

HIGHWAY MAINTENANCE

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Accounting Rule Fixes Roads

Fasten your seatbelts—pot-holes ahead! Beginning next fiscal year, and as early as July in some places, the value of public infrastructure must be stated in the annual financial statements of state and local governments. The accounting rule—a radical change that some public officials want to ignore or downplay—will put a spotlight on the condition of our nation's infrastructure. It could revolutionize how infrastructure is financed and managed, and may encourage the allocation of more money for infrastructure preservation.

For too long, public infrastructure has been built without regard for the long-term costs of operations and maintenance. This is because funding and program responsibilities have been fragmented between capital and maintenance functions. In the 1950s and 1960s, the federal government limited the use of the Highway Trust Fund to construction. That constraint forced state and local governments to use their own revenue for maintenance, which was often deferred, resulting in the premature deterioration of our nation's highways.

IMBALANCE. Today, an imbalance remains between the funds available for capital and for maintenance, despite funding increases in the past two decades for highway rehabilitation. Last year, all levels of government spent almost twice as much on capital projects as on O&M. According to the Federal Highway Administration, state transportation agencies used 60% of highway funds for capital projects but just 18% for O&M. In contrast,

local governments spent 31% of their highway funds on capital projects, but a larger percentage—40%—on O&M.

Preserving our investment in roads and highways requires a more balanced approach to maximizing highway service performance while minimizing life-cycle costs. Asset management provides such an approach by encouraging infrastructure managers to consider trade-offs between deferred maintenance and preservation, and between short-term fixes and long-term solutions.

While the concepts of asset management have long been practiced by the private sector, public officials have been reluctant to embrace them. This is because asset management focuses on preventive maintenance and preservation and requires a long time to show the benefits of reduced replacement costs. With infrastructure absent from government financial statements, public officials have considered highways and bridges as sunk costs. By not accounting for infrastructure assets, the fiscal consequences of deferred maintenance have been ignored.

Implementation of the new accounting rules will give infrastructure fiscal visibility and may encourage public officials to support the application of asset management to infrastructure. The rules

were developed by the Governmental Accounting Standards Board, a private non-profit organization that defines "generally accepted accounting principles" for state and local governments.

In 1999, GASB approved *Statement No. 34: Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*.

GASB 34 requires governments to include long-lived infrastructure assets in their annual financial statements by as early as fiscal year 2002. The rule gives two options: Report the depreciated value of infrastructure, or use the modified approach that permits respondents to report on the costs expended to preserve infrastructure assets at prescribed condition levels.

As members of the infrastructure development community, we ought to encourage public officials to use the impetus of GASB 34 to im-

proving the funding and management of infrastructure. Unfortunately, many officials will opt for depreciation-based reporting as an easier way to achieve compliance with GASB 34. Particularly if they face term limits, these officials may balk at using the modified approach because of the long time frame needed to demonstrate the life-cycle savings of asset management. As a preemptive measure, we ought to educate them about the sizable savings

resulting from infrastructure preservation. GASB 34 also provides a basis for increasing private-sector involvement in financing infrastructure renewal. That involvement is needed because traditional sources of highway funding cannot keep pace with both growth and replacement needs. The Federal Highway Administration projects an 80% shortfall in funding needed for the nation's highway system over the next 20 years.

SAVINGS. Engineers have long known that it is cheaper to maintain highways already in good condition. Bond financing of highway rehabilitation could be supported by the savings that would result from extending the service lives of roads and bridges.

Extending the service lives of highways through preventive maintenance reduces the frequency of infrastructure replacement, and potentially reduces life-cycle costs by 75%. This return would appeal to private investors, if responsible highway agencies used a portion of the savings to pay for debt service associated with rehabilitation bonds. Besides

illuminating opportunities to finance rehabilitation, GASB 34 could alert investors to prospects for financing new infrastructure, with a better assessment of the needs and timing for replacing highways.

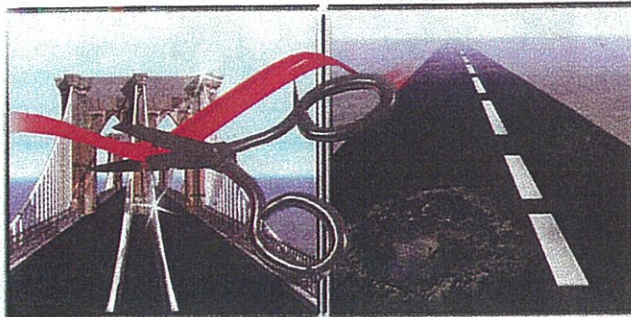
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