Nossaman **Infra Insight**

MAP-21: Surface Transportation Reauthorization Ushers in Significant Changes to TIFIA and Tolling Provisions

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On June 29, 2012 Congress passed the **Moving Ahead for Progress in the 21st Century Act** (**MAP-21**), a compromise measure to reauthorize transportation funding through the end of 2014. A bipartisan and bicameral measure, MAP-21 contains meaningful reforms that, although marred by some missed opportunities, collectively represent a significant improvement in federal surface transportation law.

In our series of E-alerts on MAP-21, we elucidate four topics important to transportation financing and development of large transportation projects: (1) TIFIA (the Transportation Infrastructure Finance and Innovation Act at 23 U.S.C. §§ 601 *et seq*), (2) environmental streamlining, (3) tolling and (4) public-private partnerships. Nossaman has been a constant advocate for many of these reforms, and commends Congress on this achievement.

We foresee continued heavy demand for TIFIA credit assistance, particularly given the more attractive features of the reenacted TIFIA program. We have some concern that the combination of the increase in coverage from 33% to 49%, the significant simplification of eligibility criteria, the removal of FHWA discretionary selection authority, the rolling application process, the availability of master credit agreements to obtain early conditional commitments, and the fairly forgiving project readiness eligibility requirement will result in a race to submit applications prematurely. Government sponsors of large transportation development projects will need to develop timely, proactive strategies to take advantage of the new TIFIA program.

Meaningful TIFIA Reforms:

- **Major Program Expansion.** The bill authorizes the TIFIA program at $750 million of budget authority for FY 2013 and $1 billion for FY 2014. This translates into approximately $7.5 billion and $10.0 billion of lending capacity in each of these fiscal years, compared with approximately $1.2 billion of annual lending capacity under prior law. This expansion exceeds even the scale recommended by the National Surface Transportation Infrastructure Financing Commission in February 2009, reflecting the recent exponential growth in demand for this program.
- **Increased Coverage of Eligible Costs**. The bill increases the maximum share of project costs that can be financed through TIFIA from 33 percent to 49 percent. As before, if the secured loan does not receive an investment grade rating, the amount of the loan may not exceed the amount of the senior project obligations. With TIFIA's low interest rates,

this increased financing capacity for each project will further help projects achieve feasibility and reduce use of federal-aid funds. However, it comes with a downside – TIFIA will not stretch to assist as many projects as it could with a 33 percent maximum share. For projects delivered as public-private partnerships, the provision of developer equity for a share of project costs combined with the investment grade requirement if TIFIA debt exceeds senior debt will likely drive down the actual TIFIA share below 49 percent.

- **Project Eligibility.** The bill eliminates the selection criteria contained in the previous TIFIA statute, a much needed reform that will help remove subjectivity from the process. The eligibility criteria have been paired down and simplified, and can be administered in an objective manner. Most important, FHWA no longer can pick winners and losers among eligible projects.
- **Letters of Interest and Rolling Applications.** The bill calls for submission of a letter of interest to initiate the TIFIA process. The letter of interest must provide a (1) general description of the project, (2) proposed financial plan, (3) status of environmental review, and (3) information related to other TIFIA eligibility requirements. Thereafter, an application may be filed. The bill requires the TIFIA program to establish a rolling application process under which eligible projects must receive credit assistance if adequate funds are available to cover the associated subsidy cost. If adequate funds are not available, a project sponsor of an eligible project may enter into a master credit agreement and wait until the next fiscal year or the next fiscal year with available funds.
- **Master Credit Agreements.** The bill introduces the "master credit agreement" as a new concept. This tool should enable applicants to improve project financial planning by obtaining early contingent commitments of TIFIA credit assistance for single projects or a program of projects secured by a common security pledge. The master credit agreement will lock in the contingent commitment so long as financial close occurs within three years after the master credit agreement is executed. For each project, the agreement must set the maximum amounts and general terms and conditions of the credit assistance, identify the dedicated non-Federal revenue sources that will secure repayment, and include USDOT's agreement to obligate funds after all TIFIA program requirements are met.
- **Project Grouping.** The bill adds to the list of eligible projects those that are "composed of related highway, surface transportation, transit, rail, or intermodal capital improvement projects eligible for TIFIA program. assistance . . . in order to meet the eligible project cost threshold . . ., by grouping related projects together for that purpose," as long as the credit assistance for the projects is secured by a common pledge.
- **Program Administration.** The bill introduces new application processing procedures, requiring the TIFIA program to notify applicants of the complete or incomplete status of the application within 30 days of application receipt, and to rule on the application within 60 days of that

notice. The bill requires the TIFIA program to "implement procedures and measures to economize the time and cost involved in obtaining approval and the issuance of credit assistance." The bill also requires the TIFIA program to submit to Congress a report listing all letters of interest and applications received from project sponsors during the preceding fiscal year on December 1 of each year, including details on the timing of the program's application processing efforts. Congress apparently is interested in seeing significant gains in the speed and efficiency of FHWA's implementation.

