“A 21st century state transportation strategy that strengthens metropolitan America and is tightly linked to the vital elements of the next economy is critical for our nation to emerge from the rubble of the recession.”

State Transportation Reform:
Cut to Invest in Transportation to Deliver the Next Economy

Robert Puentes

Few areas of policy are as critical to states' long term economic health, or as significant a share of state budgets, as transportation. However, state transportation systems face two overarching challenges: their funding sources are shrinking and their investments are not made in a sufficiently strategic, economy-enhancing way. In short, the systems are both broke and broken. An emphasis on fiscal responsibility does not mean states should slow down investing in transportation. In fact, these investments are more important than ever because of the short-term job creation effects and the long-term implications for economic competitiveness. But states cannot rely on the same sources of revenue to fund transportation projects, nor can they spend transportation dollars in the same ways. Specifically, states should:

- Use transportation dollars to leverage other state investments and the strengths of metropolitan areas.
- Use market discipline to find savings and new revenue sources
- Create or augment new public/private institutions like State Infrastructure Banks

I. Introduction

Infrastructure—along with human capital and innovation—is one of the assets that will drive the next economy and is of paramount importance to maximizing growth and opportunity. Yet in the United States, transportation and infrastructure policy is at a crossroads. The current system is both broke and broken, most recently illustrated by delays in reauthorizing federal transportation laws. Though infrastructure was a prominent feature of the American Recovery and Reinvestment Act (the stimulus package) no consensus over the next generation of transportation policy has yet emerged in Washington.

In the absence of federal action, the debate on transportation policy will shift to the state level. Few areas of policy are as critical to states' long term economic health. Transportation is also a relatively significant portion of most states' budgets. At 7.9 percent of general state expenditures, "transportation" generally ranks third among state spending categories after only "education" and "public welfare," though this varies quite a bit among the states (Alabama ranks last at 3.1 percent; Nevada ranks first at 16.7 percent. Missouri is the median at 10.7 percent).[1]

Transportation is also a significant employment sector, providing jobs to more than 4 million Americans. Yet even thought there was a slight uptick in the number of workers employed in transportation, most states, like Colorado (-5,000), New York (-12,000), Tennessee (-1,400), and Michigan (-5,100) saw job declines in this sector.[2]

While state governors and legislatures recognize that their systems are job and economic engines, infrastructure investments and the decision-making process around transportation priorities have not kept pace with the growth and evolution of the economy.[3] A more export-oriented economy will require revolutionizing our ports to support next generation shipping and telecommunications exchanges. A lower carbon future means we need to remake a transportation system almost totally dependent on petroleum-based fuels. To lead on innovation, we need to make quantum leaps on new, clean infrastructure technologies. And to ensure our investments are opportunity-rich they can no longer be sprawl-inducing and decentralizing.

But these elements tend to receive insufficient consideration in state transportation programs and planning.

To bridge this gap, states should:

- Use transportation dollars to leverage other state investments and the strengths of metropolitan areas.
- Use market discipline to find savings and new revenue sources
- Create or augment new public/private institutions like State Infrastructure Banks

II. Challenges

A 21st century state transportation strategy that strengthens metropolitan America and is tightly linked to the vital elements of the next economy is critical for our nation to emerge from the rubble of the recession. Yet state transportation systems face two overarching challenges: they are both broke and broken.

First, state transportation funding sources are shrinking. Twenty-one states—including New York, Illinois, and Florida—saw transportation program area cuts in fiscal year 2010 and 11—like Michigan—expected cuts for the next fiscal year.[4] Part of the states' funding problem is that they are still heavily reliant on the motor vehicle fuel tax (the gas tax) for the bulk of their transportation revenues. From 1995 to 2008, more than half of the funds states used for highways came directly or indirectly through state and federal gas taxes (Table 1). But slowdowns in fuel consumption overall and stagnant gas tax rates have squeezed this revenue source.[5]

At the same time revenues are down, the demands for spending have increased. A litany of reports and analyses highlight the deteriorating condition of the nation's transportation infrastructure.[6] Over a quarter of major roads' rides in urbanized areas are not at acceptable levels.[7] According to the latest data, nearly 72,000 bridges (12 percent of the total) in the U.S. are considered to be "structurally deficient" meaning their condition had deteriorated to the point that rehabilitation or replacement is approaching or imminent. More than one-fifth of the bridges are deficient in states like Oklahoma, Iowa, Pennsylvania, Rhode Island, and South Dakota.[8] In addition to its condition, U.S. infrastructure lags when it comes to the deployment of advanced information and telecommunications technology.[9]

Second, state investments are not made in a sufficiently strategic, economy-enhancing way. States also face challenges because they spend their (now-declining) transportation dollars poorly. For example, many states have tended to allocate investments via logrolling rather than evidence. As a result, projects are spread around the state like peanut butter.[10] The metropolitan areas that will deliver the next economy—since they already concentrate the assets that matter to smart economic growth like transportation—are often undermined by spending and policy decisions that fail to recognize the economic engines they are and focus investments accordingly. Nor have states been deliberate about recognizing and supporting the particular needs and challenges of both metro and non-metro areas.

