

## *Highway Funding in Texas: A Status Report*

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Highway funding in Texas will be a primary concern of the 81st Legislature. Lawmakers are expected to debate proposals to make more resources available for highways and to consider changes to the Texas Department of Transportation (TxDOT), the agency that administers highway funds in the state.

These issues arise in the context of a recent Sunset Advisory Commission review of TxDOT and a state auditor's report on the agency's accounting methods. Also, the 2030 Committee, charged by the Texas Transportation Commission (TTC) with calculating future highway funding needs, recently released a report concluding that Texas would need \$313 billion in highway funding over the next 21 years. In addition, the state will be deciding how best to use a one-time injection of \$2.7 billion for transportation projects in the recently enacted federal economic stimulus legislation.

This report reviews highway funding in Texas and the factors used to assess whether the state's resources are sufficient to meet growing demands on its roads. The report also examines proposals to expand resources for highways and to reform the agency that dispenses highway funds in the state.

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### Sources of highway funding

A substantial majority of the legislative appropriations to TxDOT goes to three primary activities related to the state's highways and bridges — planning and design, construction, and maintenance — which are divided as follows:

- **planning and design** — including engineering and design, right-of-way acquisition, traffic and road condition surveys, environmental impact studies, and funding for research programs at state colleges and universities;

- **transportation construction** — including contracts with private firms to build roads, bridges, and other facilities and money to acquire, maintain, and operate rail lines; and
- **highway maintenance** — including contracts with private entities to repair, rebuild, or rehabilitate roads and bridges; routine and preventive road maintenance by state-employed crews; repair of weather damage; and enforcement of laws on outdoor advertising and junkyards.

Additional appropriations go to aviation services, public and medical transportation, registration and titling, and administration.

TxDOT has broad authority to transfer appropriations to and among areas deemed essential to the state's transportation network. A transfer is introduced, approved, and recorded by the TTC at a public meeting through adoption of an order that contains the modified spending numbers. HB1 by Chisum, the general appropriations act for fiscal 2008-09, authorizes the agency to transfer funds into and among some of its most critical performance areas. A rider in the act authorizes the transfer of funds among contracted road maintenance, transportation construction, contracted planning and design, and right-of-way acquisition. Together, these major activities account for the vast majority of TxDOT's fiscal 2008-09 appropriation of \$16.92 billion. Among these activities, highway construction received the largest allotment with \$6.82 billion, followed by contracted maintenance with \$4.65 billion. Planning and design and right-of-way acquisition together received \$2.3 billion.

The authority to transfer funds to and among its most crucial activities allows TxDOT to influence the destination of most of its appropriations. This transfer authority, in addition to other factors, means that the agency's budgeted appropriations and actual expenditures often diverge significantly. From fiscal 1999 to fiscal 2007, spending reported in TxDOT's legislative appropriations requests differed from appropriations for transportation construction and routine and contracted maintenance. In each year from fiscal 1998 to fiscal 2007, the agency spent consistently more on highway maintenance than the Legislature appropriated for those activities and considerably

less on transportation construction than legislative appropriations would suggest.

Several initiatives beginning in 2001 aimed to expand the range of funding options for transportation projects in Texas. Taken together, these initiatives marked a significant departure from the traditional "pay-as-you-go" approach to highway finance, under which the transportation agency and its districts completed projects with available revenue, primarily from federal and state motor fuels taxes. Legislative changes after 2001 gave TxDOT more flexibility for funding transportation projects, including the authority to issue bonds, borrow from public and private interests, and enter into comprehensive development agreements (CDAs) to build and maintain toll roads.

TxDOT's current budget reflects the expanded revenue sources made available through recent legislation. The agency's current budget is an amalgam of dedicated funding sources, including state and federal motor fuels taxes, vehicle ownership and operation-related fees and taxes, and bonding authority entrusted to the TTC. The largest portion of TxDOT's \$16.92 billion fiscal 2008-09 appropriation comes from federal Highway Trust Fund (HTF) reimbursements and State Highway Fund 6 (Fund 6) revenue. Of this total, 38.4 percent, or \$6.49 billion, came from federal highway trust fund reimbursements, and 31.3 percent, or \$5.3 billion, was from Fund 6. Another 23.7 percent, or \$4.01 billion, was bond revenue. In a supplemental appropriation, the Legislature also made available \$300 million in general revenue funds in fiscal 2008, primarily to help the agency pay debt service on previously issued bonds.

### *State Highway Fund 6*

Fund 6 is the state's primary highway funding mechanism, collecting the vast majority of highway-related revenue from federal reimbursements, state motor fuels taxes, motor vehicle registrations, and various fees. The Legislature may appropriate funds from Fund 6 for various highway-related purposes, in accord with constitutionally and statutorily established limits. State statutes further restrict the dollar amount of bonds that may be issued on the fund's credit, and the Texas Constitution requires that revenue from Fund 6 be used to pay minimum necessary debt service on bonds and other public securities secured by Fund 6.

The comptroller’s fiscal 2008-09 certification revenue estimate in fall 2007 placed Fund 6 revenue for fiscal 2008-2009 at \$14.2 billion.

**Federal funding.** Federal reimbursements, primarily from the federal HTF, make up the single largest share of revenue in Fund 6. Of the total estimated balance in Fund 6 for fiscal 2008-09, about 48.6 percent, or \$6.9 billion, comes from reimbursements from the HTF for state highway-related expenditures. The HTF is funded through state-by-state collections from a number of sources, including the federal motor fuels tax of 18.4 cents a gallon, and federal taxes on tires, vehicle weight permits, and truck and trailer sales.

The most recent federal law governing federal transportation funding, the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU), authorizes reimbursements to the states of revenue from federal motor fuels and

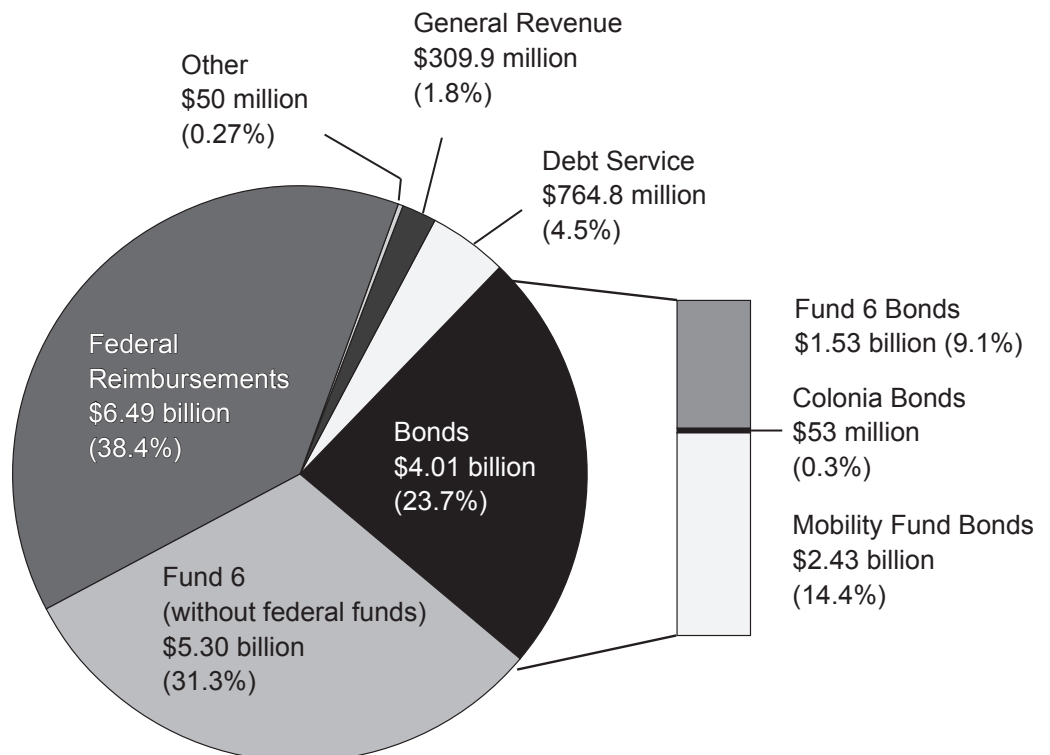
other taxes collected in the HTF. The reimbursements are divided into pre-defined highway and transit categories and must, with some flexibility, be spent on projects that adhere to restrictions in each category. Major highway funding categories include interstate maintenance, the national highway system, bridges, surface transportation, highway safety, congestion, and air quality improvement.

