THE THOMAS JEFFERSON
INSTITUTE FOR PUBLIC POLICY

A Transportation Funding Plan for Maintenance:

"A Friendly Amendment" by the Jefferson Institute

by: Michael W. Thompson

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Thomas Jefferson Institute for Public Policy

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Transportation Funding Plan for Maintenance:
"A Friendly Amendment" by the Thomas Jefferson Institute

Executive Summary:

The Thomas Jefferson Institute applauds the Governor for making transportation the key issue of this year's General Assembly session. It is long past time for Virginia to face up to its transportation needs and to figure out how to resolve them.

This paper analyzes the Governor's plan as it stands today in the General Assembly and offers a "friendly amendment" focused solely on the maintenance issue. The economic analysis was completed using our STAMP (State Tax Analysis Modeling Program) model developed by the respected economic team at the Beacon Hill Institute located at Suffolk University in Boston. The economic analysis of the Governor's Plan shows these results:

The Governor's Plan:

- Private employment increases by 3,700 jobs
- Investment increases by $23 million
- Real disposable income deceases by $1.04 billion

After seeing these results, the Jefferson Institute crafted its own plan that would increase the gas tax by 20 percent the first year and then annually index the gas tax to inflation and "off-set" that increase by indexing the state income tax brackets to inflation and making these two elements clearly "revenue neutral." The economic results of the Jefferson Institute plan are significantly better than those of the Governor's Plan:

Jefferson Institute's Plan:.

- Private employment increases by 14,950 jobs
- Investment increases by $80 million
- Real disposable income increases by $782 million

The Jefferson Institute urges the General Assembly to consider zeroing in only on the maintenance issue which is the most important element in our transportation dilemma today. Solving this problem will be a huge legacy for our Governor. Then the upcoming gubernatorial campaign can focus on how to build new roads and expand mass transit.

This paper also suggests two other actions that the General Assembly could take to open up significant additional monies for Virginia's transportation needs: re-passing that part of "3202" that gave authority to raise taxes and fees to locally elected bodies; and urging Congress to block grant to Virginia our federal transportation funds thus reducing construction costs.

The Thomas Jefferson Institute for Public Policy joins with many other groups in praising our Governor for making transportation the signature issue in this year's General Assembly. We ask that our idea be considered as a "friendly amendment" so that the maintenance piece of his proposal will have a much larger economic benefit to our state.

A Transportation Funding Plan for Maintenance:

"A Friendly Amendment" by the Jefferson Institute

by: Michael W. Thompson

Introduction

The Thomas Jefferson Institute for Public Policy joins many others in commending Governor McDonnell for confronting the transportation maintenance/construction issue in a creative way that has now focused serious attention on this festering problem. Without the Governor's proposal, transportation would have remained on the back burner. That certainly is not the case today.

Clearly the current static gas tax is not keeping up with the transportation needs here in Virginia. Inflation since that 17.5 cent gas tax was implemented 27 years ago has eroded the value of that tax, while at the same time, the fuel efficiency of our vehicles has added to the decrease in available maintenance funds.

Today's gas tax, had it increased at the rate of inflation since 1986, would be $.35 per gallon rather than the current $.175 per gallon. And fuel efficiency has, in many cases, doubled as well in this same period of time also reducing the amount of money available for transportation.

The Governor's idea of eliminating the gas tax and increasing the sales tax will automatically grow available transportation dollars with the inflation rate. The Governor believes that this idea will keep the burden of those sales taxes "equal" on the taxpayers as the prices of taxed items rise in basic tandem with the rate of inflation. There is disagreement among some of the Governor's allies about whether this approach is truly revenue neutral.

However, the Thomas Jefferson Institute believes there is a better way to reach the Governor's goal in the area on transportation maintenance (at least $500 million a year in five years) and it is a way that has a better impact on our economy.

Since maintenance is the largest problem facing our state today, and since construction money is moved every year to transportation maintenance by law, every new dollar of maintenance funds that is generated is a dollar of construction money that can remain with construction.

The Thomas Jefferson Institute has analyzed the remaining transportation bill in the General Assembly – the Governor's Plan --and a Jefferson Institute funding plan that we crafted focused solely on resolving the critical maintenance issue. To do this analysis, we used our respected STAMP (State Tax Analysis Modeling Program) model for Virginia that was developed by the economists at the Beacon Hill Institute at Suffolk University in Boston. The results are outlined below.

In addition to the analysis of these two transportation funding plans, this short paper offers two additional ideas to help confront the transportation funding problems faced by our state. These ideas will hopefully be considered by our Governor and the General Assembly for including in any transportation bill that is approved by the General Assembly.

The Governor's goal of creating a larger revenue stream for transportation maintenance that will grow with the economy makes good sense. Resolving the maintenance problem should be the first priority. This is the most immediate problem we face. Clearly the state should maintain its current assets before it builds new ones and new infrastructure should only be built if maintenance is available. This paper is focused solely on the maintenance issue and how the needed $500 million or more a year can be generated with a clearly "revenue neutral" plan.

