

Expanding Private Activity Bonds for Major Transportation Projects

Surface transportation Private Activity Bonds (PABs) are tax-exempt bonds first authorized by Congress in 2005 as part of the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU). Their purpose is to create a level financial playing field for highway and transit projects developed under long-term public-private partnership (P3) agreements. Traditional state and local government-financed transportation projects routinely use tax-exempt municipal bonds, which have lower interest rates than the taxable bonds historically available for privately financed projects. Thus, tax-exempt PABs enable the financing costs for P3 projects to be nearly the same as for traditional government-financed projects.

Prior to the advent of PABs, transportation P3 projects were few and far between. The early projects relied on bank debt, at typical bank loan interest rates. Only three such projects were financed between 1995 and 2007. Between 2005 (when PABs were authorized) and 2023, there were 14 highway P3 projects financed by revenue and 12 highway and transit P3 projects financed based on availability payments. PAB-supported P3 projects have been implemented in 13 states, from California to Virginia.

The original PABs legislation included a cap of \$15 billion worth of such bonds. By 2020, as more states began implementing P3 surface transportation projects, the cap was on the verge of being reached. In the Infrastructure Investment and Jobs Act (IIJA) of 2021, Congress increased the cap to \$30 billion. Since then, the demand for P3 projects has increased dramatically. There are at least \$31 billion of P3 project construction costs expected to reach the financing stage over the next several years. Yet, as of June 1, 2025, DOT's Build America Bureau estimated that the remaining PABs capacity was only \$500 million.

Congress could increase the surface transportation PAB cap again in the forthcoming reauthorization, but the better option would be eliminating the cap altogether. When the original legislation was enacted in 2005, PABs were seen as an experiment, and it took 16 years before the original \$15 billion cap was reached. But in only four years, the added \$15 billion is already close to being allocated. Surface transportation PABs are no longer an experiment and should now be mainstreamed as a proven tool for financing transportation P3s.

Removing the cap on PABs was first suggested by the bipartisan Special Panel on Public-Private Partnerships convened by the House Transportation and Infrastructure Committee in 2014. That panel also suggested that transportation PABs be extended to projects at airports and seaports. These proposals were endorsed as part of the Trump administration's first-term infrastructure plan, "Legislative Outline for Rebuilding Infrastructure in America," released in February 2018.

It is important to understand that transportation PABs are non-recourse bonds. They are obligations of the P3 entity: neither federal nor state taxpayers are at risk if the bonds run into trouble. Equity investors and bond-buyers alike understand this point, and they have no basis for expecting a federal or state bailout in the event of revenue shortfalls.

Both the U.S. Treasury and Congress's Joint Committee on Taxation (JCT) often express concern about expanding the scope for tax-exempt bonds. Their concern is that projects that get financed via PABs would likely otherwise be financed via taxable bonds, so the Treasury would be losing revenue from such taxable bonds. But evidence suggests this assumption is incorrect. The very slow progress of transportation P3 projects between 1995 and 2007 suggests that the private sector rejected the alternative of using taxable bonds. The few large surface transportation projects that took place during those 12 years were evidently financed by state and local governments using traditional tax-exempt municipal bonds—which are not subject to any volume cap.

Contrary to the assumptions of the Treasury and JCT, eliminating the PABs volume cap and expanding eligibility could increase federal tax revenue. The \$62.5 billion invested in transportation P3 projects through 2023 via infrastructure developers and infrastructure investment funds is expected to lead to profits for these entities, resulting in their paying federal corporate income taxes. These projects are designed, built, financed, operated, and maintained by companies from this new industry, with project terms ranging from 35 to 70 years. There is every expectation that this new industry will be an ongoing source of federal corporate income tax revenue.

Recommended legislative reform text:

- (a) Section 142(a)(15) of the Internal Revenue Code of 1986 is amended by striking “qualified highway or surface freight transfer facilities” and inserting “qualified transportation facilities”.
- (b) Section 142(m) of the Internal Revenue Code of 1986 is amended as follows:
 - “(m) Qualified transportation facilities
 - (1) In general
 - For purposes of subsection (a)(15), the term “qualified transportation facilities” means—
 - (A) any surface transportation project which receives Federal assistance under title 23,

United States Code (as in effect on the date of the enactment of this subsection),

- (B) any project for an international bridge or tunnel for which an international entity authorized under Federal or State law is responsible and which receives Federal assistance under title 23, United States Code (as so in effect),
- (C) any facility for the transfer of freight from truck to rail or rail to truck (including any temporary storage facilities directly related to such transfers) which receives Federal assistance under either title 23 or title 49, United States Code (as so in effect).
- (D) any airport project which receives Federal assistance under title 49, United States Code (as so in effect), or
- (E) any port infrastructure project which receives Federal assistance under title 46, United States Code (as so in effect).

(2) Allocation by Secretary of Transportation

Financing for qualified transportation facilities provided under this subsection shall be allocated by the Secretary of Transportation in such manner as the Secretary determines appropriate.

(3) Expenditure of proceeds

An issue shall not be treated as an issue described in subsection (a)(15) unless at least 95 percent of the net proceeds of the issue is expended for qualified transportation facilities within the 5-year period beginning on the date of issuance. If at least 95 percent of such net proceeds is not expended within such 5-year period, an issue shall be treated as continuing to meet the requirements of this paragraph if the issuer uses all unspent proceeds of the issue to redeem bonds of the

issue within 90 days after the end of such 5-year period. The Secretary, at the request of the issuer, may extend such 5-year period if the issuer establishes that any failure to meet such period is due to circumstances beyond the control of the issuer.

(4) Exception for current refunding bonds

Paragraph (2) shall not apply to any bond (or series of bonds) issued to refund a bond issued under subsection (a)(15) if—

- (A) the average maturity date of the issue of which the refunding bond is a part is not later than the average maturity date of the bonds to be refunded by such issue,
- (B) the amount of the refunding bond does not exceed the outstanding amount of the refunded bond, and
- (C) the refunded bond is redeemed not later than 90 days after the date of the issuance of the refunding bond.

For purposes of subparagraph (A), average maturity shall be determined in accordance with section 147(b)(2)(A).”.