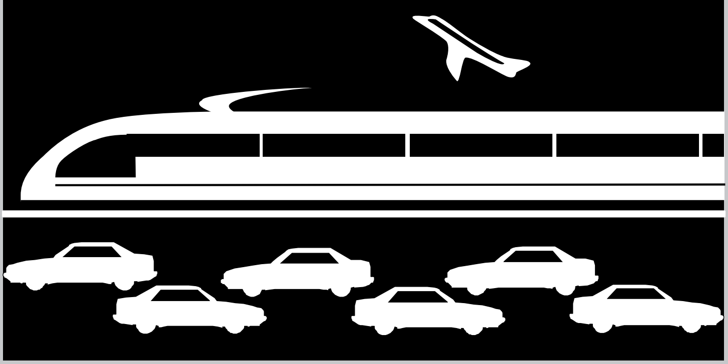
# TRANSPORTATION



LAO

65 YEARS OF SERVICE

2008-09 Analysis

# Major Issues

*Transportation*

☑

### Significant Shortfall in Funding for Highway Rehabilitation and Maintenance

- The state faces increasing costs to maintain and rehabilitate its highways as the system ages. However, the revenues which traditionally pay for these costs have grown at a much slower pace than vehicle travel, resulting in an estimated annual shortfall of over $3 billion for highway maintenance and rehabilitation. We recommend legislative actions to address this shortfall, including increasing and indexing the gasoline tax (see page A-30).

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### Proposition 1B Projects at Risk of Being Delayed

- The timely delivery of projects funded with Proposition 1B bonds depends on several factors, such as the availability of funds anticipated from other sources, adoption of program eligibility and funding allocation guidelines, and the ability of the Department of Transportation to hire the necessary state staff. We recommend measures to ensure that bond-funded projects are not delayed, including determining an ongoing process for allocating transit funds and requiring the department to present a realistic staffing plan that includes the use of contracted resources to minimize project delays (see pages A-48 through A-56).

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### Restructuring of Transit Funding Will Likely Delay Projects

- The State Transportation Improvement Program (STIP)—the state's primary program for funding transportation capital projects—is underfunded by about $1 billion from 2007-08 through 2009-10 as a result of current-year actions that changed how transit funds are allocated. While funding of STIP projects in the current year is kept on track by advancing the use of Proposition 1B bond funds, projects will likely be delayed beginning in 2008-09 (see page A-20).

☑ **Public Transportation Account (PTA) Requires Loan to Stay Solvent**

- The budget proposes no PTA money for new transit projects in 2008-09. Additionally, it assumes that up to $300 million in funding allocations made to transit projects in past years will not be paid in 2008-09. Even so, PTA will have a shortfall in the budget-year. The budget proposes a $60 million loan to PTA in order to keep the account solvent and end the budget year with a slim balance (see page A-29).

☑ **Big Hike in Vehicle Registration Fee to Fix Motor Vehicle Account**

- In order to address a projected shortfall in the Motor Vehicle Account (MVA), the Governor proposes to increase the vehicle registration fee by $11 per vehicle—bringing the total registration fee to $52 per vehicle, and to double the penalty for late registration. Absent such corrective actions, the level of MVA spending proposed by the budget would leave the account with a shortfall of over $160 million at the end of 2008-09, growing to $500 million in 2009-10, and nearly $1 billion at the end of 2010-11. If revenues and expenditures grow at historical trends, the fee hike proposal would keep MVA solvent through 2013-14 (see page A-36).

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# Overview

*Transportation*

***The Governor's budget shows a total of $13.4 billion in state-funded expenditures for transportation programs in 2008-09. This amount is somewhat lower, by $150 million, or 1.1 percent, than estimated current-year expenditures. The decrease is primarily due to lower expenditures for state and local transportation improvements funded by monies other than bond funds.***

## Expenditure Proposal and Trends

***Budget Proposal.*** The budget shows total expenditures of $13.4 billion from all state funds, including special funds and bond funds, for transportation programs and departments under the Business, Transportation and Housing Agency in 2008-09. This is a net decrease of $150 million, or 1.1 percent, below estimated expenditures in the current year. The net decrease is the result of both increases and decreases in transportation expenditures, the major components of which are:

- $540 million in additional transportation capital expenditures for primarily highway improvements by the Department of Transportation (Caltrans).
- $188 million in additional assistance to local transit systems for operations and capital improvements.
- $44 million in additional support for the California Highway Patrol (CHP) and $21 million in additional support for the Department of Motor Vehicles (DMV).
- $950 million less in state funding for local street and road improvements.

Looking just at state-funded expenditures on highways, streets and roads, the budget proposes total support that is about $400 million less in 2008-09 than the estimated current-year level. This decrease results from two changes. First, the budget proposes $540 million more in expenditures on highways and road improvements under Caltrans due to the availability of Proposition 1B bond funds. (Proposition 1B, passed in November 2006, authorizes the issuance of about $20 billion in general obligation [GO] bonds for transportation purposes.) Second, the budget proposes no Proposition 1B funds for counties and cities to improve local streets and roads in 2008-09, compared to the $950 million appropriated for these activities in the current year. Specifically, the budget assumes the current-year amount would not be fully expended for a couple of years, and thus, no additional funding would be needed in 2008-09.

For assistance to local transit systems, the budget proposes a net increase of $188 million. First, the budget proposes funding the State Transit Assistance (STA) program in 2008-09 at $743 million, in accordance with current law. This funding—from the Public Transportation Account (PTA) which derives its revenue from gasoline and diesel sales tax—would be available mainly for operational assistance. The proposed amount is about $439 million more than in the current year. Second, the budget proposes $350 million in Proposition 1B bond funds for transit capital improvements in 2008-09. This is a drop of $250 million compared to $600 million provided in the current year.

***Historical Trends.*** Figure 1 shows total state-funded transportation expenditures from 2001-02 through 2008-09. As the figure shows, over the period these expenditures are projected to more than double, increasing by $6.7 billion. This represents an average annual increase of 10 percent. Figure 1 also displays the spending for transportation programs adjusted for inflation (constant dollars). On this basis, expenditures are estimated to increase by 48 percent from 2001-02 through 2008-09, at an average annual rate of 5.8 percent.

As Figure 1 shows, state-funded transportation expenditures stayed relatively constant from 2001-02 through 2003-04. Since then, these expenditures increased steadily through 2006-07 and jumped significantly in 2007-08, increasing by 40 percent, as a result of the infusion of Proposition 1B funds. Total expenditures are proposed to drop slightly in 2008-09.

Figure 1 also shows that an increasing proportion of state-funded expenditures in the budget year will be paid from bonds. In 2008-09, bonds will account for almost 30 percent of all state-funded expenditures for transportation. At the same time, expenditures from other nonbond state sources are expected to decrease in 2008-09, by about $850 million (8.3 percent) below the current-year level.

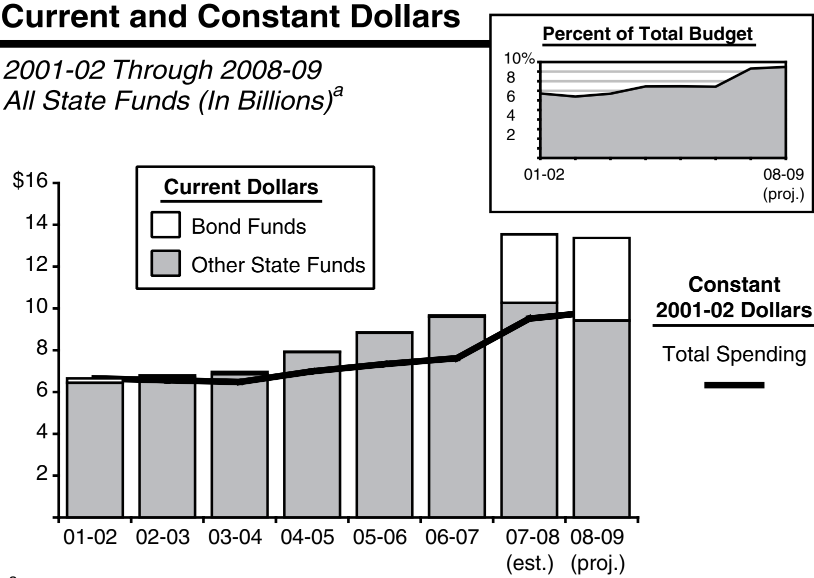
The expenditure trend shown in Figure 1 reflects a combination of changes. First, state-funded expenditures by Caltrans, mainly on state highways, have increased at an average annual rate of 12 percent since

2001-02. From 2001-02 through 2003-04, these expenditures had stayed about $3.7 billion each year. In 2007-08, these expenditures are estimated at $7.8 billion, and projected to be $8.4 billion in the budget year. As a result, spending by Caltrans has made up an increasing proportion of total state-funded transportation expenditures. Through 2003-04, Caltrans expenditures accounted for about 54 percent of state-funded expenditures on all transportation programs. The proportion has increased since then—to 62 percent in the current and budget years. This growth is mainly the result of several factors. Specifically, substantial amounts of transportation funds were loaned to the General Fund in the early 2000s through 2004-05. After that, repayments for some of the loans have allowed transportation expenditures to increase. Additionally, since 2005-06, transportation has received the full amount of gasoline sales tax revenues required under Proposition 42. The passage of Proposition 1B in 2006 has provided a further infusion of funds for transportation expenditures under Caltrans.

**Figure 1**

**Transportation Expenditures Current and Constant Dollars**

*2001-02 Through 2008-09*
*All State Funds (In Billions)[a]*




[a] Including bond funds.

Second, the same factors that have driven up Caltrans expenditures in recent years—the repayment of past loans, full funding of Proposition 42, and availability of bond funds—have also enabled the increase in state-funded expenditures for local street and road improvements as well as for transit improvements. Additionally, continued high gasoline and diesel prices in the last couple of years have generated more sales tax revenues for state funding of transit, including assistance provided through the STA program.

Third, increasing support for the CHP has also contributed to the growth in state-funded expenditures for transportation programs. Specifically, CHP's support grew by about 79 percent from 2001-02 through 2007-08 (at an average annual rate of about 10 percent), and is proposed to grow by 2.6 percent in 2008-09 over the current year. The growth is driven mainly by increases in the costs of employee (primarily uniformed staff) salaries and benefits. Additionally, the department has increased its staff, in particular traffic patrol staff, annually in the last two years. The budget proposes to continue the expansion in 2008-09, by adding 120 patrol officer positions and 44 other support positions.

Compared to the CHP and Caltrans, growth in state-funded expenditures for DMV has been modest. From 2001-02 through 2007-08, expenditures grew by 35 percent, or at an average annual rate of 5.2 percent. The growth has mainly been to implement various statutes and to modernize the department's overall information technology system. The budget proposes a 2 percent increase in 2008-09 over the current-year level, to fund essentially the same level of program activities.

As a share of total state expenditures, transportation expenditures have stayed slightly below 7 percent through 2003-04, and increased thereafter, as shown in Figure 1. In 2007-08, transportation expenditures are estimated to account for a larger proportion—about 9.3 percent—of all state-funded expenditures, and are proposed to increase to about 9.5 percent in 2008-09.

## Spending by Major Programs

Figure 2 shows spending for the major transportation programs and departments from all fund sources, including state, federal and local funds, as well as reimbursements.

***Caltrans.*** The Governor's budget proposes total expenditures of $13.9 billion in 2008-09—about $262 million, or 1.9 percent, less than estimated current-year expenditures. As Figure 2 shows, bond-funded (mainly Proposition 1B) expenditures are proposed to increase by $1.9 billion, while expenditures from other state sources will drop by about $1.4 billion. Of the total proposed expenditures, about $3.6 billion will come from bond funds, $1.5 billion from the General Fund (as required under Proposition 42) and $3.3 billion from other state funds (primarily

**Figure 2**

## Transportation Budget Summary Selected Funding Sources

*2006-07 Through 2008-09*
*(Dollars in Millions)*

| | Actual 2006-07 | Estimated 2007-08 | Proposed 2008-09 | Change From 2007-08 | |
|---|---|---|---|---|---|
| | | | | Amount | Percent |
| **Department of Transportation** | | | | | |
| General Fund | $2,629.9 | $1,438.6 | $1,485.4 | $46.8 | 3.3% |
| Other state funds | 2,869.0 | 4,700.8 | 3,298.7 | -1,402.1 | -29.8 |
| Federal funds | 3,080.7 | 4,469.3 | 3,917.8 | -551.5 | -12.3 |
| Bond funds | 52.8 | 1,674.8 | 3,570.1 | 1,895.3 | 113.2 |
| Other | 812.1 | 1,865.1 | 1,614.8 | -250.3 | -13.4 |
| **Totals** | **$9,444.5** | **$14,148.6** | **$13,886.8** | **-$261.8** | **-1.9%** |
| **California Highway Patrol** | | | | | |
| Motor Vehicle Account | $1,442.3 | $1,687.7 | $1,731.4 | $43.7 | 2.6% |
| State Highway Account | 53.7 | 59.7 | 60.3 | 0.6 | 1.0 |
| Other | 108.0 | 132.6 | 137.4 | 4.8 | 3.6 |
| **Totals** | **$1,604.0** | **$1,880.0** | **$1,929.1** | **$49.1** | **2.6%** |
| **Department of Motor Vehicles** | | | | | |
| Motor Vehicle Account | $461.8 | $501.6 | $526.5 | 24.9 | 5.0% |
| Vehicle License Fee Account | 331.4 | 363.0 | 358.7 | -4.3 | -1.2 |
| State Highway Account | 44.9 | 50.3 | 51.3 | 1.0 | 2.0 |
| Other | 19.0 | 24.7 | 21.8 | -2.9 | -11.7 |
| **Totals** | **$857.1** | **$939.6** | **$958.3** | **$18.7** | **2.0%** |
| **State Transit Assistance** | | | | | |
| Public Transportation Account | $623.7 | $304.3 | $742.9 | $438.6 | 144.1% |
| Bond funds | — | 600.0 | 350.0 | -250.0 | -41.7 |
| **Totals** | **$623.7** | **$904.3** | **$1,092.9** | **$188.6** | **20.9%** |

State Highway Account). The budget also anticipates expenditures of $3.9 billion to be funded from federal monies, and $1.6 billion to be reimbursed, mainly for work related to Bay Area toll bridges.

***CHP and DMV.*** Spending for CHP is proposed at $1.9 billion, 2.6 percent higher than the current-year estimated level. About 90 percent of all CHP expenditures would come from the Motor Vehicle Account

(MVA). The modest increase includes support to add 120 traffic officers and 44 support staff.

For DMV, the budget proposes expenditures of $958 million—$19 million (2 percent) more than the current year. About 55 percent of the expenditures would come from MVA, which derives its revenues mainly from vehicle registration and driver license fees. Another 37 percent would be funded from vehicle license fees.

***Transit Assistance.*** Current law allocates a portion of the annual PTA revenues to transit operators under the STA program, mainly for operational assistance. Due to high fuel prices, the budget projects significant revenue into PTA and correspondingly high funding of STA, at $743 million in 2008-09.

The state also provides funding assistance to transit operators for capital improvements, such as construction of rail tracks and facilities, and acquisition of equipment. Proposition 1B includes $3.6 billion in GO bond funds for transit capital improvements. The budget proposes to spend $350 million of those funds in 2008-09.

## Major Budget Changes

Figure 3 highlights the major changes proposed for 2008-09 in various transportation programs.

***Caltrans.*** The budget proposes significantly higher expenditures for capital outlay and local assistance to be funded with Proposition 1B bonds. At the same time, expenditures funded with other sources, including federal money, nonbond state funds and reimbursements are proposed to be lower by $1.7 billion.

The budget is proposing to issue $20 million in Clean Renewable Energy Bonds to convert certain Caltrans facilities to use solar energy in order to reduce utility costs. Savings will be used to pay off the zero-interest bonds over 16 years. The department is also proposing $5 million to hire parolees to pick up litter along state highways.

***CHP and DMV.*** The CHP is requesting $21.6 million to expand the number of patrol officers in 2008-09 by 120 and add 44 other staff to support these officers. This will be the third consecutive year of adding patrol staff. At the same time, the budget proposes to reduce by $40 million the department's support funding to reflect anticipated savings as a result of vacancies, mainly in patrol officer positions. The budget is also requesting $80 million to fully fund employee compensation and retirement costs.

**Figure 3**

**Transportation Programs**
**Proposed Major Changes for 2008-09**

| Department of Transportation | Requested: | $13.9 Billion | |
|---|---|---|---|
| | Decrease: | $261.8 Million | (-1.9%) |

+ $1.9 billion in expenditures from Proposition 1B bonds
+ $20 million in solar projects using Clean Renewable Energy Bonds
+ $5 million to hire parolees to pick up litter along highways

– $1.7 billion in nonbond-funded capital outlay and local assistance

| California Highway Patrol | Requested: | $1.9 Billion | |
|---|---|---|---|
| | Increase: | $49.1 Million | (+2.6%) |

+ $80 million for employee compensation and retirement
+ $21.6 million to increase patrol officers
+ $18.5 million to continue to replace radio system

– $40 million to reflect anticipated vacancies

| Department of Motor Vehicles | Requested: | $958 Million | |
|---|---|---|---|
| | Increase: | $18.7 Million | (+2.0%) |

+ $4 million to consolidate a phone center and relocate two offices
+ $0.6 million to implement new legislation

| Transit Assistance | Requested: | $1.1 Billion | |
|---|---|---|---|
| | Increase: | $188.6 Million | (+20.9%) |

+ $438.6 million for state transit assistance

– $250 million in Proposition 1B funding for transit capital

For DMV, the budget proposes $4 million to establish a consolidated telephone service center and to relocate one field office and one hearing office for the driver safety program. The budget also requests $616,000 to implement newly enacted legislation.

