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Report to the Committee on Environment and Public Works, U.S. Senate

February 2009

HIGHWAY TRUST FUND

Improved Solvency Mechanisms and Communication Needed to Help Avoid Shortfalls in the Highway Account

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GAO-09-316

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Highlights

Highlights of GAO-09-316, a report to the Committee on Environment and Public Works, U.S. Senate

February 2009

HIGHWAY TRUST FUND

Improved Solvency Mechanisms and Communication Needed to Help Avoid Shortfalls in the Highway Account

Why GAO Did This Study

The Highway Account within the Highway Trust Fund is the primary mechanism for funding federal highway programs. The account—administered by the Federal Highway Administration (FHWA) within the Department of Transportation (DOT)—channels about $33 billion in highway user excise taxes annually to states for highway projects. Although DOT and others projected that the account could run out of funds in fiscal year 2009, the balance fell more rapidly than expected and a shortfall became imminent in August 2008. In September, Congress passed legislation to provide $8 billion to replenish the account, but DOT officials anticipate the account could reach a critical stage again in fiscal year 2009.

This report (1) describes the events that led to the decline in the account balance, including how DOT responded, and (2) identifies potential improvements in mechanisms to manage account solvency. This report also includes information on strategies GAO has reported on in the past that could be used to better align account outlays and revenues. To conduct this work, GAO analyzed information in legal and budget documents, reviewed account estimates, and interviewed agency officials and stakeholders.

What GAO Recommends

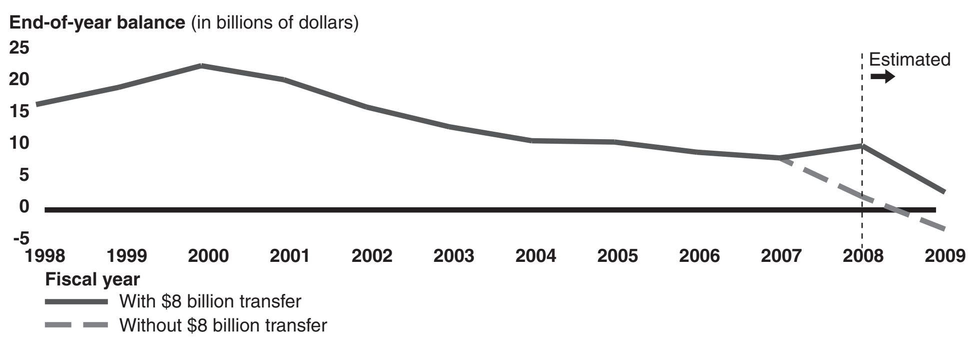
GAO is making recommendations to help DOT improve solvency mechanisms for the Highway Account and communication on the account's status with stakeholders. DOT reviewed the draft report and generally agreed with the report's findings and recommendations.

To view the full product, including the scope and methodology, click on GAO-09-316. For more information, contact Phillip R. Herr at (202) 512-2834 or herrp@gao.gov.

What GAO Found

The Highway Account balance declined for several reasons. In 2005, estimated outlays from the account specified in legislation exceeded estimated revenues and, if these estimates were realized over the fiscal year 2005 to 2009 authorization period, would draw the account balance down to about $0.4 billion by the end of fiscal year 2009. However, actual revenues for fiscal year 2008 were about $4 billion lower than the estimates due to fewer purchases of trucks and motor fuel—two primary sources of account revenue. In the summer of 2008, DOT received indicators that the Highway Account balance was declining faster than expected and developed cash management practices to slow outlays to states but estimated that the account would remain solvent through the end of fiscal year 2008. Following a large downturn in revenues allocated to the account in August, DOT officials announced on Friday, September 5—three weeks later—that the practices to slow outlays would begin the following Monday, leaving states little time to adjust. DOT officials recognize that communication with stakeholders could be improved and are developing a plan to improve communication.

Highway Account Balance, Fiscal Years 1998 through 2009



Source: GAO analysis of FHWA data.

Improving mechanisms intended to help maintain Highway Account solvency could reduce the likelihood of a funding shortfall. First, statutory mechanisms designed to make annual adjustments to the Highway Account could be modified and implemented to perform better. In fact, DOT analyses prepared at GAO's request show that these modifications could have prevented or at least signaled the fiscal year 2008 decline. Second, DOT could monitor additional indicators throughout the year—such as changes in vehicle miles traveled—to help anticipate sudden changes in account revenues. Despite improvements in mechanisms, without either reduced expenditures or increased revenues, or a combination of the two, account shortfalls will likely continue. DOT officials noted that improved solvency mechanisms would be effective only if the authorization act better aligns expenditures from the account with revenues. In the past, GAO has reported on strategies that could be used to align expenditures and revenues.

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Abbreviations

CBO	Congressional Budget Office
DOT	Department of Transportation
FHWA	Federal Highway Administration
GARVEE	Grant Anticipation Revenue Vehicle
GVW	gross vehicle weight
IRS	Internal Revenue Service
OMB	Office of Management and Budget
RABA	Revenue Aligned Budget Authority
SAFETEA-LU	Safe, Accountable, Flexible, Efficient Transportation Equity Act—A Legacy for Users
TEA-21	Transportation Equity Act for the 21st Century
Treasury	Department of the Treasury
VMT	vehicle miles traveled

United States Government Accountability Office
Washington, DC 20548

February 6, 2009

The Honorable Barbara Boxer
Chairman
The Honorable James Inhofe
Ranking Member
Committee on Environment and Public Works
United States Senate

The Highway Account within the Highway Trust Fund is the principal mechanism for funding federal highway programs. The fund, administered by the Federal Highway Administration (FHWA) within the Department of Transportation (DOT), annually channels about $33 billion in highway user excise taxes—primarily from purchases of motor fuel and truck-related items—through the account for distribution to states for highway and related spending. Although DOT, the Congressional Budget Office (CBO), GAO[1] and others have reported that the Highway Account could experience a cash shortfall in fiscal year 2009, the balance of the account dropped more rapidly than anticipated and approached a zero balance in August 2008. Congress subsequently passed legislation in September 2008 to appropriate $8 billion from the General Fund of the Treasury to replenish the account.[2] DOT and CBO officials anticipate that the Highway Account could reach a critical stage again by the fiscal year 2009 end of the current highway program authorization of the Safe, Accountable, Flexible, Efficient Transportation Equity Act—A Legacy for Users (SAFETEA-LU).[3]

Given the important role of the Highway Account in providing funds to build, operate, and maintain our nation's roadways, we were asked to examine why the account balance declined and how to better anticipate such a decline in the future. Consequently, this report (1) describes the events that led to the decline in the balance of the Highway Account, as well as actions DOT took in response, and (2) identifies improvements in mechanisms to manage Highway Account solvency that Congress and

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[1]GAO, *Highway Trust Fund: Overview of Highway Trust Fund Estimates*, GAO-06-572T (Washington, D.C.: Apr. 4, 2006); and *Physical Infrastructure: Challenges and Investment Options for the Nation's Infrastructure*, GAO-08-763T (Washington, D.C.: May 8, 2008).

