FUNDING

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Texas Department of Transportation

2019-2020 EDUCATIONAL SERIES

FUNDING

OVERVIEW

Transportation projects take many years to develop and construct. In addition to the design, engineering, public involvement, right-of-way acquisition, environmental analysis and oversight of highway construction projects, the Texas Department of Transportation (TxDOT) must also adhere to various stages of financial planning. Funding for a transportation project often comes from multiple revenue sources with different permissible uses over a period of years.

TxDOT receives funding from a variety of revenue sources and funding mechanisms. For years, state and federal motor fuels tax and state vehicle registration fee revenues were adequate to service the needs of the state highway system. Over time these revenues failed to keep up with the state's growing population and transportation needs. To address the population boom and the diminishing purchasing power of motor fuels tax revenues and registration fees, the Texas Legislature provided TxDOT with several debt financing tools to advance large projects more quickly, as opposed to paying for projects on a cash basis as the funding became available. These tools helped the state avoid the substantial effects of inflation. By fiscal year 2020, all of the proceeds from these bonding tools will be fully spent on projects. As these bond programs began to diminish, the Texas Legislature, with voter approval, created two non-traditional transportation funding sources, known as Propositions 1 and 7. Funding for Proposition 1 is derived from a certain amount of the state's oil and gas production tax revenue. Proposition 7 funds are generated from a portion of sales and use taxes, which first became available in the last half of 2018. Beginning in fiscal year 2020, a percentage of motor vehicle sales and rental tax revenue could also contribute to state highway funding as a result of Proposition 7. This document:

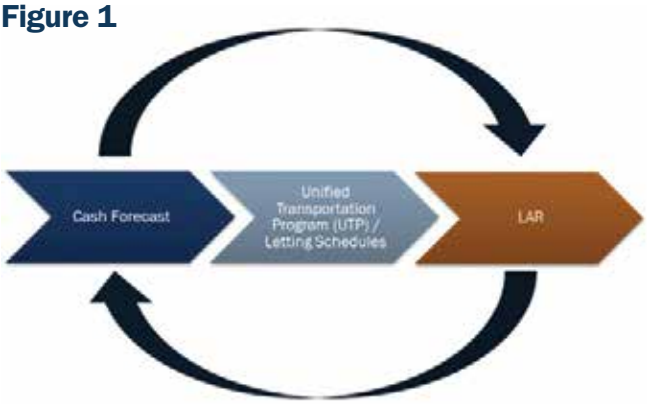
- Explores TxDOT's funding sources.
- Briefly explains how highway projects receive funding.
- Summarizes permissible uses of TxDOT's funding streams.

PERFORMANCE-BASED PROCESS

TxDOT has implemented a performance-based process to fully utilize its new, non-traditional funds, guide project selection and distribute the funds to projects in the Unified Transportation Program (or "UTP"). The Unified Transportation Program is TxDOT's 10-year, midrange planning document that guides the state's transportation project development. The creation of non-traditional revenues and funding streams has allowed TxDOT to implement scenario-based planning, which has taken the place of TxDOT's traditional project planning methodology. Rather than planning projects solely on a fiscally-constrained cash forecast based on traditional funding streams, transportation planners may add projects to the Unified Transportation Program that include plans for potential funding rather than guaranteed funding. Scenario-based planning allows TxDOT to accelerate projects or reduce the amount of projects contracted, depending on how the funds are actually appropriated and realized.

Scenario-based planning allows TxDOT district offices and local planning organizations to adjust more readily to unpredictable economic factors such as the state's oil and gas production, the changing needs of the state budget and evolving local project needs. While the exact amounts of non-traditional funds in years to come are unknown and sometimes difficult to predict, these new funds and scenario-based planning will allow the state's transportation experts to add new projects to the planning books that might not otherwise have been available. Most importantly, the non-traditional funds provided by the Texas Legislature have enabled the Texas Transportation Commission to adopt the 2019 Unified Transportation Program with more than $75 billion in planned transportation project contracts.

Figure 1



CASH FORECAST

Each month TxDOT updates its cash forecast revenues, expenditures and fund balances. Future revenues are projected based on a financial analysis that includes historical trends, current statutes, the Texas Comptroller of Public Accounts' official revenue estimates, current events and other developments. TxDOT's federal highway reimbursement projections take into account the current federal surface transportation authorization bill, continuing resolutions, redistributions and other federal requirements imposed on the use of those funds. Future expenditures are projected based on budgets established within the framework of the General Appropriations Act, base contract letting amounts developed for TxDOT's 10-year Unified Transportation Program, remaining obligations on previously awarded projects and other relevant data. To account for the effects of inflation, additional programs, legislative changes and other factors, the forecast adds a percentage of total expenditures excluding contractor payments, debt service and other agency appropriations to a growth expenditure line item. Figure 1 (*see above*) shows how the cash forecast contributes to planning and programming for transportation projects, which leads to the formation of TxDOT's Legislative Appropriations Request (or "LAR").

