White Paper:
FISCAL CONSTRAINT – OR FISCAL RESTRAINT?
ISSUES OF COMPLIANCE WITH FEDERAL REQUIREMENTS FOR STIPs, TIPs AND LONG RANGE PLANS

PREPARED FOR:
MEETING FEDERAL SURFACE TRANSPORTATION REQUIREMENTS IN STATEWIDE AND METROPOLITAN TRANSPORTATION PLANNING: A CONFERENCE

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INTRODUCTION

In the transportation community, it is generally agreed that ISTEA ushered in a new era in terms of how the Nation’s State and metropolitan areas plan and program transportation investments. Transparency of the planning process, flexibility in decision-making and resource allocation, and increased accountability to elected officials and to stakeholders alike are three of the pillars upon which the ISTEA structure is built. Less clearly articulated in the statute but arguably inherent in the policy principles that underpin it is the idea of fiscal restraint or discipline; i.e., the notion that plans and programs should not be financially unachievable wish lists but rather realistic reflections of priorities given what a State or metropolitan region can reasonably expect to receive and generate in the way of fiscal resources. At least in part, this was in reaction to what was perceived as widespread over-programming in the years prior to the enactment of ISTEA.

In 1993, FHWA/FTA promulgated regulations that expanded this requirement beyond capital investments to include existing and future financial needs to maintain and operate the existing transportation system.

In 2002, the second segment of the Transportation Research Board’s Committee on Statewide Multimodal Transportation Planning Peer Exchange (A1D01) was a discussion of fiscal constraint and financial planning issues. What this dialogue revealed was a consensus in support of the ISTEA policy objectives pertaining to financial planning but some differences in views as to how best to achieve those objectives.

On June 30th, 2005, the FHWA issued interim guidance on fiscal constraint to further explain the 1993 regulation requiring documentation and disclosure of revenues needed to implement the capital improvements and to operate and maintain the existing and planned transportation system at a level of performance agreed upon by metropolitan and State transportation agencies.

In 2006, given the new interim guidance, FHWA/FTA wished to assess the state of the practice among States in meeting the 1993 requirements for documenting and demonstrating fiscal constraint. Accordingly, in spring 2006 the FHWA Office Planning contracted with AASHTO to carry out this assessment by surveying seven State DOTs, and their corresponding FHWA Division Offices, and to make recommendations with respect to steps that could be taken to help States more effectively achieve the policy objectives of ISTEA with respect to this issue.

At about the same time, the agencies began the rulemaking process aimed at updating the Federal regulations with respect to statewide and metropolitan transportation plans and programs. As noted later in this report, the issue of fiscal constraint was a principal focus of attention during the rulemaking process. On February 14, 2007 the Final Rule was published in the Federal Register.

ORGANIZATION OF THIS REPORT

This report is organized into seven sections, as follows:

- Introduction (above)
• Background: traces the development of the Federal fiscal constraint requirement from ISTEA through the 1993 rulemaking to the Final Rule published in 2007.


• Review of findings the 2006 survey of seven State DOTs and corresponding FHWA division offices in re the fiscal constraint requirement.

• Key fiscal constraint issues in the 2007 Final Rule on Statewide and Metropolitan Transportation Planning.

• Best practices: provides a summary description of certain practices that would appear to advance the policy goals of fiscal constraint requirements.

• Conclusion.

BACKGROUND

ISTEA

ISTEA provided that metropolitan long-range plans must contain a financial plan:

“…that demonstrates how the adopted long-range transportation plan can be implemented, indicates resources from public and private sources that are reasonably expected to be made available to carry out the plan, and recommends any additional financing strategies for needed projects and programs.”

Similarly, for Metropolitan Transportation Improvement Programs (TIPs), ISTEA provided that TIPs must contain a financial plan that:

“(i) demonstrates how the transportation improvement program can be implemented; (ii) indicates resources from public and private sources that are reasonably expected to be available to carry out the program; (iii) identifies innovative financing techniques to finance projects, programs, and strategies; and (iv) may include, for illustrative purposes, additional projects that would be included in the approved transportation improvement program if reasonable additional resources beyond those identified in the financial plan were available.”

With respect to plans and programs at the State level, ISTEA is less prescriptive. For example, ISTEA provides that:

1 Transportation Research Board Committee on Statewide Multimodal Transportation Planning (A1D01) Peer Exchange, July 14–16, 2002, Wood’s Hole, Massachusetts [March 2004 (ISSN 0097-8515 0)].
3 23 USC, §134(g)(2)(B).
4 23 USC, §134(h)(2)(B).
“Each State shall develop a long-range transportation plan, with a minimum 20-year forecast period, for all areas of the State, that provides for the development and implementation of the intermodal transportation system of the State.”

However, as to the financial plan, ISTEA states that:

“The long-range transportation plan may include a financial plan that demonstrates how the adopted long-range transportation plan can be implemented, indicates resources from public and private sources that are reasonably expected to be made available to carry out the plan, and recommends any additional financing strategies for needed projects and programs. The financial plan may include, for illustrative purposes, additional projects that would be included in the adopted transportation plan if reasonable additional resources beyond those identified in the financial plan were available.” [Emphasis added.]

Similarly, with respect to State Transportation Improvement Programs (STIPs), ISTEA provides that:

“The (State) transportation improvement program may include a financial plan that demonstrates how the approved transportation improvement program can be implemented, indicates resources from public and private sources that are reasonably expected to be made available to carry out the plan, and recommends any additional financing strategies for needed projects and programs. The financial plan may include, for illustrative purposes, additional projects that would be included in the adopted transportation plan if reasonable additional resources beyond those identified in the financial plan were available.” [Emphasis added.]

Although ISTEA is less prescriptive for State plans and TIPs as it pertains to financial plans, it does have an identical requirement that both State and metropolitan TIPs “shall include a project, or an identified phase of a project, only if full funding can reasonably be anticipated to be available for the project within the time period contemplated for completion of the project.”

Interestingly, the expressions “fiscal constraint” or “fiscally constrained” do not appear in the sections of ISTEA pertaining to metropolitan and statewide planning.

1993 Rulemaking

In response to ISTEA, the joint FHWA/FTA rules governing Statewide and metropolitan transportation planning were originally promulgated on October 28, 1993. These rules, which

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5 23 USC, §135(e)(1).
6 23 USC, §135(e)(4).
8 23 USC, §134(h)(3)(D); 23 USC, §135(f)(2)(D).
had remained unchanged until the February 2007 Rule, codified the ISTEA requirements for financial plans in metropolitan plans and TIPs.

The 1993 rule required that metropolitan long range plans “include a financial plan that demonstrates the consistency of proposed transportation investments with already available and projected sources of revenue.”9 The 1993 rule amplified the statutory requirement that metropolitan plans include a financial plan by specifying that such financial plans:

(1) Consider not only capital costs but also maintenance and operations costs

(2) Include not just Federal-aid eligible projects but the “total transportation system (existing plus planned)”; 

(3) Identify revenue deficiencies by revenue source rather than simply for the plan in toto; and

(4) Identify proposed new revenues and/or revenue sources to cover shortfalls, including strategies for ensuring their availability for proposed investments

Specifically, the 1993 rule required that:

“The financial plan shall compare the estimated revenue from existing and proposed funding sources that can reasonably be expected to be available for transportation uses, and the estimated costs of constructing, maintaining and operating the total (existing plus planned) transportation system over the period of the plan. The estimated revenue by existing revenue source (local, State, and Federal and private) available for transportation projects shall be determined and any shortfalls identified. Proposed new revenues and/or revenue sources to cover shortfalls shall be identified, including strategies for ensuring their availability for proposed investments. Existing and proposed revenues shall cover all forecasted capital, operating, and maintenance costs. All cost and revenue projections shall be based on the data reflecting the existing situation and historical trends. For nonattainment and maintenance areas, the financial plan shall address the specific financial strategies required to ensure the implementation of projects and programs to reach air quality compliance.”10

With respect to metropolitan TIPs, the 1993 rule specified (in part) that:

(1) The TIP shall be financially constrained by year;

(2) Include a financial plan that demonstrates which projects can be implemented using current revenue sources and which projects are to be implemented using proposed revenue sources (while the existing transportation system is being adequately operated and maintained).

9 23CFR§450.322(b)(11).
10 Ibid.
Only projects for which construction and operating funds can reasonably be expected to be available may be included.

In the case of new funding sources, strategies for ensuring their availability shall be identified.

