



## **I-95 Corridor Coalition**

# **Federal Support for Freight Infrastructure: Policy Issues & Program Design**



*Prepared by:  
Mercator Advisors*

*January 2009*

This report was produced by the I-95 Corridor Coalition. The I-95 Corridor Coalition is a partnership of state departments of transportation, regional and local transportation agencies, toll authorities, and related organizations, including public safety, port, transit and rail organizations, from Maine to Florida, with affiliate members in Canada. Additional information on the Coalition, including other project reports, can be found on the Coalition's web site at <http://www.i95coalition.org>.

---

# **Federal Support for Freight Infrastructure: Policy Issues & Program Design**

*A Briefing Paper for the I-95 Corridor Coalition*

## Executive Summary

### I. Policy Rationale for Federal Assistance

- A. Diversity of Infrastructure Types
- B. Existing Federal Programs for Freight
- C. Potential Forms of Financial Support

### II. Guiding Principles for Project Selection

### III. Federal Program Structuring: Issues & Options

- A. Role of a Special Purpose Entity
- B. Regional vs. National Bank
- C. Federal Credit vs. Revolving Loan Program
- D. Organizational Status

### IV. The National Freight Infrastructure Development Corporation (NFIDC)

- A. Governance
- B. Dedicated Revenue Sources: Formula and Discretionary
- C. Forms of Assistance:
  - 1. Making Discretionary Grants
  - 2. Funding Loans through Federal Credit
  - 3. Allocating Tax Credit Bonds and Private Activity Bonds

### V. Next Steps

Appendix A: Federal Budgetary Policy Considerations in Program Design: A Comparison of Key Features of Dodd-Hagel and Wyden-Thune

Appendix B: Role of a Nationwide Conduit Issuer of Tax Credit Bonds (e.g., Wyden-Thune TFC)

---

## **Federal Support for Freight Infrastructure: Policy Issues & Program Design**

### **Executive Summary**

The I-95 Corridor Coalition is interested in evaluating options for developing a regional or national infrastructure bank, or other multi-state entity or special assistance program, to support the selection and financing of large freight [and passenger] transportation projects. Creating a Special Purpose Entity (SPE) and providing it with dedicated resources could bring a much-needed institutional focus, especially to increasing capital investment in goods movement projects.

This briefing paper describes how establishing a new National Freight Infrastructure Development Corporation (NFIDC or Corporation) could assist the members of the Coalition and other stakeholders in advancing major freight infrastructure investments. The same entity could also be used for advancing passenger rail projects in similar fashion, although that is not the thrust of this paper.

The concept of a federally-sponsored “national infrastructure bank” to support transportation and other infrastructure investments has received considerable public attention in recent months. Governors, financiers and trade associations have urged creation of a new national program to improve project selection and resource allocation at the national level. President-elect Obama and members of his advisory team have expressed support for the concept. Several legislative proposals to establish a national entity were introduced into Congress last session. To date, however, there has been surprisingly little detail on the technical aspects of such an initiative—such as what the organization’s budgetary status would be; what types of grant, credit or tax subsidies it should offer; and how it would be funded.

*This briefing paper builds upon previous extensive research by USDOT, the Transportation Research Board and others substantiating the need for increased federal support of investment in freight infrastructure. The focus of this paper is on “fiscal architecture”—the institutional design and programmatic structure—of such an entity. Bracketed amounts appear throughout the paper indicating that these numbers are intended to be suggestive, not absolute recommendations.*

It is assumed that a national-level entity would be established by act of Congress. Although a regional entity could be sponsored by the states within the I-95 Corridor Coalition to assist projects along the Eastern Seaboard, a national-level entity would offer important advantages in terms of access to federal funding streams and U.S. Treasury financing tools. It also could select projects on a nationwide basis that

provide the highest economic return. Rather than contributing upfront capital to fund a regional “bank”, the states, together with other stakeholders, should determine their respective funding responsibilities on a project-by-project basis. In this way, their financial participation can reflect each project’s unique characteristics and distribution of benefits.

The NFIDC is envisaged as providing both discretionary grant funding and credit assistance to projects, supported by dedicated federal resources. Therefore, it is not conceived as a “bank” in the conventional sense of a self-sustaining lending institution. For this reason, the most appropriate organizational form is a wholly-owned government corporation, whose activities would be “on-budget”. It would receive approximately [\$3.5] billion per year, potentially derived both from higher rates on *existing* freight-related taxes (such as an increase on the diesel fuel tax), and *new* revenue freight-related sources (such as a surcharge on federal customs duties). Additional federal revenues of approximately [\$6.5] billion per year would be apportioned as grants to states on a formula basis for freight projects. The formula funds would be administered by the Federal Highway Administration, not the NFIDC.

The Corporation would evaluate freight-related highway, rail and intermodal terminal projects of \$[250] million or greater in capital costs and offer the following forms of assistance:

- Give **Discretionary Capital Grants** for up to 50% of capital costs of eligible projects. Total grant assistance would be [\$18] billion over 6 years.
- Provide **Direct Loans** (and possibly loan guarantees and lines of credit) under the Federal Credit Reform Act, similar to existing federal credit programs, for up to 50% of capital costs. The TIFIA, RRIF and MARAD credit programs could be transferred to NFIDC for management. Appropriated funds of up to [\$3] billion would support as much as \$[25] billion in face amount of credit assistance over 6 years.
- Allocate issuance capacity for a new **Tax Credit Bond** program of [\$20] billion and an expanded Highway and Intermodal Transfer Facility **Tax-Exempt Private Activity Bond** program of up to [\$20 billion]. Tax credit bonds are debt obligations where the Treasury effectively pays the interest to investors, making it 0% financing to the borrower. Private activity bonds are tax-exempt obligations financing a project with private participation in ongoing management or ownership. NFIDC would select projects eligible to utilize these tax-advantaged debt instruments, but it would not serve as the issuer of these bonds itself (avoiding significant federal budgetary and liability concerns).

The total amount of grants, credit support and subsidized borrowing (through tax incentives) provided to a selected project could not exceed [75%] of eligible costs.

It is contemplated that the NFIDC would use most of the federal revenues it received over six years to fund capital grants to project sponsors and to pay the subsidy cost (loan loss reserve) for the credit assistance it provided; a small portion would be retained to cover the Corporation's annual administrative expenses. NFIDC would obtain lendable funds by borrowing from the U.S. Treasury at the long-term Treasury yield (today, in the low 3% range.) For this reason, the Corporation would *not* need to issue its own securities into the credit markets. Nor would it need to be "capitalized" with a substantial balance sheet, as would a start-up, stand-alone financial institution. Using "federal credit" will allow the Corporation to offer loans at the lowest possible rate to borrowers. This approach should be particularly advantageous in light of the volatility current affecting the credit markets and the heterogeneous nature of the transportation investments to be financed.

While NFIDC itself will not issue debt into the public markets, the enabling legislation could authorize the states to establish a separate new federally-chartered *private*, non-profit corporation (the Transportation Finance Corporation, or TFC, as proposed by Wyden-Thune) to serve as a "bond bank" for the new tax credit bond program. Unlike Private Activity Bonds, tax credit bonds are still a relatively unfamiliar form of debt instrument. Presently, there are only a handful of existing federal programs at much smaller volumes than proposed for freight infrastructure.

A centralized issuer would help broaden the market for tax credit bonds by facilitating a more liquid secondary market after issuance. The TFC could be a national-level issuing conduit available to state and local tax credit bond issuers. It would issue separate series of tax credit bonds on a "pass-through" basis for each project, each with its own pledged security and own bond rating. Although the credit of each issue would be different, the TFC could establish uniform standards for structuring, act as a central information clearinghouse for investors, and aid federal policymakers in evaluating the effectiveness of this new, deep subsidy for major projects of national significance.

