# POTEMKIN VILLAGES[1] OF THE WEST: HOW A SIMPLE PAYMENT TO COMPENSATE LOCAL GOVERNMENTS BECAME AN UNCONTROLLABLE FEDERAL SUBSIDY

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B. Sovereign Immunity Meets Federal Land Policy: What It Means to You

In general, under the doctrine of sovereign immunity, federal land holdings are exempt from state and local taxation; however, this exemption may be waived by Congress.[29] Although some criticize this immunity,[30] in response to perceived inequities Congress opted to enact a system wherein a portion of the lost tax revenue is recouped through PILT rather than create a blanket exemption.[31]

Congress enacted PILT in 1976 on the recommendation of the Public Land Law Review Commission (PLLRC).[32] In response to growing concerns over the environment and the disposal of federally held lands,[33] the PLLRC suggested that the United States reverse the then-prevailing policy toward the active disposition of all remaining ñunappropriated ˛ ]t]t

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governments uncompensated for the burdens permanent federal control imposed[35] and agreed that local communities should be offered compensation to offset the loss in local tax revenue.[36] Because federal ownership under the former regime was considered temporary, this change, therefore, occasioned reconsideration of revenue sharing programs generally.[37]

According to the Government Accounting Office (GAO), PILT is ñthe most wide-ranging programò designed to compensate local governmental bodies for the costs imposed by federal land ownership[38] and

engage in notice-and-comment rulemaking under 5 U.S.C. § 553.[45] Although other reforms may be proposed ð for example, the abolishment of PILT entirely[46] ð these are highly unlikely to succeed and might cause more harm than good.[47] By utilizing notice-and-comment rulemaking, DOI has the best opportunity to revamp its administration of PILT to bring itself into alignment with congressional intent.[48] Furthermore, this alternative is attractive because it preserves the agencyôs discretion to alter course in the future[49] and is the choice most likely to be upheld in court.[50]

Part I discusses the history of public land management in the United States, in particular the development of the current land management regime, as well as the creation of the Payment in Lieu of Taxes program. Part II examines the legislative intent behind the payments deduction provision of PILT, the administrative interpretation of the provision, and state laws that bypass this provision. Also, Part II considers judicial interpretations of PILT and any bearing that may have on the deduction issue, as well as Supreme Court decisions on the issue of judicial deference to administrative decisions and regulations. Part III examines whether, in the light of the aforementioned history and relevant law, DOI could enforce the Comptroller General Opinion requiring that service districts be independent and what effect such enforcement might have. Part IV considers various counter-arguments that might be made against strict enforcement of the deduction provision. Part V concludes by recommending that DOI administer PILT in a manner that more closely adheres to the original legislative purpose of the Act and recommends

[44] Essentially, Western legislators are fighting to make PILT a permanent mandatory program and Eastern legislators are fighting their efforts. 160 Cong. Rec. S385-01 (daily ed. Jan. 16, 2014) (statement ofvePILT -6(s)9( )-49(a)4(1p0(a)-5

and settlementò in 1900.[57] As a result, more recently, the debate has changed from ñland disposalò to ñland managementò and even ñland stewardship.ò[58]

A. 1800s through 1970s

Prior to the enactment of PILT, the primary source of revenue sharing funds between federal and local governments came ñfrom the sale of commodities from public lands.ò[59] State and local governments in areas with high concentrations of federal lands were encouraged to depend almost exclusively on the extraction of natural resources for local revenues, to the detriment or neglect of other development possibilities.[60] This early program had two major side effects on contemporary land management.[61] First, there was widespread instability in payments as the market prices for the commodities extracted ð such as timber and minerals ð rose and fell, raising concerns arose over the viability of federal programs as a dependable revenue source for local governments.[62] Second, and perhaps more importantly, the variability in federal payments had the effect of encouraging local communities to take an active role in setting the goals of land management policies.[63]

In large part, the mission of the PLLRC in 1964 was to investigate and suggest changes to the prevailing public land policy that produced these perverse incentives.[64] The situation on the ground, after over a hundred years of attempting to dispose of federal lands, left the federal government unprepared to manage vast tracts of land.[65] Although the PLLRC was advisory, the principles that it suggested were powerful and have had a lasting impact on land management, including the shift towards management for conservation and recreation rather than disposal and

development.[66] Public opinion and administrative policy provided an additional impetus for the shift, having together rendered the disposal program ñineffective.ò[67] As a result, the underlying policy objectives of federal land managements, as it stood, both produced ñno predictable administrative policyò[68] and undermined the basic assumptions of the program.[69]

