MINNESOTA'S HIGHWAY FINANCES

This section describes Minnesota's highway financing, followed by historical revenue trends since 1975.

MOTOR FUEL TAX

The state motor fuel tax is a major source of revenue for highways in Minnesota. Each one cent of gas tax yields about $30 million per year to the Highway User Tax Distribution (HUTD) Fund and thus about $18 million in revenues to the Trunk Highway (TH) Fund. The current tax yielded $823 million in FY 2010 after refunds, but before collection costs and transfers to the Department of Natural Resources (DNR).

Approximately eighty percent of motor fuel tax revenues are generated from gasoline sales. The remainder comes mostly from diesel and special fuel sales.

State law requires transfers of non-highway use gasoline tax revenues (e.g., from fuel used in boats and snowmobiles) to accounts managed by the DNR. About 3% of gasoline tax revenues, or approximately $20 million in FY 2010, were termed "unrefunded" and were transferred from the HUTD Fund to DNR accounts. As motor fuel tax revenues increase in future years as a result of legislation increasing the tax rates enacted in 2008, the amount transferred to DNR accounts will correspondingly increase.

Based on information supplied by the American Petroleum Institute, seven states have gasoline tax rates higher than Minnesota. Some states have local option gas taxes and/or levy a statewide sales tax or other statewide tax (e.g., an oil franchise tax in Pennsylvania) on gasoline sales. If additional statewide taxes such as a sales tax are taken into account, nineteen states have higher gas tax rates than Minnesota.

MOTOR VEHICLE REGISTRATION TAXES

In FY 2010, motor vehicle registration taxes, after refunds, but before collection costs, yielded $532 million. Passenger class and pickup truck vehicles generated approximately 80% of total motor vehicle registration tax revenues.

MOTOR VEHICLE SALES TAX

The motor vehicle sales tax, a 6.5% tax on the sale of new and used motor vehicles, is partially dedicated to transportation. By 2012, all of this revenue will be dedicated to transportation, with 40% allocated to transit and 60% allocated to highways by state statute. In fiscal year 2010, 47.5% of this revenue was deposited in the HUTD Fund; this amounted to $217 million.

The phase-in schedule included in legislation passed in 2007 stated that 50.25% of revenues would be transferred to the HUTD Fund in fiscal year 2010 and 56.25% would be transferred in fiscal year 2011. The 2009 legislature reduced these percentages such that, 47.5% of this revenue was deposited in the HUTD Fund in fiscal year 2010 and 54.5% will be transferred in fiscal year 2011. This was done in order to increase the percentages transferred to the transit assistance fund. This could be done because the constitution provides that *at least 40%* of motor vehicle sales tax revenues are to be allocated to transit and *not more the 60%* of these revenues are to be allocated to the HUTD fund. The revenue to the HUTD fund in fiscal year 2011 is estimated to be $261 million.

FEDERAL HIGHWAY FUNDS

The level of federal funding is a critical issue for Mn/DOT and for local governments across the state, because federal funds make up a substantial portion of transportation spending. For the TH Fund, which is the principal funding source for Mn/DOT and which also provides significant funding for the Department of Public Safety, approximately $545 million (November 2010 forecast) of federal aid agreements are forecasted to be entered into in fiscal year 2011; this is about 34% of total revenue. It is higher than normal due to additional stimulus funds. In addition, a substantial amount of federal highway revenue is made available for local government projects. Typically this is more than

$100 million per year; $211 million was received for local government use in fiscal year 2010 (the large increase is also due to additional stimulus funds).

The current transportation authorization bill, SAFETEA-LU, expired in September 2009, but has been extended by Congress through March 4, 2011, the sixth such extension since it expired. The future federal funding situation remains very uncertain, with current proposals ranging from a new authorization bill to further extensions. The state trunk highway forecast has assumed that federal funding levels for FFY2012 will be maintained at that level into the future - this will require Congressional action to achieve.

HIGHWAY USER TAX DISTRIBUTIONS

The Minnesota Constitution provides that 95% of HUTD Fund revenues are distributed as follows: Trunk Highway (TH) fund - 62%; County State Aid Highway (CSAH) fund - 29%; and Municipal State Aid Streets (MSAS) fund - 9%. The remaining 5%, referred to as the five percent set-aside, is distributed in accordance with a formula established by the Legislature, but the formula may only be changed once every six years. This formula was most recently changed by the 1998 Legislature.

Since July 1, 1999, the five percent set-aside revenues, $77 million in FY2010, have been deposited in the CSAH Fund, where they have been further allocated to the Township Roads Account (30.5%), Township Bridges Account (16%), and Flexible Highway Account (53.5%).

FLEXIBLE HIGHWAY ACCOUNT

The Flexible Highway Account was created by the 1998 Legislature by combining money from the five percent set-aside that was previously allocated to the Trunk Highway Fund, the county turnback Account in the CSAH Fund, and the municipal turnback Account in the MSAS Fund.

According to changes made by the 2008 Legislature, the commissioner of transportation must recommend allocation of money in the Flexible Highway Account to the CSAH Fund, which includes allocations to metropolitan counties (except that the shares allocated to Hennepin and Ramsey counties do not include the population of the cities of the first class – Bloomington, Minneapolis, and St. Paul) from the “excess sum,” the county turnback account, the safety improvement account, and the routes of regional significance account; the MSAS Fund (municipal turnback account); and the Trunk Highway Fund (for trunk highways that will be restored and subsequently turned back by agreement to local governments) for each upcoming two-year period as part of the biennial budget proposal.

