



Alternatives to Raising Gas Taxes

Acknowledgements

We understand that continual improvements in fuel economy and the development of hybrid and electric vehicles have reduced the real value of nominal revenues from traditional gas taxes. We also acknowledge that a properly designed gas tax is among the least destructive of taxes: if revenues are used strictly for road construction and maintenance, and not diverted to other projects, a gas tax comes somewhat close to acting like a user fee. That said, for many reasons we will outline below, we believe that gas tax increases or other transportation-related tax increases are not warranted in Arizona at the present time. (Also, given that many transportation projects in Arizona are federal-state and federal-local ventures, it is important to include in this discussion federal reforms that would improve the use of existing federal gas tax revenues and utilize private-sector investment to accomplish those projects.)

Gas tax dollars and other transportation revenues should be used for roads.

Our existing gas tax dollars at the federal and state levels should be dedicated to improving mobility, congestion, and safety on our highways, roads and bridges. Instead of increasing gas taxes, which fall hardest on the least fortunate, legislators should stop diverting gas tax dollars to non-essential and wasteful projects and use those dollars to pay for roads and bridges. As much as 28 percent of federal gas tax revenues are diverted to spending on items such as regional planning bureaucracies, bike and pedestrian trails, vegetation management, historic preservation, and transit.

Sadly, even within the category of roads and bridges, our governments often squander our transportation resources on pork-barrel projects. Perhaps the most famous recent federal boondoggle was the “Bridge to Nowhere” in Alaska. In Pima County in 2015, one of the bond proposals would have funded a new road that looked to many observers to be a personal driveway to a politically-connected developer's industrial park property. The majority on the Pima County Board also diverted road project money out of the district of a dissenting board member.

Here in Arizona, governments routinely divert gas tax money and other transportation revenues to many projects that do not serve the purpose of increasing mobility on our roads. For example, according to an Arizona Free Enterprise Club study, Phoenix spent \$110 million per mile to build light rail, despite the fact that light rail is mainly a substitute for more economical and flexible bus transit options, and despite the fact that according to Valley Metro's own projections, light rail removes less than one car in a thousand from traffic. The Club also estimated that Phoenix light rail had operating losses of over \$10 million per year.

Increases in road spending should be offset by savings in other areas.

The construction and maintenance of roads are core traditional functions of government, in part because they attempt to solve long-recognized and sometimes difficult-to-solve public-good holdout and free-rider problems. Unfortunately, many governments in modern America do not prioritize roads. Beyond misallocating existing gas tax and other transportation revenues, governments routinely spend huge amounts of money -- including most of the federal government's \$4 trillion budget -- on programs that are not core functions of government addressing traditional public-good problems. America's federal transportation budget in FY 2016 was \$75 billion -- or less than two percent of the entire federal budget.

Out of a \$1.3 billion county budget for FY 2018, Pima County allocated only \$44 million (less than four percent) to transportation maintenance and operations. All capital expenditures were \$131 million, of which only \$70 million was nominally dedicated to transportation (and some of the named road projects may hide non-automobile related capital items). Out of the \$1.3 billion total county budget, the \$114 million allocated to transportation represents less than ten percent. Meanwhile, Pima County planned to spend: \$42 million on libraries; \$41 million on behavioral health; \$12 million on "community development," "neighborhood conservation" and "community services"; \$9 million on animal care; \$5 million on a stadium district; and, \$256 million allocated in a broad category called "Non Departmental." In that context, it appears that roads are not really a priority for the majority on the Board of Supervisors of Pima County.

