

# The Broken Federal User-Pay System

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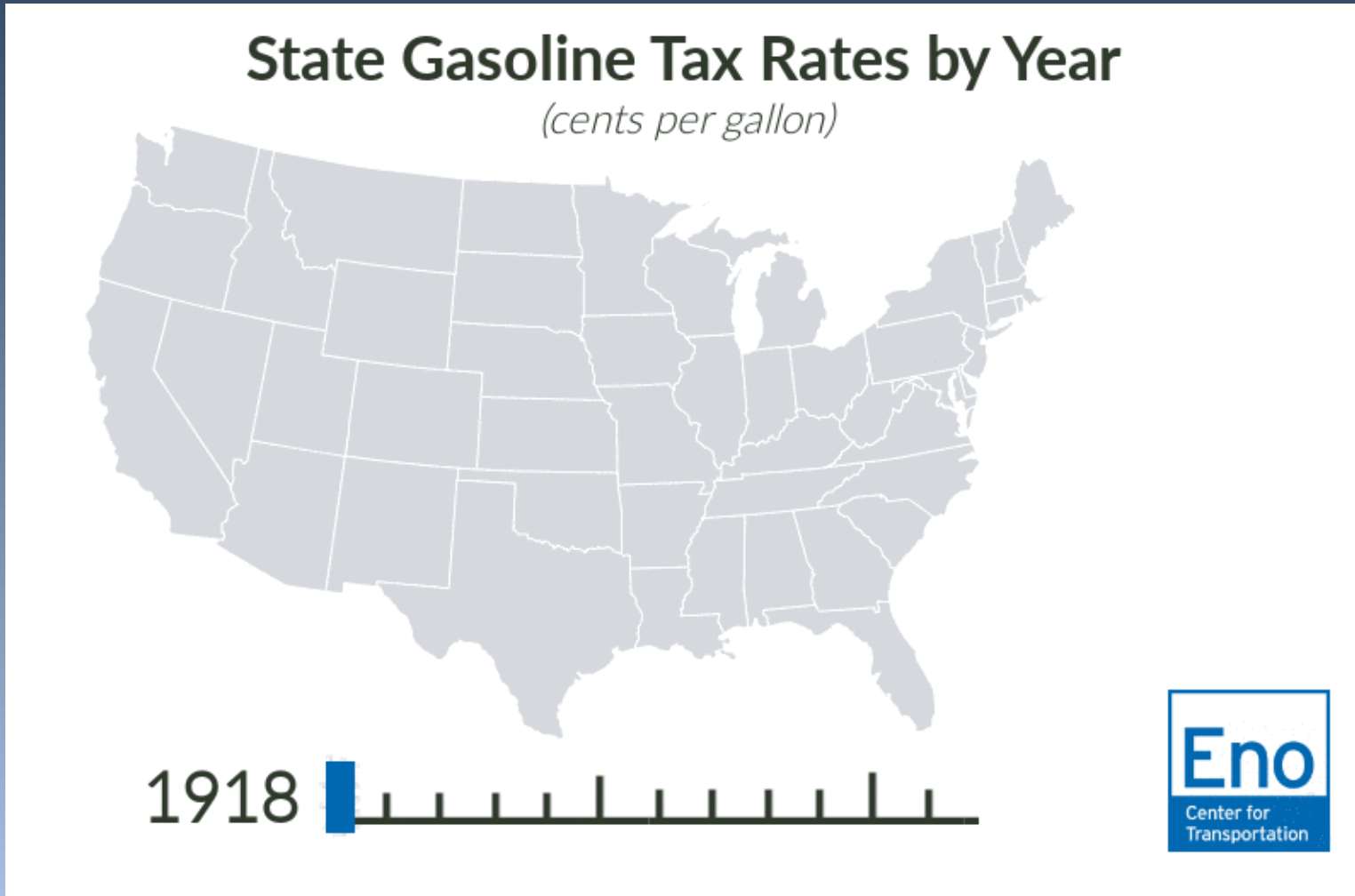
Senor Fellow

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# 1919 – First U.S. State Gas Taxes

