TESTIMONY

April 16, 2014

Funding Transportation With A Temporary Sales And Use Tax

By Joseph Miller

Missouri Senate Transportation and Infrastructure Committee

To the Honorable Members of this Committee:

My name is Joseph Miller and I am a policy researcher for the Show-Me Institute, a nonprofit, nonpartisan Missouri-based think tank that supports free-market solutions for state and local policy. The ideas presented here are my own. This testimony is intended to summarize research that analysts for the Show-Me Institute have conducted and reviewed regarding proposals to impose new taxes to pay for Missouri's transportation infrastructure.

Upon the legislature's and voters' approval, Missouri Senate Joint Resolution 48 (SJR48) would institute a 1 percent sales tax to fund significant transportation infrastructure investment in Missouri. The tax would expire after 10 years. SJR48 also proposes placing a freeze on the motor fuel tax and prohibiting the state, counties, and municipalities from tolling highways or bridges unless voters give approval.

Missouri needs adequate infrastructure investments. However, the Missouri Department of Transportation (MoDOT), the agency tasked with building and maintaining most of our state's transportation infrastructure, has an unsustainable funding trajectory. Despite cuts to staff and other cost-saving measures, cash available for MoDOT's construction projects have been cut in half in the last two years, preventing the department from adding any new projects to the State Transportation Improvement Project (STIP). By 2017, the department will not have enough funds to maintain the system as it currently exists, much less improve it.[1] This situation is the result of a gradual erosion of the user-targeted taxes that were designed

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to fund the majority of Missouri's transportation infrastructure. The impact is being felt now because state-issued bonds and federal aid allowed necessary investment to temporarily increase. With those short-term funding sources exhausted, it is incumbent on Missouri policymakers to put the state's transportation funding on a sustainable path. However, a statewide 1 percent sales tax is a highly questionable policy solution. It is economically unsound, fundamentally unfair, and takes Missouri further down the road of unsustainable, taxpayer-subsidized transportation funding.

Missouri's different modes of transportation all have variable funding methodologies. However, the majority of MoDOT's fiscal responsibilities are roads and bridges. Thus, the majority of the proceeds from a sales tax would go toward roads and bridges. Approximately 70 percent of the dedicated funding for state roadways comes from state and federal gas tax proceeds. The motor vehicle sales tax and revenue from permits provide most of the remaining funding.[2] Unlike the proposed 1 percent sales tax, these are indirect user fees. The gas tax charges drivers who actually use the roads. That money is then spent on improving road and bridge infrastructure in the state. This creates a connection between funding for roads and the demand for roads. If the gas tax is at an adequate level, as Missourians drive more, MoDOT would receive more money to maintain and construct the roads.

This system has fundamentally broken down because at both the federal and state levels, the gas tax has not increased. The gas tax in Missouri has remained at 17 cents per gallon since 1996, and the federal gas tax has not changed since 1994.[3] This means that if we account for inflation, Missouri's gas tax has lost a third of its purchasing power. At the same time, road design specifications have improved and material costs have increased faster than inflation, making project construction more expensive.[4] In addition, higher fuel efficiency in motor vehicles means that Missourians consume more road while paying less tax. Therefore, MoDOT has seen its costs rise and its revenue fall.

MoDOT avoided having to deal with funding issues for the last decade because Amendment 3 to the Missouri Constitution authorized billions of dollars in bonds and the state received federal stimulus dollars.[5] Thus, MoDOT could increase its transportation spending even as its long-term tax base eroded. Essentially, Missouri drivers received new or repaired roads and bridges without being asked to create a system to pay for their construction or long-term maintenance.

The better policy moving forward is for Missouri to modernize its user pay model so that it can fund necessary transportation infrastructure into the future. This means, if necessary, raising the gas tax and implementing tolling on major roads and bridges throughout the state.

The gasoline tax in Missouri is relatively low compared to other states. As of Jan. 1, 2014, Missouri had the sixth-lowest gasoline tax in the nation.[6] While having a low tax is not a bad thing, it is irresponsible when the expenditures it is designed to cover are being paid for through debt, federal aid, and now, potentially, general sales taxes. Furthermore, raising the gas tax is a feasible solution to MoDOT's funding problems. The decline of the effectiveness of gas taxes can be overstated. Simply raising the gas tax to its inflation-adjusted 1996 level could bring in an extra $300 million per year for MoDOT, assuming there are no significant changes in driving habits.[7] The increase in the cost of fuel would also marginally reduce demand for driving, reducing MoDOT's construction and maintenance costs.[8]

Long-term, using gasoline taxes to fund road infrastructure may not be the best model.[9] But for now and the near future, gas taxes remain an effective way to fund transportation in Missouri. License and registration fees also could be increased to help ensure that cars with extremely high gas mileage pay for using the roads. As the gas tax remains an effective funding tool, it is difficult to justify making bicyclists and pedestrians pay the same for highways as truckers via general sales taxes when the gas tax could be increased instead.

The state also could explore tolling, which basically is not used in Missouri. Tolling connects the act of using the road, bridge, or port to the method of paying for it. In 2008, the Show-Me Institute released a policy study examining how tolling could increase the use of public-private partnerships (PPPs) in addressing Missouri's transportation needs.[10] PPPs will not be the right solution for many of the transportation needs that the state faces, but for some larger projects, they offer an important option worth careful review and consideration. In some instances, public-private partnerships would allow Missouri state and local governments to deliver much-needed transportation improvements in a cost-effective, timely, and fair manner. The Lake Ozark Community Bridge has demonstrated that tolling can work in Missouri in certain situations. Reconstruction of I-70 is another example where open-road tolling could work.[11]

However, as written, SJR48 prohibits the state, counties, and municipalities from owning or operating toll bridges and highways unless they have voter approval. Instituting these additional restrictions will remove a mechanism for connecting the act of using the road, bridge, or port to the method of paying for it. SJR48 makes tolling more difficult in the state, which is a step in the wrong direction.