Listed below are several policy options local governments can use to improve the efficiency of operations. Each government service is different, and so policymakers must choose the reform that makes the most sense in the policy

context. But in general, AFP-Arizona believes that the options get better as you move down the list from contracting out to full privatization:

- Contracting Out This is the most common of private-sector alternatives. If a function of government is currently being performed by city employees, the city can often save money and get better service by using a competitive bidding process to contract that function out to the private sector. It is imperative that local governments procure, write and manage contracts carefully, to ensure that short-term contractors provide maximum value at minimal cost.
- Voucherization Vouchers empower consumers with public monies to choose among a wide variety of competitive private companies. Voucherization is often better than contracting out, which potentially creates monopolies in need of careful supervision by local government managers. For example, the current contractor managing Dial-A-Ride in Phoenix is providing poor service at a very high cost. By giving disabled citizens vouchers for ridesharing services such as Uber and Lyft, Phoenix could benefit them by more than doubling the miles they can travel, reducing ride times by hours every week, and obviating the need to schedule rides a day in advance.
- Long-Term Private Concessions A great way to transfer financial risk away from taxpayers and onto private-sector companies is to competitively bid out the management of public infrastructure assets such as parks, water facilities, wastewater facilities, and parking assets to long-term private concessionaires. (For much more about private concessions for roads, see the final section below.) For example, a concessionaire could operate a restaurant or a coffee shop in a public park for multiple years, in return for taking on the responsibilities of park maintenance and improvement. Governments must write and manage concession contracts carefully to ensure that concessionaires' incentives are properly aligned with customer service. If any concessions involve large upfront payments to local governments, the windfalls should be used to pay down unfunded pension liabilities, pay down general obligation debt, or invest in infrastructure maintenance.
- Decentralization Another good option for getting functions off budget, and to make those functions more responsive to the needs of local citizens, is to turn them over to neighborhood associations. For example, in municipalities around the country, city parks and city streets have been deeded to neighborhood associations. Further, local governments should allow master-planned communities to provide

nearly all public goods related to new developments (including abutting arterial and connector streets), rather than collecting impact fees and then bidding out construction and maintenance contracts to politically-chosen contractors.

- Full privatization In many cases the best option is for governments to avoid taking on any new government functions, and wherever possible, to discontinue existing functions through full privatization and divestment of assets. Although privatization often involves the sale of assets to private companies, privatization can also mean turning functions over to volunteers or to nonprofit groups. For example, many municipalities around the country enlist volunteers to assist police with traffic control and parks and recreation with graffiti removal. In other cases, cities have turned over the ownership and management of parks, zoos, museums, and other cultural or recreational amenities to nonprofit organizations.

Governments should reduce regulatory burdens on infrastructure projects.

By streamlining and rolling back overly burdensome regulations, permitting processes, and other red tape, governments -- especially the federal government -- can reduce unnecessary delays, speed up construction and lower costs for taxpayers, consumers, workers and businesses. These burdens unnecessarily hamper innovation and hamstring infrastructure planning, permitting, and construction. Listed below are several measures Congress and federal agencies can enact to reduce the regulatory burdens the currently stand in the way of the timely implementation of infrastructure projects.

- The federal authorities should free up States to provide infrastructure by granting additional flexibility for use of federal highway funds, and even devolving responsibility for some or even all highway infrastructure.
- Governments should eliminate duplicative planning, analysis, and approval for infrastructure projects. Federal projects typically require duplicative steps from multiple federal agencies in addition to steps imposed by state and even local governments. This can unnecessarily delay the launch of projects by years.
- Federal legislation such as the National Environmental Policy Act (NEPA) often adds unnecessary hurdles to the permitting and approval process, driving up costs and delaying projects. State and local NEPA analogs -- including plans such as the Sonoran Desert Conservation Plan -- often compound the federal regulatory and permitting burdens.

- Corporate welfare regulations limit competition and often lead to costly delays that make projects more expensive.
- Federal corporate welfare for unions -- such as Davis Bacon, prevailing wages laws, and project labor agreements -- should be eliminated. Project labor agreements between government entities and contractors set wage and benefit levels, include benefit guarantees, and often include hiring controls by unions. Any non-union workers hired under such agreements are then forced to pay union dues. All of these measures inflate the costs of transportation projects. (These privileged arrangements for union workers are notable, since only about 15 percent of all private workers are unionized.) Ending these special-interest programs would improve competition, lower costs and improve quality. And it would improve and increase opportunities for American workers who are either excluded from or forced to pay for these union carve-outs.

Private investment should be unleashed to build new infrastructure capacity.

Private capital has immense untapped potential to build new infrastructure, financed by user revenues. Private concessions for the construction, maintenance and operation of roads are often able to provide road services for less than half the life-cycle cost of the normal process.

