

Initiatives in Transportation Funding & Finance

Report and Recommendations

to

Sunne Wright McPeak
Secretary
Business, Transportation and Housing Agency
State of California

March 17, 2004

**Keston Institute for Infrastructure
University of Southern California**

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Executive Summary

Like most states, California is in a budget crisis. We are struggling to supply urgently needed services with diminishing revenues. As in many states, California's transportation funds are being cut to fund other needs. Across the country, fiscal year 2003 was the third straight year states faced budget shortfalls, with a cumulative gap of \$200 billion.

In the last three California budget cycles, transportation funding has been used to augment the General Fund. The Governor's mid-year and budget year (FY 2004-05) proposals continue that tradition by including \$2 billion – in addition to the billions previously "borrowed" or diverted from transportation accounts – in transfers and loans from transportation funds to address the ongoing budget deficit. Not only are these funds coming from sources specifically designated for transportation projects, but also from a source that recently received overwhelming voter support statewide (Proposition 42).

By continuing to divert these limited transportation funds to address our General Fund deficit problems, we risk delaying completion of many transportation projects critical to California's safety and mobility. Of equal importance, we risk severe economic loss. Every \$1 billion invested in transportation infrastructure yields 47,500 jobs and millions of dollars of economic activity.¹ But, perhaps even more important, we risk breaking promises to Californians who voted to direct their tax dollars to fund real transportation projects. California had a transportation system that once was considered the finest in the nation. If we act now, we can restore and perpetuate that legacy.

What action should we take? That question was addressed by a panel of transportation, finance and public policy professionals, which convened March 17, 2004, for a daylong discussion on the "state of transportation funding" in California. Held at the University of Southern California's Keston Institute for Infrastructure, the panel was convened at the request of California's Business, Transportation and Housing Secretary Sunne Wright McPeak. Its purpose was to evaluate what transportation funding and delivery initiatives could be

¹ Mary Peters, FHWA Administrator, January 13, 2003

undertaken immediately as part of this year's budget proposal and to recommend longer-term actions to address California's transportation funding and delivery problems.

The panel recommends the following principles in addressing these issues:

- ✓ Do no harm to the Governor's proposed budget.
- ✓ Commit to protecting California's transportation funding, beginning with the May Revise.
- ✓ Articulate a vision of transportation certainty, stability and continuity in the 2005 State of the State address.
- ✓ Provide a specific agenda of actions and reforms, including proposed legislation, as part of the FY 2005-2006 budget submittal.

With California squeezed by a suffering budget and a desperate need for transportation improvements, the panel set out to find a fiscally prudent yet entrepreneurial approach to transportation funding and financing. By including panel members from all levels of government, from other states, from the worlds of finance and project delivery, this group was able to craft a set of recommendations that are realistic, innovative and can immediately be put into action.

The recommendations are further explored in the following pages, but can be summarized here as:

1. *De-link the state's General Fund from the state transportation fund.* Begin the process of reform by pledging that this is the last year of diverting Proposition 42 revenue.
2. *Pursue "Hold Harmless", "Revenue Neutral" strategies to tapping transportation funds for General Fund deficit reduction.* Should additional transportation funds be identified over and above funds already identified in the proposed budget (such as an increase in Proposition 42 receipts due to high gas prices), these funds should be kept for transportation purposes.
3. *Revise the Administration's proposal to convert federal funding for local projects from accrual to cash and transfer the cash to the General Fund.* Leveraging these dollars for transportation is good policy; leveraging these funds to pay previously approved bond debt is not good policy, is a dangerous precedent, and hurts transportation.
4. *Explore refinancing of existing General Fund transportation debt.* Given today's interest rates, can Proposition 108, 116 and 192 debts be refinanced at a savings? If so, the incremental savings should go to transportation.
5. *Seek to monetize State Transportation assets and other facilities to fund transportation improvements.* Proceeds from the sale and/or lease of state assets, particularly transportation facilities and buildings, could be deposited in the State Infrastructure Bank and leveraged to provide badly needed funding for transportation projects.
6. *Amend Caltrans' workload reduction plan in current and budget years to provide for contracting out.* With the pent-up demand for projects, experienced construction and engineering staffing are needed to keep these projects moving and ready them for construction; otherwise California won't be ready-to-go when funds become available. Given the amount of savings involved, there is an opportunity to keep projects moving both through Caltrans and contract resources.