State transportation policies also remain rigidly stovepiped and disconnected as states fail to take advantage of potential efficiencies gained through integrated systems. By failing to join up transportation up with other policy areas—such as housing, land use, energy—states are diminishing the power of their interventions and reducing the return on their investments. This is a very different approach from how the economy functions and is out-of-step with innovations to connect transportation investments to economic prosperity. The benefits of federal, state and private investments are amplified when metropolitan areas pursue deliberate strategies across city and suburban lines that build on the

Table 1: State revenues, by source, used by select states for state-administered highways, 1995-2008

	State sources						Federal sources	Local sources
	Gas tax	Vehicle tax	Tolls	General funds	Bond proceeds	Other		
ALL STATES	22.9%	13.7%	6.1%	3.9%	14.4%	7.4%	29.7%	2.0%
California	22.0%	21.2%	3.2%	4.0%	4.9%	7.2%	28.9%	8.6%
Colorado	26.0%	20.5%	0%	6.4%	12.9%	7.7%	24.8%	1.6%
Maryland	14.6%	19.2%	10.6%	1.2%	9.2%	12.8%	32.1%	0.2%
Michigan	21.9%	15.8%	1.7%	8.6%	8.1%	6.1%	36.1%	1.7%
Minnesota	24.7%	23.4%	0%	2.0%	11.1%	5.0%	31.2%	2.7%
Nevada	38.6%	16.6%	0%	2.3%	4.3%	10.1%	27.6%	0.4%
New York	16.1%	8.8%	17.5%	4.7%	24.2%	5.8%	22.7%	0.2%
Ohio	33.8%	5.9%	6.8%	0.8%	11.6%	3.7%	35.7%	1.7%
Pennsylvania	32.1%	14.3%	11.6%	2.9%	9.2%	5.3%	24.1%	0.4%
Tennessee	34.5%	14.9%	0%	4.0%	0%	5.8%	38.8%	2.0%
Washington	25.2%	17.2%	6.3%	0.7%	3.6%	19.5%	25.2%	2.4%

Source: Federal Highway Statistics Series, 1995-2008, Table SF-3. Note: does not include 2007.

distinctive advantages of the broader metropolis.

Lastly, states have generally not had the courage to make hard choices and truly tie their transportation programs to achieving the kinds of outcomes described above. Benefit/cost or economic impact analyses are rarely, if ever, used in deciding among alternative projects and regular evaluations of outcomes are typically not conducted.[11] Most states fail to prioritize rehabilitation and maintenance on a programmatic level and instead react on a project-by-project basis. So far, efforts to reduce oil dependency are largely ephemeral. And only three states consider social equity a primary transportation goal.[12]

Incoming governors and state legislatures face serious transportation-related challenges. They can pursue band-aid approaches to shore up their budgets through standard program cuts and allow their existing programs to limp along. Or they can begin to put in place a policy framework that connects transportation to the elements of the post-recession economy in a pragmatic manner.

III. A New State Approach

An emphasis on fiscal responsibility does not mean states should slow down investing in transportation. In fact, these investments are more important than ever. But to do them right in a constrained environment, states should consider a set of low (or no) cost recommendations to enable them to marshal the resources they already have by making sure that state efforts are coordinated and efficient.

Use transportation dollars to leverage other state investments and the strengths of metropolitan areas. All too often, state agencies pursue goals and activities that work at cross-purposes or are counterproductive to one another, such as transportation and environment. The resulting duplicated services, haphazard spending, and wasted tax dollars are untenable under normal circumstances but have greater urgency as state budgets are tightening.

As the governors are putting together their cabinets they should consider strategic reorganization and appoint a "super secretariat" with the authority to link up those departments that have responsibility over investments related to transportation, economic development, commerce, housing, land conservation, and other infrastructure such as water and sewer. In this way, the state can coordinate investments to maximize economic returns in the short term (such as job creation), strategically invest for the future, and increase governmental efficiency. The state benefits not only from strategic funding and alignment of programs, but also from mechanisms for state departments to collaborate and work together in pursuit of common state goals.

