and $75,000 for taxpayers filing as single or head of household. The amount of the credit is generally limited to the taxpayer's regular income tax liability. However, a portion of the credit is refundable for taxpayers with three or more children. For these taxpayers, the child credit is refundable to the extent that their regular income tax liability, the employee share of Federal Insurance Contribution Act (FICA) taxes and half of their self-employment tax liability exceeds the earned income tax credit. The new child tax credit is expected to benefit nearly one-third of all rural taxpayers and their families. The average credit amount for those eligible for the credit is estimated to be about $800.

Education Tax Incentives. The act creates two new nonrefundable tax credits for qualified tuition and fees for post-secondary education. A Hope Scholarship Credit of up to $1,500 (all of the first $1,000 and 50 percent of the next $1,000) is allowed for each student's tuition and related expenses during the first 2 years of college. A 20-percent Lifetime Learning Credit of up to $1,000 annually ($2,000 by 2003) is available for a taxpayer's tuition and related expenses for an unlimited number of years. The act allows nondeductible contributions of up to $500 per child to an education savings account for children under the age of 18. Distributions from such an account for qualified higher education expenses are tax free. The act also allows up to $2,500 of student loan interest to be deducted for each of the first 5 years that repayment of the student loan is required. All education incentives are phased out for taxpayers whose income exceeds a specified threshold amount, which varies depending upon the particular incentive. Finally, the exclusion for employer-provided undergraduate education assistance is extended through June 1, 2000. Rural residents, especially those families with children at or near college age, will benefit from one or more of these new education tax incentives.

Savings and Investment Incentives

Individual Retirement Accounts. The act expands the availability of existing IRA's and provides a new nondeductible alternative. With regard to existing IRA's, the income that an individual who is an active participant in an employer-sponsored pension plan can earn and still make deductible IRA contributions was increased. On a joint return, the adjusted gross income limit at which deductible contributions begin to be phased out rises by $10,000 in 1998 to $50,000, and to $80,000 by 2007. For single taxpayers, the

Note: The information provided here should not be construed as USDA's providing tax advice, for which competent tax advisors/attorneys should be consulted.

amount increases by $5,000 in 1998 to $30,000, and to $50,000 by 2005. The act also allows spouses of individuals who are active participants to make their own deductible contributions, but the deduction is phased out if adjusted gross income exceeds $150,000. The new, nondeductible "Roth IRA's" allow tax-free distributions if funds are withdrawn after 5 years and the individual has reached age 59½, died, or become disabled. Contributions are phased out for couples with adjusted gross income over $150,000 and individuals over $95,000. Annual contributions to all IRA's remain limited to a total of $2,000. The act also allows penalty-free distributions from any IRA for higher education expenses and up to $10,000 of first-time home buyer expenses.

Only individuals who are covered by employer-sponsored pension plans, and their spouses, benefit from the expanded deductibility of IRA's. Nearly all rural households will qualify for the new Roth IRA's. Nonetheless, the share of farmers and other rural taxpayers who annually contribute to an IRA is relatively small (about 9 percent of farmers in any year and about 5 percent of other rural taxpayers). Thus, unless the new retirement saving options lead to a change in saving behavior, the increased availability may not result in a significant increase in retirement savings for rural taxpayers.

Capital Gains. The act reduced the maximum tax rate on capital gains held for at least 18 months from 28 percent to 20 percent. A 10-percent capital gains tax rate applies to taxpayers in the 15-percent marginal tax bracket. Because business assets are eligible for capital gains treatment, capital gains are an important component of income for farmers. About one-third of all farmers report some capital gain income each year. This is three times the frequency for all other taxpayers and twice that for other small businesses.

The act also allows a taxpayer to exclude up to $250,000 ($500,000 if married filing a joint return) of gain on the sale of a principal residence. This new exclusion can be used as frequently as every 2 years, and replaces both the previous provision that allowed the gain to be rolled over into another residence and the $125,000 lifetime exclusion for taxpayers over 55 years of age. Most rural residents will be exempt from tax on the sale of their residence as a result of this new provision. This includes farm residences, which represent about 12 percent of the value of farms.

Tax Relief for Farmers and Other Rural Businesses

Self-Employed Health Insurance Deduction. The self-employed health insurance deduction is intended to give small business owners tax benefits similar to employees receiving employer deductible health insurance. In 1997, self-employed individuals were allowed to deduct 40 percent of the cost of providing health insurance for themselves and their families. This amount was scheduled to increase to 80 percent by 2006. The 1997 Act accelerates the scheduled increases and will allow 100 percent of the cost to be deducted by 2007. This will reduce the after-tax cost of purchasing health insurance for those farmers and other rural business owners who must purchase insurance on their own.

Alternative Minimum Tax. The act repeals the alternative minimum tax (AMT) for small corporations for tax years beginning after 1997. A small corporation is defined as a corporation with 3-year average annual gross receipts of $5 million or less for the first tax year beginning after 1996 and with annual gross receipts of $7.5 million or less for any later years. This change will allow most farm and other rural small business corporations to avoid the complexities of the alternative minimum tax.

The act also provides a lower tax rate for individual taxpayers on net capital gain for alternative minimum tax purposes. Under the change, net capital gain is taxed at the same rates that apply for regular income tax purposes. Thus, capital gain that is taxed at 20 percent for regular income tax purposes will be taxed at 20 percent for AMT purposes rather than the alternative minimum tax rate of 26 percent.

Estate and Gift Tax Relief. Only about 1 percent of all estates are subject to the estate tax. Thus, estate and gift taxes are not a major concern for most rural taxpayers. However, while the aggregate importance of estate and gift taxes may be small, the potential impact of such taxes on an individual or group of individuals, such as farmers and other small business owners, can be substantial.

Concern for the effects of Federal estate taxes on farmers and other small business owners who hold significant amounts of wealth in business assets was the primary impetus for the changes to Federal estate and gift tax laws in the 1997 Act. The act substantially increases the size of a farm or other business that can be transferred tax free by increasing the basic amount each individual can transfer tax free (the unified credit) from $600,000 to $1 million by 2006 and by providing a new exclusion for qualified family business interests of up to $675,000 in 1998. The act also makes important changes to the installment payment provision which allows taxes to be paid over a 14-year period rather than within 9 months of death. These changes include lowering the interest rate from 4 to 2 percent and increasing the size of an estate eligible for this low interest rate.

