An Infrastructure *Rethink*

It's time to consolidate existing efforts. An infrastructure bank?

By Mansoor Dailami

The Trump administration has a historic opportunity to fix America's aging infrastructure. This is not a rhetorical statement, but rather a statement of economic imperative that the administration must seize the moment given the uniquely favorable environment.

Not only is there broad bipartisan support in Congress for higher federal spending on infrastructure, but there are very favorable underlying macroeconomic conditions—low funding costs, strong demand from institutional investors for infrastructure assets, and potentially large productivity gains. There are two official plans in broad outline on the table: one by the Trump administration and the other by Senate Democrats. Both plans call for $1 trillion in new investment in public infrastructure over a decade, with a key difference in the funding. The Senate plan would fund the additional investment with direct federal spending. The Trump proposal envisions a combination of federal and private funding wherein the federal government contributes $137 billion in tax credits for projects that generate their own revenue streams.

In the historical context of U.S. infrastructure legislation, the administration's current proposal is politically attractive but falls short of reforming the national infrastructure financing system, with its complex fiscal federalism, fragmented markets across states, and a tradition of using federal tax policy to subsidize infrastructure spending by state and localities. And here is the nub of the problem. In negotiating with the Congress, success is more likely with a strong, comprehensive reform package with projected positive spillovers for the tax reform agenda, growth, and job creation than with a transactional approach. Engagement with Congress should be defined not so much in terms

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In 2007, an eight-lane, steel truss arch bridge that carried Interstate 35W across the Mississippi River in Minneapolis, Minnesota, suddenly collapsed, killing thirteen people and injuring 145. The American Society of Civil Engineers calculates that from 2016 to 2025, each U.S. household will lose $3,400 each year in disposable income due to infrastructure deficiencies.

of fiscal space but in terms of the nation's infrastructure investment and financing needs.

The United States stands out in the world as a country with a highly decentralized infrastructure investment and financing structure. Public spending on transport, water, and social infrastructure is largely the domain of state and local governments that are close to end users and well-equipped to weigh the relevant costs and benefits of different investment projects. Of the total $416 billion in public spending on transport, water, and social infrastructure in 2014, for instance, state and local governments accounted for $320 billion, and the federal government accounted for almost one-quarter ($90 billion). State and local governments also have the option of using private debt financing, through the well-developed municipal bond market, to manage their budgets over time. But what seems to have been largely overlooked is the high value of infrastructure assets owned by state and local governments—almost $4 trillion of the nation's highways and bridges, airports, seaports, and transit structures (2013 estimates of the Bureau of Transportation Statistics).

Federal support for public infrastructure is a catalyst. The nexus giving the federal government political control over infrastructure, either through funding or regulation, arises from certain distinctive features of infrastructure, including its macroeconomic consequences, growth and job linkages, and network and centralizing characteristics. Roads, railways, electric grids, and telecommunication facilities offer the important function of integrating citizens into a national space in both a physical and psychological sense. On these grounds, the role of the federal government in infrastructure becomes inevitable, and the key question centers on the best financing mechanism to ensure adequate and efficient investment. As a share of total federal spending, outlays on public infrastructure have remained roughly constant at 2.7 percent during the past thirty years, but have declined in relation to the size of the economy when measured in inflation-adjusted real terms.

With budgetary resources limited, solutions for improving America's infrastructure financing system must be sought through novel approaches.

In its financier role, the federal government provides credit assistance, through an array of programs, to state and local governments to encourage investment in infrastructure, particularly in transport and water infrastructure. The Highway Trust Fund, Transportation Infrastructure Finance and Innovation Act, Railroad Rehabilitation and Improvement Financing program, and the Water Infrastructure Finance and Innovation Act have been designed to provide alternative public financing options in the form of grants, loans, and guarantees, and with different eligibility criteria and conditions. In particular the Highway Trust Fund, with its "user pays" revenue source and unique budgetary treatment, is a creative, albeit unsustainable, financing structure for federal investment in transportation and transit systems. Since the Highway Trust Fund cannot, by law, borrow or incur negative balances, its solvency has always depended on Congress to bail it out through legislative patchwork and fiscal maneuvering. Congress has authorized the transfer of about $143 billion since 2008, mostly from the Treasury's general fund, to maintain a positive balance in the Highway Trust Fund. Even with the latest federal funding authorization under the Fixing America's Surface Transportation (FAST) Act, the Congressional Budget Office projects that the Highway Trust Fund's revenues will be insufficient to meet its obligations by 2021.

