



Blue Ribbon
Committee
on Highway Finance

BlueRibbonHighways.com

INTERIM STUDY OF HIGHWAY FINANCE

July 1, 2010

Presented to:

The Honorable Mike Beebe, Governor
House Interim Committee on Public Transportation
Senate Interim Committee on Transportation, Technology and Legislative Affairs
House Interim Committee on Revenue and Taxation
Senate Interim Committee on Revenue and Taxation
Arkansas Legislative Council
Arkansas State Highway Commission
Association of Arkansas Counties
Arkansas Municipal League

ARKANSAS GENERAL ASSEMBLY

Senator John Paul Capps
Chairman



Representative Allen Maxwell
Vice-Chairman

BLUE RIBBON COMMITTEE ON HIGHWAY FINANCE

July 1, 2010

Act 374 of 2009 created the Blue Ribbon Committee on Highway Finance and charged that it define an equitable and adequate system to properly finance improvements to Arkansas's system of state highways, county roads, and city streets; to actively involve the public as full and valued partners; and to recommend legislation to the Arkansas General Assembly for consideration in the 2011 Regular Session.

The legislation requires the Committee to submit a report by July 1, 2010. The Committee submits this interim report, "Interim Study of Highway Finance", which briefly conveys its findings, to date, the objectives towards which its ultimate recommendations will be directed, the work that has been completed, and the work the Committee has remaining.

This interim report is the result of several months of work by members of the Committee, its New Revenue and Revenue Transfer Subcommittees, and its Stakeholders Task Force. Many dedicated agency personnel and concerned citizens participated in the hearings and provided testimony, recommendations, advice, and information to the Committee. Five (5) public hearings were held across the state for the purpose of obtaining input from the public in fulfilling the Committee's charge. More than 200 people attended these meetings.

The Committee will present a full and complete report on or before December 1, 2010, as it feels strongly that extra time is necessary to fully and completely discharge the important task set out in the enabling legislation.

Respectfully submitted,

A handwritten signature in blue ink that reads "John Paul Capps".

John Paul Capps, Chairman

BLUE RIBBON COMMITTEE ON HIGHWAY FINANCE

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Representative Allen Maxwell, Vice Chairman
Senator Paul Miller
Senator Gilbert Baker
Representative Bruce Maloch
Representative Bill Sample
Representative John Lowery *

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Mr. Jim McKenzie **
Mr. David Malone
Mr. Madison Murphy
Mayor Tab Townsell
Mr. Mike Wilson

Stakeholders Task Force Members

Mr. Paul Benham, III
Mr. Johnnie Bolin
Mr. Greg Carman
Mr. Al Heringer, IV
Mr. Dennis Teague
Mr. Steve Williams

* Revenue Transfer Subcommittee Chairman

** New Revenue Subcommittee Chairman

INTRODUCTION

The following is an Interim Report of the Blue Ribbon Committee on Highway Finance. The work to date of the Committee is in direct response to the Committee's purpose to define an equitable and adequate system that will properly finance improvements to Arkansas's system of state highways, county roads and city streets; to actively involve the public as full and valued partners, and to recommend legislation to the Arkansas General Assembly for consideration in the 2011 Regular Session.

Since its establishment by Act 374 of 2009, the Committee and its colleagues on the Stakeholders Task Force have discussed proposals, reports, concepts, testimony and comment from a number of sources. As part of the Committee's charge to involve the public as valued partners, five (5) public meetings in the form of focus-group discussions were held during May, 2010. The locations of the meetings were North Little Rock, Hot Springs, Fort Smith, Jonesboro and El Dorado. Comments in the public focus groups were from among those responsible for the planning, construction, maintenance and funding of state highways, county roads and city streets; local and regional transportation experts; state and local political, business and civic leaders; legal counsel; finance experts; representatives from transportation industry-related associations; economic developers; tourism officials; general road and highway users, and the public at large.

Specific testimony at Committee meetings has been received from the Arkansas State Highway and Transportation Department, the Arkansas Municipal League, the Arkansas Association of Counties, the Federal Highway Administration, Council of State Governments, Legislative Council staff, and the Texas Transportation Institute. In addition, the Committee reviewed a number of formal reports on the state of transportation funding in Arkansas and around the nation.

