Sources of Revenue for Local Transportation: What Are the Potentials and the Impediments?

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INTRODUCTION

State and local governments spent more than $45 billion to improve the nation’s transportation system last year. The federal government alone spent $25.1 billion in 1984. Even with this tremendous scale of expenditures, most people involved in planning and implementing transportation—whether highway or transit, provider or planner, administrator or technician—are faced with budget constraints that limit their ability to meet transportation needs. The task is not to decry the lack of resources or revenue, but to participate in a process of examination, thought, and creativity for effective use of current sources and creative application of new sources. Many of the old formulas do not apply today.

For the last 20 years, transportation has relied on several main revenue sources. These typically varied by the type of transportation facility or service. They include

- Highway financing
  - Federal (with small local match)
  - State motor fuel and vehicle taxes
  - Tolls
- Transit financing
  - Federal (capital and operating grants)
  - Fares
  - Local government general revenues

Many states, cities, and transit systems developed alternative revenue sources, and these have become familiar to those interested in transportation—sales tax, private participation in financing, new debt instruments, contracting arrangements, donations, lotteries, and benefit assessment districts.

Examples of these new revenue sources are many and are found in almost every region of the country. In highway financing, many states have created legislation allowing cities and counties to pass local-option motor fuel taxes. The states include New York, Alabama, South Dakota, and Oregon. In fiscal year 1982-1983, Dade County, Florida, collected $28 million from this source. The use of tolls to finance improvements is an old revenue source with new applications. The Dallas North Tollway was completed in 1968 and will be extended in 1986. In Tampa, Florida, an additional 12.3 miles has been added to the initial 5.2-mile South Crosstown Expressway. Private development-related measures vary widely, but typically use funds or land from private developers for financing part of the facility improvement. In Newport Beach, California, four developers funded 14 intersections for $1.7 million. In Palm Beach County, Florida, developers paid $1.6 million to widen a major east-west arterial.

Transit has experienced similar applications of new revenue sources. Private-sector involvement has included benefit assessment districts, various lease and sale agreements, donations, private service providers, merchant subsidies, and others.

In Madison, Wisconsin; Denver, Colorado; Los Angeles, California; Seattle, Washington; and other cities, transit improvements are being financed by property tax assessments on properties that benefit from the improvements. Tax-increment finance involves a similar principle by allowing cities to issue bonds against future increases in property values due to transit or other transportation improvements. Many of these revenue sources have been available for years, but were dismissed as politically unpalatable or because of a lack of staff capacity to implement the approach.

Dedicated taxes for transportation are gaining in popularity. Since 1981, 30 local governments have implemented a dedicated revenue source for transit from sales taxes, property taxes, and the now famous beer tax in Birmingham, Alabama. These are but a few examples of so-called new revenue sources for transportation planning. Which of these potential sources seem to enjoy the greatest popularity?

CURRENT TRENDS: WHO IS DOING WHAT?

The most significant sources of additional local revenues for transportation, both in dollar amounts and in the number of local entities considering the source, are the following:

- Tolls (highways)
- Motor fuel taxes (highways and transit)
- Sales tax (primarily transit)
- Beneficiary-based revenues (highway and transit)

Tolls

Toll financing has been used primarily for highway financing. It is a user fee imposed on those who use a transportation facility—road, bridge, tunnel, or highway. As the Interstate highway system is completed and major highway financing is turning its attention to maintenance and expansion, toll financing for new facilities may present additional opportunities for financing new facilities. Toll-road applications are of importance to the following types of facilities:

- High-speed, limited-access facilities
- Service in high-demand corridors, such as suburban to downtown
- Convenient bypass facilities to avoid major congested areas
- Immediate mobility improvements, when adequate state or local funding is not available within a reasonable period of time

There was extensive use of toll roads and facilities in the United States from 1940 to 1960. There are almost 5,000 miles of toll facilities in operation, with half these miles on the Interstate highway system. The 88 toll roads range from 1/10 of a mile to more than 50 miles. Bridges, ferries, and tunnels are also financed with tolls. Renewed interest in this source of revenue is primarily for use on commuter highways in urban areas.