SAFETEA-LU guarantees to states a minimum rate of return based on each state’s share of federal motor fuels tax revenue collected and transferred to the HTF. States with certain characteristics defined by population density, total population, median household income, interstate fatality rates, and the rate of indexed state motor fuel taxes, are governed by special rules. SAFETEA-LU also sets a minimum threshold of total reimbursements to states based on funds disbursed under the previous federal transportation authorization law, the Transportation Equity Act for the 21st Century (TEA-21).

## Sources of highway appropriations in Texas

*This chart shows fiscal 2008-09 appropriations by method of financing. Appropriations for debt service were split between Fund 6 revenue bonds payments at \$330.7 million, and Mobility Fund bond payments at \$434.2 million.*

*Source for data: Fiscal 2008-09 General Appropriations Act.*



**Total = \$16.92 billion**

The disbursement formulas in SAFETEA-LU yield varying rates of return to the states, with some states receiving a greater percentage of their contributions to the HTF in return. Some states, including Texas, are net donors to the HTF, while others are net beneficiaries. SAFETEA-LU authorizes funds in a certain amount to the state, but of this amount, the state may be reimbursed for no more than a pre-approved portion, called an obligation limitation.

**State motor fuels tax.** The second-largest share of revenue going into Fund 6 comes from the state motor fuels tax of 20 cents per gallon on diesel and gasoline and 15 cents per gallon on liquefied gas. The Texas Constitution, Art. 8, sec. 7-a, dedicates one-fourth of state motor fuels tax revenue to the Available School Fund, with the remaining three-fourths dedicated to highway-related purposes, including constructing, maintaining, and policing public roadways. One percent of the motor fuels tax revenue is deducted to enforce state motor fuels tax laws before the remainder is deposited into Fund 6. The comptroller estimated that

for fiscal 2008-09, state motor fuels taxes would account for \$4.55 billion, or 32.1 percent, of Fund 6 revenue.

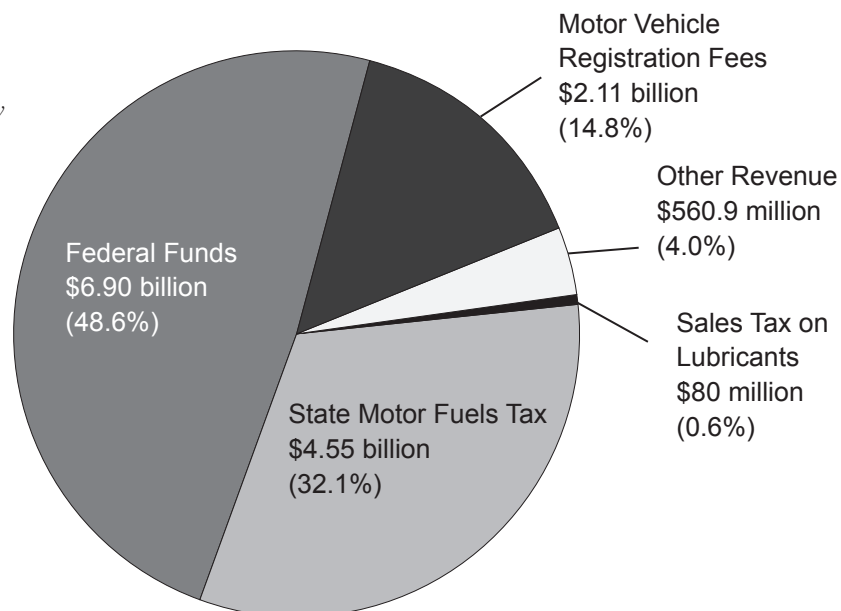
**Fund 6 revenue bonds.** Since 2003, the TTC has been authorized to issue bonds secured by revenue collected in Fund 6. In 2007, the Legislature increased the total Fund 6 bonding authority available to \$1.5 billion per year, not to exceed \$6 billion in total. The TTC recently authorized TxDOT to issue the \$2.9 billion still available in Fund 6 revenue bonds, and the Bond Review Board has approved \$1.5 billion to be issued in fiscal 2009. As of January 2009, the agency had yet to issue the approved debt.

State statutes also require that the TTC issue \$1.2 billion of the total Fund 6 bonds for projects that improve highway safety and reduce hazardous road conditions. As of January 2009, the agency had spent \$600 million in Fund 6 revenue bonds under this requirement and was identifying more projects eligible to receive the remaining bond funds.

### Fund 6 revenue sources

*This chart shows estimates of revenue for State Highway Fund 6 for fiscal 2008-09 by source. Amounts do not include balances from preceding fiscal years.*

*Source for data: Comptroller Certification Estimate, 2007.*



**Total = \$14.20 billion**

**Other sources.** Fund 6 also receives revenue from motor vehicle registration fees, sales taxes on motor vehicle lubricants, vehicle certificates, special vehicle registrations, and fees related to commercial transport. Vehicle registration fees are collected annually by counties, which may retain a portion for administration and road maintenance. The comptroller estimated registration fees deposited to Fund 6 at \$2.1 billion, or 14.8 percent of the account’s total revenue, for fiscal 2008-09. Estimated revenue from sources other than motor vehicle registrations totaled \$641 million for fiscal 2008-09, about 4.5 percent of the total share of Fund 6.

Fund 6 also receives revenue from one-time concession payments for the rights to develop and operate toll roads. In fiscal 2008, Fund 6 revenue included a \$3.2 billion payment from the North Texas Tollway Authority for SH 121 in the Dallas-Fort Worth metropolitan area. The Fund also included \$25.8 million from an up-front payment as part of a private agreement with Cintra-Zachry to develop two segments of SH 130. Current state law requires revenue received as part

of toll agreements to be spent in the geographic area in which it was collected.

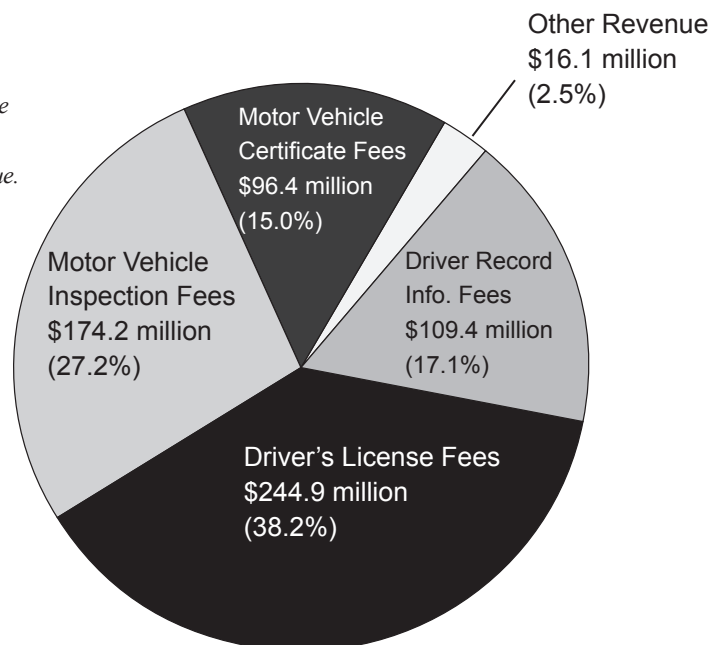
**Texas Mobility Fund**

Since it was created in 2001, the Texas Mobility Fund (TMF) has received an increasingly diversified stream of revenue from dedicated sources. The TMF is established and regulated in the Texas Constitution and further restricted by state statutes. The Legislature designated the TMF as a mechanism through which the TTC may borrow funds from public and private interests and may issue bonds for the design, construction, reconstruction, acquisition, and expansion of state highways and to help fund publicly owned toll roads. Bonds and debt obligations are secured by the revenue deposited to the TMF and by the state of Texas. Before issuing more bonds from the TMF, the comptroller must certify that the fund has available revenue equal to at least 110 percent of the amount necessary to pay principal and interest due yearly for the term of the proposed bonds.

