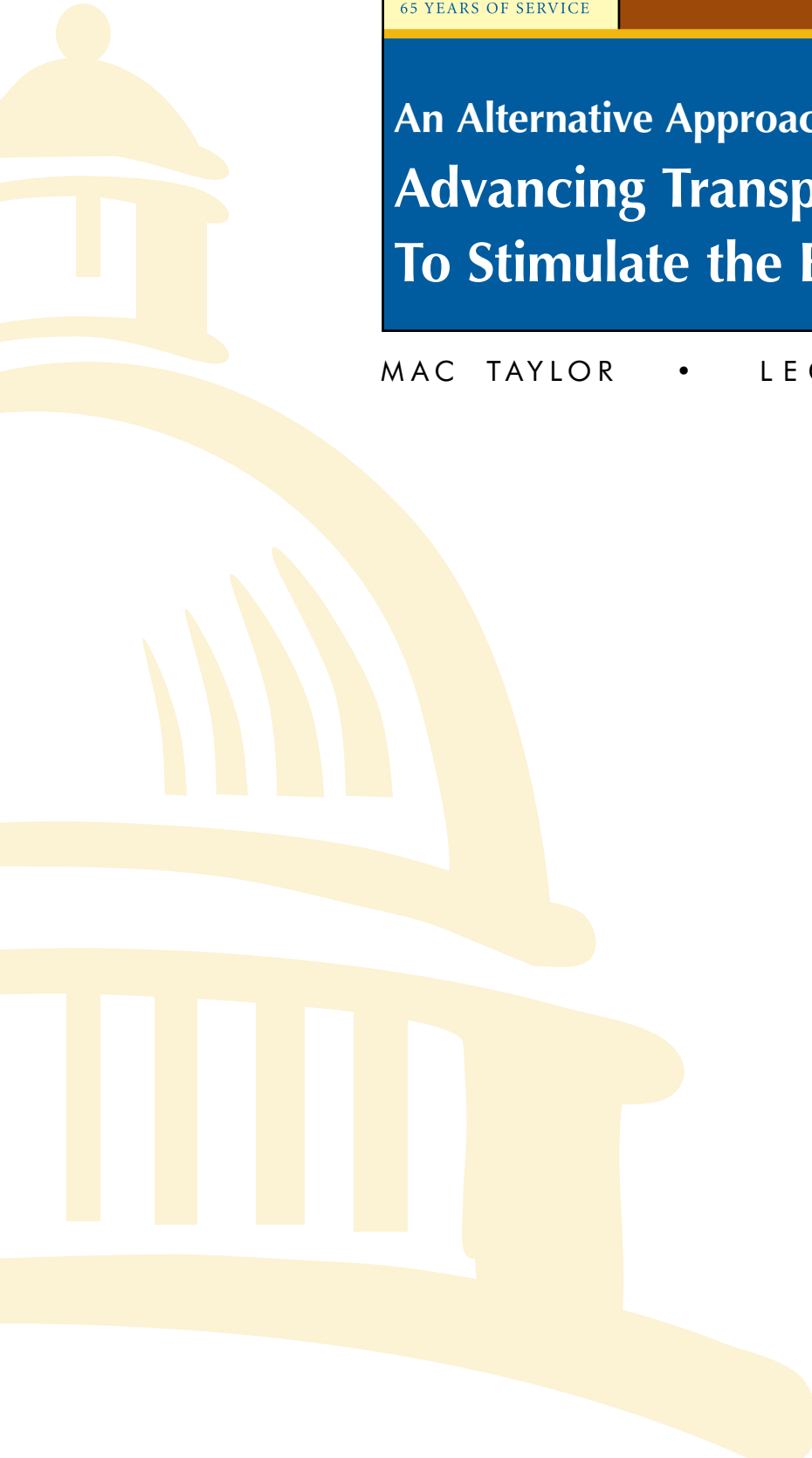


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**An Alternative Approach:  
Advancing Transportation Projects  
To Stimulate the Economy**

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**Acknowledgments**

This report was prepared by Jessica Digiambattista, and reviewed by Dana Curry. The Legislative Analyst's Office (LAO) is a nonpartisan office which provides fiscal and policy information and advice to the Legislature.

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## SUMMARY

**Issues with Governor's Proposal.** As part of his 2008-09 special session package, the Governor proposed to speed up construction of \$822 million in planned state transportation projects. We believe that the concept of accelerating transportation projects has merit. However, we identified several steps that could make implementation of the Governor's proposal difficult, as well as factors that could limit the benefits of his proposal.

