The Heritage Foundation

BACKGROUNDER

No. 3552 | OCTOBER 29, 2020

GROVER M. HERMANN CENTER FOR THE FEDERAL BUDGET

A Transportation Agenda for 2021 and Beyond

David A. Ditch

KEY TAKEAWAYS

Federal infrastructure policy should empower states to meet their populations' unique needs, enhance the public good, and manage taxpayer dollars responsibly.

Too often, federal infrastructure involvement prioritizes political goals over Americans' needs and unnecessarily drives up costs.

Uncertainty about post-pandemic travel and commuting gives Congress even more reason to limit federal control, curb spending, and reduce regulations.

At the start of the 116th Congress, there was a sense that the divided government would find few areas of agreement regarding legislation. One policy issue that typically enjoys overwhelming bipartisan support is transportation and infrastructure, but even that has succumbed to dysfunction in Congress.

Congress has so far been unable to pass legislation to reauthorize spending from the Highway Trust Fund and water development projects performed by the Army Corps of Engineers. While Congress could still act on water development after the election, the highway bill was given a one-year extension as part of September's continuing resolution rather than a standard five-year reauthorization.[1]

Although this increases the workload for the 117th Congress, it also provides an opportunity for those

This paper, in its entirety, can be found at **http://report.heritage.org/bg3552**

The Heritage Foundation | 214 Massachusetts Avenue, NE | Washington, DC 20002 | (202) 546-4400 | heritage.org

Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

legislators to address the many dysfunctional aspects of federal infrastructure policy. There are ways to increase the value of America's public infrastructure stock without increasing the national debt or hiking up taxes for hard-working families. Congress should tackle three common federal infrastructure policy problems to make this happen.

Problem 1: Hidden Cross-Subsidies for Low-Demand Infrastructure

Most federal infrastructure spending flows from the Highway Trust Fund, the Airports and Airways Trust Fund, and the Harbor Maintenance Trust Fund. Currently, each of these funds is governed by statutes that use tax revenue generated from high-demand infrastructure to subsidize low-demand infrastructure.

The federal fuel tax is the primary source of the Highway Trust Fund.[2] In theory, this means that drivers are paying for the roads they use. However, roughly 28 percent of spending from the fund is diverted away from highways. The largest of these diversions goes toward urban transit systems, which do not pay into the fund. Other diversions include streetcars, bike paths, and walking paths, which also do not pay into the fund and should not be federal concerns. Over the past several decades, this has meant hundreds of billions of dollars in taxes on drivers to support non-driving infrastructure, even though the vast majority of U.S. travel takes place by car.[3]

Several aviation taxes fuel the Airport and Airway Trust Fund, which in turn provides grant funding to airports for infrastructure activity. Statutory formulas dictate most of the grant provisions, and on a per-passenger basis, the grants heavily favor low-traffic airports. This amounts to a transfer from large to small airports, with many airports contributing relatively little to the trust fund while receiving a substantial portion of grants.[4]

The Harbor Maintenance Trust Fund, which receives revenue from a tax on cargo ships, has a 10 percent set-aside for "emerging ports."[5] Although "emerging" typically implies growth, in this context, emerging ports simply means low traffic volume and guarantees a subsidy for small ports at the expense of busy ones.[6]

The cross-subsidies and transfers are not primarily driven by policy considerations, but rather by political ones. Infrastructure needs are not evenly distributed between states and localities, yet legislation requires broad support to pass into law. As a result, small airports and harbors receive special

treatment to win support from members whose districts lack large facilities, and urban members demand the transit set-aside since their constituents drive fewer miles than those in suburban and rural areas.[7]

Such political calculations reduce the value of federal infrastructure spending. Rather than prioritizing funding for infrastructure of genuine national need that would not happen without federal involvement, current infrastructure programs are designed to fund the greatest number of discrete projects in the greatest number of locations. Since high-use infrastructure provides the greatest return on investment, this approach is exactly backwards.