For example, in California the secretary of the agency for Business, Transportation, and Housing coordinates and oversees 14 departments and several economic development programs and commissions. By executive order, Connecticut's Governor Jodi Rell established the Office of Responsible Growth in 2006 to link up policy development and capital planning in the areas of economic and community development, environmental protection, agriculture, and transportation.[13] In 2003, Massachusetts Governor Mitt Romney created a super agency called the Office of Commonwealth Development to coordinate the capital budgets of agencies responsible for environment, transportation, housing, and energy.[14]

These examples were intended mainly to coordinate resources around sustainability-type goals, but today states would benefit from better cabinet-level coordination between transportation and economic development. Michigan, for example, has a department of Energy, Labor & Economic Growth that brings together job, workforce, and economic development functions under a single agency. That office could be expanded to include transportation and environment and to centralize the economic development planning that is now carried out by the state's 14 regional agencies. New York also has a multiplicity of these agencies and has made some attempts at coordination through entities such as the Economic Recovery and Reinvestment and Smart Growth Cabinets, but there is room for deeper synchronization of these efforts.

State investments must also be coordinated with the land use and zoning regulations that localities fiercely protect. So after the policy link-up described above, they should sponsor an interagency, statewide Sustainability Challenge Competition to ensure that land use, housing, transportation, and energy conservation and efficiency are always taken into account when planning regionally for new land use and development. The competition would encourage multi-jurisdictional planning efforts and broad visions for needs like congestion relief and carbon reductions (a long-term necessity for the next economy) and reward those that can pull these disparate strands together with extra flexibility in using those funds. The sustainability challenge idea is similar to, but more ambitious than, Ohio's $1 million Local Government Services and Regional Collaboration Grant Program which is intended to improve and enhance collaboration and regional economic development among the state's municipalities.[15]

States should protect the investments that they have made over the course of decades in their metropolitan areas. A fix-it-first approach that makes system preservation the priority creates more jobs than building new capacity, up to 17 percent more jobs.[16] There is also an economic imperative to keeping transportation in a state of good repair. Infrastructure deterioration caused by deferred maintenance (presumably because of budget squeezes in the short term) can lead to greater costs in the long run. One study found that reconstructing a poorly maintained road after 25 years of neglect costs three times as much as the regular maintenance of that road over the same period.[17] And places with heavy truck traffic—such as around major ports and freight corridors—tend to see the greatest deterioration.

Only 17 states have some kind of fix-it-first policy in place to prioritize existing places and existing infrastructure.[18] In Virginia, the state code dictates that transportation funds must first be spent to pay debt service, then operations and maintenance of existing assets, then construction. To adhere to this mandate the state recently transferred $511 million in funds from its construction account to its maintenance account.[19] However, fix-it-first has to be coupled with rigorous benefit-cost analyses for all new capacity increases. In some states the reconstruction of an exurban two-lane road into a four-lane road could technically be considered a maintenance project.

Use market discipline to find savings and new revenue sources. Governors should order a full audit of their state's transportation program to ensure it is functioning in the most efficient, effective manner possible. The audit should start with standard (and useful) examinations of the inner workings of transportation departments' accounting, procurement rules, fleet management, and training. When he took over as Governor of Virginia in January 2010, Bob McDonnell called for an independent assessment of his transportation department's organizational structure, programs, and operations. His request was approved by the state legislature and in September 2010, the audit found over $600 million in immediate savings due mainly to better contracting and project acceleration.[20] A January 2009 audit of Idaho's transportation department found over $30 million in one-time savings over five years, and $6 million annually thereafter.[21]

But the audit must go farther, to investigate the entire scope of how transportation investment decisions are made within a state. For example, how closely aligned are project decisions to a cohesive strategic vision for economic growth? How coordinated are infrastructure projects? It makes no sense to make efficiency gains in a program that needs a thorough overhaul. For example, a recent audit of the Texas department of transportation recommended organizational changes intended to diminish the "singular, deeply entrenched culture" of the agency and more emphasis on business and financial management including the use of metrics to determine performance.[22]

Governors and legislators should also recognize that the fiscal crisis creates the opportunity to talk about new sources of transportation revenues – including sources that were previously considered politically infeasible. States should consider adopting market mechanisms like congestion pricing to maximize metropolitan road networks, as well as the expansion of user fees. And even voter-approved tax increases (which are evidence of willingness to pay for services) should be part of the discussion. Residents in metropolitan Phoenix, for example, recently approved a half-cent sales tax for regional transportation that is expected to generate $11 billion. Los Angeles county voters approved a half-cent increase that is projected to raise $40 billion for transportation improvements. Notably, that vote came in November 2008, right it the middle of the economic downturn.[23] Governors should encourage this kind of self help.

