U.S. Department of Transportation
Office of the Secretary of Transportation

400 Seventh St., S.W.
Washington, D.C. 20590

File DOT

Read for James

Diverted

FAX COVER SHEET

DATE: 1/12/96

TO: LAURA TYSON

FROM: SECRETARY PEÑA

MESSAGE (IF ANY):

NO. OF PAGES, INCLUDING COVER: 5

THE SECRETARY OF TRANSPORTATION
WASHINGTON, D.C. 20590

January 12, 1996

M E M O R A N D U M

TO: Laura D'Andrea Tyson

FROM: Federico Peña Federico Peña

RE: Transit Elements of NEC Urban Initiative

You and I spoke briefly several days ago about the idea of including targeted mass transit incentives in the urban-oriented initiatives package being developed by your staff. Since our conversation was so brief, I wanted to supply you with additional details.

Under Paul Dimond's leadership, the NEC-directed working group has done a terrific job of developing a range of options for the President's consideration. Many of these ideas have the potential to achieve dramatic and positive impacts on our cities. Like other officials who participated in the recent meeting of NEC principals, I am especially enthusiastic about the Brownfields redevelopment concept and related proposals to encourage redevelopment of unused land around ports and other central city infrastructure.

At the same time, I believe it is essential for us to include something for transit in the package. Mass transit is a symbol of distinctively urban government activities. But transit was hard hit in the FY 96 Federal budget; and because Congress sought to protect small city and rural transit systems, big city mass transit took a 48 percent cut in Federal operating assistance. Combined with widespread and significant reductions in state aid, this has prompted fare hikes and service reductions in major cities, including New York, Los Angeles, Oakland and the Chicago area. Mayors are facing difficulty in preserving this high visibility local government service.

We recognize that funds are limited, so we are not proposing additional appropriations or revenue-negative tax changes. Instead, we have suggested a package of tax-related ideas that would help transit and other urban transportation operators raise more **private investment**. The tax changes we propose could be implemented within existing state volume caps for private activity bond financing so there is **no loss of revenue to the Treasury**. These proposals are very much in line with the Administration's emphasis on reinvention and on encouraging inner city redevelopment through private sector investment.

Attached is a staff memorandum outlining several specific proposals. I hope you will be able to include some or all of them in the final package of urban initiatives that goes forward to the President. Paul Dimond and Ellen Seidman of your staff are meeting with staff of DOT and Treasury on Tuesday to discuss other urban policy proposals. It would be helpful if these discussions could include the transit-related proposals as well.

I appreciate your leadership in this important effort. Please let me know if you require further information or materials.

attachment

U.S. Department of Transportation
Office of the Secretary of Transportation

400 Seventh St., S.W.
Washington, D.C. 20590

To: Mozelle Thompson
Deputy Assistant Secretary for
Government Financial Assistance
Department of Treasury

From: John N. Lieber
Deputy Assistant Secretary
for Transportation Policy

Date: January 5, 1996

Re: Public Transit and Highway Urban-Oriented Tax Policy Ideas

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Following up on our meeting earlier this week, I have outlined a few additional mass transit-related tax proposals that we would like to see incorporated in an Urban initiative. These ideas are geared toward attracting more private capital to invest in urban infrastructure at little or no cost to the government, at a time when Federal transit funding is being dramatically reduced --- with dramatic impacts in terms of fare hikes and service cuts. None of these ideas require increasing state tax-exempt debt volume caps, so there need not be an associated loss in Federal revenues. However, they would dramatically improve the ability of urban infrastructure -- and especially mass transit -- to utilize private investment capital.

Tax-Exemption for Leased Transit Rolling Stock

To minimize their cash flow requirements, many transit agencies lease rail cars from private owners, rather than buying the equipment outright. Under current tax rules, the owners of the equipment may not use tax-exempt debt to purchase the rolling stock, even though it is destined for public use. In order to prevent "double-dipping" (i.e. allowing equipment owners the tax benefits of both depreciation and tax-exemption), the tax rules effectively drive up lease costs for transit agencies. The tax rule also hurts U.S. equipment manufacturers, because transit agencies are turning to "cross border" leases with German, Japanese, Swedish and Canadian equipment companies, rather than buying from U.S. companies.

A potential proposal is to waive this tax rule for rolling stock leased by transit agencies. If the tax-exempt debt is counted against a state's existing volume cap, this proposal would impose no additional cost on the U.S. Treasury.