- **Non-subordination.** Under pre-existing law, TIFIA credit assistance cannot be subordinated to the claims of any holder of project obligations in the event of bankruptcy, insolvency, or liquidation of the obligor. The bill provides that the TIFIA program must waive this requirement for a public agency borrower that is financing ongoing capital programs and has outstanding senior bonds under a preexisting indenture, provided that (1) the TIFIA credit assistance is rated in the A category or higher, (2) the credit assistance is secured and payable from pledged revenues not affected by project performance (such as a tax-backed revenue pledge or a system-backed pledge of project revenues), and (3) the TIFIA program share of eligible project costs does not exceed 33 percent. If the TIFIA program so waives the non-subordination requirement, the bill provides that the maximum credit subsidy to be paid by the Federal government must not be more than 10 percent of the principal amount of the secured loan, and that the obligor must be responsible for paying any remainder of the subsidy cost.
- **Public-Private Partnerships.** The bill allows Federal credit instruments, secured loans, and lines of credit to be repayable from payments owing to the obligor under a public-private partnership. The bill also allows applicants to submit an application under which a private party to a public-private partnership will be the obligor and identified later through completion of a procurement and selection of the private party. These changes represent much needed reforms. They confirm the ability to use TIFIA loans for availability payment public-private partnerships. They also confirm that a project owner that is pursuing a public-private partnership procurement may line up a conditional commitment for TIFIA financing in advance of completing the procurement and then transfer the TIFIA credit assistance rights to the winning proposer, to close the financing as the borrower.
- **Impact of Financial Assistance.** The bill requires the TIFIA program to determine that TIFIA financial assistance will (1) "foster, if appropriate, partnerships that attract public and private investment for the project"; (2) "enable the project to proceed more quickly. or reduce the lifecycle costs (including debt service costs) of the project"; and (3) "reduce the contribution of Federal grant assistance for the project."
- **Development Phase Activities.** The bill provides that any TIFIA credit instrument may be used to finance up to 100 percent of the cost of

development phase activities, including planning, feasibility analysis, revenue forecasting, environmental review, permitting, preliminary engineering and design work, and other preconstruction activities. This provision does not, however, alter the limit on the size of TIFIA financing to 49% of eligible costs.

- **Limited Buydowns.** The bill introduces the concept of a limited buydown, defined as a buydown of the interest rate by the obligor if the interest rate has increased between the application acceptance date or the master credit agreement date and the execution date for the Federal credit instrument. The bill provides that the interest rate of a secured loan or line of credit may not be lowered by more than the lower of (1) 1.5 percentage points (150 basis points), or (2) the amount of the increase in the interest rate. The bill is unclear on how the buydown will be administered. FHWA regulations may be needed to flesh out the buydown program and procedures.
- **Rural Infrastructure Projects.** The bill introduces the concept of a "rural infrastructure project," defined as "a surface transportation infrastructure project located in any area other than a city with a population of more than 250,000 inhabitants within the city limits." The law is unclear on how projects partially located in rural areas as defined will be treated. Here again, FHWA regulations will be needed to clarify this issue.
    - Of the total amount of funds authorized by the bill for each fiscal year, not more than 10 percent must be set aside for rural infrastructure projects. Any of these amounts so set aside that remain unobligated by June 1 of that fiscal year may be used for other non-rural projects.
    - While the eligible project cost floor remains at $50 million for most projects, rural infrastructure projects may have eligible project costs of only $25 million. The proceeds of secured loans may be used to refinance existing Federal credit instruments for rural infrastructure projects.
    - The interest rate of a loan or line of credit offered to a rural infrastructure project will be at one-half of the Treasury Rate, but only for the portion of a loan the subsidy cost of which is funded by amounts set aside for rural infrastructure projects, as described above.

