ILLINOIS FINANCE AUTHORITY

To: Members of the Authority

From: Eric Anderberg, Chair, Illinois Finance Authority (Authority)
Chris Meister, Authority Executive Director

Date: November 9, 2017

Re: **Impact of Section 3601 of Subtitle G of HR 1 (Section 3601; eliminates Private Activity Bonds or "PABs" from federal tax law) on the public mission and finances of the Authority.**

Background

We have had a lot of time to act and to think about the above issue since the morning of November 2, 2017. Like the market participants (many of whom have more skin in the game than us) and some appropriately placed congressional staff, we were surprised. On October 10, 2017, we were in DC and while we were cautioned that anything could change at any time, PABs were not on the table for federal tax reform.

State of Play

It does not appear that any amendments to HR 1 will be allowed on the house floor. Ways and Means is voting on amendments, including at least one addressing PABs.

The Senate version is likely to be out later this morning. We knew from the start that the House and Senate would each take up their own tax reform bill for starters.

The Senate cannot use the reconciliation process to pass a bill that does not meet Byrd limits. So the House can pass its bill, Senate can pass its Byrd-compliant bill, and the differences will have to be worked out in conference. What is produced by conference committee also has to be compliant with reconciliation rules in order to pass the Senate and become law.

The current congressional session ends on January 3, 2019.

Who we are

The elimination of PABs by Section 3601 of Subtitle G of HR 1 has caused us to us to think deeply about the public mission and finances of the Authority.

In short, we are stewards of a public utility that operates on a margin business within a relative value market. The proposed elimination of PABs eliminates the margin of economic value that the Authority and all PABs market participants provide. While PABs have many allies, PABs are not likely on the top of anyone elseȏs ȉdo or dieȋ list but PABs should be. For example, the Authority is currently run by thirteen volunteer board members, twelve employees and four temporary staff, but it is difficult to think of a similar sized organization that has such disproportionate positive impact on Illinois.

A 2013 national economic study by NAHEFFA (the Authority is a member) estimated that the elimination of PABs (non-profit only) would:

- Cost non-profits an additional $166.3 billion in interest expenses
- Reduce the national gross domestic product by $23.6 billion
- Lose just over 299,000 jobs generating $15.6 billion in labor income

Anticipated questions and answers

1. Percentage of the Authorityôs current bond portfolio that will be affected by the proposed elimination of PABs, if any?

   Answer: Approximately $24B of the Authorityôs $25B portfolio of outstanding conduit bonds qualify as ñprivate activity bondsò (PABs) that would be eliminated under Subtitle G of Section 3601 of HR 1.

   PABs represent approximately 96% of the Authorityôs current outstanding conduit bond portfolio.

   Outstanding bonds would not be impacted. However, if there is the refinancing or re-issuance for federal tax purposes of outstanding bonds, assuming HR 1 becomes law as of 1/1/18, these bonds would likely be taxable. After the effective date, the Authority would not be able to issue new PABs on behalf of its borrowers.

2. Rough, ballpark projections on how the elimination of PABs might affect the Authorityôs future revenue models?

   Answer: For FY 16 and FY 17, PABs have accounted for approximately 66% of the Authorityôs revenue (average operational expenditures approximately $4 million annually). The Authority is self-supporting mainly through fees charged at closing of PABs. In past years, before the expansion of the Clean Water Initiative/State Revolving Fund on behalf of IEPA (initially 2013 but really accelerating and expanding 2016-present ï currently $1.2 billion outstanding) and the 2014 defeasance (with Authority funds) of the State taxpayer-backed moral obligation local government bond portfolio as well as considering any one-time unanticipated revenues, the Authorityôs revenues derived from one-time fees (paid at closing as opposed to annual fees) from the issuance of PABs accounted for between 55% and 79% depending on the year and the one-time events.

3. Does the HR 1 repeal of PABs impact the IEPA Clean Water Initiative ï State Revolving Fund (CWI/SRF)?

Answer: No. The Authority would continue to be able to issue bonds consistent with IEPAôs current capacity/leverage plans. GOMB confirmed this as well. The Authorityôs current outstanding CWI/SRF portfolio is $1+B.

4. Does the Authority have a potential ñgoing concernò issue with respect to a potential revenue decline due to the elimination of PABs?
   Answer: No. The Authority has sufficient reserves held independently of the State budget that would allow continued operations for a period of time. The Authority has plans for revenue and mission diversification but these are untested. The Authority has shared this view with its board, staff team and external auditors.

5. Is there any other way that the Authority should be thinking about this?

   Answer: PABS are driven by the private sector ï both private (mainly non-profit) borrowers and private borrowers. PABs already effectively use the discipline of the capital markets to allow qualified borrowers to do what government would otherwise have to do (and pay for) ï or would remain undone. PABs have large social benefit with a very light government footprint. It would be irresponsible to abandon this effective tool, especially for unknown and untested theories.

