



RESTORE AMERICA'S TRANSPORTATION PROGRAM TO A USER PAY SYSTEM

Despite favorable recommendations from a series of congressional and presidential commissions, resistance to raising fuel excise tax rates is long-standing, bipartisan and persistent whether fuel prices are high or low and whether the economy is booming or suffering a downturn. We need to break free of this revenue stalemate.

CONCEPT

Replace the current federal excise (per gallon) taxes on gasoline and diesel fuel with a fixed sales tax initially set on a revenue-neutral basis. At a national average price of $3.00 per gallon for gasoline, the sales tax rate would need to be about six percent (it would need to be about eight percent for diesel since that fuel has a higher federal excise tax rate).

This solution meets three critical tests:

> It does not raise taxes.

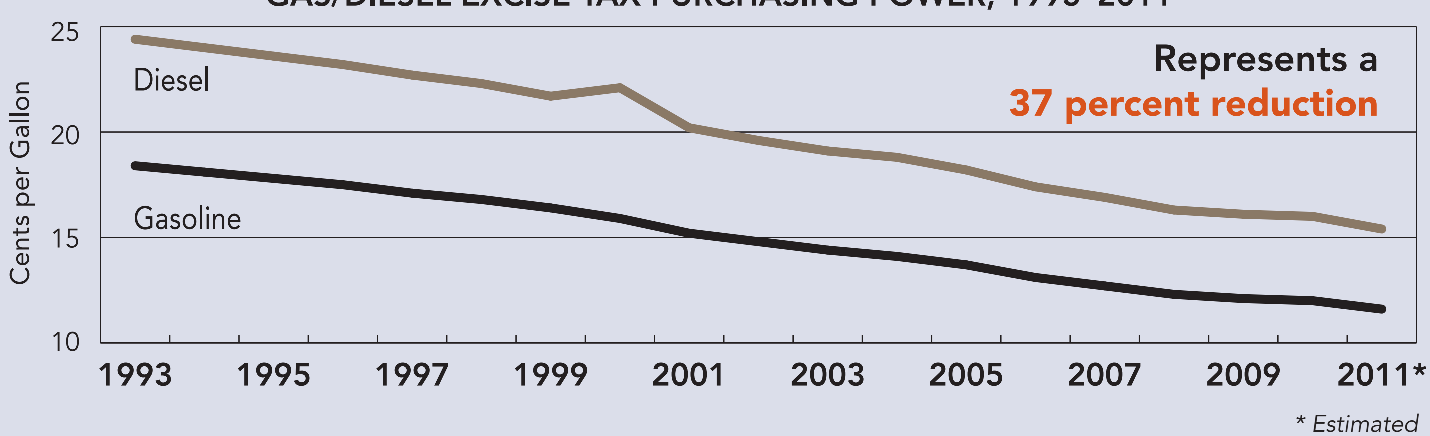
> It does not worsen the federal deficit.

> The central question before the American people is how to sustain our legacy of leadership — in economic opportunity, technological innovation, and quality of life — for a new century that presents daunting economic and national security challenges.

> It has a demonstrated potential to fund the federal surface transportation program in the future.

The federal excise taxes on gasoline and diesel fuel are responsible for about 90 percent of the revenue deposited annually in the Highway Trust Fund (HTF), the main source of funding for the federal highway and transit program. The current excise tax rates of 18 cents per gallon on gasoline and 24 cents per gallon on diesel fuel have not been adjusted by Congress since 1993 — nearly two decades ago.

GAS/DIESEL EXCISE TAX PURCHASING POWER, 1993–2011



Congress can simultaneously address the immediate crisis in transportation funding and help reduce the nation's fiscal deficit as well.

TIMELINE AND DEADLINE

- 2008–2010: $35 billion General Fund transfers to the Highway Trust Fund
- September 30, 2009: SAFETEA expired
- March 2011: Most recent SAFETEA extension expires
- March 2012: Highway Trust Fund projected to become insolvent

Revenues from the federal fuel tax are no longer sufficient to meet the obligations of the Highway Trust Fund (HTF), and additional public funding is needed. Although private capital can play a larger role in delivering future transportation improvements, much of the HTF's obligation involves rehabilitating the existing transportation system — an area unlikely to attract private dollars seeking a return on invested capital.