In developing the financial analysis, the MPO shall take into account all projects and strategies funded under title 23, U.S.C., and the Federal Transit Act, other Federal funds, local sources, State assistance, and private participation.

In nonattainment and maintenance areas, projects included for the first two years of the current TIP shall be limited to those for which funds are available or committed.

At the State level, the 1993 rule was much less prescriptive when it came to financial elements of State long-range plans. The 1993 rule required only that State plans “Reference, summarize or contain information on the availability of financial and other resources needed to carry out the plan.”

With respect to the State Transportation Improvement Plan, however, the 1993 rule specified (in part) that a STIP:

1. Be financially constrained by year;

2. Include sufficient financial information to demonstrate which projects are to be implemented using current revenues and which projects are to be implemented using proposed revenue sources while the system as a whole is being adequately operated and maintained.

3. In nonattainment and maintenance areas, projects included in the first two years of the current STIP/TIP shall be limited to those for which funds are available or committed.

4. In the case of proposed funding sources, strategies for ensuring their availability shall be identified.

As will be discussed later in this report, there was considerable consensus amongst State DOTs and FHWA/FTA with respect to the policy objectives of ISTEA and the 1993 rule; i.e., that metropolitan plans, TIPs and STIPs be fiscally realistic, that the planning and programming process be transparent, and that DOTs and MPOs be accountable to the public with respect to how funds are allocated and spent. However, there was some sentiment among State DOTs that the 1993 rule as it pertains to STIPs may to some degree have gone beyond the Congressional intent in ISTEA that, as noted above, did not require that STIPs have a financial plan.

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11 23CFR450.214(b)(6).
2005 Interim Guidance

Subsequent to the 1993 rule, FHWA and FTA provided some limited guidance on fiscal constraint, as well as specific assistance in States and metropolitan areas where demonstration of fiscal constraint has been seen as being a particular challenge. In June 2005, FHWA and FTA published “interim guidance, references, and worksheets” on fiscal constraint, stating that they were “intended to be a tool to assist FHWA and FTA field Offices in fulfilling current law requirements for fiscal constraint.” The interim guidance was posted on the FHWA website, which noted that “In the past 5 years, fiscal constraint issues have arisen in at least 10 States and several metropolitan areas. Some have raised concerns about whether FHWA/FTA have been applying fiscal constraint adequately and consistently across the country,” and that the interim guidelines were being published “in response to these recent issues and the need for consistency.”

2007 Final Rule

On June 9, 2006, the agencies published, in the Federal Register, a notice of proposed rulemaking (NPRM) proposing to revise the regulations governing the development of statewide and metropolitan transportation plans and programs and the regulations for Congestion Management Systems (71 FR 33510). As noted later in this report, the issue of fiscal constraint was a principal focus of attention during the rulemaking process. On February 14, 2007 the Final Rule was published in the Federal Register.

TRB 2002 PEER EXCHANGE ON FISCAL CONSTRAINT

For several years, the Transportation Research Board Committee on Statewide Multimodal Transportation Planning Peer Exchange (A1D01) has sponsored an annual peer exchange with the support of the Federal Highway Administration (FHWA). The second segment of the 2002 peer exchange program was a discussion of fiscal constraint and financial planning issues.

Each State DOT representative was asked to answer the following set of questions prior to coming to the peer exchange:

- How do you address financial planning in your Statewide planning process?
- How does your Statewide plan document financial planning issues?
- How do you demonstrate fiscal constraint in your State Transportation Improvement Program?
- How does the current fiscal/economic environment play into your long-range Statewide planning and programming process (es)?
- What, if any, performance measures that you may use have a financial basis?
At the exchange, FHWA staff led a discussion of the fiscal constraint and planning issues covered by the five questions and the additional topics raised by State DOT representatives. Two of these questions in particular relate directly to topics explored in the subsequent 2006 survey. Specifically:

- How is financial planning addressed in the Statewide planning process? and,

- How is fiscal constraint demonstrated in the STIP? and,

The States in attendance at the 2002 Peer Exchange were: Alaska, California, Florida, Maryland, Massachusetts, Michigan, Minnesota, Ohio, Texas, Washington and Wisconsin. Only two of these States participated in the 2006 scan, so the fact that many of the issues that arose in 2002 were also identified in 2006 suggests that they may be shared by many of the 50 States. This review of the results of the 2002 peer exchange thus provides a kind of “benchmark” for considering the 2006 results.

**Review of 2002 Peer Exchange**

*Financial Planning as Part of the Statewide Process*

All of the States said that they include financial planning as an important part of their Statewide planning processes, including some type of analysis to forecast revenues. Most of the analyses were similar and usually included an analysis of anticipated Federal funds, dedicated State funds (such as gas or sales tax), funds annually appropriated by legislatures, bond funds, local matching funds (for Federal-aid projects), and in some cases innovative financing techniques. Level of detail of the financial analyses appeared to vary significantly. While all States said that they work to financially constrain the STIP, Statewide long-range plans tended to be viewed as policy documents with less emphasis on financial planning and fiscal constraint.

*Demonstration of Fiscal Constraint in the STIP*

In general, the States said they used three steps to demonstrate fiscal constraint for STIPs: (1) estimate future funds; (2) set programming targets to be approximately equal to the estimated funds; and (3) schedule the projects to fit within the targets. It appeared that for the most part fiscal constraint was imposed at the State level and the targets then passed down to the MPOs. All of the States said that they re-demonstrated fiscal constraint when the STIP was adopted but most said that they also updated it annually if not more often as major amendments are made.

**Additional Discussion Items**

*Fiscally Constrained Transportation Plans and Programs*

A fundamental question was posed: what is the definition of “fiscally constrained”? There appeared to be some lack of clarity as whether fiscal constraint is on a cash flow basis,

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12 For reference, the 2007 Final Rule defines “Financially constrained or Fiscal constraint” as meaning that “the metropolitan transportation plan, TIP, and STIP includes sufficient financial information for demonstrating that
obligation, or reasonably available funds. Recognizing the importance for Federal, State and metropolitan partners to have a common understanding of issues pertaining to fiscal constraint, it was suggested that additional clarification might be helpful.

States generally felt that they had sufficient fiscal checks and balances in place. Some States indicated that they were not sure how much additional benefit resulted from FHWA/FTA oversight, although there was no disagreement as to the legitimacy of the stewardship role played by FHWA/FTA with respect to making sure that Federal funds are used appropriately.

Some States expressed the opinion that training of FHWA/FTA staff to make them more familiar with state financial planning and programming processes might facilitate more effective and consistent application of the 1993 Rule from state to state.

The discussion concluded with a review of the rationale for fiscal constraint in transportation plans. The goal was to make TIPs and STIPs a reasonable project list instead of an endless wish list. There was general agreement that this goal had been achieved. Fiscal constraint was also viewed as a means to show accountability of public funds and will help ensure flexible funding in future legislation. Many State DOTs said they could benefit from a more flexible interpretation of the fiscal constrain requirement without compromising achievement of these policy objectives.

The group discussed whether they felt that fiscal constraint was doing its job. All participants agreed that the goal had been achieved, whereby TIPs and STIPs were now a reasonable project list instead of an endless wish list.

Cost Estimation

There was a substantial discussion about how to maintain fiscal constraint when significant project cost overruns are experienced. All of the States acknowledged that cost estimation is a problem, from a small change in scope to a change that is out of their control, such as the price of asphalt.

Comparison to 2006 Findings

As will be seen later in this report, many of the same themes emerged in the 2006 study as were discussed at the 2002 peer exchange, even though there was only a two State overlap between the two groups of States.

Financial Planning as Part of the Statewide Planning Process

As in the 2002 peer exchange, all States participating in the 2006 scan said that financial planning is an important part of the Statewide planning process. Additionally, although all States projects in the metropolitan transportation plan, TIP, and STIP can be implemented using committed, available, or reasonably available revenue sources, with reasonable assurance that the federally supported transportation system is being adequately operated and maintained. For the TIP and the STIP, financial constraint/fiscal constraint applies to each program year.”
fiscally constrain their STIPs, there were found to be varying levels of financial planning and fiscal constraint to be found in their long-range plans.\(^\text{13}\)

**Demonstration of Fiscal Constraint in the STIP**

The general approach to demonstrating fiscal constraint was very similar among the 2002 and 2006 States: estimated revenues are compared to costs and projects are scheduled accordingly. However, a number of differences emerged. For example, some States program to authorization levels, others program to obligation authority (OA) levels, and some use a mix of the two. Revenue forecasting methodologies differ, with lesser or greater reliance on historical trends as the primary predictor of future revenues. As in 2002, there was a question raised as to what is the best approach to showing fiscal constraint: on a cash-flow basis, on an obligation basis, or on a reasonably available funds basis.

