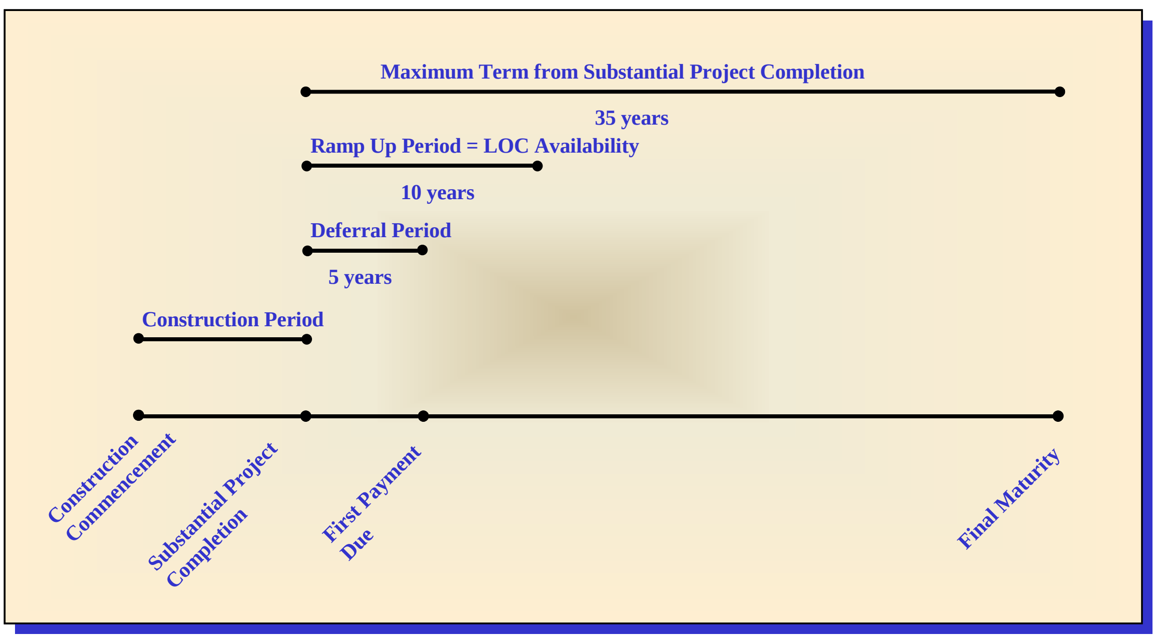
Chapter 2: Terms and Funding of Credit Instruments

The TIFIA credit program's secured (direct) loans, loan guarantees, and standby lines of credit may offer more flexible repayment terms and more favorable interest rates compared to other lenders. This chapter summarizes the terms that apply generally to TIFIA credit assistance and describes the major features of each credit instrument. A section on loan repayment and prepayment structuring provides information on financing structures and related repayment issues that may arise during negotiations. The chapter also provides an explanation of the funding controls that govern the amount of credit assistance available under the TIFIA program.

Section 2-1
Summary of Basic Terms for TIFIA Credit Assistance

Certain features of TIFIA credit assistance are the same regardless of whether the credit instrument is a secured loan, loan guarantee, or line of credit. For example, the maximum maturity of all TIFIA credit instruments is 35 years after a project's substantial completion. The DOT, at its discretion, has the ability to defer the first TIFIA payment until five years after substantial completion, depending on the needs of the project. Exhibit 2-A provides an illustrative TIFIA repayment structure for any of the three credit instruments.

Exhibit 2-A: Illustrative TIFIA Repayment Structure as Permitted by Statute



It is anticipated that, in many cases, the TIFIA credit instrument will be junior (*i.e.*, subordinate) to the project's capital markets or commercial bank debt in the priority of its lien on the project's cash flow. However, in the event of bankruptcy, insolvency, or liquidation, the DOT is required by statute to have a parity lien with respect to other creditors. The credit agreement will clearly specify the DOT's interest in the pledged security relative to other creditors.

The TIFIA statute places two other important limits on the Government's exposure to credit risk. First, TIFIA assistance must not exceed 33 percent of reasonably anticipated eligible project costs. This is to ensure that the DOT shares the credit risk with other participants. Second, the applicant must obtain an investment-grade rating (Baa3/BBB-or higher) on the senior debt obligations and a rating on the TIFIA credit instrument, both from a Nationally Recognized Statistical Rating Organization (NRSRO), in order to execute a TIFIA credit agreement. Chapter 3 provides further details on eligible project costs and credit ratings.

