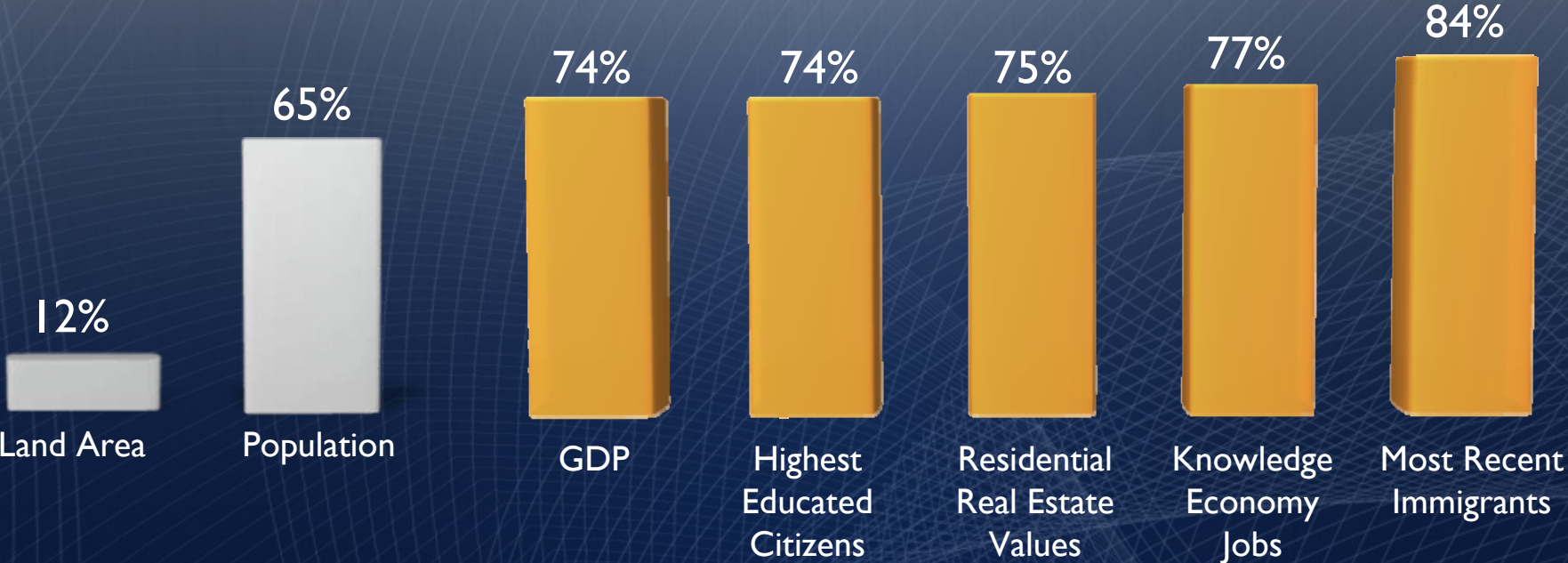


The Federal Capital Budget and Lessons for a National Infrastructure Bank

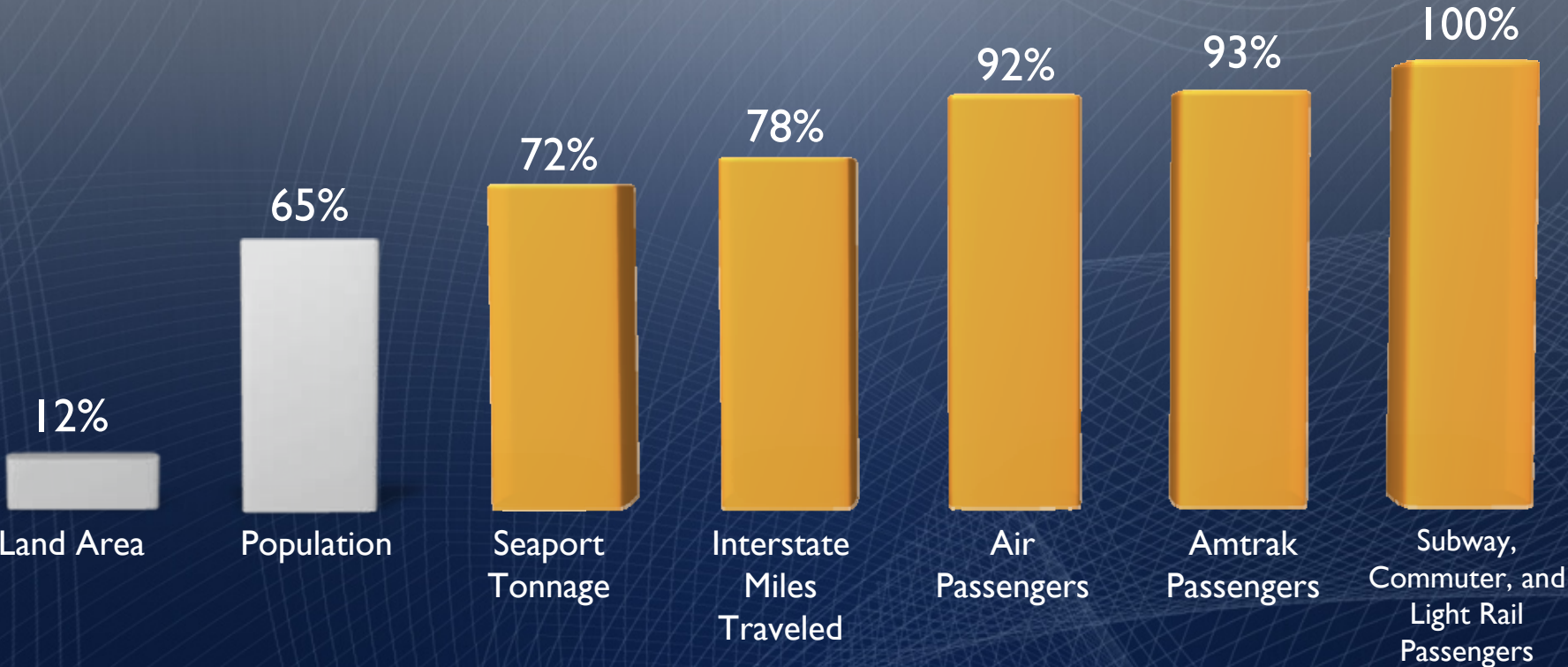


Our Country's Top 100 Metros – Engines of Growth



Source: Brookings Analysis

Our Country's Top 100 Metros – Concentrate Most of Our Transportation Functions



Source: Brookings Analysis

**Any infrastructure reform,
including the way how we
finance our roads and dams,
will have a major impact on
our metro areas.....**



The Federal Capital Budget and Lessons for a NIB

I

What Is a Federal Capital Budget and Why Should We Care About It?

II

In What Should the Federal Government Invest?

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Does the Current Federal Budget Appropriately Allocate Resources for Capital Projects?

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Lessons for the National Infrastructure Bank

What Is a Federal Capital Budget?

- **Basic segmentation model** – simple separation of federal capital spending from current expenditures;
- **Capital debt budget model** – capital spending be financed, in part or in total, by borrowing and the capital budget deficit would not count towards the total federal deficit;
- **Depreciation model** – only the depreciation would appear in the annual federal spending;
- **Fusion model** – combination of previous models.



Why We Should Care About a Federal Capital Budget?

The federal capital budget proposals aim to:

- Improve the public's understanding of fiscal policies
- Gain public acceptance for increased federal investment and borrowing for federal investment
- Shield federal investment from growing current expenditures
- Avoid the problem of spikes in federal investment

I A “Budget Reform Perennial”

Federal capital budget proposals have been debated for more than half a century with no political success.

- 1949 – the first Hoover Commission
- 1967 – the Budget Concepts Commission
- The 1980s – strong supporters – President Reagan’s Treasury Secretary Donald Regan and Martin Feldstein, Chairman of the Council of Economic Advisers
- 1996-1999 – President Clinton’s Commission to Study Capital Budgeting



In what Should the Federal Government Invest?

Federally- financed capital

Capital owned by the federal government and capital belonging to local and state governments but financed by the federal government.

- 2008 – \$1,683 billion – the net federally financed nondefense physical capital stock:
 - 25% federally owned
 - 75% state and local capital financed by federal investment

In what Should the Federal Government Invest?

Federal Investment

Federal annual spending on federally financed capital.

