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Editor-in-Chief: Karl P. Sauvant (Karl.Sauvant@law.columbia.edu)
Editor: Ken Davies (Kenneth.Davies@law.columbia.edu)
Managing Editor: Alma Zadic (az2242@columbia.edu)

Beyond treasuries: A foreign direct investment program for U.S. infrastructure

by
Geraldine McAllister and Joel H. Moser[*]

In his jobs address to a joint session of Congress last week, President Obama returned to a familiar theme: a call for nontraditional infrastructure investment as a generator of economic growth and, ultimately, jobs. The President's frequent references to "private investment"[1] and "fully paid"[2] infrastructure are encouraging, yet there is no assurance that domestic private capital investment alone is sufficient to reverse the degradation of the nation's infrastructure. As host to the largest flows of inward foreign direct investment (FDI), it is time that the United States employs this critical source of capital in tackling the nation's infrastructure deficit.

The use of foreign capital to improve U.S. infrastructure and competitiveness is not without its challenges. First, it requires the government to find a new balance between economic openness and national security concerns – no easy task, particularly with the inclusion of "critical infrastructure"[3] in the definition of national security. Nevertheless, the Committee on Foreign Investment in the United States, dedicated to reviewing the impact of FDI on national security,

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[*] Geraldine McAllister (gam2116@columbia.edu) is a Visiting Scholar at the Institute for Social and Economic Research and Policy, Columbia University. Joel H. Moser (joel.moser@bingham.com) is a senior partner in the Energy and Project Finance Group of Bingham McCutchen LLP, specializing in cross-border infrastructure investment, finance and public private partnerships, and an Adjunct Professor at Columbia University School of International and Public Affairs. The authors wish to thank Michael Likosky, John T. Livingston and Richard Robb for their helpful comments on this text. **The views expressed by the authors of this *Perspective* do not necessarily reflect the opinions of Columbia University or its partners and supporters. *Columbia FDI Perspectives* (ISSN 2158-3579) is a peer-reviewed series.**

[1]See e. g., the remarks by the President in the State of Union Address, January 25, 2011, available at: **Error! Main Document Only.** .

[2] Ibid.

[3] The term "critical infrastructure" means, subject to rules issued under this section, systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems or assets would have a debilitating impact on national security. See, Foreign Investment and National Security Act of 2007, available at http://www.gpo.gov/fdsys/pkg/PLAW-110publ49/pdf/PLAW-110publ49.pdf.

has garnered significant experience in this area. Devising a legislative and regulatory framework that provides for domestic security without excluding the United States from access to investment in infrastructure is not beyond the capacity of the government. Ultimately, failure to address this challenge will be to the detriment of both U.S. national security and economic interests. A recent Asia Society report notes: "If political interference is not tempered, some of the benefits of Chinese investment…such as job creation, consumer welfare, and even contributions to U.S. infrastructure renewal—risk being diverted to U.S. competitors."[4]

Secondly, such inflows must be encouraged and facilitated - it is not simply a case of *allowing* FDI flow into U.S. infrastructure. Low levels of political risk and a large market still make the United States an attractive investment destination; yet it is but one possible investment location, and competition is vigorous. The U.S. Government must build a program to attract and incentivize investment in infrastructure – for example, by transferring a portion of the federal budget currently spent on funding municipal bond investor tax incentives for the wealthy toward grants and other incentives, perhaps as part of the federal tax overhaul anticipated in the debt crisis resolution and as contemplated by the Simpson-Bowles commission.

Finally, an infrastructure FDI program must be scalable to provide for investment at the requisite levels. The United States has some experience in this area, having adopted public private partnerships for a number of projects. The current limiting factor, however, is deal flow. We propose a pilot program that mandates states to set aside an increasing portion of their capital programs, reaching 10% by decade-end, for funding incorporating an equity component. This federal mandate can be linked to federal funding, such as transportation funding. The net cost of this program (if any) could be borne by gradual reductions in the availability of the costly indirect subsidy of federal tax-exemption on municipal bonds, further shifting the dynamic from public debt to private investment.

A grant-based program could also work; however, whatever method is chosen, the Federal government must act quickly. Experience in other countries has shown that it can take a decade to develop a mature market for private infrastructure investment and development. Given that these may be the final days of the era of easy access to foreign capital in the Treasury bond market, now is the time to take a meaningful step toward building the alternative. Through the sale of Treasury bonds abroad, infrastructure has been substantially financed by foreign capital for decades. It is time to construct a new pathway for this capital before the old routes are washed away.

[4] Daniel H. Rosen and Thilo Haneman, *An American Open Door?* (New York: Asia Society and Woodrow Wilson International Center for Scholars, 2011), p.10, available at:http://media.asiasociety.org/ChinaFDI/AnAmericanOpenDoor_FINAL.pdf.

For further information please contact: Vale Columbia Center on Sustainable International Investment, Ken Davies, Kenneth.Davies@law.columbia.edu.

The Vale Columbia Center on Sustainable International Investment (VCC), led by Dr. Karl P. Sauvant, is a joint center of Columbia Law School and The Earth Institute at Columbia University. It seeks to be a leader on issues related to foreign direct investment (FDI) in the global economy. VCC focuses on the analysis and teaching of the implications of FDI for public policy and international investment law.

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