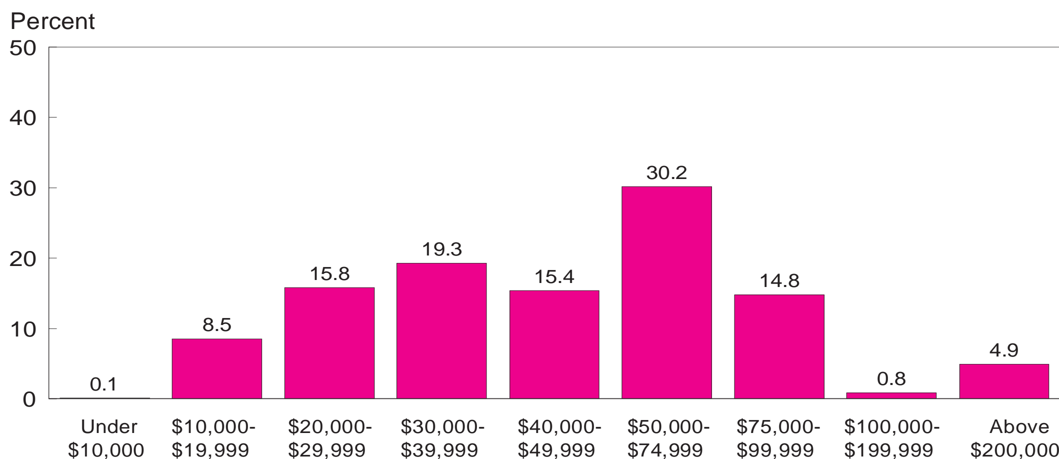
The overall effect of the 1997 changes to Federal estate and gift tax policies is that fewer farmers and other small business owners will be required to file a return or pay taxes. Those required to pay will owe less tax and will be eligible for more favorable payment terms. Thus, these changes will make it easier to transfer the family business across generations by reducing the likelihood that the business or some of its assets will need to be sold to pay estate taxes.

Special Tax Benefits for Farmers. Farmers were major beneficiaries of the 1997 Act. In addition to the general provisions, which accounted for most of the tax reduction, the act contained a number of provisions targeted specifically to farmers. These included allowing farmers to use the installment sales method of accounting for alternative minimum tax purposes, allowing farmers to defer the gain on the sale of livestock due to floods and other weather-related conditions, and temporarily restoring the ability of farmers to lower their tax liability by shifting farm income to the 3 prior tax years. The combined effect of these as well as the other changes contained in the 1997 Act, especially the capital gains and estate and gift tax provisions, is estimated to reduce Federal tax burdens for farmers by about $1.8 billion per year.

Special Tax Incentives for Low-Income People and Places

Since most of the new tax credits are not refundable and the benefits are phased out for higher income taxpayers, the primary beneficiaries of the 1997 Act are middle-income taxpayers (fig. 1). Higher income and wealthier taxpayers primarily benefit from capital

Figure 1
Distribution of tax benefits under 1997 Act for 1998
Benefits targeted to middle-income classes



Source: U.S. Congress Joint Committee on Taxation.

gains and estate and gift tax provisions. However, the 1997 Act also provides some new and expanded tax benefits targeted to low-income people and places, including incentives to hire employees from targeted groups of disadvantaged individuals or places or to encourage private enterprise development in high-poverty or distressed areas.

New Empowerment Zones. The 1997 Act authorizes the Secretaries of HUD and Agriculture to designate an additional 20 Empowerment Zones with no more than 5 of these zones to be located in rural areas. Thus, the number of rural Empowerment Zones will increase from three to eight. However, the tax incentives for the new zones are different from those available for the earlier zones (see General Assistance article).

Work Opportunity Tax Credit. The work opportunity tax credit encourages employers to hire employees from one or more of seven target groups. The seven target groups include (1) members of a family receiving assistance under the Temporary Assistance to Needy Families (TANF) program, (2) a veteran who is a member of a family either receiving AFDC assistance or assistance under a Food Stamp program, (3) an individual convicted of a felony who is hired within 1 year after conviction or release from prison and who is a member of a family whose income is 70 percent or less than the Bureau of Labor Statistics lower living standard, (4) an individual between the ages of 18 and 25 who lives within an Empowerment Zone or Enterprise Community, (5) an individual who is 16 or 17 years old who performs services for the employer between May 1 and September 15 and lives in an Empowerment Zone or Enterprise Community, (6) an individual who has a physical or mental disability that is a substantial handicap to employment, and (7) an individual between the ages of 18 and 25 who is a member of a family receiving assistance under a Food Stamp program. The credit was scheduled to expire on September 30th, 1997, but was extended by the 1997 Act for 9 months through July 1, 1998. The act also expanded the number of target groups to eight by adding a group for qualified supplemental security income recipients. The rate of the credit was also changed from 35 percent to 25 percent of wages for employment of more than 120 hours but less than 400 hours and 40 percent of wages for employment over 400 hours or more. Since the credit is higher for wages paid for employment over 400 hours, the maximum credit varies depending upon the proportion of wages eligible for the 40-percent rate. The deduction for wages paid is reduced by the amount of the credit.

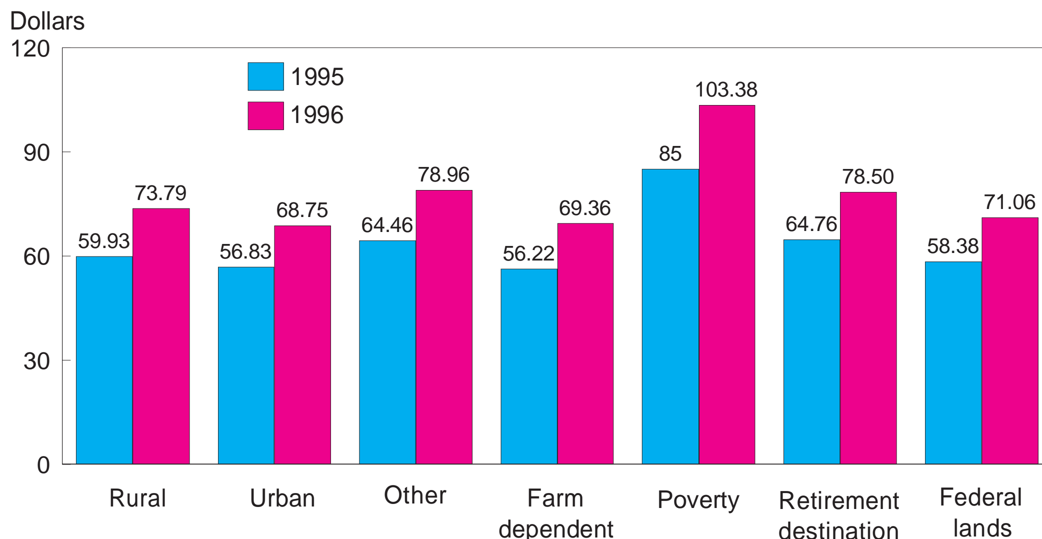
Welfare-to-Work Tax Credit. The act contains a new credit to provide employers an incentive to hire long-term public assistance recipients. The credit is equal to 35 percent of qualified first-year wages and 50 percent of qualified second-year wages. For purposes of the credit, wages are broadly defined to include not only actual wages but educational assistance covered by the tax exclusion for employer-provided tuition assistance, health plan coverage, and dependent care assistance. The credit applies to up to $10,000 per year, resulting in a maximum credit of $8,500 for the 2 years. An eligible employee must be certified as a long-term family assistance recipient by a State employment security agency. The new credit applies to employees who begin work after December 31, 1997, and before May 1, 1999. For most profitable businesses, the credit will reduce the after-tax cost of hiring a targeted employee earning $10,000 per year to about $8,000 for the 2 years. This credit is expected to assist States and localities in adjusting to the welfare reform legislation enacted in 1996 (see Welfare Reform Followup article).

