

DEPARTMENT OF TRANSPORTATION

M e m o r a n d u m

To: CHAIR AND COMMISSIONERS

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Division of BudgetsRef: **2005-06 TCRP/STIP ALLOCATION POLICY**

The Department of Transportation (Department) is presenting this issue at the request of the California Transportation Commission (Commission) staff to discuss the potential impact of the 2006-07 Governor's Proposed Budget on current year allocations.

SUMMARY:

On January 10, 2006, the 2006-07 Governor's Budget was released. The proposed budget includes \$1.4 billion to fully fund Proposition 42 and a \$920 million partial repayment of the 2004-05 suspended Proposition 42 transfer.

The 2005-06 allocation plan did not assume a Proposition 42 transfer or an advanced partial repayment to occur in 2006-07. Consequently, the additional funding proposed in the 2006-07 Governor's Budget could support an increase to current year allocations and an opportunity to advance some projects by one construction season. However, any increase to allocations must consider the recent and projected cost increases to award current and future projects. These costs could significantly impact allocations and program funding, specifically the State Highway Operations and Protection (SHOPP) program.

The table below summarizes the possible increases to current year allocations the Commission may wish to make based on the 2006-07 Governor's Budget.

| Possible Additional TCRF Allocations (millions) | Prop 42 | Repayment | Total |
|---|---------|-----------|---------|
| Traffic Congestion Relief Fund (TCRF) | \$678 | \$410 | \$1,088 |

| Possible Additional STIP Allocations (millions) | Prop 42 | Repayment | Total |
|---|--------------|--------------|--------------|
| Transportation Investment Fund (TIF) | 250 | | 250 |
| Transportation Deferred Investment Fund (TDIF) | | 255 | 255 |
| Public Transportation Account (PTA) | 73 | | 73 |
| Total | \$323 | \$255 | \$578 |

BACKGROUND:

There are possible risks associated with each of the additional revenues proposed in the Governor's budget, Tribal Gaming revenues, and risks from increasing construction costs.

Proposition 42

Proposition 42 transfers are authorized by Article XIX B of the State Constitution. Based on current estimates, the 2006-07 Proposition 42 funding would be distributed as follows:

| Proposition 42 - Full Funding (millions) | |
|---|----------------|
| Traffic Congestion Relief Fund (TCRF) | \$678 |
| Transportation Investment Fund (TIF) - for STIP | 582 |
| Public Transportation Account (PTA) - for STIP & STA* | 146 |
| Total | \$1,406 |

* PTA share of TIF is split 50/50 with Local State Transit Assistance (STA) fund.

Risks. The suspension of Proposition 42 requires the Governor to issue a proclamation declaring that the transfer of revenues would result in a significant negative fiscal impact on the government functions funded by the general fund. Since the Governor has included the transfer in his proposed budget, the risk of the Proposition 42 funding not materializing is relatively low.

Allocations. With the inclusion of Proposition 42 in the 2006-07 Governor's Budget, the Commission may, with relatively little risk, consider increasing allocations against future year funding. The increase could come in the form of funding cost increases on existing projects and voting 2005-06 STIP projects in accordance with the 2005-06 STIP/SHOPP Allocation Plan and Criteria.

- The current allocation plan calls for the allocation of \$350 million in State Transportation Improvement Program (STIP) projects from TIF, based on the assumption of no Proposition 42 funding in 2006-07. The additional Proposition 42 revenues in 2006-07 could support an increase of STIP allocations from the TIF in the current year by \$250 million to the \$600 million level in the 2006 Fund Estimate.
 - Of the \$265 million in construction supplemental costs approved to date, \$146 million is for STIP projects. The Department is evaluating how much of this amount can be funded from future year Proposition 42 funding.
 - With some additional risk, the Commission may choose to immediately allocate up to \$582 million additional funds from this source. The remaining unallocated 2005-06 STIP is approximately \$540 million. The additional amount voted this year would be subtracted from planned 2006-07 TIF allocations.
- The \$678 million of 2006-07 Proposition 42 funding for the TCRF could be used to increase TCRF allocations in the current year by this amount.
- The \$73 million of the 2006-07 Proposition 42 funding to the PTA could be used to increase current year allocations of PTA eligible STIP projects, with the remaining \$73 million transferred to the State Transit Assistance (STA) Fund.

