CALIFORNIA BUDGET PROJECT

BUDGET BACKGROUNDER

SEPTEMBER 2006

MAKING DOLLARS MAKE SENSE

HOW IS TRANSPORTATION FUNDED IN CALIFORNIA?

Introduction

Transportation projects in California are funded through a myriad of programs and revenue streams. Special funds – funds that are designated for a particular purpose – comprise the majority of state funding for transportation. This *Budget Backgrounder* provides a brief overview of California's transportation programs and examines how transportation is funded at the federal, state, and local levels. Specifically, this report focuses on spending by state agencies responsible for building and financing roads, highways, and transit.[1]

Transportation in California: Then and Now

After World War II, development in California's suburban areas was facilitated by a public commitment of resources to build an extensive freeway system. The federal government provided matching funds to the state on a nine-to-one basis through legislation dedicating $28 billion to the Interstate Highway System. During Governor Pat Brown's tenure in the 1960s, California was a national leader in expanding transportation infrastructure. In less than 20 years, from 1956 to 1972, the state Division of Highways – the predecessor to the California Department of Transportation (CalTrans) – increased the number of miles in the state highway system by 28 percent.[2]

In contrast, current state law recognizes that "Revenues available for investment in California's transportation system have not kept pace with…increasing state population, or with the increased demand on the state's transportation infrastructure."[3] In 1999, the California Transportation Commission (CTC), the body responsible for allocating transportation funds and advising the state government on transportation policies, estimated that California's unfunded transportation needs had reached $117 billion. In 2004, the CTC estimated that this figure would grow to $160 billion by 2009-10.[4] In 2004, CalTrans estimated that the deferred maintenance backlog for highways alone had reached $587 million.[5] According to CalTrans, maintenance spending on the state highway system would need to increase by $105 million per year just to stop growth in the maintenance backlog; spending would have to increase by $250 million annually to address deferred maintenance projects within five years.[6]

State Transportation Funds: Where Does the Money Come from and Where Does It Go?

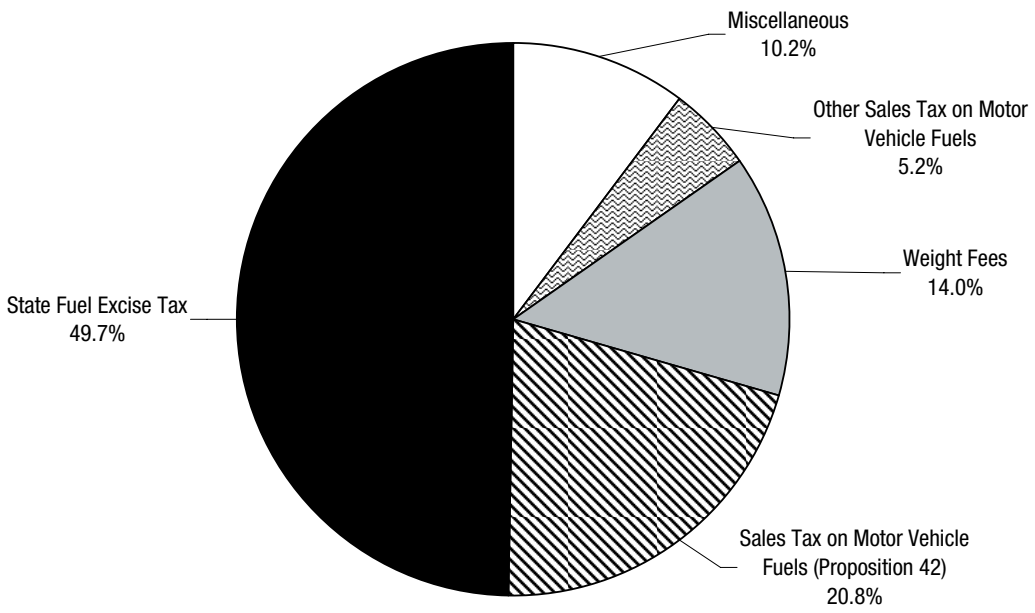
Special funds – funds that are designated for a particular purpose – comprise the majority of state funding for transportation. For example, more than half of transportation dollars are derived from the fuel excise tax (49.7 percent) and weight fees (14.0 percent), both of which are typically thought of as user fees since they are paid by drivers and are directed to transportation purposes (Figure 1). About one-fifth (20.8 percent) of state transportation dollars come from the sales tax paid on motor vehicle fuels under Proposition 42. A small portion of transportation dollars (5.2 percent) comes from other sales tax paid on motor vehicle fuels, including Proposition 111, "spillover" revenues, and sales tax paid on diesel fuel. The remainder of state transportation funds (10.2 percent) is derived from Proposition 116, Proposition 192, toll revenue bonds, and toll bridge revenues. All of these revenues are outlined in more detail below.

Fuel Excise Tax

The principal source of state revenue for transportation is the state excise tax on motor vehicle fuels. The state taxes motor vehicle fuel (the "gas tax"), diesel fuel, and alternative fuels (the "use fuel tax") on a per-gallon basis. Gasoline and diesel excise taxes will generate an estimated $3.5 billion in 2006-07.[7]

About two-thirds of these revenues are allocated to the State Highway Account (SHA), while the remainder goes to cities and counties for streets and roads. The California Constitution

Figure 1: State Funding Sources for Transportation*



* 2005-06 estimated. Miscellaneous includes Proposition 116 and Proposition 192 bond revenues, toll revenue bonds, and toll bridge revenues.
Source: Department of Finance

How Does the State Plan for Its Transportation Needs?

State transportation programs are made up of three major components. Funding for all three is administered by the California Transportation Commission (CTC):

- **The State Transportation Improvement Program (STIP)** is a five-year capital improvement plan, updated every two years, for transportation projects throughout the state. The STIP includes schedules and cost estimates for projects that add capacity to the state's transportation infrastructure, such as widening freeways or modernizing buses. STIP funds are distributed by formula to regional and inter-regional projects.
- **The State Highway Operation and Protection Program (SHOPP)** is a four-year capital improvement plan, updated every two years, for the rehabilitation and operational improvement of the state's highway system. SHOPP projects have first call on transportation dollars. The SHOPP includes schedules and cost estimates for all highway rehabilitation projects, such as repaving, as well as projects to improve safety and operations. SHOPP projects are funded based on statewide need, rather than through a geographic formula.
- **The Traffic Congestion Relief Program (TCRP)** includes funding for 141 specific transportation projects designated in state law (the TCRP is discussed in more detail below). The TCRP is funded separately from the STIP. [8]

requires state motor vehicle fuel tax revenues to be used for planning, construction, maintenance, and operation of public streets and highways, as well as planning, construction, and maintenance of public transit tracks and related facilities, such as train stations. These revenues cannot, however, be used to operate or maintain public transit facilities and services.[9]

Weight Fees

Revenues from weight fees paid by commercial truckers, also deposited into the SHA, provide about 14 percent of state funding for transportation. Weight fees will generate an estimated $961 million in 2006-07.[10]

Sales Tax on Motor Vehicle Fuels

The state also imposes a sales tax on motor vehicle fuels. These revenues flow to the Public Transportation Account, the General Fund, and the Transportation Investment Fund (Proposition 42). Revenues from this tax are estimated at $2.2 billion in 2006-07.[11]

Public Transportation Account (PTA)

The PTA was established in 1971 to support public transportation projects. At least half of PTA funds flow to the State Transit Assistance Program for mass transit operations and capital projects, while the remainder supports various other public transportation purposes.[12] This special fund derives its revenue primarily from the sales and use taxes on diesel fuel and gasoline, most notably a 4.75 percent (out of 5 percent) state sales tax on diesel fuel. Sales tax revenues deposited in the PTA will total an estimated $326 million in 2006-07.[13]

In addition, the PTA receives revenues from the sales tax paid on the portion of gas tax imposed by Proposition 111 of 1990.[14] (See the "Proposition 111: The Traffic Congestion Relief and Spending Limitation Act (1990)" box for details.) This amount totals an estimated $68 million in 2006-07. The PTA also receives "spillover" funds. Spillover occurs when sales tax revenues (at 4.75 percent) on all goods, including gas, exceed revenues (at 5 percent) on all sales, excluding gas.[15] The 2006-07 budget agreement allocates the spillover revenues, estimated at $668 million, to Proposition 42 loan repayment ($200 million), seismic retrofit of Bay Area bridges ($125 million), farmworker transportation grants ($20 million), high-speed rail development ($13 million), and transit programs ($310 million).