In addition, the budget proposes to increase vehicle registration fees by $11 per vehicle and to double penalties for late vehicle registration in order to bolster revenues to the MVA. The budget projects that the fee and penalty increases will result in additional revenue of $385 million in 2008-09 and $522 million annually thereafter.

***Transit Assistance.*** The budget proposes a significant increase of about $439 million in the STA program which provides operational assistance to transit systems. The increase is due, in part, to projected high fuel sales tax revenue (into the PTA) which funds the program. Additionally, the increase over the current-year level is also due to substantial amounts of PTA funds being used to help the General Fund in 2007-08, thereby funding STA at a lower level than otherwise would have occurred.

# CROSSCUTTING ISSUES

*Transportation*

## FUNDING FOR TRANSPORTATION PROGRAMS

***In recent years, revenues from the state gas (excise) tax and truck weight fees have not kept pace with the growing demands for highway maintenance and rehabilitation. This leaves no state funding to expand the state's highways from these revenue sources. The passage of Proposition 42 in 2002 permanently dedicated gasoline sales tax revenues to transportation uses, and provides essentially the only ongoing source of state funding to expand highways and local transit. Proposition 1B, passed in 2006, supplements this source by providing a one-time infusion of bond funds for transportation capital improvements.***

***However, actions taken as part of the 2007-08 budget package significantly changed the way the state uses some of its transit funds. In particular, a portion of gasoline sales tax revenues will be diverted from transit programs to pay for certain transportation-related activities which previously were supported by the General Fund. These changes will have not only a current-year, but also an ongoing, impact on funding for transportation programs. While the impact may be mitigated in the short run by the availability of bond funds, these changes will likely delay projects and will reduce overall transportation capital funding in the long run.***

***In the following write-up, we discuss the impact of the current-year actions on funding of the state's transportation capital program, as well as the ongoing funding constraint the state faces relative to the maintenance and rehabilitation of its highway system.***

California's state transportation programs are funded by a variety of sources, including special funds, federal funds, and general obligation

(GO) bonds. While state transportation programs have been traditionally funded on a pay-as-you-go basis from taxes and user fees, the passage of Proposition 1B in November 2006 provides almost $20 billion in bond funds to support state and local transportation programs.

## State Funding for Transportation

***Traditional State Fund Sources.*** Two special funds—the State Highway Account (SHA) and the Public Transportation Account (PTA)—have traditionally provided the majority of ongoing state revenues for transportation.

- ***The SHA.*** The SHA is funded mainly by revenues from an 18 cent per gallon excise tax on motor fuels (referred to as the gas tax) and truck weight fees. Generally, these funds have provided a predictable source of funding for transportation.
- ***The PTA.*** The PTA has been traditionally funded by sales tax on diesel fuel and a portion of the sales tax on gasoline. Some PTA revenues come from "spillover"—the amount that gasoline sales tax revenues at the 4.75 percent rate exceed the amount generated from sales tax on all other goods at the 0.25 percent rate. Most PTA revenues are fairly stable; however, spillover can vary greatly from year to year, as it corresponds with fluctuations in gasoline prices at the pump and changes in the total economy.

***More Recent State Fund Sources.*** Since 2000, state transportation programs have been supplemented by additional funding sources. In 2000, the Legislature enacted the Traffic Congestion Relief Program (TCRP), a six-year funding plan to address state and local transportation needs. The program created two new state transportation accounts—the Traffic Congestions Relief Fund (TCRF) and the Transportation Investment Fund (TIF). Both accounts have received funding from a combination of General Fund revenues (one-time) and gasoline sales taxes (ongoing) that did not previously go to transportation. In addition, Proposition 1B created a number of new transportation accounts, which are to receive revenues through the issuance of GO bonds.

- ***The TCRF.*** The TCRF was created by Chapter 91, Statutes of 2000 (AB 2928, Torlakson), to allocate $4.9 billion to 141 specific transportation projects over a six-year period from a combination of General Fund and gasoline sales tax revenues. Originally, all of the $4.9 billion was to be provided by 2005-06. However, due to the state's fiscal condition in the early 2000s, much of this funding was loaned to the General Fund. As a result, later statutes extended the annual transfer of revenues to the TCRF through

2007-08 and specified repayment of prior-year loans. The sources of repayment are to include revenues from the General Fund and bonds backed by tribal gambling revenue. By the end of the current year, the TCRF will have received about $3.8 billion. (This amount assumes the bonds are not issued in the current year to repay General Fund debt to the TCRF.) The fund will likely receive payments on prior-year loans into the next decade.

- ***The TIF.*** The TIF allocates revenues from gasoline sales taxes by formula to various transportation purposes, including local street and road improvements, the State Transportation Improvement Program (STIP), State Transit Assistance (STA), and other transit purposes. In 2002, voters passed Proposition 42, which made the transfer of gasoline sales tax revenues to the TIF permanent. The amount is estimated at $1.4 billion for the current year. These funds have been loaned to the General Fund when the state faced fiscal difficulties in previous years. However, Proposition 1A (approved by voters in 2006) restricts the state's ability to borrow these funds.
- ***Proposition 1B Bond Program.*** Proposition 1B, the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, authorizes the state to sell $20 billion in GO bonds to fund transportation projects to relieve congestion, facilitate goods movement, improve air quality, and enhance the safety and security of the state's transportation system. All funds in the Proposition 1B program are subject to appropriation by the Legislature.

## CURRENT-YEAR FUNDING ACTIONS

The 2007-08 budget provided a substantially higher level of expenditures on transportation programs relative to 2006-07 due primarily to the availability of funds authorized by Proposition 1B. As part of the budget package, actions were taken to significantly restructure the allocation of transit funding. Below, we discuss the impacts of these budget actions, as well as subsequent actions taken by the California Transportation Commission (CTC), on future funding for transportation programs.

### Major 2007-08 Budget Actions

***Fully Funded Proposition 42.*** The 2007-08 budget provided the full transfer of Proposition 42 revenues ($1.4 billion) to the TIF for transportation purposes. In addition, the budget included $83 million from spillover revenue to partially repay the outstanding amount owed from past Proposition 42 suspensions.

***Began Implementation of Proposition 1B.*** The 2007-08 budget appropriated a total of $4.2 billion in Proposition 1B funds for various transportation programs. As part of the budget package, the Legislature also adopted trailer bill legislation that further defines and directs the implementation of Proposition 1B programs. (For a detailed discussion regarding the status of each these programs, please see "Implementation of Proposition 1B" following this write-up.)

***Diverted $1.3 Billion in Transit Funds to Provide General Fund Relief for 2007-08.*** Because of the state's fiscal condition, the 2007-08 budget included a number of actions that diverted $1.3 billion in transit funds to provide one-time General Fund relief. These actions include the following.

- Use $539 million from spillover revenue to reimburse the General Fund for transportation-related debt service.
- Use $409 million from PTA to reimburse the General Fund for transportation debt service incurred in past years.
- Use $83 million to partially repay a prior Proposition 42 loan.
- Provide $129 million to fund regional center transportation.
- Provide $99 million to cover a portion of the cost of home-to-school transportation.

(As we note in a later discussion, a recent court ruling rejected a portion of the current-year diversions.)

***Significant Restructuring of Transit Funding Effective 2008-09.*** As shown in Figure 1, and discussed in greater detail below, the 2007-08 budget package also made numerous changes to the ongoing allocation of transit funding, including in particular, the allocation of spillover (gasoline sales tax) revenues. Major actions include (1) creating the Mass Transportation Fund (MTF) to provide a source of funds that can be used to reimburse the General Fund for certain transportation-related expenditures, and (2) changing the traditional 50/50 split of PTA revenues between STA and non-STA activities. The STA program provides funding assistance to transit systems. Non-STA activities include primarily intercity rail service, support of the Department of Transportation (Caltrans) mass transportation program, and transit capital improvements (funded through the STIP).

Figure 2 shows how transit funding will be allocated beginning in 2008-09 as a result of the restructuring action, compared to before the action was taken in 2007-08. Specifically, STA will no longer receive one-half of all PTA revenues, with the other one-half going to fund non-STA activities. Instead, STA would receive different shares of PTA revenues depending on the source of the revenues—whether they come from spillover, diesel

**Figure 1**

## 2007-08 Significant Restructuring of Transit Funding

✓ **Allocation of Spillover Revenues**

Chapter 173, Statutes of 2007 (SB 79, Committee on Budget and Fiscal Review)

- ***Mass Transportation Fund*** created to receive 50 percent of spillover annually beginning in 2008-09. Monies will be available to pay for transportation-related expenditures that used to be paid from the General Fund, such as debt service on general obligation bonds.
- ***State Transit Assistance*** (STA) will receive 33 percent of annual spillover (instead of one-half of all spillover under prior law).
- ***Public Transportation Account*** will receive 17 percent of annual spillover for ***non***-STA purposes (instead of one-half of all spillover under prior law).

✓ **Allocation of Proposition 42 Revenues for Transit**

Chapter 733, Statutes of 2007 (SB 717, Perata)

- ***Public Transportation Account*** share (20 percent) of Proposition 42 ***revenues*** will be split: 75 percent to STA and 25 percent to non-STA activities (instead of 50/50 previously).

**Figure 2**

## New Allocation of PTA Funds Beginning 2008-09

| Revenue Source | Prior to 2007-08 | Beginning 2008-09 |
|---|---|---|
| Spillover | 50% to STA[a]<br>50% to Non-STA[a]<br>—[b] | 33% to STA<br>17% to Non-STA<br>50% to Mass Transportation Fund (for General Fund relief) |
| Proposition 42 (20% Share) | 50% to STA<br>50% to Non-STA | 75% to STA<br>25% to Non-STA |
| Diesel Sales Tax | 50% to STA<br>50% to Non-STA | No change<br>No change |
| Proposition 111 Gas Sales Tax | 50% to STA<br>50% to Non-STA | No change<br>No change |

[a] PTA = Public Transportation Account; STA = State Transit Assistance. Non-STA includes transit capital improvements, intercity rail services, and Caltrans Mass Transportation program.

[b] Prior to 2007-08, various amounts of spillover had been diverted from year to year to help the General Fund or for other transportation purposes.

sales tax, a portion of gasoline sales tax (referred to as the Proposition 111 gasoline sales tax) , or Proposition 42 (TIF) transfers. The remaining funds would be available for non-STA purposes.

In addition to restructuring the allocation of transit funds, the Legislature also directed that on an ongoing basis, regional center transportation services will be funded from PTA instead of the General Fund.

## Impact of Current-Year Actions on Transit Funding and STIP

***The redirection of Public Transportation Account funds in the current year and on an ongoing basis reduces the amount of funding available for transit projects programmed in the State Transportation Improvement Program (STIP). Because STIP projects for the next few years were programmed before the 2007-08 budget was adopted, the total amount of projects to be funded in 2007-08 through 2009-10 exceeds the funding now expected to be available by about $1 billion. Some of these projects will likely be delayed into later years, and will not receive funding until after 2009-10.***

***Budget Actions Reduced Funding for PTA Programs.*** Because PTA is the state's primary funding source for transit, the current-year diversion of $1.3 billion and restructuring of the ongoing allocation of PTA revenues reduced the annual level of PTA money available to fund transit, including STA and non-STA purposes. Because some of the non-STA uses of transit funds (such as intercity rail services) are ongoing programs that cannot easily be scaled back, a drop in non-STA transit funds effectively results in a drop in funding for transit capital projects in STIP.

Below, we first discuss the impact of the current-year actions on transit capital funding. Specifically, we discuss (1) the magnitude of the reduction in transit capital funding, (2) how CTC responded to the drop in funding in the current year and the effect of that response, (3) what the reduction in transit capital funding means for the 2008 STIP, and (4) what alternative sources might be used to fund transit projects. We then discuss the impact on STA uses.

***STIP Funding Reduced by About $1 Billion Through 2009-10; Likely Delay Projects.*** The PTA funds that are not allocated for STA purposes are used to fund, among other things, transit capital projects in STIP. The STIP is the state's biennial program to fund capacity expansion projects on highway, rail, and transit systems. Projects are funded primarily from Proposition 42 (TIF) and PTA funds. (Proposition 1B also provided $2 billion to augment STIP funding.) The current-year budget actions reduced the amount available to fund projects already planned in the 2006 STIP, which extends from 2006-07 through 2010-11. In total, from 2007-08 through 2009-10, CTC estimates that there would be about $1 billion less in PTA funds for STIP projects planned for those years. This means that $1 billion worth of projects would need to be delayed, as they will have to await funding in later years. Alternatively, they would have to seek other sources of funding, such as local funds, or be deleted from funding altogether.

***CTC Keeps Current-Year Projects on Track by Advancing Proposition 1B Funding.*** In order to deal with the funding drop and to minimize funding disruption to STIP projects in 2007-08, CTC decided to allow projects scheduled for funding in the current year to receive a funding allocation when they become ready. In the event current-year STIP funding runs out, CTC would advance the use of Proposition 1B funds, as authorized by the 2007-08 budget package, to provide a backfill.

***CTC Action Delays Impact on Project Funding to 2008-09.*** The CTC decision will effectively delay the impact of the current-year shortfall in STIP project funding to 2008-09, thereby adding to the shortfall expected in the budget year. According to CTC staff, the commission will encourage regional transportation agencies to continue projects with local funds, where possible, in exchange for STIP funding to be provided in the future. However, not all regional transportation agencies have other sources of funds to keep projects on schedule and, therefore, some projects will be delayed beginning in 2008-09.

***Future STIP Revenues Will Fund Backlog of Projects.*** The CTC is in the process of programming the 2008 STIP, covering 2008-09 through 2012-13. The last two years of the period are expected to provide about $2 billion in new funding (including Proposition 42 TIF money and PTA revenue) that has not yet been committed to specific projects. Up to one-half of this amount will likely be used to fund the backlog of projects that cannot be funded through 2009-10.

***Transit Projects Could Be Shifted to Funds Otherwise Available for Highways…*** In recent years, the state has funded transit projects mainly with PTA. With the substantial reduction in PTA funding, however, continued funding of transit projects in STIP will likely need to come from other sources, namely Proposition 42 TIF money. Prior to the current-year budget actions, CTC had intended to use TIF dollars mostly for highway projects. Given the budget actions, CTC is allowing transit projects, in addition to highway projects, to receive allocations from TIF.

***…Or Be Shifted to Proposition 1B Funding.*** Whether transit projects will continue to be funded in STIP will be the decision of regional transportation agencies, and may depend on the availability of other funds for transit projects, such as Proposition 1B Local Transit, STA, and local funds. Proposition 1B provides $3.6 billion for local transit capital. Some of this funding could be used to continue transit projects in STIP. Caltrans is already implementing a similar approach to fund intercity rail projects—by not seeking allocations in the STIP and instead, proposing to fund some of these projects out of the $275 million set aside by Proposition 1B for intercity rail projects.

***Impact on STA.*** The STA program provides funding for assistance to transit systems. Funds for the program are mainly for operation support, such as to pay employees and purchase fuel, however, funds can also be used for capital improvements. The diversion of PTA revenues in the current year reduced funding for STA by about $290 million. Under current law, STA will receive $743 million in 2008-09, this is about $80 million less than would have been received prior to the funding changes made in the 2007-08 budget and related legislation. Beginning in 2008-09, STA will receive a greater share of Proposition 42 revenues to PTA on an ongoing basis. This is offset, however, by the reduction in the STA share of spillover revenues. Whether future funding levels for STA will be higher or lower under the new allocation formula ultimately will depend on how much spillover revenues are generated.

## Court Rejected Part of Current-Year Diversions

***A lawsuit brought against the state challenged the 2007-08 budget package's use of Public Transportation Account (PTA) revenues to provide General Fund relief. The court ruled in January 2008 that $409 million of the current-year use of PTA for past debt service was not legal.***

In the fall of 2007, the California Transit Association filed a lawsuit against the state contesting the diversion of PTA revenues to General Fund relief. In January 2008, the court ruled that the transfer of $409 million from PTA to reimburse the General Fund for debt service costs incurred in years prior to 2007-08 was illegal. The state's use of the remaining $779 million in transit funding that was contested in the lawsuit was upheld by the court.

## Expansion of the Trade Corridor Improvement Fund (TCIF) Program Would Delay SHOPP

***The California Transportation Commission plans to approve projects totaling $3 billion for the new Trade Corridor Improvement Fund program. This amount includes the $2 billion authorized for the program in Proposition 1B, as well as an additional $1 billion—including $500 million in assumed new revenue sources and $500 million redirected from delaying projects currently programmed in the State Highway Operation and Protection Program (SHOPP). We find that the proposed***

***plan would effectively give otherwise lower-priority SHOPP projects higher priority for funding.***

The CTC is responsible for administering the TCIF program, a new program established in the Proposition 1B bond act to fund projects that facilitate the movement of goods in the state. The bond act provides $2 billion for this program. In adopting the necessary guidelines for the program, CTC stated its plan to approve projects totaling $3 billion, based on the assumption that an additional $1 billion from non-Proposition 1B resources will also be available to support TCIF projects. The commission's plan is based on its finding that the state's goods movement needs far exceed the $2 billion authorized in Proposition 1B. The additional $1 billion would consist of (1) $500 million from new revenue sources (such as federal funds, user fees, and tolls) and (2) $500 million in SHA funds available for the State Highway Operation and Protection Program (SHOPP).

