Texas Transportation Commission

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April 23, 2009

The Honorable John Carona
Chairman
Committee on Transportation and Homeland Security
Texas Senate
P.O. Box 12068
Austin, Texas 78711

Dear Chairman Carona:

This is in response to your request for an overview of the situation that Texas faces with respect to transportation finance. As you know, in 2001 and 2003 the legislature provided several valuable tools that have allowed the Texas Department of Transportation (TxDOT) to accelerate projects. The Texas Mobility Fund, Proposition 14 Bonds, Comprehensive Development Agreements, and Pass-Through Financing helped get projects to construction more quickly than what would have otherwise been possible.

But we have reached the end of what we all knew would be a temporary spike in our contracting levels. The state's transportation program is settling back upon its reliance on fluctuating fuel taxes and as we have reported before, current fuel tax receipts are at reduced levels. Also our construction program for the foreseeable future must reflect the uncertainty of federal funding, historically increasing costs, lower-than-anticipated revenues, and other competing priorities of state budget writers.

The Bottom Line

As presented at the April 8, 2009 hearing of the Senate Transportation and Homeland Security Committee, during the first quarter of 2012, projected expenditures will exceed expected revenue. The forecasting data developed by the Texas Association of Metropolitan Planning Organizations and TxDOT in consultation with the Texas Transportation Institute show at this point in time our ability to finance new construction projects will only be possible if we make severe cuts in our maintenance program. There are a number of factors contributing to this reality which are outlined in more detail below.

Reliance on Debt

TxDOT has available a variety of debt programs to help advance projects. Borrowed money has helped the department continue growth in contracting over the last six years. But we are rapidly reaching the end of those programs. Using traditional funding sources such as gas tax revenues, vehicle registration fee revenue, and federal reimbursements, our contracting totals in 2010 and 2011 will be below that which we achieved in the years prior to the enactment of HB 3588 in 2003.

Texas Mobility Fund
The Bond Review Board authorized the commission to issue $6.4 billion in Texas Mobility Fund bonds based upon earlier Comptroller revenue estimates. The department began work on projects using these bond proceeds and issues the debt when the cash is needed to make payments on those projects. We have issued $5.1 billion to date and anticipate needing the remaining $1.3 billion by the end of FY 2011. However, the Comptroller is required to provide an updated revenue certification before debt can be issued. Based on the Biennial Revenue Estimate (BRE) from January, revenue will not support all $1.3 billion in needed bond proceeds. We have requested an updated 30-year forecast from the Comptroller. In the meantime, based on the BRE, we could be short at least $275 million to honor commitments. Because projects using the mobility fund are already underway, TxDOT may need to delay new projects in 2009 and 2010 in order to cover the shortfall.

Proposition 14 Bonds
As the House and Senate versions of SB 1 currently stand, the agency's construction and maintenance programs would be reduced between $66 million (Senate) and $110 million (House) over the biennium to help pay Prop 14 debt service in the 2010-2011 biennium.

We are authorized to issue $6 billion in bonds that are payable from future deposits to the State Highway Fund. Prop 14 bonds are not a new source of revenue because over the twenty years that the debt is outstanding, the debt service payments reduce the level of resources available to build and maintain highways. Used judiciously, the cost of this program is offset by avoiding the inflationary effects of pay-as-you-go financing. Used regularly, the debt service erodes the level of resources available to preserve existing assets and ensure the safety of the traveling public. For these reasons, the commission was not inclined to issue more than $3.1 billion through fiscal year 2008.

However in August 2008, as TxDOT was putting the finishing touches on its Legislative Appropriations Request, the commission received a letter from the Governor, Lieutenant Governor, and the then Speaker of the House urging the commission to make use of the remaining Prop 14 debt. The commission acceded with the understanding that other commitments cited in their letter would be achieved, particularly, ending "the practice of funding the Department of Public Safety (DPS) with gas taxes that are needed for road construction." The commission believed that the legislative leadership would end diversions by an amount sufficient to cover debt service payments on the additional $2.9 billion of Prop 14 bonds. Neither the House or Senate version of SB 1 achieves this.

In its current form, the Senate-passed version of SB 1 provides about $300 million of the $365 million necessary to cover debt service in 2010 and 2011. Because of the timing of Prop 14 debt issuance, full debt service of approximately $480 million per biennium will not be due until 2012-2013. We believe it is only prudent to assume, based on the Senate version, that only $300 million will be carried forward to that biennium, and therefore the remaining $180 million in debt service would need to come from other parts of TxDOT's budget or a commensurate amount of Prop 14 financed projects will need to be delayed and placed in line for funding through the pay-as-you-go program.

Appropriations for 2010-2011

Based on the provisions of SB 1 as it was approved in the Senate, TxDOT anticipates that it will be able to go to contract on $2 billion of construction and maintenance projects in 2010, and $1.7 billion in 2011. These totals include the issuance of all $2.9 billion in Prop 14 debt, beginning in FY 2009. It does not include $2 billion in Proposition 12 debt (backed by general revenue) which is contingent on the passage of SB 263 which authorizes the debt. Nor does it include the NTTA payment to be used in the Dallas District or federal stimulus funding. None of these sources are sustainable into the future.

