SPECIAL FEATURE

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US stimulus package has something for everyone

Washington is hardly a hub for capital markets, yet the flurry of activity there will profoundly impact how transport assets are financed. Barry Parker reports

In mid-February, US President Barack Obama signed into law the much discussed economic stimulus bill, officially the American Recovery and Reinvestment Act of 2009 (ARRA), or Public Law (PL) 111-5, ushering in the largest single economic stimulus programme in US history.

Among transport modes, rail has made clear advances; other modes receive what amounts to a supplemental appropriation of federal money in additional to the annual budget cycle for mainly existing projects. The ARRA is split between USD463 billion of direct government investment and USD325 billion of benefits that take the form of tax-based incentives. Included in the tax portion are incentives for businesses to invest in new equipment.

Driving transport spending

The tax side of the ARRA has the potential to have a positive impact on transport spending. In a recent investor conference call by US flag tanker owner OSG America LP, Myles Itkin, the company chief executive officer (CEO) and chief financial officer (CFO) of the parent company, was asked to comment on how the company might mitigate its financing burden.

OSG America, structured as a master limited partnership, is in dispute with the builder of six articulated tank barges (ATBs) - used in the refined oil products sector - and two tugboats. As OSG America reorganises its building programme, the company is also evaluating its financial alternatives.

In Itkin's answer, he detailed ways that Overseas Shipholding Group (OSG), the general partner of OSG America, might acquire vessels and charter the same ships to the partnership. However, the second half of Itkin's answer was most revealing: "We in turn could, of course, enter into certain tax leases if that proved to be attractive, particularly with certain of the benefits coming out under the stimulus plan, but all of that has to be evaluated in the overall context of tax shield."

The benefits referred to by Itkin centre on tax-related provisions of the stimulus package worth an estimated USD5 billion, according to budget analysts, that would extend "bonus depreciation" benefits into 2009 and, in certain cases, into 2010. This provision - which applies to aircraft used in US airspace as well as shipping assets used in US waters and railcars - allows a business to gain a large tax write-off by depreciating an additional 50 per cent of the cost of the asset during the year that an asset comes into service.

Edward H Kammerer, a partner in the Providence, Rhode Island, office of New England law firm Hinckley, Allen & Snyder, with a practice concentrating on business aviation, explains: "Simply stated, bonus depreciation is faster depreciation, not more depreciation." Kammerer tells Jane's: "US-based commercial and charter aircraft are clearly eligible for bonus depreciation. In fact, there are special rules for 'transportation property', which grant benefits to airlines beyond the benefits extended to users of other collateral types." He adds: "Bonus depreciation is available for aircraft manufactured both within and outside the US."

Barges and vessels - along with tugboats and also railcars - are typically written down, for tax purposes, over 10 years. Tim Wallace, CEO of Trinity Industries, a barge and railcar builder, told investors just prior to passage of the ARRA: "We are optimistic that bonus depreciation for equipment purchases within the stimulus bill will benefit our customers and could prompt some orders for barges."

The explanation of the new rules, as provided by the Equipment Leasing and Finance Association (ELFA) offers that "if only USD2 million of a USD30 million ship was paid out to a vendor in 2009, and the remainder is paid out in 2010, only a USD1 million (50 per cent of USD2 million) bonus depreciation will be allowed on the ship's cost", even though it might not be placed in service until 2010.

In the case of OSG America, three ATBs are set for delivery in 2009, two in 2010 and one in 2011. Previously announced plans call for the vessels to be built by OSG and then 'dropped down' to the partnership, but careful scrutiny of the tax implications will probably dictate the path forward.

Matthew K Rose, CEO of Burlington Northern Sante Fe (BNSF), one of the large US Class 1 railroads, comments on a similar 2008 bonus depreciation measure: "BNSF took full advantage of the last bonus depreciation provision Congress passed, making purchases that it otherwise would not have made for the duration of the policy." Rose also pushed for an investment tax credit for railroads investing in their own right-of-way, the Expansion Investment Tax Incentive, which did not feature in the ARRA.

