MEMORANDUM

DATE	November 16, 2017
FROM	Environmental Incentives LLC
TO	United States Congress Members & Staff
RE	Recommendations for increasing conservation outcomes from Farm Bill investments through NRCS programs

The Farm Bill holds great potential to stimulate and scale public-private partnerships, and significantly increase the effectiveness of tax dollar investments using market-based approaches. This memo provides recommendations for the increasing conservation outcomes from Farm Bill investments through Natural Resource Conservation Service (NRCS) programs by leveraging pay for performance procurement mechanisms. These recommendations are informed by a recent experience of Environmental Incentives and its partners attempting to implement pay for performance through a Regional Conservation Partnership Program (RCPP) funded project, and inspired by our overarching goal to increase the environmental return on investment (EROI) of taxpayer funds. Although our recent direct experience is with the RCPP, these recommendations should be considered for all existing NRCS programs, and any new NRCS programs.

BACKGROUND

New and innovative approaches to conservation are increasing the EROI of taxpayer and mitigation funds. Pay for performance procurement, credit exchanges, water funds and green bonds utilize incentives to better align public and private sector interests, and leverage private capital to produce more conservation outcomes, thus reducing the burden on taxpayer dollars. The Farm Bill funds significant investments in conservation, however as currently structured, NRCS programs investing Farm Bill funds are not capable of utilizing many of these innovative approaches. Increasing flexibility in NRCS programs is necessary to harness the benefits of these and future innovative approaches, and specific language in the next Farm Bill is needed to direct NRCS staff to use these innovative tools, and reduce NRCS and partner costs that become a barrier to their practical application.

PAY FOR PERFORMANCE PROCUREMENT

Pay for performance procurement is an effective tool to increase the EROI of taxpayer funding. Pay for performance contracts link all or some portion of payments to the delivery of verified conservation outcomes, as opposed to payments entirely based on cost reimbursement. Pay for performance procurement rewards project proponents for cost-effective delivery of conservation outcomes and reduces risk of taxpayer dollars funding projects that do not deliver the proposed magnitude of intended results. Instead of funding actions in the hope of producing conservation outcomes, pay for performance contracts allow the NRCS to cost share conservation outcomes directly. By using competitive bidding processes that rank project by cost-effectiveness and contracts that pay per unit of outcome, NRCS can reduce the level of effort needed for project review while reducing the risk that limited funding will be spent on projects that under-perform.

CHALLENGES FROM IMPLEMENTING RCPP PROJECT "GREATER OUTCOMES FOR GREATER SAGE-GROUSE"

Environmental Incentives, along with Partners for Western Conservation, State of Nevada and State of Colorado, are implementing a 2015 RCPP project titled "Greater Outcomes for Greater Sage-Grouse" with the objectives of 1) maximizing the conservation outcomes of projects funded by using outcome-based metrics to select projects and pay project proponents, 2) generating additional outcomes over time by developing a revolving fund financed by repayment of project funds when projects are used as mitigation in the future, 3) increasing conservation outcomes over time by adaptively managing the outcome-based metrics based on application on several projects across two states, and 4) increasing transparency and demand for conservation outcomes by reporting outcomes produced from all projects funded.

In order to achieve these objectives, the partners intended to use RCPP funds to administer a competitive RFP process, secure pay for performance contracts with landowners based on outcome-based metrics, implement conservation practices, facilitate adaptive management processes amongst partners, and report outcomes produced by projects. However, given that RCPP rules require funds to be distributed to land owners by NRCS using existing programs such as EQIP, which are subject to project selection, expense and contract term restrictions, several aspects of the project could not be implemented as intended, which will reduce the conservation outcomes from this funding. Further, although NRCS staff were supportive throughout, the project partners had to invest significant, unplanned match resources into redesigning the original project to work with existing NRCS programs that would have gone towards producing on-the-ground conservation outcomes.