B. Post-1976

As noted above, since 1976 land policy sharply shifted toward retention of public lands and management for environmental purposes and recreation.[70] The Federal Land Policy and Management Act (FLPMA), which created the Bureau of Land Management (BLM) and assigned to it the duty to manage most federal land, embodied this shift.[71] As a result of BLMôs sweeping responsibilities, the Secretary of Interior

amounts of nontaxable land in their jurisdictions,[76] as well as providing a more regular revenue stream for communities with heavy concentration of federal lands.[77] This is because the new policy essentially foreclosed the possibility that the majority of federal lands would ever pass into state or local hands.[78] Rather than act as a comprehensive revenue sharing scheme, the PILT Act kept the old laws in place, but deducted payments-in-lieu-of-taxes by the amount received under those other programs.[79] Today the states receiving the greatest amount of PILT are California ($41.5 million), Utah ($35.4 million), New Mexico ($34.7 million), Arizona ($ 32.2 million), Colorado ($32 million), Montana ($26.5 million), Alaska ($26.4 million), Wyoming ($25.3 million), Nevada ($23.3 million), and Washington ($17.2 million). [80]

## III. THE PAYMENT IN LIEU OF TAXES ACT: PURPOSE AND INTERPRETATION

Section 6903 of the PILT Act makes clear that payments must be reduced if the unit of government received money falls under another ñpayment lawò during the prior fiscal year.[81] However, DOI allows local governments to avoid deductions if these payments are not ñreceived byò the local governments because the monies are not under their direct control.[82] That is, if the monies are diverted to independent entities for which the local government is not ñresponsible,ò the county is deemed to have not received this money, and thus their total amount of PILT is not

[76] The costs and burdens are not simply the loss of taxes, but also the maintenance of roads through federal lands as well as policing*; see* Seastone, *supra* note 9, at 376*; see also* PUBLIC LAND LAW REVIEW COMMôN, *supra*

affected.[83] On the other hand, if the county ð or other local unit of government ð retains control, theoretically, the entity is not independent and the monies received must be deducted from PILT.[84] Because DOI has been lax in the enforcement of this condition, many states have created quasi-independent bodies to funnel ñpayment lawò funds and thus prevent deductions.[85] As enforced, states and local governments are able to ñdouble-dipò[86] because they can, and generally do, receive the benefits of both PILT and payments under other federal revenue sharing laws.[87] This is wrong because (1) it is contrary to the intent of Congress, which added the provision reducing PILT payments specifically to prevent this from occurring; and (2) it allows resource-rich counties to receive a disproportionate amount of federal funds.[88] Furthermore, if enforced as enacted, PILT would disincentivize extractive resource development by making this means of development more costly as compared to alternatives.[89]

[83] This it does in accordance with a Comptroller General Opinion requested by the Solicitor General of DOI. U.S. GEN. ACCOUNTING OFFICE, *supra* note 18, at 20.

[84] *See* discus1See

PILT.[97] Despite his assurances and those of other congressmen, however, double payments commenced because states discovered a work-around to avoid deductions.[98]

2. *Implementation and Agency Interpretation*

As issued in 1977, the original definition of ñmoney transfersò was limited to ñpayments by or through the State government to units of local government.ò[99] During the notice-and-comment process, BLM received a number of comments suggesting ñmoney transfersò should exclude ñfunds received by qualified units of local government under [other payments laws] and passed through to single purpose units of government.ò[100] After initially rejecting this suggestion,[101] BLM reconsidered and issued an amended rule in 1980.[102] This provision

[97] ñ[W]e . . . [have] very carefully deducted any revenues from timber sales, or minerals, mineral royalties, from the moneys paid in lieu of taxes under this bill so the county [does] not get a double revenue from the federal government.ò 127 Cong. Rec. 16,690 (1981).

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counties, but which state law obligated the counties to pass to another entity, were not ñreceived byò the county for purposes of

memorandum defined service districts as ñlocal government entities separate from county governments.ò[122]

3. *States Seek to Maximize Available Subsidies*

According to 31 U.S.C. § 6903(a)(1)(H), one of the federal revenue sharing program payments deducted from PILT is the Mineral Lands Leasing Act.[123] The Mineral Lands Leasing Act established a leasing system that allows private parties to obtain leases to federal lands to extract oil and gas.[124] In return, the law requires that the private party, whether an individual or corporation, pay a fee to the government in the form of ñrentals and royalties.ò[125] Fifty percent of these royalties are paid to the state where the mineral extraction activity occurs.[126] These payments are particularly important in the West-Southwest region of the United States where the top four states receiving the greatest amount of federal mineral royalty disbursement received almost two billion dollars in payments in fiscal year 2012 alone.[127]

As a ñpayment lawò under PILT, normally, any monies received under the Mineral Lands Leasing Act should be reported by the state and deducted from the countyôs PILT payment for the following year.[128] However, § 6903(b)(1)(A) only applies this reduction to ñunit[s] of general

[122] A service district might carry out functions as varied as the education of minors and the construction of road projects. *Id.*

[123] § 6903(a)(1)(H) (2006). For examples of other revenue sharing programs whose payments are to be deducted from PILT, see discussion *supra* note 109.