[2]Pub. L. No. 110-318, 122 Stat. 3532 (2008).

[3]Pub. L. No. 109-59, 119 Stat. 1144 (2005).

DOT could consider to better ensure the sustainability of the account. In addition to improved solvency mechanisms, this report also includes information on several strategies we have reported on in the past that could be used to better align expenditures and revenues.[4] To conduct this work, we reviewed statutes, regulations, budget documents, and reports related to the Highway Account and analyzed information contained in those documents. We also reviewed Highway Account estimates developed by DOT, asked DOT to conduct scenarios of the implementation of existing mechanisms that are designed to help keep the Highway Account solvent—the Byrd Test and Revenue Aligned Budget Authority (RABA)—and analyzed these scenarios. We interviewed officials from the Department of Transportation's Office of the Secretary and FHWA, Department of the Treasury (Treasury), Office of Management and Budget (OMB), Congressional Budget Office, Congressional Research Service, and the American Association of State Highway and Transportation Officials. We performed this work between November 2008 and January 2009 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

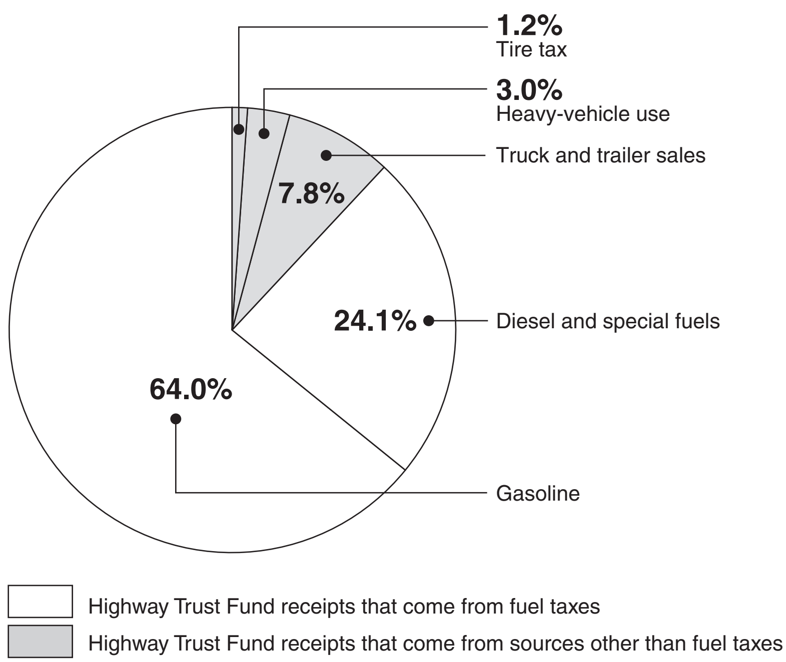
Background

Congress established the Highway Trust Fund in 1956 to hold and distribute highway user excise taxes to fund various surface transportation programs. In 1983, the Highway Trust Fund was divided into two accounts: the Highway Account and the Mass Transit Account. Receipts for the Highway Trust Fund are derived from two main sources: federal excise taxes on motor fuels (gasoline, diesel, and special fuels taxes) and truck-related taxes (truck and trailer sales, truck tires, and heavy-vehicle use taxes). Receipts from the motor fuels tax constitute the single largest source of revenue for the Highway Trust Fund (about 88 percent of total receipts from fiscal year 2005 to 2008); the gasoline tax—a flat rate of 18.4 cents per gallon—is the same amount as in 1993, although

[4] GAO, *High-Risk Series: An Update*, GAO-07-310 (Washington, D.C.: January 2007); *Surface Transportation: Restructured Federal Approach Needed for More Focused Performance-Based, and Sustainable Programs*, GAO-08-400 (Washington, D.C.: Mar. 6, 2008); and *Surface Transportation Programs: Proposals Highlight Key Issues and Challenges in Restructuring the Programs*, GAO-08-843R (Washington, D.C.: July 29, 2008).

the portion of that tax dedicated to the Highway Trust Fund has increased twice since that year. Receipts from truck and trailer sales (about 8 percent of total receipts from fiscal year 2005 to 2008) are the second largest source of revenue for the fund. (See fig. 1.)

Figure 1: Sources of revenue for the Highway Trust Fund, Fiscal Years 2005 to 2008



Source: GAO analysis of FHWA data.

The Highway Account receives the majority of the tax receipts allocated to the fund. Figure 2 shows the amount of motor fuels and truck-related taxes levied for the Highway Trust Fund and how receipts from the taxes are allocated between the Highway and Mass Transit Accounts within the fund.

Figure 2: Federal Highway User Excise Taxes and the Percentage Allocations to the Highway Account and the Mass Transit Account of the Highway Trust Fund

Motor fuel taxes

Type of excise tax	Tax rate (cents)	Distribution of tax: Highway Account, Highway Trust Fund (percent)	Distribution of tax: Mass Transit Account, Highway Trust Fund (percent)	Distribution of tax: Leaking Underground Storage Tank Trust Fund (percent)
Gasoline	18.4 per gallon	83.9	15.5	0.5
Diesel	24.4 per gallon	87.9	11.7	0.4
Gasohol	18.4 per gallon	83.9	15.5	0.5
Liquefied petroleum gas	18.3 per gallon	88.4	11.6	0.0
Liquefied natural gas	24.3 per gallon	92.3	7.7	0.0
M85 (from natural gas)	9.25 per gallon	83.5	15.5	1.1
Compressed natural gas	144.47 per thousand cubic feet	93.3	6.7	0.0

Truck-related taxes—all proceeds to Highway Account

Tires	9.45 cents for each 10 pounds of the maximum rated load capacity over 3,500 pounds
Truck and trailer sales	12 percent of retailer's sales price for tractors and trucks over 33,000 pounds gross vehicle weight (GVW) and trailers over 26,000 pounds GVW
Heavy-vehicle use	Annual tax for trucks 55,000 pounds and over GVW: $100 plus $22 for each 1,000 pounds (or fraction thereof) in excess of 55,000 pounds. Maximum tax: $550.

Source: GAO analysis of FHWA data.

