

Road and Bridge Funding Recommendations

Rick Olson, State Representative, 55th District
December 13, 2011

The Need

“The model projected that almost \$1.4 billion dollars more revenue per year would be needed in 2012-2015 and rising to almost \$2.6 billion per year by 2023 to achieve the goals set. This result is consistent with the TF2 findings regarding pavement preservation. The graphs included in the report show that this would not result in a “gold plated” road system, as many of the roads in fair condition would be just that - fair- and not good.

The conclusion reached was that if the investments projected by these models are not done, either the deferred costs of maintaining our roads will be much higher OR we choose to accept lower quality roads. From a business perspective, the set of investments recommended is the lowest longterm costs of maintaining our roads.”

Report of the Work Group on Transportation Funding of the House of Representatives Transportation Committee, September 19, 2011 Final Revised Draft, entitled “Michigan’s Roads Crisis: What Will It Cost to Maintain Our Roads and Bridges?” available for download at <http://gophouse.com/Publications/55/Michigan'sRoadsCrisis.pdf>

Because of the methodology we used (the “asset management” approach of doing the right fix in the right place at the right time to maintain a road surface at good or fair levels, rather than allow the condition to drop to poor, where the costs may be 6 to 14 times more expensive), I remain convinced the \$1.4 billion is the minimum we need to reach our 95% and 85% good or fair goals set in the study. “Either pay me now, or pay me much more later”, as the oil change ad says.

The study assumed no additional money beyond our existing resources for curing safety issues, adding capacity to lessen congestion, nothing additional for transit, etc. – just for existing pavement and bridge preservation, in contrast to the TF2 study which recommended \$3 billion including the things we excluded. In other words, we looked at the issue with the perspective of, “If I owned the entire road and bridge network, what would I need to spend to maintain my asset value?”

No legislator wishes to vote for more revenue. However, I see this situation to be parallel to the debate at the national level regarding the federal deficit. To the extent that the federal deficit is not controlled, we load a burden of debt on our children and grandchildren. With roads and bridges, if we do not properly maintain our roads and bridges and allow them to fall into the poor category, we load a burden of reconstruction and rehabilitation costs onto future taxpayers. In either case, failure to act now is not fiscally responsible.

Analysis of Incremental Approach

Some have suggested that it might be too much to do at one time to get the \$1.4 billion per year, and that it might make more sense (at least politically) to get there in \$200 million bites per year, i.e., \$200 million the first year, \$400 million the second year, etc. until we reach \$1 billion. I see two problems with this approach. First, this assumes that future lawmakers will have the will to follow through – a very questionable assumption. Second, the amounts do not achieve the objectives.

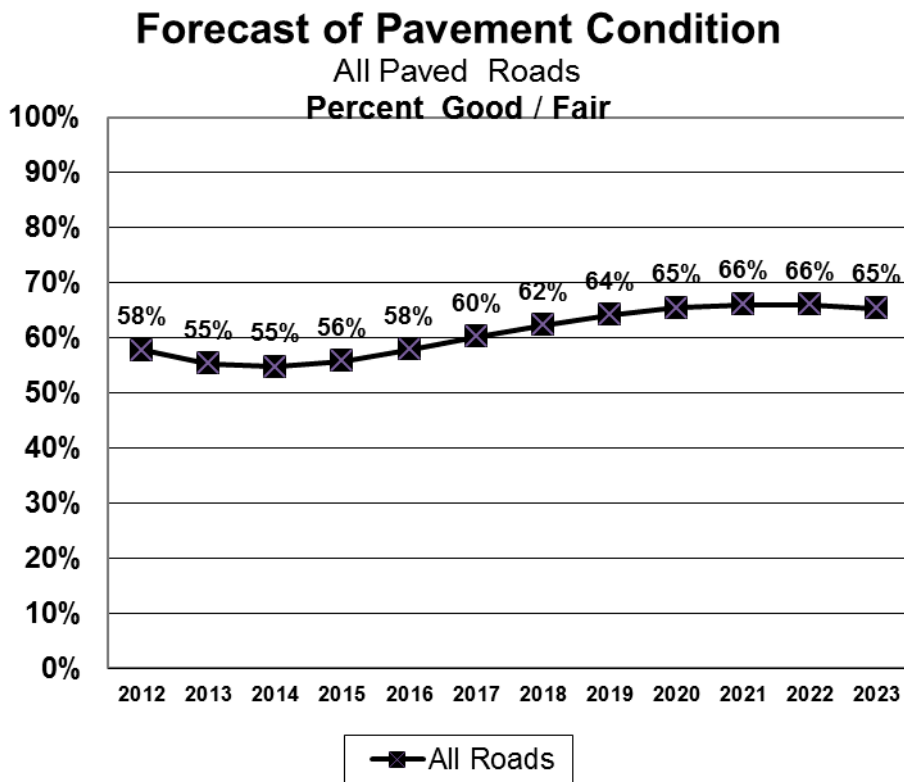
I asked Gil Chesbro, with MDOT, to rerun the models with the incremental assumptions. Here are the results of his analysis:

“Below are the forecasted pavement conditions of Michigan’s paved roads. It assumes that an additional \$200 million will be available for road preservation in 2012, \$400 million in

2013, \$600 million in 2014, \$800 million in 2015, and \$1 billion in 2016 and each thereafter.

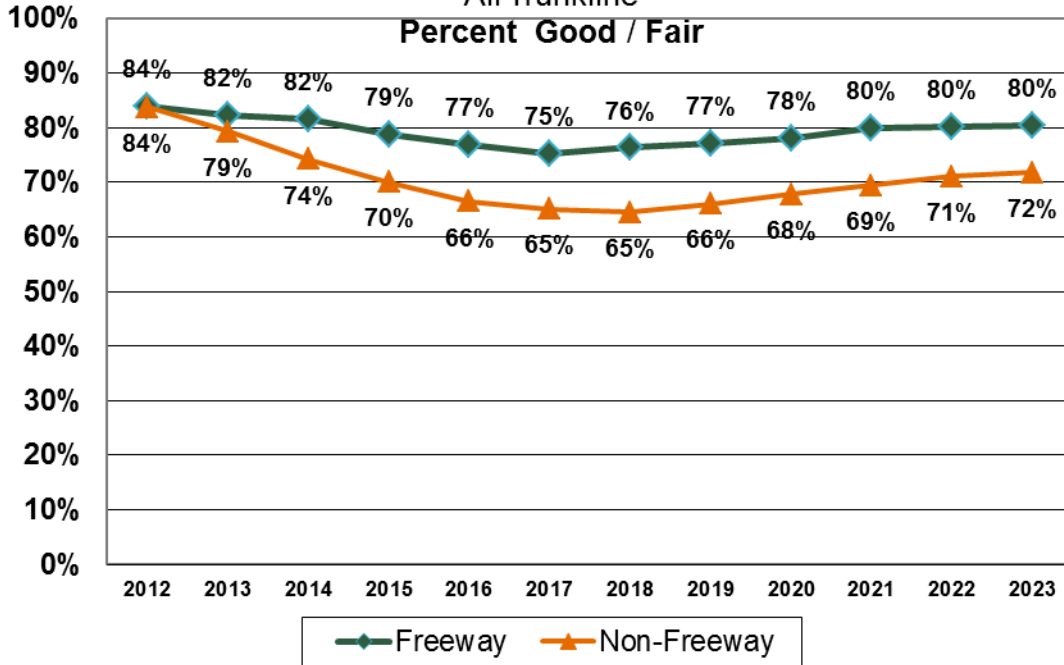
Under this scenario, trunklines will not have sufficient funding to maintain current pavement condition levels. Pavement condition will decrease rapidly in the short-term. However, the additional funding does appear to stabilize pavement condition levels at roughly 70% Good/Fair in the intermediate-term, which is a significantly higher level than the strategy based on current funding can achieve. Over time, inflation eats into the buying power that the additional funding for the new alt strategy provides and that funding can no longer support the amount of work required to maintain that level of pavement condition.

Non-trunkline pavement condition will decrease in the first few years, and then slowly improve until 2022. At that time, the combined effects of inflation and aging pavements will prevent any additional improvements in pavement condition. A decline in condition will then ensue.