To help facilitate public access to Committee activity and documents, promote information related to transportation infrastructure, and solicit public input, a Committee-sponsored website was established and publicized. The domain is www.BlueRibbonHighways.com. A brief video presentation was produced explaining the responsibility of the Committee and that responsibility's association with fact-based background on traditional highway finance and its ability or inability to fund present and future needs. The video was played as an introduction to each public focus-group discussion and continues to be offered for viewing on the Committee website.

In order to facilitate its own work, the Committee divided itself into two (2) subcommittees. The subcommittees, the Revenue Transfer Subcommittee and the New Revenue Subcommittee, conducted independent research into various revenue alternatives. Both Subcommittees made reports to the full Committee. The reports are available on the Committee website. The Subcommittee recommendations have been discussed, but have not been fully debated by the Committee, and no final Committee action on Subcommittee deliberations or preliminary recommendations had been taken at the time of this report.

In response to Chairman Capps' invitation to members to submit written ideas, options or proposals, the Committee also received, on June 16, a document titled, "Possible

Options for Generating Additional Revenue for Highways, Roads, and Streets". The discussion paper, offered by Committee member R. Madison Murphy, included five (5) options, one of which attempts to assimilate concepts from both the New Revenue and Revenue Transfer Subcommittees. The options were taken under advisement by the Committee. The discussion paper is posted on the Committee website.

INTERIM POSITION STATEMENT

Although the Committee noted the Arkansas State Highway and Transportation Department (AHTD) is ranked second lowest in the nation in administrative cost per mile (\$1,888 compared to the 2009 national average of \$8,801), resulting in the AHTD putting as much revenue into construction and maintenance as possible, the comprehensive deliberations of the Committee, nevertheless, have revealed an overriding structural problem in the funding methodology. This systemic failure of current financing has made clear to the Committee that the traditional approach to highway, road, street and bridge maintenance and construction is, in its present form, no longer sustainable when measured against a changing economic and technological environment, erosion of purchasing power, and continuing escalation of costs. Consequently, the Committee will require additional input, research and study in order to propose meaningful and relevant recommendations, thus accomplishing the Committee's mandate to define an equitable and adequate system for future, sustainable highway funding.

It is currently the plan of the Committee to provide final recommendations on or before December 1, 2010.