**LAO Alternative.** We offer an alternative approach that we believe would provide greater benefits with a similar amount of funding. Specifically, we recommend the use of revenue bonds backed by future gas tax revenues to accelerate 122 highway rehabilitation projects. These projects would be ready for construction in 2008-09, 2009-10, and 2010-11, but are not scheduled for construction until later years, due to limited funding. Our bond proposal would require voter approval. Accordingly, we recommend the Legislature place a measure on the next ballot to seek voter approval to issue \$800 million in gas tax revenue bonds to fund these projects.

## ADVANCING TRANSPORTATION PROJECTS: AN ALTERNATIVE APPROACH

As part of his 2008-09 special session package, the Governor proposed to speed up construction of some previously planned state and local transportation projects. These projects would be funded mainly with Proposition 1B bond monies. The Governor's transportation proposal includes three components: (1) \$822 million for state transportation (mainly highway) projects, (2) \$800 million for local transit projects, and (3) \$700 million for local street and road improvements. Given the current economic climate, we believe that the concept of accelerating state and local transportation projects has merit. It could repair and improve transportation systems at an earlier date than planned as well as provide a stimulus to the state's economy. However, we propose that the Legislature consider an alternative to the component of the Governor's proposal to advance \$822 million in state transportation projects that we believe would provide greater benefits with a similar amount of funding.

### **A Transportation Stimulus Package Can Have Benefits**

The California Department of Transportation (Caltrans) builds capital projects that improve, rehabilitate, and expand the state's highway system. While the plans and designs for projects are typically developed by Caltrans' staff, the construction of projects is performed by private businesses under contracts with the state.

**More Construction Firms Bidding on Transportation Projects.** Currently, Caltrans reports that it is receiving more bids on construction contracts than it has in recent years. Whereas a couple of years ago Caltrans typically received two or three bids for a project that it advertises for construction, the department is now receiving

five or six bids for a similar project. This increase in the number of construction companies bidding on transportation projects is mainly because fewer other construction jobs are available due to the current economic climate.

**Better Prices on Construction.** This increase in the number of bids has resulted in a more competitive bidding environment and lowered the price the state is paying for the construction of transportation projects. Additionally, the costs of many of the materials used to construct these projects have declined recently due to overall economic conditions. Together these two factors have substantially reduced the current cost of constructing transportation projects. In 2007-08 and thus far in 2008-09, Caltrans reports that on average construction contracts have been awarded at 20 percent below the estimated project cost. This reduction in construction costs is a stark contrast to the double-digit increases above estimated project costs seen by Caltrans in previous years.

**Advancing Projects Can Be a Win-Win Situation.** As Figure 1 summarizes, advancing the construction of transportation projects has several benefits. In light of the current competitive construction prices, the state could save by constructing more projects during a period when prices are relatively low. Constructing projects sooner than planned would also provide the transportation benefits of those projects, such as reducing traffic congestion, to the public sooner. Lastly, advancing more projects to construction would provide additional employment opportunities for the private sector in the state, thereby providing an economic stimulus.

**Governor’s Proposal**

**Advance Eleven Large Transportation**

**Projects.** As part of his 2008-09 special session package, the Governor proposes to stimulate the economy by advancing the construction of 11 large transportation projects. These projects, totaling about \$822 million in cost, would be funded mainly from Proposition 1B money (including money from the Corridor Mobility Improvement Account, the State Route 99 Account, and the Trade Corridor Improvement Fund), as well as from other state, local, and federal funds. To develop and construct these projects sooner than currently scheduled, the Governor is proposing to ease some of the requirements related to project development, as discussed below. By speeding up the development of these projects, the Governor proposes to have construction contracts for all 11 projects in place by the end of December 2009.

**Waive Environmental Review Requirements.**

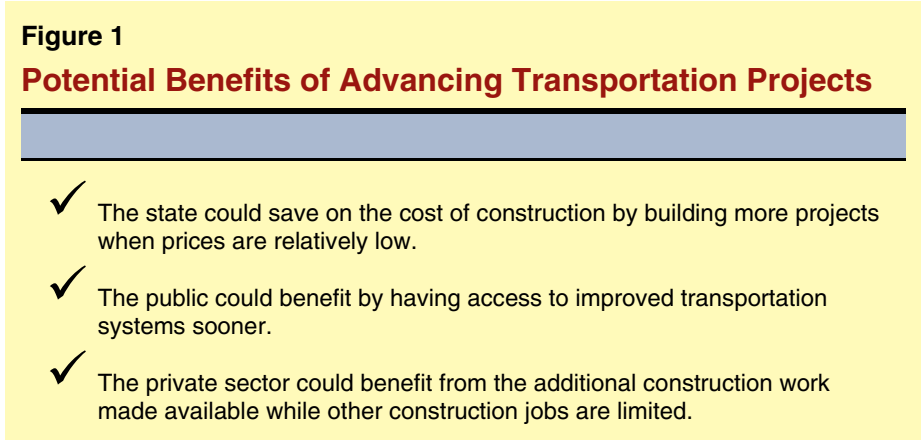
Caltrans is currently performing the work necessary to get these 11 projects ready for construction, including environmental review, design, engineering, and acquisition of rights-of-way. Therefore, even though the state may have the ability to fund these projects now, they are not yet ready to proceed to construction. To shorten the time it will take to get these projects ready

