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Op-Ed Contributor

Fiscal Blood on the Tracks

By MITCHELL L. MOSS

LIKE a tsunami that follows an undersea earthquake, collateral damage from the collapse of credit markets is about to strike the millions of daily transit riders in America's biggest cities. Public transit agencies in cities including New York, Atlanta, San Francisco and Washington are under pressure to surrender \$2 billion from their budgets because financial institutions have spotted a chance to gain a windfall from complicated tax-shelter deals known as "leasebacks."

In the heady 1990s, the federal government encouraged these leaseback deals as a quick fix for budget problems. Transit agencies like New York's Metropolitan Transportation Authority would sell their railcars and other equipment to banks, which would then lease them back to the agencies.

Leasebacks appeared to promise that everyone would emerge a winner. Banks — including many that later took federal bailout money like Bank of America and Wells Fargo — were able to cash in on substantial tax deductions through the transactions. The transit companies, which were paid with a portion of those tax savings, could use the cash to modernize their systems and make safety improvements.

Alas, as with any quick fix, the deals have set off a cascade of problems.

First, while the Internal Revenue Service declared the deals illegal in 2004, it allowed previously completed deals to remain on the books. And the situation exploded last fall when financial markets crashed and the third-party insurers chosen by the transit agencies as guarantors of the transactions lost their triple-A credit ratings (in many cases, the insurer was A.I.G.). This placed the transit agencies in "technical default" on the leases, even though they hadn't missed any payments.

In turn, many of the banks have decided to take advantage of these "technical defaults" to reap a windfall in early-termination payments. By rights, they can immediately demand from transit authorities an amount equal to all their anticipated tax savings. These can run to hundreds of millions of dollars — New Jersey Transit alone is on the hook for \$150 million.

Virtually all major city and state public transit systems in the country have at least one of these deals still on the books. If they have to make these payments, commuters will bear the brunt, in terms of higher fares and deferred maintenance.

A solution exists, however. Senator Robert Menendez, a Democrat from New Jersey, and Representative John Lewis, a Georgia Democrat, have proposed a bill that would levy a 100 percent excise tax on any lump-sum payments demanded by the banks. This would effectively force the financial industry to stop demanding default penalties and go back to the old lease payment schedule — at no cost to taxpayers.

As the nation climbs out of one of its toughest economic crises ever, we cannot be lulled into thinking the problems caused by imprudent financing techniques have vanished. Yes, the transit groups were unwise to get involved in the leasebacks, but that's no reason to let banks continue to exploit loopholes in them at the expense of transit riders. Congress must act to protect commuters and taxpayers from this insidious legacy of a careless period in American finance.

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