## I. Policy Rationale for Federal Assistance to Freight Infrastructure

The importance of efficient goods movement in the national economy has been well-documented. Recent studies by the USDOT, the Transportation Research Board, AASHTO and other respected organizations all have demonstrated the critical role that a well-functioning, multi-modal freight system comprised of trucking, rail, air cargo and marine shipping plays in supporting continued economic growth. The performance of these mostly commercial carriers in meeting increasing demand for on-time delivery of goods is inextricably linked to the condition of the infrastructure on which they operate.

But commercial prosperity is not the only public impact of a growing volume in goods shipments. Major transportation projects also result in substantial non-market spillover effects. These externalities include public safety, national security, air and water pollution, greenhouse gas emissions, energy conservation and road congestion. The presence of externalities has been a principal justification for governmental, and specifically federal, involvement in regulating and supporting what essentially is a private sector activity that uses both publicly and privately-owned surface access routes and terminals.

### A. Diversity of Infrastructure Types and Investment Approaches

Freight service encompasses a wide variety of modes—highway, rail, air and marine carriers—each with its own industry economics. Freight infrastructure assets may be classified as:

1. *Hubs*—terminals where goods are transferred, either between modes (intermodal facilities) or *within* modes (*intramodal* facilities), as with trucking distribution centers or rail yards;
2. *Connectors*--“last mile” surface links providing direct access to the hubs, frequently through densely built-up metropolitan areas; and
3. *Corridors*—longer surface routes, extending from several miles to hundreds of miles, connecting two or more hubs and often spanning multiple states.

The wide diversity of freight modes, project types, and jurisdictions has led to an equally diverse range of funding strategies, often involving some combination of user charges, public tax-supported funding, and private contributions. As a general rule, projects whose benefits are more heavily weighted towards addressing certain externalities (such as improving safety and enhancing communities) have relied to a greater degree on public, tax-supported funding. For example, a recent survey of three dozen major intermodal freight projects revealed that terminal improvement projects on average were 90 percent funded by user charges or private sector contributions, and 10 percent funded with some form of public tax-based support. The reliance on commercial charges and corporate support reflects the fact that the private business operator derives most of the benefit from a terminal facility, with only ancillary public benefits. In contrast, the surface access projects surveyed, such

as connectors and corridors, were just 37 percent user-charge or privately funded, and 63 percent publicly-funded.<sup>1</sup> In fact, only a third of the projects drew explicitly upon user charges for a portion of their funding streams. This reflects the greater emphasis on community benefits from grade separations and other similar surface access projects.

These findings suggest that any governmental initiative to encourage freight infrastructure investment should acknowledge that many projects will not be “market-based”, in the strictest sense, but reliant in varying degrees on public funding. Any policy designed to encourage investment must be flexible enough to assist both revenue- *and* non-revenue generating projects.

#### B. Existing Federal Programs for Freight

The current federal funding support for freight is diffuse and under-capitalized. Only a small portion of USDOT’s grant funding (about 2% of SAFETEA-LU authorizations) significantly targets projects that facilitate goods movement. The existing grant support is supplemented by credit support and tax incentives that may be accessed through the TIFIA, RRIF and Private Activity Bond (PAB) programs.

[see table on next page]

---

<sup>1</sup> Forthcoming chapter on “*Financial Strategies for Delivering Intermodal Freight Facilities*” being prepared for Eno Foundation, 2009.

**Table 1: Summary of USDOT Freight-Related Programs**

SAFETEA-LU Section & Title	Authorized Amt. (\$ millions)	Eligibility	Status
1301: Projects of National & Regional Significance	\$ 1,780	Variety of highway and rail “mega” projects (costing at least \$500M or 75% of state’s annual Fed. Aid—85% freight-related.	Nominally discretionary, but entirely Congressionally-earmarked to 25 projects
1302: National Corridor Infrastructure Improvement Program	1,948	Highway projects in corridors of national significance to promote economic growth and trade.	Nominally discretionary, but entirely Congressionally-earmarked to 33 projects.
1303: Coordinated Border Infrastructure	833	Variety of transportation and safety-related infrastructure and operations within 100 miles of Canada or Mexico border	Funds apportioned by formula to border states based on vehicle traffic, cargo volume and ports of entry.
1305: Truck Parking Facilities	25	Funds long-term parking areas for commercial vehicles.	I-95 Coalition has received \$5.5M grant award
1306: Freight Intermodal Distribution Pilot	30	Designated for certain inland ports and intermodal facilities (up to \$5M per project)	Nominally discretionary, but all \$30M earmarked to 6 projects.
1401: Railway Highway Crossing Program	880	Grade crossing eliminations or safety improvements (up to 90% of the cost of installing protective devices)	Formula apportionments are based on STP factors and number of grade crossings (each state gets ½% minimum).
9002: Rail Line Relocation Capital Grants	1,400	Discretionary grants to be awarded by USDOT for rail line relocation projects	An unfunded authorization; dependent on future General Fund Appropriations
<b>Subtotal: GRANTS</b>	<b>\$ 5,496</b>		
1601: Transportation Infrastructure Finance and Innovation Act (TIFIA)	Up to ~ \$6,000 (depending on subsidy estimates)	Provides loans, guarantees and lines of credit to major surface transportation projects generally costing more than \$50 million	Since 1998, credit assistance totaling \$4.8 billion has been provided to 15 projects costing \$18.6 billion.
9003: Railroad Rehabilitation & Improvement Financing Program (RRIF)	Up to \$35,000	Provides loans to freight and passenger rail infrastructure projects if borrowers pay budgetary costs (~10-15%)	Since 1998, 21 loans totaling \$748M have been originated (2% of volume cap).
11143: Highway and Intermodal Facility Private Activity Bonds	Up to \$15,000	Allows highway or rail-truck intermodal transfer facilities with private participation to access the tax-exempt bond market.	USDOT has approved \$7.4 bil. PABs for various highway projects; only 1 issue for \$589M has been sold (4% of volume cap); no intermodal..

In addition, Congress established a Railroad Track Maintenance Tax Credit program under section 245 of the American Jobs Creation Act of 2004 that was recently extended through 2009. It allows short-line (Class 2 and 3) rail carriers to claim annual tax credits for up to \$3,500 per mile for 50% of the cost of maintaining track owned or leased by them. The estimated value of the credits over 10 years is \$331 million.

There are a number of reasons why federal funding to date for freight projects has been limited:

- Most state/local planning is oriented to traditional public works, which have a broad political constituency compared with freight projects, whose direct beneficiaries may be much narrower.
- Much of the freight infrastructure (particularly freight rail) is privately-owned, and many states have legal and policy restrictions on contributing public funds to private beneficiaries.
- Projects are often intermodal in nature, and do not easily fit into existing federal program structures that are modally oriented.
- Many of the projects span multiple jurisdictions, hindering the formation of institutional entities to serve as comprehensive project sponsors and champions.
- The direct private benefits can be hard to monetize, and the spillover effects are difficult to quantify.

### C. Identifying Potential Forms of Support

In considering the obstacles to freight infrastructure investment, an important threshold distinction is whether the barrier is insufficient underlying *funding sources* (project revenues) or insufficient *access to financing* at reasonable rates and terms (leveraging tools). For projects that are economically-beneficial but not commercially self-sustaining, *Grants* are an appropriate federal policy tool for subsidizing the project's non-market benefits (externalities). *Tax Code Incentives*, such as Tax Credit Bonds and Private Activity Bonds, are an indirect way of subsidizing capital investment, and achieve some measure of market discipline in project selection through private debt and equity capital.