***Redirecting $500 Million by Delaying Existing SHOPP Projects.*** As an ongoing program, SHOPP funds capital projects to improve the state highway system, including pavement rehabilitation and safety and operation enhancements. According to CTC staff, many of the projects already identified as possible candidates for TCIF funding could also be considered SHOPP projects. However, due to limited SHA and federal funds, such projects may not have been approved for SHOPP in the past years. The commission plans to give priority to goods movement projects when approving a new SHOPP, thus enabling some TCIF projects to be funded from a mix of bond funds, SHA, and federal funds. (A new four-year 2008 SHOPP is being developed by Caltrans to be approved by CTC later this year.)

Based on our review of the commission's plan, we find that it would impact the availability of future SHOPP funding. For example, less funding would be available for other types of SHOPP projects—specifically, non-goods movement projects. Essentially, $500 million worth of projects (including support costs) currently programmed in SHOPP, which have not yet been funded, would need to be delayed in order to fund TCIF projects. Such a delay would only further constrain the limited resources projected for SHOPP in the next couple of years.

***Already Not Enough Funding for SHOPP.*** According to CTC's 2008 Fund Estimate, which projects the availability of future federal and state transportation funds, there will be about $600 million less available in 2008-09 and 2009-10 than assumed in the 2006 SHOPP. This change is primarily due to lower levels of federal and SHA funds projected to be available for SHOPP projects than initially assumed. In other words, for the next couple of years, there will not be enough funding to cover the costs of projects currently programmed in SHOPP. Thus, $600 million worth of SHOPP projects will need to be shifted to later years. This amount is in addition to the $500 million of SHOPP projects mentioned above that would have to be delayed in order to free up funds for TCIF projects, resulting in a combined total of about $1 billion worth of projects whose delivery would be pushed back. Moreover, as we discuss in more detail later in this write-up, the current SHOPP only funds a portion of the state's overall highway rehabilitation needs. Thus, CTC's plan for the TCIF program would effectively give otherwise much lower-priority SHOPP needs higher priority for funding. In addition, the plan would disproportionately impact regions in the state that do not necessarily have goods movement needs (some of the state's rural regions, for example).

# 2008-09 BUDGET PROPOSALS

## Major Transportation Proposals

The *2008-09 Governor's Budget* includes a number of proposals related to transportation funding. These proposals are summarized in Figure 3 and described below.

***Fully Fund Proposition 42 in 2008-09.*** The Governor's budget proposes to transfer $1.5 billion of gasoline sales tax revenues to TIF, the amount required under Proposition 42. Of these funds, $594 million will be used for STIP projects, $594 million will be allocated for local streets and road purposes, and $297 million will be allocated to PTA for public transit.

***Partially Repay Proposition 42 Loan.*** Due to the state's fiscal condition, the Proposition 42 transfer was suspended partially in 2003-04 and fully in 2004-05. By the end of 2007-08, there will be $670 million of outstanding Proposition 42 loans that must be repaid by the General Fund. Proposition 1A requires that the amount be repaid, with interest, no later than June 30, 2016, with the minimum annual repayment of one-tenth the amount owed. The proposed budget includes $83 million in spillover revenue (in the MTF) to repay a portion of the outstanding amount in 2008-09.

***Continue to Spend Proposition 1B Funds.*** The Governor's budget proposes $4.3 billion in Proposition 1B expenditures in 2008-09 for various transportation programs. This amount includes the first-year expenditures for two new programs—TCIF and State-Local Partnership—created under Proposition 1B. (Please see further discussion relating to these two programs in the "Implementation of Proposition 1B" and the "Department of Transportation" write-ups later in this chapter.)

***Use Tribal Gambling Revenues to Repay Debt, Instead of Bond Funds.*** Under current law, $1.2 billion in previous loans to TCRF are to

**Figure 3**

## Governor's Major 2008-09 Proposals for Transportation

- ***Fully Fund Proposition 42.*** Transfer $1.5 billion to transportation, the full amount required by Proposition 42.
- ***Partially Repay Proposition 42 Loan.*** Use $83 million in spillover revenue from MTF[a] (as discussed below) to partially repay outstanding Proposition 42 loans, as required by Proposition 1A.
- ***Spend Proposition 1B Funds.*** Proposes $4.3 billion in Proposition 1B expenditures in 2008-09 for various transportation programs.
- ***Use Tribal Compact Revenues to Repay Debt.*** Use $100 million in tribal compact revenues to partially repay transportation loans, rather than wait for bond issuance.
- ***Fully Fund Transit Assistance.*** Provides $743 million to State Transit Assistance according to current law.
- ***MTF to Provide General Fund Relief.*** Use $455 million in spillover revenues to pay transportation bond debt service and partial Proposition 42 repayment.
- ***PTA[a] to Fund Regional Center Transportation.*** Use $141 million from PTA to fund regional center transportation.
- ***PTA to Receive TCRF [a] Loan to Maintain Solvency.*** Loan $60 million from TCRF to keep PTA solvent.
- ***Defer Transfer of Gas Tax Revenues to Cities and Counties.*** Defer the monthly transfer of gas tax revenues to cities and counties for street and road maintenance, in order to provide about $500 million to meet General Fund cash needs.

a MTF = Mass Transportation Fund; PTA = Public Transportation Account; TCRF = Traffic Congestion Relief Fund.

be repaid using bonds backed by tribal gambling revenues. However, due to pending lawsuits, the bonds will not be issued in the current year, and most likely not in 2008-09. Absent the bonds, the budget proposes to use $100 million of tribal gambling revenue in 2008-09 to repay a portion of the loan. (We recommend, instead, that this revenue be deposited in the General Fund on a one-time basis in the "General Government" chapter of this *Analysis*.)

***Fully Fund STA.*** The Governor's budget proposes to fully fund transit assistance according to current law. In 2008-09, this amounts to $743 million in STA funds to be allocated for transit operations or capital projects.

***MTF to Provide $455 Million in General Fund Relief.*** As mentioned previously, MTF was created to receive one-half of the spillover revenues to fund expenditures previously paid from the General Fund beginning in 2008-09. The MTF's share of spillover is estimated to be about $455 million for the budget year. Of this amount, the budget proposes to use $354 million to pay the debt service on transportation bonds and $83 million as a partial repayment on prior Proposition 42 loans.

***Defer Transfer of Gas Tax Revenues to Cities and Counties.*** About one-third of the revenue from the state's 18 cents per gallon gas tax is allocated to cities and counties on a monthly basis to plan, construct, and maintain local streets and roads. This amount is about $1.1 billion in the current year. The State Constitution allows gas tax revenues to be loaned to the General Fund for short-term cash flow purposes if the full amount is repaid within the same fiscal year, except that the repayment may be delayed up to 30 days after adoption of a state budget for the following fiscal year. As part of the special session on the budget, the Governor is proposing legislation to defer the gas tax subventions to cities and counties for the months of April through August 2008 and make these payments in September 2008 instead, in order to facilitate short-term cash flow for the General Fund. The administration estimates that this would result in a total deferral of about $500 million.

## Aggregate Expenditures for Major Transportation Programs to Decrease

As shown in Figure 4, the Governor's proposals would, in aggregate, reduce expenditures for major transportation programs in 2008-09 relative to estimated expenditures in the current year. (These amounts include estimated expenditures for capital outlay support or pre-construction activities.) The reduction in spending is primarily due to lower levels of budget-year expenditures for STIP, SHOPP and TCRP. For example, the budget includes a roughly $500 million reduction in total STIP expenditures (including Proposition 1B funds) from 2007-08 to 2008-09. This is because (1) the current-year level for STIP includes the expenditure of one-time funds related to a loan repayment and (2) the budget-year level reflects a reduction in PTA revenues, as discussed earlier in this write-up. As indicated in the figure, the proposed budget includes an increase in Proposition 1B expenditures.

## Spending Will Focus on Proposition 1B Programs

***Under the Governor's proposed budget, a large portion of transportation expenditures will be on Proposition 1B programs. Although these programs may meet the state's transportation needs in the short term, they do not address the needs on a long-term, ongoing basis.***

**Figure 4**

## Expenditures for Major Transportation Programs

*(In Millions)*

| Programs | Estimated 2007-08 | Proposed 2008-09 | Change |
|---|---|---|---|
| STIP | $2,248 | $1,208 | -$1,040 |
| SHOPP | 3,337 | 2,915 | -422 |
| TCRP | 341 | 118 | -223 |
| Proposition 1B (Total) | 3,794 | 4,295 | 501 |
| Corridor Mobility Improvement | (471) | (1,342) | (871) |
| STIP | (576) | (1,095) | (519) |
| SHOPP | (223) | (147) | (-77) |
| Trade Corridor Improvement | (0) | (384) | (384) |
| State-Local Partnership | (0) | (153) | (153) |
| Traffic Light Synchronization | (92) | (122) | (30) |
| Highway 99 Improvement | (13) | (86) | (73) |
| Local Transit | (600) | (350) | (-250) |
| Intercity Rail | (158) | (104) | (-54) |
| Local Streets and Roads | (971) | (0) | (-971) |
| Air Quality | (250) | (250) | (0) |
| Other | (440) | (262) | (-178) |
| Local Streets and Roads | 1,155 | 1,178 | 23 |
| STA | 304 | 743 | 439 |
| High-Speed Rail | 21 | 5 | -16 |
| **Totals** | **$11,200** | **$10,462** | **-$738** |

STIP = State Transportation Improvement Program; SHOPP = State Highway Operation and Protection Program; TCRP = Traffic Congestion Relief Program; STA = State Transit Assistance.

For 2008-09, most transportation spending will be on programs authorized in Proposition 1B. As shown in Figure 4, about 40 percent (or $4.3 billion) of the proposed transportation program expenditures in the budget year will be on Proposition 1B programs. Thus, a large portion of the state's capital improvement needs in transportation will be met in the budget year through one-time bond programs rather than through ongoing programs, which is in contrast to past practices. While the bond funds can meet the state's transportation needs in the shortterm, they do not address these needs on a long-term, ongoing basis. Moreover, as we discuss in a later section of this write-up, the state's highway rehabilitation and maintenance needs are growing faster than the revenues which have traditionally paid for them.

## Delays in TCRP Funding Will Delay Some Projects

***Due to the state's fiscal condition in 2001-02 through 2004-05, a significant portion of the funding for the Traffic Congestion Relief Program was delayed or loaned to the General Fund. Repayment of the outstanding loans is likely to trickle in over the next nine years. This lengthy repayment schedule will delay projects that are ready to be funded. This is particularly true for large projects that require funding levels in excess of amounts available in any one year.***

***TCRP Funding Delayed, Loaned to General Fund.*** As mentioned previously, due to the state's fiscal condition in 2001-02 through 2004-05, a significant portion of the funding for the TCRP was delayed and loaned to the General Fund. Current law extends funding for the TCRP through 2007-08 and establishes repayment of past loans. Through 2007-08 the TCRP will have received $3.8 billion.

***Loan Repayments Will Trickle in Slowly.*** Outstanding loans to the TCRP currently total about $1.1 billion. This amount will be repaid in two ways, as shown in Figure 5. First, about $664 million will be repaid from the General Fund, under conditions set up in Proposition 1A. Proposition 1A requires that this amount be repaid by June 30, 2016, at a minimum annual rate of one-tenth the amount owed. The Governor's budget proposes to repay $83 million in 2008-09 from MTF.

Second, about $482 million is to be repaid from bonds backed by tribal gambling revenues. The Governor's budget proposes that until bonds can be issued, TCRP would be repaid using annual tribal gambling revenues. However, as Figure 5 shows, TCRP will not receive any tribal revenues in 2008-09. This is because current law requires that the $100 million in anticipated revenues must be used first to repay an SHA loan made to the program in prior years.

Given the loan repayment time lines, and assuming no issuance of tribal bonds, funding for TCRP would stretch over the next nine years, and trickle in through 2016-17.

***CTC to Allocate Projects Based on Annual Repayments.*** In view of the current funding time line for TCRP, CTC has decided to make funding allocations to projects based on the annual level of loan repayments to the program. Consequently, for 2008-09, CTC plans to allocate up to $83 million for TCRP projects. As a result, some projects that are ready to be funded in the budget year will be delayed. This is particularly true for large projects that require funding at a level in excess of the amount of tribal revenues anticipated in any one year.

**Figure 5**

**Estimated Loan Repayment to Traffic Congestion Relief Program 2008-09 and Future Years**

*(In Millions)*

| | Loan Repayment | | |
|---|---|---|---|
| Fiscal Year | Proposition 1A[a] | Tribal Revenues[b] | Total |
| 2008-09 | $83 | — | $83 |
| 2009-10 | 83 | $86 | 169 |
| 2010-11 | 83 | 100 | 183 |
| 2011-12 | 83 | 100 | 183 |
| 2012-13 | 83 | 4 | 87 |
| 2013-14 | 83 | — | 83 |
| 2014-15 | 83 | 21 | 104 |
| 2015-16 | 83 | 100 | 183 |
| 2016-17 | — | 71 | 71 |
| **Totals** | **$664** | **$482** | **$1,146** |

[a] Although Proposition 1A requires the state to repay the Traffic Congestion Relief Fund (TCRF) at the rate of one-tenth the amount owed each year, this figure assumes a rate of one-ninth as proposed by the Governor. Actual repayment level may vary in some years.

[b] Assumes bonds are not issued, and instead the state uses ongoing tribal gambling revenues to repay the TCRF in the amounts and order provided in Chapter 56, Statutes of 2006 (SB 1132, Committee on Budget and Fiscal Review). Chapter 56 specifies the repayment of loans to TCRF from the State Highway Account and the Public Transportation Account (PTA) in prior years. For example, it requires that $96 million of the $100 million in anticipated compact revenues in 2012-13 be used first to repay a PTA loan.

## PTA Requires Loan to Stay Solvent

***The budget proposes a $60 million loan from the Traffic Congestion Relief Fund to the Public Tranportation Account (PTA) to keep the account solvent in the budget year. If actual revenues to PTA in 2008-09 are less than estimated, the account could require additional loans to stay solvent.***

The diversion of PTA funds to help the General Fund in the current year is made possible in part by drawing down cash reserves in the account and delaying the payment of funding allocations made to transit capital projects in previous years. These actions combined will leave the account with a slim balance of about $26 million at the end of 2007-08.

For 2008-09, the budget assumes two actions in order to limit expenditures from the account. First, the budget expects that some past allocations made to projects (as much as $300 million) will continue to go unpaid until after 2008-09. The budget makes this assumption because projects typically take more than one year to complete, and cash outlays to pay for the cost of a project often stretch over multiple years. Second, the budget is proposing no PTA funding for transit projects programmed in STIP for 2008-09 (as discussed earlier). Even so, PTA still will not have sufficient resources to pay all projected expenditures. Budget-year expenditures include mainly STA ($743 million), intercity rail services ($106 million), and regional center transportation ($141 million). To keep PTA solvent the budget proposes a $60 million loan from the TCRF, to be repaid in 2011-12. With the loan, the account will end 2008-09 with a slim balance of $29 million. If actual revenues to PTA for 2008-09 are lower than estimated, this balance could disappear, and PTA may require additional loans to stay solvent.

***TCRF Loan Will Not Affect TCRP Progress.*** The TCRF loan to the PTA proposed by the budget, however, is not likely to impact the allocation of funds to TCRP projects. This is because funds allocated to projects are not expended immediately. Instead, funds are typically drawn down over several years, and cash for the cost of the entire project would not be needed in the budget year. The scheduled repayment of these TCRF funds in 2011-12 should mitigate any impact on projects.

## Maintenance and Rehabilitation Funding Continue to Shrink

***The costs to maintain and rehabilitate the state highway system have grown considerably in recent years. At the same time, however, the revenues which traditionally pay for these costs have grown at a much slower pace, resulting in an underfunding of highway maintenance and rehabilitation needs. In order to address this long-term imbalance between needs and resources, we recommend actions to ensure that sufficient revenues are available in future years to meet the projected costs.***

While travel on the state's highway network continues to increase, many of California's highways have surpassed their design life. As a result, maintenance and rehabilitation costs have grown considerably in recent years. (Please see the text box on page 32 for a distinction between maintenance and rehabilitation activities.) However, the Governor's budget does not include any proposals to increase expenditures on either preventive maintenance (for roadways, structures, and drainage systems) or highway rehabilitation projects. In fact, the proposed budget shows total expenditures (including Proposition 1B) on SHOPP projects to be almost $500 million less in 2008-09 than the estimated current-year expenditure level of about $3.6 billion (see Figure 4). In view of the above, the proposed budget does not address the long-term mismatch between maintenance and rehabilitation needs and the revenues to pay for them.

## Maintenance and Rehabilitation Costs Continue to Increase

The growing maintenance and rehabilitation demands resulting from the state's aging highway system consume increasing portions of SHA revenues (primarily gas tax and weight fees), which traditionally have been the state's primary source to fund capacity expansion on highways. As outlined in both the 2007 Five-Year Maintenance Plan and the 2007 Ten-Year SHOPP Plan, this trend is projected to continue.

***2007 Five-Year Maintenance Plan.*** Chapter 212, Statutes of 2004 (SB 1098, Committee on Budget and Fiscal Review), requires that Caltrans adopt biennially a five-year maintenance plan. This plan is to assess preventive maintenance needs on the highway system and recommend investments that would cost-effectively address these needs. The 2007 Five-Year Maintenance Plan recommends that the state increase its annual investment in preventive maintenance of pavement, structures (such as bridges and overpasses), and drainage (such as culverts) by $147 million in order to reduce the maintenance backlog. (In order to eliminate the identified backlog over a five-year period, the report estimated that maintenance funding would need to increase by $589 million each year.)