Section 2-2
TIFIA Credit Instruments

A summary of the main features of TIFIA secured loans, loan guarantees, and lines of credit follows. These features are established by statute. This section also addresses the rules that govern the setting of interest rates, disbursement of funds, and repayment of the TIFIA debt.

Secured Loans (23 U.S.C. §603)

A TIFIA secured loan is a debt obligation involving the DOT as the lender and a non-Federal entity as the borrower. Actual terms and conditions will be negotiated between the DOT and the borrower, but the general characteristics include:

- Use of Proceeds. The proceeds of a secured loan must be used either to finance eligible project costs or to refinance interim construction financing of eligible project costs. In the latter case, the DOT loan may refinance existing debt no later than one year following substantial completion of the project.[1]

- Amount. The principal amount of a secured loan (in combination with other TIFIA credit assistance, if any) may not exceed 33 percent of the reasonably anticipated eligible project costs. The TIFIA loan must be secured by the same revenues pledged to the senior debt. If the TIFIA credit is rated below investment grade, the amount of the TIFIA loan may not exceed the amount of the senior debt.

- Interest Rate. The interest rate on a secured loan will be equal to or greater than the yield on U.S. Treasury securities of comparable maturity on the date of execution of the credit agreement. The DOT identifies the Treasury rates through use of the daily rate tables published by the Bureau of the Public Debt for the State and Local Government Series (SLGS) investments. Adding one basis point to the SLGS rates produces the estimated average yields on comparable Treasury securities. The SLGS tables can be found on-line at https://www.treasurydirect.gov/GA-SL/SLGS/selectSLGSDate.htm. The daily TIFIA interest rate can be found on the TIFIA web site at http://tifia.fhwa.dot.gov. Interest

[1] The SAFETEA-LU provides broad authority to use TIFIA proceeds to refinance long-term project obligations if such refinancing results in "additional funding capacity for the completion, enhancement or expansion" of a project otherwise eligible for TIFIA. The DOT will define the parameters of this authority in a future rule-making. Please contact the TIFIA JPO if you have questions.

accrual on TIFIA proceeds begins immediately upon disbursement of funds to the borrower.

- Timing of Disbursements. The DOT will disburse funds as often as monthly, on a reimbursement basis, as costs are incurred for eligible project purposes. The credit agreement will specify a draw schedule, which may be amended if necessary.
- Maturity. The final maturity date of a secured loan must be no later than 35 years after the date of substantial completion of the project.
- Repayment Terms. Scheduled repayments must commence no later than five years after the date of substantial completion of the project. Level debt service is not required for project financings where pledged revenues are projected to increase over time. Debt service payments typically are scheduled semi-annually.
- Deferrals. In the event revenues are insufficient to meet scheduled TIFIA loan payments, the DOT, at its sole discretion, may allow payment deferrals. Any such deferrals shall be contingent on the project's meeting criteria established by the Secretary, including standards for reasonable assurance of repayment. There can be no assurance the Secretary will exercise this authority, however, so borrowers should negotiate a debt service schedule they are confident they can meet.
- Prepayment Conditions. A secured loan may be prepaid in whole or in part at any time without penalty.
- DOT Lien Priority. The TIFIA lien on project revenues can be subordinated to those of senior lenders except in the event of bankruptcy, insolvency, or liquidation of the obligor. In such an instance, the TIFIA lien would rise to parity with senior creditors. This provision can be effected through a master trust agreement, an inter-creditor agreement, or other agreement entered into at the time of execution of the secured loan.

Loan Guarantees (23 U.S.C. § 603(e))

A TIFIA loan guarantee is a pledge by the DOT to pay a third-party lender all or part of the debt service on a borrower's debt obligation. The DOT will seek to recover from the borrower all funds paid to the guaranteed lender, pursuant to a reimbursement agreement executed simultaneously with the loan guarantee.

By statute (23 U.S.C. §601(a)(4)), the guaranteed lender must be a "non-Federal qualified institutional buyer" as defined in 17 CFR §230.144A(a) , including qualified retirement plans and governmental plans. Prospective applicants and lenders should contact the DOT with any questions about what constitutes a "non-Federal qualified institutional buyer."

