November 30, 2012

Minnesota Transportation Finance Advisory Committee

Summary Report and Recommendations

INTRODUCTION

Governor Mark Dayton established Minnesota's Transportation Finance Advisory Committee in January 2012 to develop recommendations for the next 20 years to fund and finance the state's highways, roads, bridges and public transport systems, as well as its air, rail and port facilities. The ability of Minnesota's transportation systems to meet the needs of a growing population is one of the key measures of the state's business climate.

Investments in transportation will support an environment in which Minnesota businesses can continue to grow, ensure that the state continues to be an attractive location for companies looking to expand, and position Minnesota for the future.

Governor Dayton asked the committee to consider the implications of three future transportation scenarios for Minnesota:

- Status Quo — This scenario assumes no new funding or inflationary adjustments to the current funding stream.
- Maintaining Current Performance — This scenario assumes sufficient funding to maintain and operate the system in a condition equal to today, including existing service levels and condition ratings.
- Economically Competitive / World Class — This scenario assumes a greatly improved road surface and bridge condition, additional safety improvements, congestion reduction and some regional highway expansions, as well as significant transit and modal enhancements.

BACKGROUND

Minnesota is a great place to live, work, play, visit, start a business and raise a family, and the state's transportation system contributes to the overall quality of life and economic competitiveness.

To maintain what we have and position Minnesota for the future, we need to invest in and modernize our aging transportation infrastructure. We want a transportation system that will help Minnesota compete for jobs and talent. Doing so will provide opportunity for thousands of jobs – first in updating the infrastructure, then by attracting and keeping economic development in Minnesota.

The transportation system connects businesses to suppliers and customers around the nation and world. Minnesotans rely on the transportation system to get to their jobs and school, visit the doctor, enjoy the natural environment, shop, and take advantage of the amazing cultural, entertainment and recreational opportunities available in the Land of 10,000 Lakes. Both the state and the transportation system have great strengths as well as challenges.

PROCESS

To accomplish its charge, the committee developed a work plan for:

- Building common knowledge among committee members on transportation issues, including identified transportation needs, local issues, funding and financing possibilities, and national options and concerns;
- Identifying viable transportation funding and financing options for Minnesota; and
- Selecting the best possible options to develop into recommendations to the governor.

Initially, the committee received briefings on Minnesota's transportation systems and gained an understanding of issues and trends facing transportation, particularly those related to funding and financing. Additionally the committee received information related to Minnesota's national ranking in key size, performance and quality indicators for the various modes and systems. Plus, the committee was briefed on operations and maintenance of Minnesota's roadways and other transportation systems.

To identify the various options for recommendations, the members developed guiding principles that not only identified how the funds are generated, but how the generated funds would be allocated and spent. The committee then brainstormed 30 various options to fund and finance the gap identified. From these options the members crafted 13 transportation funding and financing recommendations to present to the governor on December 1, 2012.

CORE FUNDING AND FINANCING PRINCIPLES

The committee developed a set of beliefs on which to premise their recommendations. It was important to members that these principles provide a foundation for not only how the funds are generated, but also how these new revenues are allocated and spent. When the recommendations were completed, the committee did not recommend funding for 100 percent of the need identified; instead, it challenged all transportation providers and the state to address a portion of those needs by working more efficiently and effectively, being innovative in solutions and operations, and using technology to produce a higher quality product.

Additionally, the committee counseled MnDOT and the various transportation agencies to communicate to the public the results of their work and be accountable for meeting the 20-year needs.

The following principles, listed in no particular order, should guide the generation and allocation of transportation funds in Minnesota. The principles are intended to be used collectively.

Principles for the generation of transportation funds:

- Funding solutions must be fair and equitable – with consideration for regional, business and individual impacts.
- Funding solutions and recommendations must be long-term and sustainable.
- Transportation revenues must increase as the economy grows, whether through indexing or another type of system.
- User fees, such as the motor fuel tax, must be a part of the solution so people know what product or service they are purchasing.
- Funding solutions must embrace efficiency in the cost of collections.
- Revenue streams must recognize different needs of various geographies as well as various types of modes.
- Transportation funding sources should be specific in nature and target specific outcomes.
- Funding solutions must be marketable.
- Funding and financing options are responsive to changes in technology, demographics and the economy.