While our letting capability in 2010 and 2011 may appear acceptable to some, there are other forces at work to which we must be attentive. As you know, transportation projects take many years to complete from the time they are conceived and developed. We must look past the next biennium to ensure that our revenue forecast in the out years are sufficient to cover the obligations we incur today.

Maintenance
While transportation planning is complex, the choices before us are relatively simple. The more funding we devote to maintaining our aging system, the less money we have available to put toward new construction. And the longer we wait to maintain the system, the more costly it is to keep our roads in safe condition. At the behest of many in the legislature, the commission has reduced the amount or funding programmed for maintenance in coming years in order to mitigate the need to reduce our construction program. We were able to do so with the thought that we may be able to backfill needed maintenance funding with reduced diversions and perhaps bond funds. This scenario appears less likely now. The commission will be presented with highly difficult decisions to make with respect to how much of our lettings in 2010 and 2011 will be split between construction and maintenance.

Federal Funding
Another situation that has recently become evident in SB 1 is that there is not enough state funding in certain strategies to draw down federal funds. The Senate version of the appropriations bill provides a small amount of state funding in the strategies for New Construction and New Maintenance to draw down some of Texas' share of federal funding in the next biennium, but it may not be enough. The version approved by the House is lower by about $50 million in 2010 and $30 million in 2011. We will offer appropriators our thoughts on how to adjust the methods of finance in our appropriation to ensure that Texas does not lose federal funding. SB 1 appropriates anticipated federal reimbursements of $2.89 billion in 2010 and $2.77 billion in 2011.

On the topic of federal funding, I should note that in addition to a subpar rate of return, Texas continues to deal with the effects of federal budgetary maneuvers. Since 2006, Congress has rescinded $1.2 billion in funds apportioned to Texas. We expect another rescission of approximately $720 million at the end of this federal fiscal year. To be clear, we are well aware of Congress' tendency to rescind funds and we remain cognizant of them when we program funds. The questions surrounding the pending reauthorization of the surface transportation program and continuing rescissions contribute to the uncertainty of our program into the future. Unless substantial corrective action is taken on the federal level, Texas stands to lose up to an estimated $1.4 billion in apportioned formula funding in 2010.

Pass-Through Tolling
The House version of SB 1 includes a rider that requires TxDOT, under the pass-through tolling program, to encumber an amount not less than the reimbursements committed in the 2008-2009 biennium.

The pass-through tolling program has been a popular mechanism for local communities to advance a project to construction. However, by definition, these projects are those that have not risen to the top of a district's priority list, or there would be no need to move it up with pass-through tolling. Because funding is limited, if we continue to advance projects at the back of the list there will be little or no funding left for those identified by regional planners as top priorities.

Competing Priorities

The 81st Legislature is considering various bills that would have an impact on the amount of revenue to the State Highway Fund. There are also many bills that would increase costs that are payable from the State Highway Fund. Here are the highlights.

Exemptions
Several bills are under consideration that would provide exemptions for various entities from paying the state motor fuels tax. While these entities use highways to perform important functions, such as transit and emergency services, the exemptions begin to add up.

Additionally, there are several bills that would exempt certain individuals from paying tolls. While the amount of lost toll revenue would likely be small, the greater impact would be on commitments the state makes with its bond holders.

Lost Revenues
The subject of "diversions" is usually discussed in the context of appropriations. But there are statutory diversions as well. Current law sends approximately $85 million per year from the State Highway Fund to the Texas Emissions Reduction Plan through 2015. There is legislation under consideration this session that would continue the transfer from 2016 to 2019 when the amount transferred would increase to around $105 million per year.

Additionally, there are bills that would increase State Highway Fund support for county roads.

Increasing Costs
Lastly, there are many bills that would increase the cost of highway right of way. The department takes great care to design and construct projects in the fashion that minimizes the impact on landowners. To do so is both cost efficient and simply, the right thing to do. Over time, road projects greatly enhance the value of adjacent land. But there are certainly negative

consequences in the short term. Recognizing these circumstances, over many decades, state and federal courts have carefully created a standard that protects the rights of landowners while preserving the ability of the public to build critical infrastructure. The 81st Legislature is likely to change that standard in an effort to provide additional compensation to landowners. This would have a significant impact on TxDOT's budget.

I appreciate your solicitation of our views on our financial situation. Even during the intensity of a legislative session, we must be able to talk frankly about our challenges so that we can identify solutions. I very much appreciate your encouragement and good counsel as we work together to meet our goals to reduce congestion, enhance safety, improve air quality, provide economic opportunities, and preserve the value of our state's transportation assets. Please feel free to contact me at (512) 305-9509, or if your staff has any questions, they may contact Patrick Marotta, Government and Public Affairs Division, at (512) 305-8983.

Sincerely,

Deirdre Delisi

Deirdre Delisi
Chair
Texas Transportation Commission

cc: Members Senate Transportation and Homeland Security Committee
The Honorable Glenn Hegar, Texas Senate
Texas Transportation Commission
Amadeo Saenz, Jr., P.E., Executive Director, TxDOT