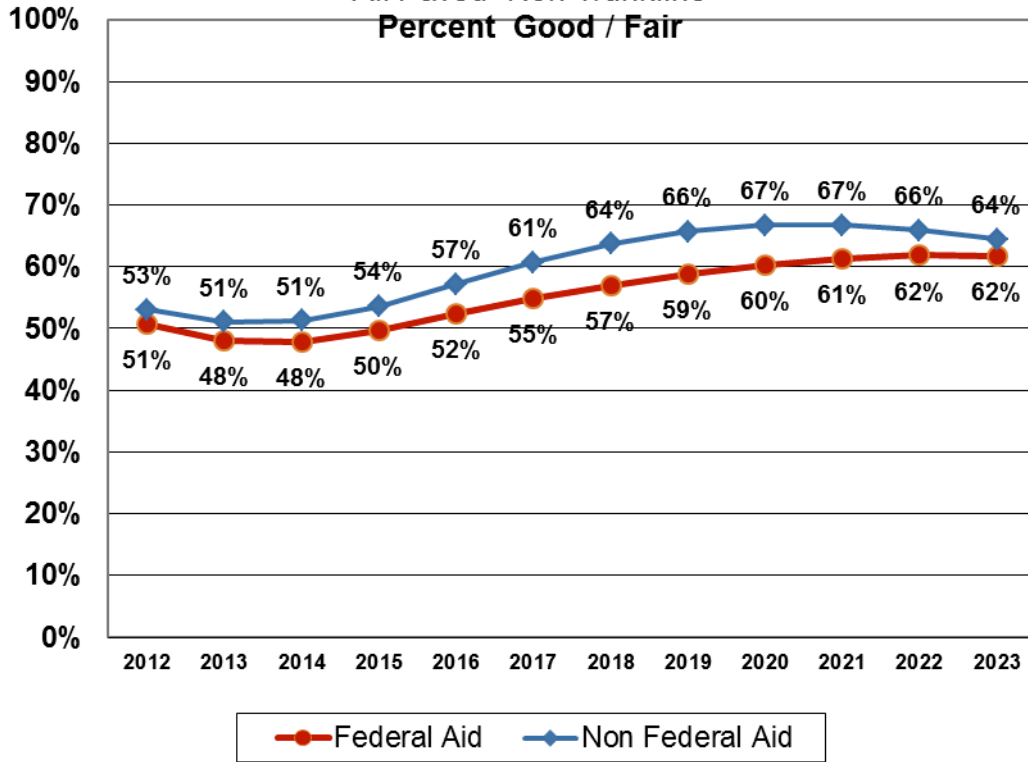
Forecast of Pavement Condition

All Trunkline



Forecast of Pavement Condition

All Paved Non-Trunkline



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Analysis of Achieving Quality Goals by Being More Efficient

Another approach may be to wring out all of the “fraud, waste and abuse” in the system and get a better bang for the buck through more efficient operations to maintain our roads and bridges. While this is a worthwhile effort and we should pursue this where possible, there just are not enough savings available to achieve the goals. Further, to the extent we focus on this, it is too easy to fool ourselves into believing, “Well, we have done something to solve the problem. Next issue!” See Appendix A for the list I have been able to compile and brainstorm through multiple conversations with others.

The biggest dollar savings may come from road agencies being required to have their employees pay a greater share of their healthcare costs than currently. Requiring municipalities to contribute some minimum amount to receive their Michigan Transportation Fund money might also generate more money at the local level. But, put the whole list together, and we probably will be hard pressed to come up with more than \$100 million or so. This is not chicken feed, but hardly \$1.4 billion.

Recommendations for Revenue Increases

In another paper entitled “The Choice is Yours: How Will We Pay for Quality Roads (or choose to endure poorer quality roads)?” I have listed multiple options, together with the pros and cons for each. Here is my list of recommended funding changes, with the more detailed explanations included in Appendix B:

\$0 Revenue neutral. \$826 million per year at 6.7% sales tax on fuel at the wholesale level, equivalent to the amount of gasoline tax collected at 19 cents per gallon and 15 cents per gallon of diesel fuel, which taxes would be simultaneously eliminated.

\$500 million Additional 3.5% sales tax on fuel at the wholesale level.

\$500 million 58% increase in vehicle registration fees.

\$150 million Eliminate the registration fee discounts immediately for all vehicles (not just new).

\$100 million Redirect to state and local road programs the portion of sales tax revenue related to gasoline sales that is currently credited to the state General Fund but is not constitutionally earmarked.