Tax-Exemption for Public-Private Highways

Central cities and inner ring suburbs often generate enough traffic to support privately-funded toll roads. Under current tax rules, public-private roadways (most of which are toll roads in urban areas) cannot issue tax-exempt debt. Because of this, many public-private road projects do not get built, and states end up using more of their ISTEA urban funding allocation for publicly funded roads, crowding out other urban projects (e.g. transit).

By amending the tax rules to permit tax-exemption for public-private roadways, we could effectively free up more ISTEA urban money for non-highway uses, which would be of great benefit to urban transit.

Tax-Exempt Bonds for Transit Joint Development

Currently, transit facilities may be financed with tax-exempt debt, but there is a 5 percent cap on the share of bond proceeds that can be used for non-transit purposes, such as joint development of retail or commercial space in a transit station. This interferes with projects that can both generate revenue for transit agencies and promote Livable Communities. The tax code could be altered to increase the 5 percent to some higher level, such as 25 percent.

Sale of Assets -- Federal Reimbursement Rule

Currently, when a city, an airport, a highway department or a transit system sells-off Federally-funded assets or rights-of-way, it must pay the Federal government back in full. That effectively eliminates much of the revenue that they could gain from an asset sale. Although the Bush Administration's Executive Order 12803 attempted to ease the reimbursement requirements, Federal transportation agencies face statutory reimbursement requirements that appear to supersede E.O. 12803.

One proposal is to seek a change in this legislative requirement, so long as the proceeds were reinvested in transportation facilities or perhaps other public infrastructure. This would free up capital for urban communities to devote to other priorities and encourage private operators to invest in urban infrastructure.

Banking Rules

Commercial banks can participate in infrastructure projects by providing bridge and construction loans. To encourage additional private investment in infrastructure, these bank financings could be counted toward Community Reinvention Act goals, to the extent they do not count already.

Please let me know if you have any questions about these proposals.

P.S. Good to see you Tuesday. Let's make a point to keep up. J.

File DOT

E X E C U T I V E   O F F I C E   O F   T H E   P R E S I D E N T

18-Jan-1996 01:07pm

TO: (See Below)

FROM: Kenneth L. Schwartz
Office of Mgmt and Budget, TCJS

SUBJECT: DOT Reorganization -- FYI

This is a "heads up" regarding a DOT surface transportation reorganization proposal which is likely to be submitted to OMB next week.

Background. The 1996 Transportation Appropriations bill contains several provisions regarding reorganization of DOT surface transportation activities. Principally, the bill:

-- reduces DOT's administrative budget by $25M in anticipation of savings to be achieved through reorganization.

-- instructs the Secretary to "reduce the existing field office structure, and to the extent practicable collocate and consolidate the Department's field offices and administrative activities."

-- allows DOT to submit a reorganization plan, by no later than the submission of the President's budget (presumably, Feb. 5), pursuant to special "fast track" rules:

* 90 days for Congressional consideration (with an opportunity for the Admin. to alter the plan before the 90 days lapse).

* A yes/no vote only -- no amendments. Failure to vote means disapproval.

DOT Proposal. Currently, DOT plans to submit its proposal to Congress by Feb. 5th. We expect to receive a DOT draft proposal next week. We anticipate that the proposal will propose a substantial number of office consolidations, closures, relocations, and co-locations. The draft reorganization would affect about 2,000-3,000 field staff in 70-80 offices. DOT's current target is to consolidate to about 45 offices. [DOT has not yet identified the number of positions to be transferred or eliminated.] The focus of the reorganization is improved service delivery, rather than budget savings. We have informed DOT that these proposed measures need to be cleared by the White House (we will forward the DOT plan to you upon receipt).

This proposal is separate and discrete from grant consolidation, which has upset the urban/mass transit community. At this juncture, DOT does not appear likely to propose headquarters merger of the Federal Transit Administration and the Federal Highway Administration. In short, we expect that interest group concerns about DOT losing its city and mass transit focus will be largely mitigated.

DOT seems to have done a good job in touching bases with Congressional committees (appropriations and authorizations), as well as the interest groups. We anticipate that OMB staff will not have substantial problems with the draft plan.

Distribution:

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DOT

January 17, 1996

URBAN ECONOMIC INITIATIVES
Establishing Port Trade Zones

I. BACKGROUND

America's economy is increasingly dependent on international and domestic trade. A huge proportion of this trade activity -- 95 percent of our country's exports and imports, and nearly one billion tons of domestic commerce -- is carried by water transportation through ports and related intermodal facilities.