Toll roads have some inherent advantages that have caused renewed interest in their use:
Motor fuel taxes are being used as a revenue source for transit and highway financing. These taxes are those taxes assessed locally that are in addition to traditional federal and state taxes. Local motor fuel taxes are used in 63 counties and 274 cities, and rates vary from 1 cent to 4 cents. As an alternative method, Indiana converted from a cents-per-gallon formula to a percentage formula, and New Mexico has indexed the tax to the average wholesale price of fuel.

The attraction of using motor fuel taxes to finance street and highway improvements is twofold: it already exists and is understood, and those who pay the tax are typically the ones who use the improvements. The fuel tax is similar to a sales tax and relates directly to the public good being financed.

The advantages of this source of revenue include:
- It provides a reliable stream of revenue.
- It has good revenue potential.
- It is a mechanism for collecting tax.
- It has high efficiency in collection.
- It is equitable for users of the system.

There are several disadvantages to this revenue source that may account for its lack of use:
- State legislatures are reluctant to share tax.
- There may be poor acceptance if the need is not clearly evident.
- The tax does not adjust with inflation if not indexed.
- It may produce border problems among local governments.

Sales Tax

A dedicated sales tax has been considered and debated by more local entities than any other local tax source, and is used primarily for transit financing. Since this tax is approved at the local level, the approval requires active participation of local residents and community leaders. It is seen as a benefit to the transit rider and automobile user, the latter through a perceived potential for traffic reduction.

The advantages of using a sales tax for transportation financing include:
- Produces large amounts of revenue
- Responds quickly to income changes and inflation
- More politically acceptable than other levies
- Administration not usually a problem, unless there are a large number of exemptions
- Administration, enforcement, and redistribution accomplished at the state level

There are several disadvantages to the use of sales tax:
- Revenues decline when consumer buying declines
- Strong competition from other public services to use this revenue source
- May encourage consumers to make purchases outside the taxing jurisdiction
- Tax is less related to transportation usage

Beneficiary-Based Revenues

Although tolls and other user-fee revenues are benefit based, they are tied to direct users of transportation. There are other beneficiaries of transportation improvements—property owners, developers, and investors. Beneficiary-based revenues refer to several value-capture techniques that seem to be gaining in popularity. These include:
- Joint development
- Benefit-assessment districts
- Tax-increment districts

Joint Development

Joint development has been used as a financing and development tool in both transit and highway development. Opportunities for direct private investment in public projects offer additional revenue potential. The number of ways in which this has occurred makes it difficult to categorize or analyze advantages or disadvantages. As in any business venture, the specifics of the project, the timing, location, individual participants, and other unique factors come into play.

In Miami, Florida, air rights were sold to developers, providing regular income based on gross income of the project. In Seattle, Washington, local businesses caused a local improvement district to be created to help finance $1.1 million of a streetcar line. In San Diego, California, two developers are paying $3.5 million for realignment and construction of a new bridge. Many cities have used privately provided funds for downtown transportation improvements in the recent surge of central business district revitalization.

An array of negotiated agreements exists for this revenue arena—donated resources, shared costs, leasing, and lease-purchase.

There are ample examples of approaches involving sector revenue:
- Washington, D.C., Metro Transit Authority’s joint-development approach to transit station development
- Merchant subsidy of transit services in Cedar Rapids, Iowa, and Champaign, Illinois
- Private donations in San Francisco, California, for overhauling the cable car system
- Privately funded marketing efforts by civic organizations for special shuttle service using rubber-tired cable cars in Fort Worth, Texas
The advantages of joint development in transportation projects include
- More rapid initiation and development of projects
- Controllable decision environment
- Flexibility in conceptualization of project
- Equity for participants in process
- Good and sufficient revenue potential

The advantages and disadvantages depend on the specific project. Possible disadvantages are
- Lack of skill levels needed for real estate and development considerations
- Uncertainty associated with some development projects
- Legal requirements requiring local or state legislation
- Potential for inefficient acquisition of resources—long negotiating period, potential for failure
- Unwarranted public participation in the development process

Benefit-Assessment Districts

These can be used to finance both transit and highway facilities. Road utility districts are authorized in Texas for property owners to build and finance roads with tax-exempt bonds. Special or benefit assessments are a way of recouping the benefit experienced by property owners, businesses, or others who receive some measurable financial benefit from development of a transportation facility. The implication is that increased access results in increased property value, increased sales, and other types of benefits. For the most part, benefit assessments are used for transit or roadway projects, involving revenue-producing properties, including commercial, industrial, and rental.