**Cost Estimation**

Cost estimation was a big concern for the 2006 States as it was in 2002. All of the States interviewed acknowledged that the constant changes in scope and costs of goods and services make this a tricky process. Different strategies were cited, such as: putting fewer projects into the STIP to allow a cushion for each project; programming by category instead of by project, or resorting to independent estimates to try to come closer to the actual project cost. All said that they try to pare back costs when it becomes evident that the cost will greatly exceed the estimate. Many States said they had a procedure whereby project cost estimates are updated several times during the development process and cost increases (or decreases) are reflected in STIP amendments.

**FHWA and DOT Differences**

Some States expressed the view that to some degree their respective FHWA Division Offices were inclined to view fiscal constraint as an accounting tool whereas the DOTs perceived it to be a planning tool. This mirrors the discussion from the 2002 conference where the definitions of fiscal constraint varied from being based on “cash-flow” (accounting) to “reasonably expected to be available” (planning).

Another comment in both 2002 and 2006 was there appeared to be some variation from state to state with respect to what is acceptable for demonstrating fiscal constraint, although this is perhaps unsurprising given that “guidance” by its very nature provides for some flexibility in interpreting certain provisions.

The 2006 States agreed with the 2002 participants in that they felt that the goal of fiscal constraint have been achieved but perhaps the requirements could be more flexible without compromising achievement of policy objectives. Some went as far as to suggest that the States’ own program management and business practices require fiscal constraint, causing them to wonder about the degree of additional benefit to the public as a result of the Federal requirements.

\(^\text{13}\) Remembering that there is no requirement that State long range plans be fiscally constrained.
These and related topics are discussed in greater detail later in this report.

2006 SURVEY

Survey Design and Participating States

This survey to assess how States are dealing with issues associated with the fiscal constraint requirement was comprised of two principal steps:

- Step 1: “Desk Scan”: each State DOT was provided with an overview memo explaining the purpose of the survey, as well as a questionnaire to be used as a general framework for an initial phone interview on the subject of fiscal constraint.

- Step 2: Following the phone interviews, site visits were made to each State DOT to explore the issues in greater detail. In addition, interviews were held at each FHWA Division Office. FTA participated in some but not all of the meetings.

Seven State DOTs participated in the survey: California, Georgia, Maine, Michigan, North Dakota, Pennsylvania and Utah. In addition, as noted, officials from the corresponding FHWA Division Offices (as well as some FTA representatives) were interviewed to get their perspective.

Going in, it was explained that the objective was “to understand the approaches that States are taking to meeting the fiscal constraint requirement from overall policy, planning and programming perspectives. However, detailed review of revenue and cost estimation methodologies is not part of this effort. Similarly, the question of what constitutes ‘adequate’ funding of operations and maintenance will not be addressed.” It was also made clear that responses to the survey, as well subsequent discussions, would be kept confidential, and that the intent was to develop a synthesis, or composite, picture of how States in general are complying with the fiscal constraint requirement and what issues/obstacles they see from their perspective.

Synthesis of Findings

What emerged from the discussions with State DOTs and FHWA divisions was a somewhat paradoxical picture of both consensus and some disagreement, of working relationships between DOTs and divisions that were sometimes cordial, sometimes a bit strained, and sometimes both. The major findings can be summarized in the following points:

1. There was broad consensus on the policy objectives of fiscal constraint.

States acknowledged the need for transparency and accountability in the transportation planning and programming process, and agreed that in the pre-ISTEA era significant over-programming of STIPs was a fairly common practice. Given the unpredictability of the project development process, and that some projects are inevitably delayed or cancelled due to environmental, technical, financial or other reasons, States believed that a modest amount of over-programming is appropriate to ensure timely use of funds and to maximize overall program delivery. However, there was general agreement that this practice must not be overused, and that DOTs
must be in the business of keeping faith with both elected officials and the public by “delivering what we promise.” Moreover, DOTs recognize that “wish list” programming is confusing and misleading, but said that this practice has largely disappeared since the passage of ISTEA.

FHW A divisions shared this consensus about the policy objectives of fiscal constraint, but were less sanguine about the degree to which the practice of over-programming had disappeared. It was observed that “DOTs operate in political environments, and concern was expressed a change of administration in the State capitol might result in pressure to shift away from fiscal restraint.”

2. There was consensus that fiscal constraint should be a planning and program management tool, not an accounting tool. Yet some States expressed some concerns with the way fiscal constraint requirements were being interpreted by their Division Office.

States seemed to prefer an approach that could be called fiscal restraint, or fiscal discipline, that achieves the policy objectives of ISTEA but does not place an inordinate administrative burden on the DOTs. The view from the States was that fiscal constraint was intended by Congress to be a planning tool, separate and apart from a State’s budget process and financial management information systems. To put it succinctly, in the words of one State DOT, “Accounting does not equal accountability. Enron had some of the best accountants in the world, but wasn’t so accountable at the end of the day.” States tended to see the STIP as a capital programming “vessel” that should not be significantly over- or under-programmed in comparison to the resources that are expected to be available. They believed they need to have the flexibility to move money and projects around to respond to real world events. They indicated that they were unsure as to the “value-added” of demonstrating fiscal constraint by source and by year, with re-demonstration required every time the STIP is amended, and some noted that this in fact pulls staff resources away from other program management activities.

Division Offices were to some degree divided on this point. Although all believed that there is an important fiscal stewardship role for FHW A/FTA, some wondered about the marginal benefit vs. burden of a more accounting-oriented approach to fiscal constraint. Other Division Offices, by contrast, were adamant that the States could not be trusted to not play “hide the ball” from MPOs, elected officials and the general public, and that FHW A/FTA need to “hold their feet to the fire” to make sure fiscal games are not being played.

3. States felt that, since ISTEA, they had put in place planning, program management and business practices that render the Federal fiscal constraint requirement somewhat redundant.

Every State cited their fiscal and program management systems and practices, and provided details of how they keep their programs in balance given expected revenues. States clearly believed that their “corporate culture” has evolved in the fifteen years since the passage of ISTEA to now embrace principles of fiscal discipline, accountability and transparency of the planning and programming process. They saw the Federal requirement as being, to some degree at least, redundant, although they acknowledged that USDOT does have stewardship responsibilities to ensure that Federal funds are properly administered and that Federal-aid projects meet Federal requirements.
4. Some States believed that the fiscal constraint requirement was being extended beyond the intent of Congress with respect to “color of money” and/or some programmatic classifications.

Generally, States saw the STIP as a capital programming document and that the demonstration of fiscal constraint should be limited to capital projects that have Federal-aid dollars in them. Figure 1 (Appendix) is an attempt to depict the areas of consensus amongst the States on this issue. There was a consensus, represented by the green area, that capital projects that have Federal funds should clearly be part of the fiscal constraint calculus, and that both Federal and State matching funds should be included. There was another consensus, represented by the area in red, that State, local and private funds for non-Federal-aid eligible projects should be excluded. There was a mix of views on the degree to which State, local and private funds should be accounted for in the demonstration of fiscal constraint.

This taxonomy is admittedly imperfect and masks numerous nuances, but it does serve to demonstrate that the States had a significantly different view of what should be included in the demonstration of fiscal constraint than did FHWA/FTA headquarters and at least some of the Division Offices. The Divisions were divided on this question. Some felt that it was not realistic to expect the States to gather data on non-Federal aid projects and highway and transit O&M, and that fiscal constraint should basically relate to programming of capital projects with Federal funds in them. Other Divisions took the view that, given the fungibility of many different fund sources and the flexibility in eligibility rules, there needs to be a full accounting of every kind of expenditure and every fund source.

5. Some States were concerned that by going down the “accounting” path to fiscal constraint, FHWA/FTA would be setting the table for fiscal constraint to become the next front in the “conformity wars.”

In States where air quality is a serious issue, some feared that the more detailed and precise the accounting requirements of fiscal constraint become, the more likely it is that advocacy groups who have a different transportation vision can use it as a “legal hook” for mounting air quality conformity challenges. For example, given the inherent uncertainty in both cost and revenue projections, groups that want to challenge a region’s planning and programming priorities may be able to creatively mount fiscal-based challenges as to whether a plan or TIP contains sufficient funding for operations and maintenance of public transit.

