COMPETITIVE ENTERPRISE INSTITUTE

WEBmemo

June 30, 2015 **No. 30**

Reimagining Surface Transportation Reauthorization

Pro-Market Recommendations for Policy Makers

By Marc Scribner*

Many transportation policy observers estimate that stagnating revenues and increases in fuel efficiency will cause the current fuel tax–reliant Highway Trust Fund to implode sometime within the next 15 years. Until that implosion, fuel taxes will become extremely regressive, as the wealthy would avoid the taxes with new, highly fuel efficient or all-electric vehicles, shifting the fuel tax burden to the working poor. This is an outcome no one wants to see.

As of March 2015, the Congressional Budget Office (CBO) is projecting a 10-year $168 billion shortfall in the federal Highway Trust Fund (HTF), with the Highway Account accounting for $125 billion of that cumulative shortfall, and the Mass Transit Account for $43 billion.[1] By the end of Fiscal Year 2025, CBO is projecting annual outlays from the HTF's Highway Account to exceed annual revenues and interest by $16 billion (47 percent), with outlays from the HTF's Mass Transit Account exceeding revenues and interest by $6 billion (150 percent).[2]

The HTF has faced similar problems for a decade. In the lead-up to the last reauthorization in 2012, a variety of HTF bailouts were floated by lawmakers. These ranged from "drilling for roads,"[3] which failed, to "pension smoothing,"[4] which passed. During the current reauthorization debates, drilling for roads is back.[5] Private pensions, having been excessively smoothed in July 2014's highway bill extension, can no longer be used as a source of fictional revenue.[6] But lawmakers from both parties are now considering corporate tax repatriation schemes to bail out the HTF, including a bill sponsored by Sens. Rand Paul (R-Ky.) and Barbara Boxer (D-Calif.).[7] In addition, Rep. John Delaney (D-Md.)[8] and President Obama are advocating for different tax repatriation HTF bailout packages.[9]

All of these bailout schemes should be rejected. Short of abolishing the current federal surface transportation programs and returning that responsibility to the states, there are a number of reforms policy makers can take that will ease the current fiscal crunch while preparing the nation for innovative transportation technologies and practices.

Most of these sensible transportation policies run counter to the six-year reauthorization bill recently introduced by Sen. James Inhofe (R-Okla.).[10] The bill, the Developing a Reliable and Innovative Vision for the Economy Act (DRIVE) Act (S.1647), largely keeps intact the

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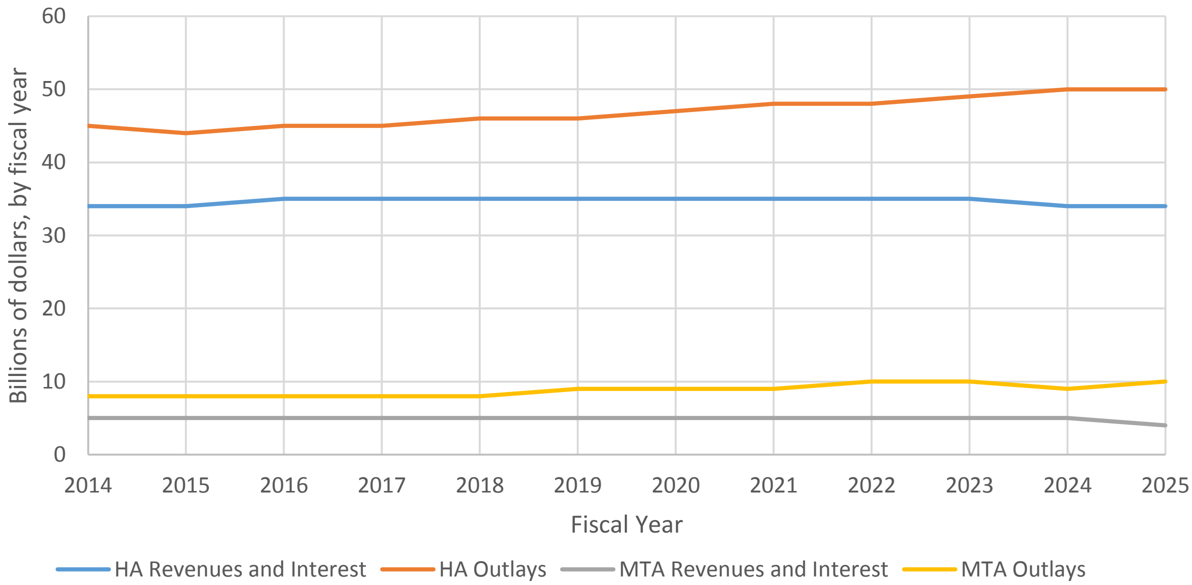
* *Marc Scribner is a Fellow at the Competitive Enterprise Institute.*