\$24 million Charge new registration fee at time of plate transfer (instead of the \$8 “transfer fee”) and not at plate expiration.

\$0 Study \$80 million per 1/10 of a cent per vehicle mile traveled (i.e., a “mileage based user fee”), based on a third party verified, self-reporting system established in conjunction with vehicle registration (vs. devices in vehicles measuring or reporting mileage).

Total: \$1.274 billion, plus savings through best practices, efficiencies

I have not included the Governor’s proposal of “up to \$40 per vehicle local option increase in the vehicle registration fee” as a part of the solution for the \$1.4 billion need, as it is an uncertain source

of revenue and if and where achieved, likely needed to fund local or regional transit systems, even if approved by the voters in a much smaller amount than the maximum allowed.

Neither have I included a fix to one of the major problems in road funding, that being the fact that the retail sales tax on gasoline goes into the School Aid Fund and the General Fund, and does not go for roads. A “potential fix” would be to (1) eliminate the retail sales tax on fuel, (2) raise the sales tax on fuel at the wholesale as suggested above to raise the amount needed and direct that to the Michigan Transportation Fund and (3) raise the retail sales tax rate on everything else sufficient to make up this loss of revenue to the School Aid Fund and General Fund. This would require a 2/3 vote in both houses of the Legislature plus approval by a vote of the people, extremely high hurdles to get over.

If the pre-Proposal A history has a lesson it is that a significant change in the tax structure put on the ballot as a “yes” or “no” question is doomed for failure. A possibility, however, would be to enact the \$1.274 billion combination of revenue changes suggested above and then put on the ballot that statutory solution as Proposal A and the “potential fix” on the ballot as Proposal B, and let the people decide between the two. The 2/3 vote needed in both houses would still be an issue, but this might be more politically palatable for legislators as the blame could be shifted to the people who would ultimately choose.

As long as the new dollars raised from the suggested combination above are targeted toward roads and bridges, they should meet the “user fee” exception to the Taxpayer Protection Pledge, with the exception of the sales tax at the wholesale level, which requires the assumption that the tax would be passed on to consumers. I have reconciled myself that that is close enough.

Now, getting the votes for this package may not be easy, but I fully believe it is attainable – if we pursue this on a bi-partisan basis, with each caucus contributing a share of the votes, and with each caucus being able to protect its vulnerable members.

We can do this, if we have the will to solve a problem that has eluded solution from legislature after legislature. We have tackled many “generational” issues so far this session. Let’s not shy away from this one just because it is hard.

Appendix A

Potential Road and Bridge Best Practices or Efficiencies

Rick Olson
December 4, 2011 (revised)

How do we create the reality and perception that taxpayers are getting value for money?

- Amend applicable Acts to allow all county commissions to absorb their county road commission entirely or in part into county government. These amendments are necessary to address current language at MCL224.6 and 247.659a) and a 1958 Attorney General opinion (Mich AG 1957-1958, No. 2945). HB 5125 and 5126 (Zorn & Switalski)
- Amend Act 51 to allow MDOT and/or the AMC, and/or the Auditor General, to conduct performance and financial audits of local road agencies MTF spending, thereby addressing a 1976 Michigan Court of Appeals ruling issuing an injunction which prohibits MDOT from conducting such audits (68 Mich App390, CRAM vs. State Highway Commission, 1976, p. 390402, and Wayne County v. Auditor General in early 2000's settled). HB 5007 (Somerville)
- Allow local road agencies to directly provide 20% match on federal road agencies. HB 4739 (Knollenberg)
- Allow for single-member county road commission districts HB 4029-31 (W. Schmidt)
- Privatize Michigan rest areas
- Eliminate MDEQ requirements for mitigation for loss of wetlands when road agency is performing work within its right of way. SB 168 (Casperson)
- CRAM Benchmarking process in development by Steve Purri's CRAM committee working on the dashboard
- Best management practices. I.e., County/City/Village Eligibility for 10% of new money going into new system/formula is contingent on each year achieving the following, with the Asset Management Council (AMC)) (MCL 247.659a) annually certifying conformity or non-conformity with six of the following eight:
 - Employees of agency must pay at least 10% or 20% (pick one) of health care premiums, or, if applicable, agency does not opt out of the provisions of Senate Bill 7 of 2011.
 - New employees must be placed on a defined contribution (401(k) or 403(b)) retirement plan
 - Participate fully in the "asset management processes" specified in act 51 (MCL 247.659a) on all federal aid and now non-federal aid highways with certification annually by the AMC in accordance with AMC guidelines. (or limit to "county primary" and city "major" roads).
 - Promulgate requests for bids from other public road agencies and private contractors for all "road work" (needs definition) in the local jurisdiction and in accordance with local bid guidelines prepared by the asset management council.
 - Develop a service consolidation plan in year 1, and by year 2 and beyond have actually consolidated at least one service with an annual pre-consolidation cost of at least \$100,000; or have developed a consolidation plan in year 1, and by year 2-5 have reduced operating costs of the entire agency by at least 10% and maintained that reduction through year 5 as compared to the baseline year.