The DOT may give preference to applications for loan guarantees rather than other forms of credit assistance. This preference is consistent with Federal policy that, when Federal credit assistance is necessary to meet a Federal objective, loan guarantees should be favored over direct loans, unless attaining the Federal objective requires a subsidy deeper than can be provided by a loan guarantee. Applicants requesting only a direct loan and/or a line of credit are required to specify the project's financial structure if the TIFIA credit assistance was instead in the form of a loan guarantee, including the amount of guaranteed loan assistance that would be required.

Characteristics of a guaranteed loan include:

- Use of Proceeds. The proceeds of a guaranteed loan must be used either to finance eligible project costs or to refinance interim construction financing of eligible project costs.[2] In the latter case, the guaranteed loan may refinance existing debt no later than one year following substantial completion of the project.

- Amount. The principal amount of a DOT loan guarantee, in combination with any other TIFIA credit assistance, may not exceed 33 percent of the reasonably anticipated eligible project costs.

- Interest Rate. The interest rate on a guaranteed loan will be negotiated between the guaranteed lender and the borrower, subject to consent from the DOT. Interest payments on a guaranteed loan are subject to Federal income taxation.

- Maturity. The final maturity date of the guaranteed loan must be no later than 35 years after the date of substantial completion of the project.

- Repayment Terms. Scheduled repayments to the guaranteed lender must commence no later than five years after the date of substantial completion of the project. Level debt service is not required for project financings where the pledged revenues are projected to increase over time.

- Deferrals. In the event that revenues are insufficient to meet scheduled loan payments, the DOT may consent to payment deferrals and a rescheduling of the guaranteed debt service. Approval of any such payment deferrals shall be contingent on the project's meeting criteria established by the Secretary, including standards for reasonable assurance of repayment. There can be no assurance the Secretary will exercise this authority, however, so borrowers should negotiate a debt service schedule they are confident they can meet.

- Prepayment Conditions. The prepayment features on a guaranteed loan will be negotiated between the guaranteed lender and the borrower, subject to the consent of the DOT.

- Default Feature. In the event of an uncured borrower payment default, the guaranteed lender will receive payment from the DOT for the guaranteed payment due. The DOT will seek recovery from the borrower of all funds advanced, pursuant to a reimbursement agreement executed simultaneously with the loan guarantee.

[2] See footnote #1. Please contact the TIFIA JPO if you have questions.

- DOT Lien Priority. The TIFIA lien on project revenues can be subordinated to those of senior lenders except in the event of bankruptcy, insolvency, or liquidation of the obligor. In such an instance, the TIFIA lien would rise to parity with senior creditors. This provision can be effected through a master trust agreement, an inter-creditor agreement, or other agreement entered into at the time of execution of the secured loan. In the event of a draw on the DOT guarantee, the guaranteed lender remains in senior position if not repaid in full, and the DOT loan for the amount of all such draws becomes a junior lien.

Lines of Credit (23 U.S.C. §604)

A TIFIA line of credit provides a contingent loan that may be drawn upon after substantial completion of the project to supplement project revenues during the first 10 years of the project's operations. The DOT will disburse funds only under certain conditions, which will be specified in the credit agreement.

Characteristics of a line of credit include:

- Use of Proceeds. The proceeds from a draw on a line of credit may be used only to pay debt service on project obligations (other than a TIFIA credit instrument) issued to finance reasonably anticipated eligible project costs, extraordinary repair and replacement costs, operation and maintenance expenses, and/or costs associated with Federal or state environmental restrictions arising after the transaction closed.

- Amount. The total principal amount of a line of credit, in combination with any other TIFIA credit assistance, may not exceed 33 percent of the reasonably anticipated eligible project costs.

- Condition Precedent for Draws. A draw may be made only if revenues from the project are insufficient to pay the costs enumerated above in "Use of Proceeds." Reserve funds need not be tapped prior to a TIFIA draw.

- Availability. A line of credit may be available for a period of 10 years following substantial completion of the project.

- Interest Rate. The interest rate on a secured loan resulting from a draw on a line of credit will be equal to or greater than the yield on a 30-year U.S. Treasury security on the date of the execution of the line of credit agreement. The DOT identifies the Treasury rates through use of the daily rate tables published by the Bureau of the Public Debt for the State and Local Government Series investments. Adding one basis point to the SLGS rates produces the estimated average yields on comparable Treasury securities. The SLGS tables can be found on-line at The SLGS tables can be found on-line at https://www.treasurydirect.gov/GA-SL/SLGS/selectSLGSDate.htm. The daily TIFIA interest rate can be found on the TIFIA web site at http://tifia.fhwa.dot.gov. Interest accrual on TIFIA proceeds begins immediately upon disbursement of funds to the borrower.