For projects unable to arrange financing due to capital market failure, the appropriate Federal role would be providing *Credit Support*. In the fall of 2008, the domestic and international credit markets have faced unprecedented disruption. For the first time since the Great Depression, creditworthy borrowers have been unable to obtain financing due to heightened investor and lender concerns about default risk and liquidity risk. A number of major financial intermediaries have either failed, required major infusions of taxpayer capital, or been forced to merge with stronger entities. The downgrading of most monoline bond insurers and the withdrawal of banks from providing credit enhancement have dramatically tightened credit to municipal bond issuers. Even the credibility of the rating agencies as monitors of default risk has been called into question. As a result, low investment-grade rated

borrowers have been unable to sell long-term debt, and even sound, mid-investment grade issuers are having difficulty gaining market access. For these reasons, there may be particular value in designing a federally-supported credit program to overcome thin, irregular and expensive access of borrowers to the credit markets.

In recent years, the USDOT has focused considerable energy in promoting public-private partnerships (P3)—especially long-term operating concessions—as a means of assisting state and local government project sponsors. It is important to recognize that P3 is not a revenue stream; it is a project delivery and management tool, and a potential source of financing. While P3 can add value in shifting project risks away from government and realizing operating or construction efficiencies, it is not a panacea. Projects still require reliable revenue streams in order to attract private investment capital. It should be noted that the capital sources drawn upon by the private infrastructure sector currently are facing challenges similar to those confronting municipal bond issuers.

## II. Guiding Principles for Project Selection

It is anticipated that larger “projects of national or regional significance” will be selected for grant support or credit assistance on a *discretionary* rather than *formula* basis. The focus would be on those freight infrastructure projects meeting threshold eligibility criteria that demonstrate the most favorable returns on public investment. In this manner, the federal resources would be allocated in a way designed to maximize programmatic effectiveness.

*Threshold Eligibility.* It is anticipated that the eligibility criteria will be similar to those set forth in the October 24, 2008 final rule published by the Federal Highway Administration for Projects of National and Regional Significance, although with broader eligibility and lower size threshold:

- Type of Project: Any surface transportation project eligible under title 23, including public or privately-owned rail facilities providing benefit to highway users, surface transportation infrastructure modifications to facilitate intermodal interchange, transfer and access into and out of ports and other activities eligible under title 23. [Also consider broader eligibility to capture desired freight rail projects – perhaps similar to RRIF eligibility to “acquire, improve, or rehabilitate intermodal or rail freight or passenger equipment or facilities, including track, components of track, bridges, yards, buildings, and shops and develop or establish new intermodal or railroad facilities.
- Size: For multi-state projects, the lesser of \$[250] million or [50%] of the Federal-aid apportionment of the State in which the project is located that has the largest apportionment.

Indicative freight-related projects of interest to the I-95 Coalition that might be candidates for assistance are rail chokepoints, highway bottlenecks, corridor reconstruction and various capacity improvements.

*Project Assessment.* The criteria for project selection should reflect the recommendations that the I-95 Corridor Coalition provided to FHWA regarding the evaluation of Projects of National and Regional Significance. Among the factors the Coalition urged be used as a basis for selection are:

- i. Functionality of the project within the National Transportation System;
- ii. The Condition and Performance of the project in serving high volume and high value commodity movements;
- iii. The Economic Value of the project, and its benefits to the regional and national economies;
- iv. Technical Feasibility of constructing and operating the project;
- v. Financial Feasibility, including appropriate allocation of public and private cost responsibility, and the ability to leverage the Federal investment with non-Federal contributions;
- vi. Organizational status of the project sponsor (institutional feasibility)
- vii. Evidence of Political Support from key stakeholders.

There is a series of related policy questions that any federal legislative proposal would need to address, including whether preference should be given to projects:

- involving long-term concessions with private operators or other private (as opposed to state/local) co-investment;
- backed by user charges instead of general or dedicated tax revenue streams; or
- demonstrating multi-state planning / cooperation / sponsorship vs. single-state projects.

The new program should strive to provide federal assistance in a more businesslike manner than traditional programs, in order to realize a more efficient allocation of resources. A primary purpose of establishing a separate entity to replace politically-driven with a more objective “value for money” assessment of alternative public investments. But it also is imperative that the selection procedure not be overly bureaucratic and process-intensive. Conventional federal discretionary grants such as FTA New Starts are perceived by many applicants as being too burdensome, time-consuming and unfocused. Even the TIFIA credit program has been criticized as being too cumbersome and inefficient. There is an apparent need for a more business-like and professional process for evaluating, negotiating and executing financial assistance packages for major projects.

*Role of Benefit-Cost Analysis.* A key decision for policymakers will be the role of benefit-cost analysis (BCA) in evaluating and selecting projects for assistance. While

BCA is a valid economic measurement tool, exclusive reliance on a numerical calculation to rank projects may be too rigid a criterion. For example, outgoing FTA Administrator James Simpson recently stated that he disagreed with the Administration's strict adherence to the cost-effectiveness test for transit New Starts as a basis for judging projects. In addition, there are practical considerations as to whether a new entity should rely on the applicant's analysis or perform its own. Having the BCA performed by the entity might ensure greater objectivity and uniformity, but it might result in lengthy time delays as the analysis is undertaken. There is also the question of balancing an "economic" BCA with narrower financial feasibility concerns. The BCA should measure both direct monetary and indirect "non-pecuniary" costs and benefits of an investment, and express them in today's dollar-value equivalent. A project with a high positive social return on investment may nonetheless represent a significant credit risk and entail a costly budgetary score.

To expedite assistance, eligible major projects should be automatic candidates for environmental streamlining efforts by USDOT and other relevant agencies. In addition, eligible major projects should be automatic candidates for procurement flexibility (SEP-15 style).

### **III. Federal Program Structuring: Issues & Options**

#### **A. Role of a Special Purpose Entity**

Creating a special purpose entity at the national level dedicated to aiding freight capital investment is designed to achieve several important benefits:

- *Improving Project Selection.* The SPE would have an independent board and staff allowing it to evaluate and rank projects nationwide, based on an objective assessment of their network benefits (improved freight flows, reduced congestion), rather than a formula-driven or politically-negotiated distribution of resources.
- *Aligning Mission and Resources.* The SPE would provide an organization whose institutional mission would be to advance capital investments in the freight sector, using a programmatic structure funded with dedicated revenue streams.
- *Overcoming Non-Market Costs.* The SPE could target investments in large projects of regional or national significance that, because of eligibility constraints or sheer scale, cannot be funded from existing funding sources. Federal investment would be justified by the public benefits, especially if those benefits are diffused and hard to monetize into project revenues.
- *Offering Multiple Tools & One-stop Shopping.* An SPE-based comprehensive freight-oriented program could incorporate various existing federal grant, credit and tax programs with new programs designed to overcome market

gaps, and rationalize how assistance is made available to project sponsors. Placing these resources within one shop would assist project sponsors by centralizing their availability, and would aid Congress and the Administration in reviewing program performance.

- *Accelerating Capital Investment.* Forming a centralized entity with the requisite staff expertise would be more effective in rapidly delivering financial assistance for freight projects with truly national network benefits than distributing the same dollar value of resources to fifty states (or even several regional entities).
- *Supplementing Existing Resources.* It is anticipated that the majority of federal grant funding would continue to be administered by existing USDOT agencies through formula assistance to states. A centralized entity would reinforce, not replace, current funding mechanisms by providing project-specific supplemental resources.

