

US water infrastructure financing

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19/03/2015

The US government wants to use the same methods that it used to attract private capital into its roads sector in financing its water sector. But its proposals so far have either been light on detail, or heavy on restrictions - or both.

In January 2015, President Barack Obama unveiled the Qualified Public Infrastructure Bond (QPIB). According to Obama, QPIBs would be a new type of municipal bond that would extend the benefits of tax-exempt private activity bonds to privately-operated solid waste disposal, sewer, and water facilities, as well as airports and ports.

The proposal was short on detail - but it explicitly excluded privately-owned facilities and those that are transferred to the private sector.

The 2016 budget that Obama sent to Congress had a little more detail on QPIBs. Alternative minimum taxpayers would still get tax relief on interest income from all QPIBs. And water projects would not count towards the per-state cap on tax-exempt issuance.

But the budget would eliminate the ability of privately-owned water projects to issue such private activity bonds. Given that previous budgets have proposed expanding the ability of privately-owned infrastructure projects to raise tax-exempt debt, the new proposals look like a step back.

Several market observers suggest that given that many PPP concessions leave assets in the nominal ownership of the public sector this ownership provision might not be too restrictive. But details from the administration have been limited, and the budget will struggle to make it through the Republican-controlled Congress.

Another financing tool already has congressional authority - but no budget.

Obama signed the [Water Resources Reform and Development Act \(WRRDA\)](#) into law in 2014. WRRDA, among other provisions, created the Water Infrastructure Finance and Innovation Act (WIFIA), a loan programme for water infrastructure projects costing more than \$20 million. Congress has not appropriated funds for WIFIA, which has not yet financed any projects.

PABs still on the menu

The [City of San Antonio in Texas and an Abengoa-led consortium](#) is developing a \$3 billion water distribution project that would be comfortably the largest US water PPP ever. It involves the design, construction, financing, operation and maintenance of new production wells, pumping stations, raw water collection, storage tanks and a 230km pipeline to deliver water under a 30-year concession.

One adviser close to the transaction suggests that the sponsors will use tax-exempt private activity bonds (PABs) to fund some of the cost, with the deal set to close later this year. "PABs or government bonds are favourable options in the current interest rate environment," the adviser says. "We don't see any signs of available WIFIA funding yet."

[The \\$980 million Carlsbad desalination project in California](#), was also financed with \$733 million of AMT and AMT-exempt tax-exempt bonds in 2012. San Diego County Water Authority was the offtaker for the Poseidon Resources-developed facility, which attracted an equity investment from Stonepeak Infrastructure Partners.

The city of Rialto in California transferred its water operations to a concessionaire owned by Table Rock Capital and Ullico, which closed a [\\$146 million taxable 4 \(2\) private placement](#) for the acquisition and upgrade in 2012. Veolia is the operator of the concession, and the city retains asset ownership, paying the project company a monthly fee for water services.

Old tools and new authority

For the larger municipally-owned and -operated water projects, tax-exempt debt has always been available. Projects smaller than \$20 million can raise financing through the US Environmental Protection Agency's Clean Water and Drinking Water State Revolving Fund (SRF) programmes.

The EPA and Army Corps of Engineers will administer WIFIA loans, whose interest rates would be based on US government borrowing costs, and have tenors of up to 35 years, with no repayment obligation until five years after substantial completion of the project.

WRRDA authorised an initial appropriation of \$20 million to each of the EPA and the Army Corps to cover the subsidy cost of WIFIA loans in 2015. This authority then increases every year to reach \$50 million for each agency in 2019.

The initial \$20 million allocation could potentially support over \$600 million in loans, and the \$50 million authorization for the final year could potentially support over \$1.5 billion in loans - but these appropriations are still pending.

While WIFIA is modelled on the US government's Transportation Infrastructure Finance and Innovation Act (TIFIA) loan programme, which has been a feature of almost every US road PPP. But the concept may not travel.

"The nature of transportation projects is very different from water projects," says David Moore, managing director and chief executive at advisory firm Clean Energy Capital. "While toll revenues cannot be guaranteed in road projects, water assets have more stable returns," he adds. TIFIA takes a more risky piece of the capital structure and allows it to be financed with attractive interest terms, but since water projects are less risky, WIFIA may not add huge value, he suggests. WIFIA loans, unlike TIFIA debt, cannot be combined with tax-exempt financing, such as PABs.

But the US water sector's financing needs are vast. Florida's Miami Dade county has just asked for expressions of interest in developing its [\\$150 million South Miami Heights water treatment plant](#) under a design, build, finance, operation and maintenance concession. At least 12 new desalination plans are under development in California, according to a 3 March 2015 report from Moody's.

US state and municipal governments are under less financial stress than six years ago, but are still coping with elderly infrastructure, and looking to find operational efficiencies. California's persistent problems with drought are the main reason for the large number of desalination projects in development. The growing cities of Texas like San Antonio need to import water from ever further away.

In the circumstances the financing tools will have to catch up with demand.

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