MAP-21 framework and fails to make key changes, some of which are endorsed by the Obama White House. Worse, it actively harms existing financing tools such as those provided under the Transportation Infrastructure Finance and Innovation Act,[11] which are needed by the private sector to compete in the transportation infrastructure market. And given Sen. Inhofe's repeated admission of, "I am a big spender in two areas—infrastructure and national defense,"[12] fiscal conservatives should be wary of his efforts regarding transportation policy, where his positions are largely indistinguishable from those of his colleague Sen. Barbara Boxer (D-Calif.).

Figure 1. CBO Projections of Highway Trust Fund Accounts



Source: Congressional Budget Office, Projections of Highway Trust Fund Accounts – CBO's March 2015 Baseline

Reforming Federal Highway Policy. Congress has long used what is known as the user-pays/user-benefits principle to guide highway funding. The Highway Trust Fund, established in 1956, was characterized by this principle for most of its history, with user tax revenues flowing into the HTF and outlays being set at or below projected revenues. Unfortunately, over the past decade, Congress has set HTF outlays above expected revenues, resulting in $60 billion HTF bailouts from the general Treasury.[13] Violating the longstanding user-pays principle has now become the new normal on Capitol Hill. From a fiscal responsibility standpoint, this is unacceptable. New practices must be adopted to reverse this dangerous trend toward general revenue transportation funding.

Many reform ideas have long enjoyed support from fiscal conservatives, including: devolving federal surface transportation responsibilities to the states, ending highway user revenue diversions to mass transit, repealing federal fuel taxation, and abolishing the Highway Trust Fund. However, such proposals are unlikely to take shape in the short run. Instead, a more realistic proposal would involve empowering states to make more of their own decisions regarding their highway systems, encouraging the adoption of innovative technologies and infrastructure management practices, and preventing legislative and regulatory interventions that would deny us these improved policies.

Short of full highway funding devolution, Congress should consider what could be called "de facto devolution." There are two element to this approach:

1) Equalize outlays with estimated Highway Trust Fund revenues and hold tax rates constant; and
2) Eliminate impediments to states generating their own user-based revenue.

In recent years, states have taken the lead on transportation funding and finance, with a number increasing their state fuel tax rates, considering public-private partnerships and innovative financing mechanisms, and expanded road user charges such as all-electronic tolling.[14]

To its credit, the Obama administration has endorsed some common sense reforms to transportation policy. These include ending the current federal prohibition on states tolling their own Interstate highway segments, and increasing the cap on and expanding the eligibility of private activity bonds (PABs) with a new bonding program called qualified public infrastructure bonds.[15] The national cap on the exempt facility PABs that support private-sector investment in transportation infrastructure is currently set at $15 billion.[16]

The case for expanding all-electronic tolling and private financing of Interstate construction and maintenance has been developed and championed by Reason Foundation Director of Transportation Policy Robert Poole.[17] Poole estimates that reconstructing the Interstate Highway System and doing necessary roadway widening will cost nearly $1 trillion over the next 20 years.[18] By charging 3.5 cents per mile for cars and 14 cents per mile for trucks, he concludes that 99 percent of the needed Interstate projects can be completed under modern all-electronic tolling revenue collection systems managed by the individual states.[19]

Critics of tolling, namely the trucking industry, will likely oppose federal and state efforts to enhance user charging. They and argue that tolling is unacceptable on roads that have already been paid for, and that too much highway user revenue is already diverted away from highways toward non-highway uses. These are legitimate grievances, but the problems are solvable. Poole has developed what he calls "value-added tolling" to address these concerns, and proposes five principles:

- Begin tolling only after major improvements (modernization/reconstruction) are completed;
- Limit the use of toll revenues to the specific highway or highway system where they are collected;
- Charge only enough to cover the cost to build, or rebuild, a highway, maintain it, and improve and eventually rebuild its facilities;
- Use tolls to replace existing user taxes, not add to them; and
- Provide a better level of service than what prevails on highways where tolling is introduced.[20]

Currently, all-electronic tolling is the best user-based regime available. Yet, direct and comprehensive road pricing may not be far off in terms of technical and fiscal feasibility. Oregon is leading the way with its Road Usage Charge program, the first major pilot of a mileage-based user fee system.[21] The program will likely prove cost-effective and fair in raising revenue, while protecting road user privacy and compliance choices.[22] The 5,000-volunteer pilot program is set to launch in July 2015.[23]

Proponents of sound transportation policy in Congress should "think outside the box" and look to new mechanisms and technologies to solve the nation's transportation problems, rather than just patching holes in the status quo. The bonus for Congress is that it need do very little in terms of embracing more robust user fees—it just needs to let states take the lead. But for this to happen, Congress must first untie the states' hands.