METROPOLITAN PLANNING ORGANIZATIONS

Metropolitan Planning Organizations (or "MPOs") are comprised of local elected officials and transportation agency representatives who oversee the planning and prioritization of transportation improvements in metropolitan areas. A Metropolitan Planning Organization is designated in each urban area of Texas with a population of more than 50,000 people. There are currently 25 Metropolitan Planning Organizations in Texas.

Once TxDOT or a Metropolitan Planning Organization identifies a needed transportation project, TxDOT staff 'programs' the project. The term 'program' describes the process by which the Metropolitan Planning Organization and TxDOT evaluate and approve the project along with other regional priorities and decide if it should be advanced to the next step of development. Projects are then prioritized and scheduled based on an assessment of available funding over the next several years for projects to be developed and built.

Meanwhile, federal law requires each Metropolitan Planning Organization to develop a Transportation Improvement Program (or "TIP") and the state to compile a Statewide Transportation Improvement Program (or "STIP") as a condition of securing federal funds for transportation projects. The Statewide Transportation Improvement Program is a four-year, financially-constrained plan composed of the 25 Metropolitan Planning Organizations Transportation Improvement Programs and the district rural Transportation Improvement Programs. Projects included in the Statewide Transportation Improvement Program, once approved by the Federal Highway Administration and the Federal Transit Administration, are then eligible to use federal funds.

UNIFIED TRANSPORTATION PROGRAM

As previously mentioned, the Unified Transportation Program is a ten-year, midrange planning document developed and adopted annually by the Texas Transportation Commission as a guide for transportation project development. The Unified Transportation Program is part of a comprehensive planning and programming process linking the planning activities of the Statewide Long Range Plan and Metropolitan Transportation Plans to the detailed programming activities under the Statewide Transportation Improvement Program and TxDOT's 24-month letting schedule. Specifically, the Unified Transportation Program is a listing of projects and programs that are planned to be developed and constructed over the next ten years. The inclusion of projects or programs in the Unified Transportation Program authorizes project development activities and serves as a communication tool for stakeholders and for the public to understand TxDOT's project development commitments.