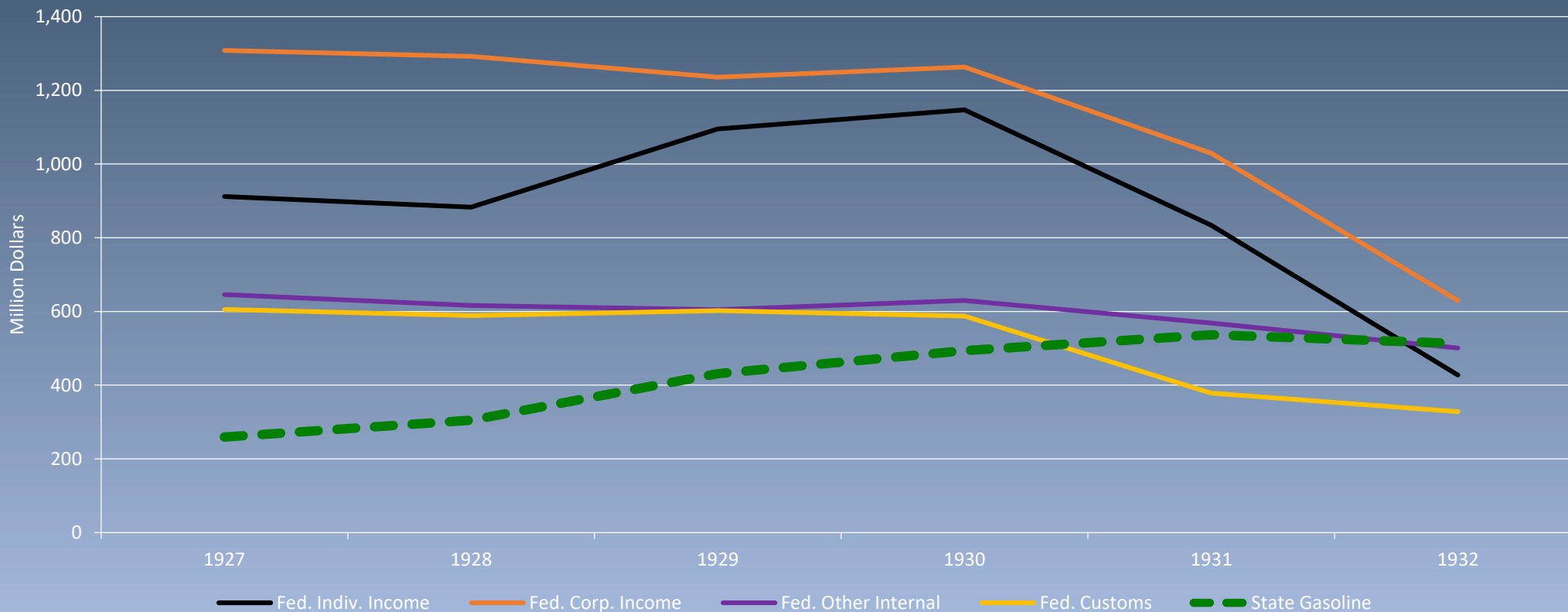
- 1916 – Federal-aid highway program created – states needed to raise their 50% matching funds.
- Western states were first to tax gasoline for roads. Gasoline tax chosen as alternative to property tax.
- Oregon – Feb. 25, 1919 – 1 cent per gallon (equal to 15¢/gal. today).
- New Mexico (1¢), Colorado (2¢), North Dakota (1¢) later that year.
- **North Carolina: 1921 (1¢)**

# 1919-1929: All 48 States Adopt



# 1932: Depression Forces Congress to Tax Gasoline

## Federal Revenue Sources vs. State Gas Tax Receipts, FY 1927-1932



# Feds Slow to Adopt User-Pay

- 1932 – Federal gasoline tax for general revenues only.
- 1934 – Federal Hayden-Cartwright Act (hypocritically) penalized states that diverted highway user tax revenues for non-highway purposes.
- 1952 – Congress enacts a law expressing sense that “each service or thing of value provided by an agency...to a person...is to be self-sustaining to the extent possible.”
- Budget Bureau/OMB begins to promote user-pay concept under every President since Truman.

# User Taxes into Trust Funds

Three steps:

1. Levy excise taxes or user fees on a sector or group.
2. Deposit those tax receipts into a special trust fund, not the general fund.
3. Enact a law providing that the only allowable appropriations from that trust fund are for programs that provide direct benefit to those who paid the excise taxes.

# Transportation Goes User-Pay

- 1956 – Highway Trust Fund.
- 1970 – Airport and Airway Trust Fund.
- 1978 – Inland Waterways Trust Fund.
- 1982 – Mass Transit Account added to Highway Trust Fund (after Congress rejected stand-alone Mass Transit Trust Fund in 1978 and 1980).
- 1986 – Harbor Maintenance Trust Fund.

# User-Pay Based on Cost Allocation

- Ideally, a user-pay, user-benefit system will be based on cost allocation that does two things:
  - Determine the costs that each class of system user incurs on the system (direct costs like pavement and bridge wear-and-tear but possibly also “externalities” like congestion, safety, noise and air quality), and
  - Tailor the revenue scheme so that the taxes and fees paid by each class of user matches up with the costs they incur.
- It is also very important that the type of user tax be as reliable and non-volatile as possible.