Of the recommended annual amount of $147 million, $85 million is for pavement maintenance contracts to eliminate the backlog of over 7,000 lane-miles in need of preventive maintenance over ten years. Additionally, $41 million is to reduce by one-half the number of structures in need of major maintenance—the plan estimates that about 20 percent of the state's 12,500 bridges are in need of major maintenance. Lastly, the plan recommends an additional $21 million to maintain 355 culverts annually, which would reduce, but not eliminate, growth in the drainage maintenance backlog. While the enacted 2007-08 budget included the additional $85 million identified in the maintenance plan for pavement preservation, the budget did not fund the plan's recommendation to increase the investment in structures and drainage maintenance by $62 million annually. For 2008-09, the Governor's budget essentially proposes the same level of spending on preventive maintenance as in the current year.

***2007 Ten-Year SHOPP Plan.*** State law requires Caltrans to prepare biennially a ten-year SHOPP plan. This plan is to assess rehabilitation needs on the highway system and recommend investments that would cost-effectively address these needs. Caltrans develops this plan by periodically inspecting the state highway system to identify areas in need of rehabilitation, safety, or operational improvements. In its 2007 Ten-Year

SHOPP Plan, the department identified a total of $55 billion in project development and capital needs over the ten-year period from 2008-09 through 2017-18, which amount to $5.5 billion on an annual basis. However, the 2008 Fund Estimate (adopted by CTC) sets aside only about $2.1 billion for each of the next several years to support SHOPP projects, a gap of over $3 billion annually. Annual revenues from the existing gas tax and weight fees will not be sufficient to address the state's identified rehabilitation needs over the period.

### Existing Gas Tax Inadequate to Cover Projected Costs

In general, state gas tax revenues have not increased enough in recent years to keep pace with escalating maintenance and rehabilitation costs because:

- ***The Gas Tax Has Not Increased in Over a Decade.*** The current state gas tax of 18 cents per gallon has been in place since 1994. Since then, inflation has eroded the value of per gallon tax revenues

### Maintaining and Rehabilitating The State's Highway System

In order to maintain and improve the quality of the state's aging highway system, highway maintenance and rehabilitation must be performed as needed.

***Maintenance.*** The maintenance division at the Department of Transportation is responsible for the upkeep of all aspects of the state highway system. The major functions are:

- Pavement maintenance.
- Roadside and drainage maintenance.
- Structures maintenance (including bridges).
- Traffic guidance and electrical maintenance.
- Support and training.
- Snow and storm response.
- Radio communications.

Adequate and periodic maintenance can significantly reduce future costs for roadway rehabilitation. The main funding source for maintenance is the State Highway Account (SHA), which consists of revenues from the state gas tax and truck weight fees.

*(continued on next page)*

by 28 percent, so that 18 cents is worth 13 cents today (in constant dollar terms) based on the California Consumer Price Index (CPI). A more targeted measure of inflation tied to the costs of highway construction projects could also be used to assess the current value of the state gas tax. For example, based on the Producer Price Index for Highway and Street Construction, the 18 cent gas tax is worth 11 cents today.

- ***Eroding Revenues.*** As shown in Figure 6 (see next page), between 1991 and 2007, travel on California roads increased by 28 percent (see dashed line). Meanwhile, gas tax revenues (adjusted for inflation) have not increased (see light-solid line). As a result, revenue generated per vehicle-mile traveled declined by more than 20 percent over the period (dark-solid line). Given the significant increases in highway construction costs over the last several years, the Producer Price Index for Highway and Street Construction discussed above would likely show an even greater decline in gas tax revenues relative to vehicle-miles traveled.

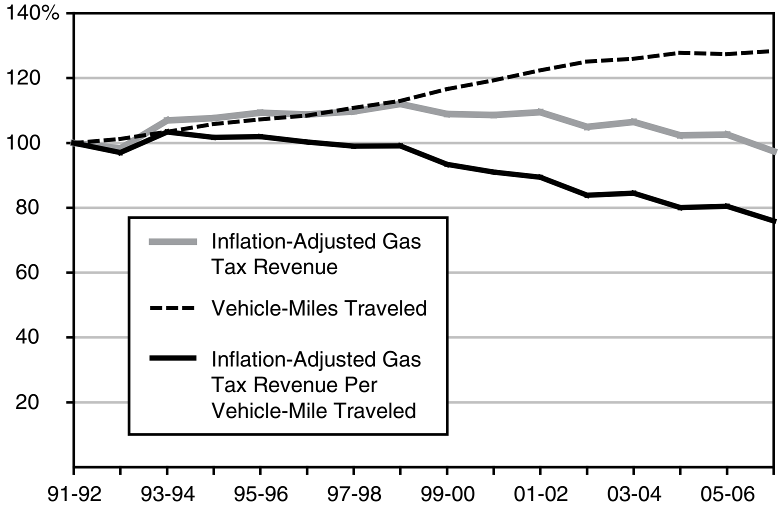
***Rehabilitation.*** While the maintenance program is supposed to do preventive work and correct small problems before they grow, the State Highway Operations and Protection Program (SHOPP) corrects highway system issues mainly through rehabilitation or reconstruction. The SHOPP primarily funds:

- Pavement rehabilitation and projects that improve roadway safety.
- Roadside preservation (including rest areas and freeway plantings).
- Operational improvements (such as ramp metering).
- Upkeep of facilities (including office buildings and equipment shops).
- Construction of railroad grade crossings.
- Hazardous waste mitigation.

Funding for SHOPP comes from SHA and federal funds. Proposition 1B authorized a onetime infusion of $750 million for the SHOPP.

**Figure 6**

**Real Gas Tax Revenues Have Not Kept Pace With Road Use**




## Funding Highway Maintenance and Rehabilitation Over the Long Haul

In deciding how to adequately fund highway maintenance and rehabilitation needs, we propose several actions to ensure long-term funding. Specifically we recommend the Legislature (1) raise the state gas tax and index it for inflation, (2) consider taxing alternative fuels, and (3) explore mileage-based fees and additional toll roads.

***Raise State Gas Tax and Index for Inflation.*** In order to address the shortfall between gas tax revenues and the state's highway maintenance and rehabilitation costs, we recommend the Legislature raise the gas tax to a level that would adequately fund these costs. We estimate that the current rate of 18 cents per gallon would need to be increased by at least 10 cents per gallon. We further recommend that the state gas tax be indexed for inflation to prevent further erosion of revenue over time. At the federal level, the National Surface Transportation Policy and Revenue Study Commission (appointed by Congress in 2005, as part of the federal transportation act [SAFETEA-LU]) recently issued a report in which it recommended increasing the current federal gas tax of 18.4 cents per gallon by at least 25 cents over the next five years, and indexing it for inflation using either a broad measure (such as CPI) or a more targeted measure (such as the Producer Price Index for Highway and Street Construction). The basis for this recommendation is to provide additional funds to states for highway improvement projects (including rehabilitation), which would effectively reduce the level of increase needed in the state's gas tax.

***Consider Taxing Alternative Fuels.*** Currently, many alternative fuels (such as ethanol and natural gas) are taxed at a lower rate than gasoline and diesel fuel. Thus, if alternative fuels become a more prevalent energy source for transportation, the Legislature should consider taxing these fuels at a comparable rate to conventional motor fuels to ensure that revenues for uses like highway maintenance and rehabilitation do not decline. This is because a greater usage of energy-efficient vehicles would not necessarily reduce the number of vehicle miles driven on the state's highways.

***Explore Mileage-Based Fees and Additional Toll Roads.*** Mileage-based fees offer an advantage over gas taxes in that these revenues are not eroded by increasing fuel economy or use of alternative fuels. Rather, the fees would closely match the extent to which motorists use highways and roads. There are privacy and technical obstacles to overcome in implementing a mileage-based approach to fund transportation. However, the state of Oregon recently undertook a pilot program to implement mileage-based fees. A recent report on the Oregon pilot program generally found that a mileage-based fee concept can be feasible as an alternative revenue collection system for replacing the state's gas tax. We recommend that the Legislature examine the policy and implementation issues that must be addressed if mileage-based fees were to be implemented in California. In addition, as an interim step towards possible greater reliance on toll revenue, the Legislature could authorize additional toll projects on a pilot basis and direct an evaluation of toll roads, including their effect on low-income drivers.

# MOTOR VEHICLE ACCOUNT CONDITION

The Motor Vehicle Account (MVA) derives most of its revenues from vehicle registration and driver license fees. In 2007-08, those fees account for 90 percent of the estimated $2.1 billion in MVA revenues. The majority of MVA expenditures support the activities of the California Highway Patrol (CHP) (69 percent), the Department of Motor Vehicles (DMV) (22 percent), and the Air Resources Board (7 percent).

## MVA Faces Deficit in Budget Year Without Corrective Actions

***The Governor's budget proposes to increase vehicle registration fees and penalties to address a projected deficit in the Motor Vehicle Account beginning in the budget year. Although our analysis finds that the administration's revenue projections are overstated, the proposal likely would provide sufficient revenue to keep the account solvent for several years.***

***Historical Spending Outpaces Revenues.*** Historically, spending for programs supported by the MVA has routinely outpaced revenues. This is largely the result of growth in the CHP, which accounts for nearly 70 percent of MVA expenditures. While revenues on average have grown about 5 percent annually, CHP's budget has grown at a rate of about 9 percent annually. In recent years, CHP's growth has been driven by a variety of factors, including negotiated salary increases, major equipment upgrades, and increased antiterrorism responsibilities following the attacks of September 2001. In our *Analysis of the 2007-08 Budget Bill*, we noted that the MVA would likely face significant shortfalls beginning in 2009-10 and possibly sooner depending on a number of factors.

***MVA Revenues Come Mainly From Vehicle Registration Fees.*** The MVA derives most of its revenues from vehicle registration fees. Of the estimated $2.1 billion in MVA revenues in 2007-08, approximately $1.7 billion (or 81 percent) is from vehicle registration fees. Vehicle registration fees consist of (1) a base vehicle registration fee of $31 per vehicle, (2) a CHP fee of $10 per vehicle, and (3) late payment penalties that vary from $10 to $100 depending on the lateness of the payment. Other sources of MVA revenue include driver license and identification card fees (12 percent), and a variety of other miscellaneous fees for special permits and certificates (7 percent).

It is important to note that there are other fees collected by DMV as part of the vehicle registration process, including the vehicle license fee. However, these fees are not deposited into the MVA.

***Proposed 2008-09 Expenditures Would Result in MVA Shortfall.*** The Governor's budget proposes total MVA expenditures of $2.4 billion, about $2.6 million more than the current year. At this proposed level of expenditure, the MVA would face a shortfall of over $160 million by the end of 2008-09 absent corrective actions. This shortfall would grow to $500 million in 2009-10, and reach nearly $1 billion by the end of 2010-11.

***Governor Proposes to Increase Vehicle Registration Fee and Penalty.*** To address the MVA shortfall, the Governor's budget proposes to increase vehicle registration fees and penalties. Specifically, the governor proposes to increase the CHP fee by $11—from $10 to $21—per vehicle, as well as add a new penalty for late payment of the CHP fee. This new penalty would be on top of other penalties currently imposed, essentially doubling the total penalty for late registration.

***Revenues Overstated.*** The budget assumes the fee/penalty increase proposal would generate $385 million in 2008-09, and about $522 million annually thereafter. The proposal requires enactment of urgency legislation, as the fee and penalty hikes are proposed to take effect in October 2008.

In reviewing the proposal, we identified a technical error in the administration's calculation of revenues. After correcting for the technical error, we estimate the Governor's proposal would increase MVA revenues by $353 million in 2008-09, and $491 million in 2009-10, about $32 million less each year than is currently reflected in the Governor's budget.

Based on current law and historical trends, even at this level of revenues, we think the Governor's proposal would generate sufficient funds to support MVA programs for several years. Specifically, our forecast of revenues and expenditures under the Governor's proposal suggests that the proposed increases would sustain the MVA through 2013-14. This assumes that spending continues at an average annual rate of about 7 percent.

***Potential Risks to the Revenue Projection.*** We would note that there are some risks to the projections: (1) it is particularly sensitive to timely passage of the fee increase proposal, and (2) it assumes little change in the behavior of individuals who register their vehicles late.

- ***Maximum Revenues Reliant on Timely Adoption of Proposal.*** Current law requires the department to send out vehicle registration notices 60 days prior to the due date for vehicle registration. In order for the department to begin collecting the higher fees effective October 2008, it must modify the vehicle registration notification statements and promptly send those out beginning in August 2008. Each month of delay could result in the loss of as much as $29 million.

- ***Estimate Assumes Registrant Behavior Unaffected by Increases.*** Despite the proposed doubling of the late penalty, the administration's revenue projection assumes that individuals will continue to pay late at about the same rate. This may be reasonable given that the last penalty increase (in 2003) failed to induce more registrants to pay on time. In fact, late payments have been increasing. However, given the magnitude of the overall proposed increase (both fees and penalties), we think it is possible that a significant number of vehicle registrants could pay more timely, thus, reducing the overall level of penalty revenues generated by the proposal.

In addition, there are a number of remaining funding pressures, and potential risks, in the programs for CHP and DMV that could bring about higher MVA expenditures and cause the MVA to draw down the reserve faster. These include:

- ***Federal Real ID Act.*** Perhaps the greatest potential new pressure on the MVA is the cost associated with the implementation of the federal Real ID Act. That law requires California to implement new standards for the production and issuance of state driver's license and identification cards. In 2006, the DMV estimated this could cost $500 million over the next six years to implement in California. Based on our review of the final Real ID regulations issued in January 2008, we would expect costs to be lower. However, the department has not released a revised estimate of costs. (For more information on Real ID, please see our discussion later in this chapter under the "Department of Motor Vehicles", Item 2740.)

- ***Major Multiyear Projects.*** As an example of another potential risk, in 2006-07 the Legislature approved a request to replace CHPs radios at an estimated cost to the MVA of about $500 million over five years. Similarly, a multiyear project was approved allowing the DMV to upgrade its information technology infrastructure. This project was estimated to cost $240 million. While our estimates assume these projects are implemented as planned, large projects often take longer and cost more to complete than originally estimated.

Overall, although the budget overstates revenues from the Governor's proposal by $32 million annually, we conclude that the proposed increase in fees and penalties would sustain the MVA through 2013-14, assuming historical rates of growth in revenues and expenditures from year to year. However, a number of risks and pressures could cause expenditures to increase and draw down the reserve at a faster rate. We will continue to monitor the fund and offer recommendations as appropriate.

# IMPLEMENTATION OF PROPOSITION 1B

***Proposition 1B, approved by voters in November 2006, allows the state to sell $20 billion in general obligation bonds to fund transportation projects to relieve congestion, facilitate goods movement, improve air quality, and enhance the safety and security of the state's transportation system. In this write-up, we (1) review the implementation of Proposition 1B, (2) identify issues that could delay the delivery of projects, and (3) recommend steps that can be taken to ensure that projects are delivered in a timely manner.***

Since 2005-06, California has spent about $20 billion annually in state, federal, and local funds to maintain, operate, and improve its multimodel transportation network. Although these expenditures have been traditionally funded on a pay-as-you-go basis from taxes and user fees, voters have approved state bonds on a limited basis to fund transportation. In November 2006, voters approved Proposition 1B (Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006), which provides $20 billion in general obligation (GO) bonds for transportation projects. These bonds provide a major one-time infusion of state funds into the transportation system to be spent over multiple years.

## MAJOR PROVISIONS OF PROPOSITION 1B

Figure 1 details the purposes for which the Proposition 1B bond money can be used. As shown in the figure, the $20 billion in bond funds are designated to relieve congestion, facilitate the movement of goods, improve air quality and enhance the safety and security of the transportation system.

The major provisions of Proposition 1B are as follows:

- ***Creates Several New Programs.*** While some of the Proposition 1B funding is directed to existing state and local transportation programs (such as the State Transportation Improvement Program [STIP] and the State Highway Operation and Protection

**Figure 1**

## Uses of Proposition 1B Funds

*(In Millions)*

| Program | Purpose | Amount |
|---|---|---|
| **Congestion Reduction, Highway and Local Road Improvements** | | **$11,250** |
| Corridor Mobility Improvement | Reduce congestion on state highways and major access routes. | $4,500 |
| STIP[a] | Increase capacity on highways, roads, and transit. | 2,000 |
| Local Streets and Roads | Enhance capacity, safety, and operations. | 2,000 |
| Highway 99 Improvement | Enhance capacity, safety, and operations. | 1,000 |
| State-Local Partnership | Match locally funded transportation projects. | 1,000 |
| SHOPP[b] | Rehabilitate and improve operation of highways. | 500 |
| Traffic Light Synchronization | Improve safety and operation of local streets and roads. | 250 |
| **Transit** | | **$4,000** |
| Local Transit | Purchase vehicles and right of way, and make capital improvements. | $3,600 |
| Intercity Rail | Purchase vehicles for state system and make capital improvements. | 400 |
| **Goods Movement and Air Quality** | | **$3,200** |
| Trade Corridor Improvement | Improve movement of goods on highways and rail, and in ports. | $2,000 |
| Air Quality | Reduce emissions from goods movement activities. | 1,000 |
| School Bus Retrofit | Retrofit and replace polluting vehicles. | 200 |
| **Safety and Security** | | **$1,475** |
| Transit Security | Improve security and facilitate disaster response. | $1,000 |
| Grade Separation | Improve railroad crossing safety. | 250 |
| Local Bridge Seismic | Seismically retrofit local bridges and overpasses. | 125 |
| Port Security | Improve security in publicly owned ports, harbors, and ferry facilities. | 100 |
| **Total** | | **$19,925** |

a State Transportation Improvement Program.

b State Highway Operation and Protection Program.

Program [SHOPP]), almost three-fourths of the bond revenues will be used to create new programs. Some of these new programs will address goods movement and security issues that have not historically been a focus of transportation funding.