   Any modest federal savings (nationally - $38.9 billion) expected from the elimination of PABs would be dwarfed by the tremendous value of the projects they have generated and continue to generate for communities throughout Illinois. The work of an MIT economist, Dr. James Poterba (Mitsui Professor of Economics at MIT and President of the National Bureau of Economic Research (NBER)), indicates that the federal revenue impact may be 40% to 50% lower ($19.4B to $23.3B) than the federal JCT estimate of $38.9B. In short, the elimination of PABs is a high damage/high cost and low or minimal return policy choice.

   While the Authority regularly works with very large numbers, reports as of late November 8, 2017, indicate that the Bryd deficit cap is $1.5 trillion and that HR 1 is currently $300B over this limit.

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To: Members of Congress and Staff
From: Eric Anderberg, Chair, Illinois Finance Authority (Authority)
Chris Meister, Authority Executive Director
Re: **TAX BILL PROVISION WOULD REMOVE A TOOL FOR FINANCING INFRASTRUCTURE AND NOT-FOR-PROFITS**

As an active participant in growing the Illinois economy, the Authority, an autonomous and self-supporting public entity, fully recognizes our nationǿs need for federal tax reform, and we appreciate and respect the difficulty and complexity of accomplishing this goal.

We are writing to inform you about the impact that one provision of the proposed law will have on Illinois.

Section 3601 of Subtitle G of H.R. 1 will remove a job retention and creation tool **--** federally tax-exempt infrastructure or ñprivate activity bondsò (PABs) **--** that allows charities and 501(c)(3) organizations such as:

- hospitals and health systems[1],
- schools ï research universities and colleges as well as charter and other private schools[2],
- museums and cultural institutions[3], and
- organizations that provide housing for seniors, students and working people[4]

to finance their capital infrastructure projects at generally lower interest rate and a longer maturity ï and to create long-term economic value for communities throughout Illinois. PABs also allow a small number of other qualified entities (small farmers and manufacturers, safe waste disposal, and logistics facilities of regional importance[5]) to do the same. **THE AUTHORITY DOES NOT FINANCE PROFESSIONAL SPORTS STADIUMS.**

At a time when lawmakers are searching for new ways to finance infrastructure, PABs already effectively use the discipline of the capital markets to allow qualified borrowers to do what government would otherwise have to do (and pay for) ï or would remain undone. Eliminating this tool would seem to be at odds with efforts to use every federal tax dollar to greatest public advantage.

To date, they have helped to leverage a relatively small federal tax exemption[6] into billions of dollars in state and local development. In just our state, Illinois, the Authority has used these bonds to finance the construction of over $24 billion in essential infrastructure projects **--** over $3.6 billion in State Fiscal Year 2017 alone.

The modest federal savings expected from the elimination of PABs would be dwarfed by the tremendous value of the projects they have generated and continue to generate for communities throughout Illinois and the nation.

We hope this information is helpful to you as you assess the merits of the important legislation. Please donǿt hesitate to contact Chris Meister (312-590-1044 or cmeister@il-fa.com or www.il-fa.com) if you have any questions about the Authority or the impact Section 3601 of H.R. 1 might have on its work in your district.

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[1] Including but not limited to Advocate, Northshore University, Northwestern, Lurie Children's, University of Chicago, OSF, Presence, Rush, Southern Illinois Health, Harrisburg, Silver Cross, Unity Point, Edward Elmhurst, Rehabilitation Institute, MercyRockford, Blessing (Quincy), Springfield Memorial, Hospital Sisters, Loyola, Sarah Bush Lincoln (Mattoon), Ingalls, Illinois Valley, Passavant (Jacksonville), Sinai, Carle, Swedish Covenant, Northwest Community, Norwegian American, Riverside
[2] Including but not limited to DePaul, Loyola, Bradley, North Central, Noble Network Charter, Intrinsic Charter, Mt. Carmel, Providence St. Mel, Elmhurst College, Midwestern University, IIT, Solomon Schechter Day Schools, Illinois Wesleyan
[3] Including but not limited to Cantigny Foundation (closes 12/17), Art Institute of Chicago, Field Museum, Science and Industry
[4] Including but not limited to Better Housing Foundation, Collegiate Housing Foundation (DeKalb, Normal, Chicago), Plymouth Place, Friendship Village, Presbyterian Homes, Three Crowns, Franciscan Communities, Bethesda Home, Clare Oaks
[5] Including but not limited to CenterPoint Joliet, Freedman Seating, Kuusakoski, Bison Gear, Camcraft, Inc., Beginning Farmers
[6] JEC estimates savings of elimination of PABs in all states at $38.9 billion over ten years. W&M Committee Majority Tax Staff, p. 48, November 2, 2018