The collection and distribution of taxes through the Highway Account is a complex process, as shown in figure 3. The collection process involves Treasury receiving excise taxes from business entities, estimating how much should be allocated to the Highway Account, and adjusting the estimated allocation after the Internal Revenue Service (IRS) certifies the actual amount that should be allocated.[5] Distribution of funds begins with a multiyear authorization act, such as SAFETEA-LU. The act provides specific amounts of annual contract authority[6] over the authorization

[5]When businesses pay excise taxes, they do not specify what specific excise tax produced the revenue; that information is provided at the end of each quarter, when businesses file tax returns with the IRS.

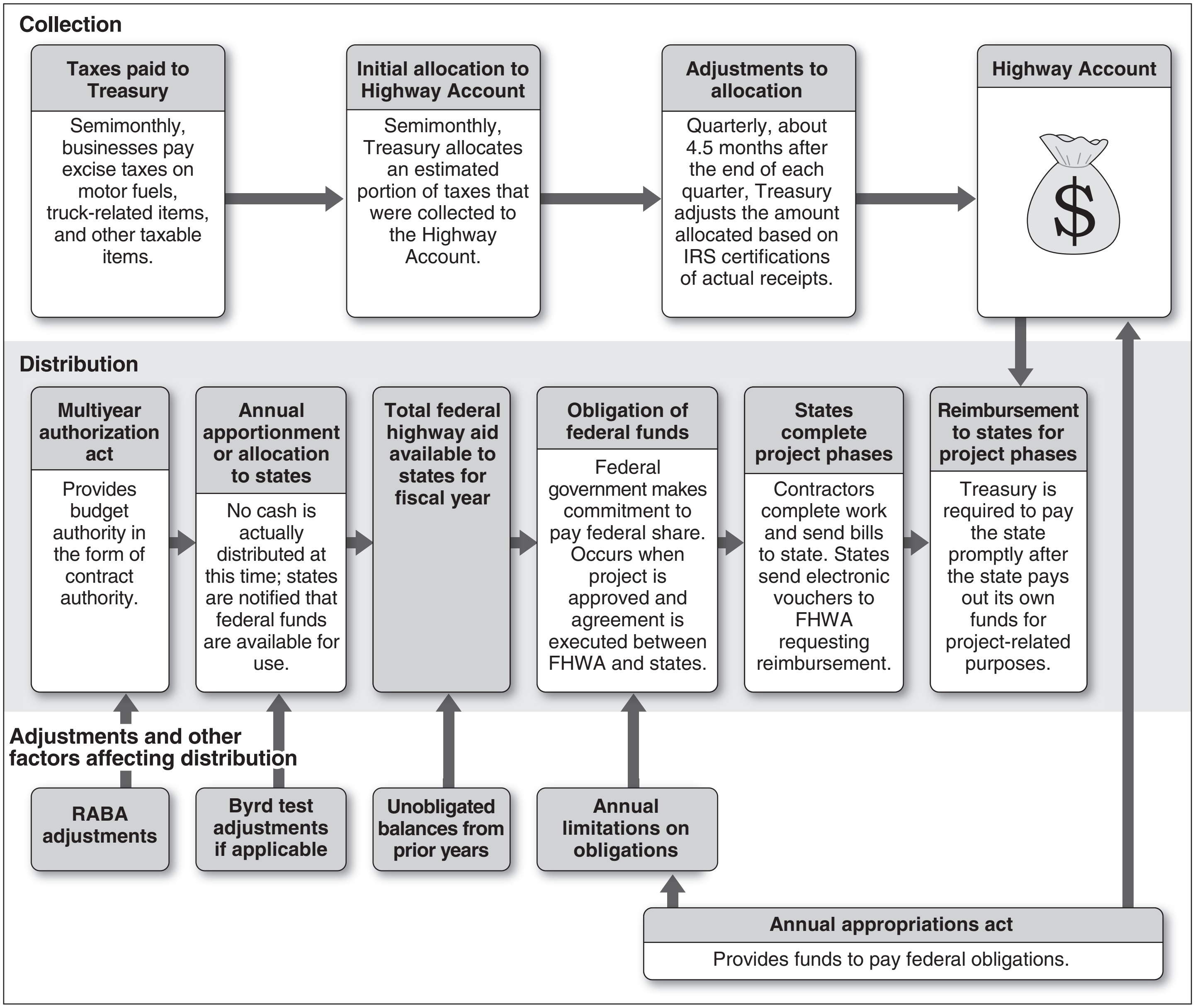
[6]Budget authority is the authority provided by federal law to enter into financial obligations that will result in immediate or future outlays involving federal government funds. Contract authority is a form of budget authority that permits obligations to be incurred in advance of appropriations. Contract authority is unfunded, and a subsequent appropriation is needed to liquidate, or pay, the obligations.

period and also specifies annual obligation limitations that establish "guaranteed" funding levels. These guaranteed funding levels are based on assumptions about future receipts to the Highway Account and can be modified in subsequent annual appropriations acts.[7] Annually, DOT apportions (through formula) and allocates to the states the contract authority provided in the authorization act.[8] DOT also divides the obligation limitations among the federal highway programs and the states based on a multistep process provided in the appropriation act. No cash is actually distributed to the states at this time; instead, states are notified of the amount of federal funds available for use in that state. DOT then obligates federal funds for approved projects. An obligation is a legally binding commitment by the federal government. Once an obligation is made, the federal government must reimburse the states when they submit a voucher for completed work, which, due to the length of time it takes to complete projects, could be months or years after the obligation is made. As phases of the projects are completed, states submit vouchers to FHWA to be reimbursed from the Highway Account. Consequently, DOT cannot directly control outlays—outlays are determined through limitations on obligations.

[7]The Transportation Equity Act for the 21st Century (TEA-21), Pub. L. No. 105-178, 112 Stat. 107 (1998), and SAFETEA-LU amended the rules of the House of Representatives to specify that it is out of order to consider a bill, joint resolution, amendment, or conference report that would result in funding at a lower level than the amounts set in the authorization acts, as adjusted.

[8]In most cases, allocated funds are distributed among the states according to statutory criteria. In some cases, Congress directs that allocated funds be used for specific projects. Congress may do this either in the legislative language or in committee reports accompanying the legislation. An example of congressionally directed funds in SAFETEA-LU is funding for High Priority Projects.

Figure 3: Process for Collecting and Distributing Highway Account Receipts



Source: GAO.

Two mechanisms are intended to help keep the Highway Account solvent by making annual adjustments to ensure there are adequate funds to reimburse states (through the Byrd Test) and align outlays with actual revenues (through RABA).

