MFP COMMITTEE # 5
April 19, 2007
Discussion

M E M O R A N D U M

TO: Management and Fiscal Policy Committee

FROM: Glenn Orlin, Deputy Council Staff Director
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SUBJECT: **Discussion:** Infrastructure financing

The Council on April 10 introduced a resolution sponsored by Councilmembers Floreen, Ervin, Knapp, and Leventhal to appoint a working group of 7 public finance and transportation experts (plus ex-officio staff representatives from the Executive Branch, Planning Board, and Council) to "recommend appropriate funding strategies to raise at least $50 million annually in Montgomery County for transportation capital projects in the County. The Working Group will determine an equitable allocation of financial obligation with a clear and predictable revenue stream." The final report from the Working Group would be due by July 1, 2007. The resolution is on ©1-2.

This packet will provide an overview of past and current transportation infrastructure financing in the County, a chronology of the major initiatives over the past 20 years, including previous task forces, that proposed new revenue sources for transportation infrastructure, and implications for this year's work on the County Growth Policy.

1. Transportation capital funding in Montgomery County. Transportation capital funding — funds for planning, design, and construction of new, expanded, or rehabilitated projects — comes primarily from 3 sources: the State, the County, and development exactions that are conditions of subdivision approvals. Nearly all Federal transportation funding is funneled through the Maryland Department of Transportation, and so is considered here as primarily a form of State revenue.

The State publishes programmed expenditures by project, not by County. Nevertheless, the State is traditionally the largest contributor to transportation capital funding in Montgomery County. The State is responsible for all improvements to "numbered" highways — such as I-270, US 29, MD 97, etc. — as well as for the improvements to Metrorail and Metrobus that would be otherwise attributable to the County, and MARC commuter rail improvements. However, at various times the County has contributed some of its own resources to the help pay for these State responsibilities.

The County's transportation capital investments for the past 3 decades have been smaller, yet significant. The trend of transportation program funding (excluding WMATA) over the last 20 years is shown below. The programmed levels in the FY94-99 and FY95-00 CIPs proved artificially high because they included about $22 million and $36 million, respectively, in future Construction Excise Tax (CET) funding, but that tax was never implemented.

Funds Programmed for Transportation Projects (% of All Funds Programmed)

	Actual Dollars	*Yr. 2007 Dollars*
Approved FY87-92 CIP	$403,865,000 (29.9%)	$719,781,000
Approved FY88-93 CIP	$503,732,000 (34.6%)	$861,904,000
Approved FY89-94 CIP	$544,811,000 (32.8%)	$881,709,000
Approved FY90-95 CIP	$578,108,000 (28.0%)	$883,309,000
Approved FY91-96 CIP	$387,826,000 (19.9%)	$568,896,000
Approved FY92-97 CIP	$360,925,000 (18.9%)	$516,465,000
Approved FY93-98 CIP	$327,578,000 (18.4%)	$454,573,000
Approved FY94-99 CIP	$358,192,000 (22.4%)	$377,893,000
Approved FY95-00 CIP	$319,813,000 (19.2%)	$426,746,000
Approved FY96-01 CIP	$248,018,000 (15.7%)	$321,920,000
Approved FY97-02 CIP	$239,756,000 (18.5%)	$305,639,000
Amended FY97-02 CIP	$276,716,000 (13.7%)	$348,264,000
Approved FY99-04 CIP	$347,500,000 (17.6%)	$428,536,000
Amended FY99-04 CIP	$373,599,000 (15.8%)	$446,163,000
Approved FY01-06 CIP	$387,335,000 (15.8%)	$450,835,000
Amended FY01-06 CIP	$408,403,000 (20.2%)	$464,419,000
Approved FY03-08 CIP	$396,604,000 (18.0%)	$438,581,000
Amended FY03-08 CIP	$433,416,000 (18.3%)	$468,013,000
Approved FY05-10 CIP	$519,139,000 (18.3%)	$547,550,000
Amended FY05-10 CIP	$529,084,000 (18.0%)	$542,840,000
Approved FY07-12 CIP	$680,032,000 (19.2%)	$680,032,000

The objective of this resolution is to add $50 million more in transportation capital funding each year. The most aggressive assumption is that such additional revenues would be available by mid-FY08. Therefore, $225 million might be added in the FY07-12 CIP, reaching about $905 million, a 33% increase over the 6-year program period. It would represent 24% of CIP funding for all County agencies. It would increase transportation's budget higher than in any CIP approved during the past 20 years. Its portion of total CIP funding would be higher than in any CIP approved since the beginning of the 1990s, but still well lower than the CIPs of the late 1980s.