General Fund

Prior to 2001-02, the remaining sales tax paid on motor vehicle fuels was deposited into the state's General Fund. The Legislature had the authority to allocate funds to transportation programs through the state budget. Beginning in 2001-02, the Traffic Congestion Relief Program (TCRP) directed the remaining sales

Proposition 111: The Traffic Congestion Relief and Spending Limitation Act (1990)

Proposition 111 increased revenues for transportation, modified the state's spending limit, and changed the formula used to calculate the state's school funding guarantee. Specifically, the measure:

- **Increased the gas tax and truck weight fees.** Proposition 111 increased the 9-cent-per-gallon state excise tax on motor vehicle fuels by 9 cents between 1990 and 1994, and increased commercial vehicle weight fees by 40 percent in 1990 and by an additional 10 percent in 1995.[16] The new revenues were directed to construction of state highways, local streets and roads, and public transit facilities.
- **Provided partial authorization for a transportation bond.** Proposition 108, the Passenger Rail and Clean Air Bond Act of 1990, included language specifying that it would only take effect if voters also approved Proposition 111, which appeared on the same ballot. Proposition 108 authorized the state to issue $1 billion in general obligation bonds to fund capital improvements on rail transit systems.
- **Changed the State Appropriations Limit (SAL) formula.** Proposition 111 changed the inflation and population factors used to calculate the SAL, which was approved by voters in 1979. The SAL is a constitutional limit on the growth of certain appropriations from tax proceeds, generally set to the level of the prior year's limit as adjusted for changes in the cost of living and population.
- **Changed the calculation and allocation of excess revenues under the SAL.** Prior to passage of Proposition 111, the state Constitution required that specified revenues exceeding a certain limit in any year must be returned to taxpayers. Proposition 111 allocated half of the excess revenues to public schools and community colleges and half to tax reductions; it further provided that excess revenues would only have to be allocated to taxpayers and schools if the limit is exceeded in two consecutive years.
- **Changed the K-14 education funding guarantee.** Proposition 111 allowed the state to reduce the Proposition 98 minimum funding guarantee for public schools and community colleges in certain low-revenue growth years. Proposition 111 also required that the funding base be restored in future years so that K-14 education funding would be restored in future years.[17]

How Are Bonds Related to Transportation?

Bonds enable the state to finance major projects, such as transportation projects, that it cannot afford on a "pay-as-you-go" basis. The state borrows money from investors and then repays this money, plus interest, over a period of years. The annual amount paid by the state to investors (principal plus interest) is known as debt service. The state issues three types of bonds related to transportation:

- **General Obligation (GO) Bonds.** While GO bonds can be placed on the ballot through the initiative process, many are placed on the ballot by the Legislature. The state Constitution requires GO bonds to be approved by a two-thirds vote of the Legislature and a majority of the voters. GO bonds are backed by the state's General Fund. The 2005-06 Budget appropriated $3.2 billion from the state's General Fund for debt service on GO bonds (3.5 percent of General Fund spending) and appropriated $11.8 billion in GO bond proceeds for various capital projects. In recent years, voters have approved three GO bonds specifically designated to fund transportation; according to the Legislative Analyst's Office (LAO), General Fund payments for debt service on these three measures total approximately $350 million per year:
    - **Proposition 108,** the Passenger Rail and Clean Air Bond Act of 1990, authorized $1 billion in GO bonds for intercity rail, commuter rail, and rail transit programs. (Proposition 108 was linked to passage of Proposition 111, the Traffic Congestion Relief and Spending Limitation Act of 1990.)
    - **Proposition 116,** the Clean Air and Transportation Improvement Act of 1990, authorized $2.0 billion in GO bonds, mostly for rail capital outlay.
    - **Proposition 192,** the Seismic Retrofit Bond Act of 1996, authorized $2 billion in GO bonds for reconstruction, replacement, and retrofit of state-owned toll bridges and highway bridges.[18]
- **Lease-Revenue Bonds.** Lease-revenue bonds, also called lease-payment bonds, were authorized by the Legislature for the first time in 1983-84. Lease-revenue bonds require a majority vote of the Legislature, but do not require voter approval. The state typically uses lease-revenue bonds to finance the construction and renovation of state facilities, such as CalTrans buildings. State agencies and departments make annual lease payments to bond holders, funded primarily through General Fund appropriations. Unlike GO bonds, lease-revenue bonds are not backed by the full faith and credit of the state. As a result, lease-revenue bonds carry higher interest costs than GO bonds. The 2005-06 Budget included $622.3 million for the General Fund's debt service obligations on lease-revenue bonds (0.7 percent of General Fund spending) and allocated $1.2 billion in lease-revenue bond proceeds for various projects.
- **Revenue Bonds.** The state uses revenue bonds to finance revenue-producing projects, such as toll bridges or parking structures. Revenue bonds are repaid with the revenues produced by these projects. Revenue bonds are authorized by the Legislature and generally do not require voter approval.[19]

tax paid on motor vehicle fuels to the Transportation Investment Fund (TIF) and the Traffic Congestion Relief Fund (TCRF).

In addition, in recent years voters have approved three general obligation (GO) bonds specifically to fund transportation, which are repaid out of the General Fund. (See the "How Are Bonds Related to Transportation?" box for details.)

The Traffic Congestion Relief Fund (Proposition 42)