**Texas Mobility Fund revenue sources**

*This chart shows estimates of revenue for the Texas Mobility Fund for fiscal 2008-09 by source. Amounts do not include bond revenue.*

*Source for data:  
Comptroller of Public Accounts.*



**Total = \$641 million**

The TMF receives fees collected for vehicle inspections, driver's licenses, driving record information retrieval, and motor carrier penalties. Of these, the largest contribution to the fund in fiscal 2008-09 came from driver's license fees, at \$244.9 million, followed by motor vehicle inspection fees, at \$174.2 million, driver record information fees, at \$109.4 million, and motor vehicle certificate fees, at \$96.4 million. Other fees deposited into the account were estimated to be \$16.1 million for the biennium. The 80<sup>th</sup> Legislature directed funds from certificates of title fees to the TMF starting in fiscal 2009. The comptroller estimated total revenue flowing to the TMF as \$641 million in fiscal 2008-09.

As of January 2009, TxDOT had issued \$5.1 billion of the total \$6.4 billion in bonds authorized through the TMF to date. According to the agency, the remaining bonds have been committed to ongoing projects and will be issued when balances associated with those projects come due.

### *General revenue*

The Legislature typically appropriates general revenue to TxDOT as needed for specific purposes. The

80th Legislature in 2007 appropriated \$300 million in general revenue to TxDOT to issue and pay debt service on bonds. TxDOT reports spending \$112 million of the general appropriation for debt service on bonds backed by Fund 6 and the remaining \$188 million on short-term debt. Another general revenue account, the Texas Highway Beautification Account, comes from fees on billboards, and appropriations from this fund total \$1.2 million for fiscal 2008-09. Overall, general revenue was 1.8 percent of TxDOT's fiscal 2008-09 appropriations.

### A highway funding crisis?

Concerns about highway funding were amplified by a fall 2007 announcement from TxDOT that the agency faced an imminent funding crisis and needed to act decisively to forestall serious long-term funding shortfalls. The agency advised district engineers that cuts to programs and some project delays were imminent, and it reduced its fiscal 2008 letting schedule, which specifies how much money district offices may spend on priority projects in a year, from a previously authorized \$4.2 billion to \$3.1 billion. TxDOT also ordered districts and divisions to reduce operating costs by 10 percent and required all purchases to be approved

## Status of the federal Highway Trust Fund

Many analysts have warned in recent years that the federal highway trust fund, which collects motor fuels tax revenue and reimburses states for eligible transportation expenses, would face financial insolvency around fiscal 2009. Analysts predicted that around this time, receipts from federal motor fuels taxes no longer would be sufficient to keep pace with reimbursements due to lower-than-anticipated returns from those taxes, diversions of HTF funds, and unanticipated highway-related expenses, such as the I-35 bridge failure in Minnesota.

President Bush's proposed fiscal 2009 budget estimated a deficit in the fund of at least \$3.3 billion. The estimate led Congress in September 2008 to enact HR 6532, transferring \$8 billion from general revenue to the highway trust fund. The bill reversed an identical transfer of funds from the trust fund to general revenue in 1998. Supporters of the measure expect it to compensate temporarily for major shortfalls in the fund, at least until SAFETEA-LU, the federal law governing fund reimbursements, is reauthorized after fiscal 2009.

The HTF also likely will be the vehicle through which funds allocated by the American Recovery and Reinvestment Act of 2009, signed by President Obama on February 17, will be distributed to states. Funds for highway construction, which total \$27.5 billion, will be disbursed using federal apportionment formulas.

by the central office in Austin. Although TxDOT later revealed that the reduction in the letting schedule had resulted from an accounting error, the agency points to multiple, converging factors from both federal and state sources that may contribute to long-term budgetary shortfalls.

TxDOT estimated that rescissions in funding from the federal highway trust fund could total more than \$1 billion for fiscal 2008-09. The agency cited as a factor the predicted financial insolvency of the federal HTF as soon as fiscal 2009, when requests for reimbursement were predicted to exceed incoming revenue. TxDOT also pointed to ongoing inflation in highway construction and maintenance costs and a decline in the resulting purchasing power of appropriations for these purposes as a major factor in the shortfalls.

TxDOT also asserted that while the 80th Legislature appropriated funding above the levels for fiscal 2006-2007, the additional funds principally were bond proceeds obligated to paying for projects that had been authorized previously. The agency argued that the limits on private partnerships to build toll roads that were imposed in 2007 by SB 792 had made it difficult to enter into such agreements. Without the option of effectively leveraging private investment in new construction, TxDOT said, it would not be able to muster enough resources to develop new road projects. The agency also noted that the Legislature had diverted nearly \$1.57 billion in transportation revenue from Fund 6 to other purposes. According to TxDOT, fiscal 2008-09 biennial appropriations included a 15 percent increase from previous biennial diversions of appropriations to other state agencies.

### *Projected funding gaps*

Even before TxDOT's announcement in fall 2007 of a funding shortage, support for expanded highway funding options had been boosted by projections of a growing gap between highway improvement demands and available funding. These projections, completed by both TxDOT and the Governor's Business Council,

compared increasing demands on state roads from growing populations, vehicle registrations, and annual vehicle miles driven with relatively fixed resources available for new roads and maintaining existing highways. Many analysts have pointed to flat motor fuels tax rates in place in Texas since 1991 and nationally since 1993 to argue that traditional transportation taxes have declined in relative value while the costs of road construction have increased.

In 2006, after asking the state's metropolitan

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planning organizations (MPOs) to identify road improvements necessary to bring congestion to acceptable levels by 2030, TxDOT identified a highway funding gap of \$86 billion by 2030. The state's MPOs estimated the combined dollar

amount needed to be \$188 billion. TxDOT estimated that in the same time frame, \$102 billion would be available from existing funding sources. A state auditor's report on the projected funding gap revised downward the \$86 billion total figure after determining that \$8.6 billion should not have been included in the total. The report revised the total projected funding gap to \$77.4 billion. The report concluded that while the projected funding gap could help assess highway funding needs generally, it should not be used to make policy or funding decisions because it contained costs that should not have been included, a mathematical error, and additional undocumented costs. In a 2006 report, the Governor's Business Council projected an even lower funding gap of \$66 billion over 25 years.

**2030 Committee.** In summer 2008, TTC chair Dierdre Delisi established a committee to assess the state's transportation needs through the year 2030. The 2030 Committee, which included transportation experts from industry, government, and academic backgrounds, held a total of six public hearings in the summer and fall of 2008.

The committee released its report on the state's transportation needs in December 2008. The committee reviewed funding needs for highway maintenance, including bridges, for urban mobility and rural mobility and safety, and for other transportation needs. The 2030

Committee suggested that the state's highway network would require \$313 billion in improvements between 2009 and 2030 — or about \$14.2 billion a year. Of this total, the committee called for \$89 billion in highway pavements, \$36 billion for bridges, \$171 billion for urban mobility improvements, and \$17 billion for rural mobility and safety.

### *Calculating funding needs in Texas*

The extent to which highway funding shortfalls in Texas constitute a crisis remains in dispute. Calculations of potential shortages are inherently imprecise, with varying definitions of “funding needs” and difficulty in projecting available future funding. Assumptions differ on ideal maintenance levels and the road and bridge expansions necessary to accommodate growing populations. Calculating the funds necessary to maintain the state's roads also relies on an assessment of their current condition.

