

Private Activity Bonds (PABs)

Transportation Finance Innovations

Quick Facts

- Provides low-cost financing to projects with private involvement.
- Aims to increase private sector investment in U.S. transportation infrastructure.
- Seven projects have been approved for almost 30% of the \$15 billion in PABs as of May 2011.

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U.S. Department of Transportation
Federal Highway Administration

PPRIVATE ACTIVITY Bonds (PABs) are debt instruments issued by State or local governments whose proceeds are used to construct projects with significant private involvement.

How Do They Work?

PABs have long provided a low-cost financing option for various types of public-benefit infrastructure projects, such as ports and water and sewer projects. However, transportation infrastructure had not been eligible for PAB financing until the passage of SAFETEA-LU. Section 11143 of Title XI of SAFETEA-LU amended Section 142(a) of the Internal Revenue Code to add highway and freight transfer facilities to the types of privately developed and operated projects for which PABs may be issued. This change allows private activity on these types of projects while maintaining the tax-exempt status of the bonds.

The law limits the total amount of such bonds to \$15 billion and directs the Secretary of Transportation to allocate this amount among qualified facilities. The \$15 billion in exempt facility bonds is not subject to any individual State's volume cap. State and local projects receiving a PAB allocation must also receive assistance under Title 23 or Title 49, United States Code (U.S.C.).

What Are the Benefits?

Passage of the private activity bond legislation reflects the Federal Government's desire to increase private sector investment in U.S. transportation infrastructure. Providing private developers and operators with access to tax-exempt interest rates lowers the cost of capital significantly, enhancing investment prospects. Increasing the involvement of private investors in highway and freight projects generates new sources of money, ideas, and efficiency.



Capital Beltway high-occupancy toll lanes was the first project to utilize PABs.

A technical paper prepared for the National Surface Transportation Policy and Revenue Study Commission estimates, in present value terms, the Federal tax-exemption subsidy for PABs to be approximately 15–20% of the amount borrowed.

How Is It Used?

With approval from the U.S. Department of Transportation (DOT) to issue PABs, the State or local government issues tax-exempt debt on behalf of the private entity undertaking the project. The private entity finances and delivers the project and is responsible for debt service on the PABs. As of May 2011, almost 30% of the authorized \$15 billion in PAB allocations had been approved by DOT for seven projects. The first project for which bonds were issued is the Capital Beltway/I-495 high-occupancy toll (HOT) lanes project.

The legislation requires that at least 95% of the net proceeds of bond issues be expended for qualified highways or surface freight transfer facilities within a 5-year period from the date of issue. If this does not occur, the issuer must use all unspent proceeds to redeem bonds of the issue within 90 days after the conclusion of the 5-year period. As an alternative, the issuer may request an extension of the 5-year period if it can establish that the failure to expend the

PAB Allocations and Issues (through May 2011)	
Bonds Issued	
Capital Beltway HOT Lanes, VA	\$589,000,000
North Tarrant Expressway, TX	\$400,000,000
IH 635 (LBJ Freeway), TX	\$615,000,000
Denver RTD Eagle Project (East Corridor & Gold Line), CO	\$397,835,000
CenterPoint Intermodal Center, Joliet, IL	\$150,000,000
Subtotal	\$2,151,835,000
Allocations	
Knik Arm Crossing, AK	\$600,000,000
CenterPoint Intermodal Center, Joliet, IL	\$1,190,000,000
I-80 RailPort, Seneca, IL	\$576,000,000
Subtotal	\$2,366,000,000
Total PAB Allocations and Issues	\$4,517,835,000

funds was due to circumstances beyond its control.

Potential Advantages

- Enable innovative procurement by providing lower cost financing to projects with private involvement.
- Assist projects that are of public benefit but that may have too much private involvement to qualify for tax-exempt financing.

Potential Limitations

- DOT allocation only provides a “license to issue.” Upon receipt of allocation, the project sponsor must still identify the public-sector issuer for PABs and follow all requirements for issuance of PABs.
- Depending on market demand, PABs may be significantly more expensive as a form of financing than traditional tax-exempt bonds or other alternatives.

Considerations

- In general, PAB projects must receive Federal assistance under Title 23 or 49, U.S.C.

- Project elements funded with Federal funds must follow all Federal-aid requirements; however, not all elements of the PAB project may have to follow all Federal-aid requirements.
- PAB allocation recipients must retain bond counsel to ensure that all IRS requirements for PABs are followed. ■

Qualified Highway or Surface Freight Transfer Facilities Include:

- ▶ Any surface transportation project that receives Federal assistance under Title 23, U.S.C., as in effect on August 10, 2005, the date of the enactment of Section 142(m).
- ▶ Any project for an international bridge or tunnel for which an international entity authorized under Federal or State law is responsible and that receives Federal assistance under Title 23, U.S.C. (as so in effect).
- ▶ Any facility for the transfer of freight from truck to rail or rail to truck (including any temporary storage facilities directly related to such transfers) that receives Federal assistance under Title 23 or Title 49, U.S.C.



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IPD’s project delivery team covers cost estimation, financial planning, and project management and assists FHWA Divisions with statutory requirements for major projects (e.g., cost estimation, financial plans, and project management plans).

PROJECT FINANCE

IPD’s project finance program focuses on alternative financing, including State Infrastructure Banks (SIBs), Grant Anticipation Revenue Vehicles (GARVEEs), and Build America Bonds (BABs).

PUBLIC-PRIVATE PARTNERSHIPS

IPD’s P3 program covers alternative procurement options (e.g., toll concessions and availability payments), which can reduce cost, improve project quality, and provide additional financing options (e.g., Private Activity Bonds [PABs]).

REVENUE

IPD’s revenue program focuses on how governments can use innovation to generate revenue from transportation projects (e.g., value capture, developer mitigation fees, air rights, and road pricing).

TIFIA

The Transportation Infrastructure Finance and Innovation Act (TIFIA) program provides credit assistance for significant projects. Many surface transportation projects—highway, transit, railroad, intermodal freight, and port access—are eligible to apply for assistance.

