Policy Proposal:
Create Permanent Disaster Recovery Bonds

Overview

In the aftermath of catastrophic events, communities find themselves in dire need of federal assistance to enable recovery and rebuild essential infrastructure. While the federal aid offered through the Stafford Act provides a much-needed resource, those funds rarely are available in the immediate wake of a disaster and are often insufficient for comprehensive recovery efforts.

Congress has created special tax-exempt bond categories in response to disasters over the past 20 years, including Liberty Bonds after September 11th, Gulf Opportunity Zone Bonds and Ike Bonds after hurricanes, and Mid-Western Disaster Recovery Bonds after severe flooding along the Mississippi River. These allocations were extremely impactful, but each required a special act of Congress that took months before capital became available. The delay left communities without the immediate resources needed to begin recovery. Gridlock in Congress in recent years has further stymied the creation of any new bond categories, leaving no additional tax-exempt financing for communities impacted by natural or man-made disasters—like the catastrophe in East Palestine, Ohio.

America needs a permanent financing tool that communities can access immediately after disaster strikes and use to leverage private investment for longer-term redevelopment of essential infrastructure. To mitigate the financial impacts of disasters on communities, a permanent category of Disaster Recovery Bonds should be created so that Congress does not need to take a special action after each catastrophic event.

Using prior disaster bond precedent as a guide, CDFA proposes immediate legislative action to provide the following resources.

Proposal #1 – Create a Permanent Category of Disaster Recovery Bonds

CDFA proposes the creation of Disaster Recovery Bonds**,** a permanent category of tax-exempt private activity bonds that could be issued by the affected communities, states, and territories in the event of a man-made or natural disaster. These bonds would not be subject to federal volume cap restrictions and would become available to the affected areas upon the declaration of a state of emergency by a state's or territory's governor. CDFA recommends an annual maximum federal allocation of $20 billion.

The use of Disaster Recovery Bonds would be authorized only in a Disaster Recovery Zone to finance (i) the acquisition, construction, reconstruction, or renovation of non-residential real property (land, buildings, and fixtures); (ii) the construction and rehabilitation of multi-family rental property for low- and moderate-income individuals, (iii) the repair or reconstruction of damaged public utilities facilities and transportation infrastructure, and (iv) the immediate repair and mitigation of severe environmental contamination to a public water source.

To increase Disaster Recovery Bond demand, this legislation will allow financial institution purchasers to deduct the interest cost of carrying an amount of such bonds not exceeding 2% of the purchaser's assets.

Proposal #2 – Provide Flexibility for Tax-Exempt Financing for Working Capital
Congress should permit state and local governments within the Disaster Recovery Zone to issue tax-exempt obligations on a short- or long-term basis (e.g., up to 30 years) for governmental working capital requirements, disregarding the deficit sizing limits imposed under current law, to provide access to funds for crucial operating cash flow and to replenish "rainy day" reserves.

This legislation would permit the eligible costs of nonresidential projects to include working capital in an amount up to 5% of the cost of the project to assist businesses in replacing lost inventory and other working capital items. This legislation also would permit the eligible costs of nonresidential projects to include the cost of acquiring or rehabilitating moveable equipment and fixtures in an amount up to 25% of the cost of the project, provided the equipment was used in the Disaster Recovery Zone by the beneficiary of the financing prior to the disaster.

Proposal #3 – Ease the Burden of Servicing Debt on Disaster Recovery Bonds
CDFA proposes that the state and local governments within a Disaster Recovery Zone must be allowed to extend repayment schedules for tax-exempt debt, regardless of the safe harbor provisions of current law that generally require the weighted average maturity of governmental tax-exempt bond borrowing to not exceed 120% of the useful lives of the financed facilities. As with bonds issued under the GO Zone Act, CDFA proposes that interest on Disaster Recovery Bonds not be an item of tax preference for purposes of the federal alternative minimum tax.

Next Steps
By enacting Disaster Recovery Bonds legislation, Congress will ensure that disaster-affected communities can immediately begin the recovery and redevelopment process. CDFA stands ready to assist Congress with the passage of these important policy considerations. For more information and for legislative guidance on this proposal, contact CDFA at info@cdfa.net or 614-705-1300.