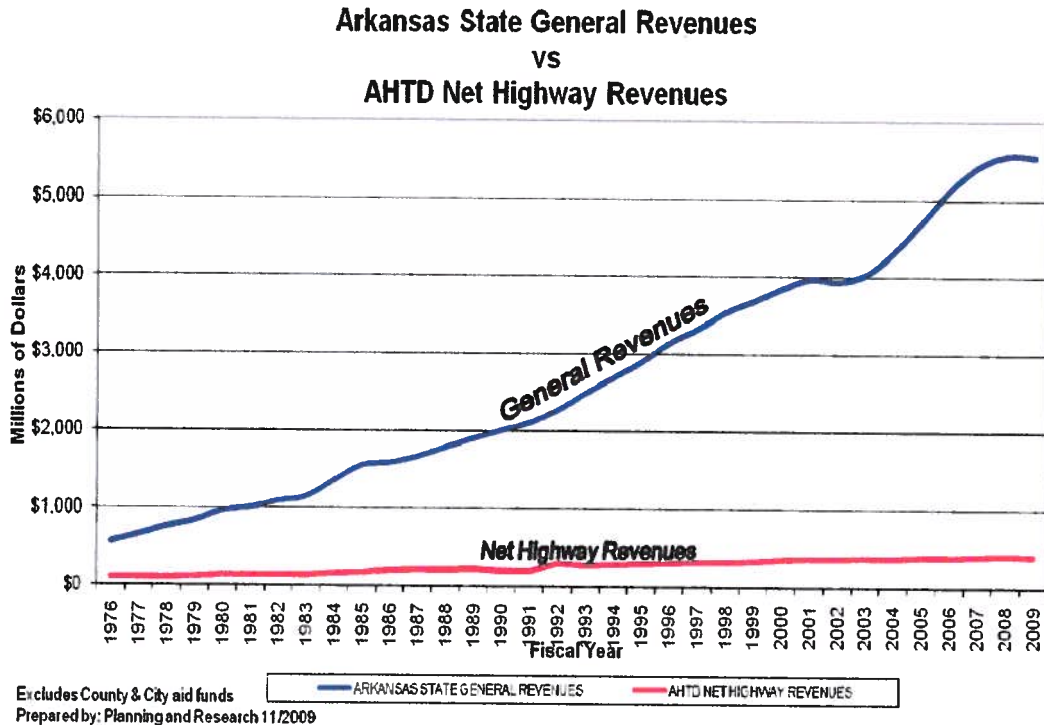
STRUCTURAL PROBLEM

Illustrative of the Committee's findings is the structural problem inherent in the current funding methodology. The Committee considered, among others, four (4) key examples of the structure's failings: the gap between general revenue represented by a five-year average growth in state tax collections, compared to revenue for highways during the same period; the increase in the Arkansas Highway Construction Cost Index, and examples of the erosion in purchasing power of the "highway dollar"; waning motor fuel consumption, resulting in the reduction of motor fuel tax collections, the funding from which makes up over 70% of total highway revenue; and the inconsistency between the state's population and the size of state and county road systems that must or should be maintained.

Revenue Gap

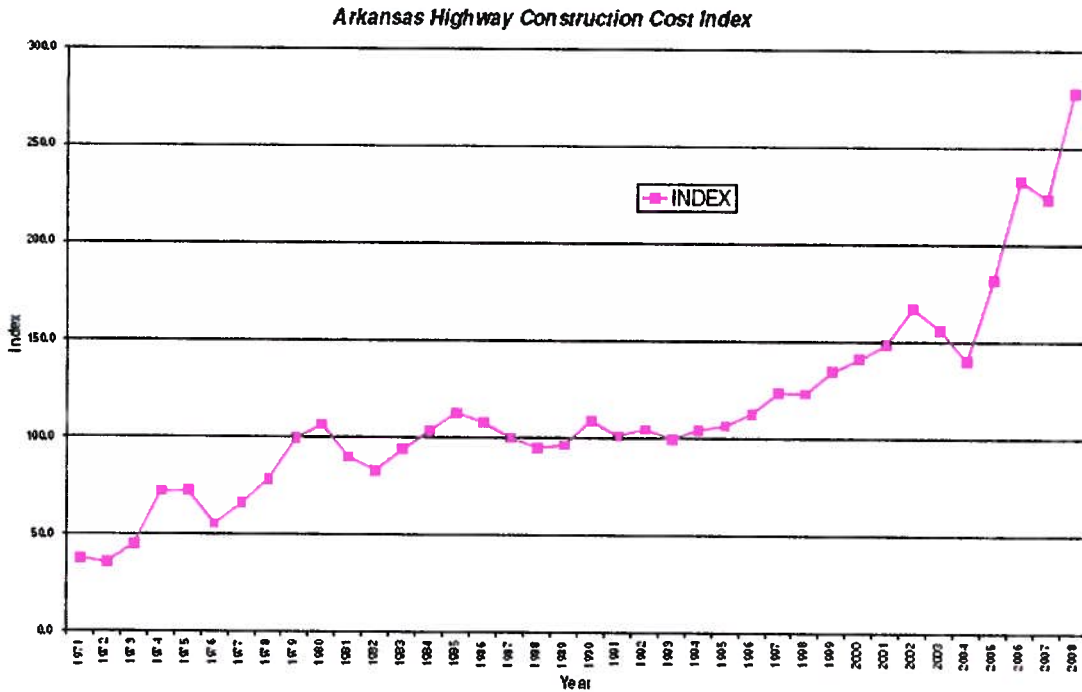
Arkansas general revenue has, for the past 30-plus years, consistently increased. The chart below shows year-over-year increases – an average of 6.6% annual growth over the most recent five-year period – as the tax base broadens and our state continues to grow.

Gross highway revenues, however, have remained relatively flat, inching up an average of 1.4% during the same most recent five-year period. Any highway revenue growth has generally been the result of increased taxes and fees, rather than natural growth due to increased consumption of motor fuels, which is the backbone of the financing system.