<u>This Jefferson Institute Plan resolves both the practical maintenance issue and the political tax neutrality issue. And this plan is significantly better for our economy.</u>

After the maintenance problem is resolved, our leaders can then look at the long-term needs in our state and craft a plan that can be thoroughly discussed by our elected leaders, business leaders and those who must ultimately pay for new transportation projects – the taxpayers. What better time to discuss the long-term transportation needs in our state, and how to resolve those needs, than in the up-coming gubernatorial election?

Our Governor's legacy for transportation can be that he solved the long-festering maintenance issue by bringing more than $560 million a year to that requirement and also protected the transportation construction fund by $560 million. By "finding" $560 million for maintenance, the Governor is also "finding" $560 million a year for construction that is now disappearing into maintenance.

The Jefferson Institute's Maintenance Funding Plan and Tax Model Analyses

Everyone recognizes that in five years at least $500 million annually is needed to pay for maintenance without "stealing" monies from the transportation construction funds.

<u>That is why the Governor's effort to confront this issue is welcomed and why the Jefferson Institute is offering this "friendly amendment" to the Governor's proposal.</u>

The Thomas Jefferson Institute's Virginia STAMP(State Tax Analysis Modeling Program) is a "dynamic" model that scores the economic consequences of tax policy in the areas of job creation, investment in the economy, and changes in disposable income. It projects those consequences over a 5 year period of time.

Revenue neutrality is very important in this debate as can be seen by the Governor's efforts to offset the elimination of the gas tax by increasing the sales tax. The Thomas Jefferson Institute has designed a transportation funding proposal that is more clearly revenue neutral than is Governor McDonnell's transportation plan <u>and the impact on our economy is greater</u>.

<u>The Jefferson Institute's Maintenance Funding Plan is simple and straight forward.</u>

First, it raises the gas tax at the rate of inflation (using an inflation rate of 2.5% a year) after raising the current gas tax of 17.5 cents by a full 20% -- or 3.5 cents – the first year. Under this plan in five years the gas tax would be 23.19 cents per gallon, or an increase of 5.69 cents. That will raise an additional $284.5 million a year based on each penny of gas tax producing $50 million in revenue.

Second, this tax increase would be "offset" by indexing to inflation the current state income tax brackets. The income ceiling for the tax brackets would increase each year by the same inflation factor as the gas tax will increase (2.5%). The income tax brackets would be adjusted so that "revenue neutrality" is achieved to the increase in the gas tax. The economic modeling results below take this into consideration.

To better understand the impact of indexing the state income tax brackets to inflation, had the income tax brackets been indexed to inflation in 1987, then the ceilings for each bracket would be double what they are today. Here are the current brackets and the inflation adjusted brackets:

Current Bracket	Inflation Adjusted Bracket
\$ 0- \$3,000	\$0 - \$ 6,056
\$ 3,001 - \$5,000	\$ 6,056 - \$10,093
\$ 5,001 - \$17,000	\$ 10,094 - \$34,315
\$ 17,001 and up	\$ 34,316 and up

<u>Under the Jefferson Institute's transportation funding plan, in year five there would be \$284.5 million dollars more generated by the gas tax and \$284.5 million less paid by income taxes. This clearly is a revenue neutral plan</u>.

And the Jefferson Institute's plan accepts the Governor's proposal of increasing the amount of current sales tax revenue earmarked for transportation over the next five years from the current one half of one percent (10% of the total sales tax goes to transportation today) to three quarters of one percent, or an additional \$283.2 million in year five.

Our Jefferson Institute Transportation Funding Plan will generate a total of at least \$567.7 million a year in five years for maintenance. This money will fill the transportation maintenance requirements that is the most critical part of our state's transportation needs today.

<u>Economic impact of the two basic transportation plans</u>

The Thomas Jefferson Institute ran the two major transportation plans detailed in this paper through our economic model and the results are outline below. These economic results are based on a five year projection and the differences are from the current projected baseline – increases and decreases highlighted below are to the economic projections used today.

<u>The Governor's Plan</u>:

- Private employment increases by 3,700 jobs
- Investment increases by \$23 million
- Real disposable income deceases by \$1.04 billion

<u>We should remember that these results are based on the entire Governor's Plan. Clearly raising the sales tax, even when off-set by eliminating the gas tax, does not impact the</u>

economy very well. And disposable income is negatively impacted. This is very important in this debate over which transportation is better.

Jefferson Institute's Plan:

- Private employment increases by 14,950 jobs
- Investment increases by $80 million
- Real disposable income increases by $782 million

The Thomas Jefferson Institute's Plan focuses only on resolving the transportation maintenance problem and this plan has a significantly better impact on the economy than does the Governor's Plan. Our plan produces more jobs, more investments and more disposable income than does the Governor's Plan even with that plan's other funding pieces.