Historically, many of our largest cities developed around the economic activity generated by ports and trade-related industries. In recent years, many of these central cities have become the major centers of unemployment and poverty as trade-related businesses have left urban core areas. One key to providing jobs is making use of the immobile transportation infrastructure -- ports, rail lines, etc. -- to revive these areas' roles as economic centers. But development is hampered by the cost of demolishing existing buildings, environmental clean-up and security. Congestion and inefficient rail and truck access, and the cost of redeveloping available land, undermine the locational advantage for the efficient intermodal movement of domestic and international cargo that these central city facilities would otherwise enjoy.

Over the last several years, Federal transportation policy -- particularly the Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA) and the President's 1994 Executive Order on "Principles for Infrastructure Investment" -- have supported the use of private sector capital to address our port and trade infrastructure investment needs. However, Federal tax policy also needs to be altered to make redeveloping urban Brownfields and underutilized land around ports and rail lines an affordable alternative to "green grass" development in outlying areas.

II. GOALS OF FEDERAL TAX INCENTIVES

Federal tax incentives targeted toward the redevelopment of industrial areas in and around our Nation's ports and freight centers will complement existing Federal programs designed to provide economic opportunity for residents of distressed urban neighborhoods -- particularly the President's Empowerment Zone/Enterprise Community (EZ/EC) Initiative. The primary goal will be to create good paying blue collar jobs by leveraging central cities' locational advantage for trade and freight-related business activity.

In addition to EZ/EC, the initiative will also link up to other significant urban initiatives of the Administration. The proposal will explicitly link with the Environmental Protection Agency's "XL for Communities" regulatory reform program, and be shaped to assure that tax incentives accelerate redevelopment of existing underutilized urban Brownfields land for port and trade-related activities.

The incentives should also help to strengthen and expand the partnerships created by the EZ/EC process. The proposed program would involve all segments of the community -- including, for the first time, many port authorities and terminal operators and trade-related private business, as well as government officials, community groups, private and non-profit sectors, and centers of higher learning that came together in support of EX/EC applications. Finally, the tax incentives should not be too broad or too restrictive; they should only facilitate investment in port and trade-related infrastructure that otherwise would be delayed or infeasible due to regulatory and/or financial constraints.

III. PROPOSAL: ALLOW TAX EXEMPT FINANCING AND EMPLOYER WAGE CREDITS FOR PORT AND TRADE-RELATED BUSINESS ACTIVITIES IN DESIGNATED PORT TRADE ZONES

Building on provisions of the President's EZ/EC Initiative, the NEC Urban Policy working group proposes to permit states and local governments to establish "Port Trade Zones" in which development of privately and publicly-owned land for port and trade-related private sector activity would receive the same benefits now made available to EZ's -- limited tax-exempt financing and employer wage credits. These tax incentives would leverage the locational advantage and infrastructure of central city areas and foster private investment to stimulate trade and economic development opportunities within our Nation's distressed core urban areas.

A new category of tax-exempt private activity bonds -- qualified port trade zone facility bonds -- would be created to enable the financing of property in designated Port Trade Zones. To qualify, 95 percent or more of the net proceeds of the bond issue would have to be used to finance qualified Port Trade Zone property. Similar to the requirements for qualified enterprise zone facility bonds, qualified Port Trade Zone property would:

- consist of depreciable tangible property (including buildings) located within the boundaries of the designated Port Trade Zone;
- have to be acquired after the Port Trade Zone designation is in effect; and,
- be used in an allowable port or trade-related activity defined below.

Qualified port trade zones facility bonds would be issued by an appropriate governmental unit. As with the current provision for tax-exempt private activity bonds for docks and wharfs, the bonds would not be subject to state volume caps, although limits on the total amount of outstanding port trade zone facility bonds allocable to any person and related person could be set. (Under the EZ/EC provisions, no more than $3 million may be allocable to any person and related person per zone or community, or $20 million for all zones and communities.)

IV. ECONOMIC BENEFITS

Currently, trade activity generates $52 billion in total personal income; $22.5 billion in business income; $14 billion in Federal taxes; and more than $5 billion in state and local taxes. The port industry supports over 1.5 million jobs nationwide.

By virtue of the limitation to communities that have already received EZ/EC designation and the central city location of most port and cargo facilities, all of the investment in a Port Trade Zone would generate private sector jobs in or nearby distressed communities. Short-term jobs would be created during the construction phase, as well as permanent jobs associated with ongoing economic activity in Port Trade Zone communities.