Purchasing Power

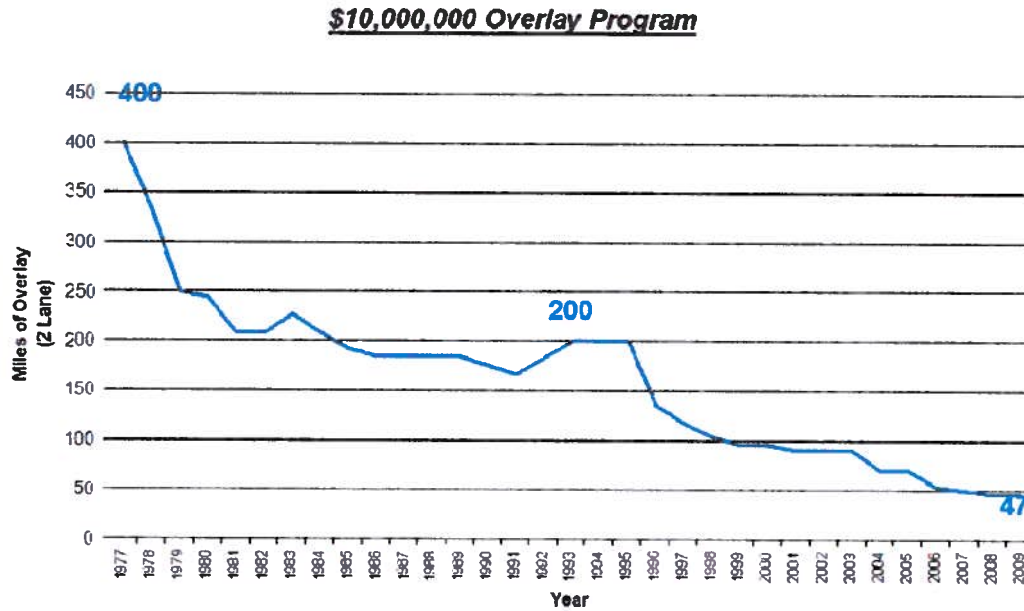
The Arkansas Highway Construction Cost Index, or the recognized measurement of construction costs specific to Arkansas, is reflected in the following chart.



The Committee recognizes the growth in funding and the cost of maintenance and construction are mismatched, with costs consistently increasing, while funding from the current system of fuel taxes and registration fees lags.

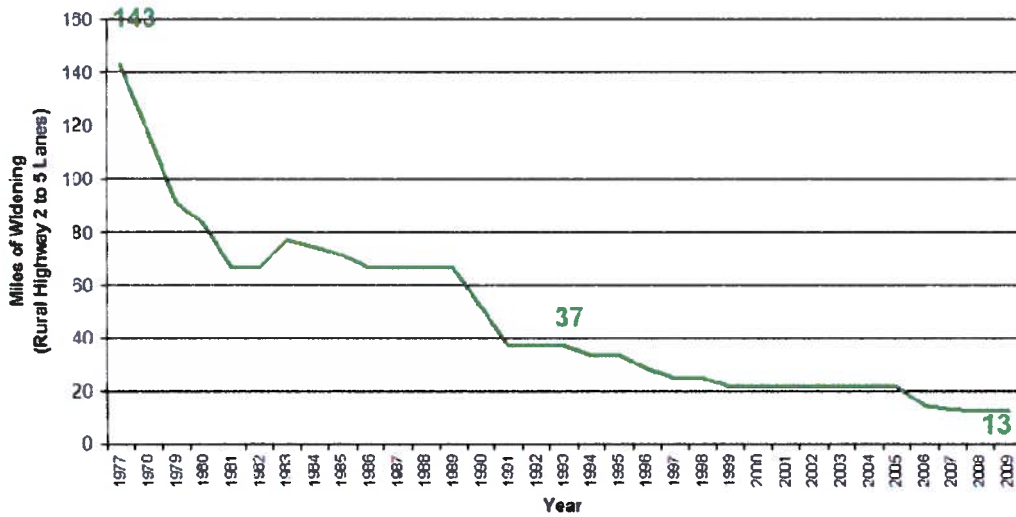
A clear result of the inequality between cost and revenue can be seen in the following erosion of the purchasing power of the "highway dollar":

- \$10 million overlay program resurfaced...
 - 400 miles in 1977;
 - 167 miles in 1991, and
 - 47 miles in 2009. (47 miles represent 12% of the mileage resurfaced in 1977 and 28% of the mileage resurfaced in 1991.)



