American Public Power Association
Council of Development Finance Agencies
Council of Infrastructure Financing Authorities
Education Finance Council
Government Finance Officers Association
International City/County Management Association
International Municipal Lawyers Association
Large Public Power Council
National Association of Counties
National Assn. of Health and Educational Facilities Finance Authorities
National Association of Local Housing Finance Agencies
National Association of State Auditors, Comptrollers and Treasurers
National Association of State Treasurers
National Council of State Housing Agencies
National League of Cities
National School Boards Association
U.S. Conference of Mayors

February 14, 2012

The Honorable David Camp
Chairman
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

The Honorable Sander Levin
Ranking Minority Member
Committee on Ways and Means
U.S. House of Representatives
Washington, D.C. 20515

Dear Chairman Camp and Congressman Levin:

The organizations listed above are writing to express our concern with a proposal in President Obama's FY2013 Budget that would significantly raise borrowing costs for state and local governments and further hamper their ability to meet our country's infrastructure needs.

The president proposes to place a cap on the value of certain tax deductions and tax exclusions, including interest on bonds issued by state and local governments, that is intended to limit tax benefits for certain higher income taxpayers to the equivalent of the 28% tax rate. Thus, under this retroactive proposal, investors with adjusted gross incomes exceeding the thresholds set by the president's proposal* would no longer be able to receive the full benefit of the tax-exempt interest they paid for when they purchased the bonds. This could amount to an effective 7-percent tax on otherwise tax-exempt interest for many taxpayers who would be in the 35% tax bracket. In the case of newly issued tax-exempt bonds, investors would likely demand higher interest rates to make up for this new tax. Such a proposal would have a <u>direct and negative impact on state and local governments and authorities</u>, and more importantly, the communities they serve. The outcome would be higher borrowing costs for state and local governments, less investment in infrastructure, and fewer jobs. This comes at exactly the wrong time as state and local government finances remain under pressure, and infrastructure and education investment is woefully inadequate.

The federal tax-exemption on municipal bond interest has been in place since the enactment of the very first federal tax code in 1913. As a result, state and local governments save, on average, an estimated two

percentage points on their borrowing to finance investment in public infrastructure. Over the past few decades, tax-exempt finance has generated trillions of dollars of investment in vital public infrastructure and has saved state and local governments hundreds of billions of dollars in interest costs.

The proposed de facto tax increase also would be retroactive in that it would apply to interest on bonds governments have already issued and investors in good faith and in reasonable reliance have already purchased. The effect would be to substantially erode the value of bonds already in investors' portfolios. This would represent a violation of the basic assumption of investors that Congress will not change the terms governing the taxability of interest for bonds already outstanding. In the nearly 100-year history of the tax-exemption, Congress has never applied a retroactive tax to bonds already held by investors.

This new tax risk will play out as higher borrowing costs for states local governments. It is estimated that state and local borrowing rates could rise by as much as a full percentage point if the proposal is enacted. State and local governments will have to pay these additional costs on every bond they issue, even though the tax is intended to affect those considered "wealthy".

We urge Congress to reject this proposal, as it runs counter to the national goal of providing cost-effective infrastructure for our citizens and because it effectively imposes places a tax on tax-exempt financing.

Sincerely,

American Public Power Association, Amy Hille, 202-467-2929
Council of Development Finance Agencies, Toby Rittner, 614-224-1300
Council of Infrastructure Financing Authorities, Rick Farrell, 202-256-0298
Education Finance Council, Vince Sampson, 202-955-5510
Government Finance Officers Association, Susan Gaffney, 202-393-8468
International City/County Management Association, Elizabeth Kellar, 202-962-3611
International Municipal Lawyers Association, Chuck Thompson, 202-742-1016
Large Public Power Council, Noreen Roche-Carter, 916-732-6509
National Association of Counties, Mike Belarmino, 202-942-4254
National Assn. of Health & Educational Facilities Finance Authorities, Chuck Samuels, 202-434-7311
National Association of Local Housing Finance Agencies, John Murphy, 202-367-1197
National Assn. of State Auditors, Comptrollers and Treasurers, Cornelia Chebinou, 202-624-5451
National Association of State Treasurers, Jon Lawniczak, 859-244-8175
National Council of State Housing Agencies, Garth Rieman, 202-624-7710
National League of Cities, Lars Etzkorn, 202- 626-3173
National School Boards Association, Deborah Rigsby, 703-838-6208
U.S. Conference of Mayors, Larry Jones, 202-861-6709

* Reduce the Value of Certain Tax Expenditures; FY13 President's Budget Proposal, Receipts, page 201

Reduce the value of certain tax expenditures.— The Administration proposes to limit the tax rate at which upper-income taxpayers can use itemized deductions and other tax preferences to reduce tax liability to a maximum of 28 percent. This limitation would affect only married taxpayers filing a joint return with income adjusted for these tax preferences of over $250,000 (at 2009 levels) and single taxpayers with income over $200,000 (at 2009 levels). The limit would apply to all itemized deductions, tax-exempt interest, employer-sponsored health insurance, deductions and income exclusions for employee retirement contributions, and certain above-the-line deductions, effective for taxable years beginning after December 31, 2012.