

4 March 2016

Practice Group:
Public Policy and
Law

A “FAIR” Chance for Infrastructure P3s in Obama Administration’s Final Budget Request

President Unveils Financing America’s Infrastructure Renewal Proposal

By Judson M. Greif, Steve A. Martinko, Peter V. Nelson

In his final State of the Union address, President Obama acknowledged that “because it’s an election season, expectations for what we will achieve this year are low.” However, the Administration’s Fiscal Year 2017 budget request includes an innovative infrastructure finance proposal that may gain traction in the 114th Congress — a new federal credit program within the Department of the Treasury to support public-private partnerships, known as the Financing America’s Infrastructure Renewal (“FAIR”) program. The FAIR program could open up an attractive new financing opportunity for critical transportation, water, energy, broadband, and social sector infrastructure.

The program would “provide direct loans to U.S. infrastructure projects developed through public-private partnerships that meet applicable environmental and labor standards,” in the amount of approximately \$15 billion over 10 years. The program would require Congressional authorization, which Treasury Secretary Jack Lew called for in testimony to the Senate Finance Committee on February 10, stating that the program represents one of several “small steps to level the playing field for private investment in public infrastructure projects.”

According to the Administration, if authorized by Congress, the FAIR program would seek to “reduce the financing cost gap between P3s and traditional procurement.” This gap is often the differentiating factor in the decision to use tax exempt debt versus other private market financing tools. While the price differential between leveraging private financing and exclusively using tax exempt debt may be a relatively small amount, even small differences can add to the cost of capital and be a deterrent to the use of alternative financing methods. Reducing this delta would make public-private partnerships a more attractive alternative for project managers at the city and municipal level, and is one of the chief objectives of the FAIR program, which aims to “level the playing field for P3s and encourage the public sector—including state and local governments—to evaluate the merits of P3s for a given project,” according to the Administration’s budget request.

The budget request underscores that such partnerships can and should be valuable tools for local project sponsors by accelerating delivery of complex projects and transferring the risks of construction and operations to private contractors with expertise in those functions.

Building on the Foundation of Successful Infrastructure Programs

Proponents of the FAIR program in the Administration, Congress, and the stakeholder community could model the FAIR program after similar subsidized federal loan programs at the U.S. Department of Transportation (the TIFIA program) and the Environmental Protection Agency (the WIFIA program). Like these existing programs, the FAIR initiative would provide

A “FAIR” Chance for Infrastructure P3s in Obama Administration’s Final Budget Request

low interest loans at or slightly above Treasury rates to organizations financing infrastructure projects. The estimated \$15 billion in direct loans provided by the program would allow sponsors to leverage significantly more capital for eligible projects. The President’s budget request indicates that these would include infrastructure projects in the transportation, water, energy, and broadband sectors as well as “certain social infrastructure” – essentially creating a catch-all for low interest infrastructure financing for a wide variety of project categories.

The variation from the TIFIA and WIFIA programs will be in how the loans are insured against the risk of default. In both of the “-IFIA” programs, interest rates on most loans are priced at equivalent-term U.S. Treasury security rates. However, the interest rate on loans issued by the FAIR program would be priced slightly higher to include the cost of insuring the loan against credit risk (e.g., defaults, recoveries, and prepayments) associated with each project. This would allow the program to attain a zero estimated subsidy cost and operate without adding to the federal budget deficit.

Many details remain to be seen on how the FAIR program might operate, including the amount of the maximum project allocation for a FAIR loan. Other issues include what type of capital could be used alongside a FAIR loan and how much private capital would be required to participate. As an example, policymakers will need to determine the proportion of total project costs eligible for financing through FAIR loans. Additionally, regardless of what that number is, what of the remaining percentage would be required to be private capital as compared to tax-exempt municipal debt? These will be important details to resolve in order to determine the efficiency of the program and may be addressed in the authorizing legislation for the program if Congress pursues it.

A Promising Initiative for the 114th Congress

The FAIR program is a positive addition to this year’s budget proposal. It will require an act of Congress to authorize and establish the program; however, the minimal cost associated with the program alongside the benefits potentially gained from bringing in more capital to infrastructure investment should seem like a winning proposition. Stakeholders with an interest in infrastructure finance should begin to engage relevant policymakers in discussions about how to take the FAIR program from concept to reality. Even if the clock runs out on the Obama Administration, cost-effective infrastructure investment is a policy idea that will always be able to find a constituency in Congress.

Authors:

Judson M. Greif

Judson.Greif@klgates.com
+1. 202.778.9283

Steve A. Martinko

Stephen.Martinko@klgates.com
+1. 202.778.9320

Peter V. Nelson

Peter.Nelson@klgates.com
+1.202.778.9358

A “FAIR” Chance for Infrastructure P3s in Obama Administration’s Final Budget Request

K&L GATES

Anchorage Austin Beijing Berlin Boston Brisbane Brussels Charleston Charlotte Chicago Dallas Doha Dubai Fort Worth Frankfurt Harrisburg Hong Kong Houston London Los Angeles Melbourne Miami Milan Newark New York Orange County Palo Alto Paris Perth Pittsburgh Portland Raleigh Research Triangle Park San Diego San Francisco São Paulo Seattle Seoul Shanghai Singapore Spokane Sydney Taipei Tokyo Warsaw Washington, D.C. Wilmington

K&L Gates comprises more than 2,000 lawyers globally who practice in fully integrated offices located on five continents. The firm represents leading multinational corporations, growth and middle-market companies, capital markets participants and entrepreneurs in every major industry group as well as public sector entities, educational institutions, philanthropic organizations and individuals. For more information about K&L Gates or its locations, practices and registrations, visit www.klgates.com.

This publication is for informational purposes and does not contain or convey legal advice. The information herein should not be used or relied upon in regard to any particular facts or circumstances without first consulting a lawyer.

©2016 K&L Gates LLP. All Rights Reserved.