**Current highways conditions.** TxDOT assesses the condition of state roads and highways with a Pavement Management Information System (PMIS) score. This system measures three aspects of road quality — distress, ride, and condition. Distress is defined as the extent of surface deterioration, such as potholes, cracks, ruts, and other surface fissures, while ride is the smoothness of the pavement surface. The condition score is a combination of distress and ride and is meant to be a basic indication of the quality of the state's roads. A condition score of 90 - 100 is described as “very good,” 70 - 89 as “good,” 50 - 69 as “fair,” and 35 - 49 as “poor.” Roads with a score below 35 are considered “very poor.”

In 2001, the TTC established a goal that 90 percent of the state's pavement lane miles be in at least “good” condition by fiscal 2012. A recent TxDOT study based on data from 2004 to 2007 found the overall percent of state lane miles receiving a “good” or better condition score dipped slightly during that period. In 2004, 87.02 percent of state lane miles received a “good” or better condition score, while in 2007, 86.76 percent received this rating — a decline of 0.25 percent. In spring 2008,

TxDOT estimated that bringing state roads to the “good” condition goal adopted by the TTC by 2019 would cost \$23 billion.

### *Estimating available highway funding*

In addition to assessing the current condition of the state's highways and estimating the funds necessary to bring the system to optimal standards, an evaluation of the current funding situation must include estimates of available future revenue. Most long-term projections of

available highway funds rest on calculations of future state and federal funding, which are derived largely from motor fuels taxes. Such estimates are complicated by current fiscal instabilities of the federal HTF, uncertainty about future re-authorizations of federal transportation funding after

SAFETEA-LU expires in 2009, and stagnation and declines in motor fuels tax revenue.

**Highway fund rescissions.** Recent and potential future shortfalls in the HTF present further obstacles to estimating the funds that may be available in the future. Funds originally authorized through SAFETEA-LU have been rescinded — that is, taken back by the federal government — each fiscal year since the law was enacted. The amount Texas is authorized to spend and subsequent rescissions of these funds have varied each year and have totaled \$924 million since fiscal 2005.

Funding rescissions generally apply to “unobligated balances,” which are funds states have yet to commit to transportation projects. Unobligated balances include accumulations of funds previously authorized as part of annual budget cycles but not spent. States have accommodated past rescissions of unobligated balances by amending project schedules to reflect the adjusted available funds. Most states have been able to provide for these rescissions by delaying or canceling projects in any of the funding categories established in SAFETEA-LU.

While the rescissions posted from 2005 through 2007 instructed each state to choose how to distribute the adjusted apportionments, the 2008 rescissions granted less flexibility to states in deciding how to

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accommodate rescinded funds. The 2008 rescissions included specific instructions on the amount of both unobligated balances and the actual programmed funding that would be rescinded. The accumulation of rescinded funding over the past several years has diminished TxDOT's unobligated balances enough to require the agency to release funds already committed to building highway projects. TxDOT funding of \$258 million in unobligated balances was subject to rescission in fiscal 2008, and the agency said it was charged with refunding \$13.5 million in funding already committed to projects.

***Uncertainty of motor fuels tax revenue.*** Some transportation analysts have speculated that sharp increases in the price of gasoline, such as those in the summer of 2008, could compel people to drive less, creating a decline in motor fuels tax revenue. Reports citing declines in gas tax revenue in 2008 have surfaced in some states, including Idaho, Louisiana, North Carolina, Vermont, and Washington. Federal Highway Administration data on national traffic trends reveal that

monthly estimated vehicle miles traveled were lower in each month from November 2007 to November 2008 than they were in corresponding months in the previous year. Cumulative national vehicle miles traveled in 2008 as of November were down 102.1 billion vehicle miles, or 3.7 percent, when compared with the previous year.

In Texas, motor fuels taxes in fiscal 2008 did not show a clear decline resulting from higher gasoline prices. Annual gasoline tax collections for fiscal 2008 exceeded those of fiscal 2007 by \$14.5 million, or 0.6 percent. Diesel fuel tax collections for fiscal 2008 grew by \$33.2 million, or 4.4 percent, from fiscal 2007. Gasoline tax revenue increased modestly in every quarter except summer when compared to fiscal 2007. In summer 2008, gasoline tax revenue fell by \$11.8 million, or about 2 percent, compared to the same time one year before. Diesel revenue increased in every quarter, although collections did not increase significantly in summer. Combined gasoline and diesel tax revenue increased \$47.8 million, or 1.6 percent, in fiscal 2008.

## Federal law governing highway funding

Most federal highway funding to the states is disbursed through the federal Highway Trust Fund (HTF), a process governed by a law known as SAFETEA-LU (the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users). Signed into law in 2005 and effective through fiscal 2009, SAFETEA-LU authorizes a total of \$244.1 billion in federal transportation reimbursements to the states for highways, transit, and safety programs.

SAFETEA-LU guaranteed Texas a 92 percent minimum rate of return for the state's contribution to the HTF for fiscal 2008-09. However, a 2006 paper by the Texas Department of Transportation (TxDOT) estimates that the true rate of return for Texas is lower than it appears in SAFETEA-LU. The paper argues that because only certain funds are taken into account when the rate of return is applied, the true rate of return for Texas is 83 percent for highway funds. When this is multiplied by the percent of motor fuels tax that goes to the highway fund from Texas, the state receives only a 70 percent return for highway programs. The paper estimates that the rate of return for transit programs is only 51 percent. Altogether, the paper argues that for each dollar Texans pay in federal motor fuels taxes, the state has returned to it only 70 cents for highway programs and 8 cents for transit programs.

Some also argue that the value of SAFETEA-LU is diminished by the abundance of earmarks contained in the statute, categorized under the law as "high-priority projects." Critics of projects designated as earmarks contend that they circumvent local planning and may divert funding from more critical projects. Highway funding analysts have identified more than 5,000 earmarks in SAFETEA-LU from 2005 to 2009. TxDOT estimated that more than 200 projects earmarked for the state in the bill could cost \$8.2 billion, yet it received \$691 million in federal funds to help with construction of the earmarked projects for the authorization period. For example, the agency received only \$8.3 million of the \$50 million earmarked for the I-69 corridor.

Quarterly variations in statewide gasoline tax collections in fiscal 2008 may be explained, in part, by the effect of rising gasoline prices on discretionary driving. Summer, the only quarter that exhibited a decline in gasoline tax revenue, is a popular travel time for many Texans. Drivers concerned by the steady increase and spikes in gas prices may have scaled back, cancelled, or postponed auto-related travel plans during summer and other major holidays.

Motor fuels tax revenue also may be affected by economic recessions, increased fuel efficiency, use of alternate means of transportation, and other factors that compel people and businesses to scale back driving. Motor fuels tax revenue for the first four months of fiscal 2009 was lower than similar months in previous years. Total motor fuels tax collections for September through December were down \$49.9 million, or 4.7 percent, when compared with the same time period the previous year.

### *Statewide infrastructure demands*

Estimates of necessary highway funding also rely on assumptions about demands on existing roads now and in the future. This demand is defined principally by the number of drivers, the average miles traveled on Texas roads, and the capacity of the existing highway system. Texas highway use statistics from 1998 to 2006 show a large increase in the number of registered vehicles, annual vehicle miles traveled, and gallons of gasoline and diesel consumed in the state. The state's status as a major domestic and international trade hub has added to the wear on the state's transportation infrastructure. Texas is a major destination and through-route for trucks hauling freight from abroad, mainly at ports of entry along the U.S. - Mexico border.

**Highway use trends.** Population growth and increases in international and domestic truck freight recently have increased demands on the state's highways. The FHWA estimates that annual vehicle miles traveled in Texas on national highway system roads rose by 20.9 percent from 1998 to 2006, while the number of registered vehicles increased by 31.6 percent. Gasoline and diesel consumption during this period increased 18.8 percent, according to estimates from the Texas Transportation Institute (TTI). From 1998 to 2006, demands on the state's highways exceeded the 2.4 percent growth in "lane miles," a measurement of the

total mileage of state-maintained roads. International truck freight also has increased in recent years. Brownsville, El Paso, Hidalgo, and Laredo all were major points of entry for trucks passing into Texas in 2006. More than 3.2 million trucks crossed the U.S. - Mexico border into Texas in 2006, with nearly half, 1.52 million, passing through Laredo. Truck freight from Mexico increased by 19.1 percent from 1998 to 2006.