Throughout the month leading to passage of PL 111-5, which coincided with Obama's first weeks in office, there was considerable political debate about the efficacy of tax incentives - of which bonus depreciation is one of many - in comparison to actual spending. Law firm Holland & Knight, which recently hosted a seminar appropriately titled 'Follow the Money', said that the US government's preference, as it spends money, will be on "infrastructure projects that can be started and completed quickly and maximise job creation".

The major spending components of the bill aimed specifically at transportation consist of USD27.5 billion for highway construction; USD8.4 billion for grants to mass transit; USD4.6 billion for the US Army Corps of Engineers, which handles inland waterway and harbour maintenance; USD1.3 billion for Amtrak maintenance; USD8 billion for high-speed rail initiatives; and USD1.1 billion for airport improvements under the Airport Improvement Plan (AIP) administered by the US Federal Aviation Administration (FAA).

Other transport-related provisions of the bill include USD200 million for modernisation of the US air traffic control (ATC) system, and USD100 million for investment in small shipyards. The Fiscal Year 2010 (FY10) federal budget, now being debated in the US Congress, will provide additional spending for many of the items covered in the ARRA.

On track for rail revolution

The efforts to promote passenger rail are perhaps the most ground-breaking. Indeed, Ray LaHood, the new US secretary of transportation, was widely quoted when he said that Obama wanted to be known as the "high-speed rail president". The USD8 billion allocation will enable the Department of Transportation (DOT) to build 11 high-speed inter-city rail 'corridors' throughout much of the eastern US, which would be linked with the midwestern states. Evocative of the early days of trans-continental railroading, Chicago - previously home to Obama - would be a major hub.

Philadelphia-based infrastructure lawyer Alan Wohlstetter, a partner at law firm Fox Rothschild, writes in a memo to clients: "The stimulus plan includes provisions modelled after the High-Speed Rail for America Act introduced by Senators John Kerry and Arlen Specter [in late 2008] to bring American rail infrastructure up to date with current world standards."

Shawna F Watley, senior policy adviser from law firm Holland & Knight's government section, explains that the DOT must prepare a plan by April for dispersing money over a three-year timeframe through grants to the individual states.

Although the Kerry/Specter bill did not gain traction on its own, its ideas were adopted in PL 111-5. In an article co-authored with colleague Nevena Simidjiyska, who focuses on general corporate matters, Fox Rothschild's Wohlstetter explains that a further post-stimulus version of their bill, containing additional tax-exempted bond schemes, is likely to be introduced during 2009. Present provisions already include a tax exemption - on the alternative minimum tax that bedevils wealthy US investors - on interest paid by private activity bonds for high-speed rail. They explain that such an exemption "will promote public-private partnerships between government agencies and private sector companies by giving them a financing vehicle to access the tax-exempt capital markets". The ARRA already contains additional tax features that ease tax rules so that tax-exempt bonds can be issued for high-speed rail facilities; the next version of Kerry/Specter will broaden their applicability, according to the Fox Rothschild team.

In the airline sector, airport improvements will build on existing programmes, with half the money allocated on a competitive basis to qualifying projects within four months of the ARRA's signing in February, and the other half within a year. Funds will be disbursed through an existing network of FAA offices to the more than 3,400 airports already eligible to receive federal money through the National Plan of Integrated Airport Systems (NPIAS). David Whitestone, a partner at Holland & Knight who specialises in the area of appropriations, transportation and government relations, says: "We expect that you will have lots of small projects rather than a few large ones."

For aviation, the real excitement can be found in a small but symbolic step towards a state-of-the-art global positioning system (GPS)-based, totally revamped ATC system, called 'Next-Gen'. DJ Gribbin, previously general counsel in the DOT, who has joined Macquarie Capital as a managing director, comments: "All of us who frequently rely on air travel hope the brief mention of Next-Gen in the budget presages a concerted effort on the part of the administration to continue progress toward expediting implementation of a satellite-based system."

