STATEMENT OF
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Mr. Chairman, I am happy to be with you today to discuss alternative ways of financing federal transportation programs. In response to a request from this and other committees, the Congressional Budget Office has examined several approaches to transportation finance. In my comments this morning, I would like to focus on five major topics: (1) why this session offers the Congress a unique opportunity to reconsider its financing mechanisms for transportation programs; (2) the difference between program and financing issues; (3) the financing approaches that are available; (4) the principal issues raised in selecting a mechanism for transportation finance; and (5) our assessment of how the various approaches rank with respect to these issues.

A UNIQUE OPPORTUNITY

For a number of reasons, the Congress has a unique opportunity in this session to reconsider the way in which federal transportation programs are financed. First, the existing Highway Trust Fund expires in 1979, and the Airport and Airways Trust Fund expires in 1980. Second, the Administration has proposed both a new highway bill and a new transit bill that consolidate programs and could be the first step toward a unified trust fund. Third, urban public transportation, intercity railroads and buses, and other modes are requesting additional federal funding, and proposals for specialized trust funds are proliferating. Fourth, a major shift in highway spending is occurring: maintenance costs, rather than new construction costs, are becoming dominant. The magnitude of these maintenance costs and the

degree to which they are assumed to be a responsibility of the federal government--as opposed to the state or local government--must be addressed. Lastly, because of the Energy Policy and Conservation Act of 1975 and the energy legislation presently pending in conference, gasoline consumption and therefore Highway Trust Fund revenues are expected to increase in the future much more slowly than the past. On account of inflation, the purchasing power of these funds will be greatly eroded. Not only is this a significant problem to the Federal Highway Trust Fund but it is also of particular concern to the states since their financing also depends primarily on excise taxes on motor fuels.

PROGRAM AND FINANCING ISSUES

In this testimony and in the forthcoming CBO report, the focus is exclusively on the way in which the programs are financed--for example, whether to use a trust fund or a direct appropriation. Program issues, which are also of extreme importance to this committee, will be addressed in later CBO reports. In particular, the following program questions were not considered as factors in evaluating the various financing mechanisms:

- Is a particular mode adequately funded?
- What is the proper mix of modes?
- Are the types of activity that qualify for federal aid suited to the mode's physical and organizational structure?
- Are the matching shares, recipient agencies, or program eligibility requirements appropriate?

These program characteristics may be easier to change or to coordinate under one set of financing mechanisms than under another. Thus, they are indirectly linked to the choice among financing mechanisms, but they are of secondary concern as far as this choice is concerned.

ALTERNATIVE APPROACHES

The broad range of techniques available for financing transportation is reflected by current practices. Highway and aviation programs are financed by trust funds that are supported by user charges; transit has been financed using both contract authority--which will be restricted in the future--and direct appropriations from general revenues; and water, rail, and some air programs are authorized and appropriated from general revenues.

This morning I would like to focus on four alternatives that illustrate distinctly different choices. These are:

- Continuation of existing financing practices, in which highways and airways are financed by the trust funds and other modes receive appropriations from general funds;
- A unified trust fund, in which all modes would receive support from a single, multimodal fund;
- Modal trust funds that would establish a separate, earmarked revenue source for each mode; and
- No trust funds whereby all modes would rely on the general fund with liberal use of advance appropriations.

PRINCIPAL ISSUES

Six principal issues underlie the choice of financing mechanisms for

federal transportation programs:

1. What changes in financing practices would improve the ability of the Congress to develop coordinated, multimodal transportation policies?

By coordinating its transportation policies, the Congress can create a more efficient transportation system as well as one that is more responsive to other national goals. Setting policy mode-by-mode rather than for transportation as a total network can produce laws that work at cross-purposes. A subsidy for small-city airlines has hurt passenger train service. A subsidy for trains can cut into intercity bus revenues. Aid to highways can result in higher levels of air pollution and lead to support for mass transit in order to reduce pollution. Setting transportation policy without taking fully into account other national problems and goals such as energy, the environment, and economic development can lead to the same sorts of conflict on a larger scale.

The financing mechanisms currently used by the Congress are not conducive to coordinated policymaking either within transportation or among other programs. For a variety of historical reasons, the Congress has adopted trust funds, contract authority, and regular appropriations from general revenues to finance transportation. These diverse practices have partially insulated some modes from consideration in a multimodal context. Highway programs, for example, affect energy, environmental, and

developmental policy, but the inflexibility of the Highway Trust Fund makes it difficult for the Congress to address these concerns.

