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Law & Policy

"Greed Is Good"

Gordon Gekko, new or old, was right: money and profit matter, even in wetland restoration. There is little dispute that wetland restoration on private property creates significant ecological benefits that can be assigned cash value. Economists have estimated the monetary value of wetland functions as fishery nurseries, flood control, and pollutant removal. Those economic benefits are spread regionally and often to locations far removed from the restored property. Wetlands used for wildlife breeding can support recreational hunting and commercial fisheries tens, hundreds, and thousands of miles away. Similarly, wetland water quality functions and flood attenuation may inure to the benefit of people living a great distance from the restoration site. Connecting the monetary value of natural habitat to the private owners of the land generating that value can be a daunting task.

Wanting to obtain and maintain property value is "good greed." Those of us who own homes would like to see our equity increase by increased housing values. Socially, that is good greed, as the conditions needed to protect and enhance individual home values—clean and safe neighborhoods, good schools, community amenities—inure to the benefit of society in general, as well as the individual homeowner.

We have not yet fully captured this good greed as a motivating factor for wetland preservation or restoration. Many professional disciplines are now focused on PES, or payment for ecosystem services. PES has a dual focus: (1) to identify and capture all of the monetary value that the ecosystem services provide society (preserved or enhanced through restoration); and (2) to incentivize preservation and restoration by giving the property owner his or her share of that monetary value of the ecosystem services. PES satisfies good greed by assigning ecosystem services their full, appropriate value so that PES can compete with the cash value of other property uses or improvements, such as constructing homes, offices, or commercial buildings.

> "We need to pay to preserve and enhance ecosystem services. We cannot meet our ecosystem restoration needs with prohibitions alone."

Payment for ecosystem services is not new. Society has long paid the landowner directly for preservation and directly paid for restoration of ecosystems. Direct purchase is the traditional method of obtaining special habitat, dating back to the conservation movement associated with President Theodore Roosevelt. It is the model that gives us national wildlife refuges, national parks, state and local preserves, and similar government ownerships. Direct payments also are at the heart of federal agricultural programs, buying conservation and wetland reserve easements on agricultural land. Direct payments give the landowner money and are paid by society as a whole, in general, through taxes.

We also have a history of indirect payments. The government encourages placing wetlands in conservation and restoration with tax benefits for land donation or for donation of funds for preservation and restoration to certain authorized recipients. This model of support for donations to nonprofit land conservancies has been used for many decades. This is a partial payment, in which the government pays less than the full land value by a reduced tax collection and the landowner also accepts less than full value by losing that part of the land value not recaptured as part of its tax deduction. The property owner's good greed is partially satisfied, even if that landowner also satisfies other desires, such as esthetic or environmental preferences.

What we have not yet mastered is development of large-scale use of PES outside of government payments. Wetland mitigation and conservation banking are major examples of PES systems completely between private parties. The banker converts the private land into an approved mitigation or conservation bank. When a third party needs to compensate for ecosystem impacts that are authorized under a permit, the mitigation or conservation banker has a market for the credits authorized by the restoration (or enhancement or creation) project. This incentivizes investment in those ecosystem improvements. The property owner benefits by receiving a payment for his or her property based on its ecosystem services value. Oversight of the mitigation bank, as provided in the 2008 Mitigation Regulations, provides control over the conduct of wetland restoration or enhancement. The property owner sees enhanced property value, satisfying good greed, by virtue of the private-to-private transaction with the banker and the private-to-private transaction between the banker and the credit purchasers. Society, through government and taxes, does not directly pay. While running the regulatory process certainly costs taxpayer money, one hopes that this cost is far below the costs of directly purchasing and restoring wetlands.

The problem is that the regulatory programs—the driver for mitigation and conservation banking PES—address only a small subset of prospective ecosystem impacts. Wetlands law has gaps. For example, not every action that adversely impacts a wetland is regulated. The law requires a "discharge of fill"; yet, altered hydrology can change wetland conditions without a regulated discharge. Federal law exempts many practices from the regulatory programs, such as maintenance of existing structures or existing agriculture. Discharges from nonpoint source runoff, carrying silt or chemical materials, are not regulated under wetland protection. Even as mitigation is strictly required and enforced under the 2008 Mitigation Regulations, the regulatory program will still provide the driver for only small quantities of wetland restoration. Similar limitations exist in the Endangered Species Act, the regulatory driver for conservation banking.

These regulatory drivers of mitigation and conservation banking PES are harsh, prohibitory mandates. For some property owners, these "do-not-destroy" prohibitions result in no payment for providing society's ecosystem services. No wonder the prospect of more regulation of private property is highly controversial!

