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September 18, 2020

The Honorable Terry Canales
Chair, House Committee on Transportation
Texas House of Representatives
P.O. Box 2910
Austin, TX 78768

Re: Transportation RFI, Interim Charge 1B

Dear Chair Canales:

My name is Brian Cassidy, and I am a partner in the law firm of Locke Lord LLP. Our firm represents several regional mobility authorities ("RMAs") and other transportation entities throughout the state, and I have been involved with transportation issues and with the development and implementation of transportation policy for many years.

We appreciate the opportunity to provide written testimony to the House Transportation Committee in response to the Request for Information, dated August 17, 2020. The written testimony set forth below addresses issues related to Interim Charge 1B, including recommendations for additional methods of funding or innovative tools that the state could utilize to deliver road infrastructure projects.

OVERVIEW

The tools necessary to effectively deliver transportation infrastructure projects are largely dependent on the funding that is available for those projects. If enough funding was available to meet all of the state's needs for new and expanded transportation projects (and maintenance of existing facilities), then the need for additional tools for project delivery would not be a compelling issue. However, Texas does not have all of the funding it needs, and the Legislature has shown little interest in conventional means of generating revenue such as increasing the gas tax.[1] Therefore, any discussion of the effectiveness of TxDOT (and other agencies) involved in delivering projects has to include the potential benefits of revenue generating (i.e., tolled) projects and alternative project delivery methods.

Propositions 1 and 7 (passed by the voters in 2014 and 2015, respectively), as well as the ending of the diversion of state highway funds to the Department of Public Safety, have directed significant funding to transportation. However, there seems to be a perception among some members of the Legislature that these measures have done all that is necessary to address the state's funding needs.

[1] The gas tax in Texas has remained at $.20 cents per gallon since 1991.

In past years, and based on a study by the "2030 Committee"[2], TxDOT had indicated it needed $4 billion in additional funding per year–$3 billion for new capacity and $1 billion per year for maintenance- just to maintain the state highway system in its current condition.[3] However, the 2030 study from which the $4 billion number was derived ***assumed*** that toll roads and comprehensive development agreements ("CDAs") would continue to be used as financing tools to develop projects. Without the continuing use of those tools, the gap in funding is significantly greater than the $4 billion figure.

This fact has been overlooked in recent years in much of the discussion about toll roads, CDAs, and transportation funding. Propositions 1 and 7 have had a significant impact on addressing the $4 billion need[4] and appear to have gone a considerable way toward providing that amount of funding. However, as noted above, the reality is that Propositions 1 and 7 (and $4 billion in new funds) were never intended to solve the state's funding needs ***without tolling or CDAs***. So, while the Legislature took bold steps to increase funding by advancing Propositions 1 and 7, it simultaneously retreated from other essential tools which were assumed to be part of the foundation on which the funding needs analysis was based.

In addition, while projections for Propositions 1 and 7 revenues remain optimistic (even in the uncertain economic climate resulting from COVID-19) it should be of concern to all transportation advocates that the state will experience budget shortfalls in other areas. Prop 1 and Prop 7 may be seen as a potential source of funds to address other non-transportation needs.[5] If that were to happen it would further impede the ability to provide needed funding for projects throughout the state.

Precluding CDAs and creating impediments to tolling may have exacerbated a problem that many thought had been solved. Unfortunately this appears to be manifesting itself in critical projects being deferred, local entities facing challenges in securing project funding, and a potential inability to access federal funding programs currently under development. For TxDOT (and its local transportation partners around the state), effective delivery of major projects in the face of limited funding can be enhanced by a wider array of tools for local funding and project delivery.

I. <u>Comprehensive Development Agreements</u>

CDAs are the Texas form of public-private partnership for roadway projects. Generally a CDA involves a contract with a private sector entity to design, construct, finance, operate, and maintain a project for some period of time (in Texas the maximum was 52 years).[6] CDAs transfer financing, revenue, and construction risk to the private sector. In some instances there is an up-front payment received from the private sector entity for the right to develop and operate the project, and often there is an agreement to share revenues between the private sector and the public entity as well. Ownership of any roadway subject to a CDA must, by law, remain with the public sector, so there is never any private ownership of public roadways under a CDA.