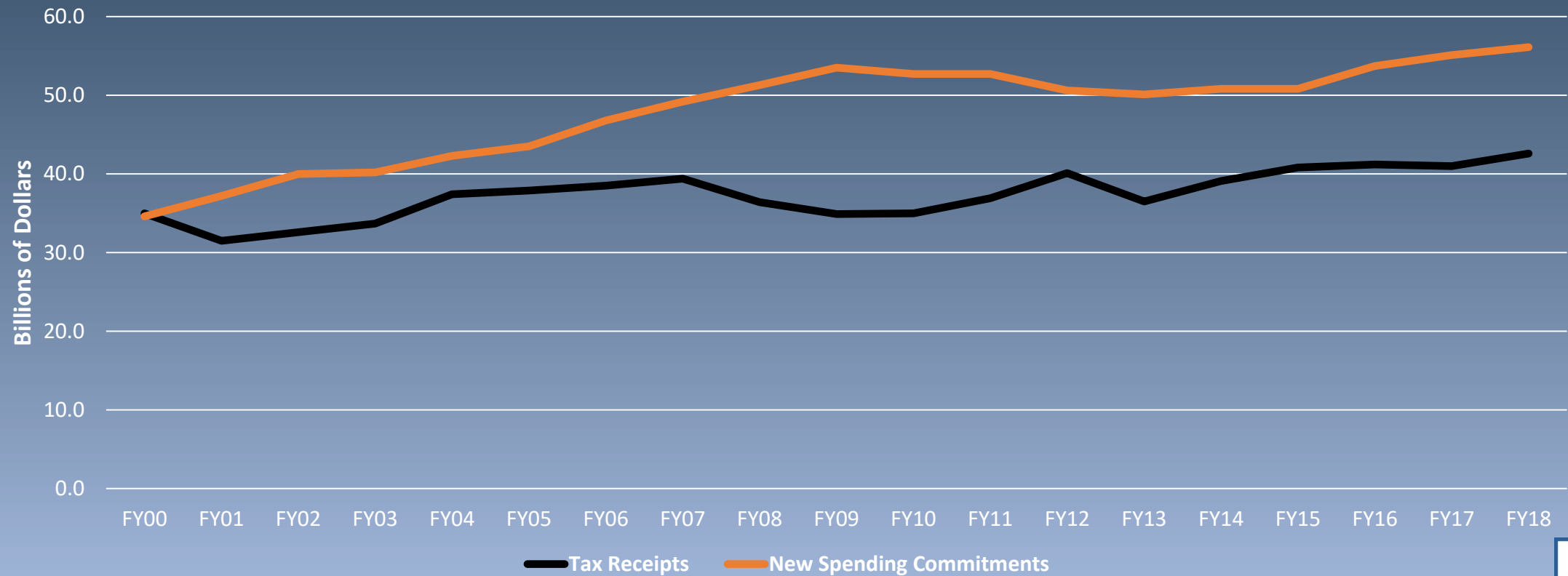


# Highway User-Pay Model: Broken

- The whole point of a trust fund is to synchronize special (non-general) tax receipts with the spending on programs that give special benefit to those taxpayers.
- Congress last raised gasoline/diesel taxes in 1993 and those taxes were transferred to the HTF in FY 1999.
- Since 2000, HTF revenues have grown an average of 1.2% per year, but Congress has enacted laws to allow new HTF funding commitments that grow an average of 3.5%/year.

# Highway User-Pay Model: Broken

Highway Trust Fund, FY 2000-2018



# Highway User-Pay Model: Broken

## STEIN'S LAW:

“Things that can't go on forever, don't.”

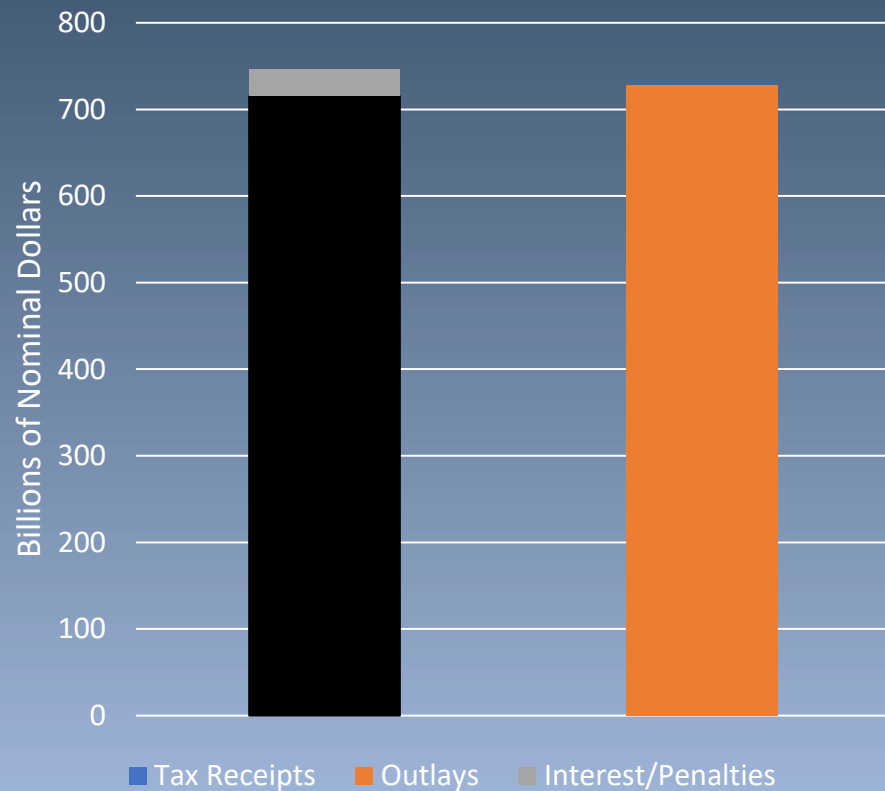
--Herbert Stein, chairman, Council of Economic Advisers under President Nixon.