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Nor has private-to-private PES made a dent in wetland and habitat restoration needs that lie outside of the regulatory program, such as restoration of historic losses. These historic losses present our greatest social challenge.

We need to pay to preserve and enhance ecosystem services. We cannot meet our ecosystem restoration needs with prohibitions alone. Nor can we rely entirely on non-economic motives, although voluntary restoration, preservation, and land donation reflect admirable personal choices. We need new ways to encourage private-to-private PES transactions to satisfy the good greed of private land ownership. ■

-Margaret "Peggy" Strand, Partner, Venable LLP

Mitigation

Beyond Soft, Mushy, or Hard: The Mitigation Rule's Preference Is Banking First

The 2008 Mitigation Rule brought about major changes to the way the U.S. Army Corps of Engineers (the Corps) conducts mitigation. One of these changes was the creation of a regulatory hierarchy, which established mitigation banks as the first option in a list of mitigation options (33 C.F.R. §332.3(b)1-6). Section (b)2 specifically describes this first option as a "preference." The preamble to the rule (73 Fed. Reg. 70 (Apr. 10, 2008)), which establishes the policy behind the rule, also discusses this hierarchy as a preference for mitigation bank credits in no less than 18 different places.

Although the preference is discussed in the preamble probably more than any other aspect of the rule, this aspect of the regulations is apparently hardest to implement. This difficulty is due to several factors: the reversal of emphasis from on-site permitee-responsible mitigation (PRM) to third-party watershed-approach mitigation; the inherent inertia in any bureaucratic organization; and the historic mistrust of entrepreneurial third-party mitigation providers.

This regulatory hierarchy has its basis in the enabling law (§314 of the National Defense Authorization Act of 2004), which requires the U.S. Department of the Army to maximize available credits and opportunities for mitigation and apply equivalent standards and criteria to each type of compensatory mitigation.

The preamble specifically links the preference and the law as follows:

> With respect to maximizing available credits and opportunities for mitigation, the preference established in today's rule for the use of credits provided by mitigation banks (see §332.3(b) [§230.93(b)]) should stimulate an increase in the number of mitigation banks and correspondingly the number of bank credits available for use.

And:

> Because there are fundamental differences in how these three types of compensatory mitigation are structured and conducted, we do not believe that Congress intended to require the promulgation of identical standards for all three methods of compensation. Instead, we interpret "equivalent" standards to mean standards which are equal in value, force, or meaning . . . We have also included a preference for bank credits over advanced credits from in-lieu fee programs. We thus believe that the final rule fulfills the statutory directive to provide "equivalent" standards for the three types of mitigation to the maximum extent practicable.

Thus, the reasons for the preference are to stimulate the "maximum" number of credits and to provide a regulatory "equivalence" to an inherently un-equivalent process, where PRM obtains all its "credits" up front, at the time of permit issuance, while mitigation banks and in-lieu fees receive credit over time.

Almost immediately after the promulgation of the rule, many mitigation bankers started talking to their respective Corps districts about the hierarchy provision in the rule, asking the district to honor the preference for mitigation banks. Across the board, many Corps officials replied that the preference was a "soft" preference, or even a "mushy" preference. At the 2010 National Ecosystem and Mitigation Banking Conference hosted by JTA Associates, several presenters reported on studies that they had conducted on the use of mitigation bank credits versus PRM, with most showing that the percentage of mitigation credits derived from mitigation bank credits had not changed appreciably due to the rule. However, during that same conference, the Assistant Secretary of the Army, the Honorable Jo-Ellen Darcy, clarified that, in her opinion, the preference was not "soft" or "mushy," but perhaps even a "hard" preference. Later in the conference, Meg Gaffney-Smith, Chief of the regulatory program for the Corps, told a packed conference room that the Corps recognized the need to document better both hierarchy and compliance with the mitigation rule in all permit decisions.

Part of the reluctance to implement this preference is that prior to the mitigation rule, standard practice was to require on-site PRM. (See Clean Water Act §404(b)(1) Guidelines and the 1990 Mitigation Memorandum of Agreement between the Corps and the U.S. Environmental Protection Agency (EPA).) This had remained the practice despite the fact that the National Academy of Sciences recommended a "watershed approach" to mitigation and the use of third-party providers in its 2001 report on compensatory mitigation.

Interwoven with the shift toward third-party mitigation for the Corps is that a permit decision is, at heart, a reactionary process. The Corps issues permits only in reaction to a permit applicant's proposal. The Corps evaluates that proposal in light of the law and the regulations and is not supposed to advocate any particular solution. The hierarchy in the rules is a change, in that it now places the Corps in a position to show a preference for a solution. Many Corps officials understandably do not want to be put in a position of advocacy, and, therefore, are reluctant to push the hierarchy, since they are not supposed to be advocates for any particular solution.

