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Pearce, delegation defend bonds

by Peter Hirschfeld

MONTPELIER — A federal tax reform under consideration in Congress could substantially increase the cost of roads, bridges, buildings and other infrastructure funded by bonds, according to State Treasurer Beth Pearce.

Among the revenue-generating tax reforms in the budget proposal unveiled by President Barack Obama earlier this year is a plan to reduce the federal tax exemption on interest earned on municipal bonds.

Investors now enjoy a nearly 40 percent exemption on their municipal bond returns, an enticement that allows issuers like the state of Vermont to secure far more favorable interest rates than they would otherwise.

“And that lower interest rate lowers the cost of borrowing for the state, and ultimately benefits the taxpayer,” Pearce said Thursday.

Pearce is among 42 state treasurers nationwide to sign a petition urging Congress and the White House to torpedo the provision. But the proposal is under serious consideration on Capitol Hill, where a new Senate bill aims to go even further by doing away with the federal tax exemptions on municipal bonds altogether.

According to an analysis by Pearce’s office, the federal exemption has saved Vermont taxpayers about $85 million over the past decade in avoided interest payments. While the risk to investors purchasing bonds issued by Vermont would continue to be minimal, Pearce says the interest rate would nonetheless spike.

Vermont last issued general obligation bonds about a year ago, when the state sold $93 million in bonds at rates of 2.2 percent. Pearce said market rates have since gone up to about 3 percent but could jump by nearly a third without the tax exemptions.

The bonds pay for infrastructure projects that make it into the annual capital bill — everything from improvements to interstate rest areas to the construction of police barracks and the repair of state bridges.

While reducing the exemption, as Obama has proposed, or eliminating it altogether, as the bipartisan Senate bill would do, might raise revenues federally, Pearce said, “I don’t think this is a cost-effective way to do it.”

The exemption has been in place since 1913.

“This is a program that for 100 years has allowed us to build and maintain our infrastructure in a cost-effective way,” Pearce said. “And it’s important to our state budget and to our continued economic growth.”

Pearce said each member of Vermont’s three-man congressional delegation opposes any changes to municipal bond exemptions.