The USD200 million represents a very small portion of the total cost of Next-Gen. The programme is expected to require approximately USD18 billion to USD20 billion through 2020 spread across some 30 capital investment programmes, with a similar amount through 2025, according to testimony by Victoria Cox, vice-president of operations planning at the FAA, during mid-March legislative hearings.

In February, the FAA issued a workplan detailing myriad incremental Next-Gen workflow items across diverse traffic management, terminal modernisation and information systems out through FY12. It is unclear how this will be paid for over the next three years and beyond.

Ironically, the US Government Accountability Office (GAO) authored a report in mid-March, warning of reduced proceeds of excise taxes that support the Airport and Airway Trust Fund. According to trade organisation the Air Transport Association of America (ATA), which represents the principal US airlines: "The trust fund initially aimed to address capital needs, such as runways and taxiways at airports and new computers and radar equipment for the ATC system. Since then, however, Congress also has used trust fund revenues to cover much of the FAA operating budget."

The maritime mode is very much on the periphery of the ARRA. The USD60 million of highway finance is allocated for passenger ferries and terminals.

The USD4.6 billion for the US Army Corps of Engineers will be devoted to existing projects. Julie Adair Minerva, a Washington, DC-based senior public affairs advisor with the public policy and regulation group at Holland & Knight, after explaining that funding will go to previously authorised channel deepening, dams and levees, adds: "If you have a brand new project that you are looking to start, this is not the opportunity."

The USD100 million allocated to small shipyards will be disbursed by the US Maritime Administration (MARAD) for improvements at shipbuilding or repair yards employing less than 1,200 people.

In the transport category, highways and roads are the major focus. During the vociferous debates on what subsequently become the ARRA, policy-makers sought avenues for deviating from the US Federal Highway Administration's (FHWA's) rigid, albeit tried-and-trusted approach, to funding.

Funding innovation

Another agency within the DOT, the Federal Transit Administration (FTA), will be looking at more innovative projects in distributing USD6.9 billion of money for rail and bus transportation systems, with an emphasis on 'green' modifications that will reduce energy consumption or emissions.

An additional USD1.5 billion goes towards modernising rail networks and for new projects. In the weeks after the ARRA was passed, money was being quickly disbursed to continuing light-rail projects around the US.

A large chunk of the grant money devoted to highway transportation in PL 111-5 will be allocated to the individual states (USD17.8 billion) and regional metropolitan planning organisations (nearly USD8 billion). The actual wording in the stimulus legislation guides states in allocating money, as follows: "Priority shall be given to projects that are projected for completion within a three-year timeframe, and are located in economically distressed areas."

Allocations among states will be based on population, and will also follow existing funding formulas that are tied to a mix of highway lane miles, miles travelled and tax payments by highway users. Money is then dispersed by the states for individual projects. The projects need to be eligible for the FHWA's existing funding criteria, including benefit-to-cost considerations, for highways across the country, including major interstate systems and secondary and tertiary two-lane roads connecting the systems. Infrastructure roads within ports, although within ARRA's purview, do not gain a special set-aside.

Although the ARRA offers a much needed salve for road projects, the US surface transportation network is facing important longer-term funding decisions. "A stimulus package that includes nearly USD40 billion for highway and transit infrastructure, while important in addressing the short-term economic crisis, will pay for only about three months of the identified annual national funding gap to maintain and improve the system - a gap that repeats itself and compounds year after year," according to the final report from the National Surface Transportation Infrastructure Financing Commission (NSTIFC), issued in late February.

The NSTIFC, convened in early 2007 - two years in advance of the upcoming five-year congressional reauthorisation for surface transport funding - recommends a fundamental shift on how the highway network is funded. In its view, the existing methods, centred around the Highway Trust Fund, are approaching the end of the line.

