The Changing Nature of State-Federal Relations in Transportation


Some years ago I had the pleasure of addressing your annual meeting in Quebec and I am delighted to have an opportunity to renew our acquaintance and join Secretary Slater in this conversation about federalism in state transportation.

I intend to address three related topics. I will begin by briefly summarizing where the transportation legislation stands today and where I believe it is going.

Next, I shall discuss how individual states are responding to the present unsettled state of the federal transportation program.

And I shall conclude by sharing some thoughts how all this is likely to affect the future state-federal relationship in transportation.

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As you probably know, the cash balance of the Highway Trust Fund is drawing dangerously close to the point where the U.S. Transportation Department will be obliged to slow down or delay state reimbursements in order to keep the Trust Fund solvent. According to the US DOT that point was to be reached in late July—in other words, as we speak.

Overshadowing this short-term concern is the more fundamental question: what will happen at the end of the fiscal year, when the existing program is set to expire and the Trust Fund finds itself out of money.

Fortunately, Congress is acting in time to avert a crisis. Just last week, the House reached a bipartisan agreement to "patch" the Highway Trust Fund with $10.8 billion in short term funding through May 2015. The bill passed the House easily (367-55) with only 10 Democrats and 45 Republicans voting against it. White House endorsement of the Republican-sponsored bill no doubt helped to smooth the way for a bipartisan vote.

But the vote did not please many advocates in the transportation community. Perversely, they hoped for a shorter extension, ending in December. This way, they thought, they could force the
lawmakers to act on a multi-year funding plan in the post-election lame duck session.

House Ways and Means Committee Chairman Dave Camp (R-MI) would have none of that. Those who argue for the short deadline, he said, "are using it as a ploy to enact a massive increase in the gas tax during the lame duck session when only a very few lawmakers are present or have any say in the matter." At this point in time, it looks like Mr. Camp will have his way.

(Ed note, 8/1: While we correctly predicted the outcome, the path toward the final vote took a circuitous route. Contrary to expectations, the Senate’s first action was to amend the House version of the bill in favor of a shorter extension through December and a different funding approach. But the House rejected the Senate amendments and sent the bill back to the Senate, stripped of the Senate language. With the House poised to adjourn for a five-week summer recess, the Senate had little choice but to accept the House version of the bill and its May 2015 deadline. Final vote was 81-13)

What will happen after next May is anybody’s guess. A six-year surface transportation measure that transportation stakeholders want, would require roughly $330 billion to maintain current (FY 2014) spending levels. But Trust Fund revenue and interest over the same period is projected by the Congressional Budget Office to bring in only $230 billion—leaving a truly staggering funding gap of $100 billion.

The only feasible way to raise this kind of money would be to very substantially increase the federal gas tax—a solution favored by many in the transportation industry. But a boost in the gas tax remains a political anathema. Only two Senators—Democrat Tom Carper of Delaware and Republican Bob Corker of Tennessee—have come out explicitly in favor of raising the gas tax. On the other hand, House Majority Leader Kevin McCarthy—and the White House—recently reiterated their opposition. There is a good reason for their opposition: a Gallup poll in April 2013 found two-thirds of Americans are against a hike in the gas tax—even if it went toward infrastructure improvements.

So what is the most probable outcome? With the Republicans likely to control the Senate next year and the presidential elections casting a shadow over any new proposal to raise taxes, there will be a huge temptation for Congress to kick the can down the road once again — beyond the presidential election and into the next Congress. Remember, it took three years and eight short-term extensions to pass the last reauthorization, MAP-21!

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**States Are Striking Out On Their Own**

Fortunately, many individual states are trying to compensate for the lack of congressional action on long term funding by raising additional revenue of their own.

Some states have increased local fuel taxes (MD, WY, MA, VT, NH). Others have introduced fuel taxes at the wholesale level (e.g. PA), floated toll revenue bonds (e.g. OH, MA) or raised highway tolls (e.g. DE). Still others have enacted dedicated sales taxes for transportation — as your host state did in November 2012. Our survey has identified more than 30 states that have launched transportation-related fiscal initiatives in the past two years.