Principles for allocation and expenditure of transportation funds:

- Enhanced safety – The major goal of transportation investments is to maintain and enhance the safety of the public in all transportation systems.
- Economic efficiency and high return on investment – Transportation investments are guided by efficiency and transparency through the development of cost-effective and performance-based solutions.

- Fair and equitable – Multiple formulas for transportation investment may be used to balance the ability to meet the needs of Minnesotans.

- Economic development, prosperity, competitiveness and job growth – Transportation investments are critical to preserve and improve mobility and accessibility opportunities for Minnesota residents and business. This in turn helps create a stronger economy and job growth by allowing Minnesota to remain competitive, allow for business development options, and preserve our quality of life.

- Strategic investment, choice and options – Transportation systems are built to a maintainable scale with a variety of options/solutions for moving people and goods from one point to another in an efficient and effective manner. Broad-based revenue streams address different geographic needs around the state.

- Balance market and public roles – Transportation investment balances the public and private roles in developing our transportation system using the market, where appropriate, and using government, where appropriate.

- Cost sharing – There is recognition that all Minnesotans benefit from transportation investments and, therefore, share in some portion of addressing costs and minimizing burdens of a transportation system.

- Flexible and responsive – As transportation needs change based on technology, demographics and/or economic conditions, the investment in transportation needs to be flexible enough to address and meet these issues.

- Building and maintaining transportation systems – Funding options address both building new transportation systems and preserving existing transportation systems.

CONCLUSIONS

The committee was asked to define the problem as they saw it. Through a series of conversations, the members developed the following conclusions. They are:

- The transportation system in Minnesota creates a critically important, positive economic impact that provides a high quality of life for the citizens of our state. Funding for this system in the future faces declining revenues while the needs and costs keep increasing, creating a funding gap. If Minnesota wants to maintain its competitive advantage, significant additional revenue will be needed during the next 20 years to address this gap and provide an economically competitive, world-class transportation system here in Minnesota.

- To fully address this challenge, we will have to work smarter by doing more with the money we have. MnDOT, the Metropolitan Council, and other government entities addressing transportation needs, must continue and enhance the delivery of high return-on-investment strategies for project development and operations.

- The transportation funding gap predicted during the next 20 years must be addressed with a comprehensive funding and investment framework that is sustainable and equitable. (See table on page 13: *20-Year Funding Needs to Achieve Desired Outcome*.) Additionally, Minnesota needs a formula that blends a return-on-investment approach with a fair, predictable and sustainable method for supporting a variety of transportation options throughout the state.

- A partnership must be created between the private and public sectors to deliver a high-quality, competitive transportation system. Additionally this partnership may be needed to generate or help generate additional revenue that provides the infrastructure for economic success.

- “Economically Competitive / World Class” means a sustainable, globally competitive, technologically innovative system that provides the foundation for a sound economic environment and a high quality of life.

- In context of economic development and tax reform, and overall competitiveness of the state, investment in transportation should be a top priority for the state of Minnesota.

RECOMMENDATIONS

In order to remain competitive in the national and growing world economy and to continue to provide a high quality of life for Minnesotans in the coming decades, the Transportation Finance Advisory Committee recommends that the state of Minnesota pursue a goal to foster and develop an *Economically Competitive / World Class Transportation System*.

The TFAC recognizes that this is an ambitious goal that can only be achieved with a bold vision and commitment and with significant new financial resources which may be attained through a limited number of options.

In order to achieve this goal, the following funding and financing recommendations are offered for consideration by the governor in his 2014-15 biennial budget:

1. System-wide Revenue Options for Roads

Increase the motor vehicle registration fees to raise revenue by 10 percent through an adjustment in the multiplier, which will generate $1.1 billion in new revenue during the next 20 years for the Highway Users Tax Distribution Fund.

The registration fee for passenger class vehicles is determined by multiplying the vehicle base value by the tax rate of 1.25 percent plus $10. The base value depreciates by 10 percent every year for 10 years. The minimum tax for vehicles 11 years old and older is $35. (MS 168.013, Subd 1a)

