



## Testimony

# The Economic and Budgetary Effects of WIFIA and SRF-WIN

DOUGLAS HOLTZ-EAKIN | JULY 12, 2018

Chairman Barrasso, Ranking Member Carper and members of the committee. Thank you for the privilege of appearing today to discuss the economic and budgetary impacts of the Water Infrastructure Finance and Innovation Act (WIFIA) and Securing Required Funding for Water Infrastructure Now Act (SRF-WIN) programs. In what follows, I hope to make three basic points:

- The WIFIA and SRF-WIN programs allow relatively few federal dollars to support a very large base of water infrastructure investments.
- The economics of infrastructure investment are conceptually straightforward and are a natural function of the public sector.
- The federal budgetary treatment of these programs correctly identifies the budgetary resources made unavailable for other purposes, but sheds no light on the basic investment decisions supported by the programs.

Let me take these in turn.

## Overview of WIFIA<sup>[1]</sup>

The Water Infrastructure and Finance and Innovation Act (WIFIA) is a federal credit program administered by the Environmental Protection Agency (EPA) for eligible water and wastewater infrastructure projects. The WIFIA program works separately from, but in coordination with, the State Revolving Fund (SRF) programs to provide subsidized financing for water infrastructure for projects. The program was established by the [Water Resources Reform and Development Act of 2014](#) (WRRDA) and authorizes the EPA to provide federal credit assistance – in the form of capital loans – to a range of drinking water and wastewater projects. The WIFIA program can provide up to 49 percent of the anticipated eligible project costs, however, total federal assistance may not exceed 80 percent of a project's eligible costs.

Eligible borrowers of WIFIA loans include local, state, and federal government entities, partnerships and joint ventures, corporations and trusts, and Clean Water and Drinking State Revolving Fund programs. The WIFIA program funds for development and implementation activities – pre-construction activities, construction, reconstruction, rehabilitation, and replacement activities, and acquisition of real property – for eligible projects.

Eligibility is also contingent on project costs, public support, and creditworthiness. The project's eligible costs must be at least \$20 million. However, the threshold is lower for projects serving rural areas. Projects serving a population of 25,000 or less must have costs of at least \$5 million. Projects that are carried out by private entities must demonstrate that the community has been consulted and that the project has the support of affected state, local, or tribal government in which the project is located. In addition, projects applying for WIFIA credit

assistance must be creditworthy and must have a dedicated revenue source. If a project is selected to receive WIFIA assistance it must abide by National Environmental Policy Act, Davis-Bacon, Buy America, and all federal cross-cutter provisions.

## **Benefits of WIFIA Credit Assistance**

The volume of credit assistance offered through WIFIA is contingent on the size of congressional appropriations the subsidy rate of the eligible program. The EPA can use congressional appropriations for administrative purposes and loan subsidy costs – the estimated cost of default. Since the EPA is required to cover only the loan subsidy costs, a greater size of WIFIA credit assistance can be generated from the congressional appropriations. The Administration's Office of Management and Budget (OMB) estimated an average 1.55 percent subsidy rate for WIFIA projects in FY2018. OMB's estimated subsidy rate for WIFIA suggests that every \$1 of WIFIA contract authority, on average, will enable the EPA to issue \$102 in WIFIA loans (1:102 direct loan leverage ratio). Since WIFIA can cover up to 49 percent of project total costs, WIFIA appropriations could yield a total water infrastructure investment ratio of 1:208, on average.

Borrowers benefit from the low interest rates of WIFIA assistance and repayment schedule. The interest rate of the loan will be equal or greater to the U.S. Treasury rate of a similar maturity, thus lowering the cost of capital for borrowers beyond the cost of traditional tax-exempt municipal bond. Additionally, repayment on WIFIA loans may be deferred for a maximum of five years after the substantial completion of the project. However, the final maturity date of the WIFIA credit assistance shall be no later than 35 years after the date of substantial completion.

In FY 2015 and FY 2016, Congress appropriated \$2.2 million to the EPA to design and staff the WIFIA program. Enactment of the [Further Continuing and Security Assistance Appropriations Act of 2017](#) provided the first appropriation of funds to cover the subsidy costs of loans issued under the program. The Act appropriated \$20 million to the EPA to begin subsidizing gross obligations for the principal amount of loans and allows the agency to use \$3 million of the total for administrative costs. The Consolidated Appropriations Act of 2017 appropriated an additional \$8 million for credit subsidies raising WIFIA's total appropriations to \$25 million. For FY 2017, the WIFIA program selected 12 projects to apply for \$2.3 billion in WIFIA loans, which, in addition to private capital and other funding resources, will help to finance \$5.1 billion in water infrastructure investment.

For FY2018, the Consolidated Appropriations Act, 2018 (P.L. 115-141), provided \$63 million for the WIFIA program (including \$8 million for administrative costs). EPA estimated that its budget authority (\$55 million) would provide approximately \$5.5 billion in credit assistance, which could support an estimated \$11 billion in water infrastructure.

## **Overview of SRF-WIN**

The SRF-WIN Act amends WIFIA to provide to State infrastructure financing authorities additional opportunities to receive loans to support drinking water and clean water State revolving funds. It combines aspects of both WIFIA and State Revolving Funds (SRFs), building upon the leveraging concept in WIFIA to

provide new funds for State Infrastructure Financing Authorities to utilize.

## **The Economics of Infrastructure Investment**

The economics of public infrastructure are straightforward. Clean water, to take a concrete example, benefits everyone simultaneously. Once it is clean for one resident, it will be clean for all. For this reason, conventional private market methods work poorly in providing infrastructure and the public sector becomes involved.

That does not change the fact that the infrastructure is valuable and provides benefits to the population. If a \$100 infrastructure investment provides  $\$B$  on average annually in benefits to the population over its lifetime, the social rate of return on investments is  $\$B/100$  or  $b$  per year.

The resources to make this investment must be drawn from the private sector via taxes or borrowing. This reduces the funds available for private investment by a corresponding \$100, which eliminates a potential investment.

If the rate of return on the private sector investment is  $r$ , then the economics of infrastructure investment can be reduced to the canonical question: are the benefits greater than the costs. In this instance, is  $b$  bigger than  $r$ ? If so, it makes sense for public policy to engender infrastructure investment.

## **The Federal Budgetary Treatment of Infrastructure Investment**

The federal budgetary presentation bears essentially no resemblance to the core economic question in play for three reasons.

First, the budget process focuses on identifying costs of programmatic activities. It makes no attempt to quantify benefits or to systemically investigate the benefit-cost question. It simply addresses a different question.

Second, the focus is on federal budget cost. It is not attempting to measure the social cost of an infrastructure investment ( $r$  in the example above). Nor is it attempting to measure the costs borne by municipal governments, state governments, private sector investors, or any other participant in the infrastructure investment.

Third, it is focused on the costs of financing the investment. In the case of WIFIA and SRF-WIN the budget costs take two forms: (a) the subsidy cost that covers the probability of less-than-100 percent recovery of the initial infrastructure investment, and (b) the revenue forgone on taxing the return on private sector investments. In the federal budget context, this is entirely appropriate as these are measures of the budgetary resources made unavailable for other uses by funding WIFIA and SRF-WIN projects.

Thank you and I'd be happy to answer your questions.

Notes

[1] This section relies heavily on the WIFIA [primer](#) written for AAF by Brianna Fernandez.