- 2008 – \$ 459.7 billion in total; \$253.8 billion nondefense investment, out of which:
 - 50% in federal assets
 - 50% in state and local assets



Purpose of Investment – Federal vs. National Capital

The Federal capital contributes to the federal government's ability to provide governmental services

- It is the sum of physical assets owned by the federal government
- Examples: office buildings, computers, and weapons systems



Purpose of Investment – Federal vs. National Capital

The National capital contributes more directly to the economic growth of the private sector

- Most of the capital in this category is not owned by the federal government
- Examples: highways, federally funded research and development and education



Both Definitions of Capital Have Problems

- **Federal capital** – safe choice for a federal capital budget
 - The federal government has control over these assets
 - The maintenance is included in the full lifecycle cost of a capital asset
- **HOWEVER ...**
 - It does not necessarily contribute to the productivity and growth of the private sector
 - Excludes the capital not belonging to the federal government and intangible assets



Both Definitions of Capital Have Problems

National capital targets the economic growth of the private sector

HOWEVER ...

- There are accounting problems with the inclusion of capital not owned by the federal government
- Federal government has limited control over the grants to state and local capital assets
- No uniform treatment of capital and maintenance across states

Federal Investment in Infrastructure Is a Fraction of Federal Spending

2008 (in billions of dollars)

Federal spending, 100.0% (\$2,983)

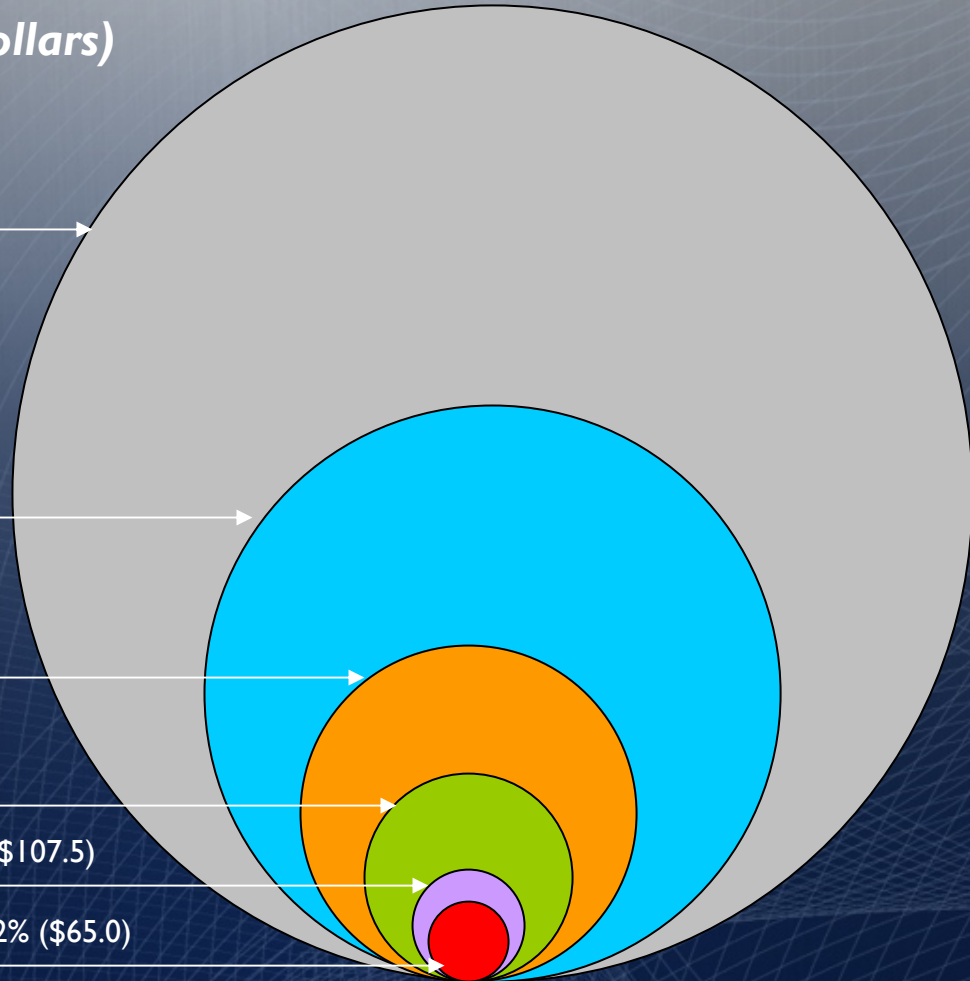
Discretionary spending, 38.0%
(\$1,135.0)