Earned Income Tax Credit Developments. The 1997 Act continues recent efforts to more precisely target the earned income tax credit (EITC), a refundable tax credit available to low-income workers who satisfy certain income and other eligibility criteria. The EITC is phased out if earned income or modified adjusted gross income exceeds a specified threshold amount. The 1997 Act adds two new nontaxable items in determining income used for phasing out the benefits of the earned income tax credit. These items are tax-exempt interest and the nontaxable portion of any pension, annuity, or distribution from an individual retirement account. The new law also increases the amount of losses from a business, including farming, that are disregarded from 50 percent to 75 percent. This change will affect a relatively small number of tax credit recipients but will dispropor-

Figure 2

Per capita earned income tax credit benefits by type of State, fiscal year 1995-96[1]

1996 benefits increased significantly compared with those in 1995[2]



[1] Refundable portion of credit only.
[2] See data definitions for State classifications.
Source: Calculated by ERS using Federal Funds data from the Bureau of the Census.

tionately reduce benefits to farmers since over half of all farmers report a net loss for tax purposes each year.

The earned income tax credit has increased in importance for low-income rural workers with the phase-in of the 1993 expansion of the credit. For fiscal year 1997, the first year to fully reflect the full phase-in of the 1993 changes, the credit provided low-income workers and their families about $28 billion in benefits with the rural share estimated at about $7 billion. About one out of every five rural residents benefited from the credit. The credit continues to provide the greatest benefits to those States classified as persistent poverty States, with the refundable portion of the credit alone providing an average per capita benefit of $103.38 in fiscal year 1996 (fig. 2). Furthermore, despite the new targeting provisions contained in the 1997 Act, the total value of the credit is expected to continue to increase, although at a much slower rate, with the total credit estimated to reach $28.5 billion in fiscal year 1998.

Fewer Tax Policy Changes Expected in 1998

The potential for a budget surplus in fiscal year 1999 enhances the prospects for further tax reductions in 1998. The Administration has proposed tax relief to provide child care assistance for working families as well as new tax incentives to promote energy efficiency, retirement savings, and increased education expenditures. Congressional proposals include relief from the alternative minimum tax, further reductions in Federal estate and gift taxes, and a reduction in the marriage penalty. Given the increasing priority being placed on addressing the long-term solvency problem of social security, however, the amount of tax relief enacted in 1998 should be limited, especially in contrast to the 1997 legislation. *[Ron L. Durst, 202-694-5347, rdurst@econ.ag.gov]*

Slowly Evolving Regulatory Changes Could Significantly Affect Rural Development

Some major regulatory changes were announced or proposed in 1997, but implementation has not been a smooth process due to legal, political, and economic challenges. The most significant changes include telecommunications, electric power, air and water pollution, public land management, and banking and finance.

Regulatory changes affect development in many ways. They are often complex, with unpredictable effects that cannot be detected until significant time has elapsed. In this section, we discuss some of the more important recent regulatory changes that were announced or proposed in 1997, affecting telecommunications, electric utilities, air and water pollution, public land management, and banking and finance institutions.

Implementation of the Complex Telecommunications Act of 1996 Progressing Fitfully

In the 2 years since the Telecommunications Act of 1996 became law, the Federal Communications Commission (FCC) and the courts have been shaping its implementation. Despite the many regulations that have been established, the only provisions fully implemented are those dealing with opening up the local phone market. Those provisions, however, have come under court challenge. The 2 years since the act became law have already shown many of the challenges, pitfalls, and economic potential in opening up the telecommunication market, an $800-billion market according to FCC Chairman Kennard, to full competition.

The consolidation and restructuring going on in the industry, the continued lack of meaningful competition in local phone service, and recent court rulings have all contributed to a great deal of uncertainty in the telecommunication market. A recent ruling by a Federal judge in Texas, for example, went so far as to strike down a key portion of the act, the provisions allowing the regional Bell companies to enter the long-distance service only if they had at first proved they had opened their local telephone markets to competition. This ruling had in effect been won by the regional Bell companies, the long-distance companies lost. There have been no clear winners across all rulings. Most lower court rulings are under appeal. The issues facing the courts basically fall into two groups: (1) the legality or intent of some provisions in the law and (2) challenges to the authority of the FCC.

While all provisions of the 1996 Act will affect rural areas, the universal service provisions will have the greatest direct effect. The FCC in May 1997 passed the first regulations to implement these provisions, granting rural households support (through reduced rates) for a full range of telephone services. States, however, still determine the phone rates. The funding mechanism for universal service has not yet been determined, but is expected to take effect on January 1, 1999. States may opt out of the Federal funding mechanism. For these and other reasons, the universal service provisions are not fully implemented.

The universal service provisions also include funding for school, library, and health care providers. Eligible public and private elementary and secondary schools as well as libraries will be able to buy any telecommunication service, including the Internet, at a discount. Discounts range from 20 to 90 percent of the provider's rate, based on need and high-cost (ruralness) factors. Universal support expenditures for schools and libraries are capped at $2.25 billion per year, though unspent funds can be carried forward to subsequent years. An estimated 9,600 health care providers will be eligible to receive telecommunication services supported by the universal service mechanism. All rural health care providers are eligible with support capped at $400 million per year.

These school, library, and health care provider provisions have also come under attack. For example, the universal service contributions by long-distance companies for these provisions are meant to be offset by reductions in access charges. Reduced access charges have saved the long-distance companies, according to some estimates, over $2 billion per year. The long-distance companies, however, have claimed the savings haven't been that high and are threatening to increase their rates to cover their contributions.