Both States and Division Offices recognized that there is no way to prevent lawsuits, and there was widespread feeling that what was then the forthcoming Federal rule on fiscal constraint should not inadvertently make it more likely that such lawsuits will succeed.

6. In States where there was a perception that FHWA/FTA had a overly strict interpretation of fiscal constraint, there was a feeling that the burden of complying with the regulation might to some degree be unhelpful to the State DOT’s efforts to hold itself accountable to elected officials and the general public.
A number of States commented that they were expending considerable resources in trying to meet the fiscal constraint requirements. They said this had become more of an accounting exercise, and they suggested that a better approach might to re-do the fiscal constraint exercise only periodically, for example when a new STIP is adopted or when a truly significant (however defined) STIP amendment occurs.

Here again, Division Offices seemed to have somewhat different views, with some basically saying, “We get together and work it out,” while others seemed to favor a stricter and more systematic approach.

7. States were concerned that, by extending to “all sources of funds” and “the entire transportation system,” FHWA/FTA might wind up usurping the authority of States and MPOs to determine what constitutes “adequate” levels of system maintenance.

States were well aware of the Federal requirement that States properly maintain, or cause to be maintained, any projects constructed under the Federal-aid highway program. But they noted that this requirement is outside the parts of statute that deal with metropolitan and statewide planning processes. Moreover, there was considerable sentiment amongst the States that the 1993 rule and 2005 interim guidance, by placing significant emphasis on giving priority to the maintenance and operation of the existing system, infringes on the rights of States and MPOs to determine the appropriate balance between system preservation and investment in new capacity. They acknowledged that the interim guidance states that “…beyond this basic requirement of proper maintenance, FHWA and FTA do not second-guess a State DOT’s or MPO’s decisions regarding uses of funding, nor would we question the priorities a State DOT or MPO has set with respect to maintenance and operation of the existing transportation system and construction of new projects.” There was broad support for this approach, but the feeling was that this flexible approach was perhaps being trumped by FHWA/FTA’s emphasis on provisions of the 1993 rule to the effect “that STIPs and TIPs must be financially constrained by year and include sufficient financial information to demonstrate which projects are to be implemented using current revenues and which projects are to be implemented using proposed revenue sources ‘while the system as a whole is being adequately operated and maintained.’” [Emphasis added.]

8. Flexibility was seen as either a positive or a negative.

There was much discussion, particularly with the State DOTs, as to whether the fiscal constraint requirement should continue as guidance or be made a rule as part of the 2006 NPRM process. The views ran the gamut of possibilities, from those States that insisted it should be a rule to those who insisted it should be guidance, often using similar arguments to make different points.

Some States said that they had arrived at a fairly amicable modus vivendi with their respective Division Office as it pertains to fiscal constraint. They tended to favor the flexibility that is

14 23USC§ 116.
15 Referring to § 116.
16 Cf CFR§450.216(a)(5) and CFR§450.324(3).
afforded by guidance rather than a rule, and they feared that a rule would yield a “least common
denominator” result that would reflect the most bureaucratic and inflexible approaches. States at
the other end of the “amicability” spectrum saw it exactly the opposite way, contending that
flexibility gives the District Office more latitude than it should perhaps have.

DOTs who preferred guidance commented that it would allow for necessary individualization,
inasmuch as all States work differently. They noted that it would be nearly impossible to make a
rule that both mostly rural as well as very urban States could both comply with. There was also
at least one Division Office that felt the same way, and indicated that it wanted flexibility to
interpret what best fits with the way each State works.

Those States that preferred a rule echoed a common theme that “the existing guidance is being
implemented as a rule, so why not just make it a requirement?” They contended that the
guidance leaves so much to interpretation that it leaves too many open questions. Contrary to
those States that preferred guidance, those that preferred rules felt that guidance would actually
enable more lawsuits because it would allow groups that want to dispute compliance too much
leeway on which to base their complaint.

Overall, there was no consensus as to whether FHWA and FTA should issue guidance or rules,
but there was agreement that either way could be a hook that groups could use as a way to
dispute transportation improvements to which they are opposed.

9. States were concerned about how often and at what thresholds STIP amendments
trigger re-demonstration of fiscal constraint.

In some States there was significant concern that the STIP be amended – and fiscal constraint re-
demonstrated – every time a routine change in project cost or schedule occurs. They recognized
that the potential exists for a major change in a major project to materially impact the State’s
fiscal capacity, and that in such instances (which they believed to be relatively rare) the STIP
should be formally amended, with public notice and, if necessary, hearings, and that the State
should be able to demonstrate how the change is going to be accommodated within the context of
fiscal constraint. But they argued that they were continually re-balancing the program to respond to
smaller changes that occur all the time and that this has no material impact on fiscal constraint
on a moving forward basis. There was also the view that what is major in one State might be
considered minor in another, so a “one size fits all” approach should be rejected and instead the
State DOT and its MPOs should work out an understanding with the Division Office as to what
constitutes a major change that would trigger a formal STIP amendment.

10. Some States were in strong disagreement with the way advance construction was being
treated in the context of fiscal constraint.

Not every State uses advance construction (AC) to an appreciable extent, but in those that do
there was significant concern over Federal guidance on how to handle AC within the context of
fiscal constraint. Generally speaking, States which have high levels of AC argued that AC
should be addressed as a strategy in the STIP/TIP and an explanation should be provided of what
AC is and how and why it is done. For example, an AC strategy might consist of using it as a
cash management/cash flow tool, in order to increase flexibility, and to make the most efficient use of available funds, while advancing projects to meet program goals. The feeling was that AC should not be required as part of the STIP/TIP project listing or demonstration of Fiscal Constraint.

To make their case for this position, States noted that:

• There is no Federal or State fund source titled “Advance Construction.”

• AC has no affect on a State’s ability to start new projects. States routinely start projects with non-federal funds with no guarantee of reimbursement.

• AC does not constitute a commitment of Federal funds to a project.

• AC is primarily used as a cash flow management tool. Rarely are projects identified for AC during the planning phase.

• Showing projects two or more times (once when it is first programmed and again when it is converted) is confusing to the public and administratively burdensome to the State. They argued that this approach adds no value over that which the STIP and TIP, as planning documents, provide in communicating the program. More than one State observed that “sometimes projects have already been completed” by the time they are converted, so listing them again at the time of conversion is confusing at best.

Division Offices wanted to assure that States are complying with the AC guidance and that the use of AC is transparent in the management of funds. Their view was that, to avoid double counting of funds, STIPs should be amended both when a project is programmed and when it is converted. States strongly disagreed, saying that double-counting is not, as a practical matter, a real danger. At least some of the Divisions acknowledged that where AC is broadly used as a cash management tool at the program level the requirement as currently interpreted can impose something of a burden on the States.

On Aug. 26, 2008 FHWA issued a final rule intended to increase state flexibility in spending federal-aid highway funds. The rule revises the regulation for advance construction of Federal-aid projects by: (a) Removing the restriction that a State must obligate all of its allocated or apportioned funds, or demonstrate that it will use all obligation authority allocated to it for Federal-aid highways and highway safety construction, prior to the approval of advance construction projects; and (b) clarifying that advance construction procedures may be used for all categories of Federal-aid highway funds, and that any available Federal-aid funds for which a project is eligible may be used when a project is converted to a Federal-aid project. These revisions make the regulation consistent with the advance construction provisions of SAFETEA-LU.

17 Federal Register / Vol. 73, No. 166 / Tuesday, August 26, 2008 / Rules and Regulations, p. 50194.
2007 RULEMAKING

In February 2007 the Final Rule was issued revising the regulations governing the development of metropolitan transportation plans and programs for urbanized areas, State transportation plans and programs and the regulations for Congestion Management Systems.

The issues with respect to fiscal constraint that were identified in the 2002 Peer Exchange and that had been brought into somewhat sharper relief during the 2006 survey of State DOTs continued to be the focus of much attention during the rulemaking process. In fact, the “Discussion of Comments” that accompanies the Final Rule states that “the largest number of individual comments we received were on fiscal constraint issues.”

Definition of “Financially Constrained” or “Fiscal Constraint”

The 2007 Rule defines “Financially constrained or Fiscal constraint” as meaning that “the metropolitan transportation plan, TIP, and STIP includes sufficient financial information for demonstrating that projects in the metropolitan transportation plan, TIP, and STIP can be implemented using committed, available, or reasonably available revenue sources, with reasonable assurance that the federally supported transportation system is being adequately operated and maintained. For the TIP and the STIP, financial constraint/fiscal constraint applies to each program year.”