- **Byrd Test**. In 1956, Congress was concerned that the proceeds of the taxes to be deposited in the Highway Trust Fund might not be sufficient to reimburse states when the states submitted their claims. To address this concern, Congress amended the bill under consideration to require DOT to compare current and projected resources with existing and projected unpaid authorizations and to adjust the amounts apportioned to the states if the two were out of balance.[9] This comparison was referred to as the Byrd Amendment or the Byrd Test. Under the Byrd Test, as modified by SAFETEA-LU, unpaid commitments in excess of amounts available in the Highway Account at the end of the fiscal year in which the apportionment is to be made must be less than the revenues anticipated to be earned in the following 4-year period. If a shortfall is projected using this test, the apportionments to the states from the Highway Account would be deferred proportionately until a recalculation shows that some or part of the deferred apportionments can be released without triggering the Byrd Test.[10] Prior to SAFETEA-LU, estimated unpaid commitments at the end of the year were required to be less than revenues anticipated to be earned in the following 24-month period. In the history of the Highway Trust Fund, the Byrd Test has twice triggered adjustments to apportionments: 1961 and 2004.[11]

- **RABA**. Established in the Transportation Equity Act for the 21st Century (TEA-21) in 1998 and modified in SAFETEA-LU, RABA was designed to align Highway Account program levels with actual revenues and help assure that the account is used to fund highway programs instead of accumulating large balances. RABA provisions require DOT, as part of the annual budget submission process, to compare current revenue estimates with revenue estimates in the multiyear authorization act, most recently SAFETEA-LU. Based on these comparisons, DOT is required to adjust both contract authority and obligation limitations either upward, when the account has greater revenues than projected, or downward, when revenues do not meet projected levels.[12] However, under SAFETEA-LU, no

[9]DOT performs this test four times per year, but the results of the test are most significant when apportionments are about to be made, usually at the beginning of the fiscal year.

[10]If the period of availability for obligation of the deferred apportionments lapses (generally, the period of availability is 4 years) before the apportionments can be released, the lapsed amounts are permanently lost.

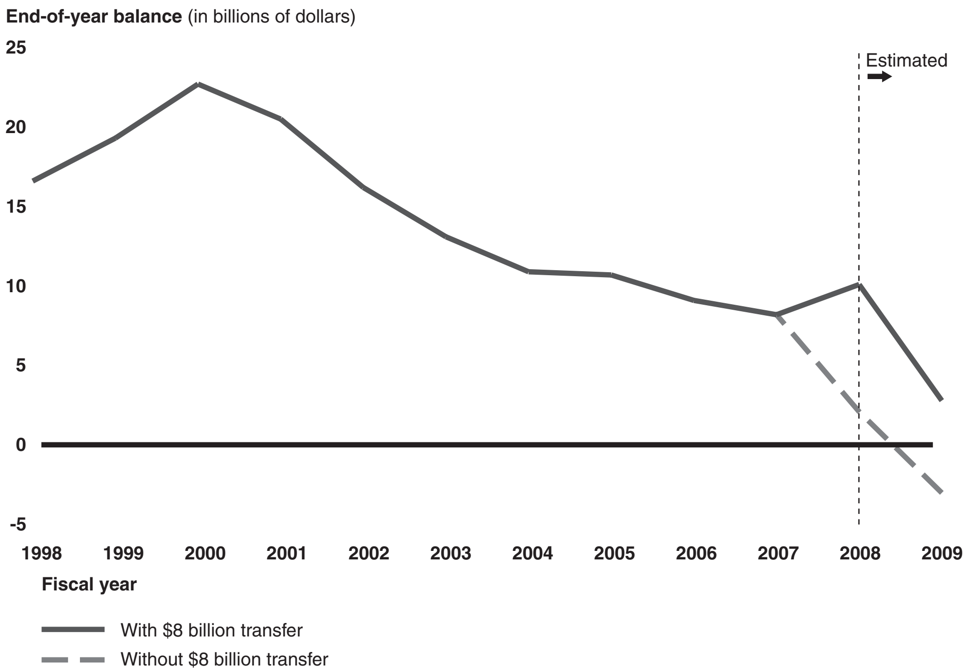
[11]As a result of triggering the Byrd Test, Interstate System construction apportionments for fiscal year 1961 were reduced; for fiscal year 2004, all Highway Account apportionments were reduced.

[12]The adjustment of annual authorizations is called RABA, but this term is often used to refer to the entire adjustment process.

downward adjustments will be made in a fiscal year if, as of October 1 of that fiscal year, the balance in the Highway Account is more that $6 billion. SAFETEA-LU also modified how the RABA adjustments were calculated in order to smooth out the effects of the adjustment over 2 fiscal years.

Despite these mechanisms, Highway Account revenues were insufficient to cover outlays, and the balance of the Highway Account has declined from fiscal year 2000 to 2008. As shown in figure 4, the account approached a zero balance near the end of fiscal year 2008; legislation on September 15, 2008—to provide $8 billion to replenish the account—and the final receipts deposit of about $2 billion[13] for fiscal year 2008 on October 8, 2008 resulted in a final fiscal year 2008 balance of about $10 billion.

Figure 4: Highway Account Balance, Fiscal Years 1998 through 2009



Source: GAO analysis of FHWA data.

[13]The $2 billion year-end receipt represents the final deposit from Treasury for fiscal year 2008. Treasury normally makes final year-end deposits for all trust funds in early October; these final deposits are routinely included in the year-end balance, although the funds are not available in that fiscal year for reimbursement to states.

Notes: The 2008 estimated balance includes a final fiscal year 2008 Treasury deposit of about $2 billion on October 8, 2008. Receipts for last quarter of fiscal year 2008 are anticipated to be certified by IRS in February 2009.

The 2009 estimated balance is based on a midsession review from July 2008.

Several Events Led to the Decline in the Balance of the Highway Account

SAFETEA-LU authorization levels, combined with lower than anticipated receipts, caused the Highway Account balance to decline over the authorization period. Although DOT has reported since February 2006 that the Highway Account balance would be depleted in fiscal year 2009 and recommended several actions to offset the decline, DOT officials acknowledge that communication with stakeholders on the status of the Highway Account could be improved and are developing a plan to improve communication.

SAFETEA-LU Authorizations and Lower-Than-Anticipated Receipts Led to the Decline of the Highway Account Balance

Estimated outlays from Highway Account programs under SAFETEA-LU exceeded estimated receipts throughout the authorization period by about $10.4 billion.[14] While estimated outlays for fiscal years 2005 through 2009 totaled $182 billion (ranging from $31.3 billion in fiscal year 2005 to $40.7 billion in fiscal year 2009), estimated receipts totaled $171.6 billion (ranging from $31.6 billion in fiscal year 2005 to $36.2 billion in fiscal year 2009). Based on the estimated outlays and receipts included in SAFETEA-LU, the Highway Account balance would be drawn down from $10.8 billion to about $0.4 billion over the authorization period, providing more federal funding for highway projects. This left little room for error. Assuming all outlays were spent, a revenue shortfall of even 1 percent below what SAFETEA-LU had predicted over the 5-year period would result in a cash shortfall in the account balance. Given the inherent uncertainty associated with estimating receipts and outlays over multiple years, a cash shortfall was always a real possibility.

