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Government Relations

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RE: Legislative Update

The Bad, the Worse, and the Ugly: With modulated understatement Governor Schwarzenegger laid out his budget plan by noting that unemployment has “ticked down” and the “economy has ticked up”.

The Governor announced that his \$82.9 billion budget projects a \$19.9 billion shortfall. It provides for “no new taxes”. His close-the-gaping-fissure proposals include \$8.4 billion in state cuts, including bombs bursting in air over IHSS, CalWORKS, SSI/SSP and other County administered programs. State workers take a big hit here, too, with furloughs eliminated and replaced with a 5% permanent pay reduction and another 5% reduction in workforce. His \$4.5 billion in “revenue shifts” include a convoluted scheme to undo voter-passed Proposition 42 and circumvent court decisions to take \$1.5 billion out of public transit, plus another \$350 million grab from redevelopment. Finally, there is that \$8.3 billion (current and fiscal years combined) he will squeeze from the federal government with the help of the four legislative leaders.

As denizens of bad budgets for many years, we can honestly say we’ve never seen a worse one—and that’s saying something. Last year’s was so very devastating, and solved so very ineffectively, that there is little salvation for the current situation. The Gov told an overflowing roomful of reporters, and the rest of California via live TV, that California baseline revenues have fallen more than 20% from their peak, and are projected to remain at 30% lower than 2007-08 projections for several more years. Of course we all remember those squirrely 2007-08 projections—one of the many factors leading to today’s mess.

The Governor called for an immediate emergency session (under terms of Proposition 58) to deal with his proposals for closing this year’s gap, and legislative leadership on both sides appear unanimous on the need to act as soon as possible. Every week without a current year fix means more slashing in the budget year. That didn’t stop the delay last year, but maybe everybody has learned something from that fiasco.

Decreased revenues are attributed by DOF to the ongoing effects of the recession, court decisions that “blocked the implementation” of some of the obviously shaky legal moves from last year, “erosion in the value of some of the savings adopted in 2009,” and “additional costs associated with population-driven and caseload-driven entitlement programs.” In September we projected all of those unrealistic factors could leave the budget \$9 billion short in this fiscal year. So -- maybe the \$6.6 billion is the *good news*. No. It’s all bad.

Gas Tax Counter Proposal: The Democrats in the Senate and Assembly are exploring all options to the Governor’s proposal to eliminate that sales tax on fuel. A formal counter proposal is expected to be unveiled next week. Due to fiscal pressures, they are working to achieve budget savings close to the \$1.8 billion in budget savings the Governor has identified for this proposal. It appears the proposal being explored also calls for the elimination of the sales tax on gasoline, but continues to collect the sales tax on diesel fuel. The sales tax on diesel fuel is the primary funding source for the Public Transportation Account, which would provide some operating funds to transit operators. The proposal would also increase the excise tax and dedicate those revenues to transportation bond debt service, but the amount of the increase has not been determined. Other items under consideration would expand local revenue options.

Additional details will be sent as they become available. The Governor’s proposal and the counter proposal does not address how it interacts with the Transit Association’s lawsuit.

Words of Warning from the Controller: Last week the Legislature got lots of advice, including some stern words from State Controller John Chiang. He announced in a letter to the legislative leaders and the Governor on Friday that although the State’s cash condition is “marginally better than it was one year ago, it is still precarious.” Chiang admonished them to quickly address the projected budget and cash shortfalls for the current and fiscal years to protect the economic recovery, enable the financing of public works projects, and prevent those residents that have been hurt by the recession from experiencing even greater hardship.

Specifically, the Controller predicts that the State’s cash position will be “weak” from March 30 through April 21. On April Fools Day it will be no joke that the State will be in the red by \$197 million. Chiang believes that \$2.7 billion in “cash solutions” are necessary to avoid a cash shortage in the current fiscal year. Further, the Controller advises that even with the solutions proposed in the Governor’s Budget adopted in a timely manner, at least another \$2 billion would be needed to protect our cash balance, just in the current fiscal year.

The Controller is worried that signs of an improving economy will lull legislators into waiting until after the May Revision to make their Budget choices. He thinks this is a dangerous tactic because the decisions that need to be made require lead time for implementation. Therefore, Chiang adds his voice to that of the Legislative Analyst in urging the Legislature to act swiftly to resolve the State’s budget woes.

