

## **3 Ways State & Local Governments Can Fund Infrastructure Projects**

While all states have different laws and regulations, here's a look at how Pennsylvania has used alternative methods to fund infrastructure projects

**William P. Conaboy, Jr.** *Counsel, Public Finance* | [william.conaboy@bipc.com](mailto:william.conaboy@bipc.com) | 215.665.5364

**Matthew T. Fine** *Advisor, Government Relations* | [matt.fine@bipc.com](mailto:matt.fine@bipc.com) | 717.237.4864

**Andrew J. Giorgione** *Shareholder, Government Relations* | [andrew.giorgione@bipc.com](mailto:andrew.giorgione@bipc.com) | 717.237.4863

**Kenneth R. Luttinger** *Shareholder, Public Finance* | [kenneth.luttinger@bipc.com](mailto:kenneth.luttinger@bipc.com) | 412.392.2165

**Thomas J. Madigan** *Shareholder, Chair of Construction Practice Group* | [thomas.madigan@bipc.com](mailto:thomas.madigan@bipc.com) | 412.562.8485

**Jason P. Wrona** *Shareholder, Real Estate* | [jason.wrona@bipc.com](mailto:jason.wrona@bipc.com) | 412.562.3920

Of all the components of President Trump's proposed infrastructure plan, the one aspect that's received the most attention is how significant a role state, local, and private entities would have to play in funding projects. As currently outlined, states, municipalities, and private companies will be responsible for footing 80 percent of the funding for infrastructure improvements, as direct federal funding will be limited to 20 percent of any individual project's costs. In addition, unless the final bill drastically departs from the proposed plan, the availability of even these reduced federal dollars will be dependent on state and local government's ability to attract private financing and/or devise ways for their infrastructure to generate revenue to help pay for itself.

Though there is still plenty of debate to come in Congress that will almost certainly alter the President's initial proposal, it appears unlikely that any final infrastructure bill will include substantial federal funding commitments. Thus, whatever form the final legislation takes, it will very likely include measures intended to incentivize state, local, and private investment in infrastructure.

**In anticipation of the increased reliance on state, local, and private funding, it's worth taking a look at how one state's procurement laws, the Commonwealth of Pennsylvania, may provide a framework for how to enable private investment in infrastructure projects.**

## Public and Private Partnerships for Transportation Act

The private financing, construction, and operation of revenue-generating public assets is the most obvious avenue for filling the funding gap for new infrastructure. In order to truly raise new funds, the public asset must generate a revenue stream sufficient to provide a return on investment to the private entity. Tolls, user fees, and utility rates are the most obvious way to generate revenue from a public asset.