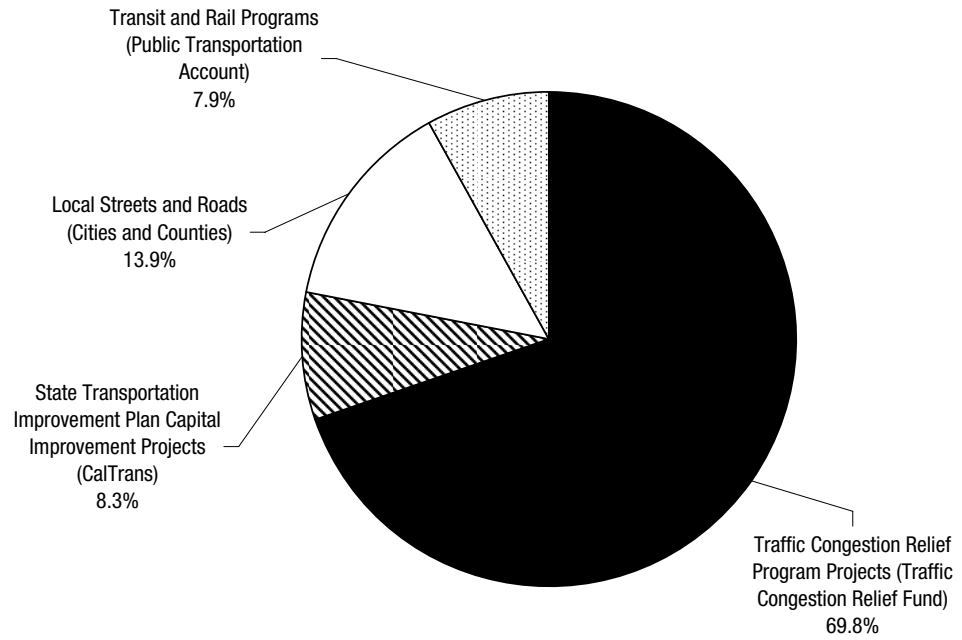
In July 2000, legislation creating the Traffic Congestion Relief Program (TCRP) was signed into law as part of the 2000-01 budget agreement.[20] This measure, signed at the height of the state's economic boom, temporarily transferred sales taxes paid on motor vehicle fuels to the newly created TIF and the TCRF. The TIF and TCRF were to be funded with $7.15 billion over six years from General Fund revenues and revenues from the sales tax paid on motor vehicle fuels. Of the initial $2 billion in funds in 2000-01, $1.6 billion was allocated to transportation through the TCRP, while the remainder was allocated to local governments for street and road maintenance and rehabilitation. The Traffic Congestion Relief Act allocated funding by formula over six years to the newly created TCRP ($5 billion); projects under the STIP ($996 million); local streets and roads ($596 million); and transit and rail programs ($568 million) (Figure 2).[21] The 2001-02 budget agreement included a measure to permanently dedicate the state's sales tax on motor vehicle fuels to transportation programs.[22] This measure was approved by voters in the form of Proposition 42 in March 2002.

Proposition 42: The Transportation Congestion Improvement Act (2002)

Proposition 42 amended the state Constitution to permanently dedicate the sales tax on motor vehicle fuels to transportation beginning in 2003-04. Specifically, the measure:

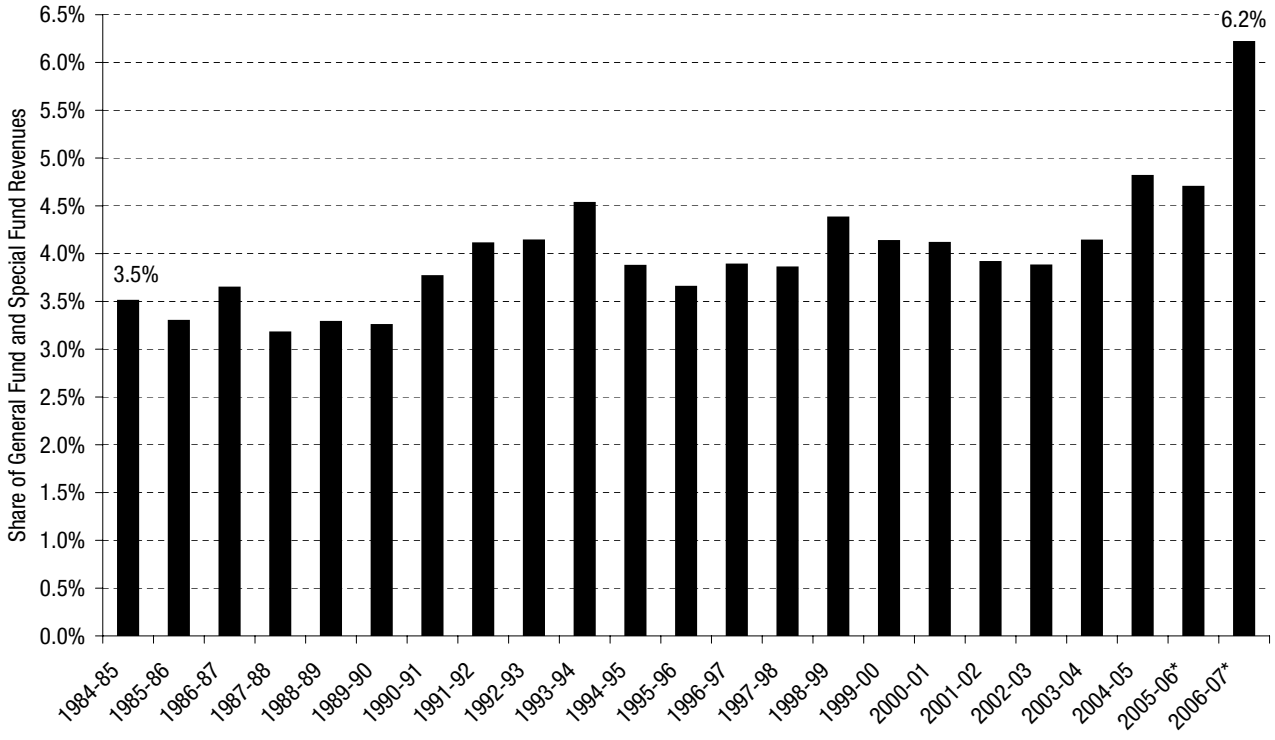
- **Maintained the Traffic Congestion Relief Act (TCRA)** allocation of revenues from the sales tax on gasoline. Specifically, under Proposition 42, the 141 projects included in the TCRP have first call on funds ($678 million per year). The remainder – originally estimated to total around $1 billion per year – is allocated to transportation-related capital improvement projects (40 percent); cities for maintenance and repair of local streets and roads (20 percent); counties for maintenance and repair of local streets and roads (20 percent); and to public and mass transit (20 percent). Half of the public and mass transit share augments the State Transit Assistance Program (allocated by formula to state transit operators) and half augments funding for the STIP.
- **Locked in the TCRA allocation, with a key exception.** Proposition 42 provided that the Legislature could modify the allocation by a two-thirds vote.
- **Locked in the transfer of revenues from the sales tax on motor vehicle fuels, but allowed for future suspensions in the event of a fiscal emergency.** Proposition 42 also provided that the transfer could be suspended with a two-thirds vote of the Legislature and a gubernatorial declaration that the transfer would have a significant negative impact on other programs. In November 2006, voters will consider an initiative making it more difficult for the Legislature to suspend Proposition 42 (see "Where Are We Now?" at the end of this report).[23]
- **Modified the allocation of revenues beginning in 2008-09.** Proposition 42 provided that beginning in 2008-09, when the TCRP ends, revenues from the sales tax on motor vehicle fuels will no longer be transferred from the TIF to the TCRF for the 141 projects. Instead, 40 percent of these revenues will be allocated from the TIF to cities and counties for local projects, 40 percent to STIP projects, and 20 percent to public transportation.[24]

Figure 2: Annual Traffic Congestion Relief Act Allocation, 2001-02 Through 2005-06



Source: Legislative Analyst's Office

Figure 3: Share of State Budget Devoted to Transportation Has Increased Over Time



* 2005-06 estimated, 2006-07 budgeted. 2006-07 amount includes prepayment of Proposition 42 loans due in 2007-08 and 2008-09.
Source: CBP analysis of Legislative Analyst's Office data

How Much Does the State Spend on Transportation?

Since 1984-85, spending on transportation has accounted for an average of 4.0 percent of total state spending (Figure 3).[25] Transportation has grown to a slightly larger share of spending since 2002-03, accounting for nearly 5 percent in 2004-05 and 2005-06. The 2006-07 budget agreement significantly increased funding for transportation on a one-time basis by prepaying several Proposition 42 loans that are due in 2007-08 and 2008-09.