Another challenge to the provisions comes in the form of questioning FCC's authority to establish the two nonprofit corporations that administer the distribution of the funds.

The next year promises to be just as turbulent for the telecommunications market as the previous 2 years have been, although the market is generally expected to gradually calm down. The real winners and losers in this market adjustment process, however, will become known only later. While there has been some discussion about opening up for Congressional reconsideration some provisions in the act, the current general consensus among analysts seems to be that this will not happen anytime soon. *[Peter Stenberg, 202-694-5366, stenberg.econ.ag.gov]*

States Are Restructuring the Electric Utility Industry to Introduce Retail Competition and Consumer Choice, So Far in the Absence of Federal Legislation on These Issues

Restructuring of the electric utility industry, to create market competition and consumer choice at the retail (distribution) end of the industry, continues to move forward in State legislatures and State public utility commissions. Once accomplished, consumers should be able to purchase electric power from the least expensive available source, and have it delivered to their electric meter by their current electric distribution company—to whom customers would pay a charge to "wheel" that power to them. Electric power companies already sell power at the wholesale market level into a competitive market place. High voltage transmission systems would continue to be regulated by Government, but paid a reasonable price to "wheel" wholesale power from generating companies to retail distribution companies. Both government regulatory pressures—and competitive market pressures—appear to be moving toward a break up of most integrated power companies where a company owns power generation, transmission facilities, and retail distribution networks. The emerging model is one in which power generation firms and retail power distribution companies may be organized independently from other segments of the business.

Under proposed Federal legislation, new start-up electric power generating facilities, including power generation from renewable resources, such as wind, solar, and biomass, would be free to start up and compete for business. There would be less government regulation of electric power companies at the wholesale and distribution or retail levels of the business. The Federal Energy Regulatory Commission (FERC) would continue to license electric power plants and power companies' high voltage transmission systems, but probably would have less regulatory oversight regarding pricing and access to electric service than before deregulation. State regulatory commissions typically would also have less authority over prices and access to service.

Restructuring is largely occurring at the State level, in response to the promise of substantial reductions in retail electric utility rates. High-electric-cost States in the Northeast and the Southwest, such as New York and California, have been in the forefront of deregulation, some of which has been by action of State legislatures and some by action of State public utility commissions. At the end of 1997, 11 State legislatures had enacted restructuring legislation, and 6 State public utility commissions had issued restructuring decisions. Twenty-two more States had legislative or regulatory efforts under way to study restructuring and to propose legislation for implementation. Federal action has not yet occurred, although several comprehensive and noncomprehensive bills have been introduced into the Congress addressing restructuring and consumer choice. The U.S. Congress is expected to act on electric utility restructuring; the Administration has recently announced a comprehensive approach to restructuring legislation.

As with most industry deregulation, some participants and consumers would benefit more than others. Electric rates in high-cost regions of the country, principally the Northeast, the Southwest, and in States where large-scale nuclear power plant projects are located, seem likely to decline. That would primarily be because lower cost electric energy can be

imported from low-cost regions of the country. Large users of electricity would be active in negotiating preferred electric rates. Many national manufacturing and commercial firms would negotiate master contracts to supply electricity to all their locations across the Nation. On the other hand, consumers in areas of the country with currently midrange electric rates may not see much change. In some States, rates could trend upward after industry restructuring. Some rural areas could experience reduced access to service and/or find their electric rates remain relatively high, compared with urban areas. Moreover, reliability and access to new service could decline or become more costly for some more geographically remote customers. That has been the experience with airline, rail transportation, and telecommunications deregulation, where more rural areas of the country continue to face firms that exercise significant monopoly pricing power. Finally, more competitive markets should cause electric rates in different regions of the country to move closer together. That would remove an incentive for businesses to relocate or start up in more rural areas of the country that previously enjoyed lower electric rates.

While electric utility industry restructuring may bring economic benefits to the Nation, three steps are important to assure that competition actually develops in the industry and that consumers are not left facing firms that exercise monopoly pricing power. First, establishing well-functioning futures and options markets in electric power will be important to assure competitive pricing. Second, in the more rural areas, statutory or regulatory universal service and reliability requirements will be important to assure continued access to service at an affordable price. Third, Federal and State regulatory bodies must be vigilant to assure competitive pricing of electric services in all areas of the country. *[Marvin Duncan, 202-694-5019, mduncan@econ.ag.gov]*

New Air and Water Regulations Could Significantly Affect Some Rural Areas

In July 1997, the Environmental Protection Agency (EPA) finalized regulations for more restrictive controls on ground-level ozone (which contributes to smog) and airborne particles. The new rules are aimed at reducing health risks, particularly for children and the elderly. However, complying with the new regulations could be costly for some places, particularly urban areas. The Clean Air Act requires localities to meet air quality standards by given deadlines. Failure to submit or implement plans to meet the standards could result in reductions in Federal highway aid. State and local governments might have to cut back on activities that generate this form of pollution, where possible, such as by making more use of mass-transit and other means to discourage auto commuting. Some places, particularly congested urban areas facing high levels of pollution and some rural areas with large and stationary power plants that produce excessive levels of pollution, may have to adopt strategies to reduce pollution. This might help some less polluted rural and urban areas to capture a larger share of future development.

To lessen the pain of complying with the new rules, EPA is phasing in the new control strategies over a 10-year period, and various policies are proposed to reduce compliance cost. Places that already have established strategies to comply with current regulations would not have to change to meet the new standards. For others, new standards for ozone and particulates would not begin to be applied until the years 2003 and 2005, respectively. A proposed tradable pollution allowance system would be used to provide market incentives for adoption of policies to reduce pollution. For places incapable of reducing pollution below the new standards, this tradable allowance system would help to limit their cost increases. In addition, as part of its Greenhouse Initiative, the Administration in its fiscal year 1999 budget has proposed to spend $2.7 billion on research and development of new energy-efficient technologies for autos and building materials, plus $3.6 billion in tax incentives for purchase of these energy-efficient products. This follows from an Energy Department study that claimed that the cost of developing such energy-efficient technologies might be compensated by cost savings from future reductions in energy use.