Currently, US interstate roadways are supported by annual budget appropriations from the federal government and by individual states. The federal portion, in turn, is funded through the Highway Trust Fund, which - analogous to its aviation counterpart - has been drawing down its capital, as driving has now declined each month since October 2007. The NSTIFC says: "The federal Highway Trust Fund faces a near-term insolvency crisis, exacerbated by recent reductions in federal motor fuel tax revenues and truck-related user-fee receipts."

For the near term, including the next five-year surface transport reauthorisation and another five years beyond that, the NSTIFC is recommending increases in taxes on gasoline and diesel fuel. However, the pathway is now being mapped for a transition to a more fuel-efficient future. In addition to the greener alternatives to automobiles being supported by the FTA, renewed moves towards automotive fuel economy and energy security figure prominently in such thinking.

Debating 'user pays' charges

In its report, the NSTIFC recommends what it describes as a "federal funding system based on more direct forms of 'user pays' charges, in the form of a charge for each mile driven (commonly referred to as a vehicle miles travelled, or VMT fee system)" and the commission encourages the individual states to follow a similar approach, including "targeted tolling" systems. The report suggests a 10-year phase-in period.

Through an online venue hosted by National Journal Online, a Washington, DC-based think-tank, Kathy Ruffalo, one of 15 NSTIFC commissioners and a transportation policy consultant, discussed the rationale for a move to VMT funding in the face of fuel efficiency - a competing policy objective.

"If there are continued reductions in VMT, the amount of revenue raised would be impacted," she argues. "However, we do not believe a reduction in VMT - in the magnitude we have seen in past months - would have as dramatic an impact on the Highway Trust Fund revenues as new technology and alternative fuel use will have on a motor fuel tax funding system."

In the online forum, participant Robert Crandall, CEO of American Airlines during the 1980s and now retired, opines: "Every citizen of the United States benefits from the existence of world-class transportation facilities. It has always seemed to me that broad based - say VAT - taxation ought to bear at least a portion of the cost of transportation services."

Responding to Crandall, Ruffalo says: "You have raised a key issue in the upcoming debate on the surface transportation bill and probably the FAA reauthorisation bill as well - should the 'user pays' principle be the foundation of any funding mechanism?"

While GPS may offer a technological solution for moving ATC beyond its present radar-based technology, GPS will probably present problems of a different sort for surface transportation: that of privacy. The politically influential American Trucking Association firmly opposed the VMT idea, but on privacy grounds, saying: "The Commission's solution to migrate to a (VMT) tax currently presents privacy concerns that are not only intrusive, but could lead to new forms of fraud and identity theft."

A bill to reauthorise the FAA's funding for the FY09 to FY12 budgets, designated as HR 915, is working its way through the labyrinth of legislative committees. The FAA's present funding level of USD14.9 billion would be expanded incrementally to USD18.4 billion in FY12. At a high level, privatisation and outsourcing of systems within Next-Gen is assumed within the budget projections.

A version of HR 915 now under study by the House of Representatives Committee on Transportation and Infrastructure was roundly denigrated by the ATA for "not making the needed changes to ensure acceleration of ATC modernisation." In a letter to the House Committee, the ATA added: "Leadership from the committee is needed to ensure that appropriate funding and programme direction is in place to accelerate the deployment of this critical programme." The ATA also came out strongly against user fees to fund the FAA; the present version of HR 915 includes an increase in fees charged to passengers using commercial airports.

Oversight challenges

The ARRA awards to the FAA are not without irony. In testimony before the committee, Calvin Scovill III, inspector general at DOT, notes that the financial crisis has brought difficulties to airports seeking to raise money in bond markets: "The economic stimulus packages contain significant funding amounts for the AIP that will help to revitalise airport development this year and next year. However, such a large infusion of new funds could create significant oversight challenges for [the] FAA."

What a nice problem to have.