High Speed Rail: Both the Assembly and Senate have conducted hearings on the High Speed Rail Authority's new business plan. While the new plan is better than past efforts, it still falls short in many areas. The LAO's review points out the lack of a risk management plan and what happens if the ridership projections do not materialize. The LAO also questions how the plan reconciles the conflict in the plan to guarantee a rate of return for private partners while the high speed rail bond act prohibits the use of public subsidy for operations. Senator Lowenthal also questioned to ridership estimates that shows higher inter-regional trips at Merced than at Los Angeles.

Transportation

Sales Tax on Fuel Eliminated: In order to circumvent the court decision that struck down the State's attempt to use public transit funds for non-transit purposes, the Governor proposes to eliminate the sales tax on fuel, which eliminates approximately \$1.2 billion in Public Transportation Account funds and \$1.4 billion in Prop 42 revenue. This proposal only to the state's share of the sales tax; local sales taxes would still apply.

The lost revenue would be partially backfilled by increasing the excise tax by 10.8 cents, which would generate about \$1.9 billion that would be appropriated as follows:

- \$629 million to backfill the lost Prop 42 funds for the STIP.
- \$629 million to backfill lost Prop 42 funds for Local Streets and Roads program. The base streets and roads funds allocated through HUTA remain unchanged.
- \$602 million would be used to pay the Prop 1B bond debt service.

However, the STIP and Local Streets and Roads programs would no longer benefit from the Prop 42 Constitutional protections, and would be subject to annual budget whims. Since the excise tax must comply with the restrictions in Article 19, transit capital projects will no longer be eligible for STIP funding.

Finance indicated that this proposal will be part of the special session on the current year budget deficit and it will require a 2/3 vote.

Short Term Gas Tax Cut: Currently, the per gallon state tax on fuel is approximately 34 cents (18 cent excise tax + the sales tax). Under the Governor's new proposal the state tax on fuel would be reduced to 28.8 cents per gallon. Department of Finance (DOF) explained that the tax rate is not fixed, but it would increase each year in order to provide sufficient revenue to pay for the debt service on transportation bonds. The total excess tax would be capped at 34 cents per gallon.

Project Impacts: This proposal eliminates all public transit funding, as well as eliminating the ability to fund transit capital projects in the STIP. While funds will linger in the PTA for the next year, the budget proposed to divert those funds to pay for bond debt service, intercity rail costs, and transit capital projects in the STIP. After the funds are gone, intercity rail would become a General Fund obligation.

As for transit capital projects in the STIP, the DOF stated there are “almost enough” remaining PTA funds to cover the PTA funded projects in the STIP. When it runs out, the remaining projects will have to fight for General Fund dollars. However, any transit capital project using Prop 42 funds or projects that do not meet the restrictions of Article 19 will need to be removed from the STIP.

State Transit Assistance: The only thing remaining in the State Transit Assistance account is bond money. The budget proposes to appropriate \$350 million in Prop 1B transit capital bonds.

Project Document Costs: The budget proposes to shift to local agencies the cost of completing “project initiation documents” (PIDs) for local projects. This transfers to locals \$12.5 million in added costs to move projects forward. Locals are already paying for this service because the state currently takes this money off-the-top when formulating the fund estimate.

GARVEE Projects: The budget proposes to increase funding from GARVEE bond funded projects by \$680 million. This is intended to accelerate work of three SHOPP projects, including Doyle Drive, SR 10/605 Interchange, and the 710 rehabilitation project. The budget estimates this will save \$11 million in project costs.

Public-Private-Partnership: The Caltrans budget includes a proposal to spend \$3.45 billion over the next 30 years, or \$115 million per year, to fund and attract private partners and investors in transportation projects.

High Speed Rail Authority: The budget provides \$958.2 million for both operations and capital outlay for the high speed rail project. The revenue source is \$581 million in high speed rail bond funds and \$375 million in federal ARRA funding.

Red Light Cameras: The budget assumes \$337.9 million would be generated by implementing a new traffic violation created for those who speed through intersections. The speeding violations would be recorded by already-existing red-light cameras and would have two tiers, depending upon the speed of the vehicle (currently the cameras capture only red-light violations). The Governor’s proposal calls for 15 percent of the revenues to be retained by the pertinent local agency, and 85 percent to be transferred to the State. Of the revenues generated, \$297 million would go to the trial courts to offset General Fund support and \$41 million would be expended to address court security costs.

Tax Collections: The Administration proposes to increase spending at the Board of Equalization by \$9.9 million, to restore resources for revenue collection activities. Now all those furloughed BOE workers can get back to collecting the taxes that pay the State’s bills. They have a similar \$14.7 million proposal to bring back Franchise Tax Board employees and hire temps to reduce the backlog. (Duh!)