According to the Discussion of Comments in the Final Rule, “Most commenters requested that three portions of the definition be deleted: (1) The phrase ‘by source,’ (2) the phrase ‘each program year,’ and (3) the phrase ‘while the existing system is adequately maintained and operated’.”

The first two points go to the heart of the issue of whether fiscal constraint is (or should be) principally a planning and program management tool or whether it is basically an accounting exercise, and reflects findings of the 2006 survey of State DOTs. The 2006 consensus among States (and some division offices) was that requiring that STIPs and TIPs be constrained by source and by year serves is of limited value and does not reflect the reality of how funds and projects are managed “in the real world.” FHWA and FTA were not persuaded, stating that they “consider demonstrating funding by year and by source necessary for decision-makers and the public to have confidence in the STIP and TIP as financially constrained.” However, in response to concerns raised, the Final Rule changes “the definition related to ‘by source’ to be consistent with the October 1993 planning rule. This change clarifies that fiscal constraint documentation should include committed, available, or reasonably available revenue sources.”

With regard to the third point, to address concerns that the FHWA and the FTA might be extending their purview beyond the Federally supported transportation system, the phrase “while the existing system is adequately maintained and operated” was changed to “with reasonable

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18 Federal Register, op. cit., p. 7225.
19 Federal Register, op. cit., p. 7263.
20 Ibid. p. 7227.
assurance that the federally-supported transportation system is being adequately operated and maintained.”

**Removal of Appendix B from the Rule**

One significant change that was made as a result of the commenting process was the deletion of “Appendix B: Fiscal Constraint of Transportation Plans and Programs” that was originally intended to accompany the Final Rule. According to the “Discussion of Comments”:

“Several State DOTs and a national and regional advocacy organization objected to including guidance documents with the regulations as Appendices A and B. These commenters noted that by including these documents with the regulation as appendices, the guidance documents would have the force and effect of law and, as a result, would ‘open up FHWA and FTA (and thus the States and MPOs) to litigation challenges based on a selective reading of short passages in these lengthy documents.’ Therefore, these commenters requested removal of the appendices. Additionally, these commenters were concerned that including these guidance documents with the regulation would make it more difficult to change these documents in response to evolving practices, as any change would require a rulemaking action.”

FHWA/FTA did not concur with the notion that State DOTs and MPOs would be subject to increased litigation based on inclusion of these appendices. However, FHWA/FTA did agree, with respect to Appendix B, that “modifications to this document may be more frequently required to respond to evolving practices” and therefore decided to remove Appendix B from the Final Rule.

Later on the “Discussion of Comments” elaborates on the thinking of FHWA A/FTA with respect to removal of Appendix B, stating that:

“When proposing Appendix B to the rule, the FHWA A and the FTA intended to raise the level of awareness and importance in developing fiscally constrained transportation plans, TIPs, and STIPs to States, MPOs, and public transportation operators. Since its introduction under the ISTEA, fiscal constraint has remained a prominent aspect of transportation plan and program development, carrying through to the TEA–21 and now to the SAFETEA–LU. The FHWA A and the FTA acknowledge that Appendix B contains a combination of guidance, amplifying information, and additional criteria. Given the level of controversy regarding this Appendix, it has been removed from the rule.

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21 Ibid.
22 Appendix A (Linking Transportation Planning and NEPA Processes) was retained.
23 Federal Register, op. cit., p. 7225.
24 Ibid.
“Instead, the FHWA and the FTA will be developing and issuing revised guidance on fiscal constraint and financial planning for transportation plans and programs soon after this rule is published.”

As of this writing the referenced revised guidance has not yet been forthcoming.

**Issues from Appendix B Retained in the Final Rule**

However, there were three elements within Appendix B that FHWA/FTA felt should be a part of the regulatory text for “clarity and completeness.” These elements were:

- Treatment of highway and transit operations and maintenance costs and revenues;
- Use of ‘‘year of expenditure dollars’’ in developing cost and revenue estimates; and,
- Use of ‘‘cost ranges/cost bands’’ in the outer years of the metropolitan transportation plan.

Each of these is discussed below.

*Treatment of Highway and Transit Operations and Maintenance Costs and Revenues*

As was found to be the case during the 2006 survey, this proved to be a sensitive issue during the rulemaking process. The “Discussion of Comments” notes that the 1993 planning rule and the NPRM interchangeably referred to the transportation system as either “existing,” “total,” or “entire,” and stated that “several State DOTs, MPOs and COGs, national and regional advocacy organizations, and others expressed concern and confusion over these terms.” Further, “Many commenters called into question the statutory authority for the FHWA and the FTA to focus on State and local government investments to operate and maintain the ‘system’ as part of fiscal constraint and financial plans supporting transportation plans and programs.”

The 2006 survey of State DOTs found similar concerns, including: the accounting practicality (and utility) of trying to keep track of funding for operations and maintenance of non-Federal aid eligible local streets and roads and transit systems; the possibility that the rule might open the door to Federal determination as to what constitutes “adequate” levels of maintenance; and the potential for interest groups seeking to block certain projects to use the issue of adequacy of funding for system operations and maintenance as a conformity-like legal strategy.

On balance, FHWA and FTA were not persuaded by these arguments, responding that:

> “The statute, as amended by the SAFETEA-LU (23 U.S.C.§134(i)(2)(C) and 49 U.S.C.§5303(i)(2)(C)), requires that the financial element of a metropolitan transportation plan ‘demonstrates how the adopted transportation plan can be implemented’ and ‘indicates resources from public and private sources that can be ‘reasonably anticipated to implement the plan.’ A metropolitan transportation plan,

\(^{25}\) Federal Register, op. cit., p. 7253.

\(^{26}\) Ibid.
as it is developed, must include consideration and recognition of how all the pieces of the regional transportation system will integrate, function and operate, not just those facilities which are or could be funded with Federal resources. To focus solely on the Federally-funded portion of the transportation system could create greater demands on limited Federal resources or jeopardize the value of the Federal investments made within that metropolitan area. Furthermore, outside the transportation planning process, there is a long standing Federal requirement that States properly maintain, or cause to be maintained, any projects constructed under the Federal-aid Highway Program (23 U.S.C. 116).

“Additionally, the FHWA and the FTA believe that the fundamental premise behind the wording in the October 28, 1993 planning rule regarding highway and transit operations and maintenance (58 FR 58040) remains sound.”

That said, the rule was revised “for purposes of clarity and consistency.” Specifically,

“§450.216(n), §450.322(f)(10), and §450.324(i) have been revised to better describe ‘the system’ as Federal-aid highways (as defined by 23 U.S.C.§101(a)(5)) and public transportation (as defined by title 49 U.S.C. Chapter 53). As background, 23 U.S.C. §101(a)(5) defines ‘Federal-aid highways’ as ‘a highway eligible for assistance other than a highway classified as a local road or rural minor collector.’ Additionally, these sections clarify that the financial plans supporting the metropolitan transportation plan and TIP and the financial information supporting the STIP are to be based on systems-level estimates of costs and revenue sources reasonably expected to be available to adequately operate and maintain Federal-aid highways (as defined by 23 U.S.C. §101(a)(5)) and public transportation (as defined by title 49 U.S.C. Chapter 53).”

In making this change, it would appear that FHWA and FTA went some distance to accommodate concerns that had been expressed during the rulemaking process. This point is made again in the “Definitions” section of the Rule, wherein “financially constrained” or “fiscal constraint” means “that the metropolitan transportation plan, TIP, and STIP includes sufficient financial information for demonstrating that projects in the metropolitan transportation plan, TIP and STIP can be implemented using committed, available, or reasonably available revenue sources, with reasonable assurance that the federally supported transportation system is being adequately operated and maintained.”

Use of Year-of-Expenditure Dollars in Developing Cost and Revenue Estimates

The Discussion of Comments section of the Final Rule notes that the 2005 Interim Guidance “indicated that financial forecasts (for costs and revenues) to support the metropolitan transportation plan, TIP, and STIP may: (a) Rely on a ‘constant Dollar’ base year or (b) utilize an inflation rate(s) to reflect ‘year of expenditure’.” The rationale stated was to “better reflect the time-based value of money,” noting that, “This is particularly crucial for large-scale projects.