In fact, actual Highway Account receipts were lower than had been estimated in SAFETEA-LU, particularly for fiscal year 2008. As a result, the account balance dropped more precipitously than had been anticipated and was nearly depleted in August 2008—1 year earlier than the end of the SAFETEA-LU authorization period. Account receipts were lower in fiscal year 2008 due to a weakening economy and higher motor fuel prices that resulted in fewer truck sales and lower motor fuel purchases—the two

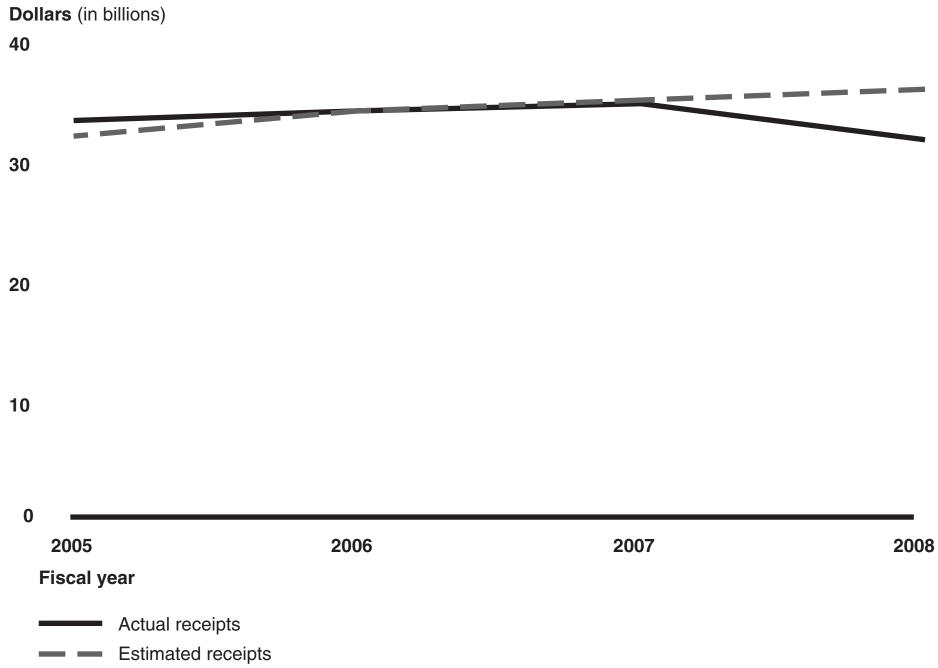
[14] Outlay estimates in SAFETEA-LU are partly based on obligations incurred in the previous reauthorization—TEA-21—as outlays can spend out over a number of years.

major sources of Highway Account revenue. Revenue associated with truck, bus, and trailer sales accounted for the largest decline—$2.4 billion (from $3.8 billion to $1.4 billion)—during fiscal year 2008. In addition, through September 2008, drivers drove 3.5 percent less compared with the first 9 months of 2007 as prices rose[15] from $3.02 to $3.71 per gallon for gasoline and from $3.31 to $4.02 per gallon for diesel for the same period.[16] Fewer miles driven resulted in fewer gallons of motor fuel purchased, which, in turn, translated into a decline in tax receipts of about $0.53 billion—about $0.083 billion for gasoline and about $0.45 billion for diesel. As a result, receipts for the Highway Account for fiscal year 2008 were $31.3 billion—about $4 billion less than the $35.4 billion estimate for that year (see fig. 5).

[15]U.S. Department of Transportation, Federal Highway Administration, Office of Highway Policy Information, Traffic *Volume Trends: September 2008* (Washington, D.C., 2008).

[16]U.S. Department of Energy, Energy Information Administration, *Monthly U.S. Regular Conventional Retail Gasoline Prices* and *Monthly U.S. No 2 Diesel Retail Sales by All Sellers* (Washington, D.C., 2008).

Figure 5: Actual Highway Account Receipts Compared with Receipt Estimates in SAFETEA-LU, Fiscal Years 2005 to 2008



Source: GAO analysis of FHWA data.

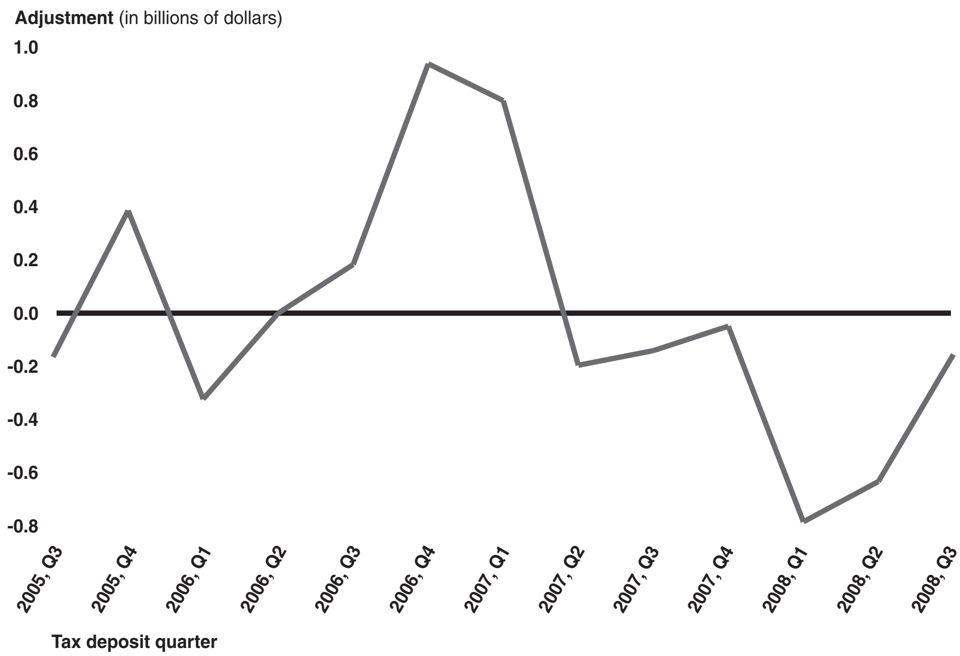
Note: Receipts for last quarter of fiscal year 2008 are anticipated to be certified by IRS in February 2009.