Create new public/private institutions. To finance the kind of major investments necessary to support the Next Economy, such as high-functioning global ports and gateways, or infrastructure that supports electric vehicles or clean technologies, states should establish a state infrastructure bank (SIB) or enhance it if one is already in place.

Beginning in 1998, when the federal government provided $150 million in seed funding for initial capitalization, SIBs have become an attractive financing tool for states. Since then, 33 states have established SIBs to finance transportation projects. Most of this support comes in the form of below-market revolving loans and loan guarantees. States are able to capitalize their accounts with federal transportation dollars but are then subject to federal regulations over how the funds are spent. Others, including Kansas, Ohio, Georgia, and Florida, capitalize their accounts with a variety of state funds and are not bound by the federal oversight which they feel helps accelerate project delivery. Other states—such as Virginia, Texas, and New York—are also examining ways to recapitalize their SIBs with state funds.[24]

But rather than bringing a tough, merit-based approach to funding, many SIBs are simply used to pay for the projects selected from the state's wish list of transportation improvements, without filtering projects through a competitive application process. A better approach would be for states to use their infrastructure banks more strategically, focusing on those transportation projects that will facilitate the flow of exports or connect workers to jobs. The projects should be evaluated according to strict return on investment criteria, not selected with an eye towards spreading funding evenly across the state. (Such an approach is analogous for how the federal government should establish a national infrastructure bank.)

States should also think beyond just transportation and create true infrastructure and economic development banks to finance not just roads and rails, but also energy and water infrastructure, perhaps even school and manufacturing development. California's Infrastructure and Economic Development Bank ("I-Bank") provides a compelling model. After its initial capitalization of $181 million in 1999, the I-Bank has funded itself on interest earnings, loan repayments, and other fees, and has supported over $400 million in loans.[25]

Then, either as part of the augmented SIB or separate, states should help broker the often complex infrastructure partnerships between the public and private sectors. A poll by the financial advisory firm Lazard shows strong willingness for states to consider private investments rather than increasing taxes, cutting budgets, or taking on more debt.[26] However, the private sector is now seeking more legislative certainty prior to bidding on projects and has little appetite for negotiating transactions that are subject to legislative or other major political approvals. While half of the states have enacted enabling statutes for public/private partnerships (PPPs), the wide differences between them makes it time consuming and costly for private partners wishing to engage in PPPs in multiple states to handle the different procurement and management processes.[27] States should therefore move to enact comprehensive PPP legislation that is accountable, transparent, and permanent. They should also push the federal government to play a helpful role with its state and metropolitan partners by creating standards and providing technical advice to be considered in PPPs. The GAO recently noted that the federal government has done much to promote the benefits of PPPs but it needs to do more to assist states and metro areas in this way.[28]

Conclusion

Our nation's transportation decisions will have enormous implications for the health of our metropolitan environment, the quality of our communities, and the vitality and prosperity of our economy.

Yet states are not in this alone. The federal government also needs to reform and invest in transportation. Under a deficit-neutral approach, the existing transportation law should be reauthorized (not simply extended), for two full years at its current funding level, to provide stability for transportation planning—including hiring workers. But even though the level of funds should remain the same, there must be reforms in how those funds are spent. These reforms include: federal performance measures in safety and system-wide asset management; a new partnership with metro areas that raise their own revenue that reduces bureaucracy and accelerates project delivery; better coordination of existing federal credit assistance programs such as TIFIA; and a permanent authorization of the so-called TIGER grants to encourage state and metropolitan innovation. [29] These critical reforms set the stage for a truly transformative six-year bill in 2013.[30]

Other initiatives like the high speed rail program represent a very different model from the late 20th century federalism in transportation with the federal government providing resources that rain down unencumbered to the state and metropolitan level. The new 21st century model of competitive award funding demands that our nation's state and metropolitan leaders develop innovative approaches to pressing transportation problems, and contribute their own funds to see the projects through. Deep commitments from a broad range of stakeholders—public/private, state/local, legislative/executive—is essential. For projects that extend beyond individual state borders, close coordination—both formal and informal—with neighboring states is essential. More than just backroom deals, these are lengthy relationships that bear real fruit in the form of finalized plans, environmental reviews, and dedicated shared funding agreements. The challenge with this model comes, as the 2010 election has shown, when new governors decide that the federal government's offer of funding is comparable to an offer of a free puppy: the on-going maintenance demands are more than they want to bear.

The recent dust-up over high speed rail proves an important point: States and governors are still in the driver's seat when it comes to transportation decisionmaking and project selection. So even with robust federal action, and a framework that puts transportation policy in the service of an American economy driven by exports, powered by low carbon, fuelled by innovation, an rich with opportunity, it is still incumbent upon the states to carry it out.

Endnotes

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