Since the distribution of money in the Flexible Highway Account is subject to decisions made in the biennial budget process, the relative amounts in the following table could be different in future biennia.

The following table describes allocations of the five percent set-aside for FY2010 through 2012, with the 2010 amount being an actual transfer, and the 2011 and 2012 amounts being the amounts that were included in the approved biennial budget:

5% Set-aside Distributions
($ in millions)

Fiscal Year	2010	2011	2012	2013
Town Road Account @ 30.5%	23.6	24.8	26.1	27.0
Town Bridge Account @ 16%	12.4	13.0	13.7	14.2
Subtotal Township Funding	35.9	37.8	39.8	41.1
Flexible Highway Account				
County Turn Back Account	41.3	33.5	44.2	45.8
Municipal Turn Back Account	-	10.0	1.6	1.6
Trunk Highway Fund	-	-	-	-
Subtotal Flexible Highway (53.5%)	41.3	43.5	45.8	47.3
Total Distributions of the Five Percent Set Aside	77.3	81.2	85.6	88.5

CSAH FUND AND MSAS FUND SPENDING

Money in these funds is allocated to all counties and to municipalities with populations greater than 5,000, based on statutorily defined apportionment formulas. The 2008 Legislature changed the process for allocation (formally termed apportionment) of this money to the CSAH Fund. Revenues derived from increases provided by the 2008 Legislature (e.g., increased gas tax rates) plus increased revenue from the percentages allocated to the Highway User Tax Distribution fund above 32% due to the phase-in of motor vehicle sales tax revenue as a constitutionally dedicated transportation revenue source are apportioned 60% based on money needs and 40% based on relative shares of the number of motor vehicle registrations in each county. For revenues not derived from increases provided by the 2008 Legislature, the apportionment is based on monetary needs (50%), relative shares of lane miles of roads (30%), relative shares of the number of motor vehicle registrations (10%), and equal shares to each of the 87 counties (10%). The allocation of money for the MSAS Fund was unchanged; the municipalities' respective shares are based on monetary needs (50%) and population (50%).

As a result of each decennial census, or as a result of the annual state demographer's estimate, additional municipalities may qualify for funding because their population grew beyond 5,000. At each census, some municipalities may stop qualifying for funding because their population fell below 5,000. As the decade progresses, additional municipalities may qualify for funding due to incorporation, consolidation, or by state demographer's estimate. Municipalities may also appeal their census counts.

Total number of municipalities qualifying for MSAS funds

	2005	2006	2007	2008	2009	2010
Number of cities:	138	138	142	143	144	147

BONDING

As of September 2010, the principal amount of outstanding trunk highway bonds totaled approximately $860 million, of which $394 million was authorized by Chapter 152 and the remainder by other laws. Approximately $337 million of interest must be paid on these bonds, for a total of approximately $1,198 million of outstanding debt service.

The total amount of trunk highway bond authorizations provided by the Legislature since 2000 is $2,485,288,000. From these authorizations, $938,450,000 of bonds have been issued. The most recent bond authorization occurred when the 2010 Legislature approved $100.1 million of trunk highway bonds and $26.445 million of trunk highway bonds for the Rochester headquarters building.

If Mn/DOT did not sell any additional bonds in the future, principal and interest on the ***outstanding*** trunk highway bonds for upcoming fiscal years are:

Debt service payments on outstanding trunk highway bonds ($ thousands)

	FY2011	FY2012	FY2013	FY2014
Principal	26,670	54,685	54,220	53,520
Interest	26,854	37,073	34,627	32,222
Total	53,524	91,758	88,847	85,742

This total repayment is reduced each fiscal year by the interest earned on the balances in the trunk highway account in the state debt service fund.

The total estimated debt service transfers from the Trunk Highway Fund is based on the currently known debt service (see above) plus estimates that are developed for planned bond sales in the future. The current estimate of these transfers is from the November 2010 forecast:

Scheduled debt service transfers from the trunk highway fund ($ thousands)

	FY2012	FY2013	FY2014
Estimated Amount:	$100,641	137,508	161,063

Source: November 2010 fund statement

The reason the estimated debt service expenditures are higher than the amounts shown in the Minnesota Management and Budget's official statement is that the fund statement reflects Mn/DOT's plans to sell significant amounts of additional bonds from the authorization provided by the 2008 Legislature. As estimates of cash flow expenditures from the $1.8 billion in additional bonding are refined, these estimates of debt service will change. In addition, any legislation enacted in the 2011 session will also result in changes.

Debt service is higher in the earlier years of repayment because the repayment schedules are based on retiring one-twentieth of the principal each year, unlike repayment requirements for a home mortgage, which are a fixed annual sum for combined principal and interest, with the amount of principal being repaid increasing each year.

ADVANCE CONSTRUCTION

Mn/DOT utilizes a type of federal financing called advance construction (AC). In general, this technique permits recognizing in the current year, federal revenues scheduled to be received in future years. This results in a number of benefits.

Even though the budgetary revenue is recognized, actual reimbursement (receipt of cash from FHWA) does not begin until the year the advanced construction agreements are "converted" to regular federal funds (the year the federal funds are actually made available through a federal appropriations act).

The cash balance in the trunk highway fund may sometimes be used to pay contractors before the project is converted and federal reimbursement received. Careful management of the use of AC has been adopted to avoid potential cash flow issues. Mn/DOT has developed and continues to refine advance construction and cash management techniques and policies.