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Policy Brief

Transportation Finance Plan Moves Forward

Transportation finance tops the list of unfinished business facing the Washington legislature. While legislators remain split between support for the governor's proposed gas tax hike and the Republican "no tax increase" alternative, only the latter appears likely to have a chance of passage. The GOP transportation finance package, HB 2894, cleared its first hurdle January 28, passing the House 56-41 on a party-line vote. Having passed the Senate Ways and Means Committee, it now awaits floor action in that chamber. No vote has been scheduled as of this writing.

Either HB 2894 or the Governor's proposal would provide funding to begin the necessary building programs without threatening existing state services. Neither, however, constitutes a long-term solution to Washington's transportation problems. In this Policy Brief, we take a closer look at the House legislation.

The four main features of HB 2894 are:

- a transfer of Motor Vehicle Excise Tax ("MVET") revenue to the transportation fund that, bolstered by savings from transportation efficiencies and reduced fuel tax evasion, will support a $2.4 billion construction program,
- a cut in the MVET,
- a change in Violence Reduction and Drug Enforcement ("VRDE") and local criminal justice program funding, and
- a one-time exemption from I-601 to avoid a reduction in the spending limit.

The governor proposed a plan which would immediately raise the gas tax five cents per gallon (three cents for the state, one each for cities and counties) and grow with the I-601 factor for five years, topping out at thirty-four cents per gallon in 2003. The indexed growth would accrue only to the state. Other financing for the plan derives from a one-time $25 million general fund appropriation, a sales tax exemption on construction labor ($75.6 million over five years), savings from unspecified efficiencies expected from the department of transportation (about $27 million over five years) and stopping fuel tax evasion ($112.5 million over five years).

Legislative leaders have said repeatedly that the governor's plan will not be considered this year.

There is no serious disagreement with the proposition that transportation funding should be increased. The following graph shows the trends in transportation spending for the decade 1988-1997. As would be expected, capital expenditures fluctuate from year-to-year more than does spending on operations.

The GOP proposal reflects the current health of the state treasury. Without transfers, tax reductions or additional spending, the state could finish the biennium with more than $850 million in unspent revenues in the general fund. Transferring some of this money to the transportation fund makes sense to lawmakers who want to begin highway improvements without raising the gas tax.

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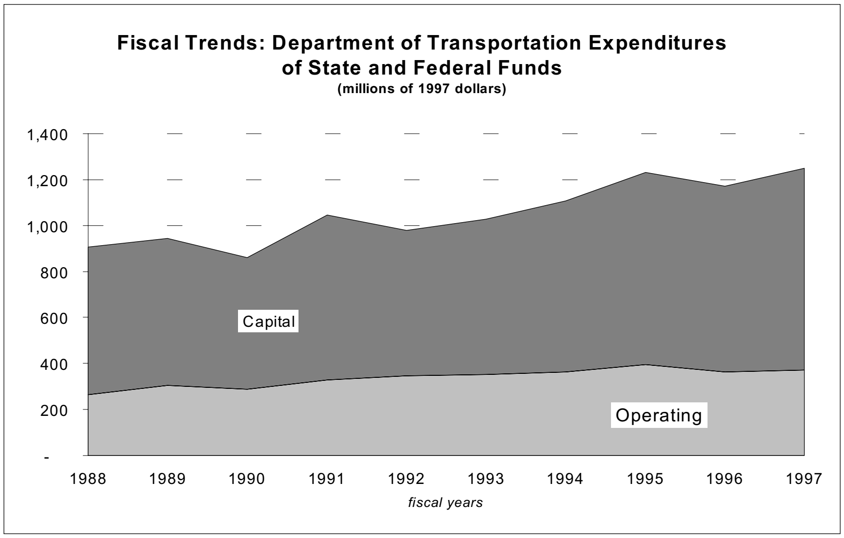

Under I-601, such transfers require lowering the general fund expenditure limit. To make the transfer without reducing the limit, Republicans want voter approval in November for a one-time exemption. The governor's office criticizes the plan, saying it amounts to spending above the limit and needlessly delays the investment. Republicans counter that their transportation budget will provide funds adequate to begin investment now.

By amending I-601, the Republican plan preserves spending capacity for the 1999-2001 biennium and beyond. Also under the plan, projected reserves equal or exceed $700 million through 2003. (See accompanying table, "Three Biennia General Fund Balance Sheet.")