TRANSPORTATION'S TWIN CRISES

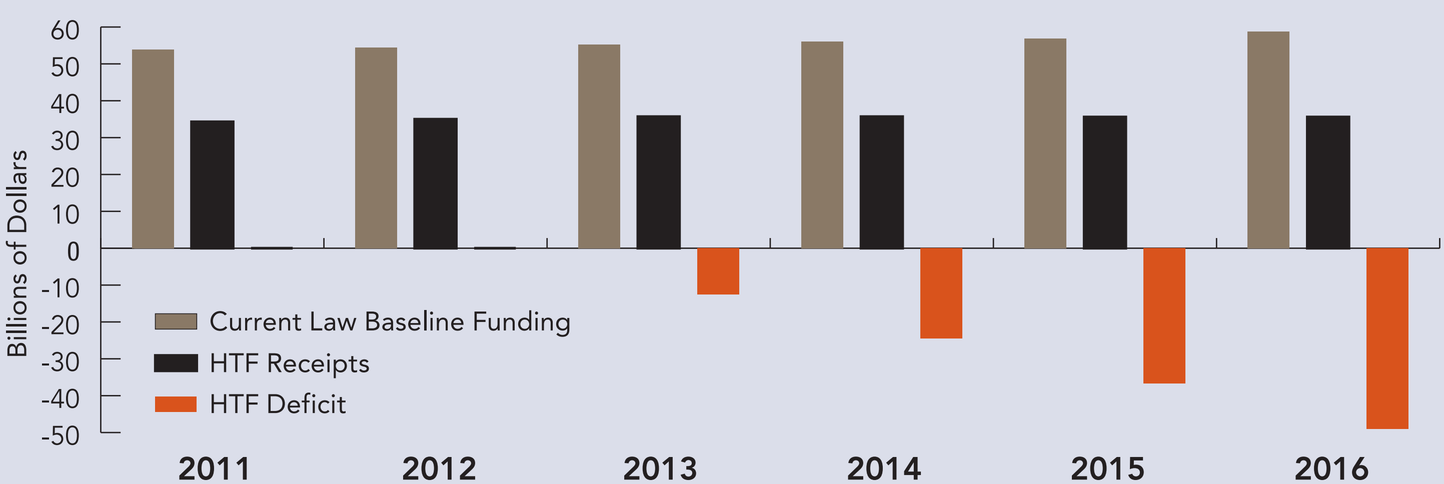
1. The Highway Trust Fund's revenue stream cannot meet current authorized levels and has become dependent on General Fund bailouts. Congress has transferred $35 billion from the general fund in 2008 and 2009 to maintain the existing program through 2011.

2. Even current authorized levels are insufficient to maintain our infrastructure in good repair, let alone provide for 21st Century improvements.

In recent years, two separate, bipartisan commissions[1], impaneled by Congress in the passage of SAFETEA in 2005, examined this issue and concluded that it would be necessary to increase federal-highway user fees to generate the funds needed to maintain the federal highway network.

Both panels, the National Surface Transportation Policy and Revenue Study Commission and the National Surface Transportation Infrastructure Financing Commission, identified a higher gas tax — after evaluating 30 possible options — as the only plausible alternative for increasing revenues in the short term. Yet, Congressional resistance to this approach remains strong.

GAP BETWEEN BASELINE FUNDING AND HTF RECEIPTS



1 *Transportation for Tomorrow*, report issued in 2007 by the National Surface Transportation Policy and Revenue Study Commission; and *Paying Our Way: A New Framework for Transportation Finance*, report issued in 2009 by the National Surface Transportation Infrastructure Financing Commission.

A NEW APPROACH: SALES TAX CONVERSION

One way out of the current revenue stalemate would be to convert the fuel excise taxes to a sales tax on fuel, initially on a revenue-neutral basis. Because the price of fuel can vary, Congress could establish a floor and a ceiling for funds generated by the sales tax to flow into the HTF.

- A floor would be the authorized highway and transit funding levels, and would be guaranteed by limited infusions from the General Fund if necessary.
- A ceiling would establish an upper range for sales tax generations to the HTF in case of dramatic escalations in the price of fuel.