- ***Involves Many Implementing Agencies.*** The monies for the myriad of Proposition 1B programs, in turn, are to be administered by a variety of state agencies. The California Transportation Commission (CTC) and the California Department of Transportation (Caltrans) are responsible for implementing many of the programs.
- ***Requires Legislative Appropriation.*** Proposition 1B specifies that all bond funds are subject to appropriation by the Legislature, either through the annual budget process or through other legislation before becoming available to a state or local entity for expenditure. The bond act specifically requires that $7.5 billion in funds from three programs—Corridor Mobility Improvement Account (CMIA), Highway 99 Improvement, and Trade Corridor Improvement Fund (TCIF)—be appropriated in the annual budget bill.
- ***Allows for Further Statutory Direction.*** The bond act explicitly allows the Legislature to provide additional conditions and criteria through statute to five new programs created by the measure. These programs are TCIF, Transit Security, State-Local Partnership (SLP), and Port Security.

## 2007-08 Proposition 1B Appropriations

As shown in Figure 2, the 2007-08 budget appropriates a total of $4.2 billion in Proposition 1B funds for various transportation programs. Of this amount, 49 percent is for local assistance, 38 percent for capital outlay, and 13 percent for support (which primarily includes project development and management). For each program, the amount of funds appropriated in 2007-08 is less than the amount of funds authorized in Proposition 1B for the program. In other words, additional bond funds will need to be appropriated for all of the programs in subsequent years.

As part of the 2007-08 budget package, the Legislature also adopted trailer bill legislation—Chapter 181, Statutes of 2007 (SB 88, Committee on Budget and Fiscal Review), Chapter 314, Statutes of 2007 (AB 196, Committee on Budget), and Chapter 187, Statutes of 2007 (AB 201, Committee on Budget)—that further defines and directs the implementation of Proposition 1B. For example, the adopted legislation imposes various requirements on the appropriate administrative agencies (like CTC and

**Figure 2**

**2007-08 Appropriations of Proposition 1B Funds**

*(Dollars in Millions)*

| Program | Support | Local Assistance | Capital Outlay | Total |
|---|---|---|---|---|
| Local Streets and Roads | — | $950.0 | — | $950.0 |
| State Transportation Improvement | $63.4 | 112.9 | $551.1 | 727.4 |
| Corridor Mobility Improvement | 14.3 | — | 594.0 | 608.3 |
| Local Transit | — | 600.0 | — | 600.0 |
| State Highway Operation and Protection | 21.3 | — | 259.0 | 280.3 |
| Air Quality | 250.0 | — | — | 250.0 |
| School Bus Retrofit | 193.0 | — | — | 193.0 |
| Intercity Rail | 1.1 | — | 187.0 | 188.1 |
| Grade Separation | 0.6 | 122.5 | — | 123.1 |
| Traffic Light Synchronization | — | 122.5 | — | 122.5 |
| Transit Security | 1.5 | 100.0 | — | 101.5 |
| Port Security | 1.1 | 40.0 | — | 41.1 |
| Highway 99 Improvement | 8.3 | — | 6.0 | 14.3 |
| Local Bridge Seismic | 0.1 | 13.5 | — | 13.6 |
| Trade Corridor Improvement | 0.1 | — | — | 0.1 |
| State-Local Partnership | 0.1 | — | — | 0.1 |
| **Totals** | **$554.9** | **$2,061.4** | **$1,597.1** | **$4,213.4** |
| **Percent of Total** | **13%** | **49%** | **38%** | **100%** |

Caltrans) relative to adopting program guidelines and reporting on how bond funds are actually spent.

## IMPLEMENTATION OF PROPOSITION 1B TO DATE

For each Proposition 1B program, Figure 3 (see next page) specifies the state entity that is responsible for administering the program. As indicated in the figure, Caltrans and CTC are responsible for administering many of the programs. Implementing agencies are generally responsible for (1) developing guidelines that specify the requirements of each program and the criteria for evaluating project nominations, (2) selecting specific projects for funding, and (3) allocating funds to specific projects.

**Figure 3**

**Proposition 1B Programs—Implementation Status**

*(As of January 2008)*

| Program | Implementing Agency[a] | Guidelines Adopted | Approved Projects |
|---|---|---|---|
| Corridor Mobility Improvement | CTC | 11/28/06 | 54 |
| Highway 99 Improvement | Caltrans | 12/13/06 | 13 |
| STIP[a] | CTC | 12/14/06 | 80 |
| Port Security | OES/OHS | 11/9/07 | — |
| Trade Corridor Improvement | CTC | 11/27/07 | — |
| SHOPP[a] | CTC | —[b] | 15 |
| Local Transit | SCO/Caltrans | 12/5/07 | — |
| Intercity Rail | Caltrans | 12/13/07 | — |
| Transit Security | OES/OHS | 12/19/07 | —[c] |
| Local Streets and Roads | SCO/DOF | 1/15/08[d] | — |
| Air Quality | ARB | —[e] | — |
| Grade Separation | Caltrans/CTC | —[f] | — |
| Local Bridge Seismic | Caltrans | — | — |
| Traffic Light Synchronization | CTC | — | — |
| State-Local Partnership | CTC | — | — |
| School Bus Retrofit | ARB | — | — |

a STIP = State Transportation Improvement Program; SHOPP = State Highway Operation and Protection Program; CTC = California Transportation Committee; SCO = State Controller's Office; DOF = Department of Finance; Caltrans = Department of Transportation; ARB = Air Resources Board; OES = Office of Emergency Services; OHS = Office of Homeland Security

b Existing SHOPP guidelines were used to select projects.

c Chapter 181 requires OHS to allocate some of the funds by February 1, 2008.

d DOF is not required by statute to adopt guidelines for the Local Streets and Roads Program. The date shown represents the date that letters were sent by DOF to cities and counties to notify them of their eligibility and inform them of the application process.

e Chapter 181 requires ARB to adopt guidelines by December 31, 2007. At the time this analysis was prepared, the guidelines had not been adopted.

f Chapter 181, Statutes of 2007 (SB 88, Committee on Budget and Fiscal Review), requires CTC, in cooperation with Caltrans, the Public Utilities Commission, and the High-Speed Rail Authority, to develop guidelines by February 15, 2008.

In reviewing the administrative agencies' efforts to implement each of the different programs, we find that (1) guideline adoption and project selection have generally been on schedule, (2) many projects are being funded with multiple fund sources, (3) CTC plans to expand the TCIF program by $1 billion, and (4) funding allocations for the Local Streets and Roads program have been unnecessarily slow.

## Guideline Adoption and Project Selection Generally on Schedule

For each of the different Proposition 1B programs, Figure 3 also indicates whether the necessary guidelines for project eligibility and selection have been adopted and whether specific projects have been selected. In general, progress of a particular program has been influenced by statutory deadlines. For example, Proposition 1B required CTC to adopt guidelines for CMIA by December 1, 2006, and an initial program of projects by March 1, 2007. As indicated in the figure, both guidelines and projects have been approved for STIP, CMIA, and Highway 99 Improvement. In programming the Proposition 1B funds for STIP, CTC decided to also program small amounts of additional revenues from other STIP sources (such as the Public Transportation Account) that were not available when the 2006 STIP was adopted. Collectively, this is referred to as the 2006 STIP Augmentation, for which the commission adopted new program guidelines. The CTC also approved projects to receive the additional SHOPP funding, using existing program guidelines. Recently, CTC adopted guidelines for TCIF and plans to select projects for the program in April 2008.

To date, a total of 162 projects have been approved and are expected to receive bond funds in the next several years (see Figure 3). However, this is not to say that these are 162 distinct projects. This is because projects may be relying on funding from more than one Proposition 1B program. For example, a few CMIA projects were also approved by CTC to receive some of the additional funding made available through the STIP augmentation.

## Projects Relying on Other Fund Sources

***Bond Funds Will Support Mainly Construction Costs.*** In implementing its respective Proposition 1B programs, CTC gave priority to projects that it determined could be delivered in a timely manner. Specifically, the commission selected those projects that would be able to go to construction within a certain time frame. For example, the guidelines for CMIA required that projects must begin construction by December 31, 2012, which is also the deadline specified in the bond act. The Highway 99 Improvement program guidelines also stated that CTC would only fund projects that could begin construction by the end of 2012. In addition to these construction deadlines, the commission also specified that bond funds would primarily support construction costs. Thus, project sponsors had to find other revenue sources, such as federal funds, local funds, or other state funds, to fund the pre-construction activities, such as environmental review and right-of-way acquisition.

***Many CMIA and Highway 99 Projects Are Also STIP Projects.*** Given the above requirements, as well as the sheer magnitude in terms of the total cost of individual projects, those projects with identifiable funds for pre-construction activities were at an advantage in the selection process. This is because CTC essentially used bond funds to speed up projects that were dependent on future STIP revenues for construction costs. Specifically, CTC decided to fund projects already programmed in the STIP—the state's ongoing program for adding capacity to its transportation system—that also met the criteria of the particular Proposition 1B program. For example, more than one-half of the projects for CMIA are also STIP projects (non-Proposition 1B). Although some of the pre-construction activities for these projects have already begun, STIP funding would still need to be allocated in the next several years to finish getting all of them ready for construction, since the bond funds are primarily for construction purposes only. The current 2006 STIP also includes specific pre-construction activities that would eventually improve Highway 99.

### CTC Plans to Expand Trade Corridor Improvement Program by $1 Billion

Proposition 1B established a new program, TCIF, to fund improvements along trade corridors with a high volume of freight movement, as well as authorized $2 billion in one-time funding to support the program. According to the bond act, the funds are not limited to projects on the state highway system. For example, TCIF can provide funding to projects that would improve the freight rail system, the capacity and efficiency of seaports, and airport ground access. Effectively, the TCIF program represents a change from the state's traditional transportation funding program. Prior to Proposition 1B, the state had no transportation funding specifically dedicated to trade corridor mobility. Furthermore, projects such as freight rail improvements have not been traditionally funded by the state in the past.

In adopting the guidelines for the new TCIF program, CTC stated its intention to initially approve projects for a total of $3 billion, based on the assumption that $1 billion in additional resources will be provided to the program. Specifically, the commission anticipates the diversion of about $500 million from the State Highway Account (SHA) to TCIF. In addition, CTC also assumes the availability of $500 million from yet to be determined new revenue sources, such as federal funds, user fees, and tolls. According to CTC staff, the overall intent of the commission is to establish TCIF as an ongoing program, rather than a one-time bond program. (Please see the "Funding for Transportation Programs" write-up in the "Crosscutting Issues" section of this chapter for further discussion regarding the implications of these actions.)

### Local Streets and Roads Allocations Unnecessarily Slow

The Proposition 1B Local Streets and Roads program allocates funds directly to cities and counties based on statutorily required formulas to enhance the capacity, safety, and operations of local streets and roads. This program is similar to the existing state program which provides a portion of the state gasoline tax revenues directly to cities and counties for street and road improvements. A key difference, however, is that gas tax subventions can be used for support or capital purposes, whereas bond funds are to be used only for capital projects that have a useful life long enough to be considered appropriate for bond funding. Additionally, bond-funded projects will be monitored regularly to ensure their timely delivery and completion.

***Department of Finance to Review Project List.*** Statute requires that before a city or county can receive a Proposition 1B allocation, a list of projects expected to be funded with bond funds must be sent to the Department of Finance (DOF). The DOF then must report to the State Controller's Office on a monthly basis those cities and counties that have submitted project lists so that allocations can be made. After the allocation of funds, cities and counties are required, upon expending funds, to submit documentation to DOF providing project details necessary to meet the accountability requirements described above.

***No Funding Has Been Allocated to Cities and Counties.*** At the time of this analysis, none of the $950 million in Proposition 1B funds appropriated for the current year has been allocated for street and road purposes. This is in part because DOF has been slow in initiating the allocation process. It did not notify cities and counties of the amount of funds they are eligible for nor provide them with the necessary information on how to file their project lists until January 15, 2008. It is unclear why it took DOF five months after the adoption of the budget to roll out the program. In comparison, the Local Transit program, which is administered by Caltrans and requires a similar process, did not experience this type of delay. Furthermore, given the similarities between the Proposition 1B Local Streets and Roads program and the existing gas tax subvention program, the Legislature would have expected the allocation of funds to progress more quickly.

## GOVERNOR'S 2008-09 PROPOSITION 1B PROPOSALS

The Governor's budget proposes appropriating about $4.7 billion in Proposition 1B funds in 2008-09, as shown in Figure 4 (see next page). This amount includes:

- About $3.3 billion to relieve congestion and make improvements on the state's highways. Although the budget includes support funding to administer the local streets and roads program, it does not appropriate additional local assistance funds for the program. The budget assumes the current-year amount would not be fully expended for a couple of years, and thus, no additional funding would be needed in 2008-09.

- $423 million for local transit and intercity rail projects.
- $750 million to facilitate goods movement and improve air quality, including $500 million for the newly created TCIF program. (Please see the "Department of Transportation" write-up for a further discussion about the proposed funding for TCIF.)
- $246 million to enhance the safety and security of the state's transportation system, including $160 million for transit and port security programs to be administered by the Office of Emergency Services.

Based on the above Proposition 1B appropriations proposed in the Governor's 2008-09 budget, roughly one-half of the total $20 billion authorized in Proposition 1B would remain available to be appropriated in future years.

## Issues for Legislative Consideration: Factors That May Slow Future Progress

The appropriation of bond funding, the adoption of program guidelines, and the selection of projects are only the first steps in ensuring that Proposition 1B projects are delivered in a timely manner. Timely delivery of bond-funded projects depends on other factors as well, such as the availability of funds anticipated from other sources. In this section, we highlight key challenges that may slow the future progress of these projects.

### Other Funds Necessary for Delivery May Not Be Available

***State Funds.*** State law requires CTC to adopt a biennial fund estimate that projects all federal and state transportation funds that would be available for expenditure over a five-year period. These funds include mainly revenues from state and federal excise taxes on motor fuels, sales tax on motor fuels, and truck weight fees. The fund estimate also projects the amount of funds to be committed to various purposes over the forecast period. Priority is given to highway maintenance and operations, local assistance, and SHOPP projects. Any remaining funds would be available for STIP projects. Based on the funding level identified in the fund estimate, CTC programs specific projects in the STIP over the five-year period, which essentially represents a commitment of state funding for these projects. For example, the 2006 STIP programmed projects from 2006-07 through 2010-11 based on the 2006 Fund Estimate.

In October 2007, CTC adopted the 2008 Fund Estimate for 2008-09 through 2012-13 (with 2007-08 included as a base year). The fund estimate projects that there would be less funding, totaling $820 million, available for STIP during the 2007-08 through 2010-11 period, relative to the 2006 Fund Estimate. In other words, the projection is that there will not be enough revenues available to fund the current STIP program. Since many of the CMIA and Highway 99 Improvement projects selected for Proposition 1B funds are also projects that rely on STIP funding for the pre-construction phases, a shortage in STIP funding could cause project

**Figure 4**

**Governor's Proposed Proposition 1B Appropriations for 2008-09**

*(In Millions)*

| Program | Amount |
|---|---|
| **Congestion Reduction, Highway and Local Road Improvement** | |
| Corridor Mobility Improvement | $1,546.9 |
| State Transportation Improvement | 1,186.9 |
| State-Local Partnership | 200.1 |
| Traffic Light Synchronization | 122.0 |
| Highway 99 Improvement | 107.7 |
| State Highway Operation and Protection | 93.9 |
| Local Streets and Roads | 0.1 |
| **Transit** | |
| Local Transit | $350.0 |
| Intercity Rail | 72.6 |
| **Goods Movement and Air Quality** | |
| Trade Corridor Improvement | $500.1 |
| Air Quality | 250.1 |
| School Bus Retrofit | — |
| **Safety and Security** | |
| Transit Security | $101.5 |
| Grade Separation | 64.8 |
| Port Security | 58.1 |
| Local Bridge Seismic | 21.1 |
| **Total** | **$4,657.4** |

sponsors (regional transportation agencies as well as Caltrans) to delay the delivery of these bond projects. Alternatively, they could decide to keep the bond projects on schedule and, thus, delay other nonbond projects. Delaying STIP projects, including those that are not receiving bond funds, into future years would effectively reduce the availability of funds in those years for new STIP projects—meaning those not currently programmed in the 2006 STIP.

***Local Funds.*** In addition to state funds, local funds—mainly local sales tax revenues—are also being used to support the total cost of many of Proposition 1B projects. The leveraging of local funds is occurring, in part, because Proposition 1B requires at least a one-to-one match of nonstate funds for TCIF, SLP, and Grade Separation grants. In addition, in selecting CMIA projects, CTC considered a project's ability to leverage local funds, particularly for large projects where matching funds are available. Similarly, some of the projects in the other bond programs are so large that they would not be able to move forward without the support of local funds. Thus, the delivery of certain bond projects could be delayed if local funds are not available at the levels initially planned.

## Legislative Clarification Needed for Some Programs

In order to ensure that the SLP and Local Transit programs authorized in Proposition 1B move forward in the budget year, the state will need to clarify its expectations of these programs. The absence of such direction could further delay project delivery.

***SLP Program Eligibility.*** Proposition 1B provides $1 billion in SLP grants to match local funds for transportation projects over a five-year period. The bond measure does not specify the types of projects eligible for funding. In adopting the 2007-08 budget, the Legislature chose to appropriate no funding for the SLP program, mainly because it wanted to further define the program in legislation. Although a few bills that seek to further define SLP have been considered during the current legislative session, none of them have been adopted.

For 2008-09, the Governor's budget proposes $200 million in Proposition 1B funds for the SLP program. In accordance with the Legislature's intent, we believe that legislation defining how the program would operate should be enacted before appropriating any bond funds for the program in the 2008-09 budget. According to CTC, it is waiting for legislative direction regarding the implementation of the SLP program before it develops and adopts the necessary guidelines.