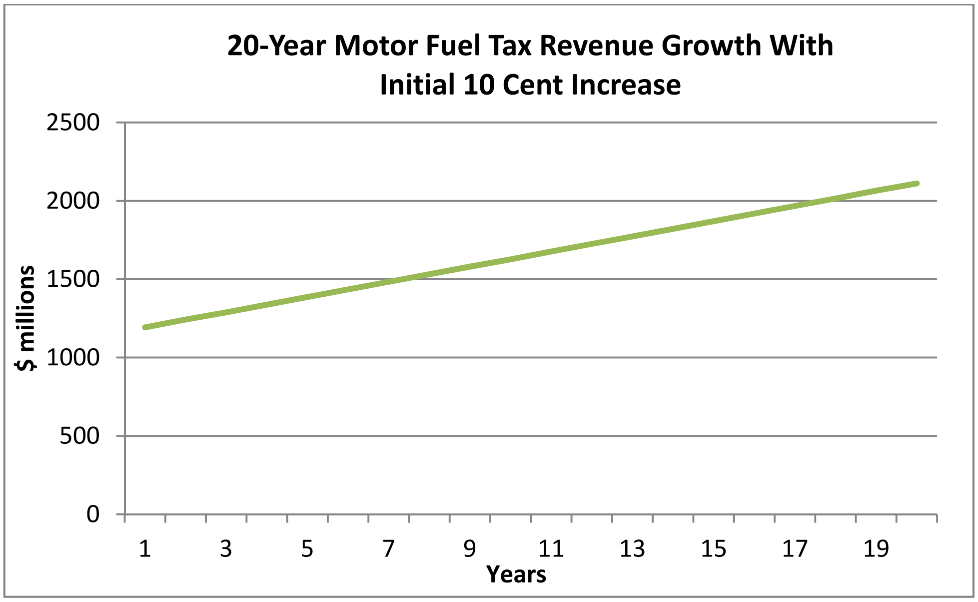
An overall increase of 10 percent in registration fee revenue could be achieved by adjusting either or both of the multipliers used to calculate annual vehicle registration fees. The depreciation rate used to determine the base value could be changed to an annual rate less than 10 percent or the 1.25 percent tax rate could be increased. This would leave the minimum tax unchanged at $35.

Rationale

- Cars are lasting longer while money collected decreases as the cars depreciate.
- Consider this as an ad valorem tax (or standard amount based on value) to keep pace/maintain value of funds collected.

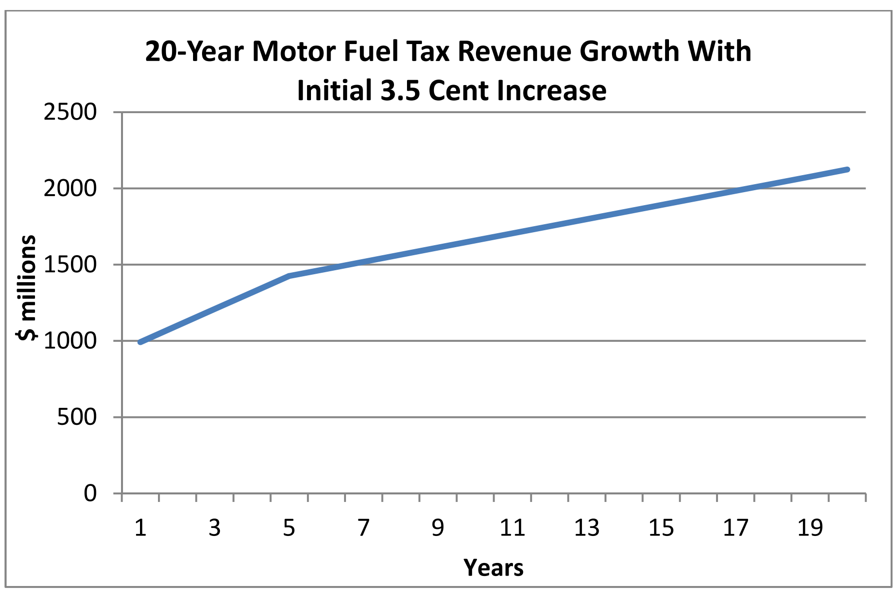
Increase per-gallon excise tax rate on motor-fuels to generate $15.2 billion in new revenue during the next 20 years for the Highway Users Tax Distribution Fund. This option can be achieved in many ways. The committee discussed the following two options in detail:

Option 1: Increase rate by $0.10 per gallon in the first year, with a subsequent phasing in of the excise tax rate at $.0156 per year for 19 years. This approach generates approximately $308 million of new revenue in the first year and total projected first-year revenue of $1.175 billion (adding to the SFY 2012 revenue baseline of $867 million).



(Assumes current vehicle mix and current levels of consumption.)