In addition, the effect of the lower receipts on the Highway Account was not fully recognized until well after the decline began because receipts are not confirmed until the IRS certifies the actual amount of receipts allocated to the account—a process that can take about 4.5 months after the end of each calendar quarter. Thus, the Highway Account operates using Treasury estimates of tax receipts to be allocated to the account until certification is completed. Treasury made a downward adjustment to the Highway Account of about $783 million on May 14, 2008, based on the difference between certified and estimated receipts from the first quarter of fiscal year 2008.[17] Another downward adjustment of about $631 million based on the difference between certified and estimated receipts from the second quarter of fiscal year 2008 occurred on August 18, which placed the

[17]The May downward adjustment was not included in the President's Mid-Session Review, which is the basis for projecting future estimates of the Highway Account balance.

account in imminent risk of a shortfall. These downward adjustments—which were at least twice as large as other downward adjustments made during the SAFETEA-LU authorization period—occurred during the seasonal peak of outlays, the summer months when most highway projects are under construction and states request reimbursement from DOT. Quarterly adjustments to the Highway Account have varied during SAFETEA-LU (see fig. 6).

Figure 6: Quarterly Adjustments to Highway Account Receipts Based on IRS Certification of Actual Results during SAFETEA-LU, Fiscal Years 2005 to 2008



Source: GAO analysis of FHWA data.

DOT Recommended Actions to Offset the Decline and Implemented Cash Flow Management Procedures, but Communication with Stakeholders Could Be Improved

Beginning in February 2006, DOT reported several times that there could be a shortfall in the Highway Account during fiscal year 2009 and recommended corrective actions to offset the decline.

- In February 2006—based on the President's fiscal year 2007 budget, which had lowered forecasted receipts based on a marked increase in crude oil prices—DOT projected a continuous decline in the Highway Account balance and a shortfall of $2.3 billion during fiscal year 2009. DOT noted that two commissions established in SAFETEA-LU would provide information on potential alternatives to support highway and transit funding.[18] DOT also stated at that time that the next reauthorization would need to address whether the Highway Trust Fund has become insufficient to fund transportation programs.

- In February and July 2007, DOT proposed forgoing an anticipated upward RABA adjustment to the obligation limitation for fiscal year 2008, estimating a Highway Account shortfall of up to $3.8 billion in fiscal year 2009 with no RABA adjustment. However, instead of forgoing the upward RABA adjustment, Congress increased the obligation limitation by $1 billion, to be used for bridge construction projects in the wake of a bridge collapse on August 1, 2007.

- In February 2008, DOT projected a shortfall of about $3.1 billion in the Highway Account in fiscal year 2009 and proposed a downward RABA adjustment of $1 billion as well as a further $800 million reduction in obligation limitations for fiscal year 2009. DOT also requested legislative authority for repayable advances from the Mass Transit Account to cover the projected Highway Account shortfall through fiscal year 2009. In July 2008, Congress proposed legislation to appropriate $8 billion from the General Fund of the Treasury to address the projected shortfall. Although DOT initially opposed the legislation, in part because the $8 billion would come from the General Fund of the Treasury, the agency requested that Congress pass the legislation in September so that states would not be adversely affected.

Indicators throughout the spring and summer of 2008—such as the downward adjustment to the Highway Account in May, the weakening

[18]Congress created the National Surface Transportation Policy and Revenue Study Commission and the National Surface Transportation Infrastructure Financing Commission in SAFETEA-LU to assess potential alternatives to the motor fuel tax as the principal revenue source for the Highway Trust Fund.

economy, evidence of fewer vehicle miles traveled, and a reduction in Treasury receipts—pointed toward a continuing decline in the account balance. According to DOT officials, based on the Mid-Session review released in July 2008, they estimated that the Highway Account balance would still be positive—about $4.3 billion—at the end of fiscal year 2008. However, DOT officials told us that after the August downward adjustment based on certified tax receipts, they realized that the account might reach a zero balance before October 2008.

In preparation for an anticipated decline in the Highway Account in fiscal year 2009, DOT explored options for keeping the account solvent to avoid violating the Antideficiency Act, which prohibits FHWA from reimbursing states unless there are sufficient funds available in the Highway Account.[19] Since DOT cannot decrease outlays that have been obligated, the agency focused on slowing down the rate of outlays—payments made to states twice each day—to better match Treasury semimonthly deposits of receipts to the Highway Account. DOT also asked all DOT agencies that receive Highway Account funds to turn in excess cash. As DOT does not have statutory authority to borrow, DOT recognized that once the cash in the Highway Account was depleted, the agency would have been unable to cover outlays until the next Treasury payment was deposited to the account. DOT officials consulted with Treasury officials on whether the frequency of receipt deposits to the account could be increased; Treasury officials responded that they could temporarily increase the frequency of deposits, but that there would be little benefit. On September 5, 2008, DOT announced that FHWA would begin reimbursing states on a weekly basis (rather than twice daily) on the following Monday and that the agency supported draft legislation to appropriate $8 billion from the General Fund of the Treasury to the Highway Account.[20] DOT also considered making

[19]The Antideficiency Act prohibits an officer or employee of the federal government from incurring an obligation, or making an expenditure, in advance or in excess of an appropriation. 31 U.S.C. § 1341(a)(1). The Federal-Aid-Highway Program is funded primarily with contract authority, and programs funded with contract authority can incur obligations in advance of an appropriation. However, DOT cannot make cash reimbursements to the states until liquidating cash is appropriated from the Highway Account. For example, the fiscal year 2008 Consolidated Appropriations Act provides a liquidating appropriation from the Highway Fund of $41.9 billion or what is available in the Highway Account. If there are no receipts in the Highway Account, DOT would incur an expenditure in excess of an appropriation and thus violate the Antideficiency Act.

[20]FHWA made three weekly payments to states using this method before Congress passed legislation for the $8 billion appropriation from the General Fund of the Treasury. As a result of moving to a weekly payment schedule, Treasury was required to pay interest to states on the delayed payments; DOT estimates the interest totaled about $100,000.

prorated payments to states—based on the percentage of funds available to cover all reimbursements—if the account balance dropped below $1 billion. Although the account balance dropped from $8.1 billion at the beginning of fiscal year 2008 to below $1 billion on August 22, FHWA ultimately did not implement this measure because the cash balance rose above $1 billion the next business day—August 25—when Treasury semi-monthly receipts were deposited.[21]

In light of the indicators throughout the spring and summer of 2008 that the Highway Account balance was approaching a zero balance faster than previously anticipated, we believe DOT officials could have communicated with state DOT agencies and Congress in a more timely manner on the status of the account and their efforts to keep it solvent. In a letter to state DOT agencies dated July 8, 2008, FHWA stated that, in the event of a shortfall in the Highway Account—still anticipated in fiscal year 2009—reimbursements to states would be delayed. DOT officials knew that the account's solvency was in question after the August downward adjustment and anticipated changing its cash management procedures, but did not publicly inform state DOT agencies until Friday, September 5 that prorated payments could go into effect the following Monday, September 8. If DOT were to implement prorated payments, state DOT agencies would then need to fund the difference between the DOT prorated payment and their obligations to contractors. State DOTs, particularly those with scheduled Grant Anticipation Revenue Vehicles (GARVEE) bond payments, were concerned of the potential impact on their ability to pay their debt service.[22] More timely communication could have allowed states to plan for changing circumstances. DOT officials acknowledge that earlier communication is desirable and are developing a plan—including a framework for notifying the Secretary of Transportation, Congress, OMB, state DOT agencies, and other stakeholders of a pending shortfall—to improve communications in the future.