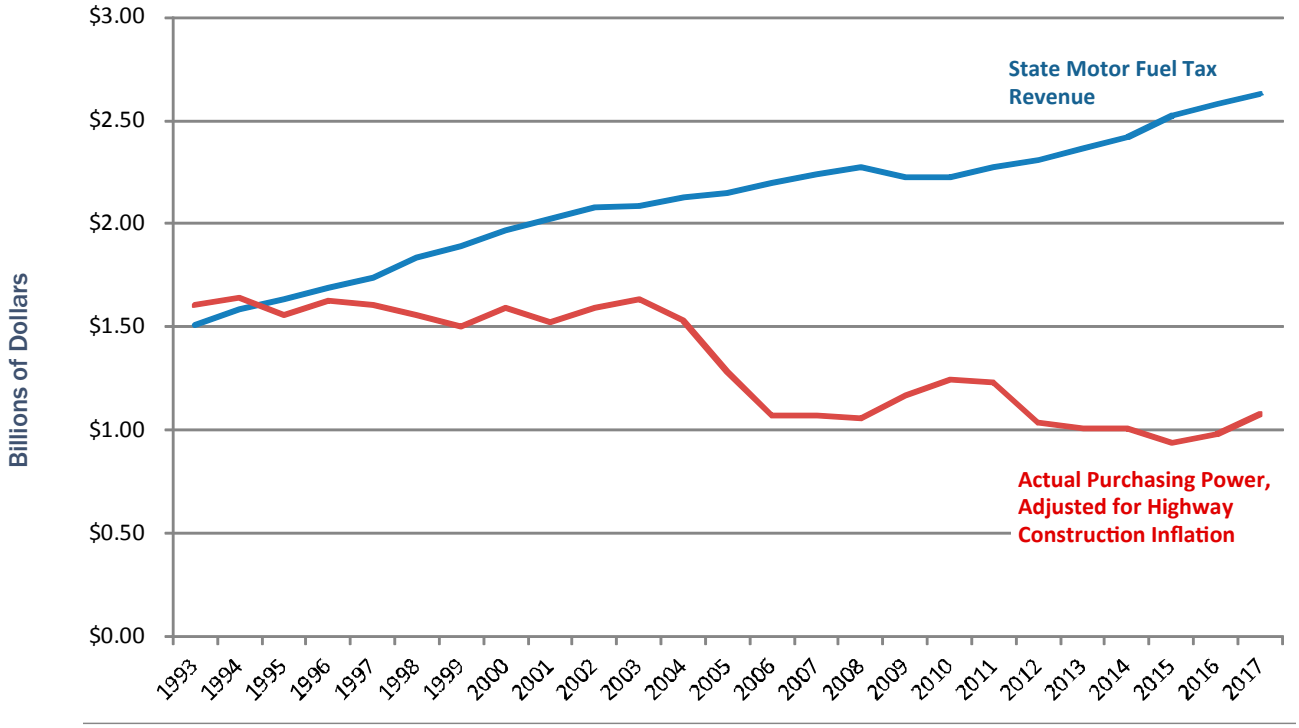
LETTING

Letting is the process of providing notice, issuing proposals, receiving bids and awarding contracts for highway improvement projects. At this stage of project development, TxDOT must have a realistic view of how much cash will be available to make progress payments on contracts awarded. In addition to biennial appropriations and past programming commitments, TxDOT must ensure there is sufficient revenue to support its new commitments and ensure that the revenue will be there beyond the biennium since each project may continue to pay out over several years.

APPROPRIATIONS

State agencies in Texas are appropriated funds by the Texas Legislature on a biennial basis. TxDOT's Legislative Appropriations Request is created one year in advance of the biennium in which the funds will be spent. When TxDOT receives its appropriation, a significant portion of the funds are used for projects that have already been awarded. The remaining funds are available to develop future projects and make payments on projects that begin in the current biennium. While TxDOT strives to deliver projects on budget and on time, the delivery of projects may be delayed for

Figure 2: State Motor Fuel Tax Revenue



a variety of circumstances, many of which are outside of TxDOT's control. These many moving parts create a greater need for budget flexibility among the project development and delivery strategies in TxDOT's biennial budget. Greater budget flexibility, meaning more transferability among project development and delivery strategies, would also contribute to the acceleration of project delivery throughout the state.

SOURCES OF REVENUE

TxDOT receives both traditional and non-traditional funding sources with different constitutional and statutory limitations. The following section summarizes each major funding source TxDOT receives, and Figure 7 on page 11 details the statutorily authorized uses of each funding stream.

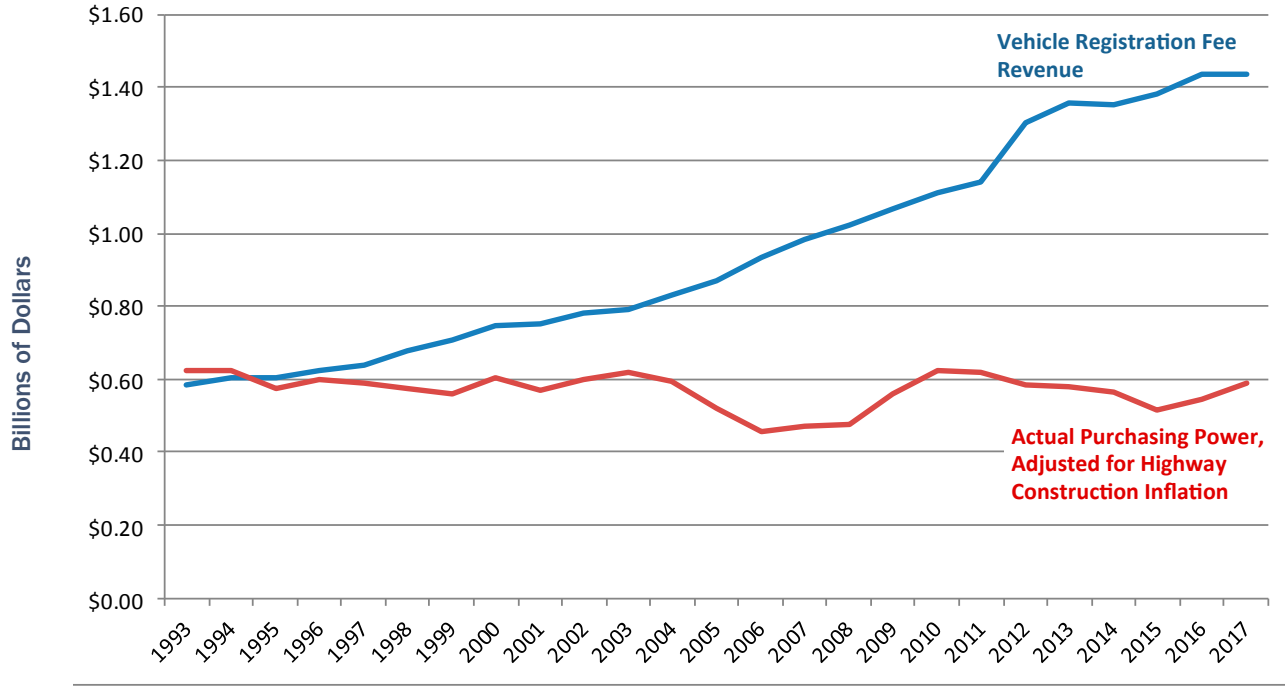
Traditional Funding Sources in the State Highway Fund