The Texas Transportation Institute predicts a gradual decline in gallons of gasoline sold and an overall leveling-off of total fuel sold over the next two decades. This prediction assumes a steady increase of fleet fuel efficiency from 17.2 gallons per mile in 2008 to 21.7 gallons per mile in 2015.

**Highway funding and inflation trends.** Highway-related expenditures more than doubled between fiscal 1999 and fiscal 2007, increasing by 105 percent from \$3.95 billion to \$8.01 billion. The value of the \$4.15 billion growth in spending during this time was tempered somewhat by inflation in the cost of maintaining and expanding highways, which eroded some of the buying power of the state's transportation funding dollars.

According to TxDOT's highway cost index (HCI), which documents and compares the cost of similar highway construction goods and services over time, construction costs increased by 66.6 percent from fiscal 1999 to fiscal 2007. The HCI is a composite of cost statistics across a variety of road construction categories. It includes costs for goods and labor necessary for road construction, including earthwork, road and bridge structure, sub-grade materials, and surfacing treatments.

When highway expenditures are adjusted to reflect inflation reported in the HCI, they show a less substantial increase. Adjusting for the recorded inflation in highway construction costs during this period, highway expenditures grew by \$911 million, or 23 percent, from fiscal 1999 to fiscal 2007.

The Texas motor fuels tax also has diminished in relative value since it was set at 20 cents in 1991. Annual inflation in all major economic sectors has eroded the buying power of the original per-gallon tax, especially when accounting for inflation in highway construction costs. TxDOT's HCI inflation measurement does not go back to 1991, so an adjusted accounting of

the motor fuels tax for observed inflation in highway building costs cannot be calculated easily. As adjusted by the Texas Consumer Price Index, which is based on inflation measurements in the Dallas-Fort Worth and Houston areas, the value of the 20-cent motor fuels tax decreased consistently from 1991 to 2008. Adjusting for inflation in 1991 dollars, the motor fuels tax in 2008 was worth about 13 cents, or 65 percent of its original value. In other words, the state motor fuels tax has lost at least a third of its inflation-adjusted value since it last was raised in 1991. The value of the motor fuels tax today would be smaller still if it were based on inflation in the cost of road construction and maintenance.

### *Short-term responses to the funding shortfall*

Much of the recent debate about highway funding in Texas has focused on whether TxDOT should have used available short-term bond funding to offset immediate shortfalls. Legislation enacted in 2007 substantially increased the Fund 6 revenue bonds available to the agency, which now total \$1.5 billion per year up to \$6 billion. Some lawmakers advocated issuing available bonds to offset immediate funding shortfalls, whereas others maintained that the agency already had surpassed a threshold of maximum advisable debt and should wait for the Legislature to convene in 2009 to address any funding shortfalls with more long-term solutions. Debate about whether the agency should issue more debt paralleled controversy over whether the state should issue general obligation bonds to support highway improvements.

In an August 2008 memo, Gov. Perry, Lt. Gov. Dewhurst, and then-Speaker Craddick urged TTC chair Dierdre Delisi to support the issuance of Fund 6 revenue bonds immediately available. They suggested the bonds would ensure sufficient funding for pressing transportation needs until the Legislature reconvened and had a chance to discuss funding strategies outlined in the memo. At a special meeting on August 29, the TTC adopted an order approving issuance of \$1.5 billion in Fund 6 revenue bonds for fiscal 2009.

## Highway funding proposals

Concerns about highway funding have prompted several lawmakers to announce intentions to address the topic in the 81st legislative session, leading to a number of proposals to revise current funding practices. With TxDOT and the TTC under Sunset review, lawmakers will have an opportunity to review both funding for highways in Texas and the administrative structure of the agency that oversees highway programs.

### *Expanding highway-related taxes and fees*

The diminishing value of the state motor fuels tax has been the subject of periodic legislative efforts to increase the tax per gallon, to index the tax to increase annually with inflation, or to allow local entities to hold elections to approve a local-option increase of motor fuel taxes in their jurisdictions.

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*Lawmakers will have an opportunity to review both funding for highways in Texas and the administrative structure of the agency that oversees highway programs.*

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### *Indexing or increasing the motor fuels tax.*

Recent discussions about expanding the statewide motor fuels tax have focused largely on indexing the tax to an inflation index, such as the consumer price index or the producer price index, rather than raising the tax directly.

Supporters of indexing or increasing the motor fuels tax say doing so is necessary to ensure the viability and longevity of the state's transportation network. They say that charges on motor fuels should be viewed as user fees, as opposed to taxes, and are functionally similar to a postage stamp in that the amount must be raised periodically to accommodate the increasing cost of providing the service. Supporters argue that increasing revenue from the sale of motor fuels would help ensure the integrity of the state's highway network and should be used in conjunction with other funding arrangements to ensure the state's ability to maintain and enhance its highways. They add that the small annual increase in gas prices that would result from indexing would have little impact on Texas families, especially relative to wide fluctuations in gasoline and diesel fuel prices in 2008.

Opponents of indexing or increasing the motor fuels tax say such an action is neither desirable nor politically feasible. Instabilities in the average price of gasoline have placed a strain on many Texas families, and any measure that would increase the price would be met with resistance by the public. Indexing the motor fuels tax, opponents say, would place an added strain on many struggling Texas families and do little to resolve the state's highway funding woes. A motor fuels tax increase sufficient to close the transportation funding gap substantially would impose an untenable burden on Texas families, opponents say.

**Local-option fees and taxes.** Another proposal would authorize local entities to hold elections to increase motor fuels taxes in their jurisdictions. Local entities could authorize a vote on a per-gallon tax on motor fuels or a sales tax on motor fuels. The option of holding elections to increase local fuel taxes could be limited to counties, or it could be expanded to other transportation entities, such as regional mobility authorities. Lawmakers also may consider other local-option measures dedicated to highway funding, including raising the cap on sales taxes for transit or allowing counties to impose additional fees for motor vehicle registration, motor vehicle emissions, driver's license renewal, mobility improvement, or parking regulation and management within their jurisdictions.

Previous debate on local-option motor fuels taxes has centered on the extent to which benefits associated with such taxes would outweigh the burdens they could impose on consumers and businesses. Supporters argue that authorizing these taxes would be permissive — left to the discretion of the residents in potentially affected jurisdictions — and would be confined largely to those areas in the state in greatest need of timely highway expansions. Opponents of local-option taxes argue that increasing taxes on a piecemeal, jurisdictional basis would create potentially dangerous precedents for localized fiscal policies that do not necessarily observe statewide goals and priorities for fiscal restraint. Imposing a higher fuels tax selectively in a single jurisdiction also might encourage some drivers to fill up in neighboring counties where gas is cheaper and may burden businesses with higher energy costs.

**Expanded motor taxes and user fees.** Texas has a variety of fees associated with vehicle ownership

and operation. Some of these fees, such as driver's license fees, fully accrue to transportation-related accounts, whereas others, such as vehicle title fees, go only partially to those accounts. Lawmakers may consider revisiting the type or amount of these fees or may look at increasing the portion of existing fees that accrues to transportation accounts. Interim discussions of transportation-related fees included the possibility of redirecting some portion of revenue collected from motor vehicle sales taxes or oil and gas severance revenue to transportation accounts.