Reforming Federal Mass Transit Policy. The Highway Trust Fund's Mass Transit Account is in much worse shape than the Highway Account over the long run. And it is funded unfairly to boot. Virtually every penny in the Mass Transit Account is diverted revenue collected from drivers—2.86 cents from both the 18.4 cents-per-gallon federal gasoline excise tax and 24.4 cent federal diesel excise tax is dedicated to the Mass Transit Account.[24]

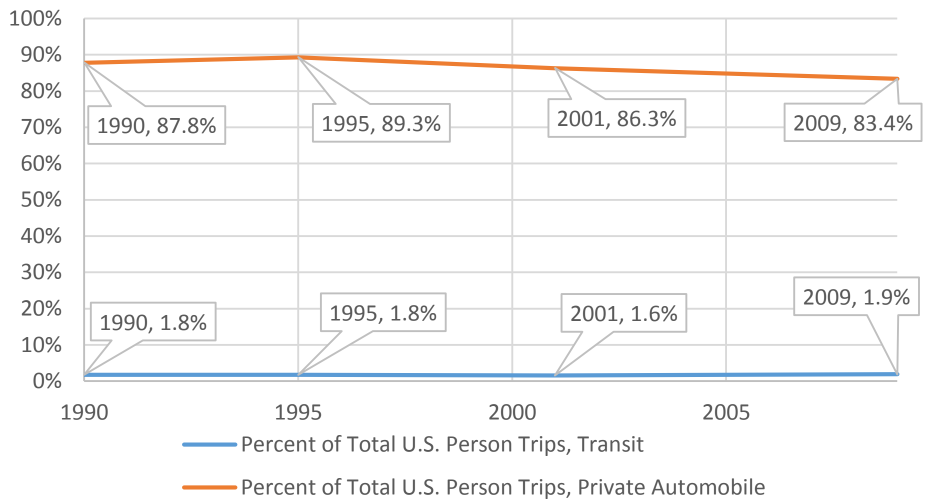
The Mass Transit Account was established within the Highway Trust Fund in 1982 by President Reagan. A recent study of newly unearthed archival material by Jeff Davis of the Eno Center for Transportation explains the motivations behind Reagan's 1982 fuel tax increase, which created the Mass Transit Account. As Davis notes, the Reagan administration assumed the fuel tax hike would fund an evolved federal-aid highway program that would lay the seeds for eventual highway and transit program devolution to the states.[25] Dedicating 20 percent of the fuel tax increase to mass transit was made to gain the support of urban liberals, who were generally opposed to fuel tax increases because fuel taxes are regressive.[26]

The surface transportation program devolution, which many believed to be imminent in the 1980s, never occurred. Today, nearly 20 percent of all federal surface transportation funds are directed to mass transit.[27] According to a recent analysis of 2010 Census data, mass transit accounts for less than 5 percent of commuting trips in the U.S., down from 6.22 percent in 1980.[28]

Moreover, commuting mode share figures overstates transit's relative importance to transportation overall, because commuting trips are approximately just 16 percent of total trips and mass transit is disproportionately used for commuting purposes.[29] The most recent National Household Travel Survey considered both commuting and non-commuting trips, and found that less than 2 percent of total personal trips are completed by mass transit in the United States.[30] According to the CBO, when expenditures from all levels of government—federal, state, and local—are considered, mass transit receives 28 percent of the $230 billion spent in 2014 on highways and mass transit.[31]