27 Federal Register, op. cit., p. 7253.
with construction/implementation dates stretching into the future. Because the transportation planning process serves as the beginning point of the larger ‘project continuum’ (i.e., moving from concept through construction, and later operations and maintenance), the FHWA and the FTA strongly believe that early disclosure of revenue and cost estimates reflecting time and inflation provides a truer set of expectations and future ‘reality’ to the public.  

Although State DOTs and others asked for continued flexibility in using either constant dollars or year-of-expenditure dollars, the Final Rule states that: ‘Revenue and cost estimates for the STIP must use an inflation rate(s) to reflect ‘year of expenditure dollars,’ based on reasonable financial principles and information, developed cooperatively by the State, MPOs, and public transportation operators.’ This language expresses the desire of the FHWA and the FTA for revenue and cost estimates to be reflected in “year of expenditure dollars.” Recognize that it might take some time for State DOTs and MPOs to convert their metropolitan transportation plans, STIPs and TIPs to reflect this requirement, the Final Rule allowed a grace period until December 11, 2007, during which time State DOTs and MPOs could still reflect revenue and cost estimates in constant dollars. After December 11, 2007, revenues and cost estimates must use “year of expenditure” dollars.

Use of Cost Ranges/Cost Bands in Outer Years of Metropolitan Transportation Plans

Noting once again that “the FHWA and the FTA will be developing and issuing revised guidance on fiscal constraint and financial planning for transportation plans and programs soon after this rule is published,” the Discussion of Comments section of the Final Rule notes that the 2005 Interim Guidance “indicated that for the outer years of the metropolitan transportation plan (i.e., beyond the first 10 years), the financial plan may reflect aggregate cost ranges/cost bands, as long as the future funding source(s) is reasonably expected to be available to support the projected cost ranges/cost bands.”

In the NPRM, the FHWA and the FTA proposed to provide this option to MPOs in developing fiscally-constrained metropolitan transportation plans. This option was retained in the Final Rule because “we believe it gives MPOs maximum flexibility to broadly define a large-scale transportation issue or problem to be addressed in the future that does not predispose a NEPA decision, while, at the same time, calling for the definition of a future funding source(s) that encompasses the planning-level ‘cost range/cost band’.”

BEST PRACTICES

Background

In this context, the term “best practice” connotes things that some States are doing to better plan and manage their programs. Sometimes these practices respond directly to Federal fiscal constraint requirements, but more often than not they are viewed by States and MPOs as tools to help them better achieve their departmental goals of fiscal accountability and transparency of the planning and programming process. States and MPOs have suggested that it would be helpful to

29 Federal Register, op. cit., p. 7253.
know how others are dealing with a variety of issues and challenges in this arena. In the conclusion to this report, it is recommended that a program of information sharing and peer exchange among the States be initiated to enhance the States’ ability to better plan and manage their program. The best practices identified here could serve as an initial basis for such an initiative.

The best practices discussed below are perhaps best thought of as being representative and do not constitute a complete or exhaustive list. In some cases they clearly follow the fiscal constraint rule/guidance. Others are included because they appear to address problems that many States and MPOs seem to encounter, or simply that they strike us as being solid, acceptable planning practices that should be considered by States and MPOs as a way to operate.

Some of the challenges that these best practices help address include: difficulties with cost and revenue estimation; small, often politically driven, earmarks; projects that extend beyond the life of the STIP; project prioritization; one-time funding increases; and operations and maintenance costs. As noted above, some of the best practices are simply good methods to follow to prevent issues from arising and to make the process of demonstrating fiscal constraint easier for all parties involved.

Selected Best Practices

The best practices reviewed below strike us as being applicable to the challenges that States and MPOs are facing relative to compliance with the fiscal constraint requirement. Depending on the size of the State/MPO and its transportation budget as well as other factors, each best practice applies to a greater or lesser degree. Overall these are model practices to consider.

1) Systematic updating of project cost estimates during the project development process

Some States and MPOs have a process for updating cost estimates throughout the project development process, which creates more work but ultimately results in fewer surprises and allows for re-prioritizing within the program when costs escalate quickly. Often times the cost estimations are conducted in advance of bid-letting which provides the opportunity to move funds around so as to be able to afford the increase or to re-scope the project to keep it close to its original budget.

For example, one State has a project cost control procedure in place where project cost estimates have to be revisited, and either revised or affirmed, at four specific points in the project development process in order to avoid big surprises. These re-estimates usually occur before bid-letting, which is usually early enough in the process to make the necessary amendments. This DOT is using a new project management system to try to find out where the big cost increases are occurring so some of the increases may be avoided in the future. They are also hoping that this will help make better estimates of increases in costs for materials and construction that are making cost estimates even more unreliable.

Another DOT reviews cost estimation at each project’s key milestones before bid-letting occurs. The administration has a philosophy of asking “are we doing the right kinds of projects? Are we
fitting the projects to what’s really necessary and not building a ‘taj mahal,’ but only what’s necessary to fix the problem?” When an MPO or regional office of the State DOT comes in for a cost increase in advance of a bid-letting, the DOT HQ talks to them to see what they can do within the existing cost estimate.

2) Proper treatment of “out of plan” and small earmarks

All States have to deal with the issue of how to address Federal earmarks that do not necessarily reflect the State’s or an MPO’s priorities. There is general recognition that such earmarks distort the program in one or more ways, including:

- **Resources:** They provide only a fraction of a project’s likely cost, thus may divert resources from higher priorities (if the project advances).

- **Timing:** They may be good projects but ones that were not envisioned to advance until a future STIP.

- **Planning:** they may simply be “out of plan,” i.e., they have not been identified through the normal 3-C metropolitan and statewide planning processes and thus require shifting established priorities and re-allocating funds among projects that are in the STIP.

The burgeoning number of earmarks is becoming an increasing administrative burden for States and MPOs, and even more so to the extent that the projects cause the above mentioned distortions. While most States and MPOs might prefer to place the burden on the local project sponsors to come up with the necessary match, political realities sometimes make this difficult. One way to avoid this sticky situation is by working proactively with their Congressional delegation to ensure that High Priority Project (HPP) earmarks are for projects in the plan and program and do not distort the investment priorities that the State and its MPOs have decided upon.

A good example of how earmarks can become a problem (sort of a non-best practice) is having a policy not to turn away any Federal transportation funds, which creates a problem when it comes to earmarks because they require additional funds beyond the earmark and this can distort the entire program.

A counter example is a strategy to help keep the plan constrained by taking out projects if there is not enough money for a particular project. For example, if $100 million is needed for a project and only $10 million has been provided in an earmark, rather than using the $10 million for design of the project with a *de facto* $90 million unfunded liability, the DOT tries to convince the local jurisdiction to seek Congressional action shifting the earmark to a smaller project and to re-visit the larger project in the context of the State or metropolitan long-range planning process.

Another State takes the approach that when there is an earmark for a percentage of the cost of project, the burden is on the local sponsor to identify the funding that will be needed to go to construction. However, perhaps as a nod to political reality, the sponsor is allowed to proceed with development phases of the project with the funds in-hand even without a full-funding plan.
in place. This State DOT would like a State policy established on how to deal with such earmarks, as this issue has come up repeatedly. Another State DOT takes a harder line: it has a policy of not matching earmarks for local projects and will not put them into the STIP unless the locals or project sponsors come up with the necessary funds.

A best practice to avoid these problems in part or entirely is to have lots of interaction with the State’s congressional delegation to ensure that earmarks reflect State and MPO priorities and do not come in “from left field.” More than one State we’ve talked to said that they put a lot of energy into this approach and that it has been reasonably effective in avoiding the political and administrative problems that “out of plan” earmarks tend to cause.

3) Having an out-year program (something between the STIP and the LRP) to deal with projects whose big drawdown happens beyond the STIP period).

While all States have a four or five year STIP and a 20-to-30 year LRP, there are many variations as to how States plan for the mid-term. The variety ranges from no mid-range plan at all to a fiscally constrained mid-range plan, typically 8, 10 or 12 years. Having a mid-range program is especially helpful when dealing with larger projects for which the majority of costs fall beyond the STIP period. By taking a look at its finances in the post-STIP period, a State can make a better informed judgment as to how best to accommodate the early stages of such projects in the STIP without setting itself up for fiscal problems in the next STIP. While this “post-STIP” look falls outside the fiscal constraint exercise, it represent a good approach for ensuring fiscal constraint in the future.