<u>Option 2</u>: Increase rate by $0.035 per gallon per year for the first five years and phase in the excise tax rate at $0.015 per year for the remaining 15 years. This approach generates approximately $108 million of new revenue in the first year and total projected first-year revenue of $975 million.



(Assumes current vehicle mix and current levels of consumption.)

Rationale

- Accentuates constitutional dedication of funds, sustainable, administratively simple and understandable

- Raises revenue for locals without another tax (62 percent to state, 29 percent to counties, and 9 percent to cities; note that 5 percent off the top goes to townships, state patrol, etc.)
- Phasing in of motor fuel tax increase addresses projected need and inflation
- Volatility and uncertainty in the federal program
- Less regressive than other fees
- Flexible phasing and indexing options are possible
- Amount collected through annual phasing in can keep pace, somewhat, with inflation
- Option 1 generates money early and provides consistency through the 20-year period
- Option 2 may be "easier to sell" but does not generate sufficient revenue until more than three years into the 20-year period

Outcomes Achieved by System-wide Revenue Options for Roads

- 83 percent of revenue target is met for the State Trunk Highway System - These measures together will generate $500 million per year on average.
- 52 percent of revenue target met for County State Aid System – These measures together will generate $235 million per year on average.
- 73 percent of revenue target met for Municipal State Aid System – These measures together will to generate $75 million per year on average.
- 80 percent of revenue target is met for the Township System – These measures together will generate $20 million per year on average.
- Expectation of efficiency gains over 20 years.
- Maintaining and enhancing infrastructure creates the opportunity for economic development, enhanced productivity, job formation and sustainable growth. (In 2012, the Federal Highway Administration estimated that 13 transportation and construction related jobs are created for each million dollars of investment.)
- Helps achieve greater productivity and economic development and opportunities for job creation.

2. Transit-Dedicated Sales Tax Options

Add $0.005 to the existing $0.0025 cent sales tax for transit in the Twin Cities metropolitan area (five counties), which is estimated to generate $200 million annually.

Direct $32 million annually to Greater Minnesota Transit to address statutory required service (71 percent of revenue gap for Greater Minnesota Transit over 20 years is $640 million).

Capture the remaining leased vehicle sales tax from the state general fund (estimated at $32 million annually) for transportation.

Rationale

The increased metropolitan area sales tax for transit:

- Recognizes the special transit needs in the Twin Cities metropolitan area
- Establishes a stronger relationship between who pays (including visitors and tourists) and who benefits from the proposed improvements
- Has significant revenue potential; is stable, predictable and inflation-proof; and is efficient to collect and administer because the tax collection and enforcement structure is already in place

Dedicating the remaining leased vehicle sales tax to Greater Minnesota Transit:

- Provides a dedicated, stable, increased source of funding
- Uses a source of funding that is already partially dedicated to transportation purposes, including Greater Minnesota Transit

Outcomes Achieved With Transit-Dedicated Sales Tax Options

The Twin Cities metropolitan area sales tax increase would:

- Provide sufficient funding to significantly expand the Twin Cities metropolitan transit system
- Improve the economic competitiveness of the Twin Cities, driving economic development and job growth
- Increase the region's competitiveness in seeking federal funds by solidifying the non-federal share of projects costs
- Allow the region to accelerate transit capital investments through bonding against the sales tax revenues independent of state or county bonding limitations
- Generate a high rate of return on investments, between $6 billion and $10 billion
- Reduce the state share of transitway capital and operating costs
- Encourage private investment by reducing uncertainty about future transit improvements
- 70 to 95 percent of the revenue gap is met under the Economic Competitiveness scenario for Twin Cities metropolitan area transit
- Maintaining and enhancing infrastructure creates the opportunity for economic development, enhanced productivity, job formation and sustainable growth. (In 2009, the American Public Transportation Association estimated that 30 transit and transit/construction-related jobs are created for each million dollars of investment.)

The increased revenue for Greater Minnesota Transit would:

- Help achieve the legislative goals for service in Greater Minnesota Transit
- Meet 71 percent of Greater Minnesota Transit needs
- Help achieve greater productivity and economic development and opportunities for job creation

3. Local Government Revenue Options

Expand the option of the wheelage tax for 80 counties in Greater Minnesota, including raising the cap limit for 87 counties.

Rationale

- Local needs addressed
- Gives locals opportunity to improve roads without adding to the property tax. Ability to locally manage funds for statewide impact (e.g., less congestion and road damage)

Enable the local option for the formation of Transportation Improvement Districts.