7. *Monitor and prepare for the infusion of funding resources from the federal change in how ethanol in gasoline is taxed.* New tax provisions could mean as much as \$400 million per year in increased federal transportation returns to California. These funds must be for transportation only and we must be ready to use them.
8. *Initiate a serious dialogue between the Administration and the state's transportation community on how to attract private funds to transportation improvements.* States across the country are leveraging their transportation funds, welcoming private investment in their transportation infrastructure programs, eliminating backlogs, and moving forward. California can and should do the same.
9. *Support Federal Initiatives for Goods Movement and other Mega Projects.* Reauthorization of federal surface transportation legislation is imminent. California potentially stands to gain hundreds of millions in benefit under two new tax incentives in the Senate version of reauthorization. Support the issuance of Federal tax credit bonds by the Build America Corporation, and support provisions for \$15 billion in private activity bonds for highway and intermodal projects.
10. *Enhance accountability for project and policy outcomes.* It is not enough to report quarterly that a project is "underway". Measurable criteria regarding a clear set of deliverables is the very least expected by a public that has approved transportation relief and now looks for urgently needed progress.

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Report and Recommendations

I. Background

California's transportation infrastructure is a legacy our grandparents left to us here in the Golden State. Because of their investment foresight, California more than 40 years ago embarked upon a major, statewide infrastructure investment program. This effort, articulated and led by California's then-Governor Pat Brown, focused on providing "the best of the best": the nation's best higher education system; the best water delivery system; and the best roads and transportation system in the country. In short, infrastructure was seen as the key to a vibrant economy, a good quality of life, and improved opportunities for all people. To a very large extent, we have grown and prospered on that investment.

Just like California's leaders of four decades ago, the state's leaders today have the opportunity to create a vision of California's transportation system of the future and to develop and implement a plan of action to achieve that vision. Given the projection that California's population will grow by 13 million residents by the year 2020, leadership like that of decades ago is needed to fulfill this vision once again.

Although action is urgently needed to address the state's chronic transportation problems, any "quick fix" cannot be done in a vacuum. Even short-term solutions and approaches must be structured within the context of a long-term commitment to improved transportation infrastructure delivery, funding and innovation. This is necessary to provide California with current and future mobility for both people and goods that will ensure a strong economy, a good quality of life, and opportunity for all Californians. Is this not the California to which we were attracted, and which we wish to leave to our children?

On March 17, 2004, a panel of transportation, finance and public policy professionals assembled for a daylong discussion on the "state of transportation funding" in California (see Appendix A for list of participants). Held at the University of Southern California's Keston Institute for Infrastructure, the panel was convened at the request of California's Business Transportation and Housing Secretary Sunne Wright McPeak. She directed the panel to evaluate what transportation funding and delivery initiatives could be undertaken immediately as

part of this year's budget proposal and to recommend longer-term actions for addressing California's structural problems in transportation funding and delivery.

A clear consensus on our panel of professionals relating to general operating principles emerged from this day of intense discussion and brainstorming, as follows:

- ✓ California's transportation crisis is the result of several factors:
 - Financing strategy is not adequately linked to demand;
 - Current funding sources lack predictability and long-term growth potential.
- ✓ The problem is systemic, structural and historic and cannot be remedied through one-time "fixes".
- ✓ Short-term recommendations are offered with the understanding that there needs to be a sustained longer-term commitment to improve certainty for transportation infrastructure funding and delivery in California, led by the Governor.
- ✓ The key to long-term certainty in transportation funding is to de-link it from the General Fund.
- ✓ Transportation investment policy should be focused on mobility, not modes..