- Maturity. The final maturity date of a secured loan resulting from a draw on a line of credit must be no later than 35 years after the date of substantial completion of the project.

- Repayment Terms. Scheduled repayments of a draw on a line of credit must commence no later than five years after the end of the 10-year period of availability and be fully repaid no later than 25 years after the end of the 10-year period of availability. Level debt service is not required. Debt service payments should be scheduled semi-annually.

- Prepayment Conditions. A secured loan resulting from a draw on a line of credit may be prepaid in whole or in part at any time without penalty.

- DOT Lien Priority. The TIFIA lien on project revenues may be subordinated to those of senior lenders except in the event of bankruptcy, insolvency, or liquidation of the obligor. In such an instance, the TIFIA lien would rise to parity with senior creditors. This provision can be effected through a master trust agreement, an inter-creditor agreement, or other agreement entered into at the time of execution of the secured loan.

Section 2-3
Loan Repayment and Prepayment Structuring

The TIFIA statute gives the DOT discretion to defer the commencement of debt service repayments for up to five years after substantial completion. The DOT also has the flexibility to structure a debt service schedule so that repayment is aligned with projected cash flows. This may include deferring partial interest and principal repayments beyond the five-year post-construction period as needed.

1. Scheduled TIFIA Debt Service. Projects are not entitled to debt service deferral. In the exercise of its discretion, the DOT evaluates the economics of each project to determine an appropriate repayment schedule. Factors in this assessment include:

   - *Availability of revenues for debt service.* Some projects are not true "project financings," but rely on tax or other revenues, which may be available for debt service even before the project is completed. In such cases, the DOT is likely to require commencement of debt service upon substantial completion, although DOT may require commencement of debt service during construction for a project not financed with user revenues. Projects most likely to be allowed significant interest deferral and heavy backloading of principal are those where project revenues support the financing and borrowers anticipate a long ramp-up period.

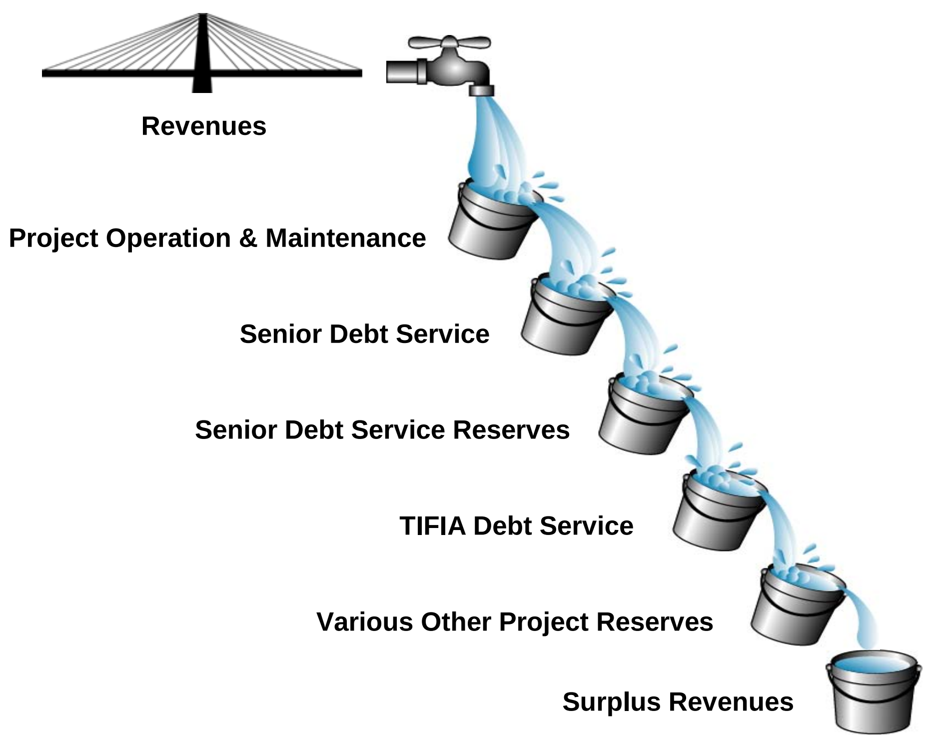
   - *Amortization of senior debt.* When the financial plan includes other debt senior to TIFIA, the DOT expects that the capitalized interest period for the senior debt is likely to end before the capitalized interest period for the TIFIA loan. Thus, the DOT may agree to continue deferring an appropriate amount of its loan interest to ensure that revenue is adequate to pay full interest on the senior debt. However, the DOT will not increase its investment in a project by deferring interest when other creditors are withdrawing their investment. Therefore, DOT's policy is not to permit any amortization of senior debt while TIFIA interest is being deferred.