Problems with the Current System

Perhaps the most important reason we should not raise taxes to pay for transportation infrastructure is that the *way* we finance transportation projects has a huge influence over what kind of projects will get built. The main problem with imposing a new transportation tax of any kind is that politicians and government bureaucrats will end up deciding what is built.

The basic reason politicians and bureaucrats waste so much of our tax money, in so many areas of government, is that they are spending other people's money. In their attempts to satisfy different constituents, politicians and transportation bureaucracies often end up using our tax money to build wasteful projects. The proper goal of our transportation infrastructure system is to spend the least amount of money to move the greatest number of people, while doing the least damage to the environment. Yet, the political process gives us a lot of very expensive

projects (such as light rail transit) that do not move the greatest number of people at the lowest cost.

Another problem is that roads built with tax money tend to come in way over-budget and way past deadline. ADOT and local governments and regional transportation authorities do try to build in bonuses for contractors who get roads built quickly, but the bonuses do not work very well, because ultimately, the bureaucrats still get the same paychecks, whether roads are built quickly or not. In an ideal world, transportation bureaucrats would make more money when they do a good job of increasing mobility, and they would get less money when they do a bad job. But that's not the way the system works.

Look at the Route 202 loop in the Phoenix Valley. It was supposed to be completed under the first half-cent county sales tax, which began in 1985. In 2005, when the first tax ended, the loop was still not complete. Only now, over 30 years later, has work begun on the South Mountain part of the loop. Indeed, it is difficult to think of very many transportation projects that have actually come in on-time and on-budget.

Also, too many of our tax-funded roads are poorly built, and have to be repaired often. But if you think about it, there is no reason for contractors to do otherwise. If roads have to be repaired, many of the same contractors will get repair contracts, and government bureaucrats will continue to collect paychecks. So in the typical government system, badly built roads often mean revenue security for contractors and job security for bureaucrats.

When we compare the life-cycle costs of typical design-bid-build tax-funded roads with toll concession roads, we find that toll concessionaires manage to build, operate, and maintain roads for much less money — sometimes as little as one-third the total cost. It is clear that much of the huge life-cycle cost savings from long-term toll concessions comes from the decisions by private concessionaires to build with thicker pavement and with other more durable structures, in order to avoid future revenue losses due to repairs.

Public-Private Partnerships

As an alternative to tax-funded financing schemes, we are proposing the use of public-private partnerships (P3s) that allow for private companies to finance, construct, operate, and maintain new transportation projects. Public-private partnerships are used for road infrastructure in dozens of countries around the

world and several States here in the US. For one among many examples, the French equivalent of the Interstate Highway System at this point is mostly privatized.

Under a public-private partnership, the government grants a long-term user fee or toll road concession to a private company. In return, the company brings in the private capital needed to build, maintain, and operate the road. Under most partnerships, the road remains the property of the government.

When a private company brings in hundreds of millions, or billions, of dollars of private capital to build a project, and when it depends solely upon tolls for income, that company faces some very different incentives than the political system does. For starters, private companies will only choose road projects that involve moving large numbers of people. Therefore, their incentives are aligned so as to provide the maximum amount of congestion relief for the entire system. If a private company is looking at building an I-10 bypass route around Tucson, it will bargain with ADOT and other governmental entities to get a route that will attract the maximum number of drivers. By doing so, the new road will pull drivers, including interstate truckers, off of I-10. That will provide maximum congestion relief for the drivers who are still on I-10.

Further, a private company wants to build a road quickly, so that it can start collecting tolls as soon as possible, and it wants to build the road well, so that it will not lose profits while lanes are under repair. Again, that is one of the main reasons why the life-cycle costs of toll roads are a fraction of the life-cycle costs of typical government roads. When repairs do need to be made, the company wants to make those repairs efficiently and effectively, so that drivers don't get into the habit of using a different roadway.

Private companies are also much more inventive than bureaucracies when it comes to problem-solving. For three decades, the French government faced a political impasse over how to finish the A86 beltway around Paris. The problem was that the road needed to go around the Palace of Versailles, but there were issues with all of the various proposed routes. A private company finally cut through the Gordian knot by proposing a toll concession to build a double-decker tunnel underneath the palace.

