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Brookings Stadium Study Draws Criticisms.

WASHINGTON – A Brookings Institution study claiming professional sports stadiums built or renovated with tax-exempt bonds during the last 16 years have cost the federal government $3.7 billion has drawn some criticism from a sports consultant and municipal market participants.

The 28-page study – Tax-Exempt Municipal Bonds and the Financing of Professional Sports Stadiums – recommends that tax-exempt financing be prohibited or limited for professional sports stadiums.

The study, authored by Brookings economists Ted Gayer and Austin Drukker, as well as researcher Alexander Gold, focuses on professional football, baseball, basketball and hockey stadiums built, significantly renovated, or under construction since 2000. Of the 45 stadiums that fit this description, 36 were funded, at least in part, by tax-exempt bonds.

The total principal amount of the tax-exempt bonds used for the stadiums was $13.0 billion, according to the study.

The authors found the federal subsidies to issuers totaled $3.2 billion, based on interest rate spreads between tax-exempt and taxable bonds, at present value using a 3% discount rate and 2014 dollars. They said the federal government suffered additional revenue losses of $500 million due the "windfall tax break[s]" from the bonds for high-income earners, also assuming a 3% discount rate and 2014 dollars.

The authors claim there are no studies that provide evidence that such stadiums benefit local economies.

"The evidence for these spillover gains is weak," they said. "Academic studies consistently find no discernible positive relationship between sports facility construction and local economic development, income growth or job creation."

But Bob Boland, with Boland Sports Practice who is also executive-in-residence and director, Master of Sports Administration and MBA/MSA dual-degree programs at Ohio University, suggested the study is flawed because it's impossible to paint sports facilities with a broad brush. Stadiums should instead be examined on a case-by-case basis, he said.

Boland said the Brookings study fails to take into account the economic development that has occurred in areas surrounding some professional sports stadiums.

He cited as an example the Verizon Center sports and entertainment arena used by the National Basketball Association's Wizards and the National Hockey League's Capitals that revitalized the Gallery Place and Chinatown areas of D.C. with many new restaurants and retail stores.

In Indianapolis, the Lucas Oil Stadium used by the National Football League's Colts and the Bankers Life Fieldhouse used by the NBA's Pacers have spurred economic development in that city's downtown area. Also, the new Yankee Stadium in New York City supported a neighborhood in the south Bronx that was starting to deteriorate, he said.

Jessica Giroux, general counsel and managing director of federal regulatory policy at Bond Dealers of America said the report ignores some of the benefits munis provide to states and localities.

"One of the most important aspects of tax-exempt bonds is that state and local governments have the ability to prioritize which projects to spend their revenue and tax dollars on without having to go through the federal process," she said. "The report ignores this aspect of tax-exempt financing and also misses the point that the true beneficiaries of the tax exemption, which are the local taxpayers who benefit from the financed projects and reduced borrowing costs associated with the usage of tax-exempt bonds to finance necessary infrastructure projects."

George Friedlander, managing director, Municipal Macro Policy and Strategy at Citigroup, Inc., said the study authors note the federal government can't control what projects get done. "They're calling that an evil, but state and local governments would call that a benefit."

Because state and local governments are spending their own money, they are more likely to finance good, he said.

Friedlander, who stressed he doesn't have a view on tax-exempt financing of stadiums, said that in his view the study is flawed in making the case for eliminating or limiting tax exemption.

"One of the things they do wrong," he said, is that they base their findings in part on the interest rate spreads between munis and corporates.

"Everyone else in the entire world, including [the Joint Committee on Taxation] has done it on a ratio basis," he said. They compare muni bond yields as a percentage of corporate bond yields.

He said that in his view the Brookings researchers should not have merely compared Moody's Investors Service's muni and corporate indices. "That doesn't tell you what a muni yield would have to be if it were taxable," he said.

The researchers, in addition to using a ratio, should have figured in at least three other factors to get an "apples-to-apples comparison," he said.

First, he said, the authors should have realized that the corporate bonds in the corporate index are typically a very large size, extremely liquid and show narrow bid/offer spreads. In contrast, the munis in the muni index, tend to be small and less liquid, with larger bid/offer spreads.

Second, "the call right has to be priced in," he said. The study looks at 20-year or longer munis and corporates. Corporates typically have "make whole calls," which discourage issuers from calling them. Munis, in contrast, have 10-year call dates, and issuers often benefit from calling the bonds.

Finally, there are more stringent disclosure requirements for corporate bonds. Investors would want a little extra yield for munis, which don't have as stringent disclosure requirements.

"In an apples-to-apples comparison the ratio would be about 71% for large issuers and 68% for small issuers," showing munis are "vastly more efficient than what [Brookings] is showing," Friedlander said. A smaller ratio means that a larger part of the benefit is going to issuers not investors, he said.

The study recommends that tax-exempt financing be prohibited or limited for professional sports stadiums.

Bonds can be eliminated, the authors said, by removing the so-called "private use test" for stadium financings, as proposed by President Obama in recent budget proposals.

“The simplest and most direct way to address this inefficient federal subsidy would be to eliminate the private payment test for sports stadiums,” the study’s authors said. Stadiums would never be able to meet the private use test, they said.

“An alternative approach would limit the federal tax subsidy by classifying stadium bonds as qualified private activity bonds, which would make them subject to a state-wide volume cap, place additional restrictions on their use, and allow financing of the bonds through taxes directed at the beneficiaries of the stadiums,” the study said.

Currently these state volume caps equal $100 per capita or $302.88 million, whichever is greater, for each state and the District of Columbia.

According to the study, for the first half of the twentieth century, local professional sports franchises funded the construction of most stadiums, it said. The Revenue and Expenditure Control Act of 1958 restricted the projects involving private parties that could be financed with tax-exempt bonds. Under that law, bonds would be taxable if more than 25% of the proceeds were used by a private party and more than 25% of the debt was paid for or secured by a private party. But the law exempted sports stadiums from those restrictions.

The Tax Reform Act of 1986 eliminated sports stadiums from being exempt from the private use and payment tests, while also reducing those tests to 10% from 25%. But this backfired, according to the study. To be eligible for tax-exempt financing, stadium bond issues had to be structured so that no more than 10% of their debt was used or secured by private sports franchises.

“This sets up a kind of matching incentive, an ‘artificial financing structure’ whereby federal tax exemption is granted if the state or local government is willing to finance at least 90% of the debt service for the bonds,” the study said. “Additionally, since this 90% of financing cannot come even indirectly from private activity if tax exemption is to be maintained, the state or local government cannot rely on stadium generated revenue, such as a tax on entry tickets to the stadium or event, or even rent collected from the team as tenants.”

The Tax Reform Act of 1986 “effectively requires that, in order to receive the federal subsidy, a state or local government must finance the bulk of the stadium, and it must rely on tax revenue unrelated to the stadium for the financing, such as general sales taxes, property taxes, income taxes, lotteries, or taxes on alcohol or cigarettes,” the study said.

The Bond Buyer

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September 14, 2016