Other Changes:

- **Total Federal Assistance.** The bill provides that the total Federal assistance provided on a project receiving a loan from the TIFIA program may not exceed 80 percent of the total project cost.
- **Eligibility Criteria / Creditworthiness.** The bill requires projects to satisfy certain creditworthiness standards in order to be eligible for assistance, including, at a minimum: (1) a rate covenant, if applicable, (2) adequate coverage requirements to ensure repayment, (3) an investment grade rating from at least two rating agencies on debt senior to the Federal credit instrument, and (4) a rating from at least one or two rating agencies on the Federal credit instrument, depending on the overall debt amount. Where

the Federal credit instrument is the senior debt, that instrument must receive an investment grade rating from at least one or two rating agencies, depending on the amount of the instrument. Preliminary rating opinion letters provided by applicants still must indicate that the project's senior obligations have the potential to achieve an investment grade rating, but the bill now requires such letters to include a preliminary rating opinion on the Federal credit instrument, regardless of whether that instrument is a senior obligation of the project.

- **Maturity Date.** Previously, the final maturity date of a secured loan had to be no later than 35 years after the date of substantial completion of the project. The bill provides that the final maturity date could be the useful life of the capital asset being financed, if such useful life is less than 35 years.
- **Loan Repayment Schedule.** The bill provides that the TIFIA program must now establish a repayment schedule for each secured loan and direct loan based on the useful life of the project, in addition to the projected cash flow from project revenues and other repayment sources.

Missed Opportunities:

- **Eligibility Criteria / Project Readiness.** As a threshold eligibility requirement, the bill will require an applicant to demonstrate a reasonable expectation that "the contracting process for construction of the project can commence by not later than 90 days after the date on which a Federal credit instrument is obligated for the project . . . ." § 602(a)(10). We understand that the drafters' intent is to assure that the obligation of budget authority (which occurs upon execution of a term sheet) occurs no sooner than 90 days before the start of the process to procure a construction contract for the TIFIA-financed project. A project readiness eligibility standard is a good thing to prevent tying up budget authority prematurely. We had hoped, however, that this would be tied to the commencement of a procurement following submission of the application, not the obligation date. The provision as written could allow applications and resulting conditional credit commitments excessively far in advance of when closing of TIFIA funding will actually be needed for the project, perhaps even well before it is evident that a project will indeed successfully proceed into and through procurement.
- **No Right to Subsidize.** Except in the narrow case of highly rated TIFIA loans that will remain subordinated after bankruptcy of the borrower, the bill lacks an express right of applicants to pay a subsidy where budget authority is unavailable. The USDOT's recent policy has been to disallow offers of subsidy.
- **NEPA.** The bill provides that no funding shall be obligated for a project that has not received an environmental categorical exclusion, a finding of no significant impact, or a record of decision under NEPA. This will preclude financial close and access to TIFIA funds for projects under contract, preliminary design and right of way acquisition prior to completion of NEPA action on the project, activities permitted under existing law and the

bill. Project owners will have to find other funding sources if they wish to move forward with preliminary design and right of way acquisition before NEPA action is completed.

- **Development Phase Costs.** The definition of Eligible Costs ties the costs to those incurred by or for the account of the obligor. Where the TIFIA obligor will be a private party to a public-private partnership, development phase costs incurred before the TIFIA credit assistance is closed will be incurred by the project owner rather than this obligor. The bill unfortunately does not clarify that these pre-financing owner-incurred costs can be reimbursed with TIFIA loan proceeds.
- **Funding.** Beginning in FY 2014, if the cumulative unobligated and uncommitted balance of funding available as of April 1 exceeds 75 percent of the amount made available to the TIFIA program for that fiscal year, the TIFIA program must distribute to the States any excess funds and associated obligation authority. Current TIFIA demand makes this scenario unlikely.

Tolling Provisions:

Under prior law, with few exceptions, tolling was prohibited on Interstate highways and many other federal-aid highways. The bill expands the exceptions, in recognition of the fact that federal fuel tax revenues are stagnant and new revenue sources are imperative to meet the growing funding gap in surface transportation. This expansion is tempered, however, by the fact that Congress has curtailed the existing toll pilot programs. Nevertheless, under the new law, tolls will play an increasingly important role in transportation financing.

Government sponsors of large transportation projects will have new toll revenue options at their disposal. They will need to develop strategies to take advantage of this new array of tolling opportunities, including use of toll concessions, as well as availability payment public-private partnerships that use tolls to reimburse public sponsors for all or a portion of the payments.