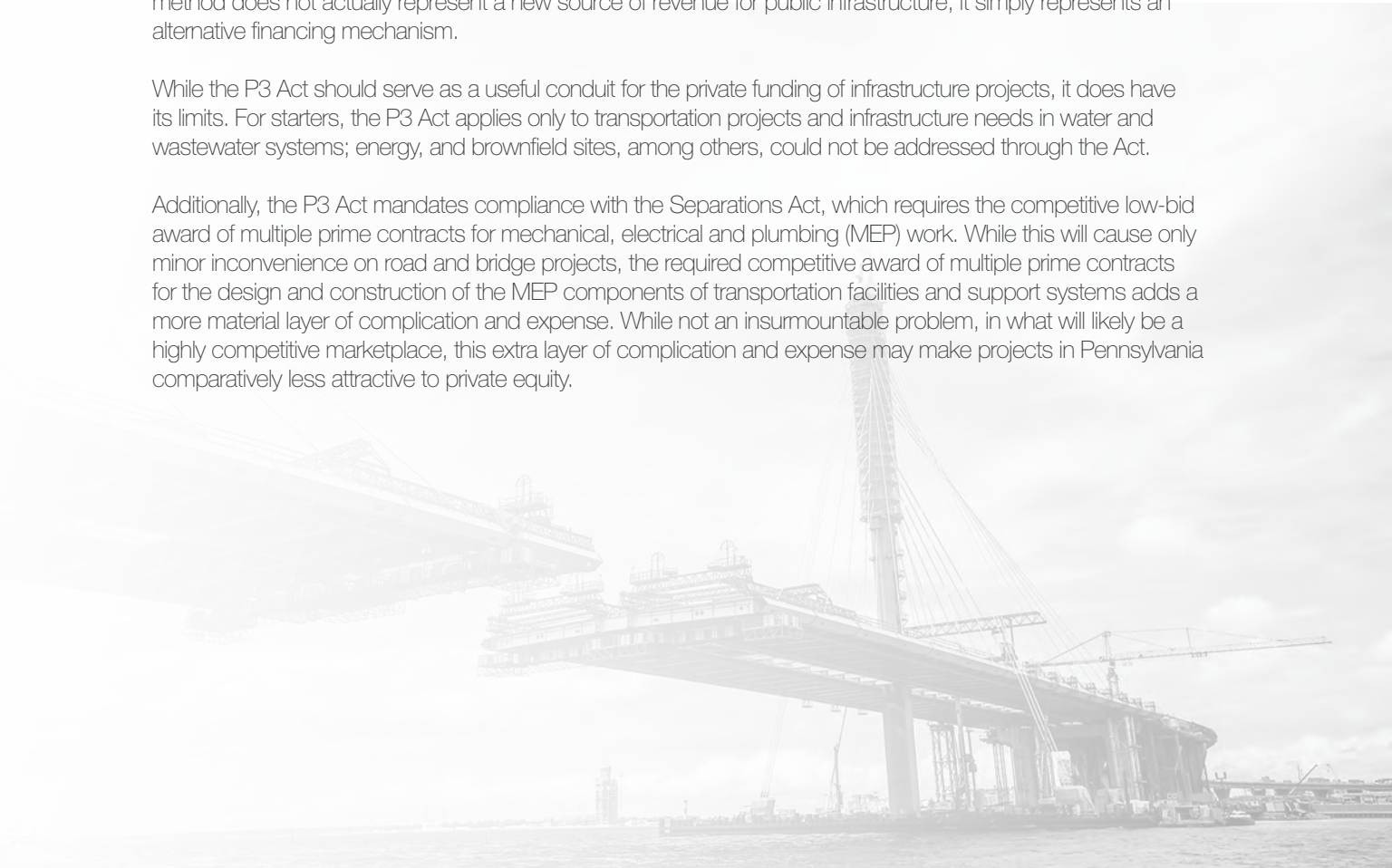
The most likely method for private funding of public infrastructure in Pennsylvania is Act 88 of 2012, known as the Public and Private Partnerships for Transportation Act or the P3 Act. The P3 Act authorizes public-private partnerships (P3s) for transportation projects, which include bridges and roads, multimodal facilities, airports, terminals and ports, and associated facilities and structures. The P3 Act authorizes a two-step, best-value award process, starting with technical submissions, followed by the creation of a “short-list” of proposers who are invited to submit price proposals. Contracts are then awarded based on a best-value analysis, which allows for consideration of factors other than price.

The P3 Act allows significant relief from the strict competitive bidding requirements of the Commonwealth Procurement Code, and allows for the use of finance-design-build-operate-maintain agreements — the most common method of procurement for P3 projects.

The process set forth in the P3 Act was used in the completion of two major projects in Pennsylvania — the Rapid Bridge Replacement Project (RBR), which bundled the replacement of 558 structurally deficient bridges into a single design-build-operate-maintain contract, and the CNG Fueling Stations Project (CNG), which involved a single contract for the design, construction, and operation of 29 compressed natural gas fueling stations at public transit agency sites across the state. Significantly, however, neither project utilized tolling or similar user fees to generate revenue to repay the private financing. Instead, both used “availability” payments, which pay for the upfront financing through a series of payments over an extended period of around 20 to 25 years. While the amount of the payments are tied to the availability of the asset (i.e., the payment is reduced if the asset is unavailable due to maintenance and repairs), it still relies on public financing (bonds or taxes) of the payment stream. Thus, this method does not actually represent a new source of revenue for public infrastructure, it simply represents an alternative financing mechanism.

While the P3 Act should serve as a useful conduit for the private funding of infrastructure projects, it does have its limits. For starters, the P3 Act applies only to transportation projects and infrastructure needs in water and wastewater systems; energy, and brownfield sites, among others, could not be addressed through the Act.

Additionally, the P3 Act mandates compliance with the Separations Act, which requires the competitive low-bid award of multiple prime contracts for mechanical, electrical and plumbing (MEP) work. While this will cause only minor inconvenience on road and bridge projects, the required competitive award of multiple prime contracts for the design and construction of the MEP components of transportation facilities and support systems adds a more material layer of complication and expense. While not an insurmountable problem, in what will likely be a highly competitive marketplace, this extra layer of complication and expense may make projects in Pennsylvania comparatively less attractive to private equity.



