



Summary of Meeting with Dan McElroy

Civic Caucus

Friday, June 2, 2006

Guest speaker: Dan McElroy, Senior Advisory on Innovation, office of Governor Tim Pawlenty

Attendance: Verne Johnson (phone), chair; Chuck Clay (phone), Paul Gilje, Jim Olson (phone), and Clarence Shallbetter

A. Introduction of McElroy— Verne welcomed McElroy to his second meeting with the Civic Caucus. McElroy has a distinguished record in several levels of government, having previously served as mayor of Burnsville, a state representative, state commissioner of finance, and chief of staff to Governor Pawlenty. Today McElroy will visit with us on two subjects, the state constitutional amendment on transportation and various innovations in the executive branch of state government.

B. Comments on the state constitutional amendment— In McElroy's opening presentation and in discussion with Civic Caucus members, the following points were made:

1. The amendment itself— The amendment will be submitted to voters in the general election in Minnesota in November 2006. The amendment provides that the revenue from the general sales tax on new and used motor vehicles will be constitutionally dedicated so that at least 40 percent will be for public transit assistance and not more than 60 percent for highway purposes. A majority of all persons voting at the election—not just a majority of those persons voting on the question—is necessary for the amendment to be adopted.

2. A need for a clear explanation and understanding of the dollar amounts— By way of introduction to the subject, Verne emphasized how critical it is that we in the Caucus, our electronic participants, and others receive a clear explanation and understanding of the dollar amounts involved. McElroy said that irrespective of the numbers he will ask Norman Foster, executive budget officer, Department of Finance, to provide accurate figures.

After the meeting Foster provided the following chart:

Minnesota State Trunk Highway Fund, February 2006 Forecast

fiscal year ending June 30, 2006

Revenues

Highway users tax distribution fund \$745,342,000 (state gasoline tax, vehicle license fees, MVST appropriation)

Federal grants 354,000,000

Investment income 2,600,000

Miscellaneous 64,448,000

Transfers 21,190,000

Total \$1,187,580,000

Expenditures

MnDOT operating expenses \$508,330,000

MnDOT state road construction 576,950,000

Department of Public Safety 73,693,000

Tort and contingent accounts 800,000

Transfer to debt service fund 36,347,000

Total \$1,196,120,000

3. MVST revenues— The motor vehicle sales tax (MVST) is estimated to yield about \$540 million in the fiscal year ending June 30, 2006. Of that amount, 46.25 percent, or \$250 million, was appropriated by the Legislature to the general fund for non-transportation purposes. The balance, \$290 million, was divided as follows: metro transit, \$116 million; greater Minnesota transit, \$7.7 million; state trunk highways, \$95 million; county highways, \$48.1 million, municipal highways, \$14.8 million, and miscellaneous, \$8.1 million. If the amendment is adopted, the entire MVST would be dedicated to transit and roads, phased in over a five-year period. By the time the phase-in is complete, MVST might total about \$600 million a year, although an official state forecast has not yet been made.

4. Highway user tax distribution fund— The constitution currently provides for a Highway User Tax Distribution Fund. All revenues from the state tax on motor fuel and from motor vehicle license fees are deposited in the fund. The constitution prescribes that 62 percent shall go for state trunk highways; 29 percent to county highways, and 9 percent, municipal highways.

For the fiscal year ending June 30, 2006, revenue deposited in the highway user tax distribution fund is estimated to total \$1.292 billion, of which \$650 million comes from the state's 20-cent gasoline tax, \$478 million from motor vehicle license fees, and \$164 million from the Legislature's MVST appropriation for state trunk highways, county highways and municipal highways.

For fiscal 2006 state trunk highways are receiving \$745.3 million; county highways, \$411.9 million, and municipal highways, \$108.2 million.

5. Other revenues available to state trunk highways— Funds available to state trunk highways also include federal matching funds, investment earnings, and some traffic fines.

6. Importance of long-term revenue guarantee — McElroy said the guarantee of funds in the constitution gives the Minnesota Department of Transportation (MnDOT) the opportunity to issue long-term bonds to pay for projects that extend over many years. As a result, MnDOT doesn't have to divide a construction project that extends over many years into many small projects. Thus, MnDOT can save considerable money. A contractor can bid for an entire project, and leave equipment on-site for the entire project, rather than bidding small segments, where equipment has to be brought on-site, only to be removed a short time later. McElroy said a project in the Rochester area would have cost \$350 million, if divided in small segments. However, with bonding and bidding as one project, the cost was trimmed to \$250 million.