Meaningful Reform:

- **New Capacity Tolling.** The bill includes new capacity tolling provisions that change existing law by significantly expanding the scope of permitted tolling on the Interstate System, with the caveat that the number of toll-free non-HOV lanes may not decrease as a result of the construction of such new capacity. The bill also authorizes new capacity tolling on highways, bridges or tunnels that are <u>not</u> on the Interstate System, again with the caveat that the number of toll-free lanes does not decrease. Specifically, the bill authorizes federal participation in projects for the:
  - initial construction of a toll highway, bridge, or tunnel or approach to the highway, bridge or tunnel;
  - initial construction of one or more lanes or other improvements that increase capacity of a highway, bridge, or tunnel (other than a

highway on the Interstate System) and conversion of that highway, bridge, or tunnel to a tolled facility, *if the number of toll-free lanes, excluding auxiliary lanes, after the construction is not less than the number of toll-free lanes, excluding auxiliary lanes, before the construction*;

  - initial construction of one or more lanes or other improvements that increase the capacity of a highway, bridge, or tunnel on the Interstate System and conversion of that highway, bridge, or tunnel to a tolled facility, *if the number of toll-free non-HOV lanes, excluding auxiliary lanes, after such construction is not less than the number of toll-free non-HOV lanes, excluding auxiliary lanes, before such construction*;
  - reconstruction, resurfacing, restoration, rehabilitation, or replacement of a toll highway, bridge, or tunnel or approach thereto;
  - reconstruction or replacement of a toll-free bridge or tunnel and conversion of the bridge or tunnel to a toll facility;
  - reconstruction of a toll-free Federal-aid highway (other than a highway on the Interstate System) and conversion of the highway to a toll facility;
  - reconstruction, restoration, or rehabilitation of a highway on the Interstate System if the number of toll-free non-HOV lanes, excluding auxiliary lanes, after reconstruction, restoration, or rehabilitation is not less than the number of toll-free non-HOV lanes, excluding auxiliary lanes, before reconstruction, restoration or rehabilitation;
  - conversion of a high occupancy vehicle lane on a highway, bridge, or tunnel to a toll facility; and
  - preliminary studies to determine the feasibility of a toll facility for which Federal participation is authorized under this paragraph.
- **Self-Executing.** The bill removes the requirement that the government sponsor and FHWA execute a tolling agreement; the bill codifies the substantive requirements, making the provision self-executing.
- **Existing Toll Pilot Program.** The bill make it unnecessary to extend or expand the Interstate System Construction Toll Pilot Program, which will continue to run until its 2015 expiration date under SAFETEA-LU.
- **HOV Lanes.** The bill changes existing law to allow the conversion of HOV lanes to tolled lanes as part of the reconstruction, restoration or rehabilitation of a highway on the Interstate System. The bill further authorizes the conversion of HOV lanes on a non-Interstate facility to a toll facility.
- **HOV Speed Restoration.** The bill modifies existing law to impose program sanctions for an agency's failure to bring an HOV facility into compliance within 180 days using the authorized measures specified. This change to existing law establishes firm federal policy on taking affirmative action to maintain reasonable speeds in HOV lanes. This reform in turn should facilitate conversion of HOV lanes to HOT lanes.

Missed Opportunities:

- **Existing Toll Pilot Programs.** The bill fails to address existing toll pilot programs, which means that Congress passed on an opportunity to preserve tolling in a small set of appropriate situations not covered by the bill's amendments. As a result of the bill's failure to reauthorize the existing 15-project Express Lanes Demonstration Program, FHWA's authority to approve Express Lanes projects expired on June 30, 2012. Furthermore, participation in both the Value Pricing Pilot Program and the Interstate System Reconstruction and Rehabilitation Pilot Program will continue to be limited – to 15 and three slots, respectively. Currently, there is only one vacancy in the Value Pricing Pilot Program and all three of the Interstate System Reconstruction and Rehabilitation Pilot Program slots are filled.
- **HOV Lanes.** Despite the improvements to existing law related to the conversion of HOV lanes to tolled lanes noted above, the bill expressly bars tolling of HOV vehicles in converted lanes on the Interstate System.
- **Low-Emission Vehicle Exemption.** Instead of allowing the exemption of low-emission and energy efficient vehicles from high occupancy requirements and from HOT lane tolling expire, the bill extends the exemption through 2017.
- **Toll Discontinuation Authority.** The bill grants the Secretary the authority to order the discontinuation of tolls should a public authority not comply with the limitations on the use of toll revenues, until such time that an agreement is reached to achieve compliance. The threat of exercise of this authority by the Secretary could conceivably undermine toll revenue financing for projects, although we believe credit markets will accept the risk.