Nearly three-quarters of funds that support transportation programs are "locked in" (Figure 4). Special funds – funds that are designated for a particular purpose – provide more than two-thirds (74.7 percent) of the dollars for transportation, meaning that transportation funds generally cannot be diverted for other purposes or, in most cases, to close a budget gap. The remaining 25.3 percent comes from the state's General Fund. In contrast, just 21.5 percent of total state spending comes from special funds.[26]

How Does the Federal Government Fund Transportation?

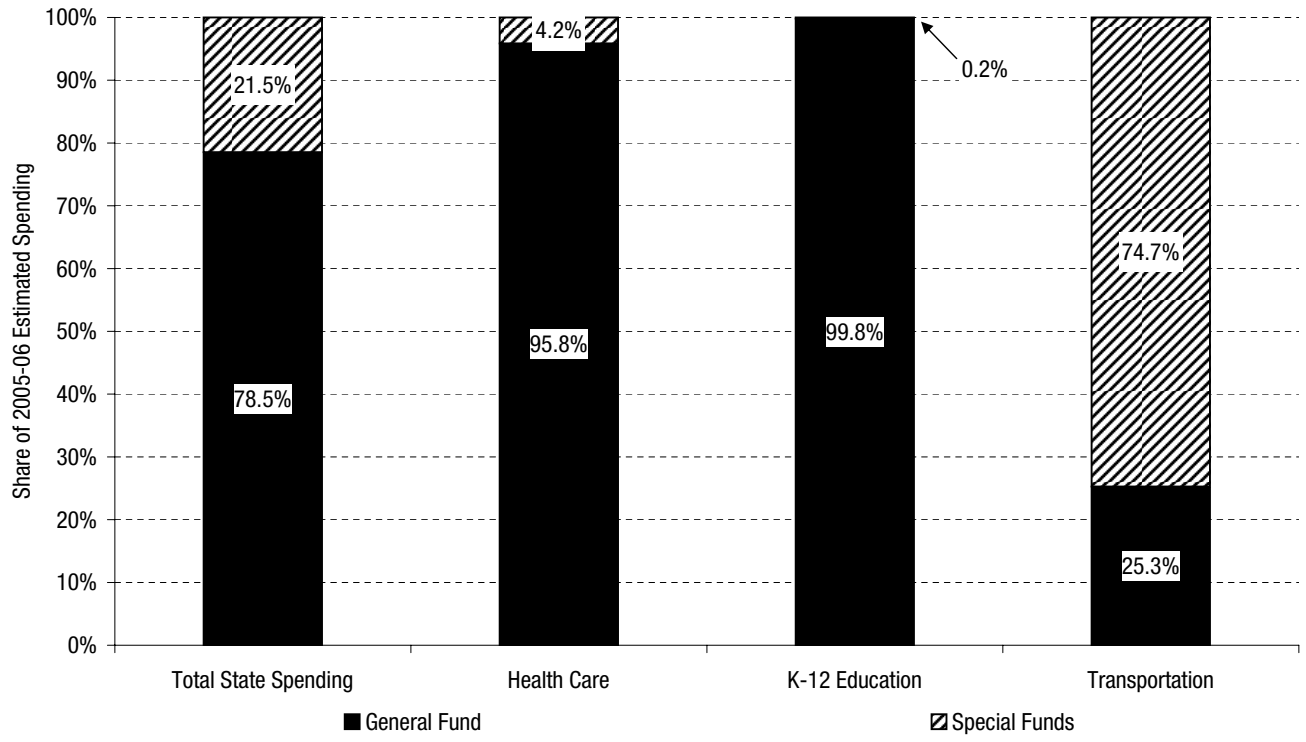
The Highway Trust Fund (HTF)

The federal Highway Trust Fund (HTF) was created in 1956 to fund the nation's highway system. The HTF, which is administered by the US Department of Transportation (DOT), derives the majority of its revenue from federal excise taxes on gasoline, diesel, gasohol, and special fuels. The federal excise tax on gasoline has been imposed at 18.4 cents per gallon since 1993, while diesel fuel taxes are set at 24.4 cents per gallon. Revenues from excise and sales taxes on tires, trucks, trailers, and heavy commercial vehicles are also deposited into the HTF, as well as fines levied from penalties for violations of federal highway safety laws.

The HTF is composed of:

- **The Mass Transit Account (MTA).** The MTA, created by the Highway Revenue Act of 1982, is administered by the DOT's Federal Transit Administration (FTA) and accounts for about one-fifth of federal transportation dollars apportioned to states. The MTA's share of the federal fuels tax is set at 2.86 cents per gallon.

Figure 4: Most State Transportation Spending Is "Locked In" Through Special Funds



Note: Proposition 42 funds are counted under General Fund.
Source: CBP analysis of Legislative Analyst's Office data

- **The Highway Account.** The remainder of the HTF, generally known as the Highway Account, funds the Federal-Aid Highway Program (FAHP) and is administered by the DOT's Federal Highway Administration (FHWA).[27]

ISTEA, TEA-21, and SAFETEA-LU

Since 1982, Congress has funded transportation programs through multi-year legislation in order to help insulate transportation projects, which tend to be long-term, from the uncertainties of annual appropriations debates. Three pieces of multi-year legislation, primarily funded by the HTF, have directed federal transportation funds to states since 1991:

- **ISTEA.** The Intermodal Surface Transportation Efficiency Act of 1991 (ISTEA) increased funding for transportation programs, provided greater flexibility, and gave greater authority to state, regional, and local governments. Under ISTEA, California received nearly $10 billion in federal transportation funds between 1992 and 1997, about 9 percent of total FAHP funds. The state received $3.1 billion in transit assistance (13.9 percent of total federal transit funds). ISTEA expired on September 30, 1997, but was extended until new legislation was passed the following year.

- **TEA-21.** The Transportation Equity Act for the 21st Century (TEA-21), enacted in June 1998, increased federal transportation funding by 40 percent over ISTEA levels. Under TEA-21, California received $14.4 billion in FAHP funds between 1998 and 2003, about 9 percent of total FAHP funds. California's share of transit monies was much higher, about 15 percent ($3.8 billion) of total TEA-21 transit funds between 1998 and 2003. Under TEA-21, the DOT distributed federal funds by formula to states each year through nine programs. TEA-21 provided states authority to transfer up to 50 percent of a state's apportionment for one program into any of the other programs.[28]

- **SAFETEA-LU.** TEA-21 expired on September 30, 2003, but Congress extended its provisions for nearly two years. On August 10, 2005, President Bush signed the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU). California will receive an estimated $23.4 billion in transportation funds through 2009, a 40 percent increase in average annual funding over TEA-21 levels. Of this amount, $18 billion is targeted for highways, $5 billion for transit, and $452 million for transportation safety. In what the LAO calls a "mixed blessing," $3.7 billion (16 percent) of California's total share of funds is earmarked

for specific projects. Not only does the state have limited authority to transfer these funds to other projects that it might consider a higher priority, such as projects already included in the TRCP, but in addition the earmarked amounts generally do not cover full project costs – meaning the state and local governments will need to provide matching funds in order to draw down federal funds and complete these projects.[29]

Does California Get Its Fair Share of Federal Highway Dollars?