# Highway User-Pay Model: Broken

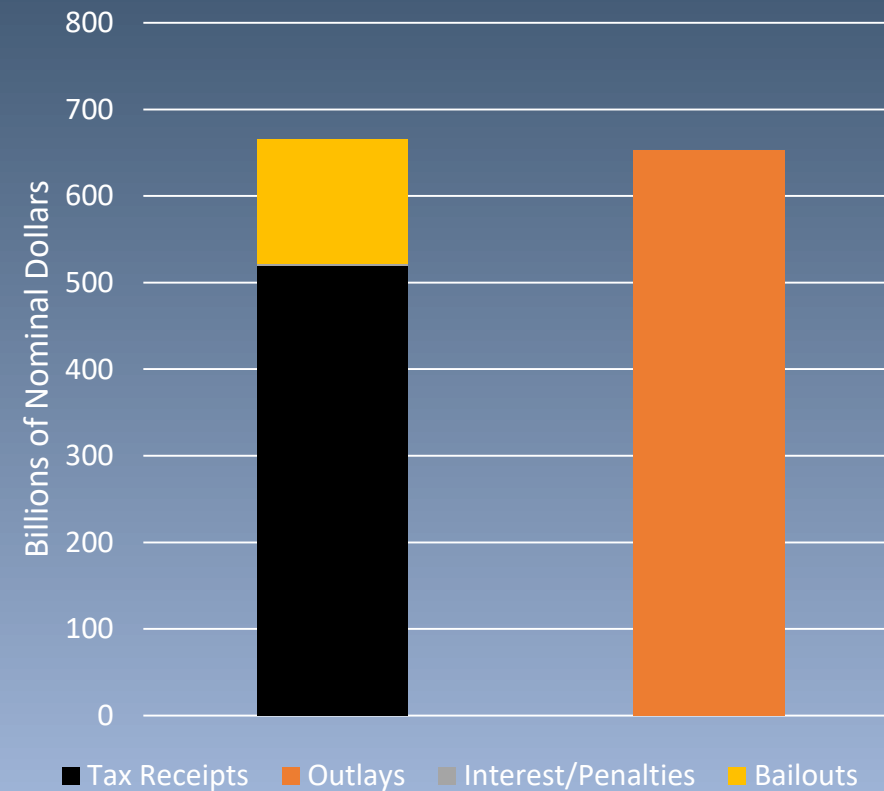
- HTF ran out of money in September 2008.
- Since then, Congress has been unable to cut spending below prior year levels but has also been unable to increase excise taxes on road users.
- Result: \$140 billion in bailout transfers from general revenues have been made since 2008.
- The last bailout (\$70 billion in Dec. 2015) will run out, at current spending levels, in summer 2021.