[21]According to DOT, these cash balances do not include cash held by two other DOT entities—the Federal Motor Carrier and Safety Administration and the National Highway Transportation Safety Administration—or the Miscellaneous Highway Trust Fund account cash balance.

[22]A GARVEE is a debt-financing instrument authorized to receive federal reimbursement of debt service and related financing costs.

Improved Mechanisms Could Help Maintain Highway Account Solvency

Improving the mechanisms that DOT uses to monitor the Highway Account balance—including improving existing mechanisms to make annual adjustments to the account and developing additional indicators to help DOT monitor and manage the account balance throughout the year—could help maintain the solvency of the account. Ultimately, however, without either reduced expenditures or increased revenues, or a combination of the two, Highway Account shortfalls will continue.

Modifying and Implementing Existing Mechanisms Could Help DOT Make Annual Adjustments to the Highway Account

Although the Byrd Test was intended to help the federal government ensure there were sufficient funds in the Highway Account when states submitted their claims, under SAFETEA-LU, the test has no effect. First, SAFETEA-LU expanded the interval over which future estimated receipts are included in the calculation from 2 to 4 years, thereby increasing the amount of receipts that would be compared to unpaid commitments in the coming year. This modification made it more difficult for the test to signal a decline in the Highway Account balance. According to a DOT analysis—prepared at GAO's request—of the impact on the Highway Account had the test remained at 2 years rather than 4, the account would have failed the Byrd Test annually for fiscal years 2005 through 2008. In other words, the existing account balance each year plus the amount of receipts anticipated to be received over the next 2 years would have been insufficient to offset unpaid commitments in the next year. According to DOT officials, it would be nearly impossible for the Highway Account to fail the Byrd Test using a 4-year window, but triggering a 2-year Byrd Test provides one of the first tangible indicators that a shortfall is imminent.

Second, even if the Highway Account had failed the Byrd Test, the resulting adjustment prescribed by the test—deferring the amount of contract authority apportioned to states—would not have curtailed future outlays from the account because the guaranteed funding levels (obligation limitations) for states in SAFETEA-LU are already lower than apportioned contract authority. For example, DOT's analysis of the effect of a 2-year Byrd Test on the Highway Account balance showed that the account would have failed the test in fiscal year 2005 because the amount of anticipated receipts fell short of anticipated outlays by $1.2 billion, indicating that $1.2 billion in apportioned contract authority to states should be deferred. However, because the amount of contract authority as of fiscal year 2005 exceeded the guaranteed funding level by more than $1.2 billion, adjusting contract authority would have not affected the amount that states were able to obligate.

In contrast, RABA is designed to affect obligation limitations and, if implemented as originally intended, could help align Highway Account spending with actual revenues. For example, in 2003, the RABA calculation called for a negative adjustment in obligation limitations of about $4.4 billion—from about $27 billion to about $23 billion—but Congress waived the negative RABA adjustment for that year as part of a supplemental appropriations act.[23] Congress chose instead to increase the obligation limit to $31.8 billion. We asked DOT to run a simulation to estimate the Highway Account balance for fiscal years 2003 to 2008, assuming the calculated downward RABA adjustment in 2003 had not been waived. According to the simulation, the account balance at the end of fiscal year 2008 would have been about $6 billion if no other changes had been made.[24] Under this scenario, the account balance would have been sufficient to reimburse states without the $8 billion infusion from the General Fund of the Treasury.

DOT officials we spoke with stated that RABA could be an effective mechanism if obligation limitations are better aligned with outlays and receipts. However, they said that the provision enacted in SAFETEA-LU requiring no negative adjustments in a fiscal year if the Highway Account balance is greater than $6 billion as of October 1 of that fiscal year may not provide a sufficient cushion to offset a possible shortfall. For example, a negative RABA adjustment of about $1 billion for fiscal year 2009 was not implemented because the Highway Account balance was greater than $6 billion as a result of the $8 billion appropriation from the General Fund. However, DOT officials said that, although they currently project a balance of about $2.7 billion in the account at the end of fiscal year 2009 (using Treasury receipt estimates released in July),[25] the account could reach a zero balance prior to the end of the fiscal year if receipts continue to be lower than anticipated and that the RABA adjustment could help delay or reduce the magnitude of such a shortfall.

[23] See the 2002 Supplemental Appropriations Act for Further Recovery from and Response to Terrorist Attacks on the United States, Pub. L. No. 107-206, § 1402, 116 Stat. 820, 898 (2002).

[24] The $6 billion estimate includes a $2 billion deposit to the Highway Account from the Treasury on October 8, 2008, but not the $8 billion appropriation from Treasury's General Fund on September 15, 2008.

[25] DOT combines its own estimates of outlays with Treasury's estimates of revenues to create an estimate of the Highway Account balance; CBO projects revenues and outlays to develop an estimate.

Effective mechanisms to annually evaluate the solvency of the Highway Account and make appropriate adjustments are important to maintaining account solvency because DOT has no control over revenues and can manage outlays only indirectly through annual obligation limitations, which are determined in legislation months or years prior to when states are reimbursed from the account. Without such mechanisms, the account balance runs the risk of declining to a level at which it may not be able to withstand a sudden drop in revenues. DOT officials agree that both of the existing solvency mechanisms have their roles in helping to maintain Highway Account solvency, although RABA has the greater potential to affect spending.[26] They also noted that solvency mechanisms—even with improvements—would be effective only if the authorization act sets account outlays in proportion to estimated program receipts and that neither mechanism is designed to deal with near-term shortfalls in the Highway Account balance.

