

Mr. BLATNIK. Mr Secretary, I am sorry. This is important. This is now specifically outlining and stating the points of this new financing, bonding?

Secretary UDALL. That is right. It is what we have called the full-financing approach to enable us to meet the full commitments envisioned by this committee in the 1966 act.

The first thing the bill would do is authorize long-term contracts—up to 30 years—with States and local public bodies. These contracts could be pledged by the States or local public bodies as security for bonds issued by them to cover the cost of the treatment plants, including the Federal share.

Under the contracts the Federal Government would pay the principal and interest on that portion of the bonds that represents the normal Federal grant share under the present act.

As you will recall under the 1966 act, this can be 30 percent, 40 percent, 50 percent, or in some instances 55 percent. Whatever that Federal percentage is, it is determined we would pay our share of these bonds and retire them as they came due.

The contracts would also provide a Federal guarantee of the non-Federal share and the payment of an interest subsidy to reduce the net effective interest rate to States and localities to a rate reasonably comparable to rates on tax-exempt municipal bonds.

4. The bill provides that the interest on bonds issued to construct these plants shall not be exempt from Federal income taxation.

Let me emphasize this nonexempt tax feature is a major element of this very important legislation. I think you will see why. It is, however, not intended as an opening wedge precedent to eliminating the tax exemption for municipal bonds—this does not represent a decision by the administration that we are going to change the law with regard to tax-exempt bonds—but we have a very special situation here. And the provision that we have in this legislation is important for three reasons:

First, the bill provides for a Federal guarantee of the entire bond, even the local share, and for an annual Federal payment of principal and interest on part of them. It would not be good policy to apply this guarantee to tax-exempt bonds.

We believe that the Federal guarantee would have the effect of lowering the risk, equivalent to a triple-A bond rating for the communities concerned.

Second, without this provision, we are convinced that the proposal would add substantially to the volume of new issues of tax-exempt bonds by State and local public bodies. This would be particularly undesirable in view of the already large volume of municipal bond issues and the current high interest rates which States and localities are required to pay. Making the proposed new bonds taxable rather than tax-exempt would avoid adding to pressures on the municipal bond market and would thus result in significant savings in interest costs to States and localities on their borrowings for other urgent needs such as schools, roads, and other public facilities.

Third, the use of taxable rather than tax-exempt bonds would also be significantly cheaper for the Federal Government, even with the interest subsidy. The reason is that, as public and private studies have demonstrated, tax-exemption costs more to the Federal Government in