# Highway User-Pay Model: Broken

## Highway Trust Fund FY 1957-2007

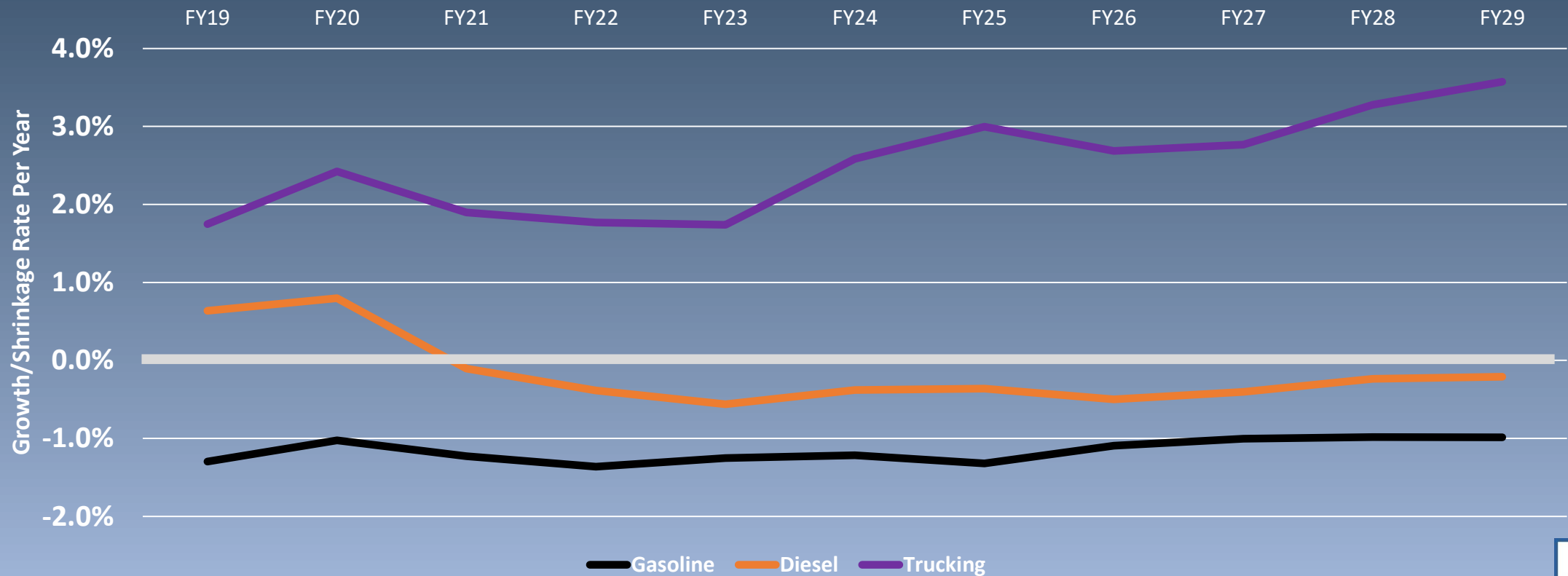


## Highway Trust Fund FY 2008-2020



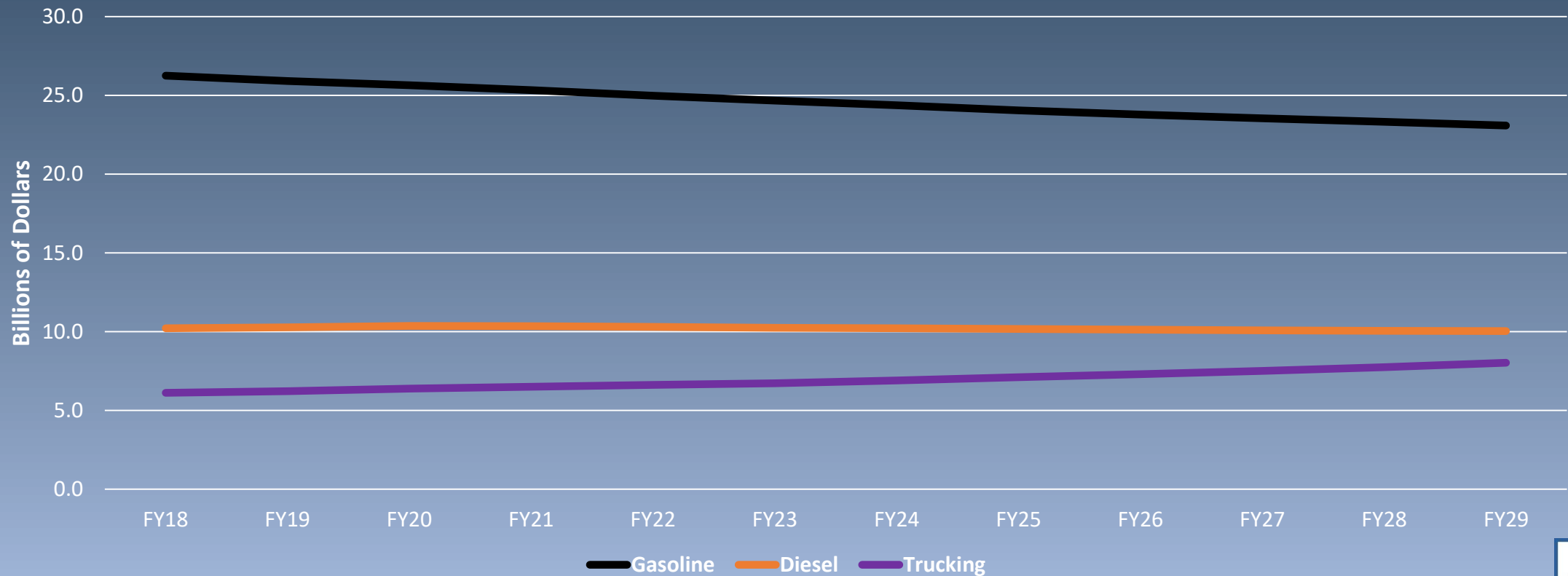
# Highway User-Pay Model: Broken

HTF Tax Receipts at Current Rates, FY 2019-2029 (CBO Jan. 2019 Forecast)