If Congress were to adopt this energy-efficiency approach and if it proved to be successful in reducing pollution costs associated with energy used in the future (neither of these if's are by any means assured), congested urban areas and their outlying rural-commuting areas, and other high-energy production and use areas (such as agriculture and mining and energy extraction areas) might benefit. Otherwise regulation-induced costs would probably rise for many of these places. However, regulation-induced pressures for less polluting autos and trucks might actually benefit some agricultural areas that produce inputs for agricultural-based ethanol, a more clean-burning fuel. Reducing ground-level ozone has the side benefit of increasing crop yields in some areas. In addition, these places would benefit from improved health associated with cleaner air. While the potential effects are great, the many uncertainties make it impossible to predict what the ultimate effects would be.

New regulatory efforts are also being proposed to restore and protect America's waterways. During the 25 years since the enactment of the Clean Water Act of 1972, the quality of the Nation's waterways has improved. Most of this has been achieved by reducing point-source pollution by communities, industries, and businesses. But nonpoint runoff pollution has escaped solution under conventional regulatory methods. Recognizing that this problem is frustrating the goal of making all waterways fit for swimming and fishing, President Clinton proposed a new Clean Water Action Plan: Restoring and Protecting America's Waters.

The Administration has asked all appropriate departments and agencies to work as a team to develop plans and set new regulations and standards for the nonpoint pollution, which is caused, to a large extent, by runoff from land and animal feeding operations. This Clean Water Action Plan has three major goals: reduce the threat to public health from water pollution; prevent polluted runoff; and achieve higher water quality on a watershed basis. EPA will provide final regulations for the runoff pollutants by March 1, 1999. National Oceanic and Atmospheric Administration (NOAA) and EPA will put in place the Nonpoint Pollution Control Programs for all 29 Coastal States by June 30, 1998.

The Action Plan calls for an additional 100,000 acres of wetlands by 2005. This plan, in concert with USDA's Buffer Initiative, will establish 2 million miles (or 35 million acres) of buffer strips that will protect waters from agricultural runoff by the year 2002. Under this plan, USDA will make sure that agricultural operations in 1,000 critical rural watersheds have the necessary technical and financial resources available to them for controlling polluted runoff. To support the Action Plan, President Clinton has asked for $568 million for fiscal year 1999, and $2.3 billion through 2003. *[Faqir Bagi, 202-694-5337, fsbagi@econ.ag.gov]*

New Public Land Use Plans Were Established for National Forests, and Legislation Amends Program Managing National Wildlife Refuge Areas

In April 1997, the Forest Service and the Bureau of Land Management announced a new land management plan covering 72 million acres of Federal forest and rangeland in eastern Oregon and Washington, most of Idaho, and small parts of Montana, Wyoming, Utah, and Nevada. According to the proposed plan, to be finalized in the spring of 1998, new, more restrictive standards would be required of anyone wishing to mine, cut timber, graze cattle, or operate recreation businesses on these lands. The new standards require examining potential effects of land use on animal and plant habitat, not only in the section of land being used, but in the entire Columbia river basin. This allows land use decisions to consider upstream and downstream effects, which may sometimes be significant. The plan would allow higher logging levels than in the past 3 years, and it proposes increases in funding that would create jobs, while helping to preserve habitat and protect endangered species.

Meanwhile, the Bureau of Land Management withdrew a policing regulation plan covering 270 million western acres that was proposed in November 1996. That plan had come under criticism for taking powers away from local authorities.

In May 1997, the Forest Service released its land management plan for the Tongass National Forest in Alaska. It would allow up to 267 million board feet of timber harvesting annually, only half the current limit but more than twice as much as actually harvested in recent years. The plan also designates portions of 32 rivers as Wild, Scenic, or Recreational and creates buffers along beaches and river mouths and increases protection for caves.

In January 1998, the Forest Service proposed a suspension on constructing and reconstructing roads that could affect 33 million acres of roadless land within 130 national forests from Idaho to southern Appalachia. The proposed suspension would last 18 months or until new analytical tools are adopted that would ensure good road construction design and better maintenance of existing roads. National Forests in the Pacific Northwest and the Tongass National Forest in Alaska were excluded from the suspension because their recently adopted forest management plans were deemed sufficient. One expected result from the road-building suspension is a small reduction in logging.

In October 1997, legislation (P.L. 105-57) amended the National Wildlife Refuge System Administration Act of 1996, providing it with a basic mission of conservation, including restoration of fish, wildlife and plants. However, hunting and recreation are also recognized as priorities. This compromise, together with new clarity of mission, is expected to engender more support for Federal management of these refuge areas, which cover 92 million acres, a larger area than the National Park System, and to play an important role in protecting plant and animal life and in providing recreation to rural and urban residents. *[Rick Reeder, 202-694-5360, rreeder@econ.ag.gov]*

Some Bank and Credit Institution Regulations Have Changed, Allowing More Branch Banking and Revising Farm Credit System Rules

Beginning June 1, 1997, the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 permitted interstate branching through bank mergers. Only two States, Montana and Texas, passed legislation opting out of interstate branching. While interstate banking will increase the pace of bank consolidation, rural banks are typically too small to attract attention from the mostly large banks that actively participate in interstate banking. New data required by revisions to the regulations governing the Community Reinvestment Act are just now becoming available to help evaluate the extent to which large banks lend to farmers and to small businesses in rural areas served by offices of those banks. Bad publicity for banks that appear to neglect the credit needs of rural areas may encourage some large banks to increase rural lending.

In 1997, Congress again came close to revising the Glass-Steagall Act, which limits bank activity in the insurance and securities industries. During the current session, the House narrowly passed legislation, but the Senate has yet to act on this issue. Prospects for a comprehensive legislative solution are complicated by conflicts between the banking, insurance, and securities industries, and between small and large banks. Many rural and other small banks fear that removing all Glass-Steagall barriers would concentrate economic power in a few giant firms. The resulting institutions would offer a wide array of financial services, but some wonder whether they would neglect the farm and small business sectors in rural areas.

In February 1998, the banking industry won a Supreme Court decision preventing what it perceives as unfair extensions of credit union common bond requirements. However, Congress may restore much of this authority to credit unions through new legislation. Several other issues remain open from prior years. At a minimum, banks want equal tax treatment for large credit unions that serve wide portions of their communities. Banks will

definitely lobby against any new attempts to gain expanded powers for Farm Credit System (FCS) institutions. Legislative proposals to improve commercial bank access to funds from the Federal Home Loan Banks and from FCS banks did not succeed in 1997. The upward trend in loan-to-deposit ratios makes it likely that similar proposals will move forward this year. It appears that rural banks generally have sufficient loanable funds, whether from deposits or from other sources, but if that situation were to change, additional sources of funds could benefit rural borrowers.