The State Highway Fund, which is also known as "Fund 6," consists of various revenues, several of which are dedicated by the Texas Constitution for highways. One of the most important revenues to the State Highway Fund is the state motor fuels tax, which levies 20 cents per gallon on gasoline and diesel and 15 cents per gallon on liquefied petroleum gas. Three-fourths of the state motor fuels tax revenue is dedicated to the State Highway Fund and one-fourth is dedicated to the Available School Fund. The legislature last raised motor fuels taxes in 1991. In fiscal year 2017, $2.63 billion in motor fuels tax revenue was deposited into the State Highway Fund. The state motor fuels tax contributes a significant amount to the State Highway Fund. However, the value of 1992 dollars when compared with highway construction costs in the present day decreases the purchasing power of those dollars. Figure 2 *(on the previous page*) illustrates the declining purchasing power of state motor fuels tax revenues adjusted to the Highway Cost Index (1992 base year).

Another significant source of funding for the State Highway Fund is motor vehicle registration fees. Not including the optional fees assessed by counties and a new processing and handling fee of $4.75, there is a base, annual registration fee of approximately $51 to register most vehicles in Texas. The revenue is shared between counties and the state. In fiscal year 2017, $1.44 billion in vehicle registration fee revenue was deposited into the State Highway Fund. Figure 3 (*see below*) illustrates the declining purchasing power of constitutionally-dedicated vehicle registration fee revenue adjusted to the Highway Cost Index (1992 base year).

While traditional revenues are declining in purchasing power, they provide TxDOT with predictable revenue sources that are ideal for long-term project planning and delivery. Traditional funds are deposited on a monthly basis and remain one of the most dependable sources of revenue for the state.

Figure 3: State Vehicle Registration Fee Revenue



Proposition 1

On November 4, 2014, Texas voters approved the ballot measure known as Proposition 1, authorizing a constitutional amendment for non-tolled highway funding. Under the amendment, a portion of oil and gas tax revenues that would have otherwise been deposited into the Economic Stabilization Fund will be deposited to the State Highway Fund. Figure 4 (*see below)* depicts the statutory procedures for Proposition 1 funding.

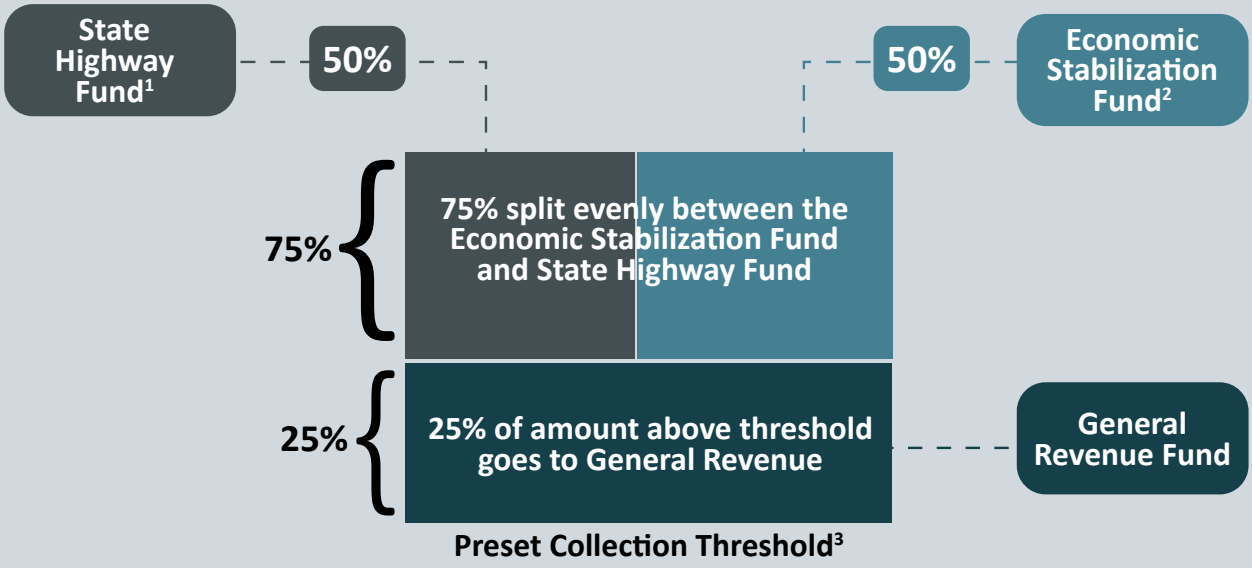
The Texas Comptroller of Public Accounts first transferred $1.74 billion in Proposition 1 funds to the State Highway Fund in fiscal year 2015. TxDOT began awarding contracts for projects funded with Proposition 1 in March 2015. As of early fiscal year 2019, the State Highway Fund has received approximately $5.4 billion, with the most recent transfer of $1.384 billion in November fiscal year 2019.