These general principles provide a foundation for beginning to build a new transportation imperative in California. Other states have faced and solved similar problems.

II. The Tale of Two States – 1998 to Present

Given the situation in which transportation funding and delivery in California presently exists, it is instructive to draw upon examples of structural transportation funding and delivery problems in other states in order to:

- ✓ Compare the nature of the problem faced by others.
- ✓ Understand the principles others applied in developing solutions.
- ✓ Evaluate the effectiveness of these solutions for California.

The panel was most fortunate in having as one of its members State Representative Mike Krusee from Texas. Representative Krusee provided an historical and practical perspective on Texas' experience over the past five years. The approaches being successfully applied in Texas may be instructive to California policymakers in addressing the similarly pressing problems in the Golden State.

A. California

In 1998, the Legislature directed the California Department of Transportation ("Caltrans") and the California Transportation Commission ("CTC") to develop a detailed inventory of California's transportation infrastructure needs for the coming decade, from maintenance of the existing system to new mobility projects, and from regional to statewide projects. Additionally, the Legislature directed that both Caltrans and the CTC identify all funding available to meet these needs including existing and anticipated federal, state and regional funds. In response, the CTC submitted a report to the Legislature that demonstrated that California required a total of \$110 billion over the next decade (1998-2008) to fund new transportation projects as well as maintenance; however, existing and anticipated funding of only \$35 billion was available to address these needs.

In 1999, the Governor and Legislature provided a one-time infusion of over \$6 billion in General Fund monies to transportation, but tied this funding to a list of specific projects. Additionally, the new funds only provided between 20% and 50% of the funding needed to implement each project. Although many of these projects were already represented on the CTC-prepared inventory, they were prioritized apart from the normal State Transportation Improvement Program (STIP) process. This resulted in the creation of a separate transportation program that, in effect, constituted a partially funded mandate. Furthermore, the Governor and Legislature were soon looking for ways to "borrow" back the \$6 billion due to the growing budget deficit within the General Fund.

Amidst growing statewide budget challenges, the voters in March 2002 overwhelmingly approved Proposition 42, which dedicated the state sales tax on gasoline to both statewide and local transportation needs. Proposition 42 initially generated an estimated \$1 billion annually in revenue, but this figure has increased as gasoline prices have escalated over the past two years. But before any funds from Proposition 42 could flow to California's transportation needs, these funds were "suspended" from being deposited into the transportation fund and were applied to defray the growing budget deficit.

With "live" projects underway, the CTC and Caltrans have had to scramble to try to find funding for projects in the pipeline. At present, a multitude of projects approved for construction by both regional agencies and Caltrans are in a queue, awaiting sufficient funding to begin construction. More than \$1 billion in projects are "ready to go" but unfunded.

Thus, in just the past five years, California's transportation infrastructure program – a program already determined to be under funded based upon the statewide needs assessment – has lost billions of dollars to the budget deficit, has suspended over a billion dollars worth of “ready to go” projects that mean jobs and economic development to California, and without correction, is poised to cancel billions more dollars in transportation projects needed throughout California.

In summary, the course that has been taken to address the larger statewide budget crisis is akin to over-farming a nutrient-rich plot of land, rapidly depleting the soil of its value, resulting in a barren patch of land that will lie fallow for years. This is not the model of success that is needed for a strong economy and good quality of life for all Californians.

B. Texas

“I have seen the future of highway finance and it works...At a time when many state DOT's are struggling to properly maintain their existing highway infrastructure, Texas is creating a whole new paradigm of how to finance, build, and operate major highways. While few states probably would or could do anything as audacious as Gov. Rick Perry's 4,000 miles of Trans-Texas Corridor, the state's other innovations should all be transferable.”

Robert W. Poole
PW Financing/February, 2004

Texas has also taken stock of its transportation infrastructure needs in the past several years. While California had identified roughly one-third of the financial resources available to meet its needs, Texas had only identified one-fourth of such resources.