#### B. Regional vs. National Entity.

The federal government can play a leadership role in helping states stimulate capital formation for freight infrastructure. Establishing a special purpose entity would bring an institutional focus to what has been, to date, a loosely-related series of federal programs nested within several federal agencies of USDOT. But should the federal policy approach be to create some form of a single national-level funder—a national infrastructure bank—or rather to foster the development of various regional infrastructure banks by groups of states, such as the I-95 Corridor Coalition?

Although a regional organization sponsored by the members of the I-95 Corridor Coalition would focus on critical projects along the Eastern Seaboard, creating a federal-level, nationwide entity would offer several important advantages. First, certain regional freight investments may have nationwide implications for efficient goods movement, national security and other priorities and merit federal support. A national entity would have a wider constituency and be more likely to enjoy broad Congressional support for federal funding. Second, a national organization would achieve greater diversification and economies of scale in operations than would a series of smaller entities with a multi-state regional scope. It likely could become operational more rapidly as well. And finally, while individual states technically could use their own resources to capitalize a regional entity, it would lack access to the favorable financing provisions available to federal agencies and government corporations through the U.S. Treasury. As the State Infrastructure Bank program has demonstrated, even when an institutional vehicle is authorized, its success will depend upon the willingness of states to commit financial and staff resources to its operations.

Because freight infrastructure encompasses a wide array of modes and project types (hubs, connectors and corridors), each project will have its own set of public and

private stakeholders and its own distribution of public and private benefits affecting specific geographic areas. Given current funding limitations, it may be unrealistic to expect states to make significant monetary contributions to capitalize a regional “bank” on a blind pool basis to support major freight projects that may be hundreds or thousands of miles away.

Every project will have its own set of stakeholders and beneficiaries, and its own project-specific arrangement for allocating funding responsibility. Accordingly, while each project may have a bespoke *regional project sponsor*, a singular *national assistance provider* would be more efficient and practical—and likely more politically feasible.

Having a multi-state entity as the *project sponsor* would demonstrate important regional cooperation and commitment to a nationally significant freight investment. Congress could adopt legislation making it easier for states to enter into multi-state compacts *without* specific Congressional approval. In this way, each project could form its own multi-state sponsor and draw upon its own set of revenue streams for the non-federal share. Establishing these project-specific entities could be a useful selection feature for critical corridor improvements.

### C. Federal Credit vs. Revolving Fund

Governmental lending programs may take one of two forms: One option is capitalizing an account which would become a loan revolving fund. The entity could make an initial set of loans to projects and recycle loan repayments as received into subsequent loans. This is the model for the EPA State Revolving Funds and the State Infrastructure Banks, both of which are state programs capitalized with federal grants. To operate at a breakeven level, such a lending pool would need to charge interest at a rate sufficient to cover its cost of capital and any loan losses. If the entity’s portfolio was funded with grants from the federal government and did not need to be repaid, its cost of funds would be zero and the entity could lend at any rate it wished, as low as 0%. If, however, the entity were to go into the credit markets and issue bonds as its source of lendable funds, its lending rate would need to cover its own interest cost plus any expected losses from the portfolio.

Loan funds revolve or re-lend only as quickly as the first round of loans is repaid. Large infrastructure projects are likely to require maturities of 30 years or longer to amortize their loans. Principal repayments may be substantially back-loaded, based on projected revenues. Consequently, the fund may revolve at a very slow pace, diminishing the potential of any significant recycling for decades.

Further, revolving funds have been most successful where there is a large number of smaller, relatively homogeneous loans, such as in the housing, agriculture and water & sewer sectors. Such portfolios lend themselves to standardization, pooling and securitization. Freight infrastructure projects, as noted earlier, will be large, complicated, “one-off” projects.

Finally, Federal policy over the last 15 years has discouraged enacting new perpetual revolving funds, which have laxer budgetary controls than other forms of credit assistance.

A second option is to operate under the Federal Credit Reform Act [FCRA or “Credit Reform”], similar to the TIFIA and RRIF programs. Under Credit Reform, the U.S. Treasury funds direct loans or provides payments under loan guarantees for the governmental entity. The budgetary resources needed to cover anticipated costs of the program, known as the subsidy cost, are based on estimates of expected losses from defaults, or interest rate subsidies below the government’s own cost of funds. The subsidy cost is determined by discounting anticipated future cash flows at a rate based on the government’s borrowing rate at the time the commitment is made, to derive a present value cost. Effectively, the subsidy cost may be thought of as a fractional loan loss reserve, which must be specifically appropriated from available budgetary resources or borrower contributions.

The balance of the loan amount in excess of the subsidy cost is funded from U.S. Treasury borrowings, using “permanent indefinite borrowing authority.” Because the subsidy cost is deemed to fully compensate the government for anticipated losses/costs, the scheduled loan repayments are deemed to offset the borrowing authority. Loan repayments may not be “recycled” to make new loans, since they must be used to repay the lending agency’s Treasury borrowings. For this reason, a revolving fund concept is incompatible with Credit Reform.

As the TIFIA program has demonstrated, being able to lend at the government’s own cost of capital is a very attractive feature for project sponsors—particularly under current credit market conditions. There are at least four reasons why direct federal credit has become a preferred source of debt capital for borrowers:

- *Low cost.* The U.S. Treasury rate represents a risk-free cost of funds. As of this writing, the 30-year Treasury yield is just over 3.0%; that is nearly three percent lower than long-term single-A rated tax-exempt bonds. On a 30-year level debt service structure, each one percent increment represents present value savings of approximately 10 percent of the face amount borrowed.
- *No Liquidity Premium.* Unlike capital market loans, there is no “illiquidity” premium in terms of higher yield exacted by investors for uncertainty concerning their ability to sell the loan prior to its stated maturity. The Federal government has no such liquidity concern.
- *Prepayment Flexibility.* The Federal government requires no prepayment penalty or call protection for a borrower electing to prepay its loan at any time. Indeed, five of the original TIFIA loans have been prepaid decades before their due dates. This gives borrowers added flexibility.
- *Lower Transaction Costs.* The costs of issuance generally are lower with federal credit.

In addition to the direct benefits to borrowers, federal credit has an important internal benefit: intrinsic leveraging of federal resources: For example, the current TIFIA program has an average budgetary (subsidy) cost of [10] cents on the dollar—versus 100 cents on the dollar for an appropriated revolving fund. That means a \$1 billion loan program may only require \$100 million of budget authority. Having the entity issue its own debt to fund the grants and subsidies contemplated would never be as efficient as having that assistance funded by general Treasury borrowing (as is the case now with existing assistance program). For reasons of both funding efficiency and budgetary cost-effectiveness, Federal credit is a very powerful tool.<sup>2</sup>

A recurrent refrain in the discussion of creating a national infrastructure bank is its potential ability to bundle up a diversified portfolio of funded loans and “securitize” them as asset-backed obligations into the credit markets. This essentially was the role that Government Sponsored Enterprises (GSEs) played in the past in the housing, agriculture and student loan sectors: purchasing loans originated by local lenders and packaging them into loan pools to sell on Wall Street.

For a federal credit program, this is not an essential function, since the U.S. Treasury does not have the same liquidity needs as a GSE. However, it is conceivable that, once a large and diversified portfolio of freight infrastructure loans was originated, it could be securitized. The federal housing, agriculture and student loan programs involved the packaging of a large number of smaller, more or less homogeneous loans into pools of marketable securities. A portfolio of freight loans would be much more difficult to assemble and securitize, given the large, complex and heterogeneous nature of the projects and the lengthy “pipeline” for funding them.