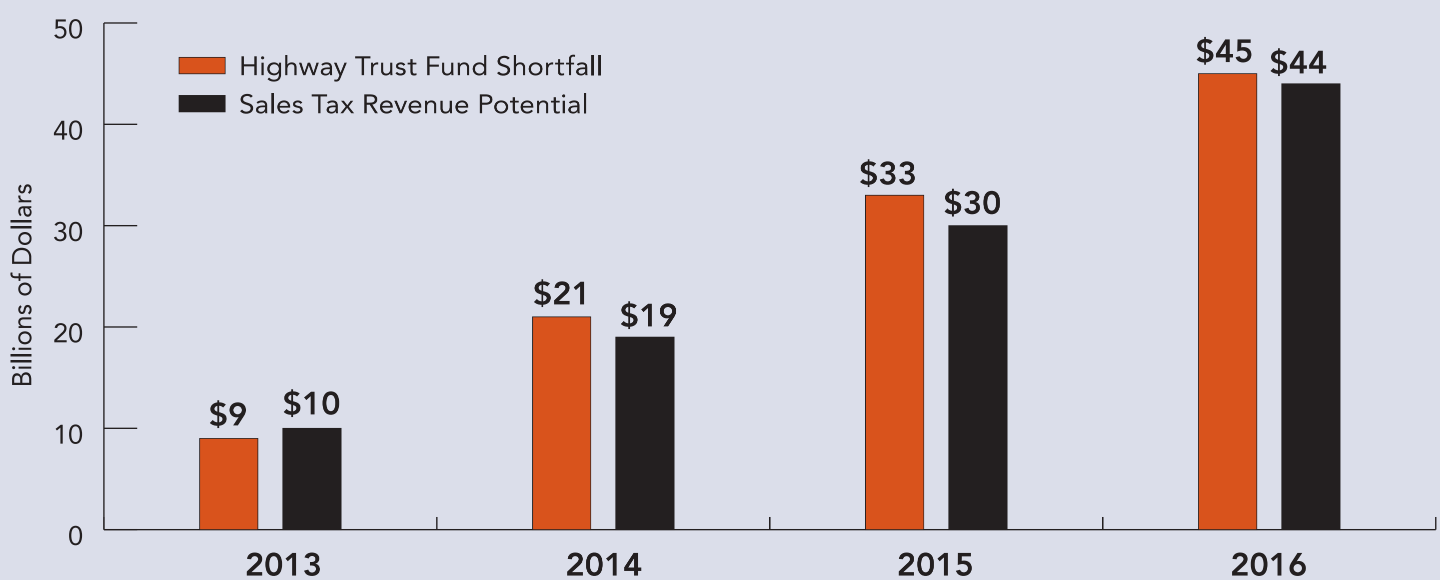
Amounts between the floor and ceiling could function similar to revenue-aligned budget authority (RABA) for transportation projects under current law. Amounts in excess of the ceiling would spill over into the General Fund to reduce the federal deficit. Accordingly, the General Fund would cover the downside price risk for the HTF, but would benefit from the upside price potential above the ceiling.

On a revenue-neutral basis in the first year, revenues are expected to be unchanged. As fuel prices increase according to U.S. Department of Energy forecasts over the next six years, cumulative revenues flowing into the Highway Trust Fund by 2016 would increase by $44 billion as compared to the current excise tax.

The chart below compares the Highway Trust Fund shortfall (the difference between authorized spending amounts and expected revenues from gasoline and diesel excise taxes, as forecast by the U.S. Department of the Treasury) with the potential net new revenue (over and above the amount expected from the current excise taxes) that could be generated by a switch to a federal sales tax on motor fuels, as estimated by the U.S. Department of Energy.

Securing dedicated user-based funding at least at baseline levels for the highway and transit programs will represent a vital first step toward the broader goal of a renewed commitment to rebuilding this nation's infrastructure.

CLOSING THE HIGHWAY TRUST FUND GAP, 2013–2016



Source: American Association of State Highway and Transportation Officials (AASHTO)




A sales tax on fuel already works in practice at the state level

Evidence that a sales tax is a better approach has been proven with recent data from the states of California and Georgia.

- In California, from 2004 to 2009, annual revenues from its 5 percent sales tax on gasoline increased by 60 percent while revenues from its 18-cents-per-gallon excise tax dropped by 7 percent.
- In Georgia, from 2004 to 2009, annual revenues from its sales tax on fuels increased by 78 percent, while in the same time period, excise tax revenue was virtually unchanged.

Like all policy proposals, the idea of replacing fuel excise taxes with a sales tax on fuel has both advantages and disadvantages. Fortunately the former appear to outnumber the latter.

ADVANTAGES

- The principal advantage is that a sales tax is self-indexing and has the potential to end divisive debates on a needed baseline level of infrastructure funding that does not erode over time due to inflation and increased vehicle fuel economy.
- This proposal represents a funding source that will likely grow when world oil prices increase as China, India and other newly industrialized countries pressure the oil markets.
- The sales tax for excise tax swap is to be imposed on a revenue-neutral basis. In terms of popular perception, however, an excise tax in the high teens and low twenties would be replaced by a sales tax in the single digits.
- Any General Fund support needed to meet the sales tax "floor" could be repaid, and amounts over the HTF revenue "ceiling" could be used for General Fund deficit reduction.
- The existing federal excise taxes have low collection costs and low rates of evasion because they are imposed on relatively few taxpayers early in the fuel supply chain. Unlike a broad-based vehicle miles traveled (VMT) fee or other forms of road tolling, a sales tax on fuel could be imposed in the same way in order to hold down collection costs. Several states already impose a sales tax on fuels and have experience in this method of tax collection.

DISADVANTAGES

- Fuel prices are highly variable in the short term, and revenue will fall when prices decline and will rise when prices increase. The "floor" and "ceiling" mechanism described above can moderate these revenue swings.
- Higher prices reduce miles traveled, and upcoming (and more stringent) federal fuel economy standards will exert a downward pressure on the number of gallons purchased. However, the sales tax proposal would enjoy an advantage over the current excise tax-based approach in either case.

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