With its current revenues, combined with bonding and the additional revenue from the proposed constitutional amendment, MnDOT would be able to sustain a billion-dollar construction budget through 2017. However, other considerations enter the picture of such an ambitious program. One is whether workers from outside the state would have to be hired to sustain such a level of construction. The other is how much disruption of traffic during construction the motoring public is willing to accept.

7. Need for constitutional guarantees— McElroy said transportation is different from other state functions in that its projects are so large and extend for such long periods of time that they can't be subject to the limits of two-year budgeting cycles.

8. Impact on non-transportation services— McElroy referred back to the fact that of the \$540 million a year that MVST produces now, about \$250 million is appropriated by the Legislature for non-transportation purposes. Revenue projections have been prepared by the Department of Finance for the 2007-08 biennium on the assumption that proposed constitutional amendment would be adopted. Those projections still reveal an \$800 million balance at the end of the biennium, which illustrates, he said, that the amendment can be approved without taking revenue from other services.

9. Why give special guarantees to transportation in the constitution?- McElroy said the key issue is the need for transportation to have guaranteed long-term sources of revenue to pay for its long term construction projects. Such a need is not present in other state functions.

10. Issues in constitutional dedication— Several issues emerged in discussion:

a. The urgent need for transportation funding— Verne emphasized that the Civic Caucus agrees with proponents of the amendment that additional funding is urgently needed for transportation. The Civic Caucus has issued a major report recommending additional funding, including an increase in the state gasoline tax. The Civic Caucus is considering a review of the constitutional amendment because of its broader implications for replacing appropriations and taxing by the Legislature with constitutional amendments by referendum.

b. Whether the amendment provides long term revenue assurance for highways— The amendment specifies that at least 40 percent must be for transit. However, the language provides no guarantees for highways. The amendment states that not more than 60 percent can go for highways, but there's no minimum. McElroy was asked, therefore, whether the amendment provides the kind of long term guarantee that is essential in funding multi-year highway construction projects with bonds. Theoretically the Legislature in every session could change the amount for highways. McElroy said the Legislature in 2006 was unable to reach agreement on changing the language of the amendment to assure 60 percent for highways.

In discussion after the meeting, Norman J. Foster, executive budget officer, Minnesota Department of Finance, noted the following language in the trunk highway section of the Minnesota Constitution: *All payments of principal and interest on bonds issued shall be a first charge on money coming into this fund during the year in which the principal or interest is payable.* Foster said that the bond houses would consider all sources of funding into the trunk highway fund, not just the new MVST amounts. Thus, Foster said, it is unlikely that bonding will be restricted because the Legislature retains control over how much of MVST is deposited in the trunk highway fund.

c. Whether a constitutional guarantee for transit restricts legislative authority— The strongest power in the amendment goes to transit, giving it at least 40 percent. With substantial amounts in transit devoted to operating subsidies—which include salaries for bus and rail employees and numbers of employees—the question was raised how the Legislature would have adequate influence over those decisions, if the amendment passes with the guarantee of funds for transit. Supposedly, much of the transit funds would be earmarked for capital investment, but the constitutional amendment gives no preference for capital over operating.

d. Whether the constitution should offer a "gift" of an apparently unintended— and possibly largely unknown—dividend for counties and cities—Counties and cities are guaranteed a total of 38 percent (29 percent for counties, 9 percent for cities) of all revenues in the highway user trust fund. Thus the counties and cities will receive an automatic 38 percent dividend if the constitutional amendment passes, even though no need for extraordinary funding county and city roads has been demonstrated nor any reason offered why counties and cities should receive such a constitutional benefit.

e. Whether state trunk highways will receive anywhere close to what is anticipated— Advocates for the constitutional amendment point out that transit and state highways need the funds desperately. The language of the amendment clearly benefits transit. But even if a maximum of 60 percent of the MVST dollars were granted to highways, additional dollars flowing into the state trunk highway funds would be a modest portion of the total. In the first place, state trunk highways currently receive about \$95 million annually from the MVST dollars that the Legislature has appropriated for transportation. So the additional benefit to state trunk highways must come from the remaining MVST dollars. But when cities, counties, and transit receive their shares, the amount for state trunk highways appears to be approximately an additional \$128 million a year.