If a new federal funding initiative for major projects included the provision of credit assistance, it would make sense to migrate the existing USDOT credit programs—TIFIA, RRIF and MARAD title XI—to the new entity to consolidate lending activity and staffing. A new program could build on the existing programmatic strengths going forward.

#### D. Organizational Status

A threshold question to be resolved is the SPE’s organizational status. Federally-related organizations may take a variety of forms, and go under various labels: Administration, Association, Authority, Bank, Corporation, Fund and Service, among others. The name is not determinative of its organizational standing or budgetary treatment; rather, its status is defined by the nature of its activities and the degree of federal involvement.

There are over a dozen separate federally-chartered organizations currently providing credit assistance to various sectors such as housing, agriculture, exporting and

---

<sup>2</sup> One aspect of federal credit is that it may not be extended to make or guarantee loans where the repayment stream consist of federally-appropriated revenues – the loans must be secured with non-federal revenues.



Federal Credit must be subject to federal budgetary controls to protect the U.S. Treasury. And allocating federal tax incentives to projects requires public accountability. The grant, credit and tax incentive programs all would benefit from ongoing Congressional oversight and performance review. These factors argue for structuring a national-level entity as an *on-budget wholly-owned government owned corporation*.<sup>3</sup> For purposes of this discussion, it is referred to as the National Freight Infrastructure Development Corporation (NFIDC or Corporation).

#### **IV. Federal Program Design Illustration – The National Freight Infrastructure Development Corporation (NFIDC)**

##### A. Governance Structure.

Federal legislation could authorize the establishment of the NFIDC as a government corporation domiciled in the District of Columbia. The legislation also would provide for an independent board of directors, with perhaps seven to eleven board members. Typically, the individuals are appointed by the President with the approval of the Senate for staggered board terms of perhaps four years. Board membership should be drawn from individuals with expertise in freight movement [and passenger transportation], public works construction, project and public finance and federal budgetary matters. The board will appoint an Executive Director who in turn will assemble sufficient staff to perform the responsibilities of the Corporation. The board will adopt by-laws to set forth corporate responsibilities in addition to those defined by statute in its enabling legislation.

*The NFIDC would have no debt issuance authority of its own; it would obtain capital for providing assistance to projects through a combination of dedicated revenues and Treasury loans, as set forth below.*

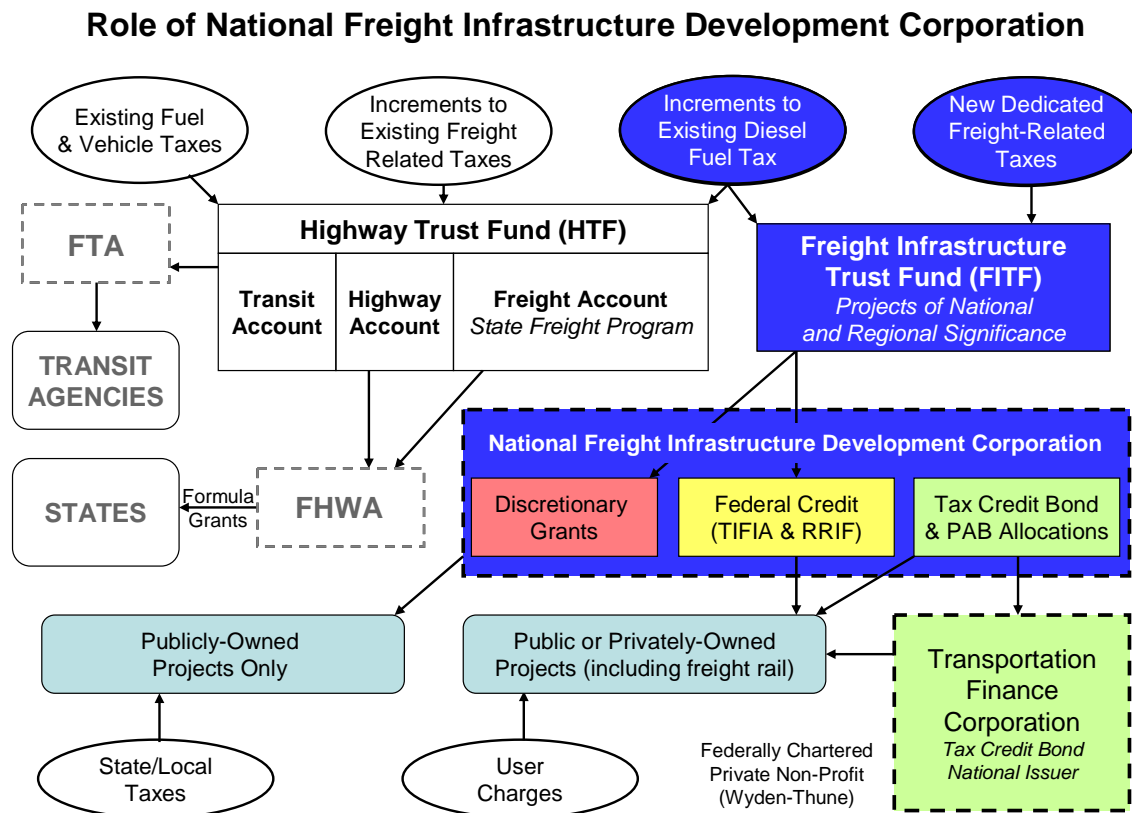
##### B. Dedicated Revenue Sources for Freight.

It is proposed that NFIDC be part of a comprehensive federal strategy to expand investment in freight infrastructure generally consistent with AASHTO's Freight Authorization Policy. Federal assistance would be divided into two categories:

- *Formula* apportionments to the States, through USDOT, using existing Highway Trust Fund revenue sources; and
- *Discretionary* grants and loans, made to advance Projects of National and Regional Significance, selected by and dispensed through the NFIDC.

---

<sup>3</sup> Other examples of wholly-owned government corporations involved in credit assistance are the Export-Import Bank, Government National Mortgage Association, Rural Telephone Bank, and Pension Benefit Guaranty Corporation



The bracketed amounts that appear below indicate that these numbers are intended to be suggestive, not absolute recommendations.

*Resources for FHWA Formula Grants.* Formula assistance to states would be administered by USDOT through the Federal Highway Administration, and because the states would identify the beneficiary projects, NFIDC would not need to be involved. Congress would authorize a state-administered freight transportation program within the Highway Trust Fund (HTF) funded at \$[18+21=39] billion over six years. Funding would be derived through dedicating some portion of existing (and/or increments to existing) freight-related tax revenue streams. Receipts would be credited to a new Freight Account within the HTF. Moneys would be apportioned annually to states on a formula basis to be determined.

*Resources for NFIDC Discretionary Grants and Credit Assistance.* Approximately [\$21] billion of revenues over the next six years would be credited to a new Freight Infrastructure Trust Fund (FITF) dedicated to assisting Projects of National and Regional Significance (PNRS). The NFIDC would use these revenues to fund its discretionary grant and credit assistance programs. The FITF would be funded through a combination of increments to existing freight-related taxes plus newly dedicated freight revenue sources. [For example, this could include a 5-cent increment to the diesel fuel tax as well as a 5% surcharge on Customs Duties in order

to generate average annual funding of \$3.5 billion, or \$21 billion over the 2010-2015 authorization period.]