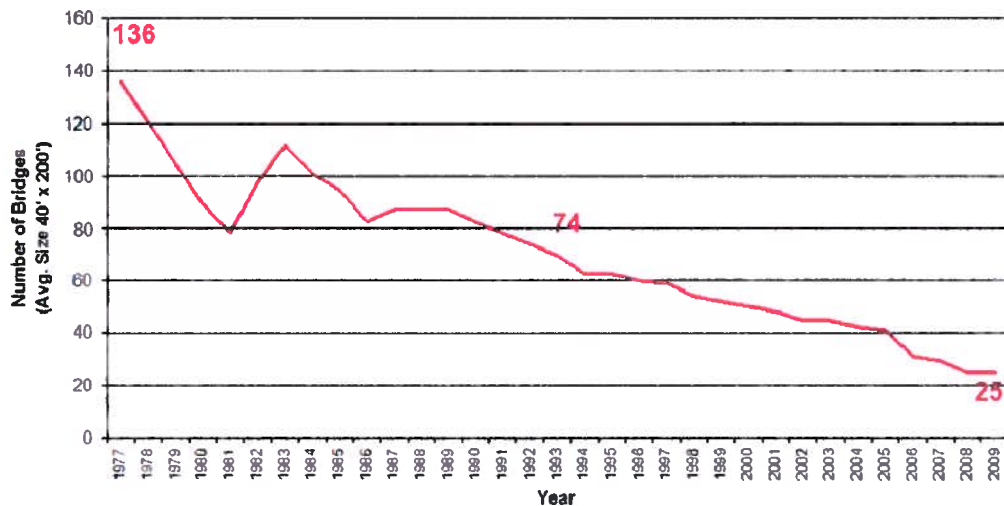
- \$100 million widening program improved...
 - 143 miles in 1977;
 - 37 miles in 1991, and
 - 13 miles in 2009. (13 miles represent 9% of the mileage widened in 1977 and 35% of the mileage widened in 1991.)

\$100,000,000 Widening Program



- \$25 million bridge program rehabilitated or reconstructed...
 - 136 bridges in 1977;
 - 78 bridges in 1991, and
 - 25 bridges in 2009. (25 bridges represent 18% of the number of bridges rehabilitated or replaced in 1977 and 32% of the bridges rehabilitated or replaced in 1991.)

\$25,000,000 Bridge Program



Fuel Consumption

As the Committee was informed of the fact consumption trends and trends in highway revenue mirrored one another, it became obvious that over 70% of the financing methodology was systemically flawed.

- Fuel consumption decreased 2.7% from fiscal year 2008 to fiscal year 2009.
- Fuel-tax revenue decreased 3.3% from fiscal year 2008 to fiscal year 2009.
- Total highway revenues decreased 1.5% from fiscal year 2008 to fiscal year 2009.

The long-term trend of reduced consumption will be exacerbated by the increase in CAFÉ standards (federally mandated miles per gallon fuel efficiency), when an average of 35 miles per gallon (MPG) is required by 2016. The new standard, for the first time, will include light trucks. After 2016, heavy trucks will be included in the MPG standards, with a federal goal of complete electrification of the light duty fleet (cars) by 2050.

