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Mr. Chairman, I am pleased to appear before this Subcommittee to discuss the need for a federal program to assist state and local governments in providing public services to areas impacted by major energy developments over the next decade. In my remarks, I will address four major issues:

- o The regional economic problems that are expected to accompany an accelerated rate of energy development;
- o The ability of state and local governments to finance the public services necessary to accommodate the development;
- o The nature of the financing problem and how it could appropriately be addressed by a federal program; and
- o The extent to which S. 1699 would represent an effective federal program.

Regional Economic Problems

For at least the remainder of this century, the United States will meet an increasing share of its energy demand through mining more coal and uranium, building more power plants, and constructing facilities to produce synthetic fuels from both coal and oil shale. When the development of these energy resources occurs in remote and sparsely populated areas of the country, the sudden influx of workers and their families may create instant cities, or "boom towns," which result in significant economic and social problems. The population attracted by energy-related developments will

need expanded state and local public services such as police and fire protection, education, and health services. In addition, a host of other services will be needed, such as local roads, water, and sewerage, which require significant capital investment and long lead times to construct. Local governments, may not be able to provide these services and facilities when they are needed. Rapid population growth may cause overcrowded housing and overburdened waste disposal systems. It may exceed the capacities of medical facilities, schools, transportation systems, and law enforcement institutions. Sometimes booms turn to busts, as, for example, when a coal reserve is depleted. The shift in economic fortunes may leave a community with excess facilities and services, as well as the burden of paying for them.

The Ability of State and Local Governments to Finance Public Services

In order to provide an approximation of the overall operating and capital costs to state and local governments of accommodating energy development, it is first necessary to develop some assumptions regarding coal demand and the construction of synthetic fuel and power plant facilities over the next decade. There is considerable uncertainty about the speed at which these resources will be developed, but we have chosen to assume that it proceeds at relatively high rates. In 1979, U.S.

coal production was approximately 770 million tons. We have assumed that it increases to 1.0 billion tons by 1985 and 1.3 billion tons by 1990. In addition, we have assumed that construction begins on approximately 20 commercial-size synthetic fuel plants and 10 to 15 mine-mouth power plants during the decade. Under these assumptions, an additional 70,000 direct jobs will be created by 1990 in the 10 states accounting for most of the growth. The operating or **noncapital** costs necessary to provide public services for these increased populations would be approximately \$330 million in 1985 and over \$950 million in 1990, assuming a 9 percent inflation rate. The capital costs of roads, sewers, firehouses, and other structures would be about \$275 million in 1985 and more than \$400 million in 1990. If the capital requirements are amortized **over** a 20-year period, the total annual cost to state and local governments would be about \$425 million in 1985 and \$1.2 billion in 1990, including operating, maintenance, and interest costs.

Turning to the revenue side, and holding the existing tax rates constant, we find that energy development will generate revenues in excess of \$500 million in 1985 and about \$1.3 billion in 1990, from severance and production taxes as well as state and local income, sales, and property taxes. In the aggregate, therefore, it appears likely that the additional infrastructure and operating costs of state and local governments will be more than offset by the additional tax revenues over the next decade,

without adjustments to the tax rates. However, a number of financial problems remain:

- o State and local governments must finance the expansion in public services before the tax base increases the tax revenues. They will therefore be forced into the capital markets to borrow these funds. Given the risks inherent in some types of energy development (for example, some **synfuels**), some communities may find it difficult to borrow.
- o Most of the costs will fall on local governments, while most of the revenues will go to state governments through production and severance taxes. Consequently, it is critical that states make these revenues available to the impacted local regions.
- o Interstate **jurisdictional** problems may exist, where most of the energy-based revenue occurs in one state while most of the services are needed in an adjoining state.
- o In the aggregate, states appear to be able to cover costs; on a state-by-state basis, however, those states that have low severance tax rates may not be able to cover the costs without raising tax rates.

The Appropriate Federal Role

Given that, in the aggregate, the state and local revenues generated by accelerated energy development should more than offset the costs, it does not appear that the federal government needs to subsidize state and local government services either through grants, **lower-than-market** interest rates, or loan forgivenesses. Instead, the appropriate role appears to be primarily to assist local governments in obtaining financing to construct

roads, sewers, schools, and other infrastructure. A federal role may exist where there are interstate jurisdictional problems—that is, where the development in one state causes economic dislocation in an adjoining state. Finally, it may be desirable for the federal government to assist the states in making full use of existing grant and loan programs. For example, grants are available from the Environmental Protection Agency to assist with sewer construction, from the Department of Housing and Urban Development for housing and community development projects, and from Farmers Home Administration for planning.

The Effectiveness of S. 1699

S. 1699 authorizes \$2 billion, or \$400 million per year, over the 1981-1985 period for grants, loans, and interest subsidies. Of this, a maximum of 40 percent can be expended in the form of grants. Additionally, it authorizes \$1.5 billion in loan guarantees. The funds necessary to finance the expected infrastructure requirements of state and local governments over the next five years are estimated at approximately \$1 billion. Of this total, a significant share (10 to 20 percent) would most likely be financed through existing federal programs or by the private sector. For this reason, the authorization level included in the bill appears to be higher than

necessary. Moreover, because revenues generated by projected energy development will more than offset the costs, one has to question the necessity for interest rate subsidies, grants, and loan forgivenesses, all of which represent a direct taxpayer subsidy for these state and local government services. If the assumptions of this analysis are correct, grants could be limited to development costs in areas with interstate jurisdictional problems, and for purposes of economic planning.

While the financing mechanism could be either a loan or a loan guarantee, the latter suffers from the major disadvantage that it tends to circumvent the budget process. The federal government currently has over \$300 billion in loan guarantees outstanding. These are not included in the budget, and therefore the Congress has very little control over them. Federal government loans, on the other hand, require a direct appropriation, and the budget authority and loan outlays are reviewed in the normal budget and appropriation process.

In conclusion, the main problem facing state and local governments in accommodating an accelerated rate of energy development over the next decade will be in financing the expansion of public services before the tax revenues arrive to pay for them. Federal assistance could be most effective through a loan program of approximately \$1 billion. This would be

preferable to a subsidy program of grants, or loans with less than market rates of interest, or loans with forgiveness provisions. Grants may, however, be appropriate for purposes of planning and where interstate jurisdictional problems occur. Loan guarantees, because they are outside the budget process, are less desirable than federal loans.

Mr. Chairman, I would be happy to answer any questions.