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OPINION: INFRASTRUCTURE IN THE US – OPEN FOR BUSINESS?

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The Trump administration has talked big about its plans to encourage investment in US infrastructure. Christopher Mann examines whether what has been revealed of the Trump infra plan so far goes far enough.

Despite being the largest economy in the world and having vast wealth at its disposal, the United States is regularly given low marks for infrastructure when compared with other developed countries. It seems unlikely, but the so-called infrastructure gap seen in so many countries is often most striking in the US. With the much-heralded Trump Infrastructure Plan due to be released next week, members of the Global Infrastructure Investor Association (GIIA), the body that represents the leading infra investors in the world, are watching with interest.

Notwithstanding the US's reputation as a free market-oriented economy, there has historically been relatively little private ownership or operation of US infrastructure (other than in energy and telecommunications). Instead, infrastructure has largely been in the hands of states, municipalities and public infrastructure authorities, which built much of the country's infrastructure in the 1960s and 1970s. Because many governmental authorities lack the political support to charge users what the infrastructure costs to build and maintain, and because they often lack construction and operational expertise, they have tended to underinvest in infrastructure.

There is bipartisan agreement that the US infrastructure needs can no longer be ignored. A document was leaked in January that purported to be a draft of the Trump Administration's statement of principles regarding a reform package to encourage new investment in infrastructure.

That draft contained a number of elements of the reforms that have been discussed since the Presidential election and provides at least the kernel of a number of key reforms. That being said, much was missing from the draft, including a statement of the overall magnitude of the Federal spending package that the Administration hopes to leverage to encourage state, municipal and private expenditure. The overall US spending level referred to in the President's State of the Union address last month was USD 1.5trn. If the Administration's frequent references to USD 200bn as the size of the overall Federal infrastructure spending package are coupled with the USD 1.5trn aggregate figure, it implies total state, municipal and private expenditure of USD 1.3 trn, a very tall order. There also have been statements that cuts from existing Federal infrastructure programs would pay for the new Federal spending. So the overall Federal and other spending levels, and the sources of revenue, remain important open questions. But overall, the draft appears to be an encouraging start.

GIIA members - pension funds, sovereign wealth funds and infrastructure funds - are looking for opportunities to deploy large sums of capital in the development, refurbishment, expansion and operation of infrastructure. Investors perceive US infrastructure assets as relatively safe investments, in some cases with revenues that mimic real GDP growth or inflation trends. Those features make infrastructure particularly attractive to pension funds and sovereign wealth funds, who are looking for assets whose growth and risk profile are well aligned with these funds' liabilities. With the right reforms to make it easier for such investors to find attractive assets, the private sector, while not providing a panacea, could provide a significant amount of the needed infrastructure investment. Six examples of potential reforms, some of which the leaked draft appears to contemplate, follow.

First, federal subsidies could be used to incentivize states, municipalities and the private sector to build infrastructure, or to transfer control of existing infrastructure through the grant of long-term concessions to private developers, operators and investors for value, making available to states and municipalities capital to build other infrastructure (so-called asset recycling, as practiced in Australia). The leaked document and public pronouncements by the Administration suggest that although the Federal government may provide a subsidy for worthwhile projects, it is not going to go out of its way to encourage such private investment over state and municipal investment, treating all such expenditure the same for purposes of receiving Federal subsidies. What will be more important in the Federal subsidy approval process is how much leverage any project applying for Federal subsidies will be able to achieve. In simpler terms, how many dollars of state, municipal or private investment in a particular project will each dollar of Federal subsidy granted to that project generate?

Second, the leaked document appears to suggest that the Administration will be expanding the availability of tax-exempt private activity bonds. Expanding the scope of PABs would incentivize private investment by reducing the cost of capital. Relatedly, the Administration could propose tax legislation to allow existing tax-exempt financing to remain in place, subject to the contractual terms of the bonds themselves, even if the public entity puts an existing asset financed by such debt in the hands of a private operator, in order to save the huge transaction costs associated with refinancing one type of tax-exempt financing with another. This appears to be under consideration by the Administration.

Third, the Federal government could facilitate private retail investment in infrastructure assets by creating an infrastructure investment trust regime similar to existing real estate investment trusts (REITs), the tax-advantaged vehicles that allow individuals to invest in the US real estate market.

Fourth, infrastructure investments could be excluded from the scope of the Foreign Investment in Real Property Tax Act (FIRPTA), which would eliminate the withholding tax on dispositions by foreign investors in any infrastructure assets that currently attract withholding under the law. This is currently a disincentive for some foreign investors to invest in certain types of US infrastructure assets.

Fifth, the Airport Privatization Pilot Program could be expanded to generate access to private capital for airport improvement and development. A number of features of the APPP restrict the attractiveness of the program, including a limit on the number of major airports that can be privatized, as well as a number of hurdles with regard to obtaining airline approval and spending proceeds on any development other than at the airport. The leaked document did not mention any reform along these lines, but many commentators and investors feel that this is among the lowest-hanging fruit in the US infrastructure space, since there are numerous examples of highly successful private operation of airports around the world.

Finally, a significant barrier to investment in infrastructure is the many layers of overlapping governmental agency oversight and the attendant delays associated with having a project reviewed by multiple agencies even within the Federal government. Streamlining the permitting process for infrastructure projects could significantly reduce the regulatory burden and encourage investment. The Administration has talked about such reforms, but there was little evidence in the leaked document that this is a focus, unless permitting reform will be rolled out separately.

The leaked document is only an indication, and perhaps an unreliable one at that, of the shape that the Administration’s proposal may take. The Congressional legislative process is a road with many twists and turns, so it is hard to predict whether the US will manage to adopt a viable infrastructure policy, much less what the shape of that policy may be. What is clear is that the United States is in desperate need of significant infrastructure investment, and with the right reforms and incentives, private investors and operators, including in particular those from outside the US, can play a key role in providing much of this needed investment

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