Unlike TxDOT's traditional funding sources, Proposition 1 deposits occur yearly rather than monthly, resulting in large cash deposits. While TxDOT has accelerated its letting schedule, there will be a significant cash balance in the State Highway Fund while these projects are delivered and paid out. Factors affecting Proposition 1 deposits are as follows:

- Fluctuations in oil and natural gas production may affect Proposition 1 deposit amounts.
- The sufficient balance of the Economic Stabilization Fund is established by a joint legislative committee or the full legislature prior to each legislative session. A higher sufficient balance or legislative appropriations made from the Economic Stabilization Fund that reduce the amount of cash available to meet the sufficient balance could mean less money is available for transfer to the State Highway Fund.
- Proposition 1 funds are set to expire after the fiscal year 2025 transfer if the legislature does not extend the statutory expiration date.

Figure 4: Proposition 1

Texas Oil & Gas Production Taxes Above Threshold
Proposition 1 funds transfers are set to expire after the Fiscal Year 2025 transfer (December 31, 2024), unless a future legislature votes to extend them.



1. Actual amounts deposited in the State Highway Fund may vary based on the minimum balance of the Economic Stabilization Fund set by the Legislature.

2. Economic Stabilization Fund is also known as the Rainy Day Fund.

3. Preset collections threshold is set at 1987 oil and natural gas production tax levels: $599.8 million in natural gas production tax revenues and $531.9 million in oil production tax revenues.

Proposition 7

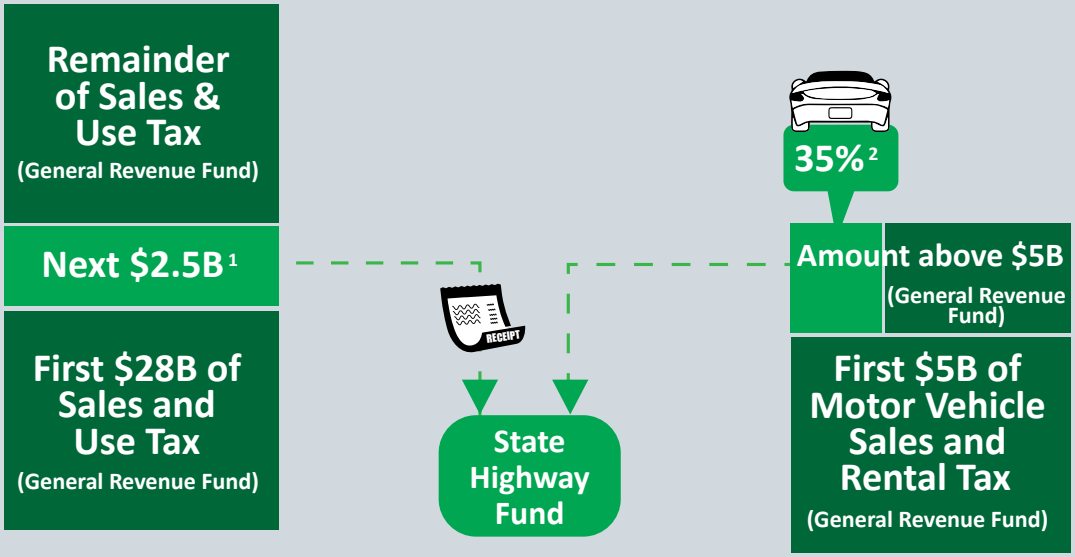
On November 3, 2015, Texas voters overwhelmingly approved Proposition 7, a constitutional amendment to dedicate portions of revenue from the state's general sales and use tax as well as from the motor vehicle sales and rental tax to the State Highway Fund for non-tolled projects. Figure 5 (*see Figure 5 below*) depicts the statutory procedures of Proposition 7 funding. The amendment allocates the funds in the following way:

- In August 2018 and September 2018, TxDOT received its first two deposits of Proposition 7 totaling $2.5 billion.
- Beginning in fiscal year 2020, if state motor vehicle sales and rental tax revenue exceeds $5 billion in a fiscal year, 35 percent of the amount in excess of $5 billion will be directed to the State Highway Fund (*see Figure 5 below*).