The DOT collects fuel and excise tax revenues and distributes the funds from the HTF in the form of grants to state, regional, and local entities through funding formulas known as apportionments. These apportionments are based on factors such as population, highway lane miles, congestion, and air quality. For years, many states – including California – have argued that apportionments caused them to pay more into the HTF than they received back. In response to these concerns, Congress created a minimum funding guarantee in TEA-21. The minimum guarantee ensured that each state received at least 90.5 percent of the funds back on program funding contributed to the HTF Highway Account (this will increase to 92.0 percent by 2009 under SAFETEA-LU).[30]

While California accounted for about 12 percent of the nation's population, it received only about 9 percent of the total federal highway apportionment dollars under TEA-21. In fact, California's share declined from 9.2 percent in 1998 to 9.0 percent in 2002. While some formulas benefit California, such as those that weight vehicle usage more heavily, the three largest federal highway programs – the Surface Transportation Program, National Highway System, and Interstate Maintenance Program – use formulas that are less favorable to California. However, California did receive more mass transit funds under both ISTEA and TEA-21 than any other state due to its high population density in urban areas and the fact that four of the largest transit systems in the country are located in California.[31]

How Do Local Governments Fund Transportation?

Counties and cities receive a share of state funding from state motor vehicle fuel taxes, as well as from federal transportation grants. Other revenue sources include local general funds, bond proceeds, and fines and forfeitures. The primary revenue sources for transportation include a one-quarter cent sales tax rate and optional voter-approved sales tax rates.

- **Uniform Local Sales Taxes.** Local jurisdictions receive funds from a local sales tax rate, established by the Transportation Development Act of 1971. All California cities and counties levy a 1.25 percent sales tax rate, of which 0.25 percent goes to transportation in the county where the sale occurred.[32] This tax is expected to generate $1.5 billion in 2006-07.[34]

- **Voter-Approved Local Sales Tax Rates.** Local-option sales taxes, some of which are earmarked for various purposes including transportation, are generally imposed in quarter-cent or half-cent increments. Eighteen counties, accounting for most of the state's population, currently have local-option sales taxes that fund transportation programs, operating costs, and agencies. Voter-approved local sales tax rates accounted for an estimated $3.0 billion in 2004-05.[35]

The state Constitution requires voters to approve any new local tax, an increase of an existing tax, or the extension of a local tax that will expire. Taxes dedicated to a specific purpose,

What Are "GARVEE" Bonds?

Grant Anticipation Revenue Vehicles, commonly referred to as GARVEE bonds, are intended to accelerate funding for state transportation infrastructure projects. GARVEE bonds are tax-exempt anticipation notes backed by annual federal transportation appropriations. In other words, GARVEE bonds allow the state to borrow against future federal funding.

- **How does the financing work?** The National Highway System Designation Act of 1995 expanded the types of bond-related costs that states could finance with federal funds. The Act allowed states to begin using a portion of federal highway funds for debt financing, rather than solely for repayment of principal on bonds. TEA-21, enacted in 1998, provided states with a minimum guarantee of federal transportation funding, significantly reducing the risk of borrowing against future federal funds. In California, GARVEE bonds are issued by the state Treasurer and financing is structured so that anticipated federal transportation funding will cover debt service payments.

- **Where does the money go?** GARVEE proceeds fund a variety of transportation projects, including toll bridge seismic retrofit and STIP, SHOPP, and TCRP projects. Bond proceeds can only be used to cover the federally-funded portion of a project (usually 88.5 percent of total project costs); the state must provide the remainder as matching funds on a pay-as-you-go basis.

- **How much money is involved?** The CTC approved the state's first GARVEE bonds in January 2004 to finance eight STIP projects. In March 2004, the Treasurer issued $614.9 million in GARVEE bonds. Due to the uncertainty of state transportation funding in recent years, the state has suspended future GARVEE financing.[33]

Is High-Speed Rail in California's Future?

In the early 1990s, pursuant to SCR 6 (Kopp, Resolution Chapter 56 of 1993), the Governor created a High-Speed Rail Commission. SCR 6 directed the Commission to create a 20-year high-speed rail plan for California and submit it to the Legislature. The Commission submitted a draft report in December 1996. Building on the Commission's work, SB 1420 (Kopp, Chapter 796 of 1996) created a High-Speed Rail Authority (HSRA). The HSRA was tasked with planning, designing, constructing, and operating a state-of-the-art high-speed train system. Since the HSRA's work was not yet complete by 2000, it was extended by subsequent legislation, and made permanent in 2002. In 2005, the HSRA completed its final environmental analysis for a 700-mile-long high-speed train system, capable of speeds up to 220 miles per hour, which could carry up to 68 million passengers per year by 2020. According to the HSRA, once it receives adequate funding, it can move forward in developing and launching operation of the initial segment of the high-speed train, estimated to take eight to 11 years.

Funding, however, has been repeatedly delayed. In 2002, SB 1856 (Costa, Chapter 697 of 2002) provided for the sale of $9.95 billion in general obligation bonds, of which $9 billion was designated for the planning and construction of a high-speed rail system connecting California's major metropolitan areas, upon voter approval in the November 2004 election. In 2004, SB 1169 (Murray, Chapter 71 of 2004) delayed the vote to November 2006. In June 2006, AB 713 (Torrico, Chapter 44 of 2006) postponed the vote to 2008; according to the author, "the state's ongoing budget deficits and precarious financial condition have diminished its ability to undertake …long-term and costly transportation projects."[36]

such as transportation, must be approved by a two-thirds vote. Proposition 218 of 1996 amended the state Constitution to enact the current restrictions on the taxing powers of local governments.

How Has the State's Budget Crisis Affected Transportation Funding?

Proposition 42 and Spillover Funds Temporarily Held in the General Fund

In order to help address the state's budget shortfall, state budget agreements between 2001-02 and 2004-05 included loans from transportation funds to the General Fund, as well as deferrals, suspensions, and reductions of annual transfers from the General Fund to the TCRP. Some of these loans were scheduled to be repaid through $1.2 billion in state-issued bonds backed by tribal gaming revenues. Issuance of the bonds has been delayed, however, by ongoing renegotiation of tribal gaming compacts and pending litigation.[37]

The PTA receives additional "spillover" revenues from the General Fund when sales tax revenues from gasoline and diesel fuels are relatively high compared to sales tax revenues from all other goods. Rising gasoline and diesel fuel prices in recent years increased the amount of spillover revenues. The Governor and Legislature took advantage of this surplus to allocate roughly $600 million in spillover revenues from 2003-04 through 2005-06 into the General Fund to help balance the budget.[38] The 2006-07 budget agreement allocates about half of the estimated $668 million in spillover revenues to non-transit purposes.[39]