[2] 2030 Committee, *It's About Time: Investing in Transportation to Keep Texas Economically Competitive* (March 2011).
[3] Later that number was increased by $1 billion in annual funding needs to address roads affected by energy sector activity.
[4] TxDOT's 10 year Unified Transportation Plan ("UTP") accounts for $74.7 billion, which includes approximately $30.8 billion in funding from Propositions 1 and 7.
[5] This would not be an unprecedented action. In 2017, then House Appropriation Chair John Zerwas filed HCR 108 which would have reduced Proposition 7 revenues that would be deposited in the state highway fund by 50% for FY 2018 and 2019. It was ultimately dropped after significant outcry from various transportation industry stakeholders.
[6] This discussion does not include "design/build CDAs", which include only the design and construction elements and do not involve financing or operation of projects by private entities.

The CDA delivery method has been used for five projects in Texas with an aggregate capital cost of $8.5 billion. One project (SH 130, Segments 5 & 6) went into bankruptcy after several years of operation; however, the restructuring process for that project has been completed and it has emerged from bankruptcy with new owners. Notwithstanding the bankruptcy, the roadway maintained continuous operation and the state was not forced to assume any of the financial obligations of the private sector developer. This demonstrates that even in the worst-case scenario the risk transfer inherent in CDAs worked as intended and the public was protected from any adverse financial or operational consequences.

Two of the five CDAs included up-front payments for the rights to develop and operate the projects, and that money has been used by the regions where the projects are located to support the financing of additional projects. All five CDA projects also provide for revenue sharing, which provides further funding for additional projects.

Unfortunately, notwithstanding the success of CDAs in Texas and other parts of the US, Texas has retreated from the model to the point where there is currently no legislative authorization for TxDOT or RMAs to use a CDA. This is true despite the fact that there are several projects with projected costs of more than $1 billion in urban areas throughout the state. Some or all of these projects could be developed through CDAs (using private sector financing) and thereby leave the massive amounts of state funding they will need available for other projects in urban and rural areas. *The Committee should consider recommending reauthorization of CDAs to enhance the ability of TxDOT and other transportation entities to partner with the private sector to deliver essential infrastructure projects.*

II. <u>Restore Funding Tools</u>

A. <u>Texas Mobility Fund</u>

In 2001, voters approved Proposition 15, which created the Texas Mobility Fund (the "TMF") and authorized grants of funds for toll roads. The Texas Transportation Commission (the "TTC") was authorized to issue debt supported by the TMF to finance the development and construction of roads on the state highway system, publicly owned toll roads, and other public transportation projects. The TMF was one of the more flexible sources of money available for use by TxDOT. However, in the 84th Legislative Session, HB 122 was adopted which imposed significant restriction on the use of the TMF. Specifically, HB 122 prohibited the TTC from issuing any additional TMF debt, except to refund outstanding obligations (to provide savings), refund outstanding variable rate obligations, and to renew or replace credit agreements relating to variable rate obligations and it specified that additional funds on deposit in the TMF in excess of what is needed to satisfy existing obligations or credit agreement requirements may be used for any of the statutory purposes other than for toll roads. In other words, HB 122 resulted in the TMF ceasing to function as a revolving fund contemplated at the time Proposition 15 was approved in 2001, and available funds are not be available for use on toll projects or any other transportation projects. *The Committee should consider recommending legislation reauthorizing the TTC to issue TMF debt and to allow funds to be used for toll roads and other transportation projects.*