The elimination of trust funds and the adoption of direct appropriations could enhance the policy process by enabling the Congress to respond more quickly to changing conditions. A unified trust fund for all modes could facilitate multimodal consideration during authorization, but this potential advantage could be difficult to realize, depending upon how the modal shares of the unified fund are determined. A rigid allocation of modal shares would cancel out the potential of this approach for achieving integrated policy. Moving to a group of separate modal trust funds would probably create even worse problems because it would institutionalize modal separation.

2. How can the Congress provide the states with sufficient financial assurance for planning purposes?

States and localities need some medium- to long-range assurance regarding future financing in order to plan effectively and to invest current resources efficiently. All modes of transportation have some construction projects that require many years to plan and build. States and localities are reluctant to invest their own resources to plan or to start such projects unless long-term funding is reasonably assured.

In making long-term commitments to the states, however, the

Congress diminishes its budgetary flexibility in future years, and thereby reduces its ability to respond to changing priorities. Thus, the Congress, in meeting the needs of the states, should guard against granting excessive assurance.

Separate modal trust funds afford the greatest overall assurance to the states and localities, and it follows that the current system of financing affords substantial assurance for highways and airways. A unified trust fund could offer assurance for each mode if modal apportionments were inflexible, but such an inflexible approach would compromise the multimodal coordination that a unified trust fund could potentially achieve. Thus, the most meaningful form of a unified trust fund is likely to offer little assurance for individual modes. Elimination of trust funds would bring less assurance than that achievable with trust funds. By using rolling, long-term authorizations and advance appropriations, however, substantial assurance could be provided even without trust funds.

3. How can the Congress maintain budgetary control?

It is clearly in the federal interest to ensure that federal spending accurately reflects legislative priorities. Financing mechanisms that set rigid, long-term spending patterns or earmark revenues clearly restrict budgetary control. The granting of contract authority under trust funds further restricts consideration by the appropriations committees.

If the various financing mechanisms are ranked according to the degree of budgetary control they would allow, individual trust funds rank lowest, followed in order by the present system and a unified trust fund. The greatest budgetary control would be gained through abolition of trust funds. Because single-year appropriations would in many cases not provide adequate assurance to states and localities, it may be desirable to sacrifice some budgetary control by moving to two- or three-year advance appropriations.

4. Would changes in financing practices provide each mode with nondiscriminatory access to the federal purse?

The financing process is imbalanced if it establishes procedural advantages or disadvantages for a mode in competing for financial aid. Highways are often said to have an unfair advantage over public transportation because the Highway Trust Fund makes it easier for them to gain continued support by allowing them to avoid the periodic justifications that were required of other modes. The growth of highway programs, however, resulted as much from the earmarked, growing source of funds that supported the programs as from the trust fund itself. In the future, trust funding with inadequate or declining revenues could prove to be a drawback rather than an advantage.

In short, whether trust funding works for or against the mode thus funded, the inherent inflexibility of this device most likely creates an

imbalance in the allocation of fiscal resources among all modes. This risk is particularly severe under current practice because the unequal ability to make short-term adjustments distorts balanced spending. This risk is least serious when all modes are financed the same way, either through a unified trust fund or from general revenues in the form of a direct appropriation.

5. Should user charges be an essential element of federal transportation finance policy, and can they be applied meaningfully under alternative financing mechanisms?

Charges related to the use of transportation facilities are termed "user charges." These charges may be collected at specific facilities (such as tolls on a bridge), or they may just reflect the general level of use (such as taxes on gasoline). User charges represent a way of recapturing from the actual beneficiaries some of the costs to the general public. Levying user charges promotes economic efficiency because users pay, directly or indirectly, for the services they receive. Proper incentives are provided, since heavier use imposes greater costs on the user and, at the same time, generates revenues to expand facilities.

The absence of user charges implies subsidies. Federal aid without related tax collections subsidizes the beneficiaries. This is not necessarily wrong, but the question should be raised: Are there valid reasons for government to subsidize particular transportation modes and their users? In many cases the answer will be yes, especially if the beneficiaries are

particularly needy or if the related benefits to society and to the economy are particularly notable. Thus, user charges might be reduced or eliminated in recognition of the need of low-income individuals for mobility, or to promote and preserve our urban centers. Whether or not user charges are continued is a value judgement that Congress must ultimately decide.