### C. Forms of NFIDC Assistance.

The Corporation would provide three forms of discretionary assistance to project sponsors: Discretionary Grants, Loans/Loan Guarantees, and Issuance Allocation for Tax Credit Bonds and Private Activity Bonds. Each mechanism is described briefly below:

1. *Discretionary Grants:* Of the approximately \$21 billion anticipated that NFIDC would receive over the six-year authorization period, \$18 billion (\$3 billion/year) would be designated for capital grants. Direct grants would be limited to projects owned by a state or local government instrumentality; no privately-owned infrastructure would be eligible. Projects would be evaluated on the basis previously described, ranked in terms of their contribution to the national goods movement system. The minimum threshold size for a project would be [\$250] million. The maximum amount of grant assistance any single project could receive would be 50 percent of eligible project costs.

2. *Credit Assistance.* The balance of funds, \$3 billion, would be available to fund the subsidy cost of providing direct loans to project sponsors, or loan guarantees and lines of credit associated with project sponsor debt.<sup>4</sup> The program would be operated pursuant to Credit Reform, similar to TIFIA. Based on an assumed average credit score of 12 percent of the face amount, a par amount of \$25 billion of project debt could be supported.

It is anticipated that most project sponsors would elect to seek direct loans (today at just over 3.0 %) because of their favorable rates and greater flexibility. Like TIFIA, a borrower could arrange a loan through NFIDC on a subordinate (junior) basis for up to 33% of project costs. If the pledge were senior lien (including co-senior with taxable or tax-exempt markets senior debt), NFIDC would be prepared to loan up to [50%] of project costs.

3. *Tax Incentives.* The third element of NFIDC assistance would be allocating issuance volume limitations under two debt-related programs: Private Activity Bonds (PABs) for major highway or intermodal projects; and Tax Credit Bonds (TCB). Tax credit bonds are debt obligations where the U.S. Treasury effectively pays the interest to investors, making it 0% financing to the borrower. Private activity bonds are tax-exempt obligations financing a project with private participation in ongoing management or ownership. NFIDC would select projects eligible to utilize these tax-advantaged debt instruments, but it would not serve as the

---

<sup>4</sup> Certain national infrastructure bank proposals have called for mechanisms such as interest rate buy-downs or sinking fund contributions as forms of credit assistance, when in actuality, they are specific uses of grant awards.

issuer of these bonds itself. For both PABs and TCBs, the bonds would need to be issued through a state or local conduit issuer, and the project would need to be governmentally-owned.

Tax incentives have a budgetary cost relating to the foregone tax receipts to the U.S. Treasury (“tax expenditures”). But unlike the grant and credit budget authority, tax measures are not funded from discretionary budget resources. Instead, they are accounted for on the mandatory spending side, along with entitlements. In order to implement any tax incentive, such as extending PABs or introducing TCBs, the “paygo” budgetary rules require Congress to identify a source of offset for the scored cost. Budgetary accounting conventions only recognize the first ten years of tax expenditures. For this reason, a 30-year bond is only “scored” or charged for the tax losses in the first decade after enactment of the bill.<sup>5</sup>

To facilitate the issuance of TCBs, it would be desirable to have a centralized nationwide entity available to project sponsors. The NFIDC could not be an issuer without raising serious federal policy concerns about contingent liability to the Treasury from the government corporation’s debt issuances. In addition, as a federal entity, its borrowing and spending of proceeds would be scored as budget authority and outlays – making such an approach unnecessarily costly and inefficient. Appendix B contains a description about how Congress could authorize the formation of a *private* non-profit corporation—the Transportation Finance Corporation or TFC--organized by the states to serve as a national issuing conduit for TCBs. The TFC would be completely independent of the NFIDC, with its own board of directors and governance structure.

*Summary.* The NFIDC would be empowered to assist freight rail infrastructure projects in three ways: by awarding grants, by funding direct loans, and by allocating tax-advantaged debt issuance authority to project sponsors. These three financing tools—contributed capital, credit assistance, and tax incentives—should enable the Corporation to aid freight projects in different ways, depending on the nature of the project, its revenue profile and its ownership structure. Governmentally-owned projects would be eligible to apply for discretionary grants. Both governmentally- and privately-owned projects would be eligible to apply for direct loans at the U.S. Treasury rate and to apply for volume cap allocations for issuing either tax-exempt bonds or tax credit bonds.

---

<sup>5</sup> Investment tax credits are another form of tax incentive, but they aren’t as well-suited to freight infrastructure as tax credit bonds for several reasons. They are illiquid, non-transferable investments, dependent on the project owner’s tax appetite. As an equity-based investment, they require a higher yield to investors than do bonds and are more difficult to market. And typically, the company, not the federal government, determines which capital investments do make.

## **V. Next Steps**

The NFIDC could bring much-needed focus and resources to stimulating capital investment in freight infrastructure.

As other federal financing initiatives such as TIFIA have demonstrated, conceptual proposals gain added traction with policy makers when there are tangible candidate projects referenced. If the I-95 Corridor Coalition wished to advance the NFIDC proposal, it could prepare a fact sheet showing how the financing and funding tools proposed for the Corporation could benefit specific freight infrastructure investments along the Eastern Seaboard.

Once the members have agreed upon a programmatic design, its features could be inserted into one of the existing infrastructure bank proposals such as Dodd-Hagel or Wyden-Thune. With a detailed concept and specific legislative language in hand, the proposal could be shared with various members of the Obama transition team as well as Congressional members and their staff for consideration.

There are several potential legislative vehicles that the proposal could be attached to: The anticipated Fiscal Stimulus bill, which appears likely to contain a significant infrastructure component (realistically the NFIDC would take a year to organize, although much of the program design work could be undertaken immediately so that it could become operational by year-end 2009); the federal surface transportation reauthorization bill; and a new standalone bill that could be introduced, similar to the Dodd-Hagel, Wyden-Thune and DeLauro bills thus far. Any tax code measure (such as one authorizing tax credit bonds) would need to be attached to one of the tax writing committees' proposals.

## Appendix A: Federal Budgetary Policy Considerations & Program Design: A Comparison of Dodd-Hagel and Wyden-Thune

The assessed “score” (budgetary charge) and other policy implications of a proposal often determine its legislative fate. Included in this assessment is the nature of the entity providing the assistance. Federal entities, whether part of cabinet-level departments, independent agencies or government corporations, have direct and obvious effects on federal spending. Even Government Sponsored Enterprises (GSEs) and other “off-budget” entities can raise significant questions about direct or indirect federal liabilities. This was emphatically demonstrated over the summer with the federal rescue of Fannie Mae and Freddie Mac. In addition, the issue of who controls or influences the allocation of resources will be important to many federal policy makers.

The evaluation of these issues is generally straightforward for existing agencies and programs. Proposals involving the creation of new entities and/or the use of new forms of assistance involve judgment calls by the budgetary scorekeepers in the legislative and executive branches—the Congressional Budget Office and the Office of Management and the Budget.

The scorekeepers assess whether an entity’s activities should be scored in the federal budget based on a series of organizational factors summarized below. If an organization is deemed “on-budget,” its spending and borrowing activities are treated as federal outlays. The key factors are:

- Ownership of the organization;
- Its source of capitalization;
- Who selects its board of directors;
- The ongoing degree of control by Congress or the Executive Branch; and
- How the proceeds are used.

It is important to note that these are more in the nature of general guidelines than immutable rules, for there is considerable variance in the actual treatment of particular organizations.

Two recent infrastructure bank proposals provide a useful contrast on these points: : The National Infrastructure Bank Act of 2007 (S. 1926, “Dodd-Hagel”) and the Build America Bonds Act of 2007 (S. 2021 “Wyden-Thune”). Dodd-Hagel proposes establishing the National Infrastructure Bank (NIB) to advance transportation projects through the issuance of \$60 billion of bonds. Wyden-Thune proposes establishing the Transportation Finance Corporation (TFC) for similar purposes, through the issuance of up to \$50 billion of bonds. A point-by-point comparison of these two bills appears at the end of this Appendix.