B. <u>Toll Project Grants</u>

The erosion of voter-approved authority from Proposition 15 continued in 2017 under the 85th Legislative Session with the adoption of "Amendment No. 12" to SB 312, the TxDOT Sunset bill. Prior to Proposition 15, the Texas Constitution required the repayment of funds advanced for the use of toll projects. In addition to creating the TMF, Proposition 15 amended Art. 3, sec. 52-b of the Texas Constitution by:

> authorizing **grants** and loans of money and issuance of obligations for financing the construction, reconstruction, acquisition, operation, and expansion of state highways, turnpikes, toll roads, toll bridges, and other mobility projects.[7]

At the time, the House Research Organization noted that the amendment "would repeal the constitutional requirement to repay Fund 6 from tolls or other turnpike revenue."[8] In other words, by approving Proposition 15, the voters specifically approved allowing grants of funds to support toll roads. Yet, Amendment No. 12 precluded exactly what the voters authorized in 2001.

Toll projects around the state are typically financed through a combination of toll revenue bonds and funds allocated to a project by a metropolitan planning organization ("MPO"). Toll revenue bonds represent a form of local funding, as the bonds are issued by a local entity (e.g., RMAs, the North Texas Tollway Authority, or a county toll road authority). Repayment is supported solely by user fees generated from the project. This money does not come from TxDOT or the state highway fund.

The MPO-allocated funds come from the portion of funds that TxDOT directs to an MPO through the statewide, formula-based allocation of state funds. MPOs (and the elected officials on MPO boards) make decisions locally regarding how to utilize funds to support projects in their region, which may include dedicating funds to support a toll project. Doing so may accelerate an important project for the region by many years (even decades) as a result of not having to wait on traditional state funding. However, even though the decision to dedicate funds to a toll project is made locally, the funds originate from the state highway fund which is administered by TxDOT. That means notwithstanding the local decision-making process, MPO-allocated funds are considered a "grant" of funds from TxDOT and will be subject to the repayment requirement established by Amendment No. 12.

The result of Amendment No. 12 is delayed projects or projects simply being rendered financially infeasible to develop as regional toll projects. The repayment requirement adds more debt to a project—beyond the maximum debt capacity that has already been determined in assessing the amount of toll revenue bonds that can be issued. Projects that cannot be developed at the local level will then rely on state funding which is already inadequate to meet the state's growing needs. Trading local funding of projects for an increase to the state's burden of doing so hardly seems like a wise trade-off in a state struggling to address the impacts of congestion on mobility, economic development, and quality of life for its citizens. *The Committee should consider recommending legislation allowing TxDOT to grant funds for toll projects*

III. Strengthen Local Funding Options

A. Optional Vehicle Registration Fee

While trading local funding for an increase to the state's responsibility to fund projects should be avoided, it is prudent to make local transportation funding options available to those communities that wish to make infrastructure development a priority.

One example where the legislature has provided a local funding tool, albeit to a small percentage of local entities, is the optional vehicle registration fee ("Optional VRF") created in 2007. Only 5 counties--Cameron, Hidalgo, Webb, El Paso, and Bexar Counties--are eligible to adopt the Optional VRF. The

[7] Tex. Const. art. III, § 52-b (emphasis added).
[8] House Research Organization, *Focus Report: Amendments Proposed for November 2001 Ballot* 45 (Aug. 13, 2001), *available at* http://www.hro.house.state.tx.us/pdf/focus/amend77.pdf.

Optional VRF allows a county to impose an additional $10 vehicle registration fee and to remit that $10 fee to an RMA to fund long-term transportation projects that are consistent with the purposes specified by Section 7-a, Article VIII, Texas Constitution.[9] In other words, the Optional VRF may only be used for roadway purposes (i.e., construction, ROW, and policing). The initial Optional VRF is adopted by order of a county commissioners court; no public vote is required and, unless committed to the repayment of an outstanding bond issuance, it may be removed or rescinded.

All of the 5 counties eligible to adopt the fee have done so, and 4 of the 5 have issued bonds secured by the fee in order to increase funding available for local projects. The tool has been very successful in enabling those counties to advance projects important to their regions for mobility, safety, and economic development.