The Farm Credit Administration (FCA) is an independent agency of the Federal Government that regulates the Farm Credit System. FCA's board of directors has established regulatory reform as a major priority. Reduction of regulatory burden continued during the year. Regulatory burden was reduced through the elimination or proposed elimination of several prior-approval requirements and the deletion of several obsolete regulatory provisions identified through public comment or internal agency review. If these initiatives are successful, FCS lenders will have lower business costs and be more customer oriented while maintaining safe and sound operations. Perhaps the two 1997 initiatives of broadest interest were final regulations concerning eligibility and scope of financing and proposed regulations on general financing agreements (GFA's) between FCS banks and the lending institutions that borrow from them.

The most controversial changes have involved final rules for eligibility and scope of financing. The changes affect loans to farmers, financing of processing or marketing operations, loans to farm-related businesses, nonfarm rural home loans, and eligibility and scope of financing for Banks for Cooperatives and Agricultural Credit Banks. The regulations place fewer restrictions on financing to legal entities, to certain foreign nationals, and for marketing, processing, and farm-related business loans. Also, definitions related to nonfarm rural home lending are tightened and harmonized with Federal Agricultural Mortgage Corporation (Farmer Mac) standards. The American Bankers Association and the Independent Bankers Association of America sued the FCA, alleging the regulations conferred powers on the FCS not intended by Congress. In November, a Federal Court dismissed the suit, but an appeal has been filed.

The final rule on GFA's revises regulations governing funding relations between FCS banks and FCS direct lender associations or non-FCS financing institutions (OFI's). OFI's, including commercial banks, could enjoy greater access to FCS financing for eligible short- and intermediate-term loans to eligible borrowers. The proposed rule reduces to two the minimum conditions under which a creditworthy OFI would be eligible for access to FCS financing. First, the OFI must make at least 15 percent of its loans to agricultural producers. Second, it must commit to establishing a funding relationship with an FCS bank for at least 2 years. The rule may also encourage more equitable treatment of FCS associations and OFI's by FCS banks. In part, this is accomplished by allowing OFI's to seek funding under certain conditions from FCS banks not chartered to serve their service area. To protect FCS safety and soundness, OFI's funding must be fully secured and full recourse to OFI capital is required.

The overall impact of these FCS changes on rural borrowers is likely to be small. Those who have been eligible to borrow from FCS lenders may notice a slight decrease in FCS rates relative to competing bank rates, although bankers are also enjoying a similar regulatory reform. Some borrowers who were formerly considered ineligible to borrow from the FCS will now be allowed to do so. Commercial banks, some of which have had trouble maintaining their deposit base, should find it easier to qualify to borrow nondeposit funds from FCS banks. However, it remains to be seen whether many commercial banks, particularly small rural ones, will overcome their traditional aversion to dealing with the FCS. *[Daniel Milkove, 202-694-5357, dmilkove@econ.ag.gov and Robert Collender, 202-694-5343, rnc@econ.ag.gov]*

Appendix table 1—Rural share of selected programs, fiscal year 1996

Agency[1] and program	1996 funding[2]	Nonmetro counties	Rural States
	Billions of dollars	Percent	
General assistance:			
HUD State/Small Cities Community Development Block Grants (CDBG)	1.135	—	24.5
EDA adjustment assistance—			
Planning support	.021	61.4	34.1
Technical assistance	.011	25.7	22.2
Special economic development and adjustment assistance[3]	.185	25.2	13.7
FEMA disaster relief	2.516	—	9.5
USDA/CSREES extension activities[4]	.407	29.6	27.0
BIA Native American assistance programs	.418	—	39.8
Infrastructure assistance:			
USDA/RUS Programs—			
Rural Water and Waste Disposal Grants	.348	78.2	26.8
Rural Water and Waste Disposal Direct Loans	.581	73.3	25.1
Rural Water and Waste Guaranteed Loans	.059	97.1	.5
Rural Electrification Loans and Loan Guarantees[4]	.699	70.8	27.4
Rural Telecommunication Loans and Loan Guarantees[4]	.457	59.9	19.0
Distance Learning and Medical Link Grants	.008	84.8	34.9
USDA/RHS programs—			
Rural Community Facilities Direct Loans	1.250	77.7	23.9
Rural Community Facilities Loan Guarantees	.053	80.5	28.5
DOT Highway Planning and Construction Grants	18.162	26.3	16.4
DOT Airport Improvement Grants[1]	1.179	13.0	20.2
DOT Nonurban Public Transportation	.139	—	20.1
EPA Clean Water State Revolving Fund	.222	—	10.8
EDA Public Works Grants	.161	55.4	25.3

See notes at end of table.

—Continued

Appendix table 1—Rural share of selected programs, fiscal year 1996—Continued

Agency[1] and program	1996 funding[2]	Nonmetro counties	Rural States
	Billions of dollars	Percent	
Business assistance:			
SBA Small Business Loan Guarantees—7(a)	7.092	18.5	12.0
SBA Certified Development Loan Company guarantees (section 504)	2.782	15.7	12.4
SBA disaster loans—			
Economic Injury Disaster Loans	.119	46.1	14.4
Physical Disaster Loans	1.224	15.2	5.9
USDA/RBS Programs—			
Business and Industry Loan Guarantees	.609	58.2	29.2
Intermediary Relending Program Loan Guarantees	.037	72.2	30.3
Rural Business Enterprise Grants (RBEG)	.044	70.3	31.7
EDA Special Economic Development and Adjustment Assistance[5]	.185	25.2	13.7
Housing assistance:			
USDA/RHS Single Family Housing (section 502)— Direct Loans and Guarantees	2.663	42.3	22.3
USDA/RHS Multifamily Housing (section 515)	.147	69.7	26.8
VA Guaranteed and Insured Housing Loans	10.504	11.0	11.7
HUD/FHA Single-Family Mortgage Insurance	59.133	5.8	7.9
HUD mortgage insurance for low/moderate income families	.102	19.0	12.0
HUD Public and Indian Housing	3.349	16.1	10.3
Share of U.S. population, 1996[6]	NA	20.3	11.4

— = Data not accurate at the county level.

NA=Not applicable.

[1]Agency abbreviations in table are HUD = U.S. Department of Housing and Urban Development; EDA = Economic Development Administration (U.S. Department of Commerce); FEMA = Federal Emergency Management Agency; USDA = U.S. Department of Agriculture; CSREES = Cooperative State Research, Education, and Extension Service; RBS = Rural Business-Cooperative Service; RUS = Rural Utilities Service; RHS = Rural Housing Service; BIA = Bureau of Indian Affairs (U.S. Department of the Interior); DOT = U.S. Department of Transportation; EPA = Environmental Protection Agency; SBA = Small Business Administration; FHA = Federal Housing Administration; VA = U.S. Department of Veterans Affairs.