Similar to Proposition 1 deposits, Proposition 7 is received through large cash deposits in a short period of time rather than being spread throughout the year. While TxDOT has accelerated its letting schedule, there will be a significant cash balance available in the State Highway Fund while these projects are delivered and paid out.

Figure 5: Proposition 7

Sales & Use Tax; Motor Vehicle Sales & Rental Tax
Proposition 7 funds (Sales & Use Tax) are set to expire August 31, 2032; and Proposition 7 funds (Motor Vehicle Sales & Rental Tax) are set to expire August 31, 2029 unless a future legislature votes to extend them.



1. This transfer of funds to the State Highway Fund took effect September 1, 2017 (Fiscal Year 2018).

2. This transfer of funds to the State Highway Fund does not take effect until September 1, 2019 (Fiscal Year 2020).

FEDERAL FUNDING

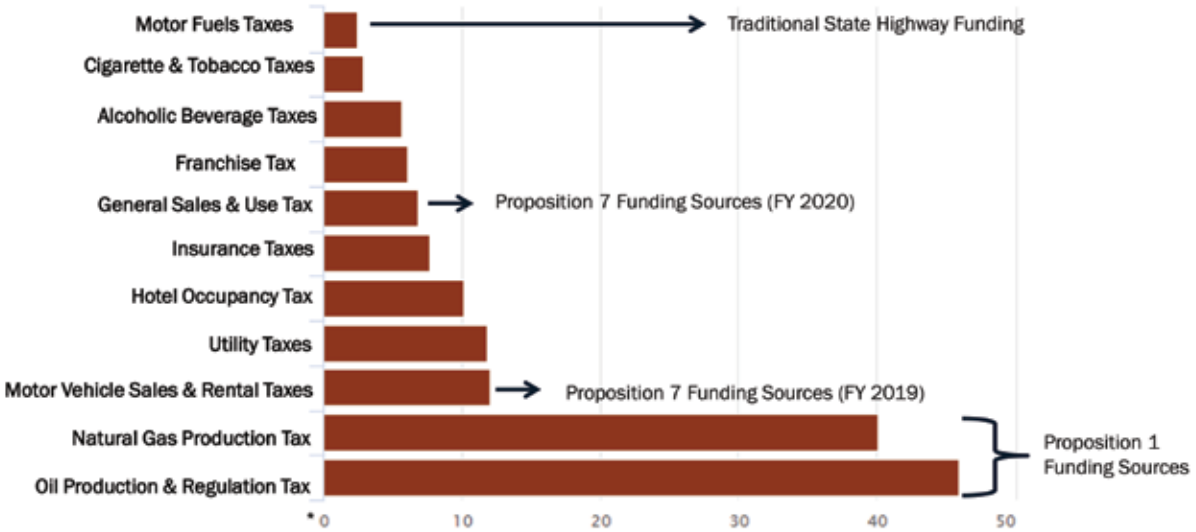
The current federal motor fuels tax rate is 18.4 cents per gallon of gasoline and 24.4 cents per gallon of diesel fuel. Revenue collected from the federal tax on gasoline and diesel supports the federal Highway Trust Fund.

Over one-third of the TxDOT budget is comprised of federal funds. For decades, federal aid for highways was supported solely by dedicated tax and fee revenue deposited into the federal Highway Trust Fund. When Congress enacted the Safe, Accountable, Flexible, Efficient Transportation Equity Act (or "SAFETEA-LU") in 2005, the surface transportation authorization legislation that determined transportation funding levels from 2005 to 2009, Congress elected to spend down the balance of the fund that had accumulated over the years. This allowed Congress to raise each state's allocation relative to the previous long-term authorization but left no room to increase federal aid after 2009-absent an increase in federal motor fuels taxes, fees or another funding mechanism. Congress decided to deposit general funds into the federal Highway Trust Fund to meet its obligations while it worked on a new authorization bill.

In August 2014, Congress reauthorized the federal surface transportation bill, known as Moving Ahead for Progress in the 21st Century (or "MAP-21"), but only provided eight months' worth of funding. Congress chose to keep federal funding at the previous elevated levels. This required the continued transfer of general funds to the federal Highway Trust Fund. The Fixing America's Surface Transportation (or "FAST") Act extended federal funding through fiscal year 2020. It too, requires the transfer of general funds to the federal Highway Trust Fund.

The federal funding amounts that appear in the General Appropriations Act are estimates of federal reimbursements for payments on projects that were obligated with earlier authority and projects obligated under the Fixing America's Surface Transportation Act.