While Texas' problem is similar in scope and scale to California's, its solution is different. Rather than infusing a one-time investment from its General Fund that, in times of economic uncertainty and/or crisis, gets taken back, Texas launched a complete restructuring of its transportation organizational and delivery context.

“With 30,000 people a month coming to the state and motorists traveling greater distances, it has become increasingly difficult for city, county and state officials to keep up with Texas' colossal transportation needs...the roadblock lies in the approval and funding stages. Project demand has greatly outstripped available funding, and as a result, unfunded projects often sit on the sidelines for years...until now.”

Drafting the Future (see Appendix B)
TxDOT

The loss of thousands of jobs in several areas of Texas due to congestion and lack of mobility led the state's leaders to look at transportation's critical importance to its economy. Based on federal studies that found that every \$1 billion invested in transportation yields 47,500 jobs and millions of dollars of economic activity, Texas leaders made a commitment to change their system of transportation project funding and delivery.

Governor Rick Perry, within his first months in office, led a statewide effort to address the transportation funding needed for backlogged projects and to empower state and local government and the private sector to implement mobility improvements more economically and faster.

In addressing its transportation challenges, Texas developed a theme: *We Are Open For Business!* That meant providing the legal, political and public policy framework to bring all potential available resources to the table in creating a menu of choices to fund and deliver projects. As a result, the state government as well as regional and local governments has billions of dollars worth of mobility projects and programs planned or underway throughout Texas (a summary of the authorizing legislation, HB 3588, is included in Appendix C).

In short, Texas created a comprehensive set of new tools to fund and finance projects, as well as accelerate and improve the efficiency of the delivery of projects. These include, but are not limited to:

- *Tolling* – Texas has commenced construction and/or is planning thousands of miles of toll facilities throughout the state. These improvements have both direct and indirect mobility benefits and leveraged capital benefits to Texas' transportation program.
- *Bonding authority* – Texans have approved a measure that allows the state to issue bonds secured with the State Highway Fund, in essence leveraging Texas gas tax and other tax revenue. The state plans to leverage up to \$3 billion in bond funds for transportation projects.
- *Texas Mobility Fund* – this fund derives a revenue stream from various transportation-related fees (e.g., driver's license fees) in order to secure bonds to leverage projects.
- *Regional Mobility Authorities* – new regional compacts that have the power to construct, maintain and operate transportation projects.

None of these changes happened in one budget year and none of them happened without leadership at the highest levels in Texas. Texas, like California, had historic structural issues that required more than a "quick fix". A clear vision for the future, coupled with a commitment to providing Texans with better mobility, a better economy and a better quality of life, provided the foundation for what today, by any measure, is overwhelming success in funding and delivering major mobility projects for the citizens of Texas.

III. The Overall Gameplan

The Keston panel clearly recognized that California's current budget crisis continues to adversely impact transportation funding and implementation. But within crisis lies opportunity. That begins with a commitment to reform transportation funding and delivery and reposition transportation infrastructure as a critical engine for both encouraging economic development and enhancing the quality of life.

Because of California's history of "feast and famine" in transportation funding, the panel believes it is imperative to begin to bring greater predictability and additional resources to our transportation infrastructure program in order to have any hope of meeting our mounting transportation safety and mobility needs.

While the panel focused on short-term solutions, all participants believe that these must be part of a longer-term, more permanent commitment of leadership and resources to stabilize and improve transportation funding and delivery. It is important to be mindful that transportation funding challenges have been cyclical in California. This is the pattern we must correct in the long-term.

As such, the lessons learned from Texas are not only instructive, but also encouraging. While it is clear that California has a unique set of issues, several of the general principles applied to the problems in Texas are applicable here:

1. *Current revenue models are inadequate to match the scope of the problem.* Texas added user fees, leveraged funds, and created more efficient delivery models for a synergy of success.
2. *Incremental "band-aids" won't provide long-term relief to our transportation problems.* We need leadership to call for a new commitment to transportation infrastructure including measurable criteria, increased local/regional and private partnership, and public accountability for results.
3. *The old model of funding and delivery will fail.* In Texas, a significant increase in public-private transportation partnerships is a core element of its solutions. We can do the same within our own California institutional and financial model.