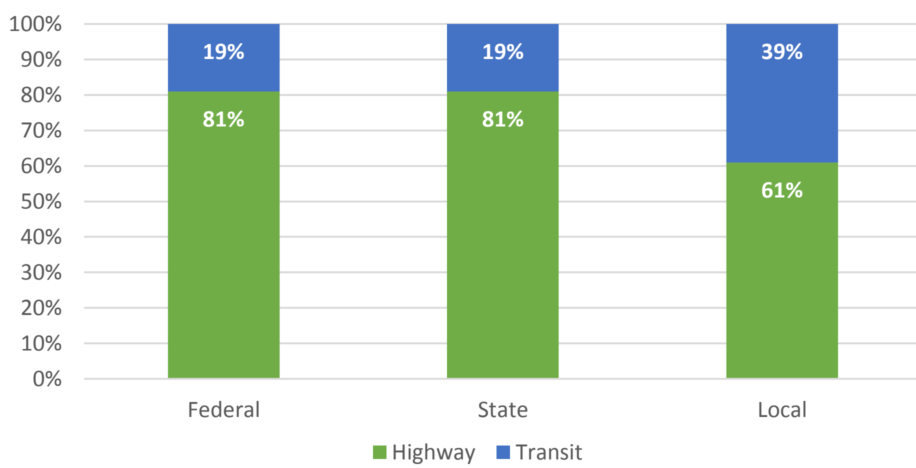
Some local government subsidies for mass transit may be justifiable to provide mobility and access to low-income residents, but it defies fiscal common sense to direct 25 percent of total government surface transportation expenditures to a mode with a market share of less than 2 percent. So, while many may support public transit subsidies based on the false belief that mass transit is effective in combatting traffic congestion, the vast majority of Americans have little desire to actually use mass transit. As *The Onion* once quipped, "A study released Monday by the American Public Transportation Association reveals that 98 percent of Americans support the use of mass transit by others."[32]

Figure 2. Share of U.S. Person Trips by Mode



Source: Federal Highway Administration, "Summary of Travel Trends: 2009 National Household Travel Survey," June 2011

Figure 3. Share of Spending, By Level of Government, 2007-2011



Source: "Intergovernmental Challenges in Surface Transportation Funding," Fiscal Federalism in Action Series, Pew Charitable Trusts, September 2014

More troubling, the Federal Transit Administration currently estimates that America's mass transit systems have an $86 billion deferred maintenance backlog and that transit agencies need to increase annual system preservation spending from $10 billion to $18 billion just to bring existing systems back to a state of good repair.[33] No one knows from where these additional funds will come, yet politicians continue pushing transit system expansions—a recipe for disaster.

Unfortunately, federal policy incentivizes ribbon-cutting over maintenance. Federal assistance to local transit is almost exclusively for new capital projects, and discretionary grants programs such as New Starts help drive rail transit waste by encouraging local transit agencies to dream up expensive and ostentatious plans.[34] Congress could remedy some of these problems by ending discretionary grants programs, rolling those funds into the traditional Urbanized Area Formula Program, and permitting the use of those federal funds for maintenance projects.[35]

If federal highway user revenues currently directed to mass transit from FY 2016-2025 were redirected back to core highway programs, the CBO's projected HTF revenue shortfall relative to outlays would be reduced from $168 billion to $77 billion over 10 years. Ending the major highway dollar diversion may be politically difficult, but it is important to remember that political pandering to the transit lobby is responsible for more than half of CBO's current projected HTF fiscal woes.

Just as important, states already fund the bulk of their own transportation needs. Given the federal government's small role relative to those of state and local governments, and even without ending the HTF diversions to mass transit, the projected $168 billon HTF shortfall would only account for about 8 percent of the nation's total surface transportation expenditures through FY 2025 assuming no increases in state and local spending. Surely, the states can pick up that slack, if Congress will let them.

Recommendations for Policy Makers. As noted, proponents of limited government are unlikely to see any radical changes in federal highway policy from Congress that would adhere to free market principles. While unfortunate, there are more modest changes that can move us in this direction, some of which enjoy bipartisan support.

To this end, Congress should reform highway policy by doing the following:

- Repeal the current federal prohibition on states tolling their own Interstate segments for reconstruction purposes, codified at 23 U.S.C. § 129.
- Uncap or greatly increase the national cap on private activity bonds, currently set at $15 billion, codified at 26 U.S.C. § 142(m)(2)(A).
- Provide technical and financial assistance to states looking to launch their own mileage-based user fee pilot programs.

The federal politics of mass transit could be described as an unfortunate mix of parochial and ideological interests battling over non-federal issues. Given that serious federal mass transit spending cuts are at the moment politically difficult, fiscal conservatives and proponents of sound national transportation policy should embrace some more modest goals to rationalize federal mass transit policy.

To this end, Congress should reform mass transit policy by doing the following:

- Work to end Highway Trust Fund bailouts and raise public awareness of the huge discrepancy between transit funding and transit use—that 19 percent of federal surface transportation funding is currently directed to a mode that accounts for less than 2 percent of trips nationwide.
- Roll existing discretionary transit grants programs such as New Starts into the Urbanized Area Formula Program.
- Realign spending priorities to a fix-it-first-strategy by allowing federal transit funds to be used for maintenance projects.

Notes

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