Figure 6: Comptroller's Index Values of Relative Annual Volatility (1996-2015)



Texas Comptroller of Public Accounts. Tax Volatility: The Ups and Downs of State Revenue. By Bruce Wright and Gregory Conte. Fiscal Notes. November 2016. https://comptroller.texas.gov/economy/fiscal-notes/2016/november/volatility.php Last visited on November 1, 2018.

Major State Funding Sources and Relative Volatility

Figure 6 (*see above*) illustrates the relative stability and volatility of various state revenue sources, some of which are deposited into the State Highway Fund. This graphic is meant to explain some of the challenges presented by incorporating some of the most volatile sources in TxDOT's long-term planning and cash forecasting.

In this index, a value of zero would represent a tax showing no volatility at all, producing returns that never deviate from longer-term trends. No such tax exists, of course. A higher index value indicates greater relative volatility — more deviation from the tax's historical trend over time.

BORROWING PROGRAMS

Before the adoption of Propositions 1 and 7, the Texas Legislature provided several tools that allowed TxDOT to finance projects through bond programs. The Texas Mobility Fund, Proposition 14 (State Highway Fund revenue bonds) and Proposition 12 Highway Improvement General Obligation bonds have accelerated the construction of billions of dollars of highway improvements.

As directed by the Texas Legislature and in compliance with federal rules associated with tax-exempt debt, the projects funded with bond proceeds are long-term capital improvements. The economic consequences and improved safety and mobility resulting from these projects will be enjoyed by taxpayers for generations to come. While most of the funds have been allocated and expended, a brief summary is provided here to explain the rules and the status of each.

Texas Mobility Fund

The Texas Mobility Fund was authorized by voters in 2001, and the Texas Legislature identified revenues to be dedicated to the fund in 2003 to advance transportation projects. The maximum bond maturity is 30 years.

The program issuance limitation is based on a certified revenue estimate provided by the comptroller. However, House Bill 122 (84th Legislature, Regular Session, 2015) prohibited the issuance of additional debt and restricts future issuances to refunding bonds for savings and replacement of credit agreements. Debt service payments are secured by fund revenues and are also backed by the full faith and credit of the state.

Texas Mobility Fund bonds are not subject to the constitutional debt limit unless there is a draw from general revenue to make a debt service payment. If there were a draw, only the amount of the draw from general revenue would count against the debt limit. To minimize the likelihood of such a draw, there is a statutory safeguard that additional debt may be issued only if the projected revenues of the Texas Mobility Fund in any year are at least 110 percent of the program's projected debt service. Specifically, this safeguard requires the comptroller to certify that annual revenue is projected to be at least 110 percent of annual debt service throughout the years the bonds will be outstanding.

Revenues to the fund totaled approximately $463 million in fiscal year 2018. The largest sources are driver license fees, drivers' record fees, vehicle inspection fees and certificate of title fees. TxDOT may directly spend Texas Mobility Fund revenue in excess of the required debt service on transportation projects. TxDOT currently has projects underway to make use of these available revenues.

State Highway Fund Revenue Bonds (Proposition 14)

State Highway Fund revenue bonds, also known as Proposition 14 bonds, were authorized by voters and the Texas Legislature in 2003. Proposition 14 bonds are secured by certain State Highway Fund revenues. All of the available bond proceeds have been issued and fully utilized. The Texas Transportation Commission committed and spent all of the $6 billion in authorized Proposition 14 bond proceeds. State law limits Proposition 14 debt to $6 billion, meaning more debt cannot be issued—even as the bonds are paid off—unless the legislature amends the statute.

Highway Improvement General Obligation Bonds (Proposition 12)

In 2007, Texas voters approved a constitutional amendment allowing the Texas Legislature to authorize the Texas Transportation Commission to issue $5 billion of Proposition 12 bonds with a maximum maturity of 30 years. In 2009, House Bill 1, of the 81st Texas Legislature, First Called Session, authorized the issuance of these general obligation bonds to pay all or part of the costs of highway improvement projects. Prior to fiscal year 2018, the bonds were paid from revenue not already dedicated by the constitution, i.e., general revenue. After Proposition 7 became a funding source for highway improvement projects and eligible for debt service on Proposition 12 bonds, the legislature used Proposition 7 funds to pay for Proposition 12 debt service in the 2018-19 biennium.

The amount of bond proceeds that can be spent, up to an aggregate principal amount of $5 billion, is subject to appropriation. All of the available bond proceeds have been issued and fully utilized. Proposition 12 bonds are a general obligation of the state. As general obligation bonds, Proposition 12 bonds are subject to the state's constitutional debt limit. The Texas Transportation Commission committed and issued the full $5 billion in Proposition 12 bonds. The state constitution limits Proposition 12 debt to an aggregate principal amount of $5 billion, meaning more debt cannot be issued even as the bonds are paid off, unless statutory and constitutional provisions are amended.