RECOMMENDATIONS TO HARNESS THE ENVIRONMENTAL BENEFIT OF PAY FOR PERFORMANCE

Allow NRCS to invest Farm Bill funds using innovative pay for performance procurement and contract mechanisms.

Competitive procurement processes and pay for performance contracts can increase the conservation outcomes generated while reducing taxpayer risk. There is an enormous opportunity to increase EROI of Farm Bill funding if NRCS directly utilizes pay for performance techniques. This change requires a cultural shift and involves a significant learning curve. However, this can be overcome with toolkits (guidance and templates), training, and internal or external consulting assistance. For example, the NRCS Conservation Innovation Grant project "Pay for Success Strategies for Western States" developed a Pay for Performance Toolbox of materials[1] to support state and local agencies to use pay for performance procurement and contracting, and can be adapted to inform federal procurement policy clarifications. In addition, pay for performance payment structures vary significantly from context to context, and thus significant flexibility in contract terms is necessary. The near and long-term benefits for the environment, landowners and staff professional development are well worth the investment. Further, the risks associated with increased flexibility in contract terms is more than offset by the reduction in taxpayer risk provided by pay for performance. Thus, NRCS should utilize pay for performance procurement strategies to increase the EROI, and provide additional benefit to landowners and regional initiatives with Farm Bill funding.

Enable non-federal partners to more flexibly invest Farm Bill funds to increase conservation outcomes and best achieve partnership goals.

Currently, Farm Bill funds must be distributed by NRCS directly to landowners through existing NRCS programs, such as EQIP and CRP. This restricts the use of the funds, and limits the innovation and flexibility of the program. Allowing for more flexibility in the use of funds can attract private capital and increase partner cost sharing, and more efficiently deploy Farm Bill and partner match funds. For example, non-federal partners may already have elements of or all of the infrastructure (e.g. competitive procurement products and outreach channels, pay for performance contracts) necessary to implement pay for performance, while existing NRCS programs may not allow or are costly to adjust to meet the objectives of the project. Further, non-federal partners will often be able to deploy funds in more flexible

[1] http://enviroincentives.com/products/pay-success-contract-mechanisms-technical-brief/

ways which will enable the use of innovative and more effective approaches – including payments based on long-term stewardship (not permanent easements), buyer of last resort mechanisms, and revolving funds. Thus, the next Farm Bill should allow federal funds to pass through state, local or private entities and enable the sponsor to run procurement processes to select projects and pay for outcomes.

Adjusting existing NRCS program products (evaluation criteria, contract terms) to implement new innovative conservation approaches can cost significantly more than developing or adjusting existing non-federal program products, and can also delay implementation and reduce the available resources to produce conservation outcomes. Further, adjusting existing NRCS program products to implement new innovative conservation approaches can produce overly complicated products which reduce landowner interest and require additional, unnecessary non-federal partner and NRCS effort to secure landowner participation. To address these challenges, non-federal partners need additional flexibility to invest Farm Bill funds, and state and local NRCS staff need to support new innovative approaches instead of defending existing program restrictions. This includes allowing the metrics, such as habitat quantification tools, developed by regional programs be used to select projects and define pay for performance terms.

Lastly, non-federal partner funding can have restrictions of its own, and additional flexibility in the use of federal funds can enable more effective use of both non-federal partner and NRCS funds. For example, non-federal partner funds may be restricted to on-the-ground conservation measures, and the increased conservation outcomes from using pay for performance procurement would more than offset the NRCS funding needed for non-federal partners to develop and implement pay for performance procurement products. Thus, federal funds should be allowed to fund program development and contract administration costs.

Require project-specific, outcome-based reporting for any pay for performance investment of Farm Bill funds to ensure transparency and accountability.

