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Operations of and Outlook for the Highway Trust Fund

Statement of
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Transportation, and Infrastructure
Committee on Environment and Public Works
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Mr. Chairman and Members of the Subcommittee:

I am pleased to have this opportunity to testify on the operations of and outlook for the Highway Trust Fund. As your Committee examines how best to use the revenues credited to the trust fund, items warranting attention include the unexpended balance as well as trust fund revenues that could be made available to meet our burgeoning surface transportation needs.

As you know, critical needs confront the nation's highway and bridge network. Yet, a $10.6 billion balance exists in the Highway Account of the Highway Trust Fund. Why? The primary reason is that limitations are placed on the amount of funds states are allowed to obligate. In addition, states have not used an estimated $1 billion in the trust fund revenues available to be obligated. According to state officials, they do not use these funds primarily because they provide a cushion against an uneven flow in federal funds.

Under recent projections, the trust fund balance at the end of its life will exceed outstanding commitments by an estimated $7.4 billion. After $1 billion authorized for emergency relief is deducted, a one-time increase in authorizations of $3.4 billion is possible. Such an increase still allows for a safety cushion of $3 billion in the fund--the maximum federal transportation officials believe is required to provide for unforseen disruptions to highway taxes or inaccurate revenue projections. Finally, to prevent future build-ups in the trust fund balance, obligation ceilings should more closely approximate expected income--revenues and interest--to the trust fund.

My testimony today will focus on the operations of the Highway Trust Fund, including yearly revenue and expenditure streams; reasons for the buildups in the fund's balance; and our observations on the process for drawing down the balances. Unfortunately, the severity of the general fund deficit has made the concept underlying trust funds--that revenues be spent for their intended purpose--quite different in reality, because various trust fund balances are used to mask the deficit. In the current budget environment, the reality is that any accelerated drawdown of the Highway Trust Fund balance can be accomplished only by increasing the deficit or at the expense of other federal programs.

I will now discuss the Highway Account.

HIGHWAY TRUST FUND--THE HIGHWAY ACCOUNT

The federal Highway Trust Fund was established in 1956 as a mechanism to support and expand the rapidly growing Federal-Aid Highway Program. The program includes the Interstate, primary, secondary, and urban highway systems, and accounts for over 80 percent of all vehicle miles traveled.

The trust fund is funded through user fees such as the federal 9-cent per gallon gasoline tax, taxes on tires, heavy vehicle-use taxes, and interest on the trust fund balance. This fund is used to reimburse state governments for money spent improving the federal-aid highway system. The federal government generally pays 75 percent of a project's cost, although for some projects, such as on the Interstate system, the federal share may be as high as 90 percent.

The trust fund is reauthorized periodically, most recently in 1987. The 1987 Highway Act authorized roughly $14 billion in funds for the Federal-Aid Highway Program for each year through fiscal year 1991. Most federal programs require congressional authorizations to be followed by appropriations that grant approval for spending or obligating program funds. Programs within the federal-aid highway system, however, generally bypass this two-step process. Rather, federal-aid authorizations are made available for obligation[1] without appropriations through what is called "contract authority."

However, not all authorized funds may be available in a given year for states' use. The Congress may impose obligation ceilings

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[1]An obligation is a commitment of the federal government to reimburse states for the federal share of a project's eligible cost.

on authorized highway funds, which, according to the Department of Transportation (DOT), are part of an overall effort to control federal spending. For instance, while $22.1 billion was available for highway programs in fiscal year 1989, the obligation ceiling was set at $12.2 billion for that year. With the exception of $2.2 billion available for programs exempt from the ceiling, the total of states' commitments for highway projects could not exceed $12.2 billion.

Highway and Bridge Needs Are Escalating

Difficult decisions face the Congress on the amount of federal funds that should be directed to highway and bridge needs. For instance, the Interstate Highway System is vital to our transportation network, as it carries slightly more than 20 percent of vehicle traffic. DOT's statistics show that over 40 percent of the Interstate is in barely tolerable or worse condition. Further, the federal Interstate preservation program, commonly known as the Interstate 4R program, is currently funded at $2.8 billion a year, but DOT estimates $4.2 billion to $5.5 billion will be needed annually through the year 2005 in federal funds for this program, if the federal cost share remains the same.