### *Increasing highway bonding authority*

In November 2007, voters approved Proposition 12 (SJR 64 by Carona) authorizing the Legislature to issue up to \$5 billion in general obligation bonds for highway improvement projects. While voters approved the constitutional amendment authorizing the bonds, the Legislature did not enact contingent legislation to authorize issuance of the bonds or appropriate the bond revenue, so no Proposition 12 bonds have been issued. SB 1929 by Carona, an enabling bill that was considered during the 2007 regular session but ultimately failed to be enacted, would have placed the proceeds from the bonds in a toll project equity fund to make loans to local, county, or regional authorities for toll or turnpike projects.

A number of lawmakers have expressed their intent to introduce legislation to specify the dollar amount of Proposition 12 bonds that should be issued and for what purposes the bond revenue should be appropriated. The language in the original proposition is sufficiently flexible to allow for a variety of transportation-related appropriations. Proposition 12 bond funds could be used broadly to pay for construction projects and associated planning and right-of-way acquisition or could go to ongoing highway maintenance.

Supporters of issuing more bonds say that doing so would help finance some desperately needed projects, which would provide a statewide benefit to the economy. Supporters note that while the Texas Constitution prohibits state-supported debt from exceeding 5 percent of uncommitted general revenue, state debt currently is well below that maximum, leaving room for additional general obligation bonds backed by state general revenue. Issuing the bonds would not have a significant

impact on the state's fiscal standing, supporters say, and Texas still would have a low debt burden compared to other states.

Supporters say borrowing against future general revenue would speed up highway projects, thus alleviating traffic congestion, enhancing productivity, improving safety, and reducing negative economic and social impacts that stem from inadequate highway infrastructure. Improving mobility sooner rather than later would aid economic development and job creation in the midst of a national economic recession. Issuing the general obligation bonds soon is critical in light of diminishing availability of Fund 6 revenue bonds and TMF bonds and in view of recent highway funding shortfalls.

Opponents of issuing more bonds say long-term borrowing to pay for state highway improvements

through general obligation bonds would require general revenue appropriations the state cannot afford to spend on debt service. Texas has a longstanding policy of funding transportation projects solely through dedicated funds. Borrowing money for construction increases costs because interest must be paid on the bond proceeds and these costs are passed along to future taxpayers and legislatures. Texas should continue to pay for the highway construction it can afford, rather than obligate scarce general revenue and drive up the cost of already expensive projects by adding interest payments.

Opponents say adding even more debt would increase the general revenue needed for debt financing and could limit the state's ability to meet other needs. They say highway projects should be paid for through Fund 6 and with bonds borrowed through transportation-related funds that are secured with revenue from motor fuels taxes and vehicle registration fees, and thus from

## Federal stimulus funds for highways

On February 17, President Obama signed the American Recovery and Reinvestment Act of 2009, commonly called the federal stimulus bill. The bill authorized \$787 billion in spending, tax cuts, and program support, including an allocation of \$48.1 billion for transportation projects. States must obligate funds for eligible projects within a limited time or the funds may be redistributed to other states. To be eligible for funds, a state also must certify that it will maintain current funding for similar highway projects.

Of the stimulus funds committed to transportation, the bill appropriates \$27.5 billion for highway, bridge, and other construction projects. Other funds include \$8 billion for inter-city high-speed rail, \$6.9 billion for transit capital assistance grants, \$1.5 billion for competitive grants for transportation infrastructure, \$1.3 billion for Amtrak improvements, and \$2.9 billion for rail and airports. Highway and bridge construction funds will be distributed by federal apportionment formulas and made available to states through reimbursements for expenses that meet certain criteria. The bill gives the highest priority to highway and bridge projects that can be completed in three years and that are in economically distressed areas, as defined in federal law. Half of any unobligated highway and bridge funds will be withdrawn and redistributed within 120 days after funds are allocated, and any remaining unobligated funds will be withdrawn after one year. Funds for public transit, rail, and other purposes are subject to different requirements.

The Legislative Budget Board estimates that the state could receive \$2.3 billion for highway and bridge construction and \$372 million in transit funds. About two-thirds of eligible highway and bridge projects will be selected by the Texas Transportation Commission and 30 percent will be for projects selected by Metropolitan Planning Organizations. The state also could receive \$2.6 million for rail modernization and may be eligible to apply for additional competitive grant funding programs for highway, transit, aviation, and rail projects.

those who use state roads. Opponents say it would not be in the state’s best interest to commit general revenue that could be used for other urgent state needs, such as education and children’s health care, to pay for debt service for bonds to build highways.

**Restoring Fund 6 appropriations**

Not all Fund 6 appropriations go to TxDOT. The 80th Legislature in 2007 appropriated \$1.95 billion, or 13.8 percent, of total Fund 6 revenue to other state agencies. The largest share of this net amount, \$1.01 billion, was appropriated to the Department of Public Safety (DPS) for a variety of purposes. Another \$720 million was appropriated for benefits for employees of several state agencies, \$120 million to other agencies for a variety of purposes, and \$100 million to the Texas Education Agency to buy school buses. In fiscal 2006-07, \$1.75 billion, or 11.7 percent, of the Fund 6 appropriation was directed to purposes other than road construction and maintenance. Of this amount, \$787.7 million was appropriated to DPS for a variety

of purposes and \$657.7 million went to state employee benefits.

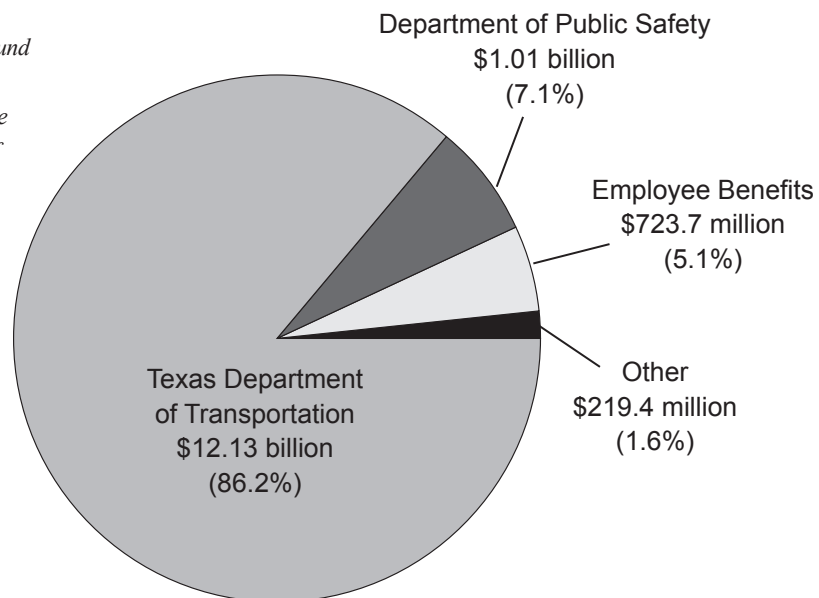
About 60 percent of DPS’s fiscal 2008-09 appropriations come from Fund 6, and revenue from the fund is disbursed across a number of departmental functions. The funding principally goes to law enforcement activities, including highway patrol, vehicle inspections and enforcement, and roadside alcohol testing. Other funds support activities of the department’s criminal law enforcement division, including narcotics enforcement, motor vehicle theft investigations, criminal intelligence services, and the crime laboratory.

Several lawmakers have expressed an interest in redirecting to TxDOT these so-called diversions from Fund 6 to agencies and purposes not directly related to highway construction. In a letter to TTC Chair Delisi, Gov. Perry, Lt. Gov. Dewhurst, and then-Speaker Craddick expressed agreement to work during the 81st legislative session to return to funding DPS with

**Appropriations from Fund 6**

*This pie chart shows appropriations from Fund 6 by agency and purpose for fiscal 2008-09. ‘Other’ amounts include \$100 million for the Texas Education Agency for the purchase of school buses.*

*Source for data:  
Legislative Budget Board*



**Total = \$14.08 billion**

general revenue instead of motor fuels taxes. Gov. Perry reiterated his support for ending Fund 6 diversions to DPS in his January 2009 state of the state address.