Providing NRCS and partners more flexibility in how to deploy Farm Bill funds should be accompanied by additional accountability to the outcomes generated from their investments to ensure innovations are producing their intended result, and so that NRCS and partners can learn from these innovations. Pay for performance contracts use quantified and verified outcomes, which provide the data needed to track and report conservation outcomes. This direct feedback between conservation practices and outcomes enhances learning and increases transparency. Specific reporting requirements should be defined for each project, and should include key milestones (e.g. project design approved, construction completed) prior to delivery of outcomes, and specific outcome metrics (e.g. Farm Bill dollars per outcome unit, total investment per outcome unit).

SPECIFIC FARM BILL ADJUSTMENTS NEEDED TO SUPPORT PAY FOR PERFORMANCE OPPORTUNITIES

The following adjustments and clarifications to Farm Bill language should be incorporated to allow for innovative pay for performance procurement approaches to increase EROI of taxpayer dollars, and provide additional benefits to landowners and non-federal partner initiatives. These could be applied to all or a subset of existing NRCS programs and should be considered for any new NRCS programs.

- **Pay for outcomes**. This means payment is not based on reimbursement of pre-defined costs, and in some cases not including practices in contracts at all. If a portion of payment is needed before outcomes are provided, then these payments should be linked to key performance and implementation milestones, but at least 25 percent of payment should be based on the amount of quantified outcomes verified for the project.
- **Allow a portion of funding to be used for program design and implementation.** Allowing a portion of funding to support development of tools and administrate a program can increase the per-dollar effectiveness of on the ground projects, and generate more outcomes than would

investing all the funding in projects when many will under-perform in the absence of performance incentives. Invest in designing and securing pay for performance contracts, applying outcome-based metrics to estimate and verify the conservation outcomes generated by a project, and developing a programmatic adaptive management plan and performance reports.

- **Allow pay for performance contract terms to meet the specific context and goal of each region**. Pay for performance procurement strategies can utilize a range of payment terms. For example, contracts used to seed-fund mitigation projects for emerging mitigation markets require unique reimbursement terms so that federal funds are not used to subsidize mitigation. Further, full delivery contracts can attract the use of private capital to finance environmental improvements.[2] This flexibility is needed to better achieve regional goals while also using federal funds more efficiently.
- **Allow constraints to be waived for selection criteria, AGI, and total funding limits.** This will allow NRCS and partners to select the projects that deliver the highest EROI and meet other program goals which are impeded by current restrictions.
- **Allow federal or matching funds to be used for project maintenance and incentive payments over decades.** Implementing conservation practices without ongoing maintenance does not ensure the durability of conservation gains. Allowing a portion of federal funds to be spent out over decades would allow for long-term performance contracts that support long-term conservation outcomes. Maintenance funds produce cost effective environmental improvements when compared to investing in projects that are not maintained and lose conservation value, and thus significantly increase EROI. Funds may need to be able to be transferred to other federal or non-federal financial instruments in order to protect those funds from being used for other uses in the future. In addition, allow non-federal funds and commitments for long-term maintenance to count as matching funds when secured by a long-term contract that ensures funds and commitments will be delivered.
- **Require reporting of conservation outcomes, cost per unit outcome and other key program-specific metrics on a publicly accessible website.** This is will provide the transparency ensure new contracting approaches are producing cost-effective results and the feedback to support learning and adaptive management.
- **Use a competitive bidding procurement processes and selection criteria to rank projects by the cost effectiveness of the outcomes produced, not the cost of the project.** Limiting project funding to the reimbursement of costs both limits the desire of producers to participate in programs and does not necessarily result in the most cost-effective outcomes. By soliciting projects from multiple parties, selecting projects at least partially by the cost per unit of conservation, and paying only for the number of verified outcomes, federal funds are assured to flow to the most cost-effective projects and there is no risk of paying for projects that under-perform.

[2] The Pay for Success Strategies for Western States Technical Brief (http://enviroincentives.com/products/pay-success-contract-mechanisms-technical-brief/) provides a framework for determining which of several different pay for performance contract approaches is most appropriate in different context.