US WATER INFRASTRUCTURE

Trump's plan hatches reforms to boost private water

The blueprint released this month includes a host of canny policy shifts which could meaningfully improve the landscape for the private sector.

This month in the Americas:

After months of speculation, the Trump administration finally unveiled its controversial $1.5 trillion infrastructure plan on 12 February.

As anticipated, new federal money will only form a limited portion of the spending, but the plan proposes a suite of reforms which could have a lasting impact on the US water market – and the role of the private sector (*see table, facing page*). With the ability of state and local governments to shoulder a greater portion of the investment burden being called into question, however, the plan faces an uphill battle in Congress.

In principle, the plan would use $200 billion in federal grants to leverage state, local and private dollars over the next ten years to stimulate at least $1.5 trillion in total infrastructure investment.

To this end, the plan's main pillar is a $100 billion infrastructure incentives programme, in which federal money would be allocated as 'incentive grants', with the criteria for evaluating applications heavily weighted towards projects that tap "new, non-federal revenues" to cover capital costs and ongoing operations and maintenance.

The remainder of the $200 billion federal packet will be allocated to programmes for rural infrastructure and transformative high-risk projects, and will also include a $14 billion appropriation to existing federal credit programmes – including the Water Infrastructure Finance and Innovation Act (WIFIA).

In addition to these flagship programmes, the plan outlines a host of permitting and regulatory reforms designed to expedite infrastructure project delivery, and policy changes aimed at levelling the playing field between public and private finance, including a $6 billion budget allocation to improve and expand the eligibility of tax-exempt private activity bonds (PABs).

Level playing field

The removal of the state-level volume cap on the issuance of private activity bonds for water projects has long been a rallying point for the private water sector in the US, and it is reassuring that provisions to effect such changes were included prominently in this month's plan.

PABs are issued by public entities on behalf of private project developers, and their tax-exempt status puts them on a similar footing to municipal bonds. The move goes hand-in-hand with proposed change-of-use cures that would preserve the tax-exempt status of outstanding municipal debt when a private sector entity acquires or leases a municipal water system.

The ability to avoid the cost premium associated with defeasing tax-exempt debt could provide significant savings, resulting in more transactions being financially viable both for the private sector and for ratepayers.

By way of example, an analysis of a potential lease of Pittsburgh's water and sewer authority conducted by Barclays and Table Rock Capital demonstrated that maintaining the tax-exempt status of the authority's outstanding debt could result in a $90 million upfront cost saving.

"Of everything proposed in the plan, this is the piece that could really unlock P3 for a much broader swathe of systems," Megan Matson, a partner at Table Rock Capital, observed to GWI.

In a similar vein, the plan also proposes expanding the Clean Water State Revolving Fund (SRF) loan programme to privately owned wastewater treatment works, and modifying the Clean Water Act to apply identical regulatory requirements to both public and private facilities.

Private wastewater treatment facilities currently face more stringent and more costly regulatory requirements than their public counterparts, and by levelling the playing field, the plan would encourage investor-owned utilities to play a greater role in the wastewater side of the business.

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>
> Jill Jamieson, JLL

Federal infrastructure

The role of federal agencies in delivering and managing federally sponsored water resources infrastructure such as dams, reservoirs and flood management systems could also be poised for a shake-up. Significantly, the Trump administration's plan includes provisions to authorise the US Army Corps of Engineers (USACE) to more effectively partner with the private sector.

Although the Water Resources Reform and Development Act of 2014 created a USACE P3 pilot programme, Jill Jamieson, an attorney with law firm JLL, explained to GWI that USACE was not given the necessary authorisations at the time to put pen to paper on such projects.

The infrastructure plan goes some way towards addressing this shortcoming, particularly by allowing USACE to collect and retain user fees for water resources projects which could provide a revenue stream for a P3 contract.

"There needs to be a way to generate ring-fenced revenues and reinvest them back into projects," Jamieson told GWI. "That would open the door to a lot of P3s in many areas."

One anticipated reform absent from this month's blueprint is changes to Office of Management and Budget scoring that would allow federal agencies such as USACE and the US Bureau of Reclamation to enter into P3 contracts using an availability payment structure, which would be necessary when a user-pay model is not feasible. Currently, these contract structures are deemed to be capital leases, requiring the federal agency to budget the entire value of the contract up front, instead of as an annual operating budget outlay.

Jamieson argues that there is ample precedent in terms of OMB having made similar scoring changes for power purchase agreements and energy service contracts, and that facilitating water resources P3s in the same manner would be "emi- ▶

nently doable" by the executive branch.

The plan also outlines a route for divesting federal infrastructure assets that would be better managed by state, local and private entities. The plan refers to just one water infrastructure project as an example – the Washington aqueduct – but with agencies such as USBR faced with a portfolio of ageing water assets and little hope of budgetary relief, the plan could open the door to a wide-ranging divestiture of federal water resources infrastructure.