Transportation funding, programming and project delivery in Texas has been completely overhauled and reinvented in the past several years. Without a holistic approach to both defining their problem and devising their solutions, Texas would not have the vast menu of options and opportunity that they have so expertly developed.

Based on the lessons of our neighbors and the severity of our problems, the panel suggested the following sequence of events related to an "action plan for California's transportation reform":

- ✓ Include the items recommended by the panel in the May Revision of the budget, including the administrative and policy directives proposed.
- ✓ Launch a major policy initiative after passage of the 2004-05 budget to reform transportation funding and delivery in California.

- ✓ Include transportation funding and delivery reform and improvement in the 2005 State of the State address and in the 2005-06 budget.

Within this context, the panel acknowledges that the current budget crisis is daunting and that transportation has to contribute its fair share to reduce the General Fund deficit. However, the panel strongly believes that steps can be taken now — beginning with this May Revise to the state budget — to conserve the state's transportation program, maintain a capital program that meets essential needs, and provide a modest job-creating economic stimulus.

The panel's immediate, short-term objective is to ensure no further degradation of the current program, which is significantly backlogged as it is. Thus, it is the panel's understanding that \$500 million per year over the next two years is needed to keep the program "whole". Therefore, to this end, the panel's specific recommendations for near-term actions follow — actions that the panel believes can generate between \$300 million and \$700 million for transportation. These recommendations must be considered as part of a long-term commitment of California's leadership to correct the instability and uncertainty in transportation infrastructure funding and delivery.

IV. What We Can Do Now - Recommendations

1. ***De-link the State's General Fund from the State Transportation Fund.*** Specifically, the panel recommends "fire walling" the Proposition 42 funds from legislative and administrative appropriation to subsidize General Fund deficits. The panel acknowledged that the May Revise to the 2004-05 state budget will not contain this provision. However, the panel strongly recommends that the Governor indicate in the May Revise that this would be the last time his administration would recommend tapping these funds. The panel further recommends that the Governor support legislative attempts, specifically ACA 29, to repeal language that permits the transfers altogether. The panel believes "fire walling" the Proposition 42 funds is imperative as: (a) a matter of public trust, given that the voters approved the constitutional amendment to fund transportation projects and not to pay down General Fund deficits; and (b) an economic stimulus since each \$1 billion invested in transportation projects yields 47,500 jobs.
2. ***Pursue "Hold Harmless", "Revenue Neutral" strategies to tapping transportation funds for General Fund deficit reduction.*** The panel believes that the Department of Finance is singling out transportation to pay a disproportionate share of the General Fund deficit. For example, transportation represents roughly 6% of State spending, but has funded and is funding reductions well in excess of that percentage. The panel is willing to pursue "revenue neutral" options to reduce the General Fund deficit and increase transportation resources in order to hold harmless transportation spending to the greatest degree possible. For example, to the extent that Proposition 42 is generating *more* revenue to the General Fund than the \$1.1 billion assumed in the initial budget documents, then that increased funding should be credited against the "delta" – or remainder of \$900 million – the Department of Finance is taking out of special transportation funds, thus holding the transportation program as harmless as possible from additional cuts.
3. ***Revise the Administration's proposal to convert federal funding for local projects from accrual to cash and transfer the cash to the General Fund.*** The accounting technique to cash out the federal funding may be a prudent cash management strategy if applied to delivering transportation projects. However, in this instance the Department of Finance proposes to use the "cash" freed up in this case to pay previous debt service for Propositions 111 and 116, which are general obligation bonds approved by the state's voters in 1990. The panel underscored in the strongest terms that the precedent the Department of Finance is setting with this proposal undermines voter trust and penalizes Caltrans and regional transportation agencies unjustly. The panel believes that the cash derived from the accounting conversion should be retained in the state highway account to pay for some of the \$2 billion in projects on the California Transportation Commission's pending allocation list. The panel acknowledged that this could create a challenge to the Department of Finance in its efforts to shore up the General Fund deficit; however, under recommendation number two noted above, the overall transportation "hit" needs re-evaluation. The panel understands the need for all programmatic elements of the state to "pitch in" to reduce the deficit – but not by reaching back to the debt service on previously approved and issued general obligation bonds.
4. ***Explore refinancing of existing General Fund transportation-related debt.*** Consistent with the above item, the panel believes that more attention should be given to