***Future Local Transit Allocations.*** Proposition 1B provides $3.6 billion for local transit capital projects such as the construction and expansion of rail and bus systems, and the acquisition of rolling stock (buses and rail cars). These funds are to be distributed to local transit agencies by formula based on population and fare revenues.

Chapter 181, Statutes of 2007 (SB 88, Committee on Budget and Fiscal Review) provided direction only for the allocation of the $600 million appropriated for 2007-08. Accordingly, Caltrans adopted guidelines for the program that only cover the current year. For 2008-09, the budget proposes an appropriation of $350 million, however it is not known how the amount will be allocated because the existing statutory formula may not apply to the budget-year funding. The "one-year only" allocation formula raises issues for project sponsors, as follows.

- ***Uncertain Allocation Process Makes Project Planning Difficult.*** Uncertainty about how funds will be allocated from year to year can hamper efforts by project sponsors to plan for projects. For instance, large projects that require funding over multiple years would be difficult to plan and fund without some knowledge of how future bond funding will be distributed from year to year, and how much funding a project sponsor could reasonably expect over several years. This uncertainty could lead to projects being proposed that might not be of the highest priority just so that the project would fit the available funding.
- ***Not Clear if Allocations Can Be "Saved Up."*** The current-year allocation formula does not specify whether transit operators can "save up" their allocations from year to year in order to make large purchases, or if annual allocations will be lost if not used. If allocations cannot be banked, project sponsors may be unable to fund larger projects. Additionally, some small transit operators may receive such a small annual allocation that they may not be able to effectively use the funds if they cannot be saved up.

## Caltrans Staffing Not on Track to Deliver Projects

Caltrans is responsible for the delivery of most highway and intercity rail projects funded by Proposition 1B. The department is also responsible for delivering SHOPP and STIP projects funded by nonbond sources (including SHA, Transportation Investment Fund, and federal funds). In order to ensure that Proposition 1B projects, as well as other non-Proposition 1B projects, will be delivered in a timely manner, Caltrans will need adequate personnel resources to plan and construct capital outlay projects. As we discussed in our January 2007 report, *Implementing the 2006 Bond Package*, before a capital outlay project can be constructed, Caltrans must first assess environmental impacts, acquire rights-of-way, and design and engineer the project. Caltrans is also responsible for overseeing the progress of project construction (including instances when others are performing the work on projects on the state highway system). Collectively, this type of work is typically referred to by the department as capital outlay support (COS).

In adopting the 2007-08 budget, the Legislature provided Caltrans $1.8 billion to fund 13,121 personnel-year equivalents (PYEs) in staff resources, including both state staff and contracted services, to design and engineer transportation projects. This level of resources was based on the department's own workload estimates. As shown in Figure 5, about 5 percent (or 640 PYEs) of the total 13,121 budgeted PYEs are intended to specifically support certain Proposition 1B programs for which Caltrans is responsible for delivering and overseeing the projects.

***Slow Progress in Hiring State Staff.*** In order for Caltrans to plan and construct all of the transportation projects—both Proposition 1B and non-Proposition 1B projects—it plans to work on in 2007-08, the department will need to hire roughly 700 PYEs in new state staff in the current year. At the time this analysis was prepared, Caltrans reported that it has hired 185 new COS staff in the first five months of the fiscal year (from July 1, 2007 through November 31, 2007). This amounts to an average of 37 PYEs per month. If the department maintains this current hiring rate, it will fill nearly 65 percent of the required 700 PYEs. This also assumes that the department will be able to contract out for project development services at the level originally planned, which is about 10 percent of COS personnel resources. Given Caltrans' likely inability to hire all the necessary state staff, we believe that the delivery of projects will be delayed.

# RECOMMENDATIONS

Based on our review of the implementation of the various Proposition 1B programs and our analysis of factors that could delay project delivery, we recommend below measures to ensure that bond funds are used to deliver effective projects in a timely manner. Specifically, we recommend the Legislature (1) establish SLP eligibility and selection guidelines, (2) determine an ongoing process for allocating future transit funds, (3) require Caltrans to provide a realistic staff-hiring plan, and (4) authorize design-build contracting for transportation projects.

## Establish Eligibility and Selection Guidelines for SLP Program

***Before appropriating funds for State-Local Partnership grants in 2008-09, we recommend the enactment of legislation to provide multiyear eligibility guidelines to ensure that the bond funds are used effectively in meeting the state's priorities.***

**Figure 5**

**Caltrans Capital Outlay Support**

*2007-08*

| | Personnel-Year Equivalents |
|---|---|
| **Proposition 1B Uses** | |
| STIP[a] Augmentation | 382 |
| SHOPP[a] Augmentation | 127 |
| Corridor Mobility Improvement | 77 |
| Highway 99 Improvement | 54 |
| Subtotal | (640) |
| **Non-Proposition 1B Uses** | |
| SHOPP | 4,360 |
| STIP | 2,828 |
| Supervision and overhead | 2,657 |
| Reimbursed work[b] | 1,469 |
| Toll seismic | 627 |
| Traffic Congestion Relief Program | 230 |
| Real property services[c] | 169 |
| Seismic retrofit | 131 |
| Soundwall retrofit | 10 |
| Subtotal | (12,481) |
| **Total** | **13,121** |

a SHOPP = State Highway Operation and Protection Program; STIP = State Transportation Improvement Program.

b Includes locally funded projects (such as Regional Measure 1 in the Bay Area).

c This refers to the management of properties acquired for current and future state highway projects.

The Governor's budget proposes $200 million for SLP in 2008-09. However, before any bond funds are spent on the program, the Legislature should ensure that eligibility guidelines are statutorily established to assure that funds are used for projects that address state priorities in the most efficient and effective manner. As discussed in our *Analysis of the 2007-08 Budget Bill*, we recommend the Legislature:

- ***Define Sources of Local Match.*** Proposition 1B requires a one-to-one match of local funds for the SLP program. However, the measure does not specify the types of fund sources that could be counted towards this match. The Legislature should define what local funds can be used as a match, which could include revenues from tolls, local sales tax measures, and developer fees.

- ***Require Fund Leveraging in Project Selection.*** Because the benefits of transportation investments are felt most at the local level, evaluating projects by their ability to tap into non-state dollars (so that state funds can be applied to more projects) makes sense. In order to stretch SLP funds, we recommend the Legislature require projects to be evaluated based on their ability to leverage local funds beyond the required one-to-one match.

- ***Structure Program to Spur New Local Investment.*** A primary source of local transportation funds is from existing local sales tax measures and transportation developer fees that have already been adopted by local jurisdictions. However, in order to spur new local funding for transportation, we propose that the Legislature adopt guidelines that would set aside a portion of the program funding for cities and counties that establish new fees or tax measures for local transportation projects. Alternatively, the Legislature could specify the term of the SLP program, as well as the annual total amount available for allocation, thus, giving local jurisdictions the incentive and time to develop and pass new local sales tax measures.

- ***Require Consideration of Air Quality Impacts.*** Given that all of California's major urban areas fail to meet federal air emissions standards, SLP project selection should consider a project's impact on air quality. In order to enable CTC to take emissions impacts into account in selecting projects, we recommend the Legislature require analysis of air quality impacts to be included in all nominations where projects would add capacity to the highway and local road network.

In the "Department of Transportation" write-up in this chapter, we recommend the Legislature adopt budget bill language specifying that the availability of the proposed $200 million appropriation for the SLP program is contingent upon the enactment of legislation regarding the program's eligibility guidelines.

## Determine Ongoing Allocation Process for Transit Capital Program

***We recommend the enactment of legislation that specifies an ongoing allocation formula for the local transit program that is applicable on a multiyear basis rather than adopting a formula one year at a time. We also recommend allowing project sponsors to bank funds over multiple***

***years of the program. If adopted, both of these recommendations would reduce funding uncertainty for transit agencies, thereby facilitating the delivery of transit projects.***

As mentioned previously, the allocation process for the transit program was only determined for the current-year appropriation. Uncertainty about future allocation formulas as well as future funding levels makes project planning difficult and can cause delays or other inefficiencies in project selection. We recommend the enactment of legislation that specifies how funds for the transit program will be allocated in 2008-09 and beyond.

- ***Determine Ongoing Allocation Process.*** The Legislature should establish a formula that directs the allocation of funds from year to year for the remaining funds in the program. Doing so would allow transit agencies to better estimate their share of each year's funding they can expect to receive. This, in turn, would enable better project selection and priority-setting to utilize the bond funds.
- ***Allow Banking of Funds.*** Under current law, project sponsors have three years from the time an appropriation is made to have a project approved and encumber funds for the project. This effectively allows project sponsors to save up to three years of transit improvement bond allocations for a project. Nonetheless, there could still be instances where project costs exceed a sponsor's three-year allocation. Because it is likely that the bond funds for transit improvements will be appropriated over a period longer than three years, we recommend the Legislature specify in statute that these bond funds can be banked over multiple years of the program. This would provide greater flexibility for project sponsors to more effectively use the bond funds.

## Maximize Resources to Minimize Project Delay

***We recommend the Legislature require the Department of Transportation to provide a realistic staff hiring plan that minimizes project delay.***

Based on the level of Proposition 1B appropriations proposed by the Governor, Caltrans will most likely continue to need substantial COS resources in 2008-09 to deliver all projects. Meeting this personnel requirement predominately through state staff is likely to be difficult, given Caltrans' slow progress in hiring state staff in the current year. Beyond hiring new state staff, Caltrans would also have to locate facilities to house these workers. In addition, the department would have to provide training in order for entry-level employees to perform many COS tasks.

Contracting out provides a means for Caltrans to perform project development workload that exceeds the capacity of its state staff to deliver. However, contracted resources have traditionally played a relatively limited role in performing COS workload at Caltrans—roughly 10 percent of total COS personnel resources in recent years. As we discuss in the "Department of Transportation" section of this chapter, the department will be submitting a revised request for COS resources this spring based on better workload estimates. (The Governor's January budget proposes essentially the same COS level as estimated for the current year, pending this revised request.) As part of the request, Caltrans should provide a realistic staff hiring plan. This plan should include (1) a breakdown specifying what portion of the workload will be completed with state staff versus contracted resources; (2)recent data on Caltrans' ability to recruit, hire, and retain COS staff; and (3) actions the department will take to attract employees and minimize attrition rate. Moreover, Caltrans should explain how its plan will minimize project delay.

## Authorize Design-Build Contracting

***We recommend the enactment of legislation authorizing a design-build pilot program to further facilitate the delivery of Proposition 1B projects.***

The design-build contracting method awards both the design and construction of a project to a single entity. The use of design-build to construct projects seeks to reduce project delivery times by integrating the design and construction processes. Under the federal transportation act (SAFETEA-LU), virtually any surface transportation project is eligible to be built using this method. Current state law, however, authorizes the use of design-build only for specific transportation projects (for example, I-405). Thus, Caltrans has little experience using this method to deliver projects. While there are potential advantages to using design-build, including the potential shortening of project delivery time, there are also potential pitfalls to avoid, including ensuring contracts are awarded fairly and competitively such that public accountability is not diminished.

We recommend that the Legislature authorize a design-build pilot program similar to that proposed by AB 143 (Núñez ), in 2006, and SB 56 (Runner), in 2007. Both bills proposed a demonstration program that would allow Caltrans and regional agencies to deliver a set number of projects using design-build. In addition, these bills required that transportation agencies report on their experiences so that the state could use the information in deciding whether to pursue future design-build projects.

# DEPARTMENTAL ISSUES

*Transportation*

## DEPARTMENT OF TRANSPORTATION (2660)

The Department of Transportation (Caltrans) is responsible for planning, coordinating, and implementing the development and operation of the state's transportation system. These responsibilities are carried out in five programs. Three programs—Highway Transportation, Mass Transportation, and Aeronautics—concentrate on specific transportation modes. Transportation Planning seeks to improve the planning for all modes and Administration encompasses management of the department.

The Governor's budget proposes total expenditures of about $14 billion by Caltrans in 2008-09. This is $262 million, or 1.9 percent, lower than estimated current-year expenditures. The proposed staffing level of 22,430 is slightly higher than the level in the current year. Caltrans' total support in 2008-09 will be provided by a variety of sources, including $4.1 billion (29 percent) from the State Highway Account, $3.9 billion (28 percent) from federal funds, $1.5 billion (11 percent) from the Proposition 42 transfer, and $3.5 billion (25 percent) from Proposition 1B funds. The remaining support will be funded from reimbursements, as well as from various smaller transportation accounts.

## PROPOSITION 1B APPROPRIATIONS

The *2008-09 Governor's Budget* proposes to appropriate a total of about $3.9 billion in Proposition 1B funds to Caltrans for various transportation programs. (While this amount represents the proposed appropriation for 2008-09, the $3.5 billion amount identified above reflects the estimated level of Proposition 1B funds that will be encumbered.) The $3.9 billion appropriation consists of a variety of proposals, including:

- $500 million for the newly created Trade Corridor Improvement Fund (TCIF) program.
- $200 million for a new State-Local Partnership (SLP) program.
- $2.1 million to support additional workload associated with the administration of various Proposition 1B programs.

Below we discuss specific budget requests for each of these three proposals. (Please see our "Implementation of Proposition 1B" write-up in the "Crosscutting Issues" section of this chapter for a more detailed discussion of Proposition 1B.)

### Appropriation Requested for Trade Corridor Improvement Not Substantiated

***We withhold recommendation on the $500 million in Proposition 1B funds proposed for the Trade Corridor Improvement Fund program, pending our receipt and review of a list of projects approved by the California Transportation Commission.***

Proposition 1B, approved by the voters in November 2006, authorized $2 billion in general obligation bonds to fund the establishment of the TCIF program. The purpose of this program is to support infrastructure improvements along trade corridors that have a high volume of freight movement. Proposition 1B specifies that the bond funds for TCIF must be appropriated by the Legislature through the annual budget process, before becoming available to a state or local entity for expenditure. In adopting the 2007-08 budget, the Legislature did not appropriate any funds for the TCIF program. For 2008-09, the Governor's budget proposes to appropriate $500 million in bond funds—$499,999,000 for local assistance in Item 2660-104-6056 and $1,000 for capital outlay in Item 2660-304-6056—to Caltrans for the program.

As we discussed in an earlier write-up on Proposition 1B, the California Transportation Commission (CTC) recently adopted the project eligibility and selection guidelines for the TCIF program. According to the approved program schedule, the commission plans to approve a list of projects for funding this April. Until CTC approves such a list, we do not have sufficient information to advise the Legislature on whether the $500 million proposed by the Governor for TCIF is the level of funding required to support projects in the budget year. For instance, there is no assurance at this time that there will be $500 million worth of TCIF projects ready for funding allocations in 2008-09. Accordingly, we withhold recommendation on the $500 million in Proposition 1B funds requested for the TCIF program, pending our receipt and review of a list of projects approved by CTC.

## Make SLP Appropriation Available Subject to Legislation on Program Guidelines

***We recommend the Legislature adopt budget bill language specifying that the availability of the proposed $200 million appropriation (Proposition 1B) for the State-Local Partnership program is contingent upon the enactment of legislation regarding the program's eligibility guidelines.***

Proposition 1B explicitly allows the Legislature to provide additional conditions and criteria through statute regarding the SLP grant program. The bond act itself provides no guidance as to the types of projects eligible for funding. In adopting the 2007-08 budget, the Legislature chose to appropriate no funding for the SLP program, mainly because it wanted the opportunity to further define the program in legislation. Similarly, as discussed in an earlier write-up, we propose that the Legislature enact legislation providing eligibility guidelines before appropriating bond funds for SLP grants in 2008-09. Such guidelines would help ensure that the bond funds are used effectively in meeting the state's priorities. It is possible that legislation specifying eligibility guidelines for SLP may not be enacted prior to enactment of the budget. Accordingly, we recommend the Legislature adopt budget bill language specifying that the $200 million appropriation in Proposition 1B funds for the SLP program, as proposed by the Governor, shall be available to the department contingent upon the enactment of legislation specifying the program's eligibility guidelines. Specifically, we propose adding the following provision to Items 2660-104-6060 and 2660-304-6060:

> The funds appropriated in this item shall be available for the State-Local Partnership program authorized in the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, contingent upon the enactment of legislation specifying the eligibility guidelines for the program.

## Proposition 1B Administration Needs Are Overstated

***The budget requests 23 new positions and about $2.1 million to administer various Proposition 1B programs. Our review finds that the department's workload estimates are overstated. Accordingly, we recommend rejecting 17 positions and $1.6 million for the divisions of mass transportation and rail. We further withhold recommendation on the remaining six positions and $491,000 for accounting workload. (Reduce Item 2660-004-6059 by $435,000, and Item 2660-004-6063 by $1.2 million.)***

The budget requests 23 additional positions for the department to administer various Proposition 1B programs. The positions requested are for administrative purposes such as accounting and project review, and are separate from capital outlay support (COS). The requested positions include:

- Ten positions for the division of rail, to implement the Highway-Railroad Crossing Safety Account (HRCSA) programs.
- Seven positions to review and approve projects seeking allocations of Local Transit funds.
- Six positions for accounting, to process invoices to be paid from the bond funds.

These positions are in addition to 24 positions authorized in the current year for similar Proposition 1B administrative activities.

***Rail Request for Ten Positions Not Justified.*** Proposition 1B provides $250 million for the HRCSA to fund grade separation and grade crossing projects. The budget requests ten positions for implementation of these programs in 2008-09. This is in addition to three positions authorized in the current year for the same activities.

The $250 million will fund two separate programs. First, $150 million is designated by the bond act to augment the state's existing grade *separation* (Section 190) program. The department estimates it will need one-half a position to implement this program based on the assumption that most of the $150 million will be allocated to projects in 2008-09 and 2009-10. Since the department has already received positions for this work in the current year, the need for an additional half-position is not justified.