The Jefferson Institute Plan compared to the Governor's Plan has a huge economic benefit:

- Private employment increases by four times – 14,950 jobs vs. 3700 jobs.
- Investment increases by almost 3 ½ times -- $80 million vs. $23 million.
- And real disposable increases by $1.822 billion.

Even if these improvement numbers are cut in half (for those who doubt the scoring results we have outlined above), they are still significant improvements over the current plan promoted by our Governor and passed by the House of Delegates.

The big difference between these two approaches is that the Jefferson Institute's Plan keeps the gas tax in place while the Governor eliminates that tax. However, the gas tax is a direct tax and many economists believe that a tax directly tied to a specific government service is more productive.

And the Jefferson Institute Plan uses the Governor's numbers for increasing the transportation funds carved from the current 5% sales tax: from half of one percent (0.5%) of the five percent sales tax to three quarters of one percent (0.75%).

Improving Transportation by taking Additional Actions

The General Assembly can take two additional actions this year that could significantly improve our transportation infrastructure and potentially generate more money for transportation. These are ideas that can bring substantially more construction dollars to our transportation needs.

1) **Re-pass the last major transportation law from 2007 (HB 3202) to conform to the Supreme Court's ruling.**

   Localities should be given more leeway in funding transportation. The Supreme Court ruled that unelected government bodies cannot raise taxes. The original HB 3202 law (a bill crafted with the leadership of then-Attorney General Bob McDonnell) gave the authority to raise various fees and taxes to the local elected governing bodies – the Boards of Supervisors, City Councils, etc. Governor Kaine changed this legislation and the Supreme Court struck down that change.

The General Assembly could simply re-pass that part of HB 3202 with its original wording. If the various taxes and fees were enacted by these localities, hundreds of millions of dollars in additional transportation infrastructure funds would be available. The issue of revenue neutrality would be a policy issue fought out at the local level where the governing bodies are closer to the taxpayers. Providing these revenue sourcing is not endorsing tax increases, but it leaves this issue to the localities to confront.

2) The General Assembly Should Memorialize Congress to Block Grant Federal Construction Money to Virginia.

Delegate Tim Hugo has said that when he was Chief of Staff for Congressman Bud Shuster, when the Congressman was Chairman of the House Transportation Committee in the mid-1990's, an internal Committee report showed that one dollar of federal transportation construction funds increased the cost of a project by 30-40% because of the additional regulations. Similar studies have been made in the past by the Reason Foundation showing the cost of federal transportation projects compared to those without federal dollars.

Virginia should ask to be a test case where federal transportation construction monies are sent directly to state without federal strings attached. If construction projects can be completed more quickly and more economically with these block grants, then Virginia will prove that the entire federal transportation construction program could become a block grant to the states. Should this idea work it would be the same as having 30-40% additional federal transportation funds available without raising additional taxes. This would be a huge benefit to our state and its economic future.

With the congressional leadership Virginia has in both the House of Representatives and in the US Senate, this federal "test" could become reality in a relatively short period of time. The results could be dramatic.

Conclusion

Governor McDonnell has done our state a great service by bringing the transportation funding issue to center stage. Funding transportation is a difficult and that is precisely why it has been avoided for far too long. Governor McDonnell has now brought this issue to the forefront of the public debate and those of good faith who have other ideas need to provide alternatives that can become reality – that can pass the General Assembly.

There are several ideas on how to "improve upon" Governor McDonnell's transportation plan from fair minded people in our state legislature and outside of elective office. All realize that Virginia simply can't sit back and let the current system run its course. If we do that then the transportation problem that we confront, especially in maintenance, will only get worse and the remedy more difficult.

The Thomas Jefferson Institute's Transportation Plan is focused solely at the overriding issue of maintenance. This plan raises $586 million a year in year five and it is accomplished in a truly revenue neutral manner. When maintenance of our current transportation system is avoided, the infrastructure problems only become more expensive to resolve. So doing nothing, or doing too little in the maintenance arena, is clearly the wrong answer.

Let's resolve this maintenance problem and then take the upcoming governor's campaign to talk through the new construction and long-term transportation needs here in Virginia. We have many long-term needs. And we need to delineate the difference between transportation "needs" to help our state's economy – new roads and bridges, expanded mass transit, airport capacity, etc in the right places – and transportation "niceties" – bike paths, roads with little economic impact, flower gardens, walking paths, etc.

Transportation maintenance must be resolved and this is a good time to do it. It alone will be a huge legacy for our Governor. Long term construction needs is an issue that can be debated in this year's gubernatorial campaign and the voters can help decide this issue.

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Michael W. Thompson is the President and Chairman of the Thomas Jefferson Institute for Public Policy, Virginia's premier non-partisan public policy foundation. He can be reached at 703-440-9447 or info@thomasjeffersoninst.org

(This paper reflects the research and ideas of the author and does not necessarily reflect the ideas of the Board of Directors of the Thomas Jefferson Institute. These ideas are not intended to support or oppose any specific piece of legislation)

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Thomas Jefferson, 1801

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