- Place on the web a report card on operating and financial statistics baseline year spending and current fiscal year spending for each year going forward, with the statistics to be included specified by the AMC.
 - Benchmark road agency financial and performance against their peers
 - In the case of counties, merging two or more contiguous county road agencies; or in the case of cities, merging two or more contiguous road agencies and/or merging the city road agency with the county road agency.
- Require local jurisdictions to expend amount equivalent to 1 mill of property tax (dedicated millage, local vehicle registration fees, special assessments or from general fund) of local money on road maintenance to qualify for MTF dollars.
 - Relax some engineering specifications that are overkill. E.g., specifications for replacement of isolated county road bridges
 - Require MDOT to put out a request for proposal for public "local road agencies" or private contractors to perform all work for all miles on state highways including in those counties/cities where MDOT currently contracts out the work to local road agencies, and most importantly in those 21 counties where MDOT currently maintains its own garages and employees and equipment. MDOT may or may not choose to accept such bids but should be required to publish on the Internet a comparison of current costs vs. costs in all bids received.
 - Don't allow money to be allocated to cities/villages below a certain size. Instead require them to contract with a road commission or neighboring city, with money that would have been allocated to them under the existing Act 51 formulas being sent to the contract partner for expenditure on that city/village's roads based on projects selected by the small city/village. Could be based on under \$150,000, or less than 20 miles in jurisdiction, or under 20,000 population. Could reduce 533 city/villages receiving money to order of about half that.

Transit:

- Evaluate current funding distribution formula for transit agencies
- Establish a minimum level of income from transit ridership. HB 4023 (Agema)
- Create framework for a SE MI transit agency

Appendix B

Recommended Road and Bridge Funding Changes

\$0 Revenue neutral. \$826 million per year at 6.7% sales tax on fuel at the wholesale level, equivalent to the amount of gasoline tax collected at 19 cents per gallon and 15 cents per gallon of diesel fuel, which taxes would be simultaneously eliminated. The percentage tax would be applied to the cost of the fuel to the wholesaler plus the federal fuel taxes (18.4 cents per gallon for gasoline and 24.4 cents for diesel fuel).

Pros:

- Taxes would be efficiently collected at the same few points as they currently are collected.
- Transitions away from eroding motor vehicle revenue sources.
- Achieves “parity” between gasoline taxes and diesel fuel taxes in terms of rates applied.
- Potential rising revenue as (or if) wholesale gas and diesel fuel prices rise.
- Meets Taxpayer Protection Pledge by being revenue neutral (at least in the short run).
- Potential political advantage of “socking it to those oil companies”.
- Potential political advantage of perception that “the gas tax has been repealed”.

Cons:

- Wholesale fuel prices rise and fall rapidly, introducing volatility to the revenue source, making long-term planning more difficult, unless restrictions on how far up or down the tax could vary from year to year are included in the bill.
- Does not fill the \$1.4 billion need if revenue neutral.

\$500 million via \$144 million per additional 1% sales tax on fuel at the wholesale level. (\$844 million gas tax + \$122 million diesel fuel tax divided by 6.7%) or about an additional 3.5% for the \$500 million.