[124] Specifically, these parties are authorized to ñsearch for and develop . . . deposits.ò James B. Martin, *The Interrelationships of the Mineral Lands Leasing Act, the Wilderness Act, and the Endangered Species Act: A Conflict in Search of Resolution*, 12 ENVTL. L. 363, 367 (1982).

[125] For example, one provision, regarding the extraction of ñgold, silver, or quicksilver [mercury] deposits,ò requires that the lessee pay a royalty of not ñless than 5 per centum nor more than 12 ½ per centum of the net value of the output at the mine.ò 30 U.S.C. Ä 292.

[126] *See* 30 U.S.C. Ä 191(a) (ñAll money received from sales, bonuses, royalties . . . and rentals of the public lands under the provisions of this chapter . . . shall be paid into the Treasury of United States; and . . . 50 per centum thereof shall be paid by the Secretary of the Treasury to the State . . . within the boundaries of which the leased lands or deposits are or were located . . . .ò); Ä 191(c)(1)-(2)(A) (ñNotwithstanding the first sentence of subsection (a) of this section, any rentals received from leases in any State . . . on or after August 8, 2005 shall be deposited in the Treasury . . . . 50 percent shall be paid by the Secretary of the Treasury to the State within the boundaries of which

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purposeò districts.[137]

accomplish their own responsibilities.[146] This practice would appear to require PILT payment reductions ð as such districts are not ñpolitically and financially independentò nor are they ñalone responsible for providing the services in questionò[147] ð and yet, such deductions are rare[148] and abuses are common.[149]

b. Pass through Laws: Theory and Examples

As revised and renumbered in 2008,[150] the State of Utah allows counties to establish so-called óspecialô service districts under the Service District Act.[151] This Act sets forth certain guidelines regulating the delegation of powers to and creation of service districts.[152] According to Utah Code Annotated § 17D-1-301(1), special service districts are governed by the county or other local government that creates the district and are limited to those powers delegated to the service districtôs administrators.[153] The authority to delegate is limited; for example, ñan administrative control board . . . [may not] levy a tax on the taxable property within the special service district.ò[154] On the other hand, the Service District Act allows for financial independence,

[146] *Id.*

[147] *Id.* at 3; see *also id.* at 4, n. 1 (ñ[T]hese functions would presumably be the responsibility of the counties in the absence of independent special districts. However, implicit in the Comp[troller] Gen[eral] opinions is the notion that these functions are not the responsibility of the county so long as they are assigned to a distinct political unit.ò).

[148] When they do occur, state and local governments are inclined to take care to avoid future deductions; see discussion, *infra* Subsection II.A.3.b.

[149] For example, in *United States ex rel. Erickson v. Uintah Special Services District*, the qui tam plaintiff alleged that Uintah County, Utah had ñremove[d] valuable deposits of tar sands that [the service district] had stockpiled for road repairs . . . for its own uses and without any accountability.ò United States *ex rel* Erickson v. Uint

Countyôs PILT payments.ò [165] Following the creation of the district, Washington County, for the first time, received the full amount of PILT due under the statutory formula.[166]

This example is particularly egregious because, the service district was created to allow the County to receive more PILT[167] during tough economic times.[168] To alleviate voter concerns, the district was not delegated the authority to impose tax obligations.[169] Local attorneys and politicians explained that the service district was the best way to bring in more federal money for Washington County.[170] An attorney for the county told the paper that ñthe formation of the district would be a win-win situation because [it will] maximize[e] the countyôs PILT money.ò[171] The purpose of the

Colorado has actually rather openly gone a step further than either Wyoming or Utah. In 2011, the Colorado General Assembly passed H.R. 1218, which explicitly ñauthorize[es] the creation of federal mineral lease districts as funding and service delivery mechanisms . . . to

The only case interpreting PILT in the FCA context is *United States* ex rel. *Erickson v. Uintah Special Services District*.[215] In *Erickson*, the plaintiff alleged that Uintah County, Utah established a service district to defraud the federal government of Mineral Lease Funds through the ñtransfer [of] Mineral Lease Funds into the general coffers of Uintah County to be applied to general county budgetary expenses . . . far beyond the single purpose for which [USSD] was created.ò[216] The failure of the county to disclose the receipt of the ñmineral lease money,ò therefore, violated the FCA.[217]