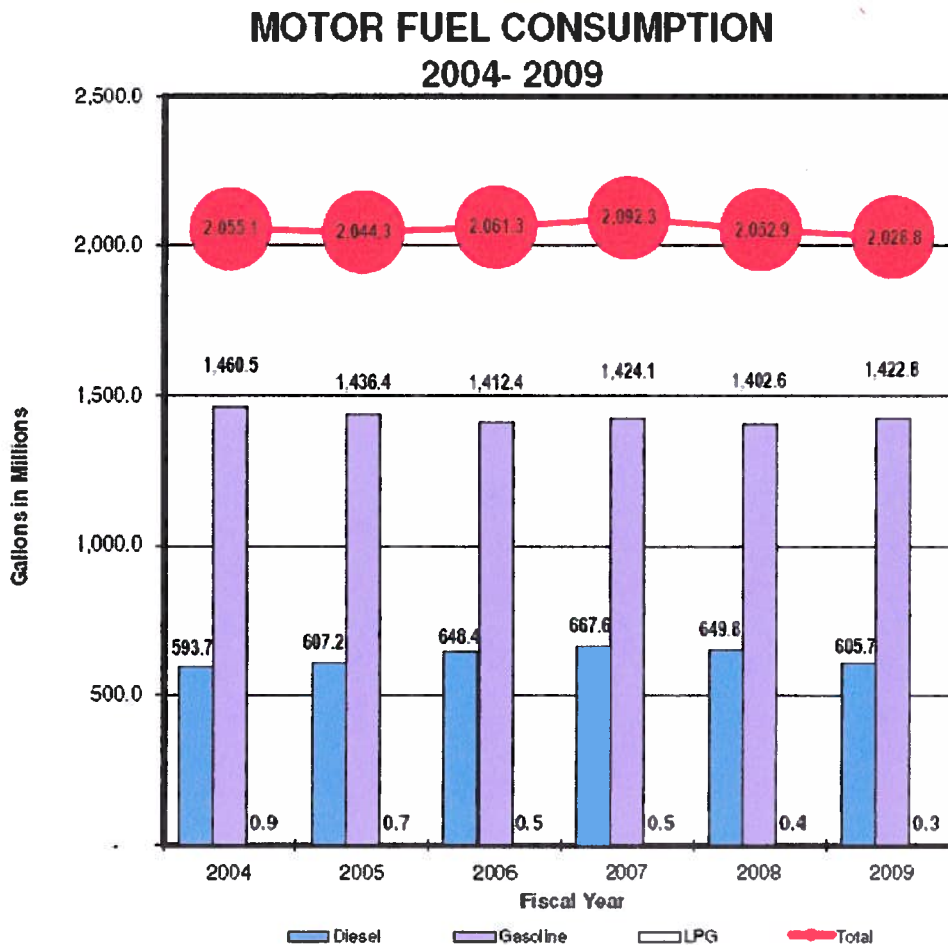


Chart prepared 6/30/2010

Rural State Anomaly

In addition to the discovery of a road, street and highway funding methodology that no longer meets the needs of a growing state, Arkansas must be included in what can only be termed an anomaly applied to rural states. This inconsistency between the population of a state and a state's system of public roadways, places an inequitable burden on road-user taxpayers.

In Arkansas's case, the state system includes 16,443 miles of highways. It is the 12th largest state highway system in the United States, comprising 16% of our public roadways and carrying 76% of Arkansas's total annual vehicle miles traveled, including 97% of all heavy-truck travel. There are 66,811 miles of county roads in Arkansas, making the county road system the 10th largest in the country, carrying 9% of the state's traffic. The balance is comprised of 14,778 miles of city streets, which carry 15% of the total annual traffic volume.

The anomaly is revealed when we are reminded the state's population of approximately 2.7 million ranks 32nd in the nation, yet we have the 12th largest state highway system and the 10th largest county road system. The result is, each Arkansas driver supports a larger number of road miles than in more populous states. Although the inconsistency is not uncommon for many rural states, this fact does not make the Committee's task of defining an equitable and adequate funding formula any less daunting.

- Arkansas's population ranks 32nd in the nation.
- Arkansas's state highway system ranks 12th in the nation.
- Arkansas's county road system ranks 10th in the nation.

Defective Formula

The current formula of adequate public roadway funding in Arkansas has, heretofore, been relatively successful because of four (4) basic factors:

- Vehicle miles traveled have continually increased.
- Motor fuel has been relatively inexpensive.
- Motor vehicle fuel efficiency has not dramatically improved.
- Highway revenues have kept relatively close to the Arkansas Highway Construction Cost Index.

Each of those factors has changed in the first decade of the 21st Century, rendering the formula defective. (And those changes are likely to be permanent.) The consequence is, the system of funding Arkansas's highways, roads and streets, fueled by the rapid increase in auto ownership and use over the past 50 years, will not be sustainable in the near term nor the long term.

One notable part of the previously successful formula, outlined above, is relatively inexpensive fuel. This fact has been aided by low gas taxes, when adjusted for inflation. In 1955, Arkansas's per gallon motor fuel tax was 6.5¢. Today's gas tax is 21.8¢. However, if adjusted for inflation, the gas tax today would be 52.6¢ per gallon and funding for Arkansas's roads and highways would be greater. The Committee is reminded, as previously learned, per gallon consumption is trending downward. There has been no realistic Committee discussion, nor is there likely to be, to bring the gas tax to inflation-correcting levels. To do so, it has been noted in public comment, would continue to rely on a methodology that is subject to a law of diminishing returns.

OBJECTIVES

The full and unfettered considerations by the Committee, the Stakeholders Task Force, and the Committee's Subcommittees, have manifested themselves in four (4) broad objectives. These objectives will provide the Committee with a guide when making further requests for and consideration of additional input, research and study, in order to make subsequent recommendations.