Benefit assessment occurs as a result of an opportunity for which these revenue sources are applicable and the process in which interested parties reach agreement. There must be a good opportunity and willing parties, and the persons or businesses most affected in an area must agree to the assessment process.

Traffic-impact fees charged to developers in Palm Beach County, Florida, and San Diego and Newport Beach, California, usually are based on projected effects of the proposed improvements by the developer. Benefit-assessment districts impose some form of tax on the businesses or property owners in the district. Assessment paving has been used for many years to provide residential street improvements, and application of this approach is possible in other situations.

Transit facilities in Denver, Colorado; New York, New York; Los Angeles, California; Madison, Wisconsin; Miami, Florida; and Seattle, Washington, have used benefit-assessment revenue as a means of financing transit improvements. The revenue is being used in various ways—capital improvements, operating funds, and maintenance. The impetus for this revenue source at times originates and is encouraged by private-sector beneficiaries, and an important feature is the intentional and necessary involvement of the private sector in the process. It is almost impossible to approve an assessment district without this effort.

Many other forms of beneficiary revenue exist and can be applied where the opportunity exists. This includes transit, street, or highway improvements. Donations of rights-of-way or property are typical examples. The state of Texas has made this important when setting priorities for highway construction. In Newport Beach, California, a developer donated land for a transit center and funds for operating a shuttle service.

The advantages of benefit assessment include
- Equitable for property owners who benefit from facility or improvements
- Limited number of participants who need to favor the approach
- Good potential revenue source; can be designed to match need
- Flexibility in application through adjustment of assessment formulas
- Can be used to leverage expenditure of other funds
- Provides stable income source
- Can be used for a variety of expenditures—capital, operation, and maintenance

Special assessment districts apply to particular projects and have various disadvantages:
- Typically, assessments do not adjust with inflation
- Administration for a single project may be complex
- Requires state legislation
- Depends heavily on agreement of property owners and others who will pay the assessment
- Relies on specific opportunities, matched with specific transit or transportation improvements

Benefit assessment offers a useful implementation tool for producing needed revenues.

Tax-Increment Districts

Tax-increment districts are beneficiary-based forms of financing that rely on the impact of public improvements to increase property values sufficiently to retire bonds issued by a local authority. They have not been used extensively with transit or transportation improvements, however. Beaverton, Oregon, is an example of a successfully completed project involving transit, street, and other improvements to a blighted area of downtown. Embarcadero Station in San Francisco, California, is another good example.

TRADITIONAL REVENUE SOURCES

These suggestions are not intended to sidetrack consideration from traditional funding sources, but to supplement them and expand the view. The traditional sources will continue to be essential. Some questions arise, however. What form will these sources take? How will the federal role change? Will there be a shift in the way transportation funds are distributed, and what impact would this have?

CONCLUSION

National trends are not as important as determining what will work in a particular community, and each of the various revenue sources should be examined in light of local circumstances. Some questions for which answers may be found are as follows:

- What are the potential and possible problems with each of these revenue sources?
- What are the potential yields of using the various sources of revenues, and what are the costs of collection and enforcement?
- What are the legal, political, and institutional impediments to using these revenue sources?
- What are the economic and social impacts of using these sources of revenues, what are the equity considerations of who pays versus who benefits, and how are the potential losers compensated?
- How do institutional structures, for instance, special districts, affect the election of revenue sources?
- Does the purpose for which the additional revenues will be used—capital versus maintenance and operations—make a difference in the revenue source?