The district court rejected this theory because the service district did not misrepresent and could not misrepresent its ñnature as a service district.ò[218] The district court further concluded that as a service district, USSD was a ñdistinct legal entity . . . under the control of the County. USSD [could not] misrepresent its dependence or independence from the County.ò[219] As Congress placed no conditions upon the disposal or use of federal lease monies, the district court found a False Claims Act claim impossible.[220]

3. *Judicial Deference (or Non-deference) to Administrative Decision Making*

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However, even assuming Congress has not spoken to the precise question nor that the statute is otherwise ambiguous, at step two the court does not have unbridled discretion to

the plain meaning of the statute, any legislative history,[237] and any other relevant canons or tools that aid judicial construction.[238] After these resources have been exhausted and if the statute

a majority, as a member of the D.C. Circuit, Judge now-Justice Scalia wrote that ñthe assessment of the GAO [is] an expert opinion which we should prudently consider but to which we have no obligation to defer.ò[263] In a more recent concurrence, Justice Scalia reiterated that Comptroller General Opinions are not entitled to *Chevron* deference.[264] This is significant because DOI relied upon the Comptroller Generalôs interpretation to set its policy on PILT.[265]

## IV. FIXING

interpretive rule.[279] Even in that case, the agency would be forced to defend the policy as though the letter did not exist.[280]

Another enforcement alternative would be for DOI to discard the Comptroller Generalôs interpretation entirely as not binding upon the agency.[281] When BLM issued the first PILT

On the other hand, the stated purpose of the 2004 rule amendment was to ñstreamline[] the budget processò ð not to make substantive changes to PILT.[299] Because the change was considered entirely administrative, full notice-and-comment procedure was not followed in the promulgation of the rule.

but that does not mean they are necessarily guilty of any crime.[308] Second, the complexities of such an action are many, as highlighted in *Erickson*.[309] There the district court noted that neither the county nor the service district submitted any claims to the federal government; rather the

PILT was explicitly intended not to allow local governments to receive multiple revenue sharing payments,[315] the agencyôs interpretation is contrary to the unambiguous direction of Congress.[316] Therefore, the plaintiff would argue DOIôs interpretation of ñreceivedò is faulty because the legislative history is clear and would ask the court to direct DOI to evaluate the independence of districts created to ñmaximize PILT.ò[317] This argument, however, is likely to fail because this particular problem with PILT was raised as early as 1979, but has never been addressed by Congress.[318] The limited legislative history could also be read as favoring DOIôs interpretation because the Senate Report explicitly disclaimed any intent to penalize counties that did not actually receive revenue sharing payments.[319]

2. *Rulemaking*

The best way forward for the agency, or at least the means most likely to hold up in court,[320] would be to conduct a full notice-and-comment proceeding, with all the procedure provided under 5 U.S.C. § 553.[321] In this scenario, the agency could take the relatively ambiguous language of PILT ð requiring payments be ñreduced . . . by amounts the unit

[314] Although there is no formal interpretation of this language, see 43 C.F.R. § 44.11, at least informally, the agency has determined that ñ[o]nly the amount of Federal land payments actually received by units of government in the prior fiscal year is deducted. If a unit receives a Federal land payment, but is required by State law to pass all or part of it to financially and politically independent school districts, or any other single or special purpose district, payments are considered to have not been received by the unit of local government and are not deducted from the Section 6902 payment,ò U.S. DEPôT OF INTERIOR, *supra* note 138, at 11.

[315] *See* 122 Cong. Rec. 25,743, 25,747 (1976) (statement of Rep. Weaver) (noting that receipts local governments received from the federal government were to be ñdeducted from the payments in lieu of taxes . . . [therefore] [t]here is not a double paymentò); S. Rep. 94-1262, at 15 (1976) (ñ[The Act] requires that any payments received under [a payment law] . . . which are *actually received* by a unit of local government are . . . deducted.ò) (emphasis added). Five years later, when amending PILT, Representative Weaver reiterated that ñwe . . . [have] very carefully deducted any revenues from timber sales, or minerals, mineral royalties, from the moneys paid in lieu of taxes under this bill so the county [does] not get a double revenue from the federal government.ò 127 Cong. Rec. 16690 (1981) (statement of Rep. Weaver).

[316] Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842 (1984).

Furthermore, as enforced and interpreted, the deduction provision is superfluous because states and local governments often avoid PILT reductions by simply diverting revenue sharing payments through service districts; see CORN, *supra* note 85 (ñIt would be in the interest of every state to enact pass-through laws. . . .ò).