Federal investment, 15.4% (\$459.7)

Nondefense federal investment, 8.5%
(\$253.8)

Public civilian capital investment, 3.6% (\$107.5)

Federal investment in infrastructure, 2.2% (\$65.0)



Contract Authority Shields Most of the Federal Investment in Infrastructure

More than 75% of the federal investment in infrastructure is transportation grants to states (\$50.4 billion in 2008)

Protected:

- DOT can obligate funds in advance of appropriations made by Congress
- Congress may control the annual spending through a limitation on obligations, but it is hard to reduce it

Contract Authority Shields Most of the Federal Investment in Infrastructure

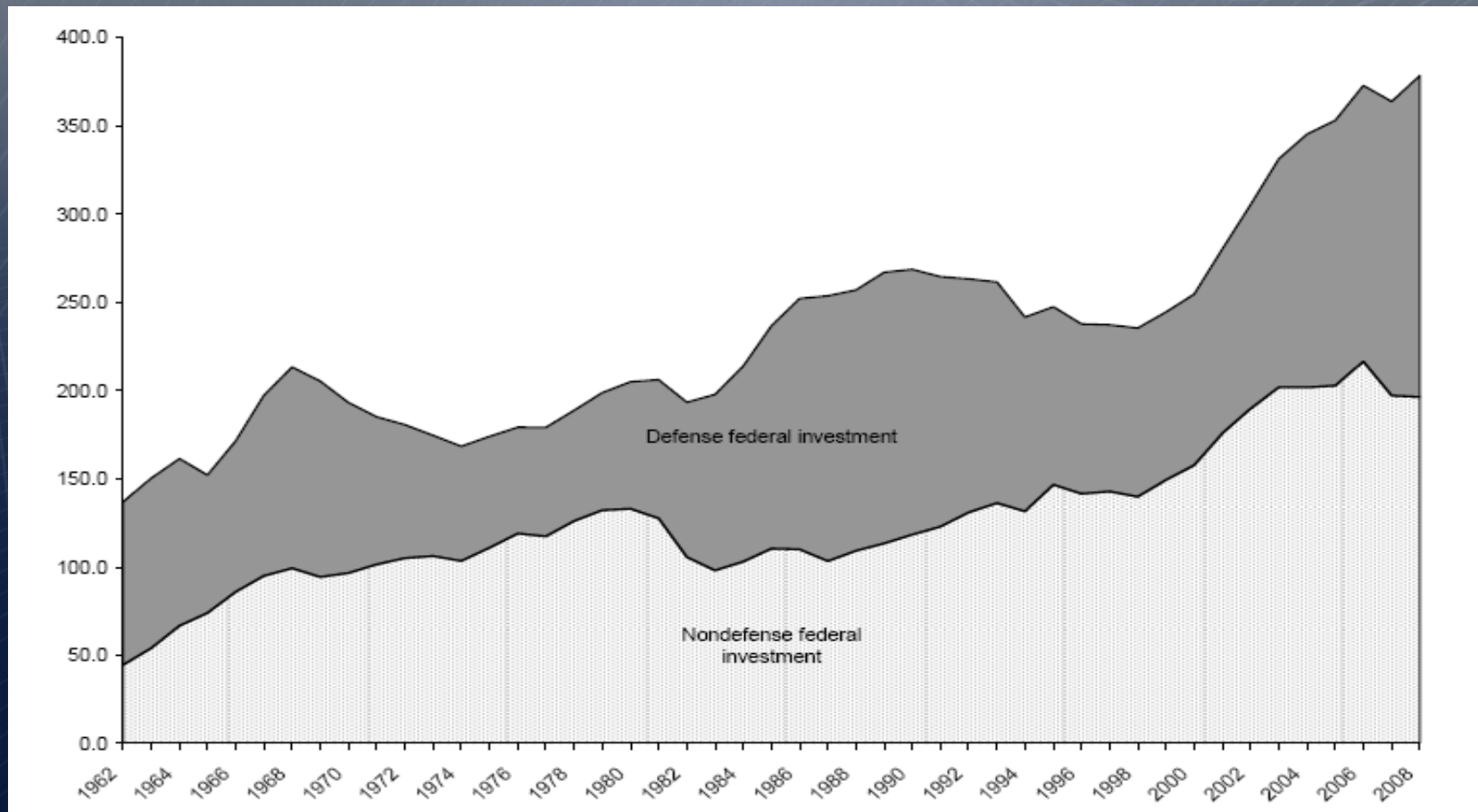
In addition, the highway and mass transportation spending is protected by:

- Budgetary firewalls (Section 8003 of SAFETEA-LU)
- Point of order included in the Rules of the House of Representatives, protecting the amounts guaranteed by the budgetary firewalls (Section 8004 of SAFETEA-LU)



Are the Current Federal Investment Rates Sufficient?

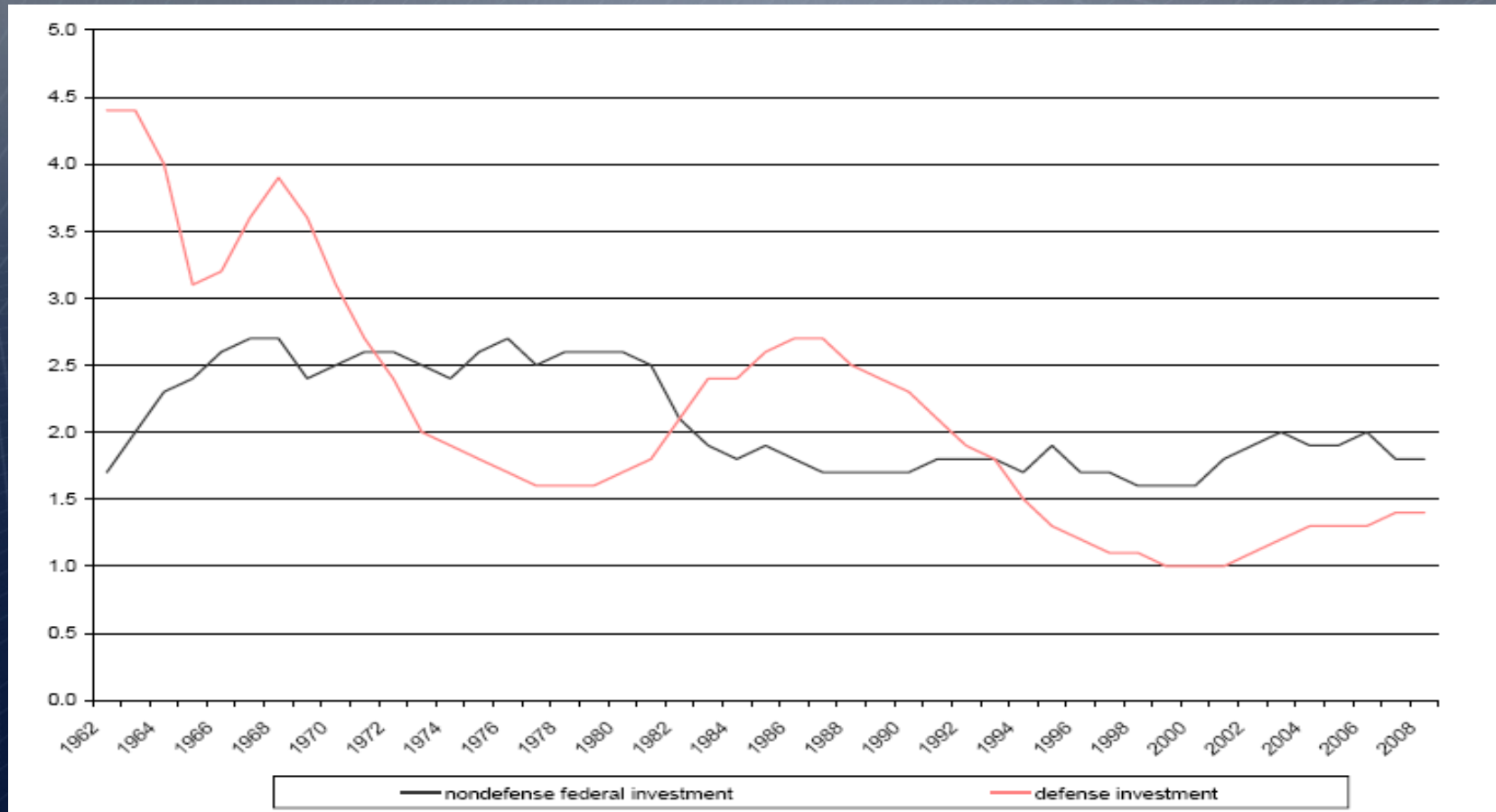
Real Federal Investment – Nondefense and Defense, 1962- 2008, billions of constant (FY 2000) dollars