Solutions. Congress should remove diversions and set-asides within these infrastructure trust funds. This would include eliminating funding for transit and "transportation alternatives" in the Highway Trust Fund and reforming funding from the Airport and Airway Trust Fund and Harbor Maintenance Trust Fund so that they no longer heavily subsidize small facilities. Such changes would improve the financial health of the trust funds, potentially enable tax cuts, enhance the economic value of spending, and remove arbitrary and unfair transfers between individuals based on the type and location of infrastructure they use.

Achieving these policies will require a concerted effort that brings public attention to the inefficiency and political manipulation inherent in current federal infrastructure programs. An example of this is the movement that led to the reduction and eventual ban on earmarks, which became synonymous with waste and corruption.[8]

Problem 2: Wasteful and Unnecessary Federal Involvement in Infrastructure Projects

The most famous example of federal infrastructure is the Interstate highway system, which began with the Federal Aid Highway Act of 1956 and was completed in 1992. While the interstate system does provide significant benefits throughout the country, it is an anomaly when it comes to federal funding of infrastructure.

Most benefits from a typical infrastructure project go to people who live in the immediate area and use the infrastructure regularly. Accordingly, most infrastructure construction and operations are handled by state and local governments along with the private sector. It is rare for an infrastructure project to provide benefits to a wide enough area to necessitate federal involvement.[9]

Yet, the federal government currently funds every sort of infrastructure imaginable, often for projects as localized as sidewalks. This leads to a variety of inefficiencies.

In some cases, federal funding is enough to make a dubious project possible. The cost of a federally funded project is distributed over a larger number of federal taxpayers, and thus attracts less scrutiny than one funded at the local level.[10]

Federal funding is skewed toward initial construction over maintenance, which is typically covered by state and local governments. State and local officials have short-term incentives to seek federal funds for new projects, but this leads to rising maintenance costs over time.[11]

Federal funding for a project triggers several costly regulatory mandates. These include the Davis–Bacon Act, which requires inflated union-rate wages; project labor agreements, which dictate union-style work rules; and Buy American rules, which increase the cost of raw materials.[12]

Federal involvement prolongs completion for genuinely worthwhile projects. The process of applying for federal funds and obtaining necessary approvals can add months or even years to the completion date. A significant factor is the outdated and redundant National Environmental Policy Act, which adds costly roadblocks to the approval process even after reforms to streamline the process were implemented by the Trump Administration.[13]

While transportation needs vary significantly between regions and localities, federal policy too often involves a one-size-fits-all approach. This includes mandating transit spending nationwide despite the limited use of transit outside New York City.[14] Further, emerging trends, such as telecommuting, ride-sharing, and automated vehicles will change travel patterns in unpredictable and unevenly distributed ways. The federal government is less nimble and responsive to such changes than state and local governments or businesses, and thus should not have a primary role in infrastructure decisions.

Solutions. Congress should reduce federal infrastructure spending across the board and cut corresponding taxes on gas, aviation, and ports accordingly. This would empower non-federal actors that have better knowledge of local and regional needs. Congress should repeal the Davis–Bacon Act, Buy American rules, and the National Environmental Policy Act, which would reduce the cost of federally funded projects. The executive branch should repeal Executive Order 13502, issued by President Barack Obama, which mandates project labor agreements on federal projects.[15]

Problem 3: Federal Discouragement of State, Local, and Private-Sector Infrastructure Activity

In addition to cross-subsidies and red tape arising from federal infrastructure spending, there are several federal policies that make it more difficult for businesses and state and local governments to raise and spend their own funds.