While both nominally entail using a new financing entity to raise tens of billions of dollars for infrastructure investment, they do so with very different federal policy implications. Some of these differences, highlighted below, have helped inform the proposal for a National Freight Infrastructure Development Corporation.:

**Measures of Federal vs. Non-Federal Status: NIB vs. TFC**

Program Feature	Federal	Non-Federal
Ownership of Entity	<p>-- The entity undertaking the financing program is part of the federal government or owned by the government (a federal agency or government corporation).                      -- The federal government has a controlling interest (majority of voting stock) or is the primary beneficiary of the entity's activities (monetary or otherwise).</p> <p>NIB <input checked="" type="checkbox"/></p>	<p>-- The entity is a state or local governmental unit or a subdivision thereof.                      -- The entity is privately owned and the federal government is not the primary beneficiary of the entity's activities.</p> <p>TFC <input checked="" type="checkbox"/></p>
Source of Capital	<p>-- The federal government is the primary source of capital for the entity / program.</p> <p>NIB <input checked="" type="checkbox"/></p>	<p>-- The entity / program derives most of its capital from non-federal sources (capital markets debt, private equity, state / local contributions).                      * <i>[Note that the proposed appropriation of future customs duties to help secure the TFC's repayment of tax credit bond principal complicates the TFC status.]</i></p> <p>TFC ?</p>
Selection of Managers	<p>-- The President and/or the Congress determine the majority of the entity's directors or managers.</p> <p>NIB <input checked="" type="checkbox"/></p>	<p>-- The entity's directors or managers are not selected by the federal government.</p> <p>TFC <input checked="" type="checkbox"/></p>
Degree of Control	<p>-- The federal government exerts significant control over the entity's policies and activities (whether through the decisions of government-appointed directors or the provision of federal financial assistance).</p> <p>NIB <input checked="" type="checkbox"/></p>	<p>-- The entity has independence in operations and program implementation.</p> <p>TFC <input checked="" type="checkbox"/></p>

Use of Proceeds	<p>-- The program results in spending oriented towards inherently federal purposes (it predominantly benefits the federal government).</p>	<p>-- Program spending is for non-federal purposes.  <i>* [Note that some observers have questioned whether the proposed minimum allocation of TFC grants would enable scorekeepers to claim that the proceeds effectively would supplement the federal-aid highway program, thus complicating the TFC status.]</i></p> <p>NIB <input checked="" type="checkbox"/> TFC ?</p>
-----------------	--	--

A comparison of the NIB and TFC proposals to the five key organizational factors highlights their differences. The NIB would be *treated as a federal entity* (based on four of the factors) with its borrowing and spending scored against the federal budget. The TFC *appears to be largely non-federal*, as intended by its sponsors, although its status with regard to “source of capital” and “use of proceeds” may be uncertain. Those questions would have to be resolved in order for the TFC to avoid being scored with federal spending when it distributes proceeds of its tax credit bonds.

#### Type of Entity

- The NIB likely would be a federal entity (independent agency or government corporation).
- The TFC likely would be a non-federal entity (two or more state infrastructure banks would be authorized to establish it).

#### Federal Borrowing

- The NIB would result in federal borrowing. It would fund its activities by issuing federal debt obligations backed by the full faith and credit of the U.S. This would require “borrowing authority”, a form of federal budget authority.
- The TFC would not result in federal borrowing. It would be authorized to issue tax credit bonds to fund its activities. This would be similar to the state/local issuance of tax-exempt governmental or private activity bonds under current law.

#### Federal Spending

- The NIB would provide grants and other assistance resulting in federal outlays that would be scored as spending in the federal “discretionary” budget, just as occurs with the provision of federal grants and credit support by the USDOT.
- The TFC would provide bond proceeds issued by a non-federal entity, intended to avoid being recorded as direct federal outlays. However, the tax credits on the bonds it issues would result in tax expenditures (revenue losses to the Treasury) that would be scored against the “mandatory” side of the federal budget, as described below.

### Control of Resource Allocation

- The NIB would manage a federal discretionary program, meaning it would select projects and provide assistance according to statutory parameters. Immediate control of the federal resources would reside with the Board of Directors, which would be appointed by the President (with Senate confirmation) and hire staff to execute its policies. The Congress would exercise control through the NIB's statutory parameters and would have explicit oversight responsibilities for this federal organization.
- The TFC would be established by two or more state-level entities (state infrastructure banks as currently drafted) and would manage a national-level program for grant assistance by means of both formula allocations and discretionary selections. The TFC would be authorized as a non-federal entity acting on behalf of state and local project sponsors (essentially a financing conduit), with the chartering states responsible for organizational details. The federal executive branch would have no control over the activities of the TFC. The Congress would exercise control through statutory provisions guiding eligible investments and funding allocations and would have some oversight responsibilities (mostly through mandated reports).

### Budgetary Treatment

Both the NIB and TFC contemplate issuing billions of debt each year. The federal budgetary impacts of bonding mechanisms like the NIB and the TFC depend on whether the initiative is deemed to be a federal government program. It is clear that a program like the NIB would be considered governmental, resulting in federal borrowing and spending (i.e., up to \$60 billion would be scored as budget authority and outlays in the federal budget). Alternatively, the issuance of bonds and the spending of proceeds by a non-federal entity like the TFC should have no direct budget impact. But to the extent the program draws upon a tax code incentive such as tax credit bonds, the cost of the tax subsidy (foregone federal tax revenues) is reflected in the federal budget each year as “tax expenditures.”

The sponsors of the Build America Bonds legislation have purposely structured the TFC to be a non-federal entity in order to minimize its cost relative to the NIB. If the TFC were viewed as a federal entity, like the NIB, its grants to states and localities would be treated as federal spending. Thus, \$50 billion of capital grants would be scored with \$50 billion of budget authority and outlays. In addition, the annual tax expenditures associated with the tax credits would be scored against the federal budget. The sponsors have estimated this revenue loss at about \$2 billion per year. If the TFC were viewed as a non-federal entity, however, only the annual tax expenditures would be scored.

*Even in the current legislative environment where Congress has quickly approved hundreds of billions of dollars in emergency spending to shore up financial institutions and stimulate the economy, the larger the budgetary footprint of a proposal, the more difficult it is for Congress to enact it.*

## Comparison of Dodd-Hagel & Wyden-Thune Infrastructure Finance Proposals

Proposal	National Infrastructure Bank Act of 2007 [S. 1926, “Dodd-Hagel”]	Build America Bonds Act of 2007 (Transportation Finance Corporation) [S. 2021, “Wyden-Thune”]
Eligible Projects for Assistance:	<p>“Projects of regional or national significance” with a potential federal commitment of at least \$75 million:</p> <ul style="list-style-type: none"> <li>•Mass transit</li> <li>•Public housing</li> <li>•Highways &amp; bridges</li> <li>•Drinking water &amp; wastewater systems</li> </ul> <p>[Federal requirements would apply to assisted projects.]</p>	<ul style="list-style-type: none"> <li>•Mass transit</li> <li>•Highways &amp; bridges</li> <li>•Railroads</li> <li>•Ports</li> <li>•Inland waterways</li> </ul> <p>[Federal requirements would apply to assisted projects.]</p>
Forms of Assistance:	<ul style="list-style-type: none"> <li>•Grants (direct subsidies)</li> <li>•Loans</li> <li>•Guarantees</li> </ul>	<ul style="list-style-type: none"> <li>•Grants</li> <li>•</li> </ul>
New Special Purpose Entity:	<p><b>The National Infrastructure Bank (NIB)</b>, a new independent <u>federal agency or corporation</u>.</p> <p>The NIB would be managed by a Board of Directors with five members appointed by the President, with the advice and consent of the Senate (loosely modeled after the Federal Deposit Insurance Corporation).</p>	<p><b>The Transportation Finance Corporation, (TFC)</b> a <u>non-federal</u> multi-state entity consisting of two or more State Infrastructure Banks.</p> <p>Not specified (would be determined by the non-federal entity)</p>
Proposal	National Infrastructure Bank Act of 2007 [S. 1926, “Dodd-Hagel”]	Build America Bonds Act of 2007 (Transportation Finance Corporation) [S. 2021, “Wyden-Thune”]