For example, one State has a twelve-year transportation program that includes all modes: highway, bridge, transit, intermodal, freight and aviation. The program was originally a six-year program but was changed to be longer-term when the DOT was unable to complete substantial parts of the program because of limited funds. The twelve-year program is revised every two years and presents the State’s priority list of transportation projects, including projects funded solely by the State as well as those that combine State, local and federal funds. Having this mid-range program between the four-year STIP and the 30-year plan enables the State to better deal with projects that start in the short-term but don’t expend all of the funds, or even the majority of the funds, within the first four years. This mid-range program is integral to the State’s fiscal management strategy by showing what funds are required beyond the first four years.

Another DOT generally looks at a three to-four-year time horizon for planning projects and tries to keep projected balances in line. Their STIP is a five-year document, and the first three years are generally for programming projects and the last two years are used as a kind of staging area for “concept development” of future projects. These projects are projected to move into a funded year within the next five years and are included for informational purposes only. Their LRP is 30-years and is broken into three “horizons,” the first horizon being 7 to 10 years, which includes the STIP and the concept development projects from the STIP and beyond. As a State with a much smaller transportation budget than the State previously discussed, this State does not really need a separate mid-range plan because it doesn’t generally have multi-year projects that extend beyond the STIP period. For them, using the concept development aspect of the STIP satisfies the need to plan beyond the short range of the STIP but in a more concrete manner than the LRP.
One unusual feature of this State’s LRP is that it attempts to identify financial resources for each of the horizon periods. As a rule, most State plans are policy-oriented documents with limited financial planning content.

One last example of how States deal well with projects that extend beyond the STIP period is a State that puts projects that did not fit within the financial envelope of the five-year STIP into an “FYI Year” in the STIP. They also have a Master Transportation Plan (MTP) that addresses the next five years after the STIP. The MTP is fiscally constrained and expected sources of funds are shown, however the “FYI-Year” projects are shown as unfunded needs that are compiled from various feasibility studies. The MTP shows the next phases of all projects in the STIP and is updated every two years.

4) Explicit linkage between State LRP and STIP (in terms of goals, objectives)

Ideally, the State’s Long Range Transportation Plan and STIP are aligned in terms of their goals and objectives and have explicitly stated linkages between the LRP and the three to five-year program. While all States theoretically base their STIP on the broader goals and objectives defined in the LRP, some States explicitly link the two plans and define in their State guidance how the two should interrelate.

In one State, the LRP’s goals and objectives are developed in conjunction with extensive public outreach. Ultimately, these are reflected in the STIP and the STIP financial plan. For example, in the State’s last long range plan, the top priorities for all modes were safety and system preservation and maintenance, which in turn guided the target to spend 80% of statewide funds in the STIP financial plan on maintenance. The STIP is explicitly designed to implement the vision, policies, goals and objectives of the currently adopted Statewide LRP.

Another State has only recently addressed the linkage between the LRP and STIP. Prior to 2004 the LRP was basically a policy document, but the newer LRP is more project-specific, at least at the corridor level. Now the State DOT requires that projects originate in the Long Range Plan before they are placed in the STIP. Another State has the STIP linked to the MPO long range plans; the Statewide Long Range Plan is more of a policy document, whereas the MPO Long Range Plans more closely reflect a longer-term version of the TIPs (which in turn make up the STIP).

5) Explicit resource allocation priorities are stated in STIP

Oftentimes the goals and objectives established in the LRP result in more specific priorities being defined in the STIP as a way to inform the allocation of scarce resources. One State has a financial guidance working group, made up of representatives from the DOT, FHWA, FTA and some MPOs and RPOs, that deals with apportioning federal funds in a needs-based manner and has changed the way some of the funds are programmed to better meet this objective. Specifically, the DOT emphasizes that maintenance should be the first priority and brings information on deteriorating bridges and other pressing maintenance needs to the annual State planning meeting to try to get the MPOs and RPOs to add maintenance projects into their TIPs. The State maintains a policy of using about 80% of the total highway funds in the STIP for
operations and maintenance (including asset rehabilitation and reconstruction) with the remainder for new construction or capacity additions. This goal is tracked and they stay very close to the goal on a statewide level. One other State explicitly said that the primary goals of the LRP and STIP are to preserve the system, and bonds and other innovative financing tools are used to fund this goal.

In another State, rather than identifying an overarching priority such as maintenance, the STIP outlines its strategy as being focused on maintaining current project delivery schedules and keeping project components fully-funded. This strategy also helped the State DOT focus on ensuring that existing projects received necessary funding before expanding the scope of the program.

6) Programming conservatively to leave a cushion

Some States program to obligation authority (OA) even though they are permitted to program to authorization levels, which are generally running 10% to 15% above OA. Other States program conservatively by including substantial contingencies in the cost of each project to try and ensure that the total costs will not exceed revenues if costs increase.

One State puts fewer projects into the STIP than it theoretically could, thus providing a program-level cushion and requiring fewer amendments than might otherwise be the case. It also programs projects in the STIP with about 10% excess budget and schedule in case project delivery slips.

Some States program against authorization levels knowing full well that OA will come in lower. However, this allows for extra programming capacity so if one project slips another can take its place without major changes to the STIP. They feel that this approach works best from the project management perspective and does not pose a problem with respect to meeting the fiscal constraint requirement. They also try to place programs in categories as lump-sum line items in order to maintain flexibility. By affording itself some flexibility, the State is better able to deliver the program in a way that might not be possible with a tighter definition of fiscal constraint.

Another State also programs the STIP to apportionments, not OA, and estimates are adjusted as funds are apportioned each year. The DOT in this State must be extra cautious due to revenues that were assumed in the past but did not come to fruition. This necessitates conservative cost estimation in case the revenue projections do not materialize.

7) Being non-specific about future revenue projections, especially for “one-time” actions

Many States face the challenge of how to show future revenues based on past actions that may have occurred once or even multiple times but are not guaranteed to occur again. Such revenues could be the result of a gas tax increase, a legislative appropriation, sales tax increase or other user fee increase such as implementation of tolls on a previously free facility.
The 2005 Interim Guidance provides that “Future revenues may be projected based on historical trends, including consideration of past legislative or executive actions.” Rather than assume specific future events (such as an action by the legislature or a vote of the people), States generally prefer to project future revenues based on past trends (which, of course, reflect past actions).

Specifically, one State has a challenge with revenue estimation and trying to account for one-time occurrences such as a gas tax increase in the late 1990s and a legislative appropriation more recently. There is no clear way to handle these one-time projections, but the DOT works with the two largest MPOs in a regional Long Range Plan Finance Committee to cooperatively develop financial projections keeping such one-time occurrences in mind.

In another State there was no separate process for State fund revenue estimation since historically the State Legislature only matches Federal funds and does not provide any more than the necessary match. The State match monies come from a dedicated transportation fund which is funded at the discretion of the legislature, which only meets every two years. Therefore, this State also has to be careful to show future matching funds as gradual growth to match federal appropriations growth as opposed to assuming specific legislative actions.

8) Clear guidance on dollar amount/project percentage cost changes that trigger an amendment with re-demonstration of fiscal constraint versus administrative action.

Prior to publication of the Final Rule, some States reached agreements with their Division Offices as to the level of a project cost change (either a dollar amount or percentage change) that necessitates a formal STIP amendment versus an administrative action. Having such clarity makes STIP amendments a more manageable process than in those States where there has to be a discussion with the FHWA or FTA Division Office on every occasion to determine whether a change can be made administratively or not. The best type of specific guidance appears to strike a balance between providing enough fiscal stewardship by FHWA/FTA without overburdening the State with paperwork. In addition, while some States said they had clear guidance on the magnitude of change that would require an amendment, it was not always clear whether the amendment required that fiscal constraint be re-demonstrated. Some States were only required to re-demonstrate fiscal constraint when they adopted a new STIP whereas others were required to do so whenever the STIP was amended. This points out the fact that different Division Offices appeared to interpret these requirements differently.

In one State official STIP amendments were done if a project cost increase was greater than 49%, but this was being reconsidered based on the dollar amount of the increase, so that a larger project would have to do an official STIP amendment at a lower percentage increase. In another State, if the cost of a project increase was relatively low it was dealt with at the MPO level. If the State DOT projected a cost increase over a certain percentage then the project would go before a State project review board.

Another State had clear guidance for amendment levels and fiscal constraint demonstration. There, the TIP and STIP had to be formally amended whenever the change accounted for 20% of the project cost or $2 million, whichever was lower. Changes for less than this amount could be
done by administrative action. The DOT was also required to show fiscal constraint with every amendment.