The County's programmed funding for transportation projects in the Approved FY07-12 CIP, by subcategory and revenue source, is shown on ©3-6. Unlike the list above, these tables capture both the $680,032,000 spending on County projects (©3-5) and $17,094,000 in spending on WMATA projects (©6). In sum, the revenue sources break down as follows:

Transportation Funding in the Approved FY07-12 CIP, by Funding Source

Revenue Source	Funding	% of Total
G.O. bonds	$339,747,000	48.7%
Impact tax	102,400,000	14.7%
Revenue bonds: Liquor Fund	80,000,000	11.5%
Federal aid	56,011,000	8.0%
Current revenue: General Fund	39,952,000	5.7%
Current revenue: Parking Districts	20,467,000	2.9%
State aid	15,704,000	2.3%
Other sources	42,845,000	6.2%

Two caveats should be noted about this chart. First, the Council recently changed its revenue assumptions for transportation impact taxes such that the CIP to be reconciled will carry only $64 million of expenditures. Thus $38.4 million will be shifted from the impact tax to G.O. bonds, reducing the impact tax's contribution to 9.2% of the total, and raising the G.O. bonds' contribution to 54.2%. Second, the Federal aid contribution is as high as it is only temporarily, due to the $52,317,000 earmark for the Silver Spring Transit Center project. Once that project is complete, future CIPs likely will have negligible Federal aid.

Development exactions are also significant. Development has always been required to build the on-site streets in a new subdivision because they are needed for access to each property. During the past 30+ years, however, the governing premise in this County has been that new development should pay a share of the off-site transportation improvements needed to address the additional traffic generated by the development. This was first manifested during the 1970s with Planning Board conditions on individual subdivision approvals, and enhanced by the road clubs of the 1980s and, more recently, by development districts in Germantown and Clarksburg. There are no reliable estimates as to how much new development has paid directly for these off-site transportation improvements, but roads in some areas — notably Germantown — were financed largely by exactions. In Germantown, improvements to key segments of MD 118, MD 355, MD 117, Father Hurley Boulevard, Middlebrook Road, Wisteria Drive, and other major roads were paid through forms of development exaction.

The revenue projected from State, County, and private sources fall well short of the need. We are halfway through the lifespan of the Council's 10 Year Transportation Plan; although there has been measured progress on the smaller projects (particularly bridge replacements, intersection improvements, and parking garages), there is a decided lack of progress towards building new roads, widening roads, and building light rail lines and other transitways (see ©7).

The cost of the Plan, which does not include many other master-planned facilities thought to be needed beyond 10 years, was $7 billion in Year 2002 dollars. In current dollars the cost translates to $9-10 billion. About $1 billion has been spent on completed projects over the past 5 years, and about $3.5 billion is programmed over the next 5 years, most of which is for the Intercounty Connector. This leaves a $5 billion deficit from State, County, and private sources.

The resolution's objective to raise an additional $50 million per year for transportation is reasonable considering the County's share of this deficit. However, the bigger problem must be solved at the State level (where there has not been a significant revenue increase since 1992) and the Federal level, which has traditionally been the source of most funding for mega-projects like the Purple Line, Corridor Cities Transitway, and widenings of the Beltway and I-270.

2. Past initiatives, including task forces. This section outlines the major efforts over the last 2 decades to find new revenue sources for infrastructure:

Road clubs (early 1980s). These were established to allow multiple builders developing in a common area to share the cost of a road improvement required as a condition of subdivision approval. New homes were required to pay $300 annually to cover the developer's principal and interest for major off-site road improvements. Two of the first road clubs were established in Germantown to build relocated MD 118 through what is now the Germantown Town Center.