<p>Duties of Entity:</p>	<p>The NIB would:</p> <ul style="list-style-type: none"> <li>•Receive, review and rate financing applications from public sponsors for eligible projects.</li> <li>•Select projects to be assisted and determine financing packages.</li> <li>•Fund its project assistance by issuing federal debt obligations</li> </ul>	<p>The TFC would:</p> <ul style="list-style-type: none"> <li>•Select projects and allocate grants (subject to the state minimum allocation noted below).</li> <li>•Fund its project assistance by issuing non-federal debt obligations.</li> <li>•Establish and manage a Trust Account in order to secure the repayment of bond principal (with bond proceeds, investment earnings, and federal appropriations based on some level of customs duties necessary to retire the bonds)</li> </ul>
<p>Project Selection:</p>	<p>According to various specified criteria, including an assessment of:</p> <ul style="list-style-type: none"> <li>•Regional or national significance</li> <li>•Promotion of economic growth</li> <li>•Infrastructure / mobility improvement</li> <li>•Environmental benefits</li> <li>•Urban land use (smart growth)</li> <li>•Project benefits vs. costs</li> <li>•Extent of private participation</li> <li>•Modal and geographic balance</li> <li>•</li> </ul>	<p>Project selection criteria are not specified; however, the TFC must meet the following provisions in allocating assistance:</p> <ul style="list-style-type: none"> <li>•Each state must receive a minimum allocation of at least 1% of the total.</li> <li>•Each state is required to update its “accepted construction technologies” to the satisfaction of the USDOT Secretary in order to receive an allocation</li> </ul>

Proposal	National Infrastructure Bank Act of 2007 [S. 1926, “Dodd-Hagel”]	Build America Bonds Act of 2007 (Transportation Finance Corporation) [S. 2021, “Wyden-Thune”]
Cost Sharing	Determined by the NIB.	Up to 80% (or even higher, based on the state “sliding scale” for federal-aid highway assistance).
Capital Raising	<p>The NIB would issue special <u>federal</u> debt obligations in the form of tax credit bonds (backed by the full faith and credit of the U.S.)</p> <ul style="list-style-type: none"> <li>• Bonding limit of <u>\$60 billion</u>.</li> <li>• Bond maturity of greater than 30 years (up to the useful life of the qualified project).</li> <li>• Other terms and conditions determined by the NIB, with Treasury consultation. Up to 1% of bond proceeds could be used for NIB administration. Bonds could be general purpose bonds – presumably resulting in a general obligation of the U.S. to repay bond principal if no dedicated repayment sources.</li> </ul> <p>Bonds could be project-based infrastructure bonds – presumably with project-based revenue streams that could be used to repay the bond principal  <i>[Technical amendments to the Internal Revenue Code necessary for the authorization of tax credit bonds have not been specified.]</i></p>	<p>The TFC would issue <u>non-federal</u> debt obligations on behalf of the states in the form of tax credit bonds – “Build America Bonds” (these would not be federal obligations or result in any federal liabilities).</p> <ul style="list-style-type: none"> <li>• Bonding limit of <u>\$50 billion</u> (over 6 years)</li> <li>• Bond maturity of up to but not exceeding 30 years</li> </ul> <p><i>[Various technical provisions to be added to the Internal Revenue Code are spelled out.]</i></p>

## Appendix B: Role of a Nationwide Conduit Issuer of Tax Credit Bonds

Tax Credit Bonds are a new type of debt instrument for sponsors of transportation infrastructure projects, with different tax attributes than tax-exempt bonds. TCBs are “taxable” tax credit bonds, meaning the investor must recognize as taxable income the annual tax credit received. In contrast to the tax-exempt municipal market, which is largely a “retail” market of individual investors, the taxable corporate bond market is dominated by institutional investors, has many fewer issuers, and is characterized by much larger average issue sizes.

Since tax credit bonds are taxable instruments, issuers will need to access a different investor base than for conventional municipal bonds. There are several relatively small tax credit bond programs currently in existence, but most involve much smaller issue volume than contemplated for freight infrastructure. The Qualified Zone Academy Bond (QZAB) program was initiated in 1998 at \$400 million nationwide annually for two years, and has been renewed since then with bipartisan support. To date, \$4.8 billion of bonds for public school modernization have been authorized, and it is estimated that approximately two-thirds of the volume cap has been utilized thus far. The more recent Clean Renewable Energy Bond (CREB) program, was first authorized in 2005 in the amount of \$800 million, and was renewed by Congress in 2008. Under both programs, the loan amounts have averaged under [\$5] million.

Freight infrastructure project sponsors are likely to face relatively high transaction costs in issuing tax credit bonds, and their issues will have only limited liquidity in the secondary (post-issuance) market. These factors may make it difficult for the capital markets to efficiently absorb the proposed \$25 billion of “new product” over the next several years.

### Role of a Conduit

Project sponsors may benefit from having the option of reaching this new investor base by issuing their Tax Credit Bonds through a centralized nationwide conduit. Essentially, the conduit would acquire the debt of the project sponsor through issuing securities backed solely by the repayment stream the project sponsor pledged to secure its individual loan. The conduit itself would have little or no assets to secure the debt; it would be issuing its bonds on a strictly “pass-through” basis.

Using a centralized issuing entity is designed to achieve the following benefits:

- Influence the drafting of regulations by the NFIDC for implementing the tax credit bond program;

- Homogenize to a certain degree the appearance of the debt to broaden investor acceptance.
- Achieve scale economies in transaction fees;
- Establish uniform standards for how the issues are structured and how tax treatment is disclosed to investors;
- Act as a central information clearinghouse for investors and for federal policymakers who will want to evaluate the programmatic effectiveness of this new tax subsidy.

Just such a nationwide issuing conduit has been proposed—the Transportation Finance Corporation (TFC)—as a conduit issuer for up to \$50 billion of tax credit bonds in S. 2021, the Build America Bonds Act of 2007, sponsored by Senator Ronald Wyden (D-OR.) and John Thune (R-S.D.).

In order to avoid certain of the federal policy “trip-wires” relating to implied federal liability, the TFC would need to be completely separate from the NFIDC. The NFIDC would allocate tax credit bond volume cap to project sponsors, but the debt would be issued either directly by state and local governments or on their behalf through the TFC. Legislative language could be patterned after an organization included as part of the Telecommunications Act of 1996 to assist schools with acquiring and financing technology improvements: The National Education Technology Funding Corporation, or Eddie Tech. Eddie Tech was intended to serve as an issuing conduit for borrowings by local school districts. While dormant to date, Eddie Tech’s organizational status as a federally-chartered private non-profit corporation could guide the establishment of the TFC. It would be available to state/local government entities if they did not wish to directly issue tax credit bonds to investors.