Are the Current Federal Investment Rates Sufficient?

Federal Investment – Nondefense and Defense Investment, 1962- 2008
(as percent of GDP)





Are the Current Federal Investment Rates Sufficient for WHAT RESULTS?

- “Top-down” evidence – federal investment has a modest impact on economic growth
- “Bottom-up” evidence – based on benefit-cost analysis for individual projects
- CBO’s 1998 analysis on data obtained from the Federal Aviation Administration and the FHWA
- Most projects – net costs or small net benefits, very few large benefits projects



Are the Current Federal Investment Rates Sufficient for WHAT RESULTS?

Increasing federal investment
indiscriminately would not produce the
desired large positive effect of the federal
investment on the economy

IV

Does the Current Federal Budget Appropriately Allocate Resources For Capital Projects?

- ***Insufficient long term planning***
 - Lack of accountability for the long run implementation of the budget
- ***Bias against maintenance***
 - Federal money for new construction does not have conditions on states to adequately maintain those assets
- ***Full budgeting***
 - Appropriations for the full costs of the asset be enacted in advance of any obligations incurred by the federal agency
 - Spikes in federal spending



Would the Capital Process Be Improved by the Introduction of a Federal Capital Budget?

Capital expenditures and borrowing

- If only the operating expenditures are taken into account for the calculation of the federal deficit- the size of the federal deficit would vary depending on what the Administration considers federal investment
- If only the capital expenditures financed by debt- more debt on top of an unbalanced operating budget

V

Would the Capital Process Be Improved by the Introduction of a Federal Capital Budget?

Depreciation

- Mismatch between federal obligations and appropriations
- No federal method of depreciation
- Mix of accrual with cash measures in the federal budget
- More difficult to estimate the short-term macroeconomic effects of the federal fiscal policy

V

Would the Capital Process Be Improved by the Introduction of a Federal Capital Budget?

Political and bureaucratic issues

- How the appropriation process would change if a federal capital budget is enacted
- How the federal agencies would deal with the federal grants for states
- Power play among federal agencies and different Congress committees on the decisions upon the accounting and budgeting issues

What's in the:

- National Infrastructure Development Bank Act (NIBDA) 2009
- The 2010 Budget

Design

- Wholly owned Government corporation – (NIBDA) 2009
- Designated federal entity – The 2010 Budget

What's in the:

- National Infrastructure Development Bank Act (NIBDA) 2009
- The 2010 Budget

Products

- Grants, loans, loans guarantees, or long term project specific bonds
- For infrastructure projects “of substantial regional and national significance”

Capital

- Paid in capital of \$25 billion over five years through appropriations

Object of investment: less budgetary conundrums than a federal capital budget investing in the national capital

- Focused only on physical infrastructure
- The bank would be a centralized mechanism to compare and prioritize infrastructure projects based on a benefit-cost analysis

Sufficient investment: likely guarantee an increase in federal spending on infrastructure

Better delivery: missing in the federal capital budget

- Money on a project basis, after a benefit cost analysis
- Projects of national or regional significance

Political appeal: needed sufficient or simultaneous support from both Congress and the Administration.

- The NIB has support from both the White House and the House currently

Conclusions

The federal capital budget

- Ambitious and wide-ranging
- Never managed to muster all the necessary political support in Congress and from the White House
- Comes with more problems than solutions

Conclusions

The National Infrastructure Bank

- Smaller and more focused than the federal capital budget
- Designed appropriately, it would have:
 - A clear object of investment
 - An articulated goal
 - It would be a more effective way to finance infrastructure

The Federal Capital Budget and Lessons for a National Infrastructure Bank