[2]Dollar amounts are for the U.S. total (includes both metro and nonmetro) for fiscal year 1996. Because the data source is the Bureau of the Census, these totals may differ from those cited from other sources.

[3]Includes economic and defense adjustment.

[4]Federal Funds data covering CSREES extension activities (includes research) and RUS electric and telephone loans only track funds to the county where central offices are located. The services provided by these programs often cover multicounty areas; hence, these data probably understate the extent to which nonmetro counties benefit from the programs.

[5]The percentages reported here refer to the entire Special Economic Development and Adjustment Assistance program, which includes both economic adjustment and defense adjustment (this program was also reported earlier under general business assistance).

[6]Data for calendar year 1996.

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

Data Sources

Federal Funds Data. The principal data source we use to indicate geographic dispersion of program funding is the Consolidated Federal Funds Reports data from the U.S. Department of Commerce, Bureau of the Census. We usually refer to these data as the Federal Funds data. Census collects these data annually from each Federal department or agency. We aggregated the latest available data (fiscal year 1996) to the county, State, region, and national levels for each program. (Unless otherwise specified, references to years are fiscal years.) We have also computed per capita estimates by type of nonmetro county and type of State (the typologies are explained later in this appendix). These per capita estimates form the basis for our information indicating the types of rural places that are particularly affected by each program.

The Census data for 1996 covered 1,146 individual programs, but not all of these programs had reliable data at the county level. Each program has individual characteristics that affect the way the data show geographic patterns. For example, funds for many programs go directly to State capitals or regional centers that redistribute the money or program benefits to surrounding areas. Examples include block grant programs and some procurement programs that involve a substantial degree of subcontracting. Census screens the data to identify such programs, and we have added our own screening, which separates out those programs that allocate 25 percent or more of their funds to State capitals. We ended up with 694 programs that we believe are fairly accurate to the county level for 1996. For the screened-out programs, we believe it is only meaningful to indicate geographic variations among States but not among counties. Thus, for some of the programs, we provide county maps and statistics, while for others we rely on State maps and statistics. Appendix table 1 lists the programs covered in this report, including the percentage of funds going to nonmetro counties (for programs deemed accurate to the county level) and the percentage of funds going to rural States (for all programs, including programs not deemed accurate to the county level).

The benefits of Federal programs do not all go to the places that receive funds. For example, money spent on national parks benefits all who visit the parks and not just those who live where the parks are located. USDA money to county extension offices may be expected to provide services to surrounding multicounty areas. Similarly, rural electric loans go to borrowers who may be located in one county but provide electric service to a much wider, multicounty area. Such spillover benefits are present in almost all Federal programs and are not reflected in the Federal funds data. In addition, different programs affect communities in different ways and have different multiplier effects on local income, employment, and community well-being. Thus, even if the reported funding dispersion is considered to be an accurate depiction of where the funds are spent, care is required when interpreting the data as program effects.

Federal Funds data may represent either actual program expenditures or obligations, depending on the form of the data provided to Census. Direct loans and loan guarantees are reported according to the volume of loans obligated, and do not take into account interest receipts or principal payments. Consequently, these data do not always correspond to program totals reported in government budget documents, such as budget authority, outlays, or obligations (see definitions).

ERS' Federal Funds Data—sorted by type of county and State and used to produce tables, charts, and maps for this publication—will be available on CD-Rom, at a cost to be announced later, as one of ERS's Standard Data Products. *[Faqir Singh Bagi, 202-694-5337, fsbagi@econ.ag.gov; Samuel Calhoun, 202-694-5339, scalhoun@econ.ag.gov; and Rick Reeder, 202-694-5360, rreeder@econ.ag.gov]*

Budget Data. We obtained information on regulatory changes and recent changes in program funding levels, such as the level and change in funding from 1997 to 1998, from various sources, including Congressional Quarterly Weekly Report, the President's Fiscal Year 1999 Budget, the 1999 budget summaries provided by major government agencies, Congressional legislation, conference reports, and legislative summaries, and from the

most recent Catalogue of Federal Domestic Assistance. In some cases, we contacted budget officials by phone to obtain information.

Population Data. Per capita funding amounts were estimated using 1996 county population estimates from the Bureau of the Census.

Definitions

Typologies. Classification systems developed and periodically revised by ERS to group counties and States by economic and policy-relevant characteristics. The county typology codes used in this issue are those described in Peggy J. Cook and Karen L. Mizer, *The Revised ERS County Typology: An Overview*, RDRR-89, U.S. Department of Agriculture, Economic Research Service, December 1994. The State typology codes were first developed in Elliot J. Dubin, *Geographic Distribution of Federal Funds in 1985*, Staff Report AGES89-7, U.S. Department of Agriculture, Economic Research Service, March 1989, and were revised for the 1996 Federal Funds *RCaT.*

County Economic Types (mutually exclusive; a county may fall into only one economic type):

Farming-dependent—Farming contributed a weighted annual average of 20 percent or more of total labor and proprietor income over the 3 years of 1987-89.

Mining-dependent—Mining contributed a weighted annual average of 15 percent or more of total labor and proprietor income over the 3 years of 1987-89.

Manufacturing-dependent—Manufacturing contributed a weighted annual average of 30 percent or more of total labor and proprietor income over the 3 years of 1987-89.

Government-dependent—Federal, State, and local government activities contributed a weighted annual average of 25 percent or more of total labor and proprietor income over the 3 years of 1987-89.

Service-dependent—Service activities (private and personal services, agricultural services, wholesale and retail trade, finance and insurance, real estate, transportation, and public utilities) contributed a weighted annual average of 50 percent or more of total labor and proprietor income over the 3 years of 1987-89.

Nonspecialized—Counties not classified as a specialized economic type over the 3 years of 1987-89.

County Policy Types (overlapping; a county may fall into any number of these types):

Retirement-destination—The population aged 60 years and older in 1990 increased by 15 percent or more during 1980-90 through inmovement of people.

Federal lands—Federally owned lands made up 30 percent or more of a county's land in 1987.

Commuting—Workers aged 16 years and over commuting to jobs outside their county of residence were 40 percent or more of all the county's workers in 1990.

Persistent-poverty—Persons with poverty-level income in the preceding year were 20 percent or more of total population in each of 4 years: 1960, 1970, 1980, and 1990.

Transfer-dependent—Income from transfer payments contributed a weighted annual average of 25 percent or more of total personal income over 3 years of 1987-89.

