MEMORANDUM

TO: Santa Clara Valley Transportation Authority
Board of Directors

FROM: Kurt Evans, Government Affairs Manager
Santa Clara Valley Transportation Authority

DATE: October 5, 2009

SUBJECT: Weekly Legislative Update: Week of September 28, 2009

FEDERAL

Surface Transportation Authorization: Just hours before the expiration of the Safe, Accountable, Flexible, Efficient Transportation Equity Act: A Legacy for Users (SAFETEA-LU) and the end of the old fiscal year, Congress passed a continuing resolution to extend funding for all federal programs, including transportation, for one month. The resolution also included a one-month extension of SAFETEA-LU, the current federal law governing surface transportation. The continuing resolution was required because Congress was not able to enact any of the appropriations bills prior to the onset of FY 2010, and because efforts to enact a longer term extension for SAFETEA-LU before its September 30 deadline fell short. The continuing resolution both authorizes and appropriates funds for federal highway and public transit programs through October 31, 2009. It was signed into law by President Barack Obama shortly after it was approved by Congress.

Efforts by the Senate to pass a three-month extension of SAFETEA-LU stalled as lawmakers tried to reach an agreement to cancel a scheduled $8.7 billion recession of highway contract authority. The House had previously approved legislation to extend SAFETEA-LU for three months, but that measure did not include language to prevent the $8.7 billion rescission. With time running out, the leadership of the Senate Environment and Public Works Committee dropped its insistence on an 18-month extension of SAFETEA-LU in favor of the three-month bill passed by the House, with new language added to repeal the rescission. However, to satisfy congressional budget rules, the legislation needed to include funding to offset the negative impact on the budget. Proposals to offset the repeal of the rescission with funds from the American Recovery and Reinvestment Act (ARRA) or the Troubled Asset Relief Program (TARP) were met with objections from House negotiators and a few Senate Republicans. These objections prevented consideration of the three-month extension bill on the Senate floor prior to the expiration of SAFETEA-LU. Therefore, the one-month extension of SAFETEA-LU included in the continuing resolution became law.

Senate leaders have pledged to renew their push for the enactment of a longer extension of SAFETEA-LU that includes a restoration of the lost highway contract authority caused by the $8.7 billion rescission. Meanwhile, House Transportation and Infrastructure Committee Chairman James Oberstar (D-MN) is still advocating for the passage of a full, six-year surface transportation authorization bill as soon as possible.

<u>FY 2010 Transportation Appropriations:</u> Both the House and Senate have passed their own versions of the FY 2010 Transportation, Housing and Urban Development, and Related Agencies (THUD) Appropriations Act, but the legislation has not yet been sent to conference to reconcile the differences. While House and Senate leaders have indicated that they hope to pass the FY 2010 THUD spending bill as a stand-alone measure in the coming days, House Appropriations Committee Chairman David Obey (D-WI) did not rule out the possibility that it could get rolled into a large omnibus appropriations bill that would cover all federal agencies and programs.

The Senate THUD appropriations bill contains $11.07 billion for public transit programs under the jurisdiction of the Federal Transit Administration (FTA), which is $590 billion more than the House legislation and $840 million more than was enacted in FY 2009. The House version provides $10.48 billion for transit in FY 2010. The main difference is the Senate's proposed substantial increase in funding for New Starts and Small Starts. The Senate bill provides a total of $2.307 billion for these two programs, $480 million more than the House measure, which recommends $1.827 billion. Meanwhile, the level of funding for the Urbanized Area Formula (UZA) Program is identical in both the House and Senate bills—at slightly more than $4.75 billion. And both versions provide $584 million for the Bus/Bus Facilities Discretionary Program, a $300 million cut from FY 2009.

Reconciliation will be necessary for the level of funding being proposed for high-speed and intercity passenger rail. The House THUD appropriations bill provides $4 billion, while the Senate version recommends $1.2 billion. The Senate legislation also appropriates $50 million for the deployment of positive train control systems (PTC), the full amount authorized under the Rail Safety Improvement Act of 2008. The House bill does not include any money for this purpose. Also at issue is the Senate's proposed allocation of $1.1 billion for a competitive multimodal grant program modeled after the Transportation Investment Generating Economic Recovery Program (TIGER) established under ARRA to provide funding for surface transportation projects of national, regional or metropolitan significance. The House measure does not include comparable provisions.

<u>Climate Change:</u> On September 30, Senate Environment and Public Works Committee Chairwoman Barbara Boxer (D-CA) and Senate Foreign Relations Committee Chairman John Kerry (D-MA) introduced climate change legislation that is designed to reduce greenhouse gas emissions more rapidly than a competing measure passed by the House in June. The Senate bill, titled the Clean Energy Jobs and American Power Act, requires a 20 percent decrease in greenhouse gas emissions by 2020 versus the 17 percent cut required in the House measure. After that, both versions mandate a 42 percent reduction in emission levels by 2030 and 83 percent by 2050.