Pros:

- If added to revenue neutral proposal, simple change.
- An increase in the tax rate would result in immediate increased revenue collections.
- The gas tax increase might not be noticed much by motorists, as gas prices fluctuate wildly.
- Increased taxes are paid a dribble at a time.
- Motor fuel taxes continue to capture out-of-state drivers’ payments as they use Michigan roads

Cons:

- Does not perfectly meet the Taxpayer Protection Pledge as it does not meet the definition of “user fee”, i.e., the payers do not receive the direct benefit from paying the fee. Vehicle owners will indirectly pay the increased taxes if the wholesalers pass 100% of the additional tax to the retailers who pass on 100% of the additional cost to the consumers. Note: To meet the definition, the revenues would also need to be used for roads and bridges, i.e., the improvement that the payers are paying to use.

\$500 million \$86.5 million per 10% increase in vehicle registration fees. E.g., it would take a 162% increase to achieve \$1.4 billion additional revenue, or about 58% for the \$500 million.

Pros:

- Individuals can itemize expense on federal income tax returns.
- Growth potential tied to increasing vehicle prices.
- More proportional to values of vehicles which correlate closer to higher incomes and greater ability to pay the increased fees than flat dollar increases. I.e., less regressive than a flat dollar increase per vehicle.

Cons:

- Places burden on Michigan residents only.
- Large registration payment due at one time.
- May lessen participation in DNR's recreation passport.
- This gets complex, as there are a number of different registration taxes established in Sections 801 through 810 of the Michigan Vehicle Code. The applicable tax rate is a function of a number of factors: the vehicle model year, the list price of the vehicle, the weight of the vehicle, the use of the vehicle and in some cases, some characteristic of the vehicle owner.

\$150 million \$150 million via eliminating the registration fee discounts immediately for all vehicles (not just new). For three consecutive years after a new car is purchased, the value of a vehicle is discounted 10 percent in order to calculate the new vehicle registration fee. (Year 1: \$8 plus .005 x Manufacturer's Suggested Retail Price (MSRP); Year 2: .0045 x MSRP; Year 3: .00405 x MSRP; Year 4 and thereafter: .03465 x MSRP). An alternative is to phase in the loss of the discounts by applying to new vehicles only, which would reduce the additional revenue to an estimated \$18 million per year and rise incrementally over time.

Pros:

- Most people would not notice as few know about the discounts.
- Since the registration fee is a road user fee and not a property tax, there is no reason why the fee should decline with the value of the vehicle.
- Individuals can itemize expense on federal income tax returns.
- Easy to implement.

Cons: No one likes to pay more taxes even if called a fee.

\$100 million House Bill 4521 (H-1) would redirect to state and local road programs the portion of sales tax revenue related to gasoline sales that is currently credited to the state General Fund but is not constitutionally earmarked. This would range from \$83.1 million (at \$3.00 per gallon) to \$112.7 million (at \$4.00 per gallon). (Agema and Proos bills)

- **Pros:** Better matches source of funds with the use of the funds.
- **Cons:** This is simply a tax shift. Activities funded by shifted taxes would either need to be cut or revenue raised in another way to make up for shifted revenue.

\$24 million \$24 million by charging new registration fee at time of plate transfer (instead of the \$8 “transfer fee”) and not at plate expiration. Purchasers of brand new cars currently are allowed to transfer their license plates from their previous automobile to the new one without paying the difference of what it would cost to register the new car.

Pros:

- Easy to implement.
- Individuals can itemize expense on federal income tax returns.

Cons: May discourage car purchases, as increases the upfront costs of purchase.

\$0 Study \$80 million per 1/10 of a cent per vehicle mile traveled (i.e., a “mileage based user fee”), based on a third party verified, self-reporting system established in conjunction with vehicle registration (vs. devices in vehicles measuring or reporting mileage). E.g., about \$80 million if 1 cent per mile. During start up phase, increase vehicle registration fees.

Pros:

- This is likely the revenue source of the future, as all vehicles would pay their fair share of the use of the roads, even the electric vehicles.
- This is the ultimate user fee system, as everyone pays in direct proportion to the amount they use the highways.
- Individuals will likely be able to itemize expense on federal income tax returns.

Cons:

- This would require setting up an entirely new revenue collection system, which requires people to imagine something other than what they already know.
- Some fear that this would ultimately lead to a system which utilizes devices in cars that serve as GPS’s which have the potential of invading the privacy of individuals.
- Places burden on Michigan residents only.
- Large registration payment due at one time.
- May lessen participation in DNR’s recreation passport if paid at same time.

Total: \$1.274 billion, plus savings through best practices, efficiencies