While infrastructure investment creates indirect benefits, there is no reason that benefit cannot be internalized into the cost of goods. For example, trucks are needed to deliver goods to consumers, even to those consumers who rarely drive on the roads. By increasing the cost of transporting these goods, which an increase in gasoline taxes or tolling would do, the sellers of these goods can pass some of this cost increase onto consumers.[12] Thus, these consumers, who could derive indirect benefits from increased infrastructure investment, will indirectly pay for the investment.

Unlike tolling and gasoline taxes, SJR48's proposed general sales tax does not connect the act of using the road, bridge, or port to the method of paying for it. This approach is not economically sound. If people pay for roads and bridges based on how much they shop and not how much they drive, it will make driving look comparatively cheap, pushing people to drive more at any gasoline price, thereby increasing congestion, pollution, and urban sprawl.[13] The subsidized increase in driving will force MoDOT to spend more money on highway expansion and road maintenance.

MoDOT's funding needs will increase due to this disconnect between road provision and user payment. At the same time, the underlying funding base will continue to erode because SJR48 freezes the gasoline tax and raises barriers to tolling. These provisions virtually guarantee that when the sales tax expires in 10 years, MoDOT will face a much worse funding shortfall than it does today. Such a shortfall will necessitate the continuance of the 1 percent sales tax or possibly a tax increase. Nobody should be under the illusion that the proposed sales tax will be temporary unless something is done to fix the user pay system that underlies transportation funding in Missouri. With this proposal, it is not possible.

The state should determine which projects deliver the greatest benefits for its residents and find the means to finance these projects in a manner that causes the least amount of harm to taxpayers. Analysts for the Show-Me Institute have commended the General Assembly for considering tolling in the past. Tolling and gas tax increases may be unpopular and general sales taxes may seem to be preferable for residents. However, the state is best served by policy that allows the delivery of state services in the least economically harmful way. If Missouri pays for these transportation bonds via a general sales tax, people who do not drive will be paying the same amount for roads and bridges as long-distance commuters will pay. Even if drivers and non-drivers both derive benefits from the increased infrastructure investment, that does not mean they derive an equal benefit. Furthermore, both groups will feel the negative externalities of an inefficient transportation system. People who commute 2 miles to work should not be paying the same for roads as someone who commutes 40 miles to work. That is not good public policy.

It is appropriate for Missouri to issue bonds to invest in transportation and to provide a dedicated funding source to pay for those bonds. However, it would be better public policy if Missouri transportation leaders did not focus on general sales taxes simply because it is the least contentious source of funds. A better alternative is to seek PPPs and tolling authorization. Short of that, gasoline tax and registration fee increases are the preferable way to fund the bonds and strengthen the transportation infrastructure in Missouri.

NOTES:

[1] Missouri Department of Transportation (MoDOT). “Bleak Financial Forecast for MoDOT.” View online here: http://www.modot.org/newsandinfo/District0News.shtml?action=displaySSI&newsId=192529.

[2] For a full breakdown of MoDOT revenue, see “MoDOT 2013 CAFR.” Pgs. 26-29. View online here: http://www.modot.org/about/general_info/documents/FY13CAFRFINALPUBLISHED.pdf.

[3] MoDOT. “Financial Snapshot: Oct. 2012.” Pg. 13.

[4] MoDOT. “A Vision For Missouri’s Transportation Future.” Pg. 34.

[5] MoDOT. “2013 CAFR.” Pgs. 122-123.

[6] American Petroleum Institute. “State Motor Fuel Taxes.” View online here: http://www.api.org/oil-and-natural-gas-overview/industry-economics/~/media/Files/Statistics/state-motor-fuel-taxes-report-summary.pdf.

[7] MoDOT. “Financial Snapshot: Oct. 2012.” Pg. 19.

[8] Hymel, Kent M., Kenneth A. Small, and Kurt Van Dende. “Induced Demand and Rebound Effects in Road Transport.” University of California-Irvine. The study suggests that a 1 percent increase in the price of fuel leads to a long-term 0.24 percent decrease in vehicle miles driven, on average. An impact study from Yale found the effect to be a 0.22 percent decrease. View online here: http://www.iaee.org/en/students/best_papers/Gillingham.pdf.

[9] Virginia Department of Transportation (VDOT). “Vehicle Miles Traveled (VMT) Tax: An Alternative To the Gas Tax for Generating Highway Revenue.” View online here: http://vtrc.virginiadot.org/rsb/rsb19.pdf.

[10] Stokes, David C., Leonard Gilroy, and Samuel Staley. “Missouri’s Changing Transportation Paradigm.” Show-Me Institute Policy Study. February 2008.

[11] For more information, see MoDOT’s “A Public-Private Partnership to Rebuild, Expand I-70 in Missouri.” View online here: http://www.modot.org/i-70p3/documents/12-01-07WHITEPAPER.pdf.

[12] The amount of the increase in prices passed along to the consumer due to higher transportation costs depends on demand elasticity, elasticity of supply, and market competition of the goods in question. For example, see Maritime Administration, U.S. Department Of Transportation’s “Impact Of High Oil Prices On Freight Transportation: Modal Shift Potential In Five Corridors Technical Report.” Pgs. 13-15.

[13] Brand, Dan. “Impacts of Higher Fuel Costs.” View online here: http://www.fhwa.dot.gov/policy/otps/innovation/issue1/impacts.htm.

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