Advance Repayment of 2004-05 Proposition 42 Suspension

The total repayment of \$1.35 billion from the 2004-05 Proposition 42 suspension was originally scheduled to occur in 2007-08. The \$920 million in 2006-07 is a partial repayment. The remaining \$430 million is still forecast to occur in 2007-08. As proposed in the 2006-07 Governor's Budget, the distribution of the early repayment of the 2004-05 Proposition 42 suspension would be distributed as follows:

| Proposition 42 - Repayment of 2004-05 Suspension (millions) | |
|--|--------------|
| Traffic Congestion Relief Fund (TCRF) | \$410 |
| Transportation Deferred Investment Fund (TDIF) - for STIP | 255 |
| Local Streets and Roads | 255 |
| Total | \$920 |

Risks. Allocating funds from the proposed repayment of \$920 million in advance of the enactment of the 2006-07 is riskier than early allocation of the aforementioned Proposition 42 funds. This is because this funding must be approved by the legislature in the budget trailer bill, the distribution differs from existing law, and because these funds may not be received until late in the fiscal year.

Allocations. The 2006 Fund Estimate assumed that the STIP portion of this repayment would be available in 2007-08. The early repayment of these funds will mean that \$255 million in STIP funding from Transportation Deferred Investment Fund (TDIF) will be available one year earlier than planned. Additionally, the \$255 million is slightly greater than the \$226 million estimated in the 2006 Fund Estimate. With some risk, the Commission may wish to allocate \$255 million in STIP projects from the TDIF in advance of passage of the budget bill.

The repayment of the 2004-05 Proposition 42 suspension includes \$410 million for the TCRF. Since the remaining allocations for TCRP projects in the current year is less than the \$678 million provided by Proposition 42, the Commission does not need to consider risks associated with allocating these funds in advance of passage of the budget bill.

Tribal Gaming Revenues

Risk. Assembly Bill (AB) 438 (Chapter 113, Statutes of 2001) amended Government Code Section 14556.8 to authorize loans from the SHA and PTA to the TCRF in 2001 to backfill TCRF loans to the General Fund. The Director of Finance is required to repay these loans to the SHA and PTA by June 30, 2007 and June 30, 2008, respectively. In 2004, the Governor negotiated a compact with five Indian tribes in AB 687 (Chapter 91, Statutes of 2004) that authorized the use of Tribal Gaming bonds to repay these loans in 2005-06. However, lawsuits challenging the compact have delayed the issuance of these bonds.

| Tribal Gaming Revenue (millions) | |
|---|----------------|
| State Highway Account (SHA) | \$465 |
| Traffic Congestion Relief Fund (TCRF) | 290 |
| Public Transportation Account (PTA) | 122.5 |
| Locals | 122.5 |
| Total | \$1,000 |

The 2006-07 Governor's Budget assumes the sales of Tribal Gaming bonds will begin in Spring 2006, but it is now more likely to be delayed beyond the start of the 2006-07.

Allocations. Because the timing of this revenue is so uncertain, there would be significant risk in allocating these funds prior to receipt. Therefore, the Department continues to recommend the allocation of the Tribal Gaming Revenues be delayed until the bonds can be sold.

Construction Costs Increases

Through the Commission's February 2006 meeting, supplemental costs are estimated to total \$265 million. These costs include increased costs on prior year projects and costs to award projects that have come in above the Engineer's Estimates. This total does not include projects that have been voted by the Commission and not yet awarded.

Impact to Allocations. Whatever changes to current year allocations the Commission considers, it must also take into account the potential impact of the recent cost increases to award projects, as well as any supplemental funds requests from prior year projects. In light of these circumstances, it would be prudent to set aside a reserve of the additional allocation capacity to cover these potential cost increases.

TCRP PROJECTS

The Commission may wish to consider additional factors in making allocations for TCRP projects.

Remaining 2005-06 Projects Ready for Allocation

Based on the October 2005 TCRP Progress Report and accounting for allocations made to date, approximately \$535 million will be requested for project allocations for the remainder of the current year. Funding and project type include:

- \$372 million for construction or procurement.
- \$79 million for pre-construction projects that include STIP funding.
- \$84 million for pre-construction activities for projects with construction funded by TCRF (and other funds) in 2006-07 and beyond.