In general, transportation programs with trust funds are financed by user charges, and financing mechanisms that rely on trust funds are most likely to adhere to the principle that the user pays. Trust funds have generally been the legislative price for the imposition of user charges. The increased highway excise taxes and the air ticket tax are recent examples. Trust funds, however, are not the only way to impose user charges. For example, prior to the creation of the Highway Trust Fund, highway user charges were informally linked to highway expenditures without reliance on any formal dedication or accounting. Proposals for waterway user charges have not, to date, included a trust fund arrangement; rather, they have been based on the premise that federal costs should be recovered.

6. What implications would changes in federal financing mechanisms have for state and local government organizational structures?

In order to be most effective, federal financing mechanisms should minimize the difficulties that other agencies have in using the funds. For example, a change in the cycle of federal funding may upset the timetables at other levels of government, force administrative changes, and create

unnecessary delays.

The unified trust fund raises the greatest concerns about organizational compatability. In order to maintain Congressional flexibility--and that is the major strength of this approach—apportionments to individual modes would need to be somewhat uncertain, and state organizations that are fragmented by mode might not be able to handle shifts in apportionments efficiently. Whether or not a unified trust fund is a desirable arrangement in the long run; it would be almost impossible to establish such a fund immediately, using existing organizational structures. Similarly, moving away from trust funds in highway and airway finance could create transitional difficulties for the organizations that have responsibilities in those areas. Separate modal trust funds and the extension of current policies would pose the least amount of organizational problems.

ASSESSMENT OF ALTERNATIVES

At this point, I would like to summarize how the alternative financing mechanisms stand in terms of the principal issues. The relative importance of these issues is a subjective matter, and none of the available financing mechanisms stands out as being clearly superior.

Current Financing Practices. The current financing practices have two serious defects. First, because of their uneven treatment of the modes

and their lack of any comprehensive multimodal review, they restrict the ability of the Congress to coordinate the transportation policies that it develops for each of the modes and they make it difficult to alter transportation policies to blend with environmental, energy, developmental, and other national priorities. Second, the current practices are not conducive to good fiscal control because of the varied and sometimes inflexible instruments they employ, and because they exempt so much spending from the normal appropriations process. On the other hand, current practices offer substantial continuity of support to the states and localities, although this assurance has been uneven across modes. Also, state and local organizations have grown up around existing financing procedures, and continuation of existing practices would minimize the organizational adjustment required from these agencies.

Unified Trust Fund. A unified trust fund could consolidate fiscal decisions for transportation as a whole and permit better Congressional coordination of modal financing, depending upon the degree to which intermodal conflicts are resolved at the authorization stage. It is not clear, however, whether a workable way can be found to review counterproductive policies and spending across transportation activities. Assuming that a way is found, the unique advantage of a unified trust fund would be its joint consideration of modal shares; this seems likely to yield reduced mode-by-mode assurance to states and localities because substitutions among the modes would be possible. This advantage would be lost if modal allocations were determined according to an inflexible formula. Separate, functionally

oriented trust funds--such as the creation of two trust funds, one for intercity modes and the other for urban transportation--would have the same general advantages as a unified trust fund.

Separate Modal Trust Funds. By contrast, if each mode had its own trust fund, the weaknesses of the present situation would be further entrenched. Separate modal trust funds would institutionalize the barriers to integrated policymaking and to improved fiscal control by insulating each mode from the policies of the others. This would be especially true if contract authority continued to be granted for trust fund programs. Comprehensive, multimodal coordination of transportation activities would be even more difficult to accomplish than it is now. This approach would, however, offer the greatest assurance to the states and localities, although it would mean a substantial loss of Congressional control.

No Trust Funds. The elimination of trust funds appears to be the most promising of the options reviewed here, because it substantially strengthens the roles of the Congress to make policy and to exercise fiscal control. By placing all modes on an equal and flexible footing, the Congress would increase its coordination and review of transportation policies through both the authorizing and the appropriating committees. Many are concerned with the loss of assurance that the appropriations process imples for states and localities. The use of advance appropriations, however, could provide any degree of assurance deemed necessary. State organizations and legislative processes would require several years to adjust to this process.

None of the financing mechanisms is ideal in every respect. Nevertheless, it is clear that the current situation could be greatly improved. Pressures on transportation policymakers are likely to intensify considerably in the next decade, and the Congress could reduce these stresses by starting now to overhaul the financing mechanisms used for transportation assistance.

Mr. Chairman, I would be happy to answer any questions that you or Members of the committee might have.