## Asset Recycling

Another approach to generating revenue to help fund new projects is “asset recycling.” “Recycling” simply refers to the sale or lease of an asset to raise funds to apply to the construction of a new asset or the repair or improvement on an existing asset (which may or may not be revenue-generating assets) without incurring new debt. With the asset recycling approach, which is also frequently referred to as asset “monetization,” the government often receives an upfront cash payment and the private entity takes over operation and maintenance costs associated with the monetized asset and collects the revenue stream generated from it. With a leasing agreement, the government maintains ownership of the property, and at the end of the lease period can either resume operation of the asset or negotiate a new lease and operation and maintenance agreement.

One of the biggest issues with asset recycling is that the private operator has the option – and often explicitly promises in its bid or proposal – to increase rates and fees, which could upset officials and voters alike. In Chicago, for example, the city leased its street parking meters to a private operator, which led to significant increases in parking fees and the loss of \$974 million in revenue for the city over the term of the 75-year lease.

The Chicago parking monetization is an extreme and cautionary example of why government needs to carefully consider the rate increases that often come with asset recycling transactions. In contrast to the Chicago parking monetization, many government asset monetizations welcome stable and predictable rate increases in exchange for lower up-front proceeds. Scranton, Pennsylvania, for example, leased its parking assets to a non-profit entity and sold its sewer assets to a public for-profit operator. Both transactions included fee and rate increases that were less than what the government-operated parking and sewer operators could have offered. And, in both the Scranton parking and sewer transactions, officials there made careful decisions to receive lower up-front proceeds in exchange for lower and longer term rates and fees.

However, complicating matters further, governments must first identify which assets it would want to consider recycling — not an easy task. Officials must collect comprehensive information regarding revenue generation and life-cycle costs in order to determine the fair market value of the asset, which requires assembling expertise in the legal and financial fields with experience in the sale and/or lease of public assets. Especially careful analysis must go into the potential sale or lease of an asset where the up-front proceeds generated from the monetization will fall short of fully funding the identified infrastructure needs, meaning other sources of funding would still need to be identified.

## Governmental Funding Programs and Mechanisms

The funding gap created by the reduced direct federal spend will likely require the creative and flexible use of multiple funding tools. There will not be a one size fits all solution and many projects may require a multi-faceted funding strategy.

To this end, there are a number of existing governmental funding programs and mechanisms that should be explored as potential components of capital stacks to cover funding shortfalls for infrastructure projects. For instance, the Commonwealth’s Redevelopment Assistance Capital Program (“RACP”), which is a highly competitive grant program administered by the Office of the Budget, has been a source of grant funds for infrastructure projects in many Pennsylvania municipalities. RACP proceeds are dedicated to the acquisition and construction of regional economic, cultural, civic, recreational, and historical improvement projects, have a regional or multi-jurisdictional impact, and generate substantial increases or maintain current levels of employment, tax revenues, or other measures of economic activity. Examples of RACP funded infrastructure projects include water and sewer infrastructure, transportation infrastructure, and governmental buildings.

Another program that could be tapped for an infrastructure project is the Multimodal Transportation Fund, administered by the Commonwealth Financing Authority (the “CFA”). This competitive program awards grants for the development, rehabilitation and enhancement of transportation assets, improvements to the streetscape such as lighting and sidewalks, pedestrian safety projects, connectivity of transportation assets, and transit-oriented development. Grants are available for projects with a total cost of more than \$100,000 and may be made in an amount up to \$3 million. This is clearly a program that should be considered as a resource for an infrastructure project.

The Pennsylvania Department of Transportation administers a similarly named competitive program – the Multimodal Grant Program – which provides grants for projects which coordinate local land use with transportation assets to enhance existing communities; projects related to streetscapes, lighting, sidewalk enhancement, and pedestrian safety; projects improving connectivity or utilization of existing transportation assets; and projects related to transit-oriented development.

Finally, to the extent infrastructure projects are expected to generate private real estate development, a tax increment financing (“TIF”) should be considered. A tax increment financing can be used to capture the incremental real estate taxes generated by private development spurred by an infrastructure project to secure a private financing. There are additional, subtle mechanisms that can be used to further secure a TIF, the applicability of which needs to be discussed with counsel. Multi-modal transportation facilities are a type of project that is ripe for consideration of a TIF, given the private development often associated with them.

**All of these funding programs and mechanisms are complex, nuanced, deadline-driven and require guidance by trained professionals experienced in evaluating whether a proposed infrastructure project qualifies.**



**Learn more about our insights on Trump’s Infrastructure Plan at [BIPC.com](https://www.bipc.com)**