(NOTE: The objectives have not been prioritized. Consequently, the list below is arranged in no particular order.)

- To protect from further erosion the existing tax base of highway, road, street and bridge funding
- To restore construction and maintenance purchasing power
- To preserve, maintain and enhance the safety of existing state and local systems
- To add new capacity to state and local systems

The Committee may also determine the framework in which recommendations designed to meet these objectives will be made; how the recommendations relate to various maintenance and construction plans, and the possibility of requiring approval by the general electorate of legislative action on new and/or restructured financing methodologies.

OPTIONS FOR FURTHER CONSIDERATION

As the Committee continues to debate a wide variety of options that could provide a collaborative method to sustain, in the decades ahead, equitable and adequate funding, there is no debate on the inability of the current funding system to provide the necessary resources for effective transportation infrastructure going forward. Now recognizing the dilemma, the choice of the Committee is to require additional information and study based on the deliberations of the Subcommittees, input from Committee testimony, and the comments received from interested citizens.

This report would not be complete if the Committee did not cause to be listed here as many of the viable funding options as possible. It should be noted, these options are in no particular order of importance or priority, nor are they mutually exclusive. They are to be taken, however, as a menu of possibilities requiring further study; understanding the Committee's additional work will adhere to the stated purpose of defining an equitable and adequate – a fair and sufficient – system to properly finance improvements to Arkansas's highways, county roads, city streets and the bridges that connect them.

Options

- Analysis of vehicle license and registration fee revenue, including like fees in surrounding states
- Indexing motor fuel excise taxes to the Arkansas Highway Construction Cost Index three-year trailing average
- Review of existing GARVEE bonds, the Interstate Rehabilitation Program, and the implementation of the next proposed program
- Analysis of a 5-, 10- and 15-year bonding authority for system preservation, congestion relief, and/or new capacity
- Analysis of the Federal Highway Administration Cost Allocation Study on the evaluation of highway-related costs attributable to different vehicle classes, and the extent to which user fees paid by different vehicles cover their highway cost responsibility *(Note: The study has not yet been released by the Federal Highway Administration. The study's release is expected during the summer.)*
- A bond issue to be retired by a one-half-cent (1/2¢) general sales tax; sales tax to sunset upon retirement of the bonds, at the end of 10 years, or sooner; proposal submitted to the general electorate for approval
- Levy of a new excise tax on the wholesale price of motor fuels; levy to be phased in over a time period to be determined
- Removal of the current sales tax exemption on motor fuels

- Levy of a special sales tax in addition to the existing sales tax on new and used vehicles and dedicating the revenue to the highway fund
- Transfer of existing road-user-related sales taxes – new and used vehicles, auto repair parts and services, tires and batteries – phased in from general revenues to the highway fund over a period ranging from 4-10 years
- Study of “triggers” as they may relate to the implementation and/or use of revenue sources, including revenue transfers over time
- Maintaining the traditional split of highway revenue among the state, cities and counties consistent with the 70%-15%-15% formula
- Analysis and projection of the status of the Federal Highway Trust Fund, including Congressional re-authorization of SAFETEA-LU, the current federal surface transportation law, and/or short-term continuing resolutions of SAFETEA-LU and available federal revenue
- Long-term, future study of a Vehicle Miles Traveled (VMT) tax concept based on federally mandated fleet fuel efficiency, resulting fuel consumption and the future impact on motor fuel revenue
- Analysis and projection on the timing of implementation and use of revenue generated from the Streamlined Sales Tax
- Study of local partnerships, regional authorities and local-option revenues
- Review of the current State Aid for Counties program and its structural application to a like program for city aid
- Review of statutory and constitutional law relative to legislative referrals of financing structures to the general electorate for approval, including, but not limited to, an initiated act

Upon the timely review, study, evaluation, consideration and analysis of the above options, the Committee will prepare and submit a final report, along with its recommendations for proposed legislation, to the Governor; House Committee on Public Transportation; Senate Committee on Transportation, Technology, and Legislative Affairs; House Committee on Revenue and Taxation; Senate Committee on Revenue and Taxation; Arkansas Legislative Council; Arkansas Highway Commission; Association of Arkansas Counties, and Arkansas Municipal League.

A copy of this interim report will be posted on the Committee website at www.BlueRibbonHighways.com.