Creative funding

The fact that the new infrastructure plan is predicated on shifting more responsibility for infrastructure investment into state and local hands is likely to result in stiff opposition as the package is fleshed out in Congress. Municipal budgets are already strained, and recent cuts to state and local tax deductions as part of the federal tax reform package will make it even harder to raise additional revenues.

"The real challenge is how this will be articulated into legislation that is politically palatable to both sides of the aisle," Jamieson observed to GWI. "One of the big concerns we're already hearing is that the $100 billion incentive programme is great for cities and states that can afford to pay more, but what about the rural and poor communities that may not have sufficient access to revenue sources?"

Nevertheless, the focus on "new" non-federal funding routes could encourage water utilities to think more creatively about their sources of revenue, incentivising innovative rate structures and business models.

"It's going to require municipalities to be more creative in terms of how they package the 80% state and local prong to attract the 20% federal contribution," suggested Adam Krantz, CEO of the National Association of Clean Water Agencies, adding that this could result in alternative revenue streams – for example from resource recovery projects – becoming more attractive.

Rural water systems could also be faced with the same necessity to innovate, which could prove challenging, due to their more limited technical and financial capacity.

Although the plan allocates $50 billion in grants for rural infrastructure, it reserves $10 billion of this for rural "performance grants", which would be allocated to states that have developed comprehensive rural infrastructure investment plans demonstrating how their rural projects align with the same evaluation criteria as the infrastructure incentives programme.

Bill Teichmiller, CEO of EJ Water Cooperative, suggested to GWI that the intention here is to encourage the long-term sustainability of rural water systems – a process which is likely to contribute to the consolidation of the nation's 47,000 small water utilities.

Although the plan envisions an expansion of the WIFIA programme to provide financial assistance for water system acquisitions and restructurings – enabling it to serve as a "mechanism for consolidation in the water industry" – much of the onus for encouraging consolidation and regionalisation is likely to fall on the rural infrastructure investment plans developed by state governments. ■

TRUMP'S INFRASTRUCTURE PLAN AT A GLANCE

The 53-page document has a number of implications for the water sector. GWI examines the most relevant.

Infrastructure incentives programme
- » $100 billion in federal incentive grants to encourage increased state, local and private investment in infrastructure projects, including water resources, drinking water, wastewater, and stormwater facilities.
- » Evaluation criteria will be heavily skewed towards evidence that projects will secure "new, non-federal revenue" (weighted at 70%). Other criteria include the use of more efficient project delivery approaches (10%) and new technologies (5%). A final application score is then calculated by multiplying the weighted evaluation score by the percentage of non-federal revenues used to fund the project.
- » Incentive grants are contingent on predefined project progress milestones, and would not exceed more than 20% of total project costs.

Rural infrastructure programme
- » $50 billion allocated to states for capital investment in rural infrastructure projects, including water and wastewater.
- » $10 billion of this is reserved for performance grants for states that develop rural infrastructure investment plans which align with the same evaluation criteria as the incentives programme, including securing long-term, sustainable non-federal funding.

Transformative projects programme
- » $20 billion for ambitious high-risk infrastructure projects, including water and wastewater, that might otherwise struggle to secure private sector investment.
- » The programme would also provide technical assistance, while federal funds could support planning, piloting and capital construction phases.

Water Infrastructure Innovation and Financing Act (WIFIA) programme
- » Budget authority of existing programme extended, and current $3.2 billion lending limit removed.
- » Eligibility expanded to include additional project types such as flood mitigation and Superfund sites.
- » Authorises credit assistance for water system acquisitions and restructurings.
- » Eligibility expanded to include wholesale water facilities – e.g. desalination projects.

Private activity bonds
- » Eliminates state-level volume cap for water projects and expands eligibility to include flood control projects and stormwater facilities.
- » Eliminates alternative minimum tax preference on PABs to lower borrowing costs.
- » Change-of-use cures to preserve the tax-exempt status of government debt after an acquisition or lease.

Wastewater project policy reforms
- » Authorises the Clean Water State Revolving Funds (SRFs) to provide financial assistance to privately owned wastewater treatment works.
- » Applies identical regulatory requirements to privately owned and publicly owned WWTPs.

Federal water resources infrastructure
- » Authorises user fee collection and retention for an existing US Army Corps of Engineers (USACE) water infrastructure P3 pilot programme.
- » Expands USACE's authority to engage in long-term contracts.
- » Authorises the divestiture of federal infrastructure assets to state, local, or private entities.
- » Expands the authority to accept non-federal funds for water resources infrastructure investment.

Land revitalisation (Superfund/Brownfield programmes)
- » Create a Superfund revolving loan programme to provide low-interest funds for site remediation.
- » Allow sites on the Superfund National Priorities List to be eligible for Brownfield grants.

Permitting reforms
- » Institutes a "one agency, one review" federal environmental review structure with a 24-month firm deadline on completing reviews and issuing permits under the National Environmental Policy Act.
- » Increases the term of National Pollutant Discharge Elimination System permits from 5 to 15 years.

Source: The White House