Consensus Committee on Growth Management (1985). The 'Consensus Committee' appointed by the Council consisted of 11 voting members: 5 business representatives, 5 civic representatives, and the chair, former Councilmember William Colman. The principal purpose was "to determine short-term congestion on roads and in schools during the next three years while permitting growth to continue in the County at levels that will not subject citizens to further unacceptable traffic density." Regarding infrastructure financing, the committee recommended:

1. Primary reliance on general property tax as revenue source for such expansion;
2. Facilitation of property tax utilization through more use of special taxing districts;
3. Imposition of a county gasoline tax for transportation purposes other than Metro (6-5 vote);
4. Imposition of a county auto registration fee (6-5 vote); and
5. Use of impact fees imposed on new development to allow 50-50 private sharing of transportation facility expansion costs in planning areas where thresholds [staging ceilings] have been reached or exceeded, to be replaced by county revenue sources as soon as possible (6-5 vote).

The majority in the 6-5 split votes consisted of the business representatives and the chair. The Committee considered several other revenue measures, but did not recommend them. The Executive summary is on ©8-12.

Countywide Construction Excise Tax (1986, 1991-1994). Councilmember David Scull proposed a countywide excise tax that would have collected $3.25/sf on most new development, with the revenue to be used for public school projects. The Council enacted the bill, but it was vetoed by County Executive Gilchrist and the Council did not override the veto.

In 1991 the Council again approved a countywide Construction Excise Tax of $4/sf for office and retail uses, $2.40/sf for industrial uses, $3.75/sf for single-family units or additions, $3/sf for multi-family units or additions, and $1/sf for non-profit space. County Executive Neal Potter signed the tax into law, but the Council delayed its effective date several times during the early 1990s due to sluggish growth and a crippled building industry. The Council ultimately repealed the never-implemented tax in 1994.

Transportation impact fee/tax (1986-present). County Executive Gilchrist proposed impact fees on new development to fund master-planned improvements that would increase transportation capacity. He initially proposed fees in three areas: Germantown, Clarksburg, and Eastern Montgomery County (Fairland/White Oak and Cloverly). However, he retracted his proposal for fees in Clarksburg when Planning Board Chairman Norman Christeller argued that an impact fee there would generate premature development pressure. The Council enacted the impact fee law during spring 1986, and it took effect the following August.

The law has been revised many times in the past 2 decades. The fee rates were amended biennially to reflect construction cost inflation, updated master plans, and other policy changes. In 1998 State road improvements were dropped from the list of projects eligible to be funded. In 1990 the law was successfully challenged in court, resulting in curative legislation that converted the fee to an excise tax. In the late 1990s Clarksburg was added as a third impact tax district. In 2001 the Council enacted a countywide impact tax law for the first time, setting the rates in Metro Station Policy Areas at half the level as elsewhere; County Executive Duncan vetoed the bill, and the Council did not override the veto. Later in 2001 the Council enacted Mr. Duncan's version of a countywide impact tax, which had the same general structure but with lower rates and an extended (2-year) phase-in period. Finally, in 2003, the Council raised the rates substantially; setting Clarksburg's residential rates 50% higher than the general rates and its non-residential rates 20% higher; tightened credit allowances; implemented an automatic biennial inflation-based rate adjustment; and allowed future Councils to revise the rates by resolution without enacting a bill.

Task Force to Examine Future Budget Needs (1989). The Council appointed a 13-member task force (9 citizen voting members and 4 staff non-voting members), chaired by William Hussmann, to examine the projected growth in both capital and operating budget needs and to suggest means to fund them without an increase in real per-capita property taxes, which had been steeply rising.

The Task Force's recommendations were far-ranging. It proposed limiting the increase of operating budget revenue to 10% annually and allocating it in specific proportions to inflationary costs, employee compensation, increases due to population and student enrollment, and program catch-up and improvement. For the capital budget it proposed a piggy-back gasoline tax, a supplementary auto registration fee, a parking tax on non-residential spaces, and tolls on the Intercounty Connector and other limited access roadways. The report's introduction and summary of conclusions and recommendations is on ©13-23.

Parking space tax (1990). Councilmember Bruce Adams proposed an annual tax of $120 for each commercial parking space, to be paid to a new Transportation Trust Fund (in a corollary bill) for transportation infrastructure. During deliberations on the bill the proposed rate was reduced to $60/space for the first 1000 spaces in a parking facility, $30/space for additional spaces up to 2,000 spaces, $15/space for additional spaces up to 5,000 spaces, and no additional tax for spaces over 5,000 spaces. The tax would be adjusted annually for construction cost inflation. The bills were passed by the Council but vetoed by County Executive Sidney Kramer. The Council did not override the vetoes.