for construction, the Governor proposes to statutorily exempt the projects from the California Environmental Quality Act (CEQA). This means that these projects would not be required to undergo a review of their potential environmental impacts. Exempting these projects from the state’s environmental review process would reduce the amount of work that needs to be completed before these projects can go to construction. For large projects, this could advance the timing by several months to over a year.

However, eight of the projects identified in the Governor’s proposal also require federal environmental review as part of the National Environmental Policy Act (NEPA). Providing an exemption from the state requirement alone may not substantially reduce the amount of work required before these projects could be built, as they must also comply with the federal environmental review requirements. Thus, to address this potential limitation, the administration would seek waivers from the federal government to exempt the eight projects from the NEPA requirements.

**Streamline Permitting.** To further speed up these 11 projects, the Governor also proposes to streamline the permitting process of certain state and local agencies. Specifically, the Governor proposes to statutorily set time limits within which permit applications must be reviewed

and processed by these agencies. For instance, Caltrans is required to obtain permits from the California Department of Fish and Game when projects are located in or near the habitat of an endangered species. Permits of this type can often take 60 days or



longer to be issued. Under the Governor's streamlining proposal, state and local agencies would have 15 days to respond to a permit request. According to Caltrans, a more streamlined permitting process could potentially get these projects ready for construction several months sooner.

**Authorize Design-Build Contracting.** The Governor also proposes legislation that would authorize the use of design-build procurement on a pilot basis, which could include some projects identified in this proposal. Design-build procurement would allow Caltrans to contract with a private business to perform both the design and construction on a given project. This method allows projects to begin construction when they are only partially designed. This differs from the traditional procurement method in which the state contracts with private businesses only for the construction of projects after they are fully designed. Our review indicates that several of the 11 projects proposed to be advanced would need to use a design-build procurement method in order to meet the target of being under contract by December 2009.

### **Governor's Proposal May Be Difficult to Implement and Has Limited Benefits**

Our review identified several steps to implementing the component of the Governor's proposal relating to accelerating state transportation projects. Additionally, a couple of factors could potentially limit the benefits from this proposal. We discuss these issues below.

- **No Plan Proposed for NEPA Waivers.** While the Governor's plan would require the exemption of federal environmental requirements under NEPA, the proposal does not provide details regarding how and when the state would obtain these waivers.

- **Legislation Required.** Exempting certain projects from CEQA, streamlining the permitting process, and authorizing the use of design-build procurement each require statutory changes.
- **Construction May Not Occur Sooner if Preconstruction Work Not Funded.** Many Proposition 1B-funded projects are scheduled to receive bond funds that can be used only to pay for construction. These projects must rely on funds from other sources, mainly Proposition 42 (state gasoline sales tax revenue) and local funds to pay for preconstruction activities such as engineering and design work. The construction of these projects may not occur sooner than previously planned if the preconstruction activities are not completed or funded.
- **Some Projects Would Only Be Accelerated by a Few Months.** Several of the 11 projects are currently scheduled to begin construction in early 2010. The Governor's proposal thus would accelerate these projects to construction by only a few months.
- **State May Not Benefit Fully From Competitive Construction Prices.** Because large projects typically receive fewer bids, the Governor's proposal might not capture the full benefits of the current competitive bidding environment. In addition, these projects will only provide a stimulus impact in a few regions of the state where these 11 projects are located.

While there would be challenges to implementing the Governor's proposal, accelerating the 11 projects would provide some benefits to the extent that they could proceed to construction earlier than planned.

**Advancing SHOPP Projects:  
An LAO Alternative Proposal**

In light of the limitations of the Governor’s proposal, we offer below an alternative approach to accelerate additional transportation projects to construction over the next couple of years in order to provide transportation benefits and to stimulate the economy. Our alternative could be implemented either in lieu of the Governor’s proposal or in conjunction with it.

