OCTA

February 15, 2018

To: Legislative and Communications Committee

From: Darrell Johnson, Chief Executive Officer

Subject: State Legislative Status Report

Overview

An amendment is proposed to the Orange County Transportation Authority's 2017-18 State Legislative Platform to sponsor legislation related to disadvantaged communities. An update is provided on a state audit request to analyze fluctuations in transit funding. An overview is provided of a proposed regulatory framework to require the use of zero-emission buses. A summary is provided of the Legislative Analyst's Office report on the extension of the cap-and-trade program. A summary is provided on the cap-and-trade expenditure plan and the Governor's executive order on zero-emission vehicles. A verbal update will be provided on the Governor's fiscal year 2017-18 state budget.

Recommendation

Amend the 2017-18 Orange County Transportation Authority State Legislative Platform to sponsor legislation to clarify how a transportation project may provide benefits to disadvantaged communities.

Discussion

Sponsor Legislation to Clarify Disadvantaged Community Benefits from Transportation Projects

The cap-and-trade program is one of the key policies the California Air Resources Board (ARB) has implemented to meet the greenhouse reduction requirements outlined under AB 32 (Chapter 488, Statutes of 2006) and SB 32 (Chapter 249, Statutes of 2016). Last year the Legislature created increased legal certainty as it relates to the program through the passage of AB 398 (Chapter 135, Statutes of 2017), which extends the authority to implement the cap-and-trade program through 2030. With the enactment of this legislation, it is expected that the revenues generated from the cap-and-trade program will generate anywhere from $2 billion to $7 billion annually through 2030.

Each year, 60 percent of these revenues are dedicated to ongoing appropriations, including five percent annually for the Low Carbon Transit Operations Program (LCTOP), ten percent annually for the Transit and Intercity Rail Capital Program, and 20 percent annually to the Affordable Housing and Sustainable Communities Program. While transit, rail, and other types of transportation projects may qualify for each of these programs, only LCTOP is allocated by formula, while the other programs are competitive grants. LCTOP is allocated pursuant to the State Transit Assistance Formula, with Orange County Transportation Authority (OCTA) receiving about 5.4 percent of the total funding provided each year, based on farebox revenues and population. In the Governor's proposed fiscal year 2018-19 state budget, it is estimated that OCTA will receive about $9.7 million.

Each cap-and-trade funded program must meet specific targets of investment for the benefit of disadvantaged communities (DAC), as defined using the California Environmental Protection Agency's (CalEPA) California Communities Environmental Health Screening Tool (CalEnviroScreen). This tool utilizes a multitude of factors including demographics, health vulnerability, socioeconomic factors, air pollution, pesticide use, water quality, and toxic releases from facilities. Using this tool, CalEPA then identifies census tracts throughout the State that score highest when combining each of these factors. Overall, in the latest version of CalEnviroScreen, Orange County has 69 census tracts within the top 25 percent of DACs, a drop of 17 census tracts from the previous version of the tool. Because census tracts are very small in nature, the vast majority of Orange County is not considered to be a DAC. This further limits where OCTA can use cap-and-trade funding for transportation projects.

The development of CalEnviroScreen was required as a result of the passage of SB 535 (Chapter 830, Statutes of 2012), which first required that a percentage of cap-and-trade funding be used for the benefit of DACs. Later, AB 1550 (Chapter 369, Statutes of 2016) added requirements related to the investment for the benefit of low-income communities, and further limited investments deemed beneficial for DACs to only include investments in projects that are located within a DAC. AB 1550 removed the ability to show a benefit to a DAC by investing in an area surrounding