restructuring the existing Proposition 108, 116, and 192 debts. Savings achieved should be applied to reducing the overall “hit” on transportation funds needed to keep a “bare bones” program moving forward.

5. ***Seek to monetize State transportation assets and other facilities to fund transportation improvements.*** As part of the May Revise, the panel recommends that the Governor authorize the Department of Finance to determine whether State assets--such as transportation facilities constructed or acquired in prior years with transportation funds--can be used to generate private sector funding for new capital investment, through sale-leaseback, concession, and other mechanisms. Proceeds derived from such transactions would be deposited into the State Infrastructure Bank (SIB), which, similar to the Texas Mobility Fund, would make investments in new transportation projects that had the potential to leverage additional funding.

For example, the State could consider converting high occupancy vehicle (HOV) lanes to high occupancy toll (HOT) lanes on one or more highways, to be operated by governmental or public-private consortia. The operator would pay an upfront fee to the State that would be deposited into the SIB in return for the right to collect tolls at agreed-upon levels. The SIB would make investments in expanding those facilities or in other new projects. In order to expedite implementation of this technique, the State could consider initially paying shadow or pass-through tolls based on actual utilization, until such time as user-charge collecting systems could be installed. At that point, the projects would be fully self-sustaining.

6. ***Amend Caltrans’ workload reduction plan in current and budget years to provide for contracting out.*** The panel concurs with Caltrans’ position that it be held to its position-reduction target of 1,600 positions in FY 2004-05 but not be held to the dollar reduction target in order to transfer those funds into contracting out authority. The panel believes this is a prudent action to be announced in the May Revise of the 2004-05 budget. By retaining the authorized funding, Caltrans can begin to contract out essential design work to keep critical elements of the transportation program going. Moreover, since the funds that are assumed as savings are special funds and not General Funds, the panel believes that the General Fund should not be affected. In addition, contracting out will have a positive impact on jobs and the economy.
7. ***Monitor and prepare for the infusion of funding resources from the federal change in how ethanol in gasoline is taxed.*** Congress has adopted a new taxing formula for ethanol in gasoline, which will increase federal funds to California by more than \$400 million per year—or over \$2 billion over the life of the next five-year fund estimate. Mindful of what has happened in the past fifteen years when new infusions of funding becoming available, the panel urges the Administration to provide Caltrans with budget authority to contract out as well as undertake reimbursed work with internal staff. Closely aligned with recommendation six, the panel is concerned that if Caltrans is not ready to undertake planning, environmental, engineering, and construction activities, it will take two or more years to begin spending the funds. As with recommendation six, the panel believes this recommendation should be included in the May Revise of the 2004-05 budget and incorporated into the Governor’s 2005-06 budget.
8. ***Initiate a serious dialogue between the Administration and the state’s transportation community on how to attract private funds to transportation improvements.*** The panel believes that California can overcome the “boom-and-bust”

aspect to transportation resources by developing mechanisms to attract private capital to planning, funding and implementing transportation projects, such as tolling, private activity bonds, warranties and operating agreements, and other instruments. Different forms of private participation may be more suitable, depending upon whether the policy objective is maintaining existing infrastructure, managing current facilities to achieve greater productivity, or expanding and building new infrastructure. The panel urges the Governor to call for this dialogue as part of the May Revise to the 2004-05 budget message so that its recommendations could be included in the Governor's 2005-06 budget.