While the Senate climate change bill does not yet specify investment levels, negotiations to assign emission allowances, the source of funding under a cap-and-trade program, are well under way. Under the provisions of the legislation, allowances must meet one of three primary goals: (1) protecting consumers from price increases; (2) assisting industry in transitioning to clean energy; or (3) spurring energy efficiency and the deployment of clean energy technology. Numerous grant programs to fund clean transportation, as well as state and local government energy efficiency efforts, are proposed to be funded through allocations or the auction of allowances.

With regard to transportation, the Senate climate change legislation generally outlines the structure of potential investments, including for public transit, and introduces significant new planning provisions with regard to greenhouse gas emissions. Some level of emission allowances is proposed to be set aside for urban and rural transit formula funding, while a separate fund would be created for a new competitive grant program for all types of emission-reducing transportation investments. Each percent of emission allowances could be worth between $600 million and $1 billion in new annual investment, which would ultimately be determined by the market value of those allowances under the cap-and-trade program.

Some of the specific transportation-related elements of the Senate climate change bill are as follows:

<u>Emission Standards for Heavy Duty Vehicles</u>: Requires the U.S Environmental Protection Agency (EPA) to establish greenhouse gas emission standards for heavy duty vehicles and engines, as well as for off-road vehicles and engines.

<u>State and MPO Planning Efforts</u>: Authorizes the EPA to establish national emission reduction targets for the transportation sector, as well as standardized emission models and related methodologies to be used by states and metropolitan planning organizations (MPOs). The EPA is required to finalize the federal rules within 18 months of enactment of the legislation and to update them every six years. MPOs would be required to adopt emission targets no later than two years after the adoption of the federal rules. Emission-reduction strategies must be integrated into regional plans. These strategies may include: (a) efforts to increase public transit ridership, as well as biking, walking and the use of other non-motorized transportation modes; (b) implementation of zoning and land-use requirements; (c) travel demand management activities, such as carpools, vanpools and car share programs; (d) pricing measures; (e) telecommuting; (f) intercity bus and intercity passenger rail improvements; and (g) freight improvements. The bill establishes a grant program administered by the U.S. Department of Transportation to support state and MPO planning efforts, with awards to MPOs based on population. Performance grants would also be awarded based on a variety of criteria, including the quantity of total greenhouse gas emissions reduced; cost-effectiveness; and increases in mobility options for low-income households, minorities, the disabled, and the elderly.

<u>State Programs for Greenhouse Gas Reduction and Climate Adaptation</u>: Distributes an unspecified sum of proceeds from emission allowances for the implementation of projects, programs or measures designed to reduce greenhouse gas emissions and to build resilience to the impacts of climate change. Roughly 10 percent of allowance proceeds are reserved for funding

coastal state economic protection programs and 1 percent for supporting climate change response programs administered by Native American tribes. Of the remaining proceeds, 50 percent would be dedicated to public transit grant programs, while the rest would go for state and local programs designed to fund water systems mitigation and adaptation partnerships, flood control and response, recycling efforts, and air quality improvements.

<u>SmartWay Transportation Efficiency Program</u>: Expands an existing EPA loan and fuel-saving technology deployment program called the SmartWay Transport Partnership to help the trucking industry upgrade to more fuel efficient and less polluting vehicles.

<u>Investments in Clean Vehicle Technologies</u>: Distributes an unspecified amount of emission allowances for: (a) the development and demonstration of a national transportation low-emission energy plan; (b) the use of domestically produced plug-in electric drive vehicles; and (c) grants to reduce diesel engine emissions.

The Clean Energy Jobs and American Power Act is being viewed by both supporters and opponents of climate change legislation as largely a starting point in what is expected to be intense and difficult negotiations in the Senate. Most GOP senators have voiced strong opposition to a cap-and-trade program, calling it a massive energy tax on consumers as energy prices increase amid the shift away from fossil fuels. And numerous centrist Democrats, especially from rural areas and from states with energy intensive industries, have expressed reluctance to support any bill that does not protect against energy cost spikes and does not protect domestic industries.

The unveiling of the Senate climate change legislation came just hours before the EPA announced new rules to crack down on greenhouse gas emissions from factories, power plants and other industrial facilities. The move represented a clear signal from the Obama Administration that it is prepared to act on climate change if Congress does not. The proposed EPA rules require new facilities and those undergoing major maintenance to limit their greenhouse gas emissions using the "best available" technology. That might include energy efficiency steps or the use of equipment currently under development to capture greenhouse gases and funnel them into storage.

<u>STATE</u>

<u>Tax Commission:</u> The Commission for the 21st Century Economy released its long-awaited report on how to re-engineer California's tax structure, which includes recommendations to flatten out the state income tax, eliminate other taxes and impose a new form of consumption tax on most businesses. Gov. Arnold Schwarzenegger immediately embraced the commission's recommendations and called for a special session of the Legislature to consider them. The Governor said he would sign the plan as is, although he acknowledged that lawmakers should have a chance to analyze and "tweak" it. He called on the Legislature to take action by the end of the year, but Assembly and Senate Democratic leaders made no promises on a timetable.