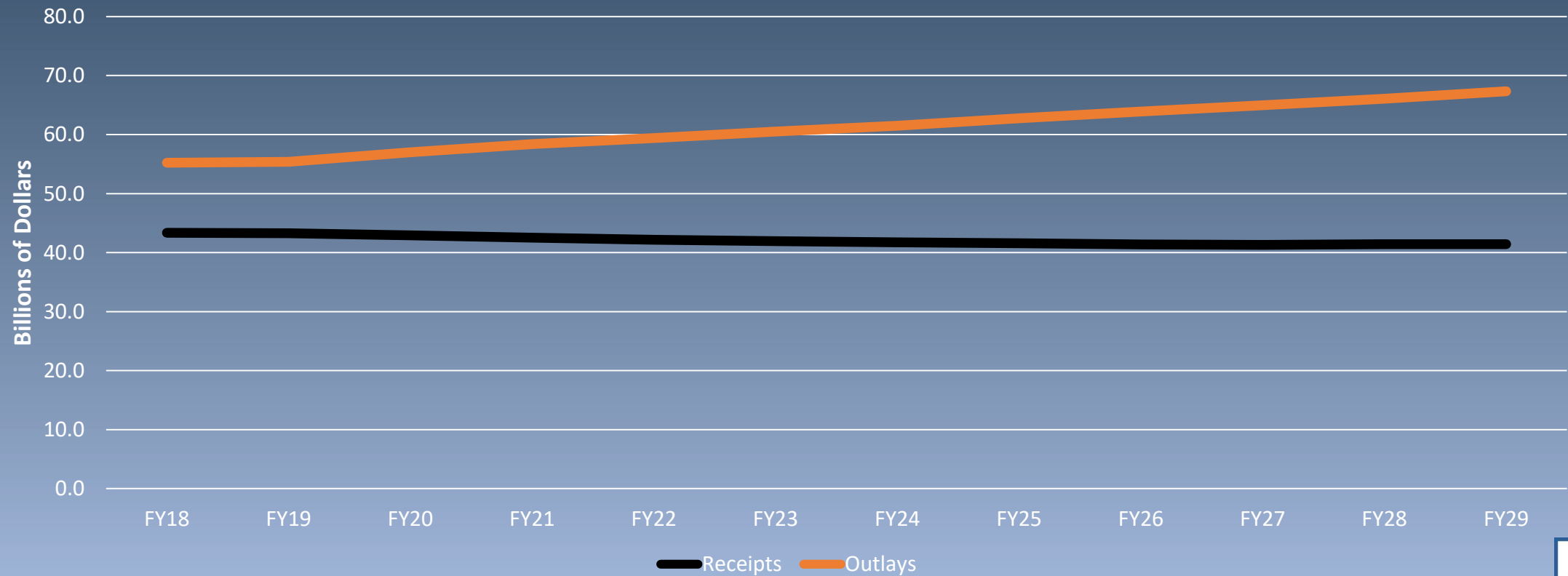
# Highway User-Pay Model: Broken

HTF Tax Receipts at Current Rates, FY 2018-2029 (CBO Jan. 2019 Forecast)



# Highway User-Pay Model: Broken

HTF Receipts vs Outlays, FY 2018 – FY 2029 (CBO May 2019 Forecast)