The Commission may wish to choose an aggressive allocation policy that immediately allocates the funding provided by Proposition 42. Under this policy, the total amount of 2005-06 allocation requests can be approved. Remaining revenues from Proposition 42 funding in 2006-07 and the potential of \$410 million in funding from the advance repayment of 2003-04 Proposition 42 suspension can be used to continue allocating funds in 2006-07.

AB 1335 Letter of No Prejudice

The Commission has approved a total of \$693 million in AB 1335 Letters of No Prejudice (LONPs). To date, approximately \$116 million of this amount has been allocated from 2005-06 Proposition 42 funds to completed LONPs, for the purpose of liquidation and reimbursement.

Lead agencies have indicated that approximately \$31 million of the approved LONPs will be completed in 2006-07. The Department recommends that the Commission reserve funding from 2006-07 Proposition 42 funding to reimburse agencies for their costs to deliver the completed project components.

SB 66 Provisions for LONPs

On September 29, 2005, Senate Bill 66 was approved. The Bill recommended that, commencing with 2006-07, the Commission shall review and revise its AB 1335 Letters of No Prejudice (LONP) guidelines. The review is necessary to assure that lead applicant agencies that have an approved LONPs as of June 30, 2005, are reimbursed on an equitable basis that serves the interest of the entire state transportation program, taking into account various factors, including, but not limited to, all of the following:

- The impact on allocations for other projects.
- The cash flow requirements necessary for projects with existing allocations.
- The extent to which the agencies have had to defer other high priority STIP or TCRP projects because of advancing their own funds.
- The extent to which reimbursements would be spent on the construction phase of other STIP or TCRP projects.
- Any adverse impact on the agency's other high priority projects of postponing reimbursement until project completion, as opposed to allowing payment to be made based upon the amount of funds expended on eligible costs for a project, payment to be made upon the documentation of those eligible costs.
- The level of commitment made by the agency in expending its own funds for any component of a transportation project.

The proposed Guidelines includes these factors and allows up to one-half of the resources appropriated in a given fiscal year to the TCRF will be reserved for allocation and reimbursement for approved LONPs.

2006-07 Project Allocations

According to information submitted by lead agencies in the October 2005 TCRP Progress Report, \$839 million in project allocation requests will come forward in 2006-07 (not including LONPs previously discussed). Of this amount:

- \$255 million for construction or procurement.
- \$54 million for pre-construction projects that include STIP funding.
- \$529 million for pre-construction activities for projects with construction funded by TCRF (and other funds) in 2006-07 and beyond.

Allocations made for these projects will be dependent on the allocation policy adopted for the remainder of 2005-06, the level of funding provided in 2006-07, and the amount of funds reserved for LONPs. The Department recommends that the Commission review its allocation criteria upon final passage of the budget bill.

TCRF Repayment of loans from the State Highway Account

The \$465 million included in Tribal Gaming bond funding for the SHA is to repay loans made from the SHA to the TCRF in 2002-03. Under current statutes, the loans are due for repayment no later than June 30, 2007. If the lawsuits regarding the Tribal Gaming bonds are not resolved by this date, and if the dates for loan repayment is not extended as discussed earlier, the TCRF may be obligated to repay this loan from whatever funds remain in the TCRF.

This risk can be mitigated by Proposition 42 funding for the TCRF in 2007-08. The Governor has proposed a firewall to preserve full funding for Proposition 42. The 2007-08 Proposition 42 funding provides sufficient resources to the TCRF in the event that the TCRF must repay the SHA in lieu of Tribal Gaming funds.

Cash Management Strategy

Due to the uncertainty of future funding for the TCRF, the Department has recommended that the TCRF be managed on a modified accrual basis where allocations are limited to the resources appropriated to the fund. The balance in the TCRF will remain relatively high as project expenditure occurs over several years.

If the Governor's proposal to implement a firewall to protect Proposition 42 funding is approved by the voters, the Department would recommend that the TCRF be managed on a cash-flow basis. This would allow the Commission to allocate funds in advance of actual appropriation to the TCRF since funds in future fiscal years would be guaranteed from Proposition 42. The Commission would still need to consider the risks associated with allocating funds from revenues due in future loan repayments that may be outside a Proposition 42 firewall.