[Bond Case Briefs]

Municipal Finance Law Since 1971

[Is It Time for an Infrastructure Garage Sale?]

Australia has had success with 'asset recycling.' Maybe turning old into new could work here too.

The Trump administration's proposed federal budget calls for spending $200 billion over 10 years to "incentivize" infrastructure investment by state and local governments. One key to the strategy is reportedly "asset recycling" — selling or leasing infrastructure assets to the private sector and using the proceeds to pay for upgrades, maintenance and new infrastructure. If the administration is indeed embracing this reinvestment mechanism, it deserves our serious consideration.

Asset recycling was developed by the Australian government in 2014. It may have hit the Trump administration's radar screen because Australia's 2016 budget demonstrated that $5 billion in federal funding incentives had stimulated more than $20 billion in infrastructure investments through asset recycling. It also attracted institutional investors by creating project pipelines, the lack of which has long impeded the development of a U.S. infrastructure market. Top Trump administration officials and advisers — including Vice President Mike Pence, Transportation Secretary Elaine Chao, National Economic Council Director Gary Cohn, and Steven Roth and Richard LeFrak, co-chairs of the President's Infrastructure Advisory Committee — have been championing the concept.

Asset recycling also involves another key to the Trump administration's trillion-dollar infrastructure strategy: the engagement of the private sector through public-private partnerships. P3s have received mixed reviews worldwide, and P3 activity in the United States has consistently trailed most countries. To move the debate on P3s forward in Australia, the government of Prime Minister Tony Abbott introduced the concept of asset recycling. Officials reasoned that tapping into a source of funding for needed infrastructure that would not cost taxpayers or add public debt might have the potential to overcome reservations about P3s.

To encourage Australian states and territories to mine their balance sheets for assets that could be divested, the Abbott government offered to contribute 15 percent of the value from the proceeds of divested assets to new infrastructure projects being financed with the proceeds from divested assets. The states and territories had a two-year window to identify the assets to be sold or leased and reach an agreement with the federal government.

Some jurisdictions jumped at the opportunity. New South Wales, for example, netted $3 billion from port leases to a consortium of Australian pension funds and a government-owned investment fund, then used the proceeds to improve roads and transit facilities. Tasmania sold an airport to fund transportation, agricultural water storage and irrigation projects.

Could what worked in Australia — essentially a garage sale of government-owned infrastructure — work in the United States? Maybe, but we've got some big challenges. In addition to the reluctance of local officials to give up control of infrastructure, current tax law provides powerful disincentives to the selling or leasing of assets. Assets that are sold or leased must not only repay associated tax-exempt debt, but state and local governments would also have to finance any new debt that is incurred on a more expensive, taxable basis.

Those challenges aren't insurmountable, as Indiana has shown. In 2006, the state leased the Indiana Toll Road, netting $3.5 billion after repaying $300 million of tax-exempt debt. The state put the proceeds into its infrastructure fund, which has since financed other transportation assets without taking on any additional debt or imposing tax increases.

Estimates of the potential value to be realized in the U.S. through recycling of existing revenue-generating assets — including not only toll roads but also ports, airports, bridges, water systems and parking facilities — exceed $1 trillion. And these estimates do not include the value of providing a reliable source of funding for infrastructure projects requiring "availability payments," the disbursements to concession-holders based on project or performance milestones.

As with other approaches to selling or leasing public assets to the private sector, any plan involving asset recycling will need much discussion to address risks. How do we guard against assets being sold on the cheap? How can we protect the public from potential misuse of market power by new private owners tempted to boost profits by increasing user charges? Other issues span the need to ensure that adequate regulatory frameworks govern divested assets to the task of assessing the impact of political pressure on market competitiveness. Not trivial issues.

Just as traditional public-private partnerships are not a silver-bullet solution to infrastructure financing, nor is asset recycling. Distinguishing assets most suited for recycling from those that are not will be tough. Resource-strapped governments will be hard-pressed to develop comprehensive asset inventories and master lifecycle management practices. And public pensions could be put under additional pressure to buy assets that don't fit into their investment strategies.

But it may be worth the work required. A federally driven asset-recycling program could help state and local governments access capital — without incurring debt or raising taxes — to build a new generation of infrastructure assets. More importantly, it would signal that the U.S. infrastructure market is open for business.

GOVERNING.COM

BY JILL EICHER | JUNE 1, 2017