Transferring general revenue in an amount adequate to fund the agencies and other expenses now dependent on Fund 6 revenue would place these agencies in competition with other state needs for limited general revenue funds. Debate on redirecting diverted Fund 6 revenue to TxDOT is likely to focus on whether doing so would constitute a *de facto* transfer of general revenue to highway funding, and if so, whether this transfer is necessary or desirable in the context of limited funds.

### *Revising tolling practices*

Alternative means of financing transportation projects, including toll roads, have been an ongoing source of controversy in the state. Opposition formed against proposed local toll projects and the Trans-Texas Corridor, which would have included a network of toll roads connecting major population centers in the state and acting as thoroughfares for domestic and foreign freight. TxDOT recently announced plans to suspend work on the TTC as a whole, focusing instead on key routes contained in the proposal.

Some have opposed the concept of toll roads entirely, while others have criticized private development and operation of toll roads through comprehensive development agreements (CDAs), “non-compete” clauses in contracts with private developers, TxDOT’s management of planning and contracting, and toll facilities added to existing roads and highways.

***Private participation in toll projects.*** Debate about the effectiveness and desirability of private financing of toll roads hinges on several factors, including the availability of public funding, the amount of risk inherent in toll road development, the state’s ability to build, operate, and maintain such roads efficiently, and the value of long-term returns on toll road investments.

Supporters of private financing of toll roads say private financiers can bring abundant resources to toll projects that are unavailable to the public sector. They note that many private toll road developers have international asset and capital bases that they may leverage to finance the initial acquisition and

construction of toll facilities. Private toll road development agreements may bring the state more initial income in the form of concession agreements, provide the state a portion of ongoing revenue collections, and relieve the state from the responsibility of building or maintaining the road.

Supporters say that by selling the rights to develop and operate toll projects to private entities, the state shields itself from the unavoidable risks associated with these projects. These risks, supporters say, are inherent in every aspect of toll development. Estimates of initial construction costs, maintenance and operation costs, how many drivers are willing to pay tolls, and what price drivers will pay to use toll roads are all unknown values that determine the ultimate profitability of the project.

Miscalculations in project planning and market studies could cause revenue forecasts to fall short, creating risks of project failure and bankruptcy. Leasing toll projects to private developers eliminates such risks for the state and provides revenue in the form of concession fees and other contractually specified returns. States may refuse to aid private toll operators who lease the rights to develop unprofitable toll roads. Florida, for example, has turned down requests for help from private toll developers.

Supporters also say private developers often maintain and operate toll facilities more efficiently and consistently. Private entities have a vested interest in maintaining toll roads because deteriorating road quality affects the number of drivers using the road and the amount of revenue collected by the tolling authority. State maintenance of roads, by contrast, is subject to the vagaries of politics and the legislative appropriations process. Money may be directed to new road construction and away from maintenance and operation, and such diversions from maintenance result in declining road quality over time.

Opponents of private financing of toll roads say the value of the transportation assets the state loses by leasing out development rights usually exceeds any benefits it might enjoy as a result of ceding operation rights. Opponents say that the capacity of private financing to minimize the risks inherent in developing a toll road is overstated. Private developers are not likely to gamble with toll roads that they do not expect

to yield significant net profits over their lifetime, and it is unlikely that the state could credibly deny financial or contractual assistance to a private interest operating a failing tollway. Toll projects that do not expect to yield generous returns on investment are not sought as aggressively by private interests.

Because roads are built only at great public expense and are built on rights of way often acquired through eminent domain and because roads act as critical public assets by giving motorists access to important destinations, the state is deeply invested in their continued, viable operation. As a result, the notion that the state could simply deny requests for intervention or assistance that, if withheld, could lead to the failure and closure of a tollway is highly questionable. If a private

company leased a toll project that failed to be profitable, the state would be compelled to take on the expense of buying out the private entity and assume maintenance of the road or to amend the contract to include terms more favorable to the private interest.

Opponents say the best course for toll road development is to offer the option to local tolling authorities before offering it to private interests. Local, public tolling entities and private interests share pressures to maintain toll roads as time passes, and they have more flexibility and self-determination in decision-making than does the state. Local, public tolling authorities also provide for the recirculation of revenue from toll roads into maintaining local transportation infrastructure. Successful public toll

## Current law on financing toll roads

SB 792 by Williams, enacted by the 80th Legislature in 2007, placed a limited, two-year moratorium on the state's entering into contracts that would authorize private entities to operate or collect revenue on toll roads. The bill provided exceptions for specifically designated highways and for tolled lanes added to existing highways if the projects met other conditions. With some exceptions, SB 792 also accelerated the expiration date for TxDOT's authority to enter into comprehensive development agreements, which are contracts with private entities to finance, construct, maintain, operate, or expand a tolled highway project, from August of 2011 to August of 2009, and it limited the spending of revenue from these agreements to the geographic area in which the revenue was collected.

SB 792 also gave local toll authorities the right of first refusal, or primacy, over private entities for developing toll projects in their areas. If a local entity opts to develop a project but does not adhere to a specified timeline, the option to develop the project reverts to TxDOT and the TTC, which must develop it within the same timeline. The bill charges TxDOT and the TTC with helping local entities develop, finance, build, and operate a toll project undertaken by a local entity.

Local entities must negotiate toll development agreements with TxDOT. A tolling agreement must be preceded by a market valuation study carried out jointly by the negotiating parties that includes traffic, cost, and revenue projections. If a local toll entity and TxDOT cannot reach an agreement on terms and conditions, the project becomes ineligible for development as a toll road.

SB 792 also raised the cap on the dollar amount of Fund 6 revenue bonds that TxDOT may issue from \$3 billion to \$6 billion and increased the agency's annual cap on issuing bonds from \$1 billion to \$1.5 billion. The bill also established a legislative study committee to examine the implications of private toll road developments. In December 2008, the Legislative Study Committee on Private Participation in Toll Projects released its report stating that conventional finance methods no longer are sufficient to provide necessary highway improvements and must be supplemented with carefully crafted public-private partnerships.



roads become future engines of transportation funding, whereas privately funded toll roads export revenue to shareholders internationally.

**Market valuation.** Lawmakers may take up other aspects of current law governing private financing of toll roads, largely contained in SB 792 by Williams, enacted by the 80th Legislature in 2007. Debate about SB 792 paralleled broader discussions about private involvement in highway development. Much of the debate on the bill centered on the market valuation process it established. The market valuation process requires TxDOT and a local public tolling entity, which has primacy over private entities to develop toll projects, mutually to agree to the terms and conditions for the development, construction, and operation of a toll project being negotiated. The market valuation study also requires that TxDOT and the local authority take into account traffic and revenue projections for the project and that they agree to the assumptions and other factors upon which these projections are based.

Critics of the way the bill's market valuation process has been implemented say it is an inordinately complicated and drawn-out process and should be overhauled or eliminated. Flexible language in the bill, they say, has been interpreted as authorizing what amounts to a "concession fee" on local tolling authorities for the right to develop and manage a toll road. Critics say this merely substitutes one pot of public funding for another, as local entities must recover the cost of upfront bond issuances through increased toll fares.

Without these massive upfront payments that have become associated with the market valuation process, public toll entities could direct more revenue to other local projects, rather than pay off bond obligations that accrue substantial interest over time, critics say. The market valuation process does not account for the long-term value inherent in publicly owned and operated toll roads, critics say, and it mistakenly applies the same standards of value to public and private resources. Revenue from public toll projects, they claim, will be reinvested in local infrastructure over time.

Others argue that while imperfect, the market valuation process has merit in creating a systematic process for negotiations between TxDOT and local tolling entities that serves as a stand-in for negotiations with private entities. Without a structure for bargaining, such negotiations would be highly project-specific and could create overwhelming advantages for public tolling entities compared to private bidders. Without a parallel process, TxDOT would have little leverage to negotiate toll development proposals with public entities that best serve the state's greater interests. With revisions, the market valuation process could be tailored to better suit the needs of the state and public tolling entities, say its supporters.

