Agenda Item 3b

METROPOLITAN TRANSPORTATION COMMISSION

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Memorandum

TO: Legislation Committee

DATE: July 6, 2009

FR: Executive Director

RE: <u>FY 2009-10 State Budget Update</u>

Almost a week into the new fiscal year, the Legislature has once again been unable to reach agreement on a state budget. On Thursday, June 25, the Assembly supported in a bipartisan manner a package of cuts designed to alleviate the near term threat that — in the absence of a budget — the state would need to issue "IOUs" beginning on July 1. The package was unable to win support from Senate Republicans or the Governor, who argued for a more comprehensive approach. The state began issuing IOUs last week, but banks have said that they will stop honoring them after July 12.

While the final elements of a budget deal are unknown, the budget conference committee approved several weeks ago the Governor's proposed redirection of $986 million in gasoline tax funds that current law would allocate to cities and counties for local streets and road repairs. This results in an estimated $184 million loss to Bay Area jurisdictions, as reported to this committee last month. These funds are one of the few sources available to local jurisdictions to pay staffing and day-to-day operating costs associated with public works departments. According to estimates provided by the California State Association of Counties, the reduction would result in 838 staff layoffs at the Bay Area's nine counties. This does not include staffing cuts that would likely result among the region's 101 cities. All told, the anticipated layoffs and funding cuts can be expected to have a significant negative impact on the ability of local governments to respond to the most basic of needs — from major pothole repairs to traffic signal problems.

The Assembly followed up this effort with another budget package contained in Assembly Bill 39 by a vote of 44-30, which includes a package of spending cuts, along with tax and fee increases, designed to close an estimated $19.5 billion shortfall. Using a mechanism attempted earlier this year which allows a tax increase to be passed by a majority vote as long as the overall bill is revenue neutral, the Assembly proposal eliminates the state's 18-cent/gallon gasoline and diesel fuel excise taxes and replaces them with fees in a like amount. The legislation provides that the excise tax would be eliminated beginning on October, 1, 2009, allowing for approximately $2.3 billion in tax increases for FY 2009-10 and $3.1 billion in FY 2010-11.

As noted in our analysis of this proposal when it first surfaced last January, replacing excise taxes with user fees raises the following concerns:

1. Legal Nexus Test – Less Flexibility in Expenditures and Distribution
Revenue generated by the fees would be subject to a legal nexus test which requires that the expenditure of revenues provide a direct benefit to the user. Fees may also be spent for mitigation of the

adverse effects associated with a fee payer's activities. How broadly "user benefit" and "mitigation" could be defined is a legal question that would have immense ramifications for this fee. For instance, would public transit be considered an eligible expense? Would existing distribution formulas — such as those used in the STIP — hold up under a fee scenario? There are differing legal opinions on these questions, including differing opinions from the State's Legislative Counsel, and no doubt the subject would likely lead to litigation. If plaintiffs sought injunctive relief, the court could halt the imposition of the fee until litigation is resolved, resulting in substantial uncertainty for transportation programming purposes.

2. Funds Would Likely Be Subject to Article XIX of the State Constitution
Article XIX restricts taxes imposed on motor vehicle fuel to the research, planning, construction, improvement, maintenance and operation of state highways, local streets and roads, and mass transit guideways.

3. Loss of Funding for Public Transportation Account (PTA)
By eliminating the state excise tax on gasoline, the proposal also eliminates one of the sources of PTA funding — the sales tax imposed on the first 9 cents of the gasoline excise tax, commonly known as the "Proposition 111" portion, so named for the 1990 ballot measure that increased the state's gasoline tax from 9 cents to 18 cents per gallon. In FY 2010, approximately $64 million was estimated to be deposited in the PTA from this source. While the Legislature has imposed a three-year moratorium on the State Transit Assistance program, which is funded by the PTA and has diverted other PTA capital funds to the General Fund, MTC and others strongly support *restoring* the use of PTA funds for genuine *public transit* purposes.

State Court of Appeal Finds Diversion of Transit Funding "Illegal"
In a related development, the California Transit Association last week scored a strong win in its lawsuit against the state for diverting $1.2 billion in public transit funds in FY 2007-08. While a trail court had largely upheld the diversions, the Court of Appeal interpreted the term "mass transportation" to mean "public transportation on mass transit." Consequently, the court ruled against the use of PTA funds for home-to-school transportation, debt service for public transit-related bonds, and transportation of the developmentally disabled to regional centers under the Department of Developmental Services. How this ruling will affect the FY 2009-10 budget remains to be seen, but all observers expect the state to appeal the case to the State Supreme Court.

We will update the Committee with the latest developments on the state budget at the July 10th meeting.

Steve Heminger

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