Other Revenue Sources Have Declined

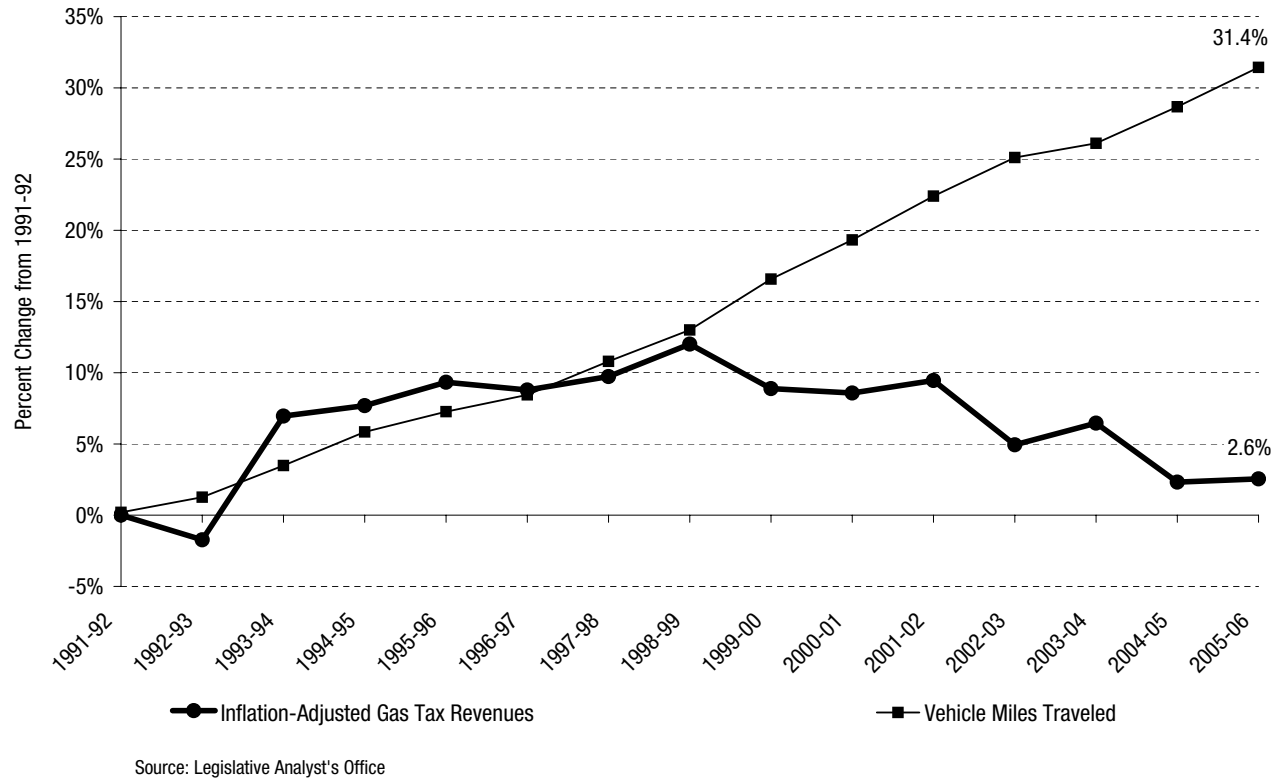
A number of other factors have also reduced transportation revenues in recent years:

- **Truck weight fees.** In 2000, then Governor Davis signed legislation to change how truck weight fees were imposed.[40] This change was intended to be revenue neutral – not intended to either increase or decrease revenue collections. However, 2002-03 revenues were $124 million lower than anticipated as a result of the change. To address this problem, legislation was signed in 2003 to increase truck weight fees as of January 1, 2004.[41] In the meantime, however, a total of $223 million in revenues were lost that would otherwise have gone to transportation.

- **Federal gas tax receipts.** The state's conversion from gasoline blended with methyl-tert-butyl-ether (MTBE) to ethanol-blended gasoline caused a one-time loss in federal gas tax receipts.[42] Since ethanol-blended fuel was taxed at a lower rate than non-ethanol-blended fuel, the conversion resulted in an estimated loss of about $560 million in federal gas tax revenues in 2005-06. Recent federal legislation, however, adjusted the rate on ethanol-blended fuel to make it equal to that of non-ethanol-blended fuel, thereby increasing federal gas tax receipts to the state again.[43]

- **Gas tax revenues.** In addition, revenues derived from the state excise tax on gasoline and diesel fuels have not increased proportionately to the number of miles traveled on California's roads. As the gas tax increased from 9 cents per gallon to 18 cents per gallon during the early 1990s, inflation-adjusted gas tax revenues generally kept pace with vehicle miles traveled (Figure 5). From 1998-99 to 2006-07, however, inflation-adjusted gas tax revenues are projected to decline 8 percent, as compared to a 16 percent increase in vehicle miles traveled.[44] Since gas tax revenues have not kept up with inflation, fewer transportation projects have been funded through the gas tax, despite the fact that travel has increased.

Figure 5: Gas Tax Revenues Are Not Keeping Pace with Travel



Source: Legislative Analyst's Office

Where Are We Now?

The 2006-07 budget agreement provides full funding for Proposition 42 ($1.4 billion) in 2006-07, as well as prepaying $1.4 billion in outstanding Proposition 42 loans that are due in 2007-08 and 2008-09.

California voters will consider two transportation-related measures in November 2006:

- **Proposition 42 Lock-In.** The public works package approved by the Legislature in May included SCA 7 (Torlakson, Resolution Chapter 49 of 2006), a constitutional amendment limiting the circumstances under which Proposition 42 can be suspended. SCA 7 will appear on the November 2006 ballot as Proposition 1A. Similar provisions were contained in Proposition 76, the California Live Within Our Means Act, which was defeated by the voters in November 2005.
- **Transportation Bond.** Proposition 1B, the Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006, authorizes $19.9 billion in GO bonds for transportation. The Legislature passed this measure in the form of SB 1266 (Perata, Chapter 25 of 2006) as part of a comprehensive public works package. From 1972 to the present, voters have approved only two of the five transportation GO bond measures that have been placed on the ballot.[45]

Erin Riches and Adrienne Fernandes prepared this Budget Backgrounder. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the CBP is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP's website at www.cbp.org.

Appendix A: Who Are the Major Players in Transportation Policy?

Federal

- **The US Department of Transportation (DOT)** is responsible for administering policies and programs to protect and enhance the safety, adequacy, and efficiency of the nation's transportation system and services. The DOT was created by federal legislation in 1966.
- **The Federal Highway Administration (FHWA) and Federal Transit Administration (FTA),** two divisions within the DOT, administer federal highway and transit funds.

State

- **The California Legislature** appropriates money to fund transportation projects and programs. The Legislature has delegated to other state and regional players the authority to select specific transportation projects.
- **The California Department of Transportation (CalTrans)** is responsible for operating and maintaining the state highway system, as well as planning and designing related capital improvement projects. CalTrans was created by state legislation in 1972, consolidating the Department of Public Works and Aeronautics.
- **The California High-Speed Rail Authority (HSRA)** oversees planning and construction of an intercity high-speed rail system. The HSRA was created by legislation in 1996 as an independent authority with nine board members appointed by the Governor and Legislature.
- **The California Transportation Commission (CTC),** made up of nine members appointed by the Governor, advises the state on transportation projects and is responsible for allocating state and federal funds to transportation projects throughout the state. The CTC was created in 1978, replacing the California Highway Commission, the State Transportation Board, the Aeronautics Board, and the California Toll Bridge Authority.

Regional

- **The state's 26 Regional Transportation Planning Agencies (RTPAs)** are created by special legislation, councils of governments (COGs), local associations of government, and local transportation commissions. The first RTPAs were created by the Transportation Development Act in 1971. RTPAs administer state funds, allocate federal and local funds, and select projects for the Regional Transportation Improvement Program in the STIP.
- **The state's 18 Metropolitan Planning Organizations (MPOs)** are federally required planning bodies, designated by the Governor, that provide transportation planning for each urbanized area with a population of over 50,000. These organizations are typically the same as an urban region's RTPA (for example, the Metropolitan Transportation Commission is both the RTPA and MPO for the Bay Area). MPOs outline their transportation priorities in a 20-year Regional Transportation Plan.