In addition, the number of deficient bridges on the federal-aid system has grown since 1982. Bridge deficiencies on the federal-aid system increased from about 70,000 to 77,000 from 1982 to 1988, according to DOT's statistics. Much of this increase is due to the rapid growth in deficient Interstate bridges. Federal statistics show an increase in deficient Interstate bridges from approximately 4,900 in 1982 to almost 8,200 in 1988.

Build-up in the Highway Trust Fund Balance

In the first 12 years of its existence, the trust fund balance remained at $1 billion or less. (See fig. 1.) After a rapid growth in the 1970s, the balance peaked at $12.6 billion in 1979. Through fiscal year 1989 the trust fund has accumulated revenues and interest totaling $219.6 billion and has made available $209 billion to the states. The current trust fund balance is $10.6 billion, with projections estimating a 1991 trust fund balance of $11.6 billion.

The effect of trust fund revenues and expenditures on the trust fund balance is illustrated in figure 2. The rear block represents income to the trust fund. From 1983 to 1989 income to the trust fund has generally increased. The center section indicates expenditures from the fund that were at times greater than, equal to, and less than income. The solid black section represents the trust fund balance, which illustrates the excess of trust fund income over expenditures.

Since the beginning of the trust fund in 1956, the interest earned has totaled $14.7 billion through 1989. In recent years, interest earned has ranged from $800 million to $1.1 billion per year. We see no distinction in revenues credited from user receipts and revenues credited as interest income in terms of the amounts to be made available from trust fund balances.

Reasons for the Build-up in the Highway Trust Fund Balance

The Highway Trust Fund balance exists, in large part, because of funds that are not obligated for highway projects. These unobligated funds occur for several reasons. (See fig. 3.) A primary reason accounting for the Highway Trust Fund balance is congressionally established obligation ceilings, which constrain the federal funds available for states to spend on highway projects. The funds that are restricted from states' use accumulate in the trust fund, contributing to the growth in the fund's balance. In fiscal year 1989, the Highway Trust Fund balance was $10.6 billion and ceilings accounted for approximately $8 billion of the balance.

Another explanation for the trust fund balance is that states did not obligate approximately $1 billion in funds they had accumulated that were exempt from obligation ceilings. State officials said they have held on to these funds primarily to protect themselves against an uneven flow of federal funds.

Obligations Ceilings Constrain States' Spending

The authorization of federal-aid highway funds is not a guarantee that those funds will be available for states to use in a given year. In the late 1960s, the administration instituted impoundments, which temporarily forced states to delay obligations. About a decade later, these impoundments were replaced by congressionally set obligation ceilings. The effect was the same--both restricted states from obligating the total amount of funds authorized.

For instance, in 1983 the obligation ceiling, set at \$12.4 billion, permitted states to spend close to the amount originally authorized by the Congress. In 1989 the obligation ceiling was set at approximately \$2 billion below the original authorization, according to DOT records.

To exacerbate the situation, the funds that are restricted from obligation in 1 year carry over to the next year. Although these unobligated funds could be made available in addition to new authorizations in the next year, newly imposed obligation ceilings restrict states from spending these funds. (See fig. 4.) The result is that the margin between funds that states may obligate as defined by the ceilings, and the funds that could be available for state spending, continues to widen.

If the states were permitted to obligate more federal-aid funds, several indicators point to states' ability to provide the necessary matching funds. I would like to make note of two such indicators--annual requests for additional obligation authority and states' use of a procedure that enables them to start projects without obligating federal funds. A redistribution of obligation authority occurs annually after August, at which time obligation authority released by some states is given to states requesting additional authority. For fiscal years 1987 through 1989, states requested between $2.4 billion and $2.8 billion in additional obligation authority, although approximately $800 million was actually available for redistribution. Over the 3-year period, states' requests totaled nearly $8 billion.

States are able to advance the construction of approved federal projects prior to receiving obligation authority. In essence, under advance construction procedures states use their own funds until additional federal obligation authority becomes available. When it does become available, states convert the projects to the appropriate federal program categories and funds are obligated to cover the federal share of project costs. Since 1987 the advance construction balance ranged between $2 billion and $2.6 billion.

