Legislative Analysis

LOCAL FEDERAL AID EXCHANGE PROGRAM

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Senate Bill 465 (S-4) as passed by the Senate
Sponsor: Sen. Jim Runestad

Senate Bill 466 (S-1) as passed by the Senate
Sponsor: Sen. Michael D. MacDonald

House Committee: Transportation
Senate Committee: Transportation and Infrastructure
Complete to 1-24-22

SUMMARY:

Senate Bills 465 and 466 would amend 1951 PA 51 ("Act 51") to establish a program under which the Michigan Department of Transportation (MDOT) would be required, under certain specific conditions, to award money to local road agencies from the State Trunkline Fund in exchange for federal-aid obligation authority allocated to local road agencies. To put it another way, MDOT would be required to replace, under specific conditions, federal aid allocated to local road agencies with State Trunkline Fund monies. For the balance of this analysis, this program will be referred to as the "local federal aid exchange program."

Senate Bill 465 would amend section 10o of Act 51 to establish the local federal aid exchange program. Specifically, the bill would require MDOT to award money from the State Trunkline Fund (STF) to local road agencies in exchange for ***federal aid obligation authority*** allocated to local road agency projects, if allowed by federal law and rules.[1]

The bill would require that MDOT make specific STF monies available for the local federal aid exchange program. The amounts for each state fiscal year (FY) are as follows:

- FY 2022-23: $25.0 million.
- FY 2023-24: $35.0 million.
- FY 2024-25 and each subsequent fiscal year: $45.0 million.

The bill would provide for the reduction of these designated amounts under certain conditions. Specifically, the designated STF set-asides would be reduced if necessary 1) to match all available federal-aid obligation authority—presumably for the state trunkline capital construction program; and 2) to provide for debt service, the ***minimum state-funded program***, routine state trunkline maintenance, administration, "and all other functions of the department."[2]

If MDOT reduced the statutory set-asides for the local federal aid exchange program, the bill would require the department to submit a letter of explanation to the chairs of the House and

[1] The bill defines ***federal aid obligation authority*** to mean "federal aid obligation authority and an equal amount of contract authority."
[2] The bill defines ***minimum state-funded program*** to mean "preservation, preventive maintenance, maintenance operations, safety, administration, and all other essential functions not eligible for federal aid, as determined by the department."

Senate standing committees on transportation, the chairs of the House and Senate appropriation subcommittees on transportation, the Senate Majority Leader, and the Speaker of the House of Representatives.

The bill includes seven subsections that further define the local federal aid exchange program. However, the sections refer to "state money" in exchange for federal aid obligation authority, rather than to STF monies specifically. It is understood that the term "state money" is intended to mean STF monies.

The bill would do all of the following:

- Authorize local road agencies to apply for state money in exchange for 100% of the federal aid obligation authority allocated by the department to a local road agency project in either a metropolitan planning organization (MPO) Transportation Improvement Program or a rural transportation improvement program.
- Require that MDOT publish announcements, instructions, forms, and deadlines on its website.
- Indicate that if local road agency application exceed the amount of state money available, awards must be made in the order received.
- Require that MDOT exchange state money, i.e., STF monies, with local road agencies at 90% of local federal aid obligation authority; i.e., 90 cents STF for each $1.00 of federal aid exchanged.
- Require that MDOT pay the state money exchanged "when sufficient federal aid obligation authority is received from the Federal Highway Administration (FHWA) to cover the exchanges, not including any year-end redistributions."
- Establish the first priority for the use of state money exchanged for federal aid obligation authority as "the local federal aid project for which the federal aid obligation authority was originally proposed." The bill would require that any surplus be applied to [other] federal aid eligible projects or returned to the department. The bill also would require that completed work be reported to the Transportation Asset Management Council investment reporting tool.
- Require that state money exchanged for federal-aid obligation authority be expended not less than three years after the exchange. If this requirement cannot be met, the bill would require the local agency to identify an alternative federal aid eligible project that could be constructed within the three-year period or return the money to the department.
- Indicate that, with respect to the local federal aid exchange program, state money is subject to current limits on local force account work as provided under 23 USC 112 and related MDOT policies governing local force account work.[3] The bill indicates that this restriction would apply only to state money awarded in exchange for federal obligation authority and "not to any money garnered through other means."
- Require that contracts between local road agencies and contractors for projects funded under the local federal aid exchange program include federal wage and benefits schedules consistent with Section IV of Form FHWA 1273, or any successor form, and provide that covered workers are third party beneficiaries of the contract requirements.

[3] Force account work generally refers to capital construction work performed by road agency forces, as opposed to work performed by private contractors under contract.

Other Changes
The bill would make an additional amendment to section 10o not directly related to the local federal aid exchange program, specifically, with respect to the current requirement that 23% to 27% of certain federal-aid highway funds appropriated to the state from the federal government be allocated for programs administered by local jurisdictions. Current law indicates that these designated local agency funds "be distributed to local agencies for transportation purposes in a manner consistent with state and federal law." The bill would amend the sentence to indicate that the designated federal funds "be distributed to local **road** agencies for transportation purposes in a manner consistent with state and federal law." The word "road" would appear to preclude use of local federal-aid funds for transit programs. It is our understanding that currently, as part of the local federal aid planning process, some local federal aid funds are "flexed" for transit programs.