- *Returns on equity*. Just as the DOT will defer commencement of its return on investment in favor of senior debt, so equity investors, who will be subordinate to TIFIA, must defer commencement of their return. The DOT will not permit any distribution to equity until all currently accruing TIFIA interest is paid. The DOT will negotiate, on a project-by-project basis, the priority and relationship of TIFIA repayment and equity payouts.

2. Prepayment and Refinancing. Although TIFIA provides long-term financing, the DOT does not intend that TIFIA become part of a project's permanent capital structure where a strong revenue stream and vigorous project economics permit prepayment or substitution of the TIFIA credit instrument. The DOT will negotiate a debt service schedule that provides a high probability of repayment and avoidance of default. In return, the DOT typically requires that excess revenues – not needed for project purposes – be applied to prepayment of the TIFIA loan. The DOT also will seek to structure the financing in a way that encourages borrowers to replace the TIFIA loan with capital markets debt at such time as project economics support refinancing.

Exhibit 2-B shows a typical flow of funds for a project that includes both senior and subordinate TIFIA debt. The chart demonstrates how senior debt service (as well as reserve accounts for the benefit of senior bondholders) generally accumulates revenues ahead of TIFIA debt service.

Exhibit 2-B: Example of Project Flow of Funds



Section 2-4
Taxation Issues

With regard to the TIFIA program, the TEA 21 Conference Report states:

> "The Conference recognizes that the Congress enacted the Deficit Reduction Act of 1984 provision prohibiting the combination of Federal guarantees with tax-exempt debt, because of concerns that such a double-subsidy could result in the creation of a 'AAA' rated security superior to U.S. Treasury obligations. Accordingly, any project loan backed by a loan guarantee as provided in TIFIA must be issued on a taxable basis….
>
> "...The Conferees are aware that present Federal income tax law prohibits the use of direct or indirect Federal guarantees in combination with tax-exempt debt (section 149(b) of the Internal Revenue Code of 1986). The TIFIA provisions of the conference agreement do not override or otherwise modify this provision of the Code."

The DOT urges all applicants, and particularly those intending to use tax-exempt bonds in connection with TIFIA loans or lines of credit, to consult with the Internal Revenue Service, the Department of the Treasury, or their bond counsel.

Section 2-5
TIFIA Program Funding

The TIFIA program is governed by the Federal Credit Reform Act of 1990 (FCRA), which requires the DOT to establish a capital reserve, or "subsidy amount," to cover expected credit losses before it can provide TIFIA credit assistance. Congress places limits on the annual subsidy amount available. Through SAFETEA-LU, Congress authorized $122 million for each Federal fiscal year from 2005 through 2009. As of the publication date of this program guide, short-term extensions of the surface transportation reauthorization act have been enacted continuing highway programs that were authorized through fiscal year 2009, and the anticipation is that Congress will reauthorize an equivalent amount of budget authority for the TIFIA program in fiscal year 2010. Based on experience, this funding amount can support more than $2 billion of average annual credit assistance.

The amount of TIFIA budget authority available in a given year is subject to several factors, as described below.

- Federal-aid Highway Obligation Limitation. This obligation limitation pertains to most of the programs funded from the Federal Highway Trust Fund (including the TIFIA program) and is determined through the appropriations process each year. As with appropriations processes for other Federal programs, this limitation typically reduces the total funds available for obligation in the year ahead. A typical limitation reduces obligation authority between 10 percent and 15 percent.

- Program Administration Expenses. The TIFIA statute authorizes the DOT to use up to $2,200,000 of authorized budget authority annually to administer the TIFIA program. In addition, the statute authorizes the DOT to collect and spend fees to cover expenses related to reviewing, negotiating, and servicing credit agreements.

- Future-year Reservations. As discussed later in Chapter 6, the DOT may in rare circumstances make future-year contingent commitments of budget authority. To ensure that additional projects have access to the program in future years, the DOT will not reserve more than 25 percent of the amount of budget authority authorized for a single fiscal year.

- Carry-over Resources. Any budget authority made available but not consumed in previous fiscal years may carry over and increase the amount of budget authority available in a given fiscal year.