Local

- **Cities and counties** adopt land use and growth policies and nominate transportation projects for funding by their local RTPA.
- **Transit agencies,** such as Bay Area Rapid Transit (BART), nominate transportation projects for funding by RTPAs and deliver transportation services.[46]

Appendix B: A Transportation Glossary

The following list identifies the transportation-related acronyms and initiatives referenced in this report.

Federal

DOT	US Department of Transportation
FAHP	Federal-Aid Highway Program
FHWA	Federal Highway Administration (part of the DOT)
FTA	Federal Transit Administration (part of the DOT)
GARVEE	Grant Anticipation Revenue Vehicle (otherwise known as "GARVEE bonds")
HTF	Highway Trust Fund
ISTEA	Intermodal Surface Transportation Efficiency Act of 1991
MTA	Mass Transit Account (part of the HTF)
SAFETEA-LU	Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (2005)
TEA-21	Transportation Equity Act for the 21st Century (1998)

State

CalTrans	California Department of Transportation
CTC	California Transportation Commission
HSRA	California High-Speed Rail Authority
PTA	Public Transportation Account
SHA	State Highway Account
SHOPP	State Highway Operation and Protection Program
STIP	State Transportation Improvement Program
TCRA	Traffic Congestion Relief Act
TCRF	Traffic Congestion Relief Fund
TCRP	Traffic Congestion Relief Plan/Program
TIF	Transportation Investment Fund

Regional

MPO	Metropolitan Planning Organization
RTPA	Regional Transportation Planning Agency

State Ballot Initiatives

Proposition 42	Transportation Congestion Improvement Act (2002)
Proposition 108	Passenger Rail and Clean Air Bond Act of 1990
Proposition 111	Traffic Congestion Relief and Spending Limitation Act (1990)
Proposition 116	Clean Air and Transportation Improvement Act of 1990
Proposition 192	Seismic Retrofit Bond Act of 1996
Proposition 218	Voter Approval for Local Government Taxes. Limitations on Fees, Assessments, and Charges. (1996)
Proposition 1A	Transportation Funding Protection (2006)
Proposition 1B	Highway Safety, Traffic Reduction, Air Quality, and Port Security Bond Act of 2006

ENDNOTES

[1] Appendix A provides a brief description of the major public entities in transportation policy at the federal, state, regional, and local levels. Appendix B provides a glossary of acronyms used in this report.

[2] Ellen Hanak and Mark Baldassare, eds., *California 2025: Taking on the Future* (Public Policy Institute of California: 2005), pp. 160-161.

[3] California Government Code, Section 14550(c).

[4] California Transportation Commission, *Transportation Funding Shortfall* (August 6, 2004), downloaded from http://www.catc.ca.gov/ on June 29, 2005.

[5] Legislative Analyst's Office, *Analysis of the 2004-05 Budget Bill* (February 2004), pp. A-58 through A-59.

[6] Legislative Analyst's Office, *Analysis of the 2006-07 Budget Bill* (February 2006), p. A-47.

[7] Department of Finance, *Governor's Budget Summary 2006-07*, pp. 39-40 and California State Legislature, *Revenue and Taxation Reference Book 2005* (February 2006), p. 109.

[8] Legislative Analyst's Office, *California Travels: Financing Our Transportation* (May 2000), pp. 38-44 and pp. 62-64 and California Transportation Commission, *Overview of Transportation Programming in California* (April 2003), downloaded from http://www.catc.ca.gov/mission.htm on July 18, 2006.

[9] California Constitution, Article XIX, Section I and Legislative Analyst's Office, *California Travels: Financing Our Transportation* (May 2000), p. 21.

[10] Department of Finance, *Governor's Budget Summary 2006-07*, p. 220.

[11] Personal communication with Anne Maitland, Department of Finance (June 6, 2006) and California State Legislature, *Revenue and Taxation Reference Book 2005* (February 2006), p. 82.

[12] Legislative Analyst's Office, *Public Transportation Account: Options to Address Projected Shortfall* (January 4, 2000), pp. 3-4.

[13] Personal communication with Anne Maitland, Department of Finance (June 6, 2006).

[14] The state sales tax rate when Proposition 111 was passed was 4.75 percent.

[15] Personal communication with Anne Maitland, Department of Finance (June 6, 2006) and Legislative Analyst's Office, *Public Transportation Account: Options to Address Projected Shortfall* (January 4, 2000), pp. 3-4.

[16] The tax and fee increases were contained in legislation passed in 1989. The increases were contingent upon passage of Proposition 111, which appeared on the ballot in June 1990.

[17] Full text of Propositions 111 and 108, downloaded from Hastings Law Library, University of California, Hastings College of the Law at http://holmes.uchastings.edu/cgi-bin/starfinder/0?path=calprop.txt&id=webber&pass=webber&OK=OK on July 21, 2005. Also see California Budget Project, *School Finance in California and the Proposition 98 Guarantee* (April 2006).

[18] Legislative Analyst's Office, *Overview of the 2006-07 May Revision* (May 15, 2006), pp. 15-16 and full text of initiatives, downloaded from Hastings Law Library, University of California, Hastings College of the Law at http://holmes.uchastings.edu/cgi-bin/starfinder/0?path=calprop.txt&id=webber&pass=webber&OK=OK on November 29, 2005.

[19] California Budget Project, *A Mini-Primer on Bonds* (February 2006).

[20] AB 2928 (Torlakson, Chapter 91 of 2000) and SB 406 (Ortiz, Chapter 92 of 2000).

[21] Legislative Analyst's Office, *California Spending Plan 2000-01* (August 2000), pp. 46-47.

[22] ACA 4 (Dutra, Resolution Chapter 87, 2001).

[23] Also see California Budget Project, *Proposition 1A of 2006: What Would Be the Impact of "Locking In" the Proposition 42 Transfer?* (August 2006).

[24] Full text of Proposition 42, downloaded from Hastings Law Library, University of California, Hastings College of the Law at http://holmes.uchastings.edu/cgi-bin/starfinder/0?path=calprop.txt&id=webber&pass=webber&OK=OK on October 13, 2005; California Transportation Commission, *2005 Annual Report to the California Legislature* (Adopted December 15, 2005), pp. 9-12; Legislative Analyst's Office, *California Spending Plan 2000-01* (August 2000), pp. 46-47; and Legislative Analyst's Office, *California Spending Plan 2001-02* (September 2001), p. 43.

[25] Transportation spending includes the California Transportation Commission, Special Transportation Programs, the Department of Transportation (CalTrans), and the High-Speed Rail Authority. California Highway Patrol (CHP) and the Department of Motor Vehicles (DMV) are not included because these departments' expenditures are primarily for public safety and driver regulation rather than transportation. CBP analysis of Legislative Analyst's Office data.

[26] CBP analysis of Legislative Analyst's Office data and California Budget Project, *What Would Be the Impact of "Locking In" the Proposition 42 Transfer?* (May 2006).

[27] Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Highway Programs* (Public Policy Institute of California: 2003), pp. 5-6; US Department of Transportation, *Financing Federal-Aid Highways*, downloaded from http://www.fhwa.dot.gov/reports/fifahiwy/fifahi05.htm on June 20, 2005; Federal Highway Administration, Office of Policy Development, *Primer: Highway Trust Fund* (November 1998), p. 3; and Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Transit Assistance Programs* (Public Policy Institute of California: 2004), pp. 2 and 4.