Commission to Review the Efficiency and Effectiveness of Government (1991). This 12-member commission (9 voting citizen members and 3 non-voting staff members) were appointed by the Council to recommend improvements to government structure, programs to be reduced or eliminated, user fees to be implemented or raised, and means for better budgeting and program evaluation. One of its recommendations was to implement an annual County vehicle registration fee, either as a flat fee ($10 per vehicle was suggested) or based on a vehicle's blue book value.

Economic Advisory Committee (1992). The EAC's 10-member Infrastructure Financing Subcommittee produced a report in February 1992 examining financing options for the transportation infrastructure. The subcommittee emphasized a "share the burden" approach that would raise money from the general population, auto users, and new development. It recommended gaining State authority for a County-levied 1% blue book tax, a Transportation Utility Tax on existing residences and businesses proportionate to the traffic demands they create, and use of tax increment financing districts. These taxes would be levied along with the already approved (but as yet unimplemented) Construction Excise Tax. The report's executive summary and recommendations are on ©24-28.

Development Approval Payment (1993-present). The Council approved an alternative review procedure proposed by Councilmember Adams as part of the FY93 Annual Growth Policy that allowed developments in certain Metro Station Policy Area, as well as small residential subdivisions (no more than 100 units per subdivision) in most other policy areas, to meet their transportation adequate public facilities requirements by paying a Development Approval Payment (DAP) at building permit issuance. The DAP rates, established in Chapter 8 of the Code, are virtually the same as the Construction Excise Tax rates adopted in 1991. DAP revenue was to be used for transportation capacity improvements in rough geographic proportion to the location of the subdivisions making the payments, except for 20% of the revenue which was diverted to the Housing Initiative Fund (HIF).

Over the years very few MSPA developments opted to use the alternative review procedure, but it was frequently used for small residential subdivisions. During the past decade about $7.3 million of DAP revenue has been collected, of which $1.5 million was directed to the HIF and $5.8 million to fund transportation projects. The 2003 Growth Policy (which took effect in July 2004) discontinued the alternative review procedure for small residential subdivisions. It continued the MSPA procedure, but keyed its approvals to a doubled impact tax. Some DAP funds continue to trickle in as subdivisions approved under the procedure before July 2004 reach the building permit stage.

Development Districts (1994-present). The Council enacted a law in 1994 that created a process to review and approve development districts. The property owners in a district are assessed an annual property tax surcharge to pay the principal and interest on County bonds, the proceeds of which pay for the major infrastructure of the district. Three development districts have been established: West Germantown, Kingsview Village Center, and Clarksburg Town Center. Bonds have been issued for the first two, but the County has not yet issued bonds for the

Clarksburg Town Center district. Two other potential development districts in Clarksburg have not yet been approved.

Most of the infrastructure funded by the development districts is transportation related, but by no means all of it. Of the $38,369,000 for development district projects funded to date in the CIP, $23,723,000 (61.8%) is for transportation projects.

Infrastructure Financing Working Group (1994). The Council appointed a 22-member working group consisting of 15 voting members (7 from civic/environmental backgrounds, 7 from business/development/financing background, and one individual) and 7 non-voting staff members to recommend "a comprehensive program to address transportation infrastructure financing needs in Montgomery County." It proposed a version of the EAC's "share the burden" approach (the so-called "3-legged stool"), which recommended: a 10 cents/gallon gasoline tax increase at the State level, or alternatively a 5 cents/gallon State gas tax increase plus a new 5 cents/gallon County tax, raising $40 million for projects in the County; a 0.5% tax on the blue book value of vehicles, raising $20 million; a Transportation Utility Tax on all homes and businesses, raising $20 million; and a modified Construction Excise Tax, raising $12 million. The report's executive summary is on ©29-33.

Expedited Development Approval Excise Tax (1998). The Council enacted an alternative review procedure, commonly known as "Pay and Go", that allowed most development to meet its transportation adequate public facility requirements by paying an Expedited Development Approval Excise Tax (EDAET). The EDAET rates were higher in moratorium areas than in other areas. This procedure has generated about $7.8 million for transportation infrastructure that adds capacity. Several months after "Pay and Go" took effect, a new Council restricted its scope to residential development, and a few months later it was repealed altogether. Like DAP, EDAET payments are still being made from subdivisions approved under "Pay and Go," but this revenue is diminishing rapidly.