MVET Transfer — The Motor Vehicle Excise Tax pays for local criminal justice programs, ferry operations, public health programs, transportation and transit services. As well, about 22% of the MVET is deposited in the state general fund without earmarks. The GOP plan transfers a share of the tax (about $184 million in 99-01) to the transportation fund, providing most of the 25-year funding stream to support a $2.4 billion spending package. For the balance, the GOP plan incorporates savings from efficiencies and reduced fuel tax evasion as does the governor's proposal.

The financing package will fund a five-year, $2.4 billion capital investment expected to be paid off over twenty-five years — about what most advocates see as the essential first step toward resolving a $25-30 billion problem. The capital plan, however, including the share to be financed through debt, has not yet been defined. About 70-75% of the Republican plan is likely to be bonded. The governor, whose program would use proceeds from the gas tax increase to support a $1.6 billion bond issue (about two-thirds of his proposed investment plan), identified a set of priority projects, many of which are likely to be on the Republican agenda as well. The revenue stream from the gas tax hike could permit a more rapid debt retirement than anticipated through the GOP plan.

MVET Credit — The MVET is based on the manufacturer's suggested retail price of a vehicle and is levied in lieu of a personal property tax.

The GOP plan includes a $40 per vehicle MVET credit and changes the depreciation schedule so that vehicles will no longer be assessed at 100% of value in the second year of ownership. The result is an estimated $360 million savings for taxpayers in the 1999-01 biennium; most of the money would otherwise have gone to the state general fund.

For a two-car family, the savings over ten years from the Republican plan is estimated to be about $789 dollars. The governor has proposed a $35 MVET credit, without a change in the depreciation schedule, for a ten-year savings of about $686.

If, as expected, the February revenue forecast is down, the MVET credit may have to be reduced to maintain adequate reserves. As the table indicates, the tax cut removes more revenues from the general fund than does the transfer.

Criminal Justice and VRDE Funding — The GOP plan shifts funding for local criminal justice and VRDE programs from the MVET to the state general fund. Currently, those programs receive earmarked funding from the MVET, with deposits in the criminal justice accounts limited to the prior year's funding plus inflation; excess revenues are deposited in the VRDE account. Under HB 2894, in FY 2000 an initial appropriation from the general fund of $6.6 million will be made to the county criminal justice account, $18.6 million to the municipal criminal justice account and $8.4 million to the VRDE account. These sums are 10% greater than the MVET deposit would have been. In addition, the amounts are to be increased annually by the I-601 growth factor, which is based on inflation plus population growth.

While it's appropriate for these programs to be returned to the general fund ("GF"), this plan sets a dangerous precedent by assuring some GF programs a full share of the I-601 growth factor. This skews priority-setting. Also, it's unfortunate that I-601, while requiring a re-basing of the spending limit for transfers out of the general fund, does not permit an equivalent adjustment when programs are transferred into it. The omission makes it difficult to reduce the number of dedicated funds by incorporating them into the GF.

THREE BIENNIA GENERAL FUND BALANCE SHEET

(Dollars in Millions)

HB 2894

	1997-99	1999-01	2001-03
RESOURCES			
Unrestricted Beginning Balance	**$513**	**$548**	**$489**
Revenue Forecast	19,432	21,233	23,054
MVET transfer to Motor Vehicle Fund	(43)	(184)	(206)
MVET tax cut ($40/vehicle and depr.)	-	(366)	(393)
Local criminal justice & VRDE transfers	-	(13)	(9)
Potential Other Tax Cuts (July '98)	(75)	(161)	(178)
Adjusted Revenue Forecast	19,314	20,509	22,268
Total Resources	**$19,827**	**$21,056**	**$22,757**
EXPENDITURES			
Estimated Expenditures	**$19,085**	**$20,550**	**$22,206**
SPENDING LIMIT			
Working I-601 Limit	**$19,147**	**$20,550**	**$22,206**
RESERVES			
Emergency Reserve	194	211	273
Unrestricted Ending Balance	548	489	489
Total Reserves	**$742**	**$700**	**$763**

Source: House Appropriations Committee

Amending I-601 — To avoid a reduction in the I-601 limit, proponents of HB 2894 want a one-time amendment in the terms of the initiative, asking the voters to "reaffirm and strengthen" the limit and assure that "other programs funded from the general fund are not adversely impacted" by the transfers.