**Highway Rehabilitation Projects Are Ready to Go.** The State Highway Operation and Protection Program (SHOPP) is the state’s program for rehabilitating the highway system. Projects include primarily pavement and structures (bridges) rehabilitation, major reconstruction, and safety improvements. As we have noted in our past analyses of the budget bills, the limited availability of funding for highway maintenance and rehabilitation means that there is a significant volume of highway rehabilitation work that cannot move forward on a timely basis. (See, for example, the *Analysis of the 2008-09 Budget Bill*, page A-30.)

While Proposition 1B provided a one-time infusion of \$500 million for SHOPP projects, most of these funds have already been appropriated, with only about \$100 million remaining for 2009-10 and beyond. Our recent discussions with Caltrans identified 122 SHOPP projects with estimated construction costs of about \$800 million that will be “plan-ready” (that is, designed and engineered and ready to go to construction) in

2008-09, 2009-10, and 2010-11. These projects, however, are not currently scheduled to start construction until later years due to limited funding. As Figure 2 shows, these projects include work ranging from pavement rehabilitation to drainage rehabilitation to safety improvements on state highways.

**Use Future Gas Tax Revenues to Fund More SHOPP Projects Now.** State funding for SHOPP comes mainly from the excise tax on gasoline and diesel fuel (commonly referred to as the “gas tax”). Gas tax revenues have traditionally funded projects on a pay-as-you-go basis; however, the use of these funds could be advanced by issuing revenue bonds backed by future gas tax revenues. By issuing \$800 million in gas tax revenue bonds, construction of 122 projects that are plan-ready could be carried out ahead of schedule. Caltrans, however, does not currently have the authority to bond against future gas tax revenues. The State Constitution allows the state to issue bonds backed by gas tax revenues, but only if the bond proposal is approved by the voters.

**Figure 2  
SHOPP Projects Ready for  
Construction Ahead of Schedule**

*(Dollars in Millions)*

Type of Projects	Projects	Capital Cost
Pavement rehabilitation	20	\$296
Mobility improvements	18	127
Safety	30	125
Stormwater and Americans with Disabilities Act	15	80
Major damage restoration	12	55
Bridge rehabilitation	7	34
Roadside rest area rehabilitation	6	33
Drainage rehabilitation	4	12
Facility improvements	4	11
Landscape rehabilitation	4	11
Erosion protection	2	11
<b>Totals</b>	<b>122</b>	<b>\$794</b>

Source: California Department of Transportation

**LAO Alternative Has Many Benefits. . .**

Bonding against future gas tax revenues to construct SHOPP projects ahead of schedule would have many benefits to the state.

- ***Benefit From Competitive Construction Prices.*** As noted earlier, Caltrans is currently awarding construction contracts for an average of 20 percent less than the estimated cost of the project. Advancing projects to construction sooner would allow the state to benefit from a highly favorable bidding environment. This would result in state savings and at the same time put Californians in the construction industry to work. In addition, accelerating many small projects would likely better capture these cost savings, because small projects typically receive more bids than larger projects.
- ***Fund a Portion of SHOPP Backlog.*** The state has substantial needs for the rehabilitation of the highway system. More timely funding of these needs would provide transportation benefits to the public sooner and may save the state the cost of additional repairs that might be needed if these projects were delayed.
- ***Most Regions Would Benefit.*** The 122 projects are located in 44 counties throughout the state. Advancing these projects would provide construction work and transportation benefits throughout the state. In addition, these projects may better capture the benefits of a competitive bidding environment because they are not concentrated in the same few regions of the state.
- ***No Environmental Exemptions Required.*** In contrast to the Governor's proposal,

exemptions from the environmental review process would not be needed under the LAO alternative. This is because plan-ready SHOPP projects would have completed the necessary environmental review and clearance and would fully comply with state and federal environmental requirements.

**. . .And a Few Challenges**

While our alternative would provide many benefits, we note that it would still have some trade-offs and challenges. Debt service on the revenue bonds would need to be paid from future gas tax revenues. This would leave less funding available for SHOPP projects in future years. For instance, assuming revenue bonds are issued for a 25-year term at an interest rate of 5 percent, the debt service payment would be about \$57 million annually. This amount would equate to about 4 percent of the state's annual funding for the SHOPP program.

Additionally, it could be challenging to issue bonds at this time due to the climate in the nation's financial sector. However, because these bonds would be backed by a stable and dedicated revenue source, gas tax revenue bonds could potentially be issued even in the current financial markets. Furthermore, as we noted above, issuing these revenue bonds would require approval of the proposal by the voters.

**LAO Recommendation**

Despite the above challenges, we think the net benefits of our alternative proposal are significant. Accordingly, we recommend the Legislature enact legislation to place a gas tax revenue bond proposal on the next ballot to provide \$800 million in bond funds to construct plan-ready SHOPP projects.