Recordation Tax increment (2002). To generate more revenue for school capital projects, Councilmember Michael Subin proposed increasing the recordation tax, with the increment dedicated solely to the capital program of Montgomery County Public Schools and to Montgomery College's Information Technology project. With one exception, the recordation tax increment has proven to be the most successful capital revenue generator of any initiated by the County before or since, having raised as much as $44 million in FY06 (although the most recent estimate for FY07 will only be $32 million). The exception is the increase in General Obligation bond issuances over the past 15 years, rising from $100 million in FY92 to $275 million in FY07.

Go Montgomery! (2002). In early 2002 the Planning Board recommended, through its Transportation Policy Report (TPR), a set of transportation projects and programs to be built in the short- and medium-term. That spring County Executive Duncan proposed a 'Go Montgomery!' program that identified his transportation priorities over the same time-frame. Later that summer the Council approved the definitive '10 Year Transportation Plan,' which continues in revised form today.

The main new feature of Go Montgomery!, however, was a proposed three-part funding package: a 10-cent State-wide gasoline tax (part of which would come to the County), a $25/vehicle registration fee, and a dedicated 3 cents/$100 increase in the County property tax. The General Assembly approved legislation allowing the County to collect a vehicle registration fee, but Governor Robert Ehrlich vetoed it and the veto was not overridden. In the end, none of the 3 funding elements happened.

Public school impact tax (2003). Councilmember Tom Perez proposed this tax as a corollary to the Development Impact Tax for transportation facilities. Unlike the transportation impact tax, the school impact tax applies only to residential development, and its rates include an element of progressivity: a single-family detached home larger than 4,500 sf pays a $1 increment for each square foot above that level, with a maximum increment of $4,000.

The yield from the school impact tax has been disappointingly low since its inception in 2004. In the first year there was little revenue because developments rushed to apply for permits ahead of the March 1, 2004 effective date. Revenue has continued to lag due to the slowdown in the new home sales market, and a change in the market from predominantly single-family homes (which pay a high impact tax) to multi-family units (which pay a low tax).

Liquor Fund revenue bonds (2006). Given the long list of unfunded State transportation priorities, the Council's Transportation and Environment Committee decided in February 2006 to revisit the long-standing policy against spending significant County funds on State roads. County Executive Duncan later proposed a new $80 million CIP project to do just that. The Executive's recommendation was an important step in the direction set by the Committee but by itself did little to advance State projects, since the first funds would not have been available until FY10, and the bulk of it would not have been available until FY12.

Councilmembers Steve Silverman and Nancy Floreen proposed to supplement the Executive's proposal by another $80 million, all to be programmed in FYs 07-09. This would be done by issuing revenue bonds backed by proceeds from the Liquor Fund. The candidates for funding are those projects in the Council/Executive joint letter on State transportation project priorities. In May 2006 the Council programmed $160 million for State and WMATA transportation projects, of which about $25 million has been appropriated for 4 specific projects.

While this approach is generating significant one-time revenue for transportation infrastructure, it is not producing new County revenue. Rather, it essentially earmarks funds that otherwise would be available to cross-subsidize other portions of future Operating and Capital Budgets over the next 20 years.

3. Relationship to the Growth Policy. In law, the Growth Policy has a very narrow purpose: to determine how and when master-planned development is staged in concert with the provision of adequate public facilities. However, infrastructure financing is a closely related issue, and on occasion the Council has acted on the two together. This occurred in spring 1986 when the AGP was established and the CET and transportation impact fees were debated. This pattern recurred during the autumns of 1999, 2001, and 2003. The Council's December 12, 2006 resolution calls for these two issues to air again this summer.

The Infrastructure Financing Team is one of four Planning Board staff teams helping develop the comprehensive Growth Policy amendment due to the Council on May 21. Most of its research has focused on how the transportation and school impact taxes compare to similar taxes in other jurisdictions. In its draft Second Interim Report the team referred in passing to the Recordation Tax, development districts, and tax increment financing districts, but since its focus is on development-related issues, it has not turned its attention to other potential revenue sources.

If the proposed task force is convened and can produce suggested revenue sources by July 1, its product would be a useful complement to the Planning Board's analysis of impact taxes. In fact, rather than duplicating the Planning Board's work, this task force could be directed to examine revenue sources that are *not* primarily derived from new development. In July the Council could then weigh the respective merits of all these proposals.

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