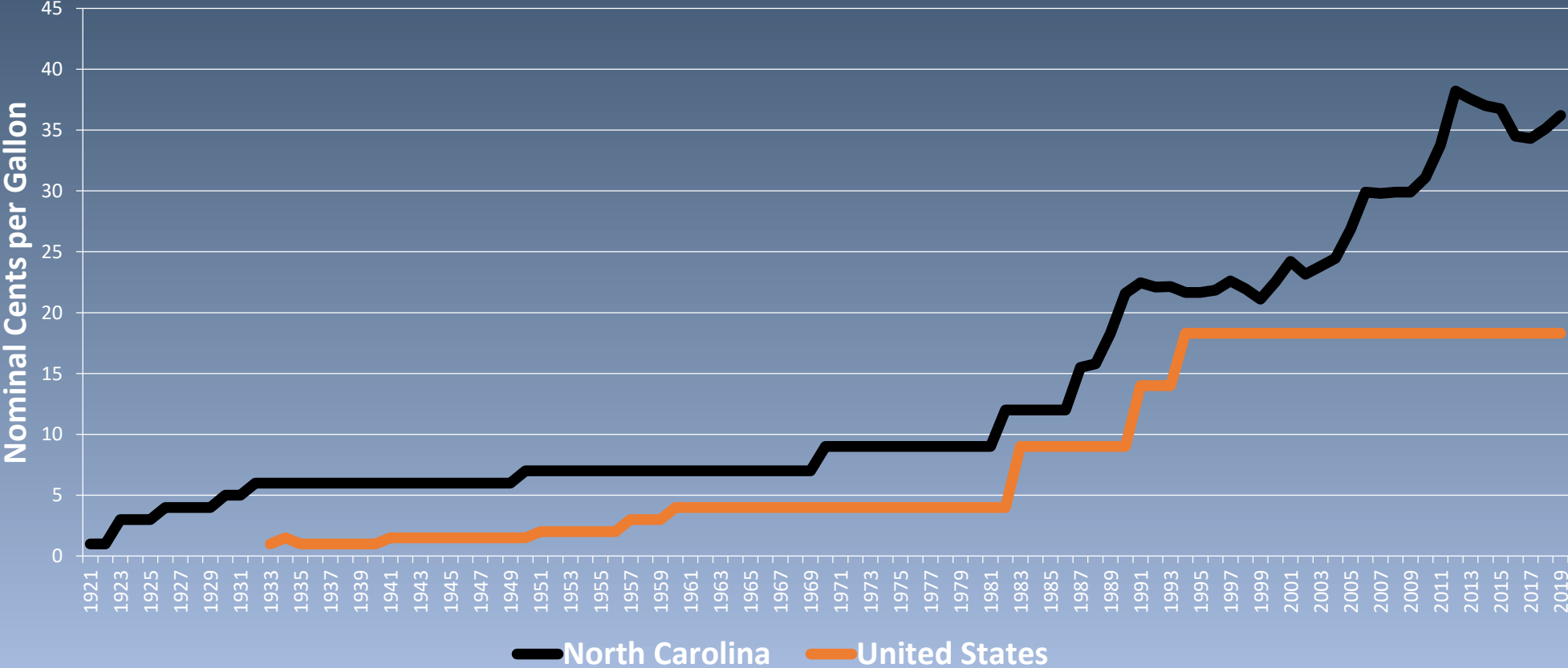


# Highway User-Pay Model: Broken

- At CBO baseline tax/spending levels, HTF will run a \$12.1 billion deficit in FY19, rising steadily to \$25.9 billion in FY29.
- HTF tax increase/bailout cost of baseline 6-year bill for FY 2021-2026: \$102 billion.
- HTF tax increase/bailout cost for 10 years (to FY 2029): \$176 billion.

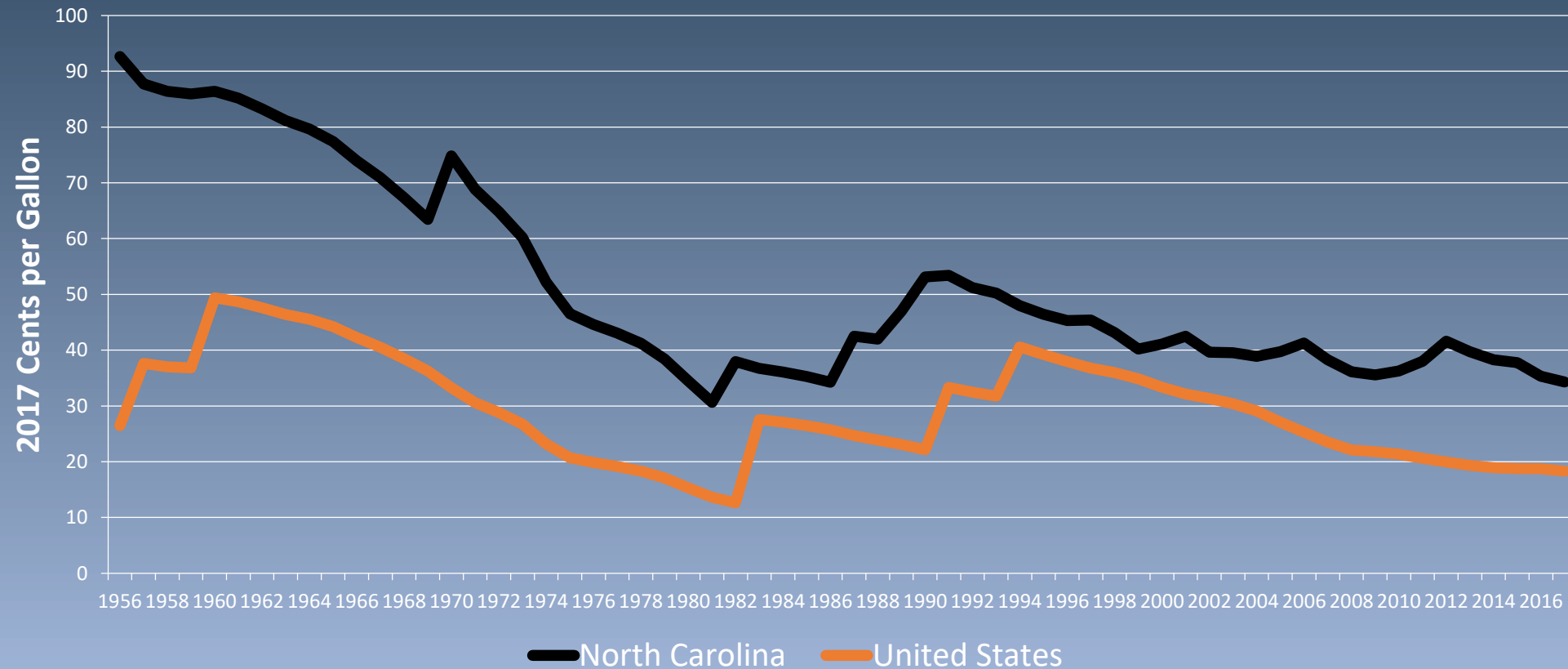
# Revenues – Nominal Rates

Gasoline Excise Tax Rates (Nominal), 1921-2019



# Revenues – Lost Buying Power

Gasoline Excise Tax Rates (2017 ¢ Using BEA Producer Price Indices), 1956-2017



# New User Tax Revenues Needed

- Keeping total HTF solvent for a 6-year reauthorization bill at current (FY18 plus inflation) spending levels would require an immediate (Oct. 1 2019) gas/diesel tax increase of 9 cents per gallon.
- Or other revenues. Or more bailouts.
- Additional increases needed for post-2026 solvency and any desired program growth.