[317] Such an example might be that of Washington County, which openly stated that ñthe formation of the district . . . maximizes the countyôs payment in lieu of taxes money.ò SPECIALLY FUNDED TRANSPORTATION SPECIAL SERVICE DISTRICT A 143.85 237.28 Tm[(D)] TJETB50048 0F6817vJ(A)-27(L)36( 0 09(l)18(e)4( )-69(o)-19(r)-6( )-69(s)9(p

because notice-and-comment procedure allows parties to participate in the rulemaking process[333] and requires the agency to respond to relevant comments in a substantive way,[334] such a procedure is much more likely to be viewed as legitimate and democratic than an otherwise arbitrary decision by the agency.[335] Furthermore, the use of notice-and-comment rulemaking may help the agency to preserve its discretion in the event of a judicial decision on the matter.[336]

3. *Statutory Change*

As enacted, PILT is incredibly complicated[337] and easily misread and misapplied.[338] The statute, therefore, should be changed either to end the possibility of abuse by the states[339] or to eliminate the payment law deduction provision.[340] The law could also be restructured to promote community development, perhaps by requiring that the money be spent in a particular manner[341] or that it be distributed in such a way as to encourage conservation of resources rather than consumption.[342]

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A single payment system for federal revenue sharing and land payments was proposed as early as the PLLRC report,[343] but was implicitly rejected by the Congress that enacted PILT.[344] Such a system would have several benefits, including likely increased administrative efficiency.[345] Currently, PILT is simply another layer on top of what was already an incredibly complicated system.[346] For example, payments to local governments under ten different payment laws are deducted from PILT[347] and the acreage of federal land managed by the Departments of Agriculture, Defense and Interior ð through no less than seven distinct agencies ð is used to calculate the federal acreage in the jurisdiction of the local county.[348] DOI then relies on the states themselves to accurately pass on data indicating the precise levels of revenue sharing payments distributed to local governments.[349] Moreover, considering that the basic purpose of all federal land payment schemes has been to provide adequate compensation for lost taxes, a single system could also be designed to pay true tax equivalency for un-taxable federal land.[350]

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INCENTIVES FOR PROTECTING THE ENVIRONMENT, at vi (2001), *available at* http://yosemite.epa.gov/ee/epa/eerm.nsf/vwAN/EE-0216B-13.pdf/$file/EE-0216B-13.pdf.

[343] In fact, the PILT program was proposed as an alternative to the existing system of revenue sharing payments because ñthe system of revenue sharing [bore] no relationship to the direct or indirect burdens placed on state and local governments . . . . Although [these programs] were originally designed to offset the tax immunity of Federal lands, the existing revenue sharing

Such a system is not, however, without serious defects, likely those which led the enacting Congress of PILT to create PILT instead.[351] The complex bureaucratic operation of the current regime engenders special interests, which would not likely give up their favored position without a fight.[352] Presumably the losers under the mandate would be incentivized to adopt alternate revenue streams or exploit existing streams to their benefit in new ways, while those unable to do so would simply suffer the loss of revenue.[353]

Congress could also decide, rather than reauthorize PILT or even continue the program, to discontinue PILT entirely. This seemingly drastic option is not without its proponents; however, this is perhaps the least likely to occur given the complex history and interests involved in PILT.[354] Although the program may be, in effect, a Western subsidy,[355] it is a *bipartisan* Western subsidy[356] that supports that most basic unit of Western consciousness: the small-town, rural community.[357] An attack on PILT is, despite the contradiction in terms, an attack on the

sharing monies comes closer to approximating the correct level of payment.[375] Congress perennially promises greater amounts of PILT, but has failed, until recently, to appropriate sufficient funding.[376] These payments are also limited such that a governmental unit often receives less than ñit would receive if actual property taxes were being distributed.ò[377] Moreover, counties and local governments are unable to enforce the authorized PILT obligation[378] where Congress has failed to appropriate enough money to cover the obligation.[379] Therefore, being able to receive PILT and 6903(a) payments in full more closely approximates the ñcorrectò amount of PILT[380] and is more reliable for local governments planning yearly budgets and

received if development did not occur, but still had to cover the costs that development created, the county would have the incentive to seek alternative forms of development.[387] On the other

payments and discouraging states from creating inefficient ñsubdivisions or districtsò for the sole purpose of ñmaximiz[ing] federal payments.ò[391] At the same time, as written, the Act is very complicated[392] and provides for inequitable payments[393] that local governments contend are below,[394] and others contend are significantly above,[395] true tax equivalency of the communities receiving them.[396] Congress, therefore, should amend PILT to provide more equitable payments