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Implementing the preference is also stymied by the Corps' historic mistrust of private, entrepreneurial third-party mitigation providers by Corps staff. Speaking very broadly, and based on my experience as both a regulator and a banker, the two groups of people are very different in outlook and temperament. One group is cautious and bound to follow established rules and regulations; the other needs to take risks and develop new practices. It follows, then, that there would be some natural friction between the two groups, which has led to both real and perceived mistrust. Not surprisingly, both sides have been disappointed with one another over the preference issue. The mitigation banking community has been frustrated that Corps officials have not, in the bankers' opinions, been either informing or promoting the regulatory hierarchy, while Corps officials have been annoyed at the mitigation bankers for pushing a solution that applicants may not put in their permit applications.

The mitigation rule puts no modifiers—soft, mushy, or hard—to the preference. Mitigation banks are first in a hierarchy of mitigation.

Corps headquarters, EPA headquarters, and mitigation bankers have agreed that part of the solution will be better documentation in permit decisions of both the hierarchy and compliance of a permit with all the required components of a mitigation plan (33 C.F.R. §332.4(c)). Mitigation bankers are also asking Corps districts to better highlight available mitigation options and the rule hierarchy on Corps websites, similar to the way they provide applicants with access to permit forms and guidelines for permit applications. The ongoing rollout of the Regional Internet Bank Information Tracking System database will help, but it is not really designed to help an applicant figure out mitigation options and hierarchy. The Chicago District used to have a mitigation guidelines handout that explained the different mitigation options available to an applicant. Something along those lines, set up to explain the hierarchy, would be most helpful.

The mitigation rule puts no modifiers—soft, mushy, or hard—to the preference. Mitigation banks are first in a hierarchy of mitigation. The preamble to the rule discusses why. Although the rule provides for district engineers to be able to override the preference, those reasons are limited, and must be documented. I ask the Corps to both provide applicants with easily accessed information about mitigation options in the district, and to provide documentation in the permits as to the compliance with the preference. ■

-David Urban, Director of Operations, Ecosystem Investment Partners President, National Mitigation Banking Association (2010-2011)

The views expressed here are the author's only and not the stated policy of either Ecosystem Investment Partners or the National Mitigation Banking Association.

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What revenue source seems to be the most recession-proof? Interestingly, if perhaps not surprisingly, it is lottery proceeds. All three states that have lottery proceeds directed to conservation activities—Arizona, Colorado, and Minnesota—report that revenues have been steady or increasing over the past few years.

Regardless of the economy, income from some revenue sources that come from voluntary actions can be affected by competition. Both New York and Ohio give taxpayers the opportunity to make a contribution toward conservation programs on their tax forms. New York's Return a Gift to Wildlife fund was the first on-the-tax-form contribution option in the state; it began in 1984. The initial revenue from the program was between \$1.5 million and \$2 million annually, but recently it has decreased to about \$500,000 annually. Over that same period, six other contribution options were added to the tax form. Did competition from the other options lead to the decrease? Somewhat surprisingly, the answer is no. Revenues were already sharply down before the second contribution option was added to the tax form, and most of the funds seem to follow the same pattern of having revenues increase sharply at first, flatten out for a few years, and then start to decrease. In fact, people who donate to one fund are actually likely to donate to multiple funds. Revenue for the Ohio Wildlife Fund has a pattern of being higher in odd-numbered years and lower in even-numbered years. What is the cause of this unstable if predictable revenue pattern? One theory is that, for a long time, the Wildlife Fund was one of two contribution options on the tax form. Every other year, it was listed as the first contribution option, and those years correspond with the years of higher revenue. The stability of this revenue source may be as arbitrary as its position on the tax form.

Conclusion

As states and tribes look to diversify their finances by instituting any of the multitudes of revenue sources that are being used successfully across the country, it is important that they understand that success is not guaranteed simply because the funding source worked somewhere else. It is critical to investigate the factors that made the funding source successful and determine whether those same factors will apply with their wetland program. In particular, states and tribes should focus on any legal hurdles to implementing the funding mechanism, fully understand the legislative process ahead, and be realistic about the likelihood that the governing body will approve the mechanism. Also, states and tribes should assess whether the revenue source will come directly to their program and whether it will be protected from being used for other general fund priorities. Finally, states and tribes should investigate the likely stability of the revenue source and its sensitivity to economic factors, the housing market, and competition from other options. With this research, states and tribes can make a more informed decision about whether a particular funding mechanism is worth pursuing for their program. ■

ENDNOTE

1. *See* http://www.fhwa.dot.gov/policyinformation/statistics/2008/mv1.cfm (last visited Sept. 1, 2010).