#### *Exploring new funding options*

In the wake of TxDOT's announcement of funding shortfalls, the threat of fiscal insolvency in the federal HTF, and project suspensions stemming from the 2008 letting schedule reductions, state lawmakers may decide to explore new funding options.

**Using pension plans as investment.** At a March 2008 Senate Finance Committee hearing, lawmakers heard testimony from pension fund investment experts on the feasibility of using state pension reserves to support the development of infrastructure projects and discussed the advantages and disadvantages of such investments.

A March 2007 TxDOT study on pension plan investment in transportation infrastructure reported an estimated rate of return for infrastructure investments of between 12 and 16 percent. Pension investments in infrastructure, according to the study, may take the form of public or private trading of infrastructure funds, public-private partnerships for toll roads and other user-fee funded infrastructure, or outright purchase of an infrastructure project. The study argued that the largest risk in such investments is that infrastructure projects could be derailed before they were developed fully or before contracts were executed fully.

The TxDOT study cited a federal requirement, known as the exclusive benefit rule, that pension plan

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*State lawmakers may decide to explore new funding options.*

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assets be used only for the benefit of employees and beneficiaries of the plan. State pension plans in general are subject to different investment philosophies and are beholden to their respective boards of trustees and investment managers, and pension investments must be approved through internal processes. Texas Constitution, Art. 16, sec. 67a(3) charges state retirement system boards with investing funds in the interest of the fund's long-term health and with attention to the likely return and security. The provision allows the Legislature to restrict the investment discretion of a pension board.

One means of promoting pension fund investment in infrastructure would be to establish transportation finance corporations, which could collect revenue that could be used for funding those road projects with good long-term return potential. Gov. Perry, Lt. Gov. Dewhurst, and then-Speaker Craddick suggested this in an August 2008 memo to TTC Chair Delisi as one possible solution to transportation funding challenges to be pursued in combination with ending diversions from Fund 6 and authorizing \$5 billion in approved general obligation bonds for roads.

Debate about promoting pension fund investment in infrastructure projects may focus on the state's ability to encourage such investments, how to quantify risks associated with infrastructure projects, potential controversy surrounding state pension investment in toll road projects, and likely returns on investment obtained through such projects.

**Vehicle Miles Traveled (VMT) tax.** One approach to raising revenue for transportation that has received some national attention is taxing drivers based on the number of miles traveled, rather than the amount of fuel consumed. This approach, called a vehicle miles traveled (VMT) fee, has been implemented on a limited basis in a pilot program in Oregon. The program uses electronic odometer devices and gas pumps specially designed to track miles driven and assesses fees accordingly. Participating vehicles also are fitted with GPS devices to exclude miles driven outside state lines.

Supporters of the VMT say the long-term value of the motor fuels tax is threatened by greater fuel efficiency and fluctuations in gas prices. The less people drive and the more efficient the fleet at large, the less revenue is available for transportation projects. VMT

programs can be tailored to local political conditions and modified to reward more fuel-efficient cars and other vehicles with less impact on the environment or on transportation infrastructure.

Opponents of the VMT argue that its net value in efficiency in taxation would be overshadowed by the serious privacy concerns it would pose and the incentives it would eliminate for buying newer, more fuel-efficient cars. Fully and effectively implementing the VMT, opponents say, would require equipping automobiles with invasive technology that tracked their location, miles traveled, and course of travel. This information would have to be stored and accessed to levy an accurate fee, and as such would present the potential for gross invasions of privacy and unwarranted surveillance.

### *Reforming TxDOT*

Several policymakers and advocates have suggested that the state not only should address funding for transportation improvements but also should revise how transportation projects are managed and implemented in Texas. Much of this discussion centers on the extent to which TxDOT is transparent in selecting projects and contractors, responsive to public concerns, accountable to legislative policies and intentions, and capable of efficiently planning and implementing infrastructure improvements around the state. Broader concerns about the agency have come into focus in two state agency reviews of its operations and finances — one by the Sunset Advisory Commission and another by the state auditor.

**Planning and financial management.** At a joint hearing of the Senate Finance and Transportation and Homeland Security committees in February 2008, several lawmakers expressed concerns about planning and financial management practices at TxDOT. These concerns were magnified by an agency revelation that the reduction in the 2008 letting schedule was the result of an accounting error. According to TxDOT's testimony, an internal miscalculation in the 2008 letting schedule based on the July 2007 forecast prompted the release of an erroneously inflated letting authorization of \$4.2 billion. The agency trimmed the original, overstated figure to \$3.1 billion and released the revised schedule to district engineers in fall 2007. The

accounting error revealed at the hearing prompted a call for a state auditor's investigation into the agency's financial management and accounting practices.

**Sunset advisory process.** Subsequent hearings on the announced shortfall, along with ongoing review of the agency by the Sunset Advisory Commission, resulted in further review of TxDOT financial and planning practices. The Sunset staff report, released in June 2008, recommended extending the agency, whose authorization is due to expire in 2009 under the Sunset process, for only four years, to 2013. The staff report suggested that TxDOT has come to evoke distrust and frustration among the public and lawmakers and that this hampers the agency's ability to carry out its mission effectively. It recommended enhancing legislative oversight and measures to restore confidence in the agency's operations and administration.

The report recommended that to increase accountability, the five-member TTC should be dissolved and replaced with a single commissioner appointed by the governor and subject to Senate confirmation every two years. If the governor failed to appoint a commissioner by February 28 of each year that the Legislature was scheduled to meet, the lieutenant governor could appoint a commissioner without confirmation.

The report also recommended that a legislative oversight committee made up of members of the House and the Senate be broadly charged with monitoring TxDOT's construction-related operations, analyzing the transportation system, assessing funding options and recommending strategies, advising on potential corrective legislative action, and reviewing the agency's research program. The report also called for transferring contracting and funding authority for the Texas Transportation Institute (TTI), the state's premier transportation research program housed at Texas A&M University, directly to the Legislature. This would move the authority to enter into interagency contracts from TxDOT to the Legislature, which would fund highway research programs directly through the legislative appropriations process.

In December 2008, the Sunset Advisory Commission issued its decisions regarding TxDOT, upholding many staff recommendations, including replacing the five-member TTC with a single appointed

commissioner, establishing a transportation legislative oversight committee, and continuing the agency for four years until 2013. The commission also recommended transferring the agency's motor vehicle functions, including vehicle titles, the motor vehicle and motor carrier divisions, and burglary and theft prevention, into a new agency, the Texas Department of Motor Vehicles. The recommendations also would require TxDOT to establish a Rail Transportation Division that would be charged with developing rail plans, coordinating funding for rail projects, and overseeing projects funded through state funds set up to fund rail improvements.

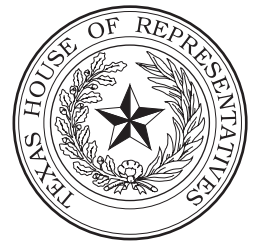
**State auditor's report.** In February 2008, Lt. Gov. Dewhurst and then-Speaker Craddick directed State Auditor John Keel to conduct a comprehensive review of TxDOT's financial processes. The audit request was prompted by TxDOT's revelation that its 2008 letting schedule had been erroneously inflated due to an accounting error. The letter asked the auditor to give special attention to the agency's cash forecasting practices and assumptions, formulas it uses to assign and move funds to and among districts, and its claims that the cost of highway maintenance increased by 60 percent between 2002 and 2007.

The State Auditor's Office issued its report in September 2008. The report determined that the \$1.1 billion cash forecasting error resulted from lack of communication, misinterpretation of cash forecast results, and an overly complex reporting structure. The report acknowledged that the agency had taken corrective steps by relocating divisions involved in projections and forecasting to the department's finance division. The report recommended that the department keep the full TTC better informed of significant developments affecting the agency and implement a documented and formal process for determining contract award schedules. The report also advised the department to follow established procedures for cash forecasting and implement a forecast approval process that clearly specifies which individuals and divisions are responsible for reviewing the forecast and in what time frame.

— by **Andrei Lubomudrov**

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