f. What is included in the definition of "transit"— Light rail, buses, and commuter rail are included in the definition, but it isn't clear if high-occupancy-vehicle lanes on freeways would be legitimate uses of transit funds.

g. Why remove legislative discretion over use of tax dollars— Persons in the Civic Caucus said the effect of the transportation amendment would be to reduce the Legislature's authority in determining tax levels and appropriations. It is difficult to see, they said, why that would represent good public policy.

h. Why set a precedent for other functions?— Persons in the Civic Caucus said that the transportation amendment can be cited by advocates for other functions as a precedent that ought to be followed for their revenue needs, too. A risk exists that many functions would then have constitutionally-determined revenue protection.

11. Governor's position on other possible amendments - McElroy emphasized that under the constitution the Governor doesn't play a role in submitting amendments to the voters. The Legislature submits amendments without the Governor's signature, and the Governor has no veto power over submitting amendments. McElroy reminded the group of how the constitutional amendment on transportation got on the ballot. The amendment was part of an omnibus transportation bill submitted to the Governor in 2005. The Governor vetoed the bill, but the provision for the constitutional amendment could not be vetoed because the Governor plays no role in such provisions. Thus the amendment is on the ballot.

In terms of other amendments, it was noted that the Governor is on record to call for a special session on an amendment guaranteeing natural resources a share of the state sales tax, provided the House and Senate agree in advance. McElroy said the Governor does not favor a sales-tax-dedication amendment for arts and public broadcasting.

C. Comments on innovation in state government— McElroy distributed a report prepared in May that summarizes innovations in the executive branch of state government and collaborations among state agencies and local units of government. In his comments and in the discussion the following points were raised:

1. More dollars for direct services— McElroy said that over the last several months a special task force of six state agency leaders, supplemented by work teams involving up to 400 state employees, has put together about \$200 million worth of administrative savings that have been translated into more dollars for direct services. The effort is known as "Drive to Excellence".

These changes have not involved cutting services, so unions have supported the effort. Others who want services expanded have applauded, as well as those who want more production from state government without higher taxes.

McElroy said that he, as the Governor's representative, is coordinating the activities, not directing them nor deciding what should be done. The state agencies themselves are in charge. A web site outlines the activity in detail: <http://www.state.mn.us/portal/mn/jsp/home.do?agency=Excellence>

McElroy distributed a nine-page document outlining specific changes in many state agencies. The introduction said the effort is to transform state government

"into an enterprise-focused business organization. The multi-year effort is reducing duplication of services, modernizing business methods, streamlining processes, improving service, and reducing costs." Core participants in the Civic Caucus have received complete copies of the document.

2. A new attitude of cooperation— State employees see themselves as cooperating with the Governor's goals and with those of the state agency leaders. To illustrate this point he told a story about a custodian who had 14 notches on her broomstick, one for every commissioner she had outlasted. The custodian responded positively to a challenge that she put a notch in her broom for every commissioner she has helped.

3. Comparison with past efforts— McElroy said efforts at economizing and efficiency were undertaken under different names during the administrations of Wendell Anderson, Arne Carlson, and Jesse Ventura. A distinctive characteristic of the current undertaking, he said, is the concept of using administrative dollars that are saved for improving direct services to people, not just reducing spending. Additional legislative authority isn't needed when you're just trying to run the business better, he said. Legislators need to resist the temptation to use administrative savings for tax cuts instead of letting state agencies use the money for improving services. In fact, the administration isn't all that interested in drawing undue attention to the program for fear that some people might try to exploit the effort by cutting taxes.

4. Sources for ideas— Interestingly, state government vendors have been a good source of ideas, as well as cities and counties.

5. A prototype for other states?— Asked whether Minnesota is leading the nation in changing the culture of state government, McElroy said he believes a sustainable model has been developed that works for Minnesota but he doesn't know about other states.

D. Thanks— Verne thanked McElroy for a most stimulating meeting.

The Civic Caucus is a non-partisan, tax-exempt educational organization. Core participants include persons of varying political persuasions, reflecting years of leadership in politics and business.

A working group meets face-to-face to provide leadership. They are Verne C. Johnson, chair; Lee Canning, Charles Clay, Bill Frenzel, Paul Gilje, Jim Hetland, John Mooty, Jim Olson, Wayne Popham and John Rollwagen.