9. ***Support Federal initiatives for goods movement and other mega-projects.***

Congress will be finalizing the pending six-year federal surface transportation authorization bill within the next several weeks. While much attention has been focused on how California would fare under various formulas under consideration for apportioning Federal resources, the State stands to gain hundreds of millions of dollars under two new tax incentives proposed in the Senate version of the bill. One proposal entails the issuance of Federal tax credit bonds by a newly established private nonprofit entity known as the *Build America Corporation*. The Corporation would be authorized to assist goods movement projects, rail, and other mega-projects generating regional and national benefits. The Corporation would issue interest-free 30-year bonds, where the project sponsor would be responsible for repaying principal and the Federal government would pay the interest by granting the investor an annual Federal tax credit. Financially, this is tantamount to 80 percent Federal grant assistance. The other Senate tax-related proposal would authorize up to \$15 billion of private activity bonds for highway and intermodal projects. This would allow tax-exempt debt to be issued for projects with substantial private participation in their ownership or operation.

Given the significant budgetary constraints at the Federal level, such measures may offer the best chance California has in the near term to obtain substantial Federal assistance for major investments such as goods movement, passenger rail and intermodal facilities. The panel urges the Governor to support these federal proposals in preparation for House and Senate deliberations on reauthorization in April 2004.

10. ***Enhance accountability for project and policy outcomes.*** The panel feels strongly that direct public accountability for measurable results is essential to the success of California's transportation program. Commensurate with its recommendations, the panel recommends that the Governor and the Secretary direct Caltrans to provide a set of criteria to the Secretary by which all project and policy outcomes are tracked and reported quarterly. Communicating to the public -- whether and how effectively -- project delivery objectives are being met will strengthen the partnership of state, local and private sector players in improving California's transportation infrastructure.

V. Where We Go From Here - Recommendations

The Keston panel, as part of its recommendation to begin the process of transportation funding and delivery reform now, developed a series of additional recommendations that the Administration should consider as part of its development of an overall transportation reform program.

As the Administration develops an agenda and approach to transportation funding and delivery reform in California, it should consider the following approaches subsequent to the May Revise process for the 2004-2005 budget:

1. ***Develop a menu of opportunity for California transportation by adopting comprehensive transportation funding, finance and delivery reforms.*** Many states are beginning to understand that their maintenance and mobility needs are outstripping their ability to pay for transportation infrastructure at any more than a fraction of what is in their programs. More and more states are beginning to focus on new methods, approaches, and partners to help achieve their transportation infrastructure goals and objectives. The current pay-as-you-go approach, resulting in backlogs of transportation projects, is giving way to leveraged capital, private investment, and methods and mechanisms to create long-term revenue streams to pay not only for the capital investment in transportation infrastructure, but for the ongoing operating and maintenance costs as well.

Clearly, the Texas model warrants further study, evaluation and action. The panel was grateful to have Texas State Representative Mike Krusee share his experience in reforming transportation funding and delivery in Texas, and the panel believes that California can learn from what other states, regions, and nations are doing to bring critically needed safety, congestion relief and mobility to their citizens. To this end, included in Appendix B of this report is a summary of the massive transportation reform legislation undertaken and approved by Texas. The panel recommends that this information, along with other examples, be distilled and sorted into the beginnings of a legislative program for California transportation reform.

2. ***Begin meaningful leveraging of existing transportation resources.*** As part of the notion of creating a “firewall” around transportation funds, including Proposition 42, the panel spent a significant amount of time discussing the value of using some of the revenue stream at California’s disposal to leverage additional funding. One notion for consideration is the idea of setting aside a portion of transportation revenues (e.g., Proposition 42) as security for a transportation revenue bond to fund the backlog of allocated but pending transportation projects (\$1.7 billion), a portion for deferred maintenance, and the balance for significant statewide projects. For example, reserving \$400 million per year of Proposition 42 proceeds as revenue stream for a transportation bond could generate up to \$4 billion in proceeds for these purposes – consistent with what Texas has done in leveraging their State Highway Fund. The principle of “leverage” – whether existing or future resources – is one with which the panel strongly identified and strongly recommends be a going forward theme as part of any statewide reform effort. The panel recommends that the leveraging – of existing transportation and/or future transportation revenues – be an integral part of any legislative effort.