The remaining $100 million provided for grade *crossings* will be used for a yet to be defined program of projects that the CTC will develop in consultation with the High-Speed Rail Authority. The budget requests 9.5 positions for the department's expected role in the implementation of this program. At the time this analysis was prepared, guidelines for this new program had not been adopted, but are required to be adopted by February 15, 2008. Without final guidelines, the department's role in the program is not yet certain. However, the department's estimated workload assumes that the guidelines will designate these funds to augment an existing grade crossing (Section 130) program, which is administered by Caltrans. It is unclear why the department makes this assumption since neither the bond act nor current law requires that these funds be used for the existing grade crossing (Section 130) program. Furthermore, a draft version of the guidelines being developed by CTC for this program does not appear to support this assumption. In fact, the guidelines may ultimately require a much smaller role from the department, necessitating only one or two staff positions. Without knowing what role, if any, the department will have in the implementation of this program, the request for positions and $1.2 million is premature.

***Mass Transportation Request Overstated; Reject Seven Positions.*** Proposition 1B provides $3.6 billion for Local Transit capital projects. Statute requires the department to review applications for these funds, determine if projects are appropriate for bond funding, and notify the State Controller's Office of allocations to be made. The budget requests seven positions, in addition to the four authorized in the current year, for the department to handle this work in 2008-09.

In the current year, the Local Transit funds will be allocated in two separate application cycles. At the time this analysis was prepared, the department is completing the first cycle of application review and approval for projects applying for the $600 million appropriated for this program in the current year. This first cycle reportedly required six staff to review applications totaling about $450 million. Four of the staff were authorized for the program in the current year and two were redirected from other programs. If workload stays at the current-year level, providing two additional positions may be justified, so that these staff do not have to continue to be redirected from another program. However, the level of workload necessary to implement this program will most likely fluctuate from year to year based on the amount of funds appropriated. For instance, the budget proposes a funding level of $350 million for the program in 2008-09, this is significantly less than the $600 million provided in the current year. At the lower level proposed for 2008-09, the current staff (of four) should be sufficient to review and approve project applications, and adding staff is not warranted. Accordingly, we recommend rejecting all seven positions and $435,000.

***Accounting Request Does Not Fully Consider Project Time Lines.*** The department requests six positions and $491,000 for accounting workload expected in 2008-09 related to the use of Proposition 1B funds. These positions would be in addition to 17 accounting positions authorized in the current year. The main function of the requested staff would be to process invoices to pay contactors on bond-funded projects. Our review shows that the department's accounting workload estimate is too high. Instead, this workload will be substantially lower in 2008-09 than estimated for mainly two reasons: (1) not all bond programs have been defined and projects for some programs have not yet been selected, and (2) some of the bond programs will only fund construction costs, with many of the projects not going to construction until 2012 or 2013.

Department staff acknowledged that the workload estimates for 2008-09 may not have fully considered the impact of project time lines, and, therefore, may have overstated the number of positions that will be needed. Furthermore, the department indicated that it will be updating the accounting workload estimates and submitting a revised request in the spring. Accordingly, we withhold recommendation on the request for $491,000 and six positions.

# OTHER ISSUES

## COS Request Will Be Amended

***We withhold recommendation on the $1.9 billion requested for capital outlay support staff because staffing needs will be revised during the May Revision when more accurate information on the workload for various state transportation programs becomes available.***

Capital outlay support is the term used by the department to refer to work required to produce capital outlay projects. Before a capital outlay project can be constructed, Caltrans must assess environmental impacts, acquire rights-of-way, and design and engineer the project. Caltrans is also responsible for overseeing the progress of project construction. The COS budget consists primarily of the salaries, wages, benefits, and operating expenses of the more than 10,000 state staff who perform these functions. It also includes the costs of consultants who perform a portion of this work. The COS budget does not, however, include the salaries and benefits of the contractors who construct the actual projects; these costs are part of the capital outlay budget.

The Governor's budget proposes $1.9 billion to fund COS activities in 2008-09—this is essentially the same level as estimated current-year expenditures. The department indicates that it will revise these estimates in the spring as part of the May Revision. By that time, the department will have more accurate estimates regarding the amount of project development work that will be performed during 2008-09. Pending our receipt of the new workload estimates, we withhold recommendation on the department's COS request.

## TPMS Contract Terminated

***We recommend the Department of Transportation report at budget hearings on (1) why the contract to develop the Transportation Permits Management System (TPMS) project was recently terminated and (2) what steps it plans to take to develop an automated permitting system for oversize vehicles, as initially envisioned by the Legislature. Since there is no contract in effect at this time for TPMS, we further recommend deleting from the budget all funding associated with the project.***

***(Reduce Item 2660-001-0042, Schedule 10, by $551,000. Delete Item 2660-494.)***

Caltrans has the authority to issue special permits to oversize vehicles—those that exceed statutory limits on vehicle size, weight, or loading—to allow them to travel on the state's highways. These permits specify the routes oversize vehicles are allowed to take in order to ensure the safety of the highway system. Currently, Caltrans issues these permits manually, which makes the process susceptible to human error. In fact, the department had a poor safety record related to its oversize vehicle permits in the late 1990s. From 1996 through early 2000, there were 31 accidents in California involving oversize vehicles that struck and damaged bridges, one of which resulted in a fatality.

***Automated Permit System Proposed in 2000.*** As an interim measure to reduce errors in the permitting process, Caltrans received funding in the 2000-01 budget for personnel to manually double-check each permit before it was issued, which is still the process being used today. As a long-term solution, Caltrans simultaneously initiated efforts in 2000 to replace its manual permit writing process with an automated system as is used in other states. The Bureau of State Audits concluded in May 2000 that the proposed automated system, known as TPMS, should provide a safer, faster, and more efficient system for issuing oversize permits in comparison to the current system, including the manual double-checkers. The plan called for a new system that would (1) verify eligibility of permit applicants, (2) determine safe truck routes, (3) track applications through the permitting process, (4) issue and automatically deliver permits, (5) assess fees, and (6) maintain financial accounting records. (The text box on the next page provides a time line of the key events associated with the development of the TPMS project.)

***TPMS Contract Approved in 2002.*** As part of the 2000-01 budget, the Legislature appropriated a total of about $12 million to Caltrans for the development of an automated permitting system. In December 2001, the Department of Finance (DOF) and the Department of Information Technology approved a Feasibility Study Report (FSR) for the TPMS project. This report identified a total project cost of about $13 million and estimated an implementation date of October 2002. Following the approval of the FSR, the Department of General Services (DGS) approved in January 2002 a contract between Caltrans and a private contractor for the development of TPMS.

***Project Has Experienced Numerous Delays and Cost Changes.*** Since the approval of the FSR and contract for the development of TPMS, the project has been delayed on more than one occasion. According to Caltrans, this is largely because the private contractor has essentially been unable to deliver a satisfactory product. In September 2003, DOF approved a Special Project Report (SPR) that delayed the implementation of the project from October 2002—the initial implementation target date—to August 2004. Subsequently, a second SPR was approved by DOF in May 2005 that further delayed the project by more than a year to October 2005. This particular SPR also identified an increase in the total project cost to about $15 million.

Due to concerns that the October 2005 implementation deadline would not be met, Caltrans hired another private consultant to conduct a 30-day independent assessment of the project. This consultant, in fact, concluded that the October 2005 deadline was not attainable and that several changes would need to occur in order to complete the project at a later date. Recommended changes included restructuring the project team and

## Chronology of TPMS

| | |
|---|---|
| **2001** | The Department of Finance (DOF) and the Department of Information Technology approve the Feasibility Study Report for the Transportation Permits Management System (TPMS) project, with an expected implementation date of October 2002 and a total cost of about $13 million. |
| **2002** | The Department of General Services (DGS) approves a contract between the Department of Transportation (Caltrans) and a private contractor for the development of TPMS. |
| **2003** | The DOF approves a Special Project Report (SPR) to delay the implementation of TPMS from October 2002 to August 2004. |
| **2005** | The DOF approves a second SPR to further delay the project from August 2004 to October 2005, as well as increase the total project cost to about $15 million. |
| | Caltrans hires a consultant to conduct an independent assessment of the project, which concluded that several changes needed to occur in order for the project to be completed in a timely manner. |
| **2006** | Caltrans, the private contractor, and DGS made several attempts to reach agreement on amendments to the contract. |
| **2007** | The contract for the TPMS project between Caltrans and the private contractor is terminated. |

hiring an independent qualified project manager. Despite implementing many of these recommendations, the project schedule was delayed even further than expected. Over the next couple of years since the completion of the independent assessment, Caltrans, DGS, and the private contractor developing TPMS attempted to reach agreement on amendments to the existing contract. However, such efforts proved unsuccessful.

***Six Years Later...No Project and Development Has Ceased.*** On December 31, 2007, Caltrans and the contractor reached a settlement to terminate the existing contract for the TPMS project. As a part of this settlement, Caltrans agreed to pay the contractor about $1.7 million. With this payment, a total of about $2.6 million would have been provided to the contractor since the initial contract was approved in 2002. In terms of total expenditures on TPMS, Caltrans staff reports that a total of about $10.5 million has been spent on the project. In addition to the settlement payments, this amount includes funds spent on state staff, equipment, and the independent project assessments. However, despite these expenditures, the department still does not have an automated permitting system at this time—about six years after the FSR for the project was approved.

***Caltrans Needs to Explain What Happened.*** In view of the above, we recommend the Legislature require Caltrans to report at budget hearings on why the contract for the TPMS project has been terminated and what lessons it has learned from this experience. As part of that report, the department should also specify what steps it now plans to take in terms of developing an automated permitting system for oversize vehicles, as originally envisioned by the Legislature. Moreover, since there currently is no contract for the development of the TPMS project, we further recommend that the Legislature remove from the proposed 2008-09 budget all funding associated with the project. Specifically, we recommend deleting $551,000 in Caltrans' budget designated for TPMS maintenance and operation expenses. In addition, we propose deleting Item 2660-494, which proposes to extend the liquidation period for funds initially appropriated in the 2000-01 budget for TPMS. Caltrans staff concurs that this item is not needed.

# HIGH-SPEED RAIL AUTHORITY
# (2665)

The California High-Speed Rail Authority (HSRA) is responsible for planning and constructing an intercity high-speed rail system. The authority consists of nine board members appointed by the Legislature and Governor, as well as staff to support program operations and administration.

The budget provides $1.7 million and 9.5 positions for the administration of HSRA. The budget also includes $3.5 million in reimbursements from the Orange County Transportation Authority (OCTA) for project-specific environmental review for a portion of the Anaheim to Los Angeles segment of the proposed high-speed rail system.

***Bond Measure Scheduled for November 2008 Ballot.*** Chapter 697, Statutes of 2002 (SB 1856, Costa) authorized the sale of $9.95 billion in general obligation bonds, $9 billion of which would be for planning and construction of a high-speed rail segment between San Francisco and Los Angeles. The other $950 million would be for projects that provide connections with the high-speed rail system and other modes of transportation. The bond measure was initially scheduled to be placed on the November 2004 ballot, however, the measure was postponed twice and is now scheduled for the November 2008 ballot. The Governor's budget summary indicates that proposed modifications to the bond measure may be forthcoming, however, at the time this analysis was prepared, the Department of Finance was unable to provide any details on the proposed changes.

## Project Work Will be Stopped Before Voters Weigh in

***The budget does not provide funding for High-Speed Rail Authority (HSRA) to contract for project development work. This will effectively stop work on the project beginning July 2008. If voters pass a bond measure on the November 2008 ballot to fund the project, the state would incur unknown costs to restart the project and hire new contractors to continue project development. The Legislature should consider if it***

***wants to provide some funding for HSRA to continue the project until voters make their decision in November 2008.***

***Budget Provides No Funding for Contract Services.*** The budget provides staff support for HSRA, but does not provide any funding for contract services. The HSRA contracts out for almost all the work on the project, utilizing state staff only for contract and program oversight. In the current year, about $17 million in project development work is being carried out through the following key contracts.

- ***Program Management***—direct and manage regional engineering and environmental teams, and develop the basic design for a statewide high-speed train system.
- ***Financial Plan***—develop a plan to fund the development, construction, and operation of the system with various state, federal, and private resources.
- ***Corridor-Specific Contracts***—conduct project-level engineering and environmental work that must be completed before projects can advance to construction. Work is currently being done on the following corridors.

  — Anaheim to Los Angeles

  — Los Angeles to Palmdale

  — Bay Area to Merced

By providing no funding for contract services in 2008-09, work by contractors will have to stop at the end of the current year.

***Reimbursements May Not Materialize Without Continuation of Some Contract Services.*** The Governor's budget includes $3.5 million in reimbursements from OCTA to pay for specific environmental work on the Anaheim to Los Angeles corridor. The HSRA staff indicate that the reimbursement will cover only a portion of the costs of the environmental work on that corridor. With no state funding, it is not clear whether the scope of work can be reduced to cover only the portion of work OCTA is willing to pay for. It is also not clear whether OCTA would want to proceed with, and pay for, a limited scope of environmental work.

***Work on the Project Will Stop Before Bond Measure Goes to Voters.*** Providing no funding for HSRA's contract services will effectively stop all work on the development of a high-speed train system from July 2008 until early November 2008, when voters decide on the bond measure. If the bond measure passes, it would take HSRA some time to restart the project. The state would also incur unknown costs to hire new contractors to continue project development work.

If the Legislature does not want work on the project to cease, it should consider providing some funding for HSRA to continue project development work. The Legislature can consider a number of funding level options. For instance, the Legislature could fund the continuation of all the active contracts through November 2008. This would require approximately $19 million. Alternatively, the Legislature could fund a much reduced level of activity, such as funding through November 2008, work on the Anaheim to Los Angeles corridor only. The HSRA estimates that this would require about $ 5 million, including about $3.5 million in state funds and $1.5 million to be reimbursed by OCTA.

# CALIFORNIA HIGHWAY PATROL (2720)

The California Highway Patrol's (CHP's) core mission is to ensure safety and enforce traffic laws on state highways and county roads in unincorporated areas. The department also promotes traffic safety by inspecting commercial vehicles, as well as inspecting and certifying school buses, ambulances, and other specialized vehicles. The CHP carries out a variety of other mandated tasks related to law enforcement, including investigating vehicular theft and providing backup to local law enforcement in criminal matters. In addition, the department provides protective services and security for state employees and property. Since September 11, 2001, CHP has played a major role in the state's enhanced antiterror activities.

The CHP's overall level of staffing is about 11,000 positions. The department is comprised of uniformed (sworn) and nonuniformed (nonsworn) personnel, with uniformed personnel accounting for approximately 7,600 positions, or 70 percent, of total staff.

The budget proposes $1.9 billion in support for CHP in 2008-09, about $49 million (2.6 percent) above estimated current-year expenditures. The increase reflects proposed increases for employee compensation, patrol officer staffing, and continued implementation of the enhanced radio communication system, partly offset by decreases, most notably for anticipated savings from officer vacancies.

Most of CHP's budget is funded from the Motor Vehicle Account (MVA), which derives its revenues primarily from vehicle registration and driver license fees. For 2008-09, MVA funds would comprise nearly 90 percent of CHP's support costs.

## CHP Unable to Fill Requested Officer Positions

***For 2008-09, the department requests authority to hire an additional 120 road patrol officers, as well as $4 million to fund 44 new staff to support the officers. We recommend the Legislature reject the proposal because based on the department's own estimates, it will not be able to fill the requested positions in the budget year. (Reduce Item 2720-001-0044 by $4 million.)***

***Budget Proposal.*** The Governor's budget requests $21.6 million for 120 patrol officers, and 44 staff—11 uniformed and 33 nonuniformed—to manage and provide administrative support to the officers. The request would bring CHP patrol officer positions to 6,493 in 2008-09 and subsequently to 6,543 in 2009-10. However, due to the high number of officer vacancies at CHP (discussed below), the budget also proposes a $40 million reduction in the department's funding level to reflect savings from anticipated vacant officer positions. The net effect of these two proposals is that for 2008-09 there would be approximately 300 *unfunded* officer positions (including the proposed 120 new officer positions) in CHP. While the budget does not provide funding for the proposed officer positions, it does provide funding (about $4 million) for the 44 support positions.

***Background.*** Over the past two years, the Legislature has added 360 patrol officers and 80 staff to support those officers. Information provided by CHP shows that the department has not been able to fill its new officer positions. At the time this analysis was prepared, the department had approximately 450 vacant officer positions out of a total of 6,423 authorized officer positions. According to CHP, the high number of officer vacancies reflects a combination of factors, most notably the challenge of recruiting and retaining qualified candidates.

***Analyst's Concern and Recommendation.*** Absent the requested positions, the department will begin 2008-09 with approximately 400 vacant officer positions. At CHP's current officer attrition rate (26 per month), an estimated 312 additional officer positions will become vacant during the fiscal year, bringing the total vacant officer positions to 712. According to CHP, it expects to graduate 399 cadets from the academy; thus, ending the fiscal year with 313 vacant officer positions. As such, the department will not be able to fill the requested positions in the budget year. In fact, CHP likely would not fill its current vacancies—and begin to fill the requested positions—until 2010-11. Although the department acknowledges that it will not be able to fill the new positions in the budget year, it nonetheless indicates that the additional position authority is a priority. We find no justification for providing the additional officer positions in 2008-09. We therefore recommend the Legislature reject the request for 120 new officer positions.

The purpose of the 44 support positions is to handle the higher supervisory and administrative workload associated with adding more officer positions. Consistent with our recommendation to reject the proposed officer positions, we also recommend the Legislature reject the requested support positions and delete the amount requested to support these positions ($4 million).