In a related section, the bill would amend language that currently indicates that the average allocation percentage of local federal aid "be adjusted to reflect any voluntary agreements made by the department with local jurisdictions regarding the state buyout of federal aid." Specifically, the bill would strike the work "voluntary." Under terms of Senate Bill 465, the exchange of federal aid for state money would be voluntary with respect to participating local road agencies but would be a mandate with respect to MDOT and the use of STF monies.

MCL 247.660o

Senate Bill 466 would amend section 10 of Act 51, the section that currently defines the distribution of the Michigan Transportation Fund (MTF). Under current law, 39.1% of net MTF revenue, after various statutory deductions, is appropriated to the STF for purposes described in section 11 of Act 51, i.e., for state trunkline programs. The bill would add an additional designation of STF revenue, in addition to the section 11 designation, specifically, for the local federal aid exchange program.

MCL 247.660

The bills are tie-barred to one another, which means that neither could take effect unless both were enacted. Both bills would take effect October 1, 2022.

FISCAL IMPACT:

These bills concern the distribution of federal-aid highway funds in Michigan—between MDOT for state trunkline capital improvement programs, and local road agencies for eligible local capital construction programs.[4]

Senate Bill 465 would establish the local federal aid exchange program. Under circumstances defined in the bill, MDOT would be required to exchange STF money with local agencies for federal-aid highway funds suballocated to those agencies.

[4] The distribution of federal-aid highway funds in Michigan is described in detail in the House Fiscal Agency "Fiscal Brief: Allocation of Federal Aid to Local Road Agencies," published February 7, 2019.
https://www.house.mi.gov/hfa/PDF/Alpha/Fiscal_Brief_Allocation_of_FederalAid_to_LRA_Feb19.pdf

Senate Bill 466 would effectively earmark STF funds for the local federal aid exchange program from the MTF distribution to the STF, specifically, the bill would earmark: $25.0 million for the fiscal year ending September 30, 2023; $35.0 million for the fiscal year ending September 30, 2024; $45.0 million for the fiscal year ending September 30, 2025, and each subsequent fiscal year.

These annual earmarks of STF revenue would be used to reimburse local road agencies from state restricted funds for local federal-aid highway funds exchanged with MDOT.

The practice of exchanging federal aid for state restricted money has been sanctioned by boilerplate language included in transportation budget acts for approximately 20 years. The language in the FY 2021-22 transportation budget act, 2021 PA 87, is as follows:

> Sec. 402. A portion of the federal DOT-FHWA highway research, planning, and construction funds made available to this state shall be allocated to transportation programs administered by local jurisdictions in accordance with section 10o of 1951 PA 51, MCL 247.660o. A local road agency, with respect to a project approved for federal aid funding in a state transportation improvement program, may enter into a voluntary buyout agreement with the department or with another local road agency to exchange the federal aid with state restricted transportation funds as agreed to by the respective parties. The state restricted transportation funds received in exchange for federal aid funds shall be used for the same purpose as the federal aid funds were originally intended.

For some local road agencies, in specific circumstances, the use of 100% local or state restricted funds, rather than federal funds, could result in lower project costs and accelerated project delivery. Projects funded with 100% local or state restricted funds are generally not subject to certain regulations attached to federal aid, including Davis-Bacon prevailing wage requirements. However, Senate Bill 465 appears to address this requirement with respect to state money used in the local federal aid exchange program.

The amount of potential savings to local road agencies cannot be readily estimated. The amount of savings to a local road agency participating in the local federal aid exchange program would vary depending on the nature of the specific local project.

The cost to MDOT has not been determined at this time. The program would require some additional administrative burden for the department. It is not clear of the reimbursement percentage, 90 cents STF in exchange for $1.00 of federal aid is sufficient to offset that administrative burden.

Between 1999 and 2007, MDOT worked with interested local road agencies to establish a voluntary state-local federal aid buyout program. Under this program, MDOT entered into voluntary agreements with requesting local road agencies to "purchase" federal-aid highway funds in exchange for state restricted STF revenue at a rate of 75 cents of STF revenue for each $1.00 of local federal aid.

This state/local federal aid buyout program ended in 2008 as MDOT needed to conserve STF revenue in order to match federal aid for its own state trunkline construction program.

The department had been concerned that a mandatory exchange program could affect its ability to ensure that statewide federal transportation performance measures and targets are met, including safety, pavement condition, and bridge condition targets. The department had also been concerned that a mandatory program could affect its ability to match federal aid for the state trunkline road and bridge construction program. It is not clear if the conditions established in Senate Bill 465 satisfy those concerns.

Although MDOT no longer exchanges federal aid with local road agencies, it does facilitate voluntary transfer agreements between local road agencies. This program is described as the Local Federal Fund Exchange (LFFE).[5]

During FY 2019-20 there were 17 exchange agreements: six county road commissions were buyers of federal aid and 17 road commissions were sellers of federal aid. The purchasing local road agencies were primarily road commissions in urbanized areas, and the selling agencies were generally in nonurbanized areas. These agreements typically provide for the payment of 80 cents of state restricted funds in exchange for $1.00 of federal aid.

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[5] LFFE program guidelines are found at this link:
https://www.michigan.gov/documents/mdot/Federal_Exchange_Guidelines_2019_638688_7.pdf