The overall U.S. economy would benefit from new investment in port and trade infrastructure by increasing productivity and helping to accommodate increase trade volume linked to NAFTA, GATT and overall economic growth. New business activity and jobs increase Federal, state and local tax income tax revenues, which would help offset the loss in tax revenues from issuing tax-exempt debt. The local real estate tax base would also increase. Spending for public sector entitlement programs would decrease to the extent that the unemployment rolls are reduced. The demand for new infrastructure investment in outer ring exurbs and edge cities would also decrease, as some of these businesses returned to the center city.

V. EVALUATION OF APPLICATIONS

A. Secretarial Review of Applications

State and local governments would nominate specified tracts of urban land within their boundaries but outside existing EZ/EC's for designation as Port Trade Zones, provided minimum eligibility requirements are met. Applications would be submitted to the Secretary of Transportation, who will approve or disapprove the nominations after review of each application and after consultation with the EZ/EC Community Empowerment Board.

As part of the review process, the Secretary of Transportation would evaluate the effectiveness of the Port Trade Zone in meeting the Federal goals previously discussed. To assist the Secretary, applicants would have to submit a strategic plan for the Port Trade Zone which builds upon the strategic plan already in place for the EZ/ECs. The Port Trade Zone strategic plan would include a description of (1) how the Port Trade Zone would remove the barriers to economic development within the community and create opportunities for resident of EZ/ECs in proximity to the Port Trade Zone; (2) the community involvement in the development of the Port Trade Zone and the partnerships that will be established to implement the Port Trade Zone; and, (3) the mechanism that will be used to evaluate and improve the effectiveness of the Port Trade Zone in meeting overall goals.

Applications for Port Trade Zone status would have to be submitted within ___ months of publication in the Federal Register, and approval/disapproval of Port Trade Zone status would have to be made within ___ months after receipt of a completed application.

B. Selection Criteria

1. Eligibility

Port Trade Zones would be restricted to metropolitan areas that already contain designated Empowerment Zones (EZs), Supplemental Empowerment Zones (SEZs), Enterprise Communities (ECs) or Enhanced Enterprise Communities (EECs). More than 70 metropolitan areas have designated EZ/SEZ/EC/EECs; over 40 are port communities located along the coastline, the Great Lakes and the commercially navigable inland waterways. (See Attachment) This includes a large proportion of U.S. cities with substantial numbers of unemployed, including New York, Los Angeles, Chicago, Philadelphia, and Detroit. All EZ/EC communities could be permitted to obtain designation as Port Trade Zones, or a limit could be set on the number of Port Trade Zones that the Secretary could designate.

2. Physical Features

The Port Trade Zone would have to be located:

- in proximity to publicly-owned port property used for trade-related activities -- with the exception of rail access lines, which could be extended out to 10 miles;

- in areas containing substantial concentrations of urban Brownfields;

- for non-port communities in proximity to significant rail freight centers and transfer facilities; and,

- in areas accessible to residents of urban Census tracts currently designated as EZ/SEZ/EC/EECs.

Rather than specifying the maximum allowable distance between a Port Trade Zone, the EZ/SEZ/EC/EEC and port property, applicants would have to describe how the Port Trade Zone would enhance economic opportunity for residents of distressed urban neighborhoods within the EZ/ECs. In cases where Port Trade Zones would be located within existing urban Brownfields, projects would benefit from revised tax rules under consideration for such contaminated areas. And all projects within the zone would participate automatically in EPA's XL Community Pilot Program, which grants communities flexibility in implementing

EPA's XL Community Pilot Program, which grants communities flexibility in implementing environmental regulations in exchange for a commitment to achieve greater environmental performance.

The Port Trade Zone would be required to have a continuous boundary, or consist of not more than three non-contiguous parcels -- the same requirement as EZ/ECs. The total land area within the zone could be no more than 500 acres, and would be reduced by some formula to be determined for rail access lines extended out beyond port property. At most, a Port Trade Zone would be equivalent to about three-fourths of a square mile -- 1/25th of the total area of land within a metropolitan area that can be designated as an EZ/SEZ/EC/EEC.

