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S&P: Temporary State Gas Tax Suspensions Likely Will Not Affect Revenue Or General Obligation Bond Ratings

NEW YORK (S&P Global Ratings) April 12, 2022–S&P Global Ratings today said that temporary state gasoline tax suspensions, implemented recently by a few U.S. states, and under discussion by others, are unlikely to lead to rating changes on highway user tax-supported debt. To date, only three states with gas tax-supported bonds outstanding–Connecticut, Maryland, and New York–have suspended collection of their gas taxes, each for a limited time. None of the states anticipates a drop in debt service coverage compared with originally budgeted projections. However, we continue to monitor the situation and to the extent future state gas tax suspensions result in material declines in debt service coverage, we could potentially take a rating action. At the same time, we don't expect state gas tax suspensions will have a significant impact on general obligation (GO) bond ratings, which are usually paid from state general funds, and not the dedicated state transportation funds that pay highway user tax-secured debt. We also expect state general fund reimbursements to a transportation fund for lost tax revenues, if any, will be relatively small compared with overall general fund revenue, and have a limited effect on GO credit quality.

In general, gas tax revenues are only one component of pledged highway user tax revenues, and bonds secured by these revenues typically enjoy high coverage of debt service, well above their additional bonds tests (see "U.S. Highway User Tax Bonds Prove Resilient," published July 14, 2021, on RatingsDirect). The state highway funds into which pledged gas tax revenues are deposited often have a changing mix of different revenues and tax rates, designed to match state long-term capital programs for roads and bridges, and frequently adjusted by legislatures to keep up with inflation and infrastructure needs. Such other revenues might consist of state motor vehicle registration fees or sales taxes on cars.

States have an incentive to provide adequate state highway funding so that transportation fund revenues, after payment of debt service, can be used to pay for ongoing road maintenance and capital improvements. We believe a temporary tax change on one component of pledged highway user tax revenue is unlikely to have a long-term impact. To the extent that a temporary gas tax cut was made permanent, or debt service coverage was lowered to levels below an additional bonds test, further review could be warranted. A greater risk is the potential long-term threat of reduced gas consumption from electric vehicles (see "California's Order Requiring Zero-Emission Vehicles Poses Challenge To Gasoline Taxes," published Oct. 21, 2020). High retail gas prices, a justification for the temporary tax suspensions, are not likely to be significantly lowered because of the suspensions, since state tax often represents only a small portion of the overall cost of gas to the consumer.

States also have an incentive to demonstrate adequate security for bondholders so they can pursue ongoing capital programs. Details for Connecticut, Maryland, and New York State, which have highway user tax bonds outstanding, are below. A fourth state, Georgia, has also temporarily suspended its gas tax but does not have rated highway user tax debt, while Florida's legislature has passed a one-month gas tax suspension for October, which the governor has not yet signed into law.

Connecticut's most recent April 2022 monthly projection indicates that growth in state transportation fund revenues above originally budgeted fiscal 2022 levels will more than compensate for the estimated $90 million loss of pledged highway user tax revenue from suspending collection of the state's 25-cent per gallon gas tax to June 30, 2022, from April 1, 2022. Even with the approximately $90 million loss, Connecticut estimated in April 2022 that overall growth in state transportation fund revenue has raised projected transportation fund revenue to $2.07 billion from a budgeted $1.89 billion, and that motor fuels tax revenue, after the gas tax suspension, would come in at $480 million, its budgeted level. The amount of gas tax loss from the suspension approximates the extra amount of gas tax over the adopted budget that Connecticut would have collected based on recent updated revenue projections.

Maryland is suspending collection of its motor fuels tax for 30 days, to April 16, 2022, from March 18, 2022. The state motor fuels tax is 36.1 cents per gallon for gasoline and 36.85 cents per gallon for diesel fuel. Maryland estimates a loss of approximately $100 million due to the suspension, compared with fiscal 2022 total pledged highway user tax revenue of approximately $3.5 billion. In addition, a pending supplemental state budget, which has already passed the state senate, would reimburse Maryland's dedicated purpose account to offset the loss.

New York State enacted a suspension of the Metropolitan Commuter Transportation District (MCTD) sales tax, as well as the motor fuel tax imposed on gas and highway diesel from June through December 2022, which will apply to about 16 cents of the state's approximate 33-cent gas and 32-cent highway diesel tax surcharges outside the MCTD and 16.75 cents within the MCTD. New York does not issue bonds secured by gas tax revenues. However, the New York Metropolitan Transportation Authority (MTA) issues dedicated tax fund debt, which is in part supported by state-distributed motor fuel taxes. The governor's executive budget projected before the tax suspension that motor fuel tax distributed to the MTA dedicated tax fund for the full 2023 fiscal year would be $94.6 million, or only about 3% of total projected MTA dedicated tax fund revenue. The tax suspension covers only seven months, is for less than the full gas and highway diesel tax rates, and the state budget will reimburse the MTA and other local entities for the lost revenue from state general fund money. The cost to the state is estimated at $585 million, or less than 0.5% of estimated state revenues in fiscal 2023.

Other states have also floated proposals to temporarily suspend their gas tax, and we will evaluate such proposals when and if they are enacted. Not all proposals may lead to temporary gas tax suspensions–for example, a proposal to do so in Massachusetts was defeated recently in the state legislature.

This report does not constitute a rating action.

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