State Types (the first three types are mutually exclusive; a State may fall into only one category; the remainder are overlapping).

Because many Federal programs do not have accurate county-level data, we developed a State typology to assist in differentiating among types of States and their funding levels. First, we categorized States into three groups (rural, urban, and other) based on the percentage of a State's population residing in urban parts of metro areas. We defined four other types of States: farming-dependent, persistent-poverty, retirement-destination, and

Federal lands. In each case, we used the same kinds of measures that were used to construct ERS's county typologies. However, the cutoffs were lowered because States have more internal socioeconomic diversity than most counties.

ERS's State types are defined as follows:

Rural—In 1993, 45 percent or less of the State's population resided in urban areas within the metro areas.

Urban—In 1993, 70 percent or more of the State's population resided in urban portions of metro areas.

Other (neither urban nor rural)—More than 45 percent but less than 70 percent of the State's population in 1993 resided in urban portions of metro areas.

Farming-dependent—In 1991-93, 4 percent or more of the total labor and proprietor income came from farm labor and proprietor income.

Persistent-poverty—Fifteen percent or more of a State's persons had income below poverty in 1960, 1970, 1980, and 1990.

Retirement-destination—A State's aged (over 60) population in 1990 increased by 5 percent or more due to net inmigration from 1980 to 1990.

Federal lands—The Federal Government owns 28 percent or more of total land in the State.

These State types were illustrated in figures 1-5 of the 1996 Federal Programs *RCaT*.

Rural States include Alaska, Arkansas, Idaho, Iowa, Kentucky, Maine, Mississippi, Montana, Nebraska, New Hampshire, North Carolina, North Dakota, South Dakota, Vermont, West Virginia, and Wyoming.

Urban States include Arizona, California, Colorado, Connecticut, Delaware, District of Columbia, Florida, Hawaii, Illinois, Maryland, Massachusetts, Nevada, New Jersey, New York, Rhode Island, Texas, and Utah.

Other States include Alabama, Georgia, Indiana, Kansas, Louisiana, Michigan, Minnesota, Missouri, New Mexico, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Tennessee, Virginia, Washington, and Wisconsin.

Farm-dependent States include Arkansas, Idaho, Iowa, Kansas, Montana, Nebraska, North Dakota, South Dakota, and Wyoming.

Poverty States include Alabama, Alaska, Arkansas, District of Columbia, Georgia, Kentucky, Louisiana, Mississippi, New Mexico, South Carolina, South Dakota, Tennessee, and West Virginia.

Retirement-destination States include Arizona, Florida, Hawaii, Idaho, Nevada, New Mexico, North Carolina, Oregon, South Carolina, Utah, and Washington.

Federal lands States include Alaska, Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming.

Regions

Census Regions—We used the conventional four Census-defined regions as follows:

Northeast: Connecticut, Maine, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island, and Vermont.

Midwest: Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin.

South: Alabama, Arkansas, Delaware, District of Columbia, Florida, Georgia, Kentucky, Louisiana, Maryland, Mississippi, North Carolina, Oklahoma, South Carolina, Tennessee, Texas, Virginia, and West Virginia.

West: Alaska, Arizona, California, Colorado, Hawaii, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington, and Wyoming.

In most cases, we used only the nonmetro portion of these regions when referring to county-level data variations.

Metro and Nonmetro Areas

Metro areas. Metropolitan Statistical Areas (MSA's), as defined by the Office of Management and Budget, include core counties containing a city of 50,000 or more people or have an urbanized area of 50,000 or more and a total area population of at least 100,000. Additional contiguous counties are included in the MSA if they are economically integrated with the core county or counties. For most data sources, these designations are based on population and commuting data from the 1990 Census of Population. The Current Population Survey data through 1993 categorizes counties as metro and nonmetro based on population and commuting data from the 1980 Census. Throughout *Rural Conditions and Trends,* "urban" and "metro" have been used interchangeably to refer to people and places within MSA's.

Nonmetro areas. These are counties outside metro area boundaries. In *Rural Conditions and Trends*, "rural" and "nonmetro" are used interchangeably to refer to people and places outside of MSA's.

Rural-Urban Continuum County Codes

Classification system developed by ERS to group counties by the size of their urban population and the adjacency to metropolitan areas. (See Margaret A. Butler and Calvin L. Beale, *Rural-Urban Continuum Codes for Metro and Nonmetro Counties,* 1993, AGES 8428, U.S. Department of Agriculture, Economic Research Service, September 1994).

Metro counties—

Central counties of metro areas of 1 million population or more.

Fringe counties of metro areas of 1 million population or more.

Counties in metro areas of 250,000 to 1 million population.

Counties in metro areas of fewer than 250,000 population.

Nonmetro counties—-

Urban population of 20,000 or more, adjacent to a metro area.

Urban population of 20,000 or more, not adjacent to a metro area.

Urban population of 2,500 to 19,999, adjacent to a metro area.

Urban population of 2,500 to 19,999, not adjacent to a metro area.

Completely rural or less than 2,500 urban population, adjacent to a metro area.

Completely rural or less than 2,500 urban population, not adjacent to a metro area.

Nonmetro adjacent counties—

Nonmetro counties physically adjacent to one or more metro areas and having at least 2 percent of the employment labor force in the county commuting to the central metro county.

Budgetary Terms

Budget authority. The authority becoming available during the year to enter into obligations that will result in immediate or future outlays of government funds. In some cases, budget authority can be carried over to following years. It can take the form of appropriations, which permit obligations to be incurred and payments to be made, or authority to

borrow, or authority to contract in advance of separate appropriations. Supplemental appropriations provide budget authority when the need for funds is too urgent to be postponed until the next regular annual appropriations act.

Obligations incurred. Once budget authority is enacted, government agencies may incur obligations to make payments. These include current liabilities for salaries, wages, and interests; contracts for purchase of supplies and equipment, construction, and the acquisition of office space, buildings, and land. For Federal credit programs, obligations are recorded in an amount equal to the estimated subsidy cost of direct loans and loan guarantees.

Outlays. This is the measure of government spending. Outlays are payments to liquidate obligations (other than repayment of debt), net of refunds and offsetting collections.

Direct loan. This is the disbursement of funds by the Government to a non-Federal borrower under a contract that requires repayment, with or without interest.

Loan guarantee. This is any guarantee, insurance, or other pledge with respect to the payment of all or a part of the principal or interest on any debt obligation of a non-Federal borrower to a non-Federal lender.

Fiscal year. A fiscal year is the U.S. Government's accounting period. It begins October 1 and ends September 30 and is designated by the calendar year in which it ends.