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With budgetary resources limited, solutions for improving America's infrastructure financing system must be sought through novel approaches to legislation and federal funding commitments. On the legislative front, it must be recognized that the existing infrastructure legislative process in the United States, with separate committees for transportation, water, energy, and communications, limits the scope for comprehensive action. Yet technological advances, which have increased the potential for integration of service delivery across infrastructure sectors, are pushing for a more comprehensive and all-sector approach.

Regarding federal funding commitments, it makes imminent sense to consolidate the multiple federal infrastructure programs into a single program. The idea can be seen as building on long-standing proposals to create a federal infrastructure bank (including a proposal by President Obama in his 2013 budget). A federal infrastructure bank could ensure financial stability and enhance opportunities for viable public-private partnerships at the state and local level. Pooling existing programs under one mega structure would offer the advantages of greater transparency, administrative efficiency, and comparative evaluation of projects across transport and water infrastructure areas. With sufficiently large seed capital and a dedicated revenue stream (dedicated taxes, fees, and user charges), a federal infrastructure bank would be insulated from the larger budgetary politics of taxation and fiscal deficit reduction. One proposal for raising the required large sum of capital for a federal infrastructure bank is to use a one-time tax on repatriated corporate earnings. Taxed at a rate of 10 percent, these earnings would generate about $200 billion, which would go a long way to inspire confidence in federal funding commitments. The idea of using this tax revenue to pay for long-term infrastructure spending has attracted wide support, including from the Community Development and Infrastructure Bipartisan Tax Working Group.

One upshot of the idea behind a federal infrastructure bank is to bring a new focus to stimulate public-private partnerships and help to draw institutional capital towards infrastructure projects at the time when the Trump administration is expected to deliver major tax and regulatory reforms. It is almost ironic that the United States lags other advanced countries in infrastructure privatization and asset management. In the United Kingdom, for example, according to a recent report by PricewaterhouseCoopers, about 56 percent of the United Kingdom's water assets and all of its major airports, together with most ports and passenger rail rolling stocks, now reside with private financing vehicles owned by a variety of foreign and domestic pension plans, unlisted infrastructure funds, and sovereign wealth funds.

The United States has all the necessary capital market and institutional ingredients to become a leader in the public-private partnership market, pushing the global frontier toward an asset market approach to infrastructure finance. As sectors such as telecommunications and electricity are privately owned and operated, the scope for privatization and public-private partnerships is confined to transportation, water utilities, and wastewater infrastructure, which are authorized by state and local public-private partnership legislation. As of now, thirty-four states and the District of Columbia have enacted transportation public-private partnerships by statute, with a number of projects reaching financial close, paving the way for other states to follow. With states driving the public-private partnership market, federal efforts could focus on leveling the playing field for private and public investment through aligning of tax incentives, and promoting greater understanding and harmonization of the intricacies of project finance deals and procurement rules that currently vary from state to state. While the public policy issues of intergenerational equity, access, and affordability justify the use of tax revenues to fulfill infrastructure needs in the minds of many policymakers, the nature of how the tax system redirects resources to infrastructure should be reviewed afresh in conjunction with the tax reform agenda the Trump administration has outlined.

As for private infrastructure—largely, electricity and communications—the fundamental challenge is establishing a regulatory structure to promote adequate investment in the face of rapid technological change, while adapting to the fair pricing, reliable supply, and universal access objectives typically pursued in public infrastructure. Here, there is much to be learned from experiences in countries with both centralized (United Kingdom and France) and federalist (Germany and Canada) governments, as well as from the United States' own history of electricity utility regulation and restructuring going back to 1882. ◆

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