It is not clear how the 2007 Final Rule will affect these practices. In its “Definitions” section, the rule defines amendment to mean:

“...a revision to a long-range statewide or metropolitan transportation plan, TIP, or STIP that involves a major change to a project included in a metropolitan transportation plan, TIP, or STIP, including the addition or deletion of a project or a major change in project cost, project/project phase initiation dates, or a major change in design concept or design scope (e.g., changing project termini or the number of through traffic lanes). Changes to projects that are included only for illustrative purposes do not require an amendment. An amendment is a revision that requires public review and comment, redemonstration of fiscal constraint, or a conformity determination (for metropolitan transportation plans and TIPs involving ‘non-exempt’ projects in nonattainment and maintenance areas). In the context of a long-range statewide transportation plan, an amendment is a revision approved by the State in accordance with its public involvement process.”

Further, the Final Rule defines “administrative modification” to mean:

“...a minor revision to a long-range statewide or metropolitan transportation plan, Transportation Improvement Program (TIP), or Statewide Transportation Improvement Program (STIP) that includes minor changes to project/project phase costs, minor changes to funding sources of previously-included projects, and minor changes to project/project phase initiation dates. An administrative modification is a revision that does not require public review and comment, redemonstration of fiscal constraint, or a conformity determination (in nonattainment and maintenance areas).”

The “Discussion of Comments” section of the Final Rule goes on to state that “State DOTs and MPOs should work with the FHWA and the FTA to identify thresholds for a ‘major’ change in project cost. Examples of thresholds could include, but are not limited to, project cost increase that exceeds 20 percent of the total project cost; or project cost increase that exceeds a certain dollar amount, for example, the increase in costs exceeds the programmed amount by $50,000 or $100,000.” This would appear to provide the flexibility inherent in the “best practices” cited above.

Elsewhere, however, the Final Rule “Discussion of Comments” states:

“Many of the MPOs and COGs and most of the State DOTs opposed the statement in paragraph §450.316(a) [“TIP Revisions and Relationship to STIP”] that ‘in all areas, changes that affect fiscal constraint must take place by amendment of the TIP.’”

30 Federal Register, op. cit., p. 7261.
31 Ibid.
32 Ibid., p. 7226.
FHWA and the FTA realize that there are minor funding changes to projects that a region could determine would fall under the definition of ‘‘administrative modifications,’” and these would not need to go through the full TIP amendment process. However, the FHWA and the FTA include this requirement because any change which requires an amendment has ripple effects throughout the program and thus should be subjected to the full disclosure of a TIP amendment.\footnote{Federal Register, op. cit., p. 7248.}

It is not completely clear whether this “ripple through” language will encourage Division Offices to perhaps be less flexible in reaching accommodation with State DOTs and MPOs as to what is ‘major” and what is “minor” when it comes to STIP and TIP changes.

9) \textit{Involve FHWA/FTA Division Office as the STIP is developed so there are no surprises}

One way to avoid problems in the demonstration of fiscal constraint to the Division Offices of FHWA and FTA is to make them a partner in the STIP and LRP development process. Most States claimed a very open working relationship with their Division Offices and indicated that there is a lot of interaction as well as regular status meetings to ensure that they are apprised of the latest issues. Nevertheless, in some States there was, and possibly still is, considerable tension between the DOT and the Division Office over the fiscal constraint issue.

In one State, a financial guidance working group made up of DOT, FHWA, FTA and some MPOs and RPOs meets regularly whenever a new STIP is developed to discuss cost and revenue projections, identify new project expenditures and review the program to make sure that it meets fiscal constraint guidance. Revenue targets are agreed upon by consensus of this working group. While difficult to achieve, consensus makes it easier to demonstrate fiscal constraint because all parties are in agreement. This constant involvement of the FHWA and FTA Division Offices helps to ensure that there are no eleventh-hour surprises and that any questions that the Federal agencies may have are worked out at the working group level instead of later in a more public setting where disputes can present a greater problem. In addition to the financial working group, the DOT meets monthly with the FHWA Division Office to keep them in the loop. Additionally FHWA is included in the weekly meeting between the DOT’s programming office and the Secretary so that they know of any upcoming issues as soon as they arise.

10) \textit{On-line system for STIP amendments}

Some State’s have set up a quick and easy way of making amendments and changes to the STIP to enable projects to move forward with the least administrative burden. Many States either have or are in the process of developing systems to give implementing agencies a way to enter and change their projects electronically. In addition, many MPOs are moving to on-line systems as they develop the TIPs that are rolled-into or referenced in the STIP.

One State has a project management system on a password-protected website that allows MPOs and RPOs to update their project and cost information. They also have an electronic STIP amendment process whereby MPOs and implementing agencies, once they’ve obtained the
required local approvals, can request STIP amendments via e-mail and the approval process is then conducted entirely electronically.

Another DOT has a computerized Project Management System that has fiscal constraint functionality inherently built in. STIP development is linked to this management system, whereby the regions enter projects into the system and the DOT puts in the available dollars by category and the expenditure and revenues must match up. Still another DOT is in the process of developing an automated STIP tool that will help keep the program fiscally constrained by creating a uniform format for showing projects, funding and costs.

11) Independent cost estimations

In order to counter speculation that the DOTs are underestimating costs in order to demonstrate fiscal constraint or are overestimating costs to allow for scope or cost increases without amending the STIP, some States have turned to independent cost estimates. One such State has started using independent costs estimates for their projects in part because their estimators were envisioning a much smaller project than what actually ends up being built. One State noted that oftentimes this is because the use of Federal funds for rehabilitation projects inevitably expands the scope of their projects beyond what the DOT had originally intended (e.g., to meet federal standards).

CONCLUSION

As previously noted, what emerges from this overview of the fiscal constraint issue is a picture that is, paradoxically, characterized by both consensus and some disagreement with respect to the Federal fiscal constraint requirement. While there is strong support across the board for the policy objectives of accountability, realism and transparency in the planning and programming process, there is disagreement, at least in some States, with some details of the approach being required by FHWA/FTA. Moreover, many States question the value-added of what they see as an accounting-oriented approach, and they are concerned that the resources being required to meet these requirements may detract from their ability to achieve the very policy objectives upon which there is so much agreement.

The Division Offices, for their part, seem to have a range of views on the subject. Some are to a degree aligned with the views of their State DOT and appear to have embraced an “accountability, but with flexibility” mantra that has yielded a relatively smooth working relationship on the issue of fiscal constraint. Other Divisions take what is perceived to be a sterner view, and in those cases a much more adversarial picture emerges.

Some, perhaps most, of the issues identified in this report may be resolved one way or the other as a result of the 2007 Final Rule and the yet-to-be-issued subsequent guidance. But this remains to be seen.

That said, one of the original objectives of the 2006 survey was to “provide a basis for structuring a technical assistance program to assist States that may be falling short of compliance.” When asked what kind of technical assistance they would like, without exception
the States indicated that they are not in need of particular assistance as it pertains to technical requirements of fiscal constraint (although there was general support for TRB and other technical forums for improving cost estimation methodologies). Rather than technical assistance *per se*, what the States seem to want is the opportunity to share with each other, and with FHWA and FTA, the varying planning, program management and business practices they have instituted over the last decade and a half since ISTEA so as to achieve the relevant policy objectives inherent in ISTEA in the most effective manner possible. The recommendation that emerges from this, then, is that AASHTO and AMPO partner with FHWA, FTA, State DOTs, MPOs and other stakeholders who have a vital interest in this issue to develop a regular and sustained program of information exchange and dialogue.
### APPENDIX

**States’ Views on what Should (and Should Not) be Included in the Demonstration of Fiscal Constraint**

**Figure 1**

<table>
<thead>
<tr>
<th>Programmatic Classification</th>
<th>Federal-aid Eligible</th>
<th>Not Federal-aid eligible</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Matching</td>
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<tr>
<td>State</td>
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<td>Local</td>
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<tr>
<td>Private</td>
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</tbody>
</table>

#### Color of Money

- **Federal**
- **State**
- **Local**
- **Private**

- **Consensus to Include**
- **Consensus to Exclude**
- **Mixed Views**

- **Highway Capital**
- **Highway - System Preservation**
- **Transit Capital**
- **Transit O&M [capitalized - §5307 eligible]**
- **Local streets and roads - Capital [e.g., HPP, STP-L]**
- **Local streets and roads - Capital**
- **Transit O&M [not Federal-aid eligible]**
- **Highway - Routine Maintenance [not Federal-aid eligible]**
- **Local streets and roads - Maintenance**

![Figure 1](image-url)