Declining Federal Investment: Some Policy Issues

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Who Is This?

Albert Gallatin, Secretary of the Treasury, 1801-1814
1808 Report on Roads and Canals

Gallatin reported to U.S. Senate that:

- Projects should be undertaken when annualized savings in transportation costs exceed annual cost of capital
- Some projects can be undertaken without direct aid from government
- More often there are circumstances that justify government funding (scale, social benefits, etc.)
- Delays in funding and construction constitute “an injurious addition to the real expense”
Synthesizing Gallatin

- Rearranging and paraphrasing –
  - Efficient transportation systems provide important benefits to national and to regional economies, as well as to private interests.
  - It is reasonable to share the cost of these systems between government and the private sector.
  - But benefits are needlessly lost when:
    - Projects are pursued which are not economically, environmentally, or otherwise feasible.
    - Projects are delayed or pursued intermittently due to funding problems.
The Situation Today

- Declining federal investment in waterways and ports

  Symptoms:
  - Large backlog of project starts
  - Intermittent funding for projects under construction
  - Large backlog of maintenance/rehabs
  - Reduction or elimination of preventive maintenance

- Results – higher costs and lower benefits
Some Questions

- Assuming that the goal is an effective, efficient, and sustainable water transportation system:
  - Should the federal government fund projects incrementally?
  - Is a stable source of funding important?
  - Should costs be shared with the industry? Why?
  - Is the tax/trust fund method the best way to finance industry's share?
Incremental Financing

- Largely an artifact of the federal budget process
- However, this creates an opportunity for weeding out underperforming projects
  - ONLY IF: ongoing projects are prioritized according to remaining beneficial effects vs. remaining adverse effects
    - Note that effects may be economic, environmental, social, etc.
    - Beneficial and adverse effects are measured on a with-without basis
    - Not easy to do correctly, and not often done correctly
Stable Funding

- Is stable funding important?
  - For new construction and major rehabilitation, stable, predictable funding potentially reduces cost.
  - But so does the opportunity to identify and remove or reconfigure underperformers.
  - For maintenance and minor rehabilitation, stable funding is critical.
    - Without stable funding, first casualty is preventive maintenance.
    - Second casualty is premature failure.
Arguments for Cost Sharing

- It allows beneficial projects to move forward in a tight federal budget environment
  - Arguable and unknowable
- It spreads costs in a more equitable manner
  - Beneficiaries bear more cost than non-beneficiaries
- It promotes efficient investments
  - Creates pressure to reduce project costs and eliminate unnecessary features
  - But: non-federal sponsors have little incentive or legal ability to consider external effects
Equity

- Benefits received should at least equal to the funds contributed
  - Taking account of the passage of time
- There should be no large cross-subsidies
  - Between waterway systems
  - Between ports
Cost Overruns

- Cost overruns can be caused by funding delays, funding interruptions, unexpected events, etc.
- Which party should bear the risk of cost overruns?
  - Where overruns are due to government funding issues, government should bear the risk
  - This argues for a cap on local shares
Efficiency

- Projects should produce the largest possible benefits for the funds expended
- Projects should be prioritized on the basis of benefit/cost ratio
- Ongoing projects should be prioritized and funded on the basis of remaining benefit/remaining cost ratio
- Cost sharing should be uniform for all management measures
What About the IWTF and HMTF?

- **Equity**
  - **Fail**: large cross-subsidies create persistent groups of winners and losers
  - **Fail**: trust funds share in costs of government-created funding delays and interruptions

- **Efficiency**
  - **Partial success**: IW Users Board may influence project formulation and selection
  - **Fail**: trust fund revenues not uniformly applied to construction, rehabilitation, maintenance
Recommendations

- Reduce cross-subsidies
  - Harbor cost sharing should be port-specific
  - Inland waterway cost sharing should be waterway system-specific

- Cap local shares
  - Local share should be set at the time of first appropriation, and should not be subject to factors under the control of government
    - e.g., funding delays/interruptions, project delivery issues
Recommendations (cont.)

- Make cost sharing uniform across management measures
  - Construction, rehabilitation, maintenance (incl. Preventive) should be treated equally
- Correctly prioritize ongoing projects
  - Remaining benefit/remaining cost ratio