Monitoring Additional Indicators throughout the Year Could Help DOT Anticipate Sudden Declines in the Highway Account Balance

In addition to modifying existing mechanisms that are applied annually, monitoring indicators throughout the year that could signal sudden changes in the Highway Account revenues could help DOT better manage the account balance and anticipate changes. Monitoring the account balance is particularly important during times when the account balance drops to a level at which a sudden decline in revenues or increase in outlays could put the account at risk of reaching a zero balance. Indicators that DOT could monitor throughout the year include data from Treasury's monthly statements and vehicle miles traveled (VMT) data from FHWA. According to DOT officials, as a result of the decline in account revenues last summer, they are more experienced in cash management for the account and are exploring additional indicators that could be used to monitor the account balance on a daily basis. Regular monitoring of indicators that affect revenue flowing into the Highway Account would improve DOT's ability to anticipate whether a downward adjustment might occur when receipts are certified by IRS.

Monitoring additional indicators would also enhance DOT's plan for communicating with stakeholders on the status of the Highway Account. Specifically, establishing trigger points for key indicators would prompt

[26]RABA adjustments to obligation limitations have the largest impact the year after the adjustment is made because a significant portion of the Highway Program outlays are in the year following obligation.

DOT to report to stakeholders on potential problems. For example, one indicator could be the account balance, and the trigger could be when the balance drops below a certain level. However, since the account balance typically varies throughout the year—building up during winter months when states are not able to work on road projects and drawing down during summer months as projects are implemented and states submit vouchers for reimbursement—the trigger could vary accordingly. According to DOT officials, they are closely monitoring the account balance and plan to communicate regularly with stakeholders.

Although Improving Mechanisms Could Help Maintain Highway Account Solvency, Other Measures Are Needed to Ensure Long-Term Fund Sustainability

Although improved mechanisms could help maintain the solvency of the Highway Account, ultimately, without either reduced expenditures or increased revenues, or a combination of the two, shortfalls will continue. In the past, we have reported that the following strategies could be used to better align expenditures and revenue:

- **Ensure current revenue sources (i.e., fuel taxes) are aligned with outlays**. The Highway Account's current source of revenue could be better aligned with actual outlays. According to CBO and others, the existing fuel taxes could be altered in a variety of ways to address the erosion of purchasing power caused by inflation, including increasing the per-gallon tax rate and indexing the rates to inflation.

- **Ensure users are paying fully for benefits**. Revenues can also be designed to more closely follow the user-pay concept—that is, require users to pay directly for the cost of the infrastructure they use. This concept seeks to ensure that those who use and benefit from the infrastructure are charged commensurately. Although current per-gallon fuel taxes reflect usage to a certain extent, these taxes are not aligned closely with it and do not convey to drivers the full costs of road use—such as the costs of congestion and pollution. We have reported that other user-pay mechanisms—for example, charging according to vehicle miles traveled, tolling, implementing new freight fees for trucks, and introducing congestion pricing (pricing that reflects the greater cost of traveling at peak times)—may better recoup costs.

- **Supplement existing revenue sources**. We have also reported on strategies to supplement existing revenue sources. A number of alternative financing mechanisms—such as enhanced private-sector participation—can be used to help state and local governments finance surface transportation. These mechanisms, where appropriate, could help meet growing and costly transportation demands. However, these potential financing sources are forms of debt that must ultimately be repaid.

- **Improve the efficiency of current facilities**. Finally, better managing existing system capacity and improving performance of existing facilities could minimize the need for additional expenditures. We have reported that the efficiency of the nation's surface transportation program is declining and that the return on investment could be improved in a number of ways, including creating incentives to better utilize existing infrastructure.

Furthermore, sustainable surface transportation programs require targeted investment with adequate return on investment from not only the federal government but also state and local governments and the private sector. Many current surface transportation programs are not effective at addressing key challenges because federal goals are numerous and sometimes conflicting; roles are unclear; programs lack links to the performance of the transportation system or of the grantees; and some programs do not use the best goals and approaches—such as rigorous economic analysis—to ensure effective investment decisions. Consequently, GAO has called for a fundamental re-examination of the surface transportation program.

Conclusions

Drawing down the account balance over the SAFETEA-LU authorization period provided additional federal funding for state highway projects, but it also reduced the account balance to a level at which it was not able to withstand the sudden downturn in revenues in fiscal year 2008. While DOT's cash management efforts in August kept the account solvent until Congress could approve the $8 billion appropriation from the General Fund of the Treasury, such ad hoc efforts should not be part of a fiscally sound, sustainable funding approach. If Congress's goal is to maintain the Highway Account at a minimum balance in order to maximize funding provided to states, then improved mechanisms are needed to help keep the account solvent. Specifically, modifying and implementing existing mechanisms that help DOT annually evaluate account solvency and propose adjustments is important because adjusting obligation limitations is DOT's only option for managing the amount of funds that eventually are distributed to states. Furthermore, monitoring indicators throughout the year—such as VMT—could help DOT better anticipate changes in account revenues. In addition to improved solvency mechanisms, another critical aspect of maintaining the account balance at a minimum level is communicating with stakeholders on the status of the account. Acting on "lessons learned" from the summer of 2008, DOT is developing a communication plan to augment existing communication channels. In light of another potential shortfall in the account in fiscal year 2009, monitoring the account balance and communicating regularly with Congress are particularly relevant. It is also important to note that without either reduced expenditures or increased revenues, or a combination of the two, Highway Account deficits will likely continue.

Recommendations for Executive Action

To improve DOT's communication with stakeholders on the status of the Highway Account and the mechanisms the agency uses to help maintain account solvency, we are recommending that the Secretary of Transportation take the following three actions:

- Identify changes to existing solvency mechanisms designed to make annual adjustments to the Highway Account and communicate to Congress the potential benefits and limitations of these changes.
- Monitor additional indicators that can impact the account balance throughout the year to better anticipate sudden changes in the balance.
- Include in its proposed communication plan a periodic reporting schedule that includes information on the status of the Highway Account balance—based, in part, on information gained from monitoring additional indicators—and actions that may be needed to maintain account solvency.

Agency Comments and Our Evaluation

DOT officials reviewed a draft of this report and provided comments through e-mail. The officials generally agreed with the report's findings and recommendations and provided technical corrections, which we incorporated as appropriate. While they agreed that the account's solvency mechanisms could be improved, they noted that even improved mechanisms would be effective only if the account balance is at a sufficient level to withstand sudden declines in receipts, and future program levels are set to match estimated program receipts.

As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the report date. At that time, we will send copies to interested congressional committees and the Secretary of Transportation. This report will also be available at no charge on the GAO Web site at www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-2834 or herrp@gao.gov. Contact points for our Offices of Congressional Relations and Public affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix I.

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Appendix I: GAO Contact and Staff Acknowledgments

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Staff Acknowledgments

In addition to the contact named above, Sara Vermillion (Assistant Director), Richard Calhoon, Jay Cherlow, Patrick Dudley, Carol Henn, Hannah Laufe, Maureen Luna-Long, and Amy Rosewarne made key contributions to this report.

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