During the 86th Legislative Session, over a dozen bills and amendments, impacting over two dozen counties, were filed to authorize additional counties to adopt the Optional VRF. Many of the impacted counties adopted resolutions in support of the legislation and traveled to the Capitol to advocate for the need for more local funding options. Despite the widespread support, no legislation was adopted to expand the list of counties able to adopt the Optional VRF. *The Committee should consider recommending legislation allowing additional counties to enact the Optional VRF.*

Related to the Optional VRF is authorization that two of the counties (Cameron and Hidalgo) have to increase the amount of the Optional VRF to $20 through approval of the increase by a vote of county residents. In other words, the Optional VRF of up to $10 can be enacted by action of their commissioners' courts, and the fee can be increased by another $10 through an approval of the additional increase by a vote of county residents. Such an action would increase the amount that could be leveraged to support projects, but only if there is a public vote. Other counties with authority to enact the initial $10 fee have pursued legislation that would provide for this additional fee pursuant to a public vote. *The Committee should consider recommending legislation allowing additional counties to adopt an additional Optional VRF of up to $10 subject to a vote of the county residents.*

B. <u>Transportation Reinvestment Zones ("TRZs")</u>

TRZs are a concept that RMAs and other local governmental entities have actively supported since their creation in 2007. TRZs are an innovative tool for generating transportation project funding by capturing and leveraging the economic growth that results from a transportation project. Development of new projects, and the expansion or improvement of existing projects, often spurs increased economic development in areas around a project. This economic development can be in the form of construction of new homes and businesses in previously undeveloped areas or through the redevelopment of existing areas which, as a result of a project, experience improved access to homes and businesses. As development or redevelopment occurs, property values in those areas increase. A TRZ allows a municipality, county, or a port authority to designate a geographic area around a transportation project and to capture the increase in ad valorem tax revenues resulting from the increase in property values for use in connection with the financing of the project.[10] In this manner the economic growth attributable to the project is used to support the funding of the project.

[9] *See* TEX. TRANSP. CODE §502.402(e)

[10] TRZs can also be formed to capture the incremental growth in sales tax in an area resulting from increased commercial activity. *See* TEX. TRANSP. CODE §222.110.

While it has long been clear that counties (unlike cities) do not have the authority to issue debt secured by a tax increment, a 2015 Attorney General opinion suggested that counties may not be authorized to form a tax increment financing zone and collect a tax increment, even if no bonds are issued and regardless of whether the tax increment funds are used to support the costs of a project that benefits the entire county.[11] The opinion concluded that: "absent a constitutional amendment, it is likely a court would conclude that a county may not form a [TRZ], to the extent that doing so utilizes a captured increment of ad valorem taxes to fund a county-created tax increment reinvestment zone." As a result there is now a lack of confidence in what has otherwise proven to be a valuable tool for counties to fund transportation projects. *The Committee should consider recommending legislation to grant counties clear constitutional authority to utilize tax increment financing in connection with TRZs.*

SUMMARY OF RECOMMENDATIONS

- The Committee should consider recommending reauthorization of CDAs to enhance the ability of TxDOT and other transportation entities to partner with the private sector to deliver essential infrastructure projects.
- The Committee should consider recommending legislation reauthorizing the TTC to issue TMF debt and to allow funds to be used for toll roads.
- The Committee should consider recommending legislation allowing TxDOT to grant funds for toll projects.
- The Committee should consider recommending legislation allowing additional counties to enact the Optional VRF.
- The Committee should consider recommending legislation allowing additional counties to adopt an additional Optional VRF of up to $10 subject to a vote of the county residents.
- The Committee should consider recommending legislation to grant counties clear constitutional authority to utilize tax increment financing in connection with TRZs.

Very truly yours,

C. Brian Cassidy

[11] *See* Tex. Att'y Gen. Op. No. KP-0004 (2015).