The commission was created by Gov. Schwarzenegger through an executive order that was issued last October in response to a growing realization that California's tax system, which is heavily weighted toward income taxes on more affluent taxpayers, had become a revenue roller coaster. When the state's economy expands, billions of extra dollars flow into the General Fund, triggering automatic spending increases and encouraging lawmakers to dole out the influx. But when the economy cools, revenues plummet, leaving huge budget deficits. The commission was charged with considering ways to update and stabilize the state's tax structure, and make it less vulnerable to economic booms and busts. Specifically, it was tasked with coming up with recommendations to:

- Establish a 21^{st} century tax structure that fits with California's 21^{st} century economy.
- Stabilize state revenues and reduce volatility.
- Promote the long-term economic prosperity of the state and its citizens.
- Improve California's ability to successfully compete with other states and nations for jobs and investments.
- Reflect principles of sound tax policy, including simplicity, competitiveness, efficiency, predictability, stability, and ease of compliance and administration.
- Ensure that the tax structure is fair and equitable.

The commission consisted of 14 members—seven appointed by the Governor and seven by the legislative leadership. It was chaired by Gerald Parsky, a Rancho Santa Fe investor who is a former University of California regent and former Republican state party chairman.

When the panel began its deliberations, it quickly became apparent that there were no easy answers. In fact, Gov. Schwarzenegger had to give the commission two deadline extensions after initially expecting its recommendations in April. His last executive order, which was issued in July, specified a September 20 deadline. In the end, only nine of the 14 members supported the final report.

The commission's plan revolves around three key elements, which when taken together, are intended to be "revenue-neutral" in terms of their impact on the General Fund:

1. Lowering personal income taxes for all filers by reducing the number of tax brackets from six to two. This change would be phased in over three years. Single filers would have an automatic deduction of $22,500. For joint filers, it would be $45,000. Filers would pay 2.75 percent on taxable income up to $28,000 single and $56,000 joint. They would pay 6.5 percent on all taxable income above those levels. The only itemized deductions would be for mortgage interest, property taxes and charitable contributions, and all tax credits would be eliminated. While all filers would pay lower taxes, the new tax brackets would make the system less progressive in nature. The drop to 6.5 percent from 9.55 percent is most significant for higher-income earners, who already pay most of the state's personal income taxes. Currently, personal income taxes account for 55 percent of General Fund revenues. Under the commission's proposal, it would drop to 32 percent.

2. Reconfiguring business and sales taxes. Under the commission's plan, the state would eliminate the corporation tax immediately in 2012, and phase out the state sales tax over a five-year period. The state sales tax rate is currently 6 percent because of the temporary

1 percent increase that was enacted as part of the FY 2010 budget deal. Under the commission's plan, the state sales tax would continue to be applied to purchases of motor vehicle fuels in order to keep in place the funding source for Proposition 42 and the Public Transportation Account. In addition, retailers would still charge locally imposed sales taxes.

3. Imposing a new consumption tax. To make up for the loss of corporation and state sales tax revenues, as well as to cover any revenue loss resulting from the changes to the personal income tax, the state would impose a new business net receipts tax—essentially a value-added tax that firms doing business in California would pay on all revenues minus the cost of purchases (but not the cost of salaries and benefits). The proposed rate is 4 percent, lower than the current corporation and state sales tax rates. The tax would be phased in over five years, starting at 2 percent in 2012. The policy dilemma facing the commission was that California has become more of a service-based economy, but services currently are not subject to the sales tax. To get at this issue, the panel ultimately decided that a business net receipts tax would be more politically palatable than trying to extend the sales tax to services.

Despite Gov. Schwarzenegger's support, the commission's recommendations immediately came under fire from inside and outside the State Capitol Building. Neither Senate President Pro Tem Darrell Steinberg (D-Sacramento) nor Assembly Speaker Karen Bass (D-Los Angeles) expressed enthusiasm for the plan. Steinberg said there are questions about how it would affect funding for education and other essential state services, while Bass commented, "I know there have been concerns raised by the business community, and concerns raised by advocates for middle-class families and low-income workers."

Meanwhile, Art Pulaski, head of the California Labor Federation, called the report a "profound disappointment, offering no solutions to better support our state's middle class." He said the commission's plan would shift the tax burden from the wealthy to middle- and low-income families, and "entomb California in perpetual recession." California Chamber of Commerce President Alan Zaremberg declared that report is "fatally flawed." The major concern of business groups is that the new business net receipts tax is untested and could become a hurdle that makes California less competitive with other states.

NOTE: Also contributing to this report were Susan Lent with Akin Gump Strauss Hauer & Feld; Mark Watts with Smith, Watts & Company; and Scott Haywood, VTA's Policy and Community Relations Manager.