3. ***De-link the State's General Fund from the Transportation Fund– Part II.*** Consistent with the first two items in preparation of an overall reform program, an effective way to help ensure that transportation resources are not redirected to other purposes would be to establish a separate State debt financing program backed by a pledge of specific transportation revenues. The panel suggests that creating a state transportation trust fund borrowing program — similar to what is in use in over a dozen other states — not only would reduce the likelihood of transfers, but also would likely result in more favorable bond ratings, with corresponding reductions in interest cost. For example, most statewide transportation programs enjoy “AA” credit ratings, whereas California’s current general obligation rating is only “BBB”.
4. ***Develop a Golden State Corridors Program to compete for Federal support.*** As noted above, Congress is in the final stages of reauthorizing federal surface transportation legislation. Two key provisions – the issuance of Federal tax credit bonds by the *Build America Corporation* and up to \$15 billion of private activity bonds for highway and intermodal projects – are opportunities for California. The panel recommends that the Administration identify the *Golden State Corridors*, the handful of very critical, strategic goods and people movement corridors in California (e.g., Interstate 5) that could compete for funding from these proposed provisions in federal legislation. It is the panel's suggestion that being prepared strategically with a discrete set of transportation infrastructure investment opportunities that focus on not just California's economy, but the nation's economy in the form of interstate and international trade, could be a strategic advantage for California in attracting more Federal resources than by formula alone.
5. ***Allow Counties and Cities to select project delivery efficiency.*** Large, complex transportation capital investments often benefit from having a single-purpose public agency exclusively responsible for planning, developing, constructing, financing and operating the project. Under current State law, if one or more counties or municipalities wish to form a joint powers agency to serve as sponsor for a particular project, they must obtain approval from the legislature in Sacramento. This process can become politicized and the enabling legislation can encounter lengthy delays, to the detriment of the project. The Governor should propose state legislation authorizing political subdivisions to enter into arrangements to establish a joint powers agency without further State approval.

Appendix A
Infrastructure Financing Panel

John Barna, Vice President, Planning Company Associates, Inc.

Jack Basso, Director of Management and Business Development for the American Association of State Highway and Transportation Officials (AASHTO)

Nick Bollman, President, California Center for Regional Leadership

Donald H. Camph, President, Aldaron, Inc.

Diane Eidam, Executive Director of the California Transportation Commission

John Ferrera, Assistant Secretary for Transportation, Business, Transportation and Housing Agency

Stuart Gabriel, Director, The University of Southern California Lusk Center for Real Estate

Genevieve Giuliano, Professor, The University of Southern California School of Policy, Planning, and Development

David Grannis, President, Planning Company Associates, Inc.

Tony Harris, Chief Deputy Director, California Department of Transportation

Robert M. Hertzberg, Chair of Los Angeles of Economic Development Corporation

Gary H. Hunt, Partner, California Strategies, LLC

Michael I. Keston, Chairman of the Board, Keston Infrastructure Institute

Norman R. King, Executive Director of San Bernardino Associated Governments (SANBAG) and the County Transportation Commission

Mike Krusee, Representative, Texas House of Representatives, District 52

Stephen Lenzi, Senior Vice President, Public Affairs, Automobile Club of Southern California

Daniel A. Mazmanian, C. Erwin and Ione L. Piper Dean and Professor and Dean, The University of Southern California, School of Policy, Planning, and Development

Therese W. McMillan, Deputy Director, Policy, Metropolitan Transportation Commission (MTC)

Robert K. McCleary, Executive Director for the Contra Costa Transportation Authority

David Seltzer, Principal, Mercator Advisors, LLC

Robert A. Wolf, President, Germania Construction Corporation

David Yale, Director of Regional Programming, Los Angeles County Metropolitan Transportation Authority (MTA)

Geoffrey S. Yarema, Partner, Nossaman, Guthner, Knox & Elliott, LLP