## No Report on Tactical Alerts

***We recommend the Legislature delete the $10 million budgeted for CHP tactical alerts in 2008-09 because the department has failed to provide information to the Legislature justifying this level of proposed spending. (Reduce Item 2720-001-0044 by $10 million.)***

Following the terrorist attacks of September 11, 2001, CHP officers were placed on 12-hour shifts, or "tactical alerts," to enhance preparedness and provide an immediate increase in the level of security services. Since that time, the department has retained some funding in its budget for a similar tactical response should the need arise. The Governor's budget proposes to continue the funding at $10 million.

Last year, the Legislature adopted budget bill language requiring the department to report by December 31 of each year on its prior-year tactical alert activities. The purpose of the report was to provide the Legislature information upon which to determine the appropriate level of funding for the coming fiscal year. At the time this analysis was prepared, the Legislature had not received the department's report on tactical alerts. Absent the required information, there is no basis to justify the funding level for tactical alerts. We therefore recommend the Legislature delete the funding.

# DEPARTMENT OF MOTOR VEHICLES (2740)

The Department of Motor Vehicles (DMV) is responsible for protecting the public interest in vehicle ownership by registering vehicles and for promoting public safety on California's streets and highways by issuing driver licenses. Additionally, DMV licenses and regulates vehicle-related businesses such as automobile dealers and driver training schools, and collects certain fees and tax revenues for state and local agencies. The department operates 215 facilities, which include customer service field offices, telephone service centers, commercial licensing facilities, a headquarters, and driver safety and investigations offices.

The budget proposes total expenditures of $958 million for support of DMV in 2008-09. This represents an increase of $19 million, or 2 percent, above the estimated current-year expenditures. This increase is mostly the result of increases for employee compensation, the full-year cost of prior-year budget adjustments, and facility consolidation and relocations. The budget proposes a staffing level of 8,250 personnel for 2008-09, which is a slight decrease compared to the current year.

About $526 million (55 percent) of the department's total support will come from the Motor Vehicle Account and $359 million (37 percent) from the Motor Vehicle License Fee Account. The remaining support will be funded primarily from the State Highway Account and reimbursements.

## Update on Federal Real ID Act

***In January 2008, the United States Department of Homeland Security released its final regulations for implementation of the federal Real ID Act. In this piece, we briefly summarize highlights of the final regulations and recommend the Department of Motor Vehicles report at budget hearings on specific actions California must take if the state decides to implement Real ID.***

***Background.*** In 2005, federal legislation, known as the Real ID Act, was signed into law. The act mandates states to modify driver licenses and identification cards to meet federal standards by May 2008. It also requires the states to follow certain procedures in the issuance of these documents. The law stems from the recommendations of the 9/11 Commission, and is intended to strengthen national security by making it more difficult for terrorists to gain access to certain services. Under the act, a state may choose not to meet the federal requirements; however, its citizens would not be able to use the state-issued driver license and identification cards for federal purposes, such as receipt of federal services or air travel.

Amid growing opposition to the Real ID act by states, including some states that refused to implement the act, the federal Department of Homeland Security (DHS) in March 2007 issued draft regulations and solicited nationwide input from various stakeholders. During the 60-day public comment period, stakeholders raised numerous concerns regarding the requirements of Real ID. These concerns mostly related to privacy and security of personal information, the lack of federal funding, unreasonable timelines, and increased customer wait times at DMV offices. After consideration of the issues raised during the comment period, DHS released its final regulations in January 2008, five months before the federal statutory deadline for state compliance with the act.

***Final Real ID Regulations Provide States More Time, Some Issues Unresolved.*** The final regulations generally provide states greater flexibility with regard to certain provisions of the act, and more time to implement the required changes. However, some key implementation issues remain unresolved, most notably how state DMV data systems are to be configured to comply with the document verification requirements of the act. We discuss these issues in more detail below.

Figure 1 (see next page) shows the federal compliance time line adopted by DHS in the final regulations. As the figure shows, states have until 2017—as compared to 2013 under the draft regulations—to fully comply with the act.

***Immediate Request For Extension Necessary.*** It is important to note that while the final regulations provide states more time to fully implement the act, states are required to immediately file for an extension to be exempt from the May 2008 deadline. This first extension is good through December 2009. According to DMV, it has already requested this extension.

As a condition of receiving a second extension, which is good through May 2011, states are required by October 2009 to certify that certain "benchmarks" have been met. For example, a state may be required to show that it has taken steps to incorporate certain information into its driver license and identification cards, or that it has begun to implement security standards at the offices that issue license and identification cards as required by the act. States that fail to meet those benchmarks would not be eligible for a second extension, and potentially risk limiting the usefulness of their driver license and identification cards for purposes of commercial air travel and entry to federal facilities. Beginning in May 2011, states must begin issuing Real ID-compliant cards.

Overall, states have up to approximately three years—from May 2008 to May 2011—to make all of the necessary process and card feature modifications required by the act. Then, for up to the next six and one-half years (from May 2011 to November 2017), states are required to issue Real ID-compliant cards.

***Age-Based Issuance of Real ID Compliant Cards.*** The most significant change from the proposed regulations relates to the issuance of Real ID-compliant driver license and identification cards. Under the original proposal, states would have been required to issue new driver license and identification cards to all cardholders within five years (by May 2013), a requirement DMV estimated would cost California about $300 million. The final regulations provide states about nine years to implement the provi-

**Figure 1**

**Real ID Compliance Time Line**

| | |
|---|---|
| 05/11/2008 | By May 11, 2008, the federal government cannot accept state-issued driver licenses or identification cards for official purposes from states that have not been determined to be in compliance, unless the state has requested an extension by mid-March. |
| 12/31/2009 | The initial extension will terminate unless the state, by October 11, 2009, has requested an additional extension and submitted certification that certain REAL ID benchmarks have been met. |
| 05/11/2011 | Driver license and identification cards will not be accepted from states that are not in full compliance with the provisions of REAL ID. States must begin issuing REAL ID compliant licenses. |
| 12/01/2014 | Federal agencies cannot accept driver license or identification cards for official purposes from any individual born after December 1, 1964, unless the issuing state is in compliance with certain provisions. |
| 12/01/2017 | Federal agencies will not accept any driver license or identification cards for official purposes unless the cards are issued by states that certify compliance with certain provisions. |

sion. Specifically, states have until 2014 to issue new cards to individuals born after December 1, 1964, and until 2017 for those born before that date. Giving state DMVs more time to issue the Real ID cards significantly eases the fiscal and operational impacts of the federal act. Since fewer cardholders will be required to visit a DMV field office in any given year to apply for the new driver licenses, fewer staff resources and infrastructure changes will be required, and customer wait times will not be as long.

***State Requirements for Real ID Verification Processes Still Unknown.*** One of the major requirements of Real ID is that states use several national databases to verify the authenticity of identification documents presented in applications for driver license and identification cards. However, since the databases had not yet been developed, it was impossible for states to comply with the act by the required date. To address this issue, the regulations simply require states to become compliant as the systems become available.

The regulations provide no further guidance as to the technology requirements for complying with the data verification provisions of the act. However, DHS has indicated that it is working with states, other federal agencies, and the American Association of Motor Vehicle Administrators (AAMVA) to define requirements for a network and "hub" to support data verification and the state-to-state data check requirements. The technology solution currently under consideration is AAMVAnet, the network system operated by AAMVA to support the Commercial Driver's License Information System on behalf of the US Department of Transportation.

***Real ID Privacy Concerns Still to Be Addressed.*** Various requirements of Real ID raised concerns regarding the privacy and security of personal information. For example, the act requires states to share certain information to ensure that no individual holds more than one driver license. It also requires the cards to use machine-readable technology, which potentially enables private vendors—for example, a grocery store—to collect the personal information of its customers from the card.

In response to privacy concerns, DHS indicates in its final rules that it plans to issue "privacy and security best practices to help guide states in protecting the information collected, stored, and maintained pursuant to Real ID." The regulations also require states to prepare a security plan for state facilities and information systems. The department further indicates that it is working with various federal and state entities to develop a governance structure for information sharing between the systems that allows states to protect the autonomy and security of information in their respective databases. Finally, the federal department also suggests that if cardholders experience abuses regarding third-party misuse of the cards, Congress and the states can determine later whether and how to address these abuses.

***Still No Serious Federal Plan to Fund Real ID***. The DHS estimates it will cost states about $4 billion to implement Real ID, significantly less than the $11 billion estimate derived from a nationwide survey by the National Governor's Association, the National Conference of State Legislatures, and AAMVA. The DHS largely attributes the difference to the longer compliance time lines and state discretion adopted in the final regulations. However, until states have an opportunity to closely review the regulations, it is too early to know if the $4 billion estimate is realistic.

The federal government has appropriated a total of $90 million to support Real ID implementation in the states. Of this amount, only $6 million has been awarded, and California did not receive any of the funds. Additionally, states are allowed to use up to 20 percent of their State Homeland Security Grant Program funds for this purpose. In the final regulations, DHS states that the Bush administration is "continuing to work with Congress on the availability of additional funding to the States for this purpose."

To date, the Legislature has provided DMV approximately $27.5 million related to Real ID. The funds have been used to enhance DMV's ability to efficiently manage the higher volume of field office customers that would be required to fully implement the act within the time lines initially contemplated by the federal government. For example, the department is in the process of upgrading its Web site infrastructure to allow more customers to transact business without having to visit a field office; thereby, freeing up resources in the field offices to handle the increased workload anticipated to result from Real ID. For 2008-09, DMV expects to spend $2.5 million to continue these efforts.

***Department Should Report on Revised Implementation Plan and Costs.*** In 2006, DMV's preliminary estimate pegged the state cost at about $500 million over five years for additional staff, facilities, and technological improvements required to implement the act in California. In light of the longer time lines for Real ID compliance, and other changes included in the final regulations, we recommend the Legislature direct the department to report at budget hearings on (1) the specific actions that the state has to take to meet the benchmarks required for certification under the federal regulations, and (2) its revised cost estimate. Based on our initial review of the final regulations and discussions with DMV, we think it is reasonable to expect the overall cost to be lower than DMV's preliminary estimate of $500 million.

We would also note that Real ID implementation will require statutory changes to conform state law to federal law and regulations. As yet, no explicit statutory authority exists to implement the act. We would further recommend that the department report at budget hearings on the statutory changes that will be required to implement the act.

## No Report on Information Technology Modernization Project

***The budget requests $33 million for the third-year funding of a multiyear project to update the Department of Motor Vehicles's technology infrastructure. We withhold recommendation on the request pending receipt and review of the overdue report on the project's status.***

In 2007-08, the Legislature provided $24 million for the second-year funding of a multiyear project to update the technology infrastructure that supports DMV's core functions. The DMV estimates the project will cost approximately $240 million when completed. The *2007-08 Budget Act* also contains language requiring DMV to report annually in December on the status of the project. Specifically, the department is required, at a minimum, to report on its progress toward planned milestones, planned versus actual expenditures, and any variations from the original scope of the proposal.

The budget requests $33 million for the third year of the information technology modernization project. Prior to receipt of the report, there is little information upon which to determine if the funds requested are reasonable and consistent with DMV's current schedule and costs. We therefore withhold recommendation on the request pending receipt and review of the required report. The report will allow the Legislature to determine if the project is on schedule and budget before committing the additional funds.

# FINDINGS AND RECOMMENDATIONS

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## Crosscutting Issues

### *Funding For Transportation Programs*

A-20 ■ **Current-Year Actions Underfunded the State Transportation Improvement Program (STIP).** About $1 billion in STIP projects from 2007-08 through 2009-10 could be delayed as a result of the reduced revenues to STIP. The California Transportation Commission (CTC) has kept projects on track in the current year by advancing the use of bond funds, but the underfunding will need to be addressed in 2008-09.

A-22 ■ **Court Rejected Part of Current-Year Diversions.** A recent court decision ruled as illegal the current-year use of $409 million in Public Transportation Account (PTA) funds to pay past debt service.

A-22 ■ **Trade Corridor Improvement Fund (TCIF) Program Plans Would Delay Existing Transportation Projects.** In addition to the $2 billion authorized in Proposition 1B, CTC plans to direct an additional $1 billion from other fund sources (including $500 million available for the State Highway Operation and Protection Program) to support TCIF projects. Changing the funding priority of rehabilitation and safety projects would delay the delivery of existing transportation projects.

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A-26 ■ **Transportation Spending Will Focus on Proposition 1B Programs.** Under the Governor's proposed budget, a large portion of transportation spending will be on programs authorized in Proposition 1B. Although these programs may meet the state's transportation needs in the short term, they do not address them on an ongoing basis.

A-28 ■ **Delays in Traffic Congestion Relief Program (TCRP) Funding Will Delay Some Projects.** Funding for TCRP was initially delayed and is now expected to trickle in over the next nine years. This lengthy repayment schedule will delay some projects, particularly large projects that are ready, but require funding levels in excess of the amount that is available.

A-29 ■ **PTA Requires Loan to Stay Solvent Through 2008-09.** The budget proposes a $60 million loan from the Traffic Congestion Relief Fund to keep PTA solvent. Even with this loan PTA will have a slim fund balance and may require additional loans if revenues are lower than estimated.

A-30 ■ **Maintenance and Rehabilitation Funding Continue to Shrink.** As the state highway system ages, the costs to maintain and rehabilitate state highway miles are increasing much faster than the revenues which pay for them. We recommend actions to ensure that sufficient revenues are available to address long-term maintenance and rehabilitation needs.

### *Motor Vehicle Account Condition*

A-36 ■ **Motor Vehicle Account (MVA) Faces Deficit Without Corrective Actions.** The Governor's budget proposes to increase vehicle registration fees and penalties to address a projected shortfall in the MVA beginning in 2008-09. Although our analysis finds that the administration's revenue projections are overstated, the proposal likely would provide sufficient revenue to keep the account solvent for several years.

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***Implementation of Proposition 1B***

A-52 ■ **Establish Eligibility and Selection Guidelines for State-Local Partnership (SLP) Program.** Recommend enactment of legislation specifying the multiyear eligibility guidelines for SLP, in order to ensure that the bond funds are used effectively in meeting state priorities.

A-54 ■ **Determine Ongoing Allocation Process for Transit Capital Program.** Recommend enactment of legislation to specify an ongoing allocation process and to allow banking of funds over multiple years, to reduce funding uncertainty and facilitate project development.

A-55 ■ **Maximize Resources to Minimize Project Delay.** Recommend the Legislature require the Department of Transportation to provide a realistic staff hiring plan that minimizes project delay.

A-56 ■ **Authorize Design-Build Contracting.** Recommend enactment of legislation authorizing a design-build pilot program to further facilitate the delivery of Proposition 1B projects.

## Department of Transportation

A-58 ■ **Appropriation Requested for Trade Corridor Improvement Not Substantiated.** Withhold recommendation on the $500 million in Proposition 1B funds (Items 2660-104-6056 and 2660-304-6056) proposed for the Trade Corridor Improvement Fund program, pending receipt and review of a list of approved projects.

A-59 ■ **Make State-Local Partnership (SLP) Program Appropriation Available Subject to Legislation on Program Guidelines.** Recommend the Legislature adopt budget bill language specifying that the availability of the proposed $200 million appropriation (Proposition 1B) for the SLP program is contingent upon the enactment of legislation regarding the program's eligibility guidelines.

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A-59 ■ **Proposition 1B Administration Needs Overstated. Reduce Item 2660-004-6059 by $435,000 and Item 2660-004-6063 by $1.2 million.** Recommend the Legislature reject 17 positions and $1.6 million for the divisions of mass transportation and rail on a workload basis. Withhold recommendation on six positions and $491,000 for accounting workload.

A-62 ■ **Capital Outlay Support (COS) Request Will Be Amended.** Withhold recommendation on the $1.9 billion requested for COS staff because staffing needs will be revised during the May Revision when more accurate information on the workload becomes available.

A-62 ■ **Transportation Permits Management System (TPMS) Contract Terminated. Reduce Item 2660-001-0042, Schedule 10, by $551,000. Delete Item 2660-494.** Recommend the department report at budget hearings why the contract to develop TPMS was recently terminated. Since there is no contract in effect at this time, we further recommend deletion of all funding in the budget for the project.

## High-Speed Rail Authority

A-66 ■ **Project Work Will Be Stopped Before Voters Weigh in.** Most work on the project will likely be stopped if funding for contract services is not provided. If a bond measure is passed in November 2008, the state will incur an unknown cost to restart the project. The Legislature should consider if it wants to provide some funding for project work through November 2008.

## California Highway Patrol (CHP)

A-70 ■ **CHP Unable to Fill Requested Officer Positions. Reduce Item 2720-001-0044 by $4 Million.** Recommend the Legislature reject the proposal because the department will not be able to fill the requested positions in the budget year.

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A-71 ■ **No Report on Tactical Alerts. Reduce Item 2720-001-0044 by $10 Million.** Recommend the Legislature delete $10 million budgeted for tactical alerts in 2008-09 because the department failed to provide the Legislature its annual report on prior-year tactical alert activities and spending.

## Department of Motor Vehicles

A-72 ■ **Real ID Update.** Recommend the Legislature direct the department to report at budget hearings on (1) specific actions that the state has to take to meet the benchmarks required for certification under federal Real ID regulations, (2) its revised costs, and (3) any statutory changes required to implement the act in California.

A-77 ■ **No Report on Information Technology Modernization Project.** Withhold recommendation on the third-year funding of the Department of Motor Vehicles (DMV's) information technology modernization project ($33 million) pending receipt and review of the required annual report from DMV. The report will allow the Legislature to determine if the project is on schedule and budget before committing the additional funds.