# Highway Cost Allocation – Broken

- No federal cost allocation study since 1997.
- No attempt to adjust federal excise tax structure to match cost allocation since 1982.
- 1997 study said pickup trucks/SUVs slightly overpaid, heaviest trucks underpaid by thousands of dollars each.
- New developments since 1982 – hybrids pay less and EV's pay zero towards their wear-and-tear, congestion, safety costs.

# Gas Tax Still Best Short-Term Option

- At the federal level, despite future rate of decline, motor fuels taxes are still the best user-pay option for the next 20 years.
  - Fewer than 2,000 points of collection (wholesale tank farms).
  - Moving to vehicle or driver-based taxation would increase number of IRS tax collection points over 100,000-fold.
  - Fuels taxes could be supplemented by heavy truck fees and EV user fees for better cost allocation, if desired.

# Highway-Transit Split: Broken

- "Treaty of 1982" – every penny of 1982, 1990 and 1993 gas/diesel increases split 80-20 between Highway Account and Mass Transit Account.
- Congress has allowed transit spending to get farther ahead of its dedicated revenues than highway spending.
- HTF Highway Account needs 80% of an immediate 8.5 cent gas/diesel tax increase to stay solvent for 10 years.
- HTF Mass Transit Account needs 20% of an immediate 13.5 cent increase to stay solvent for 10 years.

# Bailouts Not Reflected in Fed. Policy

- No reason highways are entitled to 80% of bailout money drawn from income taxes, Customs duties, bond borrowing.
- HTF bailout money fungible with fuel tax money – killed share-based “rate of return” arguments.
- If bailouts continue, no reason not to make HTF spending more multimodal, less stovepiped.



# Reliability of NC's Funding Share

- Under the FAST Act, NC is guaranteed 2.66 percent of each year's federal-aid "formula" highway funding each year through FY 2020.
- Why 2.66 percent?
- Because federal-aid highway funding distribution has been stuck in time for over 10 years – state shares of total funding are essentially frozen at the FY 2009 levels, which was the last year of the 2005 highway bill.

# NC's FY 2009 Federal Funding

	NC Total	U.S. Total	NC Share
Factor-Based Formulas (Lane-miles, VMT, population, fatalities, bridge cost, safety, etc.)	\$697.4 million	\$26,205.5 million	2.6612%
Equity Bonus to get NC to 92% gas tax rate of return (% in vs % out)	\$316.4 million	\$9,591.8 million	3.2986%
SAFETEA-LU Earmarks	\$66.5 million	\$4,450.7 million	1.4941%
<b>EQUALS</b>	<b>\$1,080.3 million</b>	<b>\$40,248.0 million</b>	<b>2.6841%</b>
FY14 adjustment to get TX to 95% rate of return (\$\$ in vs \$\$ out)			-.0209%
<b>NC guaranteed share for FY 2015-2020</b>			<b>2.6632%</b>

# NC's FAST Act Federal Funding

	NC Share	Times U.S. Total	Equals Base	TX 95% Adjust.?	NC Final
FY 2015	2.6632%	\$37,798.0 million	\$1,006.6 million	none	
FY 2016	2.6632%	\$39,727.5 million	\$1,058.0 million	none	\$1,058.0 million
FY 2017	2.6632%	\$40,547.8 million	\$1,079.9 million	-\$7.0 million	\$1,072.9 million
FY 2018	2.6632%	\$41,424.0 million	\$1,103.2 million	-\$5.3 million	\$1,097.9 million
FY 2019	2.6632%	\$42,358.9 million	\$1,128.1 million	-\$1.7 million	\$1,126.4 million
FY 2020	2.6632%	\$43.369.8 million	\$1,155.0 million	?????	?????

- If the next authorization brings back real needs-based formulas, this share could change (possibly for the better).
- Big “if.”

# User-Pay Should Be Mended...

- To continue the user-pay, user-benefit model:
  - Spending levels should be roughly synchronized with user tax/fee receipts, either through increasing spending or cutting taxes/fees.
  - User taxes and fees should periodically be analyzed to ensure that costs are fairly allocated to different classes of system users and between system users and the federal government.

# ...Or Ended

- User-pay trust funds have historically been exempted from most restrictions in the federal budget process.
- If the Highway Trust Fund can't be mended (by reconciling spending and user taxes and thus ending the need for more bailouts), a strong argument can be made for ending the trust fund – or at least ending its exemptions from spending caps, sequestration, etc.