Short-Term Borrowing

TxDOT is authorized to issue short-term debt that is secured by the State Highway Fund to carry out its functions. This debt is subordinate to Proposition 14 debt obligations. The purpose of this program is to ensure that TxDOT can have as many projects underway as possible without carrying a "cushion" in the State Highway Fund balance should payments come in more quickly or revenues come in more slowly than anticipated.

Toll Revenue Bonds

The Texas Transportation Commission is authorized to issue project revenue bonds (or toll revenue bonds) where the bonds are secured by the toll revenue collected for the project. To date, the Texas Transportation Commission has issued such bonds for the Central Texas Turnpike System in Austin, State Highway 249 and the Grand Parkway (State Highway 99) in Houston.

The bonds do not constitute an obligation of the state, TxDOT or any other agency or political subdivision of the state. In other words, the only source of revenue that can be used to pay for the toll system debt is toll revenue collected from the corresponding toll system.

Figure 7:
Permitted Uses of Funding Streams

Funding Source	Non-Tolled Highways	Tolled Highways	Rail — Passenger	Rail — Freight	Transit	Aviation	Ports
Proposition 1 Funds	✓						
Proposition 7 Funds	✓						
State Highway Fund — Dedicated [1]	✓	✓					
Proposition 14 Bonds	✓	✓					
Proposition 12 Bonds [2]	✓	✓					
Texas Mobility Fund — Revenue [3]	✓		✓		✓		
Texas Mobility Fund (TMF) — Bond Proceeds [4]	✓	✓	✓		✓		
State Highway Fund — Non-Dedicated [5]	✓	✓	✓	✓	✓	✓	✓
Regional Subaccounts [6]	✓	✓	✓	✓	✓	✓	✓

Texas Mobility Fund, Proposition 14 and Proposition 12 bond programs are unavailable or suspended.

1. State Highway Fund-Dedicated includes federal reimbursements.
2. Proposition 12 bond proceeds may be used to provide funding for highway improvement projects with no distinction between tolled and non-tolled highways. During the 2010-11 biennium, Proposition 12 proceeds were restricted to non-tolled projects.
3. The Texas Constitution allows Texas Mobility Fund bonds to be used to develop and construct state highways, "to provide participation by the state in the payment of a portion of the costs of constructing and providing publicly-owned toll roads and other public transportation projects." "Other public transportation projects" is undefined and therefore may be available for more types of transportation projects than what is listed here.
4. Texas Mobility Fund, revenues in excess of funds required to pay Texas Mobility Fund debt service were prohibited to pay for toll expenditures as part of 2015 legislation.
5. "State Highway Fund—Non-Dedicated" includes limited revenue sources.
6. Regional Subaccount funds may only be used for transportation, highway, and air quality projects as defined by Section 228.001 of the Transportation Code in the region where the project from which those funds were derived is located. The revenues are deposited to the State Highway Fund but are not dedicated by the Texas Constitution.

TEXAS DEPARTMENT OF TRANSPORTATION

VALUES:

People
People are the Department's most important customer, asset, and resource. The well-being, safety, and quality of life for Texans and the traveling public are of the utmost concern to the Department. We focus on relationship building, customer service, and partnerships.

Accountability
We accept responsibility for our actions and promote open communication and transparency at all times.

Trust
We strive to earn and maintain confidence through reliable and ethical decision-making.

Honesty
We conduct ourselves with the highest degree of integrity, respect, and truthfulness.

VISION:

A forward-thinking leader delivering mobility, enabling economic opportunity, and enhancing quality of life for all Texans.

MISSION:

Through collaboration and leadership, we deliver a safe, reliable, and integrated transportation system that enables the movement of people and goods.

GOALS AND OBJECTIVES:

- **Deliver the Right Projects –** Implement effective planning and forecasting processes that deliver the right projects on-time and on-budget.
- **Focus on the Customer –** People are at the center of everything we do.
- **Foster Stewardship –** Ensure efficient use of state resources.
- **Optimize System Performance –** Develop and operate an integrated transportation system that provides reliable and accessible mobility, and enables economic growth.
- **Preserve our Assets –** Deliver preventive maintenance for TxDOT's system and capital assets to protect our investments.
- **Promote Safety –** Champion a culture of safety.
- **Value our Employees –** Respect and care for the well-being and development of our employees.

Texas Department of Transportation ®

This document is part of an educational series on transportation issues produced by the Texas Department of Transportation. This document, the full Educational Series and other helpful resources can be found online at www.txdot.gov keyword search "State Legislative Affairs".