Transportation funding at the state level was one of the subjects of today’s morning session co-chaired by Scott Bennett (Director of the Arkansas State Highway Department) and Sherri
LeBas (Director of Louisiana DOT). Listening to those two state DOT officials describe their successful revenue raising efforts reminded me of an observation by Sen. Roger Wicker (R-MS), that states have become veritable "laboratories for fiscal experimentation."

At the local level, things have not been standing still either. A growing number of local jurisdictions are approving bond issues and dedicated sales taxes to support local transportation improvements.

Collectively, these measures are generating billions of additional dollars for state and local transportation programs— and making up for the absence of increased federal funding. As the congressional votes suggest, the successful efforts to raise more revenue at the state level also may have lessened the sense of urgency to tackle a multi-year transportation reauthorization.

**Financing Major Transportation Investments**

To further make themselves fiscally independent, many states have turned to financing large-scale construction projects with long term credit—they are borrowing front-end capital and repaying it over extended periods of time with dedicated sources of revenue. To raise capital, states are using a variety of financing tools such as TIFIA loans, Private Activity Bonds, toll revenue bonds and private equity contributions.

As many as 22 jurisdictions have done so in the last several years. This includes several SLC members, such as Texas (North Tarrant Express project in Fort Worth), Florida (Interstate 4 reconstruction in Orange County), Virginia (Interstate 95 Managed lanes) and North Carolina (Interstate 77 managed lanes north of Charlotte).

In turning to long-term credit to finance major transportation investments, states are following in the footsteps of the private sector. All of the nation’s privately owned infrastructure--- railroads, pipelines, telecommunications networks, power plants and refineries--- are funded with loaned capital. So are many transportation improvements at the local level—using tax-exempt municipal bonds. Now, state roads and bridges are joining the ranks of infrastructure projects that are increasingly financed with long term investment capital.

Another way in which states are procuring costly new facilities is by entering into public-private partnerships These allow states to shift the burden of financing large-scale construction projects to private contractors and concessionaires. In the last two years six states have entered into such partnerships--- with private contractors funding up front the cost of highway design and construction and getting repaid over time with so-called “availability payments.” More such partnerships are expected in the future as states gain familiarity with this type of financing arrangements.

In sum, states are not standing idly by, waiting for Congress to come to the rescue with more money. Instead, Governors, state legislatures and local governments are taking aggressive steps to make themselves less dependent on federal aid. They are increasing fuel taxes, passing local bond referenda, financing large-scale construction projects with long term credit, and entering into investment partnerships with the private sector. In other words, states are taking matters into their own hands and becoming masters of their own transportation destiny.

Will the states' growing fiscal independence— this de facto devolution as some call it--- make the Highway Trust Fund superfluous? I doubt it —at least not in the foreseeable future. At an estimated $34 billion a year, federal fuel taxes provide the states with essential, hard to replace
help in maintaining and modernizing the Interstate Highway System.

But big-ticket capital investments no longer will need to be funded with Trust Fund revenue. They will be increasingly financed with long-term capital. At least that's the scenario envisioned by some visionaries looking for a permanent solution to the Highway Trust Fund crisis.

Shifting major capital expenditures out of the Trust Fund, they contend, would help align spending from the Fund more closely with incoming tax revenues as proposed in this year’s House Budget Resolution. This, in turn, would put an end to the recurrent Trust Fund shortfalls of the past decade, eliminate the need for periodic bailouts and make the Trust Fund structurally sound in a permanent way.

As for the states, greater fiscal independence will help them gain a substantially enhanced role in transportation --- it will empower them to set their own spending priorities and do away with burdensome federal mandates. Conversely, increased state fiscal autonomy combined with continuing federal budgetary constraints, will lead de facto to a more limited federal role in transportation. It's an outcome that conservatives have long been urging and hoping for, and one which, I suspect, will please many of you as well.

Let me conclude by commending Senator Norris for placing the issue of federalism in transportation on the Council of Governments’ policy agenda. I cannot think of a more effective way of signaling to congressional lawmakers that the time has come to seriously rethink the state-federal relationship in transportation. The message you are sending to Washington is clear: the times have changed and the existing fiscal model, conceived in another era to fund the Interstate Highway program, no longer fits contemporary needs. Legislative reform is needed in the next Congress to strengthen decision-making authority of state governments and give local leaders more latitude to manage their transportation programs on their own terms. Let us hope your voice will be heard.

Thank you for the chance to share these views with you.

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