Best of all, public-private road partnerships could bring tens of billions of dollars to Arizona. A decade ago, former US Transportation Secretary Mary Peters

estimated that over \$400 billion in worldwide capital was available for transportation infrastructure projects in America. That number is even higher now.

Further, public-private partnerships are more robust than government bonding. Not only do governments face caps on the total amount of bonded debt, but the private sector can mobilize more capital for a given road project than traditional tax-exempt financing. The tax-exempt debt markets hold governments to very conservative standards, which limits the amount they can raise for any given project cash flow. But private firms are able to take on more risk and can be less conservative in their projections of future traffic, so they're able to generate more capital for a given project, all things being equal. And it is the private companies — not taxpayers — that take the hit if the traffic and revenue projections are off.

Modern electronic tolling technology makes road pricing, including variable pricing, very easy. With transponders, or using cellphone networks, drivers no longer have to stop at toll booths. We already have express toll lanes (or high-occupancy/toll "HOT" lanes) for congestion relief in Orange County, Denver, Minneapolis, San Diego, and the Capitol Beltway area around Washington, DC.

Finally, a major advantage of public-private partnerships is fairness. We should all be able to agree that people should pay for what they use. With private, toll-based financing, you get a system in which people pay for what they use.

While private-sector solutions are readily available for freeways and for neighborhood streets, the major challenge to the private-sector provision of roads currently is arterial and connector streets. Arterial and connector streets can be easily privatized where they abut new master-planned communities, but their provision in older parts of town is subject to trickier economic and political problems. In the near term, tax financing will continue to be necessary for legacy arterial and connector streets, though it would be best to move toward taxes (such taxes are sometimes called "rentals" or "leasehold rents" in the transportation studies literature) that more accurately match local property owners with the roads from which they benefit.

General Guidelines for P3 Projects

AFP-Arizona does not support the collection of tolls on existing roads that have already been built with taxpayer dollars, because that could be a form of double-taxation. Any funds coming back to the government from tolls or leases should not be used for new, unrelated government spending, but to maintain and improve

portions of the existing road system -- such as many legacy arterial and connector streets --- that are not easily converted into P3s. Further, toll road concessions should be designed so as to avoid imposing new burdens on local residents, by giving them pre-paid toll accounts or tax rebates. (On interstate freeways, P3s can also offer interstate truckers access to low-tax gasoline.)

AFP-Arizona also urges governments commissioning road projects -- whether under the standard or P3 models -- to avoid committing eminent domain abuses. One of the great things about private toll road builders is that they want to minimize their costs, including the cost of acquiring right-of-way, so very little land is actually condemned in most P3 road projects. Concessionaires know that every day their projects are not operational is a day that they're not earning their money back, so they have more incentive and flexibility than government entities to negotiate attractive deals with landowners. Concessionaires essentially act as agents of the government to negotiate and cut checks to landowners, but they are subject to all of the same procedural and constitutional protections in the existing right-of-way acquisition process. The main difference is that they can cut deals on the spot and can pay much more to landowners than a government entity may be allowed to.

As with other kinds of contracting out and concession granting, it is imperative that governments procure, write and manage P3 road contracts carefully, to ensure that contactors provide maximum value at minimal cost.

Barriers to P3 Infrastructure Development

To conclude, the current system of tax-financed infrastructure is a dead-end road. The more quickly we move away from tax financing, the better we are going to be able to solve our congestion, mobility, and pollution problems.

Unfortunately, governments are moving slowly to utilize private-sector capabilities. Although Arizona passed P3 enabling legislation in 2009, ADOT has not yet moved forward with any projects. And there are presently numerous federal governmental restrictions that prohibit or limit private investors from operating and/or owning infrastructure. For example, Arizona is not allowed to toll new lane-miles on interstate highways or to commercialize interstate rest stops. These two barriers demonstrate the federal aversion to allowing the benefits of private enterprise in traditional public infrastructure. Federal legislators should remove these restrictions, while maintaining an appropriate level of oversight.