States are barred from tolling Interstate highways, aside from a handful of legacy roads that were built before 1956. This ban forces states to rely heavily on gas tax revenue, which is problematic as hybrid and electric vehicles comprise an increasing share of automobiles.[16] The improving efficiency of electronic tolling means that tolls are much less expensive to implement than they were when the tolling ban was first imposed. Further, tolls are a better way to link the costs and benefits of a highway to its users, rather than gas tax increases that hit drivers regardless of their highway use.[17]

The federal government subsidizes state and local infrastructure activity by making interest on qualifying municipal bonds tax-free, which lowers federal revenue by tens of billions of dollars per year.[18] There is no limit on this subsidy. Tax-free interest is also available to private-sector surface transportation infrastructure activity through private activity bonds (PABs), which are capped at $15 billion in active bonds.[19] The value of this tax subsidy is $100 million per year, a minuscule amount compared to municipal bonds.[20] The structure of this lopsided federal subsidy makes infrastructure financing much more affordable for state and local governments than similar competing private-sector projects, serving to constrict private activity.

The federal government limits how airports can monetize their passengers in order to pay for infrastructure projects. Specifically, airports can only impose a Passenger Facility Charge (PFC) of up to $4.50 per person, which has been the case since 2000.[21] Critics of the PFC refer to it as a "tax," but it is in fact a user fee, which is the ideal way to pay for infrastructure. Further, airports face market pressures on pricing, such as competition with other modes of transportation (including nearby airports), meaning there would be natural limits on facility charges without the arbitrary federal cap. The $4.50 limit makes it harder for airports to properly finance activities, such as expansion and modernization, and serves to make airports dependent on federal subsidies from the Airport and Airway Trust Fund.

Solutions. Congress should lift the ban on states tolling Interstate highways, which would reduce state government reliance on Washington and on gas taxes. Congress should level the playing field between municipal bonds and PABs, which would most likely mean increasing or eliminating

the $15 billion limit on PABs.[22] Finally, Congress should remove the PFC limit, which would enable airports to expand and modernize in years to come. This should be coupled with a reduction in federal aviation taxes and spending.

Conclusion

While it might seem to some that the easiest way for the federal government to enhance the nation's transportation infrastructure is through an increase in spending and subsidies, the opposite is the best path forward. Many current rules and programs are badly outdated, or serve primarily to enhance political goals rather than the public good, creating tremendous cost and inefficiency. Reducing federal spending and regulation would create space for the private sector, and state and local governments, to increase the quality and capacity of transportation infrastructure that Americans need most.

David A. Ditch is Research Associate in the Grover M. Hermann Center for the Federal Budget, of the Institute for Economic Freedom, at The Heritage Foundation.