Concern with maintaining the integrity of the spending limit complicated earlier attempts to craft a transportation finance package that did not rely on a gas tax increase. Because I-601 limits expenditures only from the general fund, it creates an incentive to shift funds to unlimited, nongeneral fund accounts. The issue is addressed in Section 4(4):

"If the cost of any state program or function is shifted from the state general fund on or after January 1, 1993, to another source of funding, or *if moneys are transferred from the state general fund to another fund or account*, the office of financial management shall lower the state expenditure limit to reflect the shift." (Emphasis added.)

Without the exemption, the transfer under HB 2894, therefore, would result in a lower expenditure limit. For the 99-01 biennium the reduction would be about $74 million; for the current biennium, about $83 million.

Clearly, lowering the limit to reflect expenditure transfers corresponds with the objectives of I-601; if a program has been removed from the general fund, general fund spending capacity should be reduced. For example, if special education programs were to be shifted from the general fund to a newly-established dedicated fund, it would be logical to reduce the general fund by a like amount.

Adjusting the limit to reflect a transfer of revenues not directly associated with a general fund spending program seems to go beyond the strict logic of expenditure limitation. The revenue transfer does not necessarily reduce the spending commitments to be made from the general fund. In HB 2894, the general fund is relieved of no ongoing expenditure responsibility (to the contrary, the criminal justice and VRDE responsibilities are added). Exempting the transfer, then, is not inconsistent with the intent of I-601.

In addition, citizens generally perceive the MVET as a transportation tax. And, in fact, more than half the tax is earmarked for transportation and transit purposes. The proposed transfer is consistent with both the perception and the common use of MVET funds.

The GOP plan increases the earmarked share of the MVET targeted for transportation projects. No new fund is established; no general fund responsibilities are shifted from under the I-601 cap. If all transfers from the general fund are required to meet a similar test, this proposal will spawn few clones.

Nonetheless, any effort to amend I-601, however justifiable on technical grounds, establishes a precedent sure to be invoked on behalf of other, less meritorious, measures.

Conclusion — The Republican plan, like the governor's proposal, should be considered as a short-term, transitional, transportation package ¾ an element, not a comprehensive solution.

While the governor's proposal assures more money for a longer period of time, Republican leaders have repeatedly said that there won't be a gas tax increase this session.

Even if approved by the voters, the HB 2894 package will provide only $2.4 billion, the minimum sought by transportation interests. If the plan becomes law, the issue should be revisited in 1999. Then, the emphasis should be on transportation reforms. Both the Washington Transportation Alliance and the Washington Roundtable have identified important actions to be considered. Many of them are consistent with previous Washington Research Council objectives. Some simply reflect good business sense.

A few examples of reforms for consideration:

- **The transportation department should be more accountable.** Reorganization under the direct control of the governor's office should be examined. The department grew out of a consolidation of a various independent agencies in 1977. To "take politics out of public works," governance was vested in an independent commission. The decision should be reconsidered. Direct gubernatorial appointment could make the department more visible and accountable.
- **State policy should make greater use of private-public partnerships.** Although Washington's 1993 Public/Private Initiatives in Transportation Act fueled substantial opposition to toll roads, that disappointment should not preclude future innovation. As the Washington Roundtable notes, "privatization provides a viable alternative to raising taxes if done correctly." Market demand incentives, like congestion pricing, should also be tried.
- **Other opportunities for making effective use of limited funding should be pursued.** Construction costs can be reduced by streamlining regulatory processes and repealing prevailing wage laws. Exempting transportation construction from the sales tax would assure that all tax dollars intended for transportation infrastructure are used for roads. (Imposing the sales tax on state highway projects simply transfers transportation dollars to the state general fund.)
- **Transportation financing should be overhauled.** The complex web of earmarks, fund dedications, and intergovernmental transfers should be streamlined, increasing public understanding and accountability. Current funding formulas should be reconsidered, with the goal of combining long term stability with the flexibility required to address high priority projects.
- **The gas tax will have to be increased.** As we have said before, this quantity-based tax does not keep pace with prices or inflation. Periodically, it must be raised simply to maintain purchasing power.

For all its deficiencies, the approach taken in HB 2894 represents a viable first step toward addressing the state's transportation problems. However, a comprehensive solution to the state's on-going transportation challenge will balance increased tax support with policy reforms, efficiencies, and strict accountability. Next year's legislature already faces unfinished business.

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