Rationale

- Provides an opportunity to raise local /regional revenues that can be used on high-priority local / regional needs

Enable local option sales taxes for transportation in 80 counties without the need of a referendum.

Rationale

- Provides increased capacity to locals and uses the County Transit Investment Board model, which has been highly effective in advancing Twin Cities metro area transit projects
- Addresses local road needs

Outcomes Achieved With Local Government Revenue Options

- Enhanced options and opportunities for project development and improvements
- Increased flexibility for counties to address local projects
- Additional jobs created

Expand regional transit capital levy (aka transit taxing district) in entire seven-county Twin Cities metropolitan area and use funds for capital and operating needs. Governance issues need to be considered.

4. Project-Level Revenue Options

Expand MnPASS System (which includes the concept of dynamic pricing) and dedicate revenue to multi-modal enhancements on managed lanes.

Rationale

- Provides added reliability for users of the system
- Provides additional funds and flexibility for MnPASS development
- Option of dedicated lane accelerates travel time between destinations, allows opportunity to "create time" because of efficient travel

Employ Value Capture concepts around transportation improvements.

Rationale

- Captures a percentage of value not otherwise realized from the development for transportation enhancement in an area through the use of development fees or other tools

Explore the following areas in more depth:

- Tolling options targeted for new capacity
- Public-private partnerships opportunities for enhancement and financial leveraging of transportation projects
- Monetizing assets to generate revenue

Rationale

- Current state law only allows tolling of new capacity
- Tolling with partnerships may advance projects sooner

Outcomes Achieved With Project Level Revenue Options

- Accelerated MnPASS expansion and associated transit benefits
- Enhanced options and opportunities for project development and improvements
- Additional jobs created

Continue state role in bonding for local roads and bridges, transit, ports, passenger rail, freight rail, safe routes to school (General Obligation Bonding).

Rationale

- Continues historic state role in support of local transportation facilities development

Outcomes Achieved

- Allows flexibility to meet needs not otherwise provided for
- Provides a buffer to local needs not otherwise provided for

20-Year Funding Needs to Achieve Desired Outcome ($billions)

	Scenario 1	Scenario 2	Scenario 3
System/Mode **(Includes funding for bikes and pedestrian needs associated with highway projects)**	**Anticipated transportation revenue for the next 20 years: Baseline**	**Increment added to baseline to maintain current performance for the next 20 years**	**Increment added to baseline to become economically competitive/world class system for the next 20 years**
State Highway System*	$18.0	$5.0 $250 mil Annual Funding Gap: AFG	$10.0 - 12.0 $500 mil.- $600 mil AFG
County State Aid System *County System*	$5.0 TBD	$3.0 $150 mil AFG $4.0 $200 mil AFG	$9.0 $450 mil AFG $9.0 $450 mil AFG
Township Roads		$0.3	$0.5
Municipal State Aid System *Municipal System*	$1.6 TBD	$1.0 $50 mil AFG $5.0 $250 mil AFG	$2.0 $100 mil AFG $8.0 $400 mil AFG
Greater Minnesota Transit	$1.9	$0.2 $10 mil AFG	$0.9 $45 mil AFG
Metropolitan Area Transit	$8.5	$1.8 $90 mil AFG	$4.2 - $5.7 $210-$285 mil AFG
Passenger Rail	$0.1	—	$5.0 - 7.0 $250-$350 mil AFG
Freight - Rail and Ports	$0.3	$0.3 $15 mil AFG	$0.6 $30 mil AFG
State Airports (Not MAC System)	$1.4	$0.6 $30 mil AFG	$0.8 $40 mil AFG
Metropolitan Airports Commission(MSP and Reliever airports)	$2.5	$0.0	$0.6
Totals	**$39.3**	**$21.2**	**$50.6 - $56.1**

IN CLOSING

The Transportation Finance Advisory Committee recommends that the state of Minnesota pursue the *Economically Competitive / World Class Transportation System* option in order to repair and modernize our transportation infrastructure.

In addition to helping Minnesota compete economically for jobs and talent, an Economically Competitive/ World Class system will enhance our high quality of life by connecting people to everything that matters -- jobs, education, healthcare, entertainment, shopping and recreation and more.

We are seeking a statewide high-performing, efficient and reliable transportation system that is maintained at optimal levels, funded and financed through sustainable means, enhances our quality of life and supports a vibrant economic climate.

It will move Minnesota in a smart direction.