Some Highway Programs Are Exempt
From Obligation Ceilings

The Congress also authorizes highway funds that it exempts from the obligation ceilings. When the Congress exempts programs from the obligation ceilings, it permits states to spend 100 percent of the funds authorized for that program. Exempt funds represent a small portion of the entire highway program. For instance, since 1983 the amount of funds not subject to obligation ceilings has ranged annually from approximately $700 million to $2.2 billion. The Congress may designate any number of programs as exempt and may change the categories from year to year.

The most significant exemptions from obligation ceilings, in dollar terms, are the minimum allocation program and demonstration projects. The minimum allocation program guarantees that states receive back at least 85 percent of their revenue contributions to the trust fund. In fiscal year 1990, 19 states received minimum allocation funds. Minimum allocation funds account for approximately 67 percent of the exempt funds in 1990, and demonstration projects account for 31 percent. The remaining 2 percent is comprised of a variety of small programs.

Although states are free to use all of these funds, the unused amount has grown from $0.2 billion in fiscal year 1983 to the fiscal year 1989 level of approximately $1 billion. (See fig. 5.) The bulk of this $1 billion is composed of minimum allocation funds, which, according to state transportation officials, are held by states as protection against an uneven flow of federal funds. Saving these funds is particularly attractive to states because minimum allocation funds may be used in a variety of program areas, unlike other highway funds, which are generally restricted to use within a specific road system.

The Fund Could Support a Higher Authorization Level

A common belief is that the trust fund balance represents a surplus. This view, however, is not accurate since the balance plus projected future revenues will be needed to cover commitments.

For instance, the fiscal year 1989 trust fund balance of $10.6 billion is needed to cover commitments (unpaid authorizations), but the trust fund balance is not sufficient to cover all outstanding amounts that were authorized through 1989. The authorized amounts outstanding, including those constrained from state spending through obligation ceilings, totaled about $31.6 billion in fiscal year 1989. Consequently, an apparent shortfall of $21 billion exists.

This situation, however, is permitted because when the Congress established the trust fund, it also established a safety mechanism to ensure that sufficient funds would be available to liquidate commitments at the end of each fiscal year. As revised by the Surface Transportation Assistance Act in 1982, the Byrd Amendment now permits the total projected commitments at the end of the fiscal year to exceed the trust fund balance so long as income projected for the following 2 years is sufficient to cover the difference.

In a May 1989 report to the Senate Appropriations Committee, we pointed out that the trust fund could support a higher level of program activity because future total revenues over the fund's authorized life are expected to exceed the level of future authorized commitments. At the time of our review, the anticipated amount of funds exceeding all commitments was $7.4 billion.

Federal transportation officials, however, believe that a safety cushion of between $1 billion and $3 billion would be necessary to guard against unforeseen disruptions to highway tax revenues or inaccurate revenue projections. Further, since the time of our review, $1 billion in Emergency Relief funds was authorized because of the highway and bridge damage caused by the October 1989 Loma Prieta earthquake in California. Assuming a conservative safety cushion of $3 billion and taking into account the additional $1 billion authorized, the trust fund could support $3.4 billion in additional authorizations.

Now I will address the Mass Transit Account of the Highway Trust Fund.

HIGHWAY TRUST FUND--MASS TRANSIT ACCOUNT

The Highway Revenue Act of 1982 established a special Mass Transit Account (MTA) in the Highway Trust Fund to fund several Urban Mass Transportation Administration (UMTA) grant programs, including the Section 3 Discretionary Grants and Section 8 Planning Grants programs. MTA receives revenues from 1 cent of the motor fuel tax. Through fiscal year 1991, MTA is expected to receive income of about $13.5 billion.

The Congress has provided permanent contract authority to obligate $10.4 billion of the $13.5 billion through fiscal year 1991. However, the annual appropriations process has placed limitations on obligations of the MTA funds to about $9.7 billion. Consequently, UMTA is not authorized to obligate about $3.8 billion.

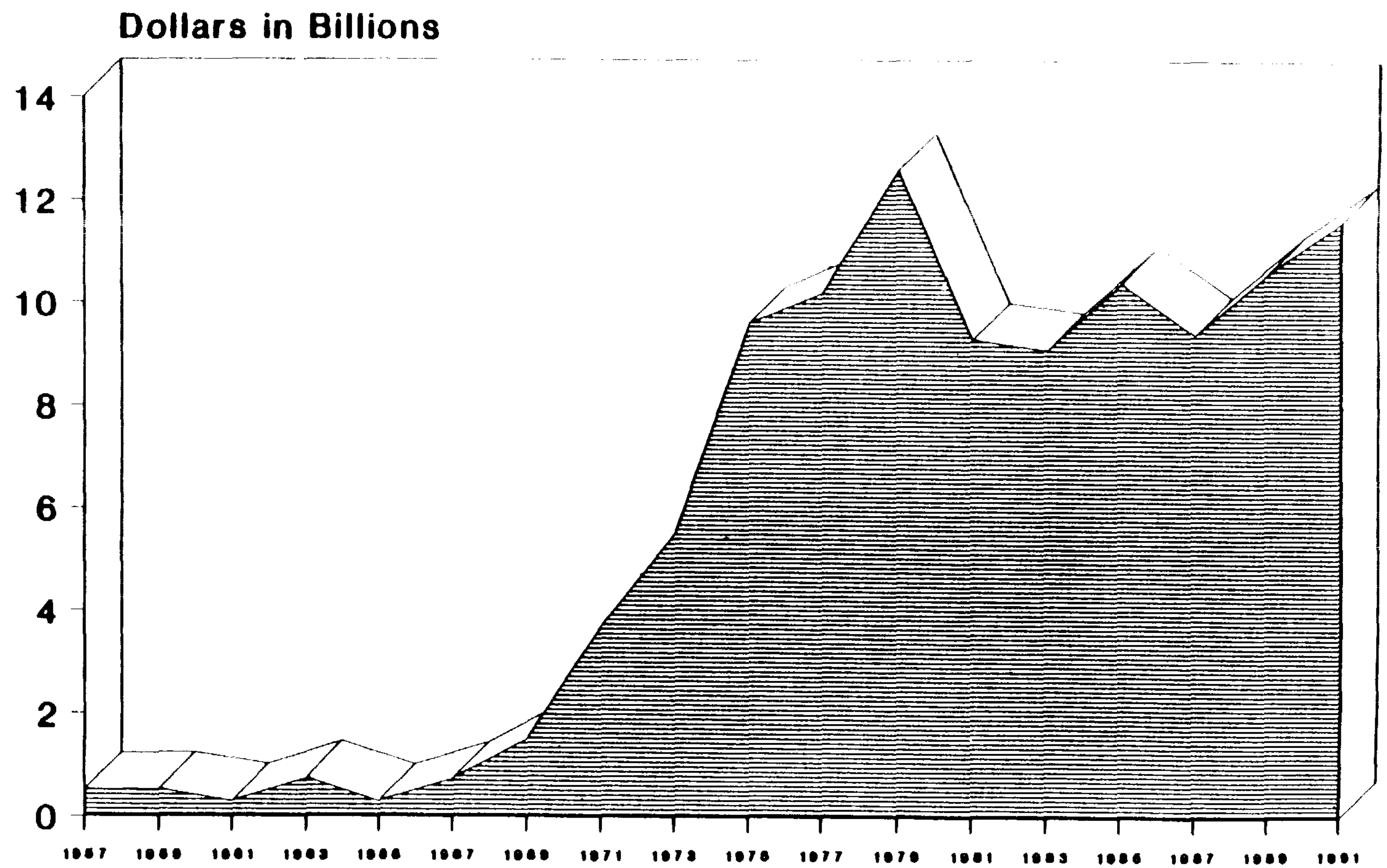
UMTA is expected to obligate all of the $9.7 billion MTA funds authorized to be obligated and to incur expenditures totaling about $5.7 billion through fiscal year 1991. Therefore, about $4 billion of the obligations are not expected to be funded at the end of fiscal year 1991. These obligations will not be funded because obligated funds remain available until expended, and expenditures for some projects, such as construction of new transit systems, are incurred over a number of years.

Finally, the MTA balance at the end of fiscal year 1991 is expected to be $7.8 billion. However, about $4.0 billion of this balance is committed to prior years' obligations that have not been funded. As previously discussed, the remaining MTA balance consists of the $3.8 billion funds not authorized to be obligated.

This concludes my testimony. I will be glad to answer any questions at this time.

Figure 1

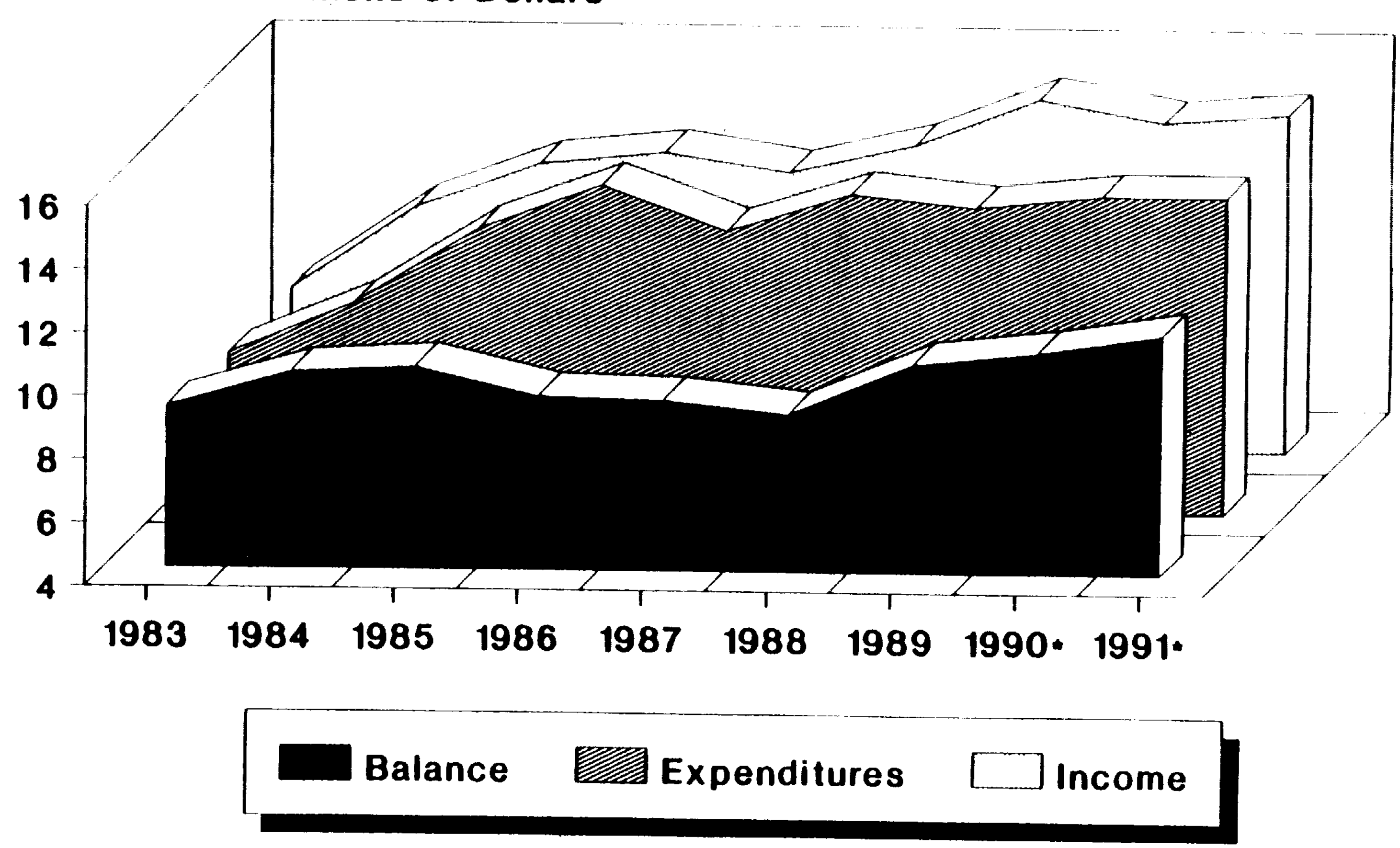
Highway Trust Fund Balance Growth
Highway Account-FY 1957-91*



*FY 1990-91 represent FHWA projections

Figure 2

Change in Highway Trust Fund Balance Highway Account-FY 1983-91



*Represents FHWA Projections

Figure 3

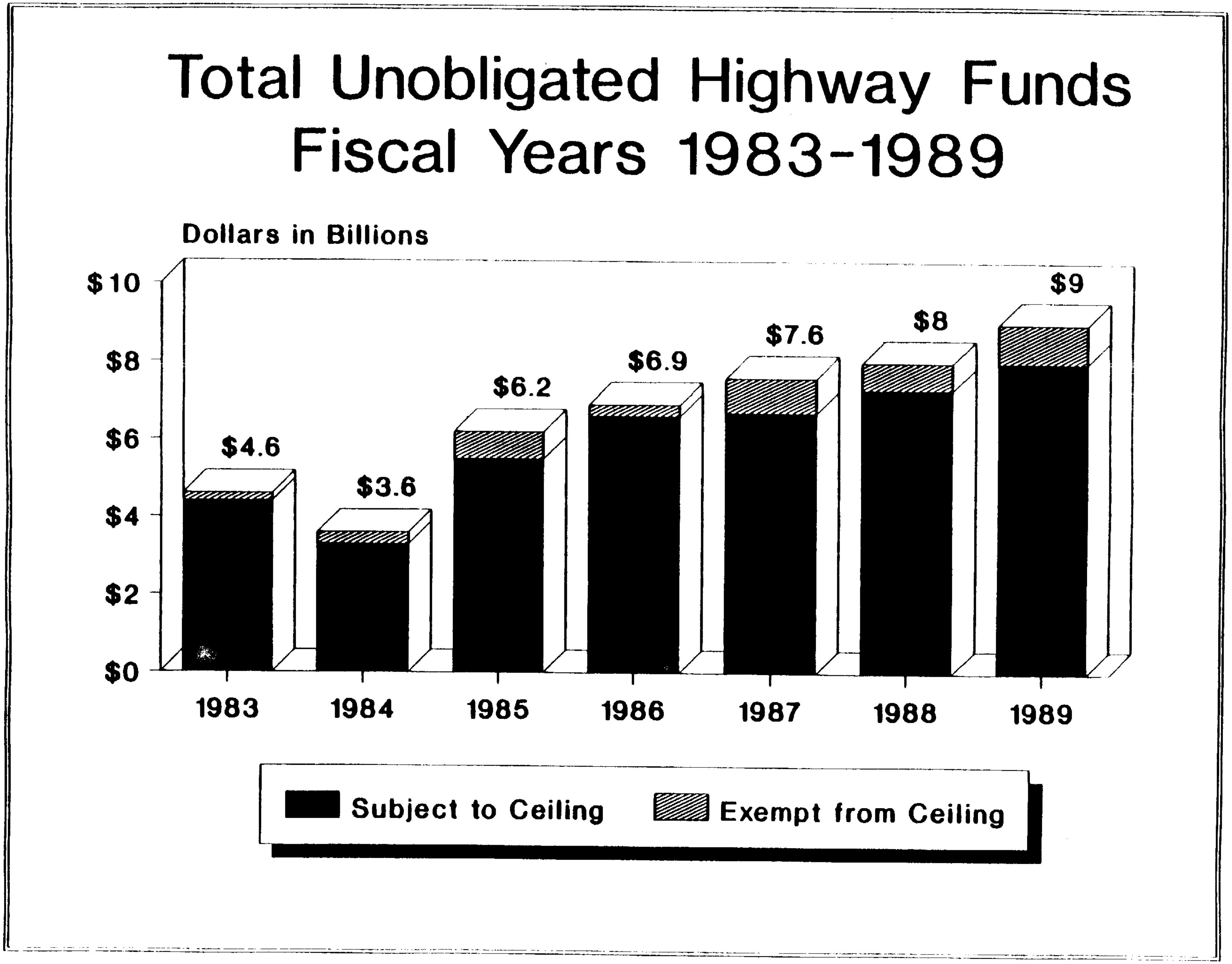
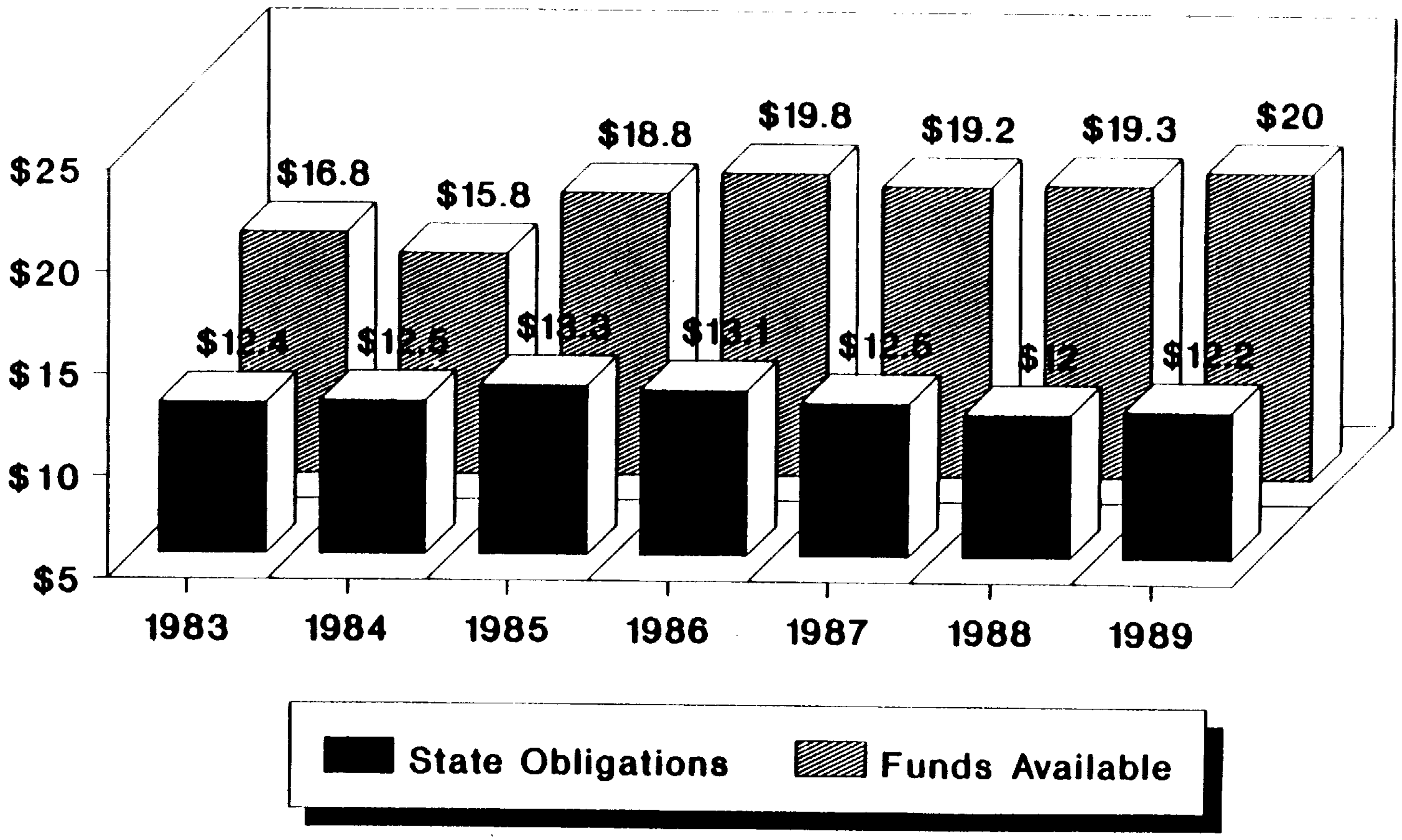

Total Unobligated Highway Funds
Fiscal Years 1983-1989
Dollars in Billions
$10
$8
$6
$4
$2
$0
$4.6
$3.6
$6.2
$6.9
$7.6
$8
$9
1983
1984
1985
1986
1987
1988
1989
Subject to Ceiling
Exempt from Ceiling

Figure 4

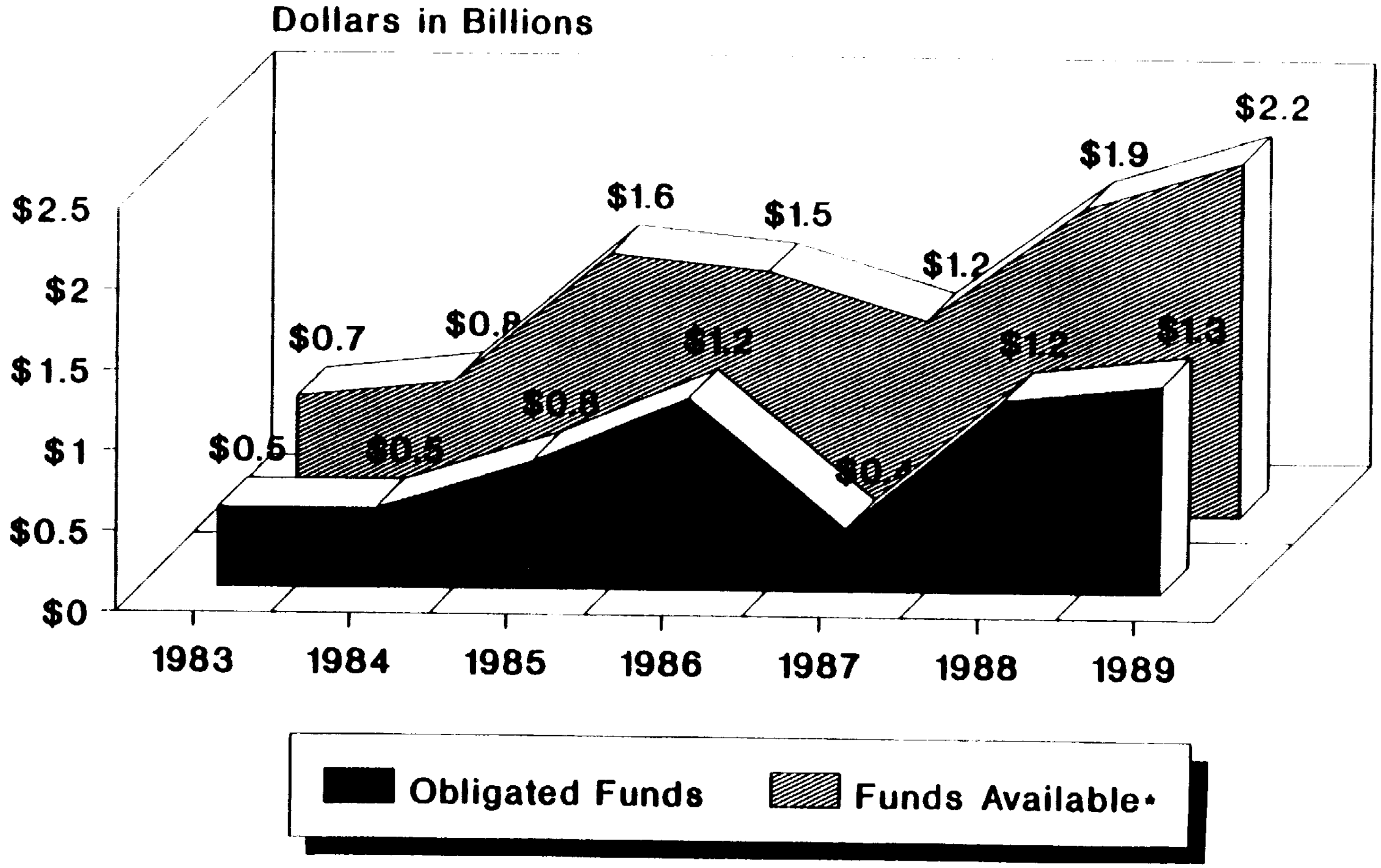
States' Expenditures of Available Funds* Fiscal Years 1983-1989



* Funds Subject to Obligation Ceiling

Figure 5

Obligation of Exempt Funds*
Fiscal Years 1983-1989



* Funds Exempt from Obligation Ceiling