[28] Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Highway Programs* (Public Policy Institute of California: 2003) pp. 4 and 8; Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Transit Assistance Programs* (Public Policy Institute of California: 2004), pp. 8-9; California Institute for Federal Policy Research, *California Capitol Hill Bulletin* (Volume 4, Bulletin 29, September 4, 1997); American Public Transportation Association, *TEA 21 Transit Funding Provisions: An APTA Primer on Transit Funding Provisions of the Transportation Equity Act for the 21st Century and Related Laws* (updated January 2005), p. 4; and California Institute for Federal Policy Research, "California Share of Federal-Aid Highway Programs, FY 1998-2003" (revised March 2004), downloaded from http://www.calinst.org/datapages/TEA21-hwy.htm on June 28, 2005.

[29] Federal Funds Information for States, *Issue Brief 05-32: Federal-Aid Highway Reauthorization Finally Enacted* (August 15, 2005) and Legislative Analyst's Office, *Funding for Transportation: What the New Federal Act Means for California* (January 19, 2006).

[30] Federal Funds Information for States, *Issue Brief 05-32: Federal-Aid Highway Reauthorization Finally Enacted* (August 15, 2005), p. 3.

[31] Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Highway Programs* (Public Policy Institute of California: 2003), pp. 1-30; Tim Ransdell and Shervin Boloorian, *Federal Formula Grants and California: Federal Transit Assistance Programs* (Public Policy Institute of California: 2004), pp. 3-5; and Public Policy Institute of California, *Just the Facts: California's Share of Federal Highway Funds* (February 2003).

[32] Propositions 57 and 58, approved by voters in March 2004, authorized the state to sell "Economic Recovery Bonds" in order to finance a portion of the state's budget shortfall. These bonds are backed by revenues from a one-quarter cent dedicated sales tax rate beginning July 1, 2004. Cities' and counties' sales tax rates were reduced by the same amount. In return, cities and counties received an equivalent increase in property tax revenues, and schools' share of property tax revenues was

reduced on a dollar-for-dollar basis. This transaction – called the "triple flip" – will remain in place until the economic recovery bonds are repaid, estimated to be between nine and 14 years.

[33] California Government Code, Sections 14550 through 14555.9; State Treasurer Philip Angelides, *Analyses of GARVEE Bonding Capacity 2005* (April 2005), pp. ii and 7; California Transportation Commission, *2004 Annual Report to the California Legislature* (adopted December 9, 2004), p. 28; California Transportation Commission, *2005 Annual Report to the California Legislature* (adopted December 15, 2005), p. 99; and Legislative Analyst's Office, *Grant Anticipation Revenue Vehicles: An Option to Finance Transportation Projects* (August 1999).

[34] California Department of Transportation, Division of Mass Transportation, *Transportation Development Act: Statutes and California Codes of Regulations* (January 2005), pp. 1-5, downloaded from http://www.dot.ca.gov/hq/MassTrans/tdao.htm on December 7, 2005 and Legislative Analyst's Office, *State of California Revenues, 1950-01 to 2006-07* (updated June 2006), downloaded from http://www.lao.ca.gov/LAOMenus/lao_menu_economics.aspx on August 15, 2006.

[35] These counties include Alameda, Contra Costa, Fresno, Imperial, Los Angeles, Marin, Orange, Riverside, Sacramento, San Bernardino, San Diego, San Francisco, San Joaquin, San Mateo, Santa Barbara, Santa Clara, Santa Cruz, and Sonoma. Madera County's tax expired in 2005. Santa Cruz County also has a permanent sales tax that supports transit operations, but not transportation construction programs. "Self Help Counties Measure Election Results," downloaded from http://selfhelpcounties.org/ on July 18, 2006; personal communication with Self-Help Counties Coalition (November 28, 2005); and State Board of Equalization, *2004-05 Annual Report* (June 2006), Table 21c.

[36] Text and legislative analyses of SCR 6 (Kopp, Resolution Chapter 56 of 1993), SB 1420 (Kopp, Chapter 796 of 1996), AB 1703 (Florez, Chapter 791 of 2000), SB 796 (Costa, Chapter 696 of 2002), SB 1856 (Costa, Chapter 697 of 2002), SB 1169 (Murray, Chapter 71 of 2004), and AB 713 (Torrico, Chapter 44 of 2006); and California High-Speed Rail Authority, *Fly California: A Blueprint for Building California's High-Speed Train*, downloaded from http://www.cahighspeedrail.ca.gov/ on April 27, 2006.

[37] Legislative Analyst's Office, *California Spending Plan 2002-03* (September 2002), p. 58; Legislative Analyst's Office, *California Spending Plan 2003-04* (October 2003), pp. 52-53; Legislative Analyst's Office, *California Spending Plan 2004-05* (September 2004), p. 59; and Legislative Analyst's Office, *California Spending Plan 2005-06* (September 2005), pp. 49-50.

[38] Legislative Analyst's Office, *California Spending Plan 2003-04* (October 2003), p. 53; *California Spending Plan 2004-05* (September 2004), p. 59; *California Spending Plan 2005-06* (September 2005), p. 51; and Legislative Analyst's Office, *Analysis of the 2006-07 Budget Bill* (February 2006), p. A-23.

[39] Legislative Analyst's Office, *Major Features of the 2006 California Budget* (July 2006), p. 25.

[40] SB 2084 (Polanco, Chapter 861 of 2000).

[41] SB 1055 (Senate Committee on Budget and Fiscal Review, Chapter 719 of 2003).

[42] MTBE was certified in 1979 by the US Environmental Protection Agency to help gasoline burn more cleanly and as an anti-knock compound. In response to rising public concern about possible groundwater contamination resulting from MTBE, then Governor Gray Davis issued an Executive Order in 1999 declaring that MTBE presented an environmental risk to Californians and directing state agencies to take steps to eliminate the use of MTBE in California gasoline by December 31, 2002. California Air Resources Board, *Cleaner-Burning Gasoline Without MTBE* (updated August 9, 2004), downloaded from http://www.arb.ca.gov/fuels/gasoline/cbgmtbe.htm on August 24, 2006.

[43] Legislative Analyst's Office, *The 2005-06 Budget: Perspectives and Issues* (February 2005), pp. 179-181.

[44] Legislative Analyst's Office, *Analysis of the 2006-07 Budget Bill* (February 2006), pp. A-30 through A-31 and data obtained through personal communication with Legislative Analyst's Office (June 24, 2005).

[45] Department of Finance, *Chart K-9: General Obligation Bond Proposals by Program Areas, 1972 to Present* (January 2006), downloaded from http://www.dof.ca.gov/Budget/BudgetFAQs.asp#10%20on%202/15/06 on August 17, 2006.

[46] US Department of Transportation, *The United States Department of Transportation: A Brief History*, downloaded from http://dotlibrary.dot.gov/Historian/historian.htm on November 30, 2005; US Department of Transportation, *DOT Organizations*, downloaded from http://www.dot.gov/summary.htm on November 30, 2005; Legislative Analyst's Office, *California Travels: Financing Our Transportation* (May 2000), pp. 38-39; California Department of Transportation, "Fact Sheet: Important Events in CalTrans History," downloaded from http://www.dot.ca.gov/hq/paffairs/about/cthist.htm on December 28, 2005; Legislative Analyst's Office, *Analysis of the 2006-07 Budget Bill* (February 2006), p. A-50; California Department of Transportation, "MPOs & RTPAs Contact List" (updated January 10, 2006), downloaded from http://www.dot.ca.gov/hq/tpp/ on July 19, 2006; and Paul G. Lewis and Mary Sprague, *Federal Transportation Policy and the Role of Metropolitan Planning Organizations in California* (April 1997), p. 21.