Endnotes

1. Public Law No. 116–159, H.R. 8337, Continuing Appropriations Act, 2021 and Other Extensions Act, 116th Congress, https://www.congress.gov/bill/116th-congress/house-bill/8337 (accessed October 20, 2020).
2. The Highway Trust Fund currently operates at a deficit, and Congress has used general fund transfers to fill the gap. However, highway fund diversions long predated the deficits. See David A. Ditch, Nicolas D. Loris, Adam N. Michel, and Kevin D. Dayaratna, "Paying for Surface Transportation Infrastructure: Four Wrong Routes, Four Good Paths," Heritage Foundation *Backgrounder* No. 3422, July 17, 2019, https://www.heritage.org/budget-and-spending/report/paying-surface-transportation-infrastructure-four-wrong-routes-four-good.
3. Randal O'Toole, "Transportation Costs and Subsidies by Mode," The Antiplanner *Policy Brief* No. 20, September 17, 2019, http://ti.org/antiplanner/?p=16441 (accessed October 20, 2020).
4. Michael Sargent, "End of the Runway: Rethinking the Airport Improvement Program and the Federal Role in Airport Funding," Heritage Foundation *Backgrounder* No. 3170, November 23, 2016, https://www.heritage.org/transportation/report/end-the-runway-rethinking-the-airport-improvement-program-and-the-federal.
5. Congressional Research Service, "Distribution of Harbor Maintenance Trust Fund Expenditures," September 10, 2020, https://crsreports.congress.gov/product/pdf/IF/IF11645 (accessed October 20, 2020).
6. Emily Goff, "House Water Resources Bill: Shortcomings Threaten to Overshadow Reforms," Heritage Foundation *Issue Brief* No. 4048, September 17, 2013, https://www.heritage.org/environment/report/house-water-resources-bill-shortcomings-threaten-overshadow-reforms.
7. The origins of the Highway Trust Fund's transit account stem from legislative fights in the late 1970s and early 1980s. As the country became more urbanized, urban members began to wield more power, especially in the House. The 1982 gas tax increase included the creation of a transit account within the trust fund specifically to secure urban support. See Jeff Davis, "Reagan Devolution: The Real Story of the 1982 Gas Tax Increase," Eno Center for Transportation, September 9, 2015, https://www.enotrans.org/wp-content/uploads/Reagan-Devolution-The-Real-History-of-the-1982-Gas-Tax-Increase.pdf (accessed October 20, 2020).
8. Justin Bogie, "Earmarks Won't Fix the Broken Budget and Appropriations Process," Heritage Foundation *Backgrounder* No. 3353, September 20, 2018, https://www.heritage.org/budget-and-spending/report/earmarks-wont-fix-the-broken-budget-and-appropriations-process.
9. David A. Ditch and Nicolas D. Loris, "Improving Surface Transportation Through Federalism," Heritage Foundation *Backgrounder* No. 3450, November 12, 2019, https://www.heritage.org/budget-and-spending/report/improving-surface-transportation-through-federalism.
10. Ibid.
11. Ibid.
12. Ibid.
13. Diane Katz, "Curbing Abuses of a Politicized NEPA," Heritage Foundation *Backgrounder* No. 3524, August 25, 2020, https://www.heritage.org/government-regulation/report/curbing-abuses-politicized-nepa.
14. Randal O'Toole, "Transit's Dim Future," The Antiplanner *Policy Brief* No. 39, February 11, 2020, http://ti.org/antiplanner/?p=16817 (accessed October 20, 2020).
15. Presidential Documents, "Executive Order 13502 of February 6, 2009: Use of Project Labor Agreements for Federal Construction Projects," *Federal Register* Vol. 74, No. 27 (February 11, 2009), p. 6985, https://www.govinfo.gov/content/pkg/FR-2009-02-11/pdf/E9-3113.pdf (accessed October 20, 2020).
16. While some states might opt to shift to a vehicle-miles-traveled tax to pay for roads, implementing such a system at the federal level would be a mistake. See Ditch, Loris, Michel, and Dayaratna, "Paying for Surface Transportation Infrastructure: Four Wrong Routes, Four Good Paths."
17. Ditch, Loris, Michel and Dayaratna, "Paying for Surface Transportation Infrastructure: Four Wrong Routes, Four Good Paths."
18. Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2019–2023," December 18, 2019, https://www.jct.gov/publications/2019/jcx-55-19/ (accessed October 20, 2020).
19. Congressional Research Service, "Infrastructure Finance and Debt to Support Surface Transportation Investment," November 16, 2016, https://crsreports.congress.gov/product/pdf/R/R43308 (accessed October 20, 2020).
20. Joint Committee on Taxation, "Estimates of Federal Tax Expenditures for Fiscal Years 2019–2023."
21. Marc Scribner, " Modernizing the Passenger Facility Charge to Increase Airport Investment, Reduce Federal Spending, and Save Travelers Money," Competitive Enterprise Institute, August 13, 2019, https://cei.org/content/modernizing-passenger-facility-charge-increase-airport-investment-reduce-federal-spending (accessed October 20, 2020).
22. Ideally, the interest exclusion should be eliminated for both municipal bonds and PABs. Expanding the subsidy to private-sector activity is a second-best alternative that should be done in conjunction with limiting PAB-eligible projects to those that directly compete with public-sector alternatives.