3. Employment

At least 25 percent of the employees of qualified Port Trade Zone facilities would have to be residents of Census tracts designated as EZ/SEZ/EC/EECs -- slightly less than the 35 percent requirement for Enterprise Zones business that also benefit from tax exempt bond financing. The employer wage credit provisions of the President's EZ/EC initiative would also be extended for EZ/EC residents that are employed within designated Port Trade Zones.

Applicants would have to identify job training available to residents of EZ/EC tracts and would have to demonstrate that the jobs available to these residents would provide an opportunity for upward mobility. In addition, applicants would have to identify sources of transportation that would be available to carry residents between their homes and job sites.

VI. ALLOWABLE ACTIVITIES WITHIN PORT TRADE ZONES

Under the Section 142(a) of the Internal Revenue Code (Code), some port and trade-related development can already be conducted using tax-exempt debt. Under the existing "docks and wharves" exemption, public entities, including port authorities, may issue tax-exempt debt for certain facilities and equipment on their own property, even if the facilities and equipment exist for the benefit of private entities.[1] Under IRS interpretation of Section 142(a), tax exemption is limited to property located along or close by the waterfront.

Under the proposal, Section 142(a) would be amended to permit the appropriate governmental unit to finance facilities used in trade-related activities within designated Port Trade Zones, including:

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[1] The facility or equipment being financed must be owned by the public entity, can be financed for no more than 80 percent of its useful life, and must be returned to the public entity at the end of the financing or purchased at a fair market price. The private business then leases the facility or equipment at a lease rate which equals the debt service.

- Warehousing and distribution facilities, including long-term storage
- Facilities used to assemble, process, manufacture or repair merchandise that is shipped or received through the port;
- Offices for employees engaged in port-related activities;
- Staging and storage areas for containers and other cargo;
- Passenger areas;
- Ship repair and maintenance facilities at the port site;
- Land set aside for environmental purposes or future use (must be left dormant);
- Structures alongside which a vessel docks;
- Cargo handling facilities, including cranes, forklifts, conveyors and other equipment used in the loading and unloading of cargo;
- Harbor and channel dredging and slack water harbor facilities;
- Facilities for fire and rescue operations; and,
- Roadways, rail facilities, and related improvements providing immediate access to port facilities or rail or other freight transfer facilities.

VII. DURATION OF PORT TRADE ZONE STATUS AND REPORTING REQUIREMENTS

The Department of Transportation will require periodic reports for designated Port Trade Zones. These reports will describe the actions that have been taken in accordance with the Port Trade Zone strategic plan to ensure that Federal and state/local goals are being met. Port Trade Zone status, and the tax exemption on qualified port trade zone property, would apply for the economic life of the facilities and equipment, as long as they were used for allowable port-related activities and the benchmark goals of the Port Trade Zone strategic plan are being met.

Attachment
Potential Port Trade Zone Urban Areas
(Based on Existing EZ/EC designations)

Empowerment Zones - (5 out of 6)

Deepdraft Ports

Maryland - Baltimore
New York - New York, Harlem and South Bronx
Pennsylvania - Philadelphia

Great Lakes Ports

Illinois, Chicago
Michigan - Detroit

Supplemental Empowerment Zones - (2 out of 2)

Deepdraft Ports

California - Los Angeles City & County

Great Lakes Ports

Ohio, Cleveland

Enhanced Enterprise Community - (4 out of 4)

Deepdraft Ports

California, Oakland
Massachusetts, Boston
Texas, Houston

Inland and Shallow Draft Ports

Missouri, Kansas City (MO & KS)

Enterprise Community - (33 out of 60)

Deepdraft Ports

California, Los Angeles/Huntington
California, San Diego
California, San Francisco/Bayview/Hunters Point

Connecticut, Bridgeport
Connecticut, New Haven
Delaware, Wilmington
Florida, Dade County, Miami
Florida, Tampa
Louisiana, New Orleans
New Jersey, Newark
New York, Albany/Schenectady/Troy
Oregon, Portland
Rhode Island, Providence
South Carolina, Charleston
Virginia, Norfolk
Washington, Seattle
Washington, Tacoma

Great Lakes

Michigan, Muskegon
New York, Buffalo
Wisconsin, Milwaukee

Inland and Shallow Draft Ports

Illinois, East St. Louis
Iowa, Des Moines
Kentucky, Louisville
Louisiana, Ouachita Parish
Minnesota, Minneapolis
Minnesota, St. Paul
Missouri, St. Louis
Nebraska, Omaha
Pennsylvania, Pittsburgh
Tennessee, Memphis
Tennessee, Nashville
West Virginia, Huntington