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APR 17 2007

Honorable Stephen L. Johnson
Administrator
United States Environmental Protection Agency
1200 Pennsylvania Avenue, NW
Washington, DC 20460

Dear Administrator Johnson:

There is a long history of concern over the large shortfalls in infrastructure investment in the drinking water and clean water sectors. A 2002 EPA report estimated capital needs of $602 billion over a twenty-year period ending in 2019.[1] While this amount may be modest by comparison to the overall U.S. capital market, it has proven beyond the means of many local government providers of water services. The same EPA report found that current rates of capital spending in these sectors would fall short of infrastructure needs by some $224 billion over the twenty-year period.

The 1986 Tax Reform Act created a new category of bond--the private activity bond (PAB) -- which would be eligible, under certain conditions, for tax exempt status. The PAB category replaced an earlier provision for similar bonds, usually known as industrial development bonds (IDBs). The Act also set a substantially more restrictive limit, or cap, on the total volume of PABs which can be issued in a given State each year.

In its first-ever Advisory Statement to the Administrator[2], this Board argued that the unified State volume caps were constraining tax-exempt financing in a way that was limiting the supply and/or increasing the cost of investment funds for environmental facilities.[3] Accordingly, the Board recommended that bonds for environmental purposes be either (1) reclassified as government bonds or (2) specifically exempted from the State volume caps.

This recommendation was repeated several times in various forms during the following 16 years. In 1999, the Board advocated reclassifying all public-purpose bonds for water and wastewater projects as tax-exempt government

1 U.S. Environmental Protection Agency, "The Clean Water and Drinking Water Infrastructure Gap Analysis," Washington, D.C., September 2002.
2 Environmental Financial Advisory Board, "Incentives for Environmental Investment: Changing Behavior and Building Capital," U.S. Environmental Protection Agency, Washington, D.C., August 9, 1991.
3 Ibid., pp. 15-16.

bonds.[4] That same report also recommended a State volume cap exemption for watershed restoration bonds. In 2001, while addressing the need for increased participation by the private sector in providing environmental services, the Board identified the State volume cap on PABs as one of three major barriers.[5] At that time, the Board stated that:

"EPA should support the exemption of private activity bonds from state volume caps, whose proceeds finance public-purpose drinking water and wastewater facilities."[6]

It has now come to the attention of the Board that the President's budget for Fiscal Year 2008 includes a proposal that is virtually identical to the Board's 2001 recommendation. If adopted, the effect would be to exempt, from the unified State volume cap, qualified private activity bonds (PABs) used to finance the "furnishing of water" and/or "sewage facilities."

The Board continues to support the work of the Clean Water and Drinking Water State Revolving Funds, believing that they have already made, and will continue to make, a large contribution to closing the investment gap. However, much more needs to be done.

After reviewing the President's proposal, the Board concludes that its adoption will be another important step in the effort to finance needed water supply and wastewater infrastructure. We believe that the proposed exemption will increase the supply of capital for these purposes as well as lower the cost of capital to many of those communities already making use of private investment.

The Board expresses its full support for this proposed change in the tax law and is prepared to assist EPA in any way in its efforts to achieve this.

Sincerely,

A. James Barnes
Chair

4/04/07

A. Stanley Meiburg
Designated Federal Official

cc: Benjamin Grumbles
Assistant Administrator for Water

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4 Environmental Financial Advisory Board, "Recommendations and Final Report on Financing Opportunities for the Clean Water Action Plan," U.S. Environmental Protection Agency, Washington, D.C., July 1999, p. 12.

5 Environmental Financial Advisory Board, "Private Sector Initiatives to Improve Efficiencies in Providing Public-Purpose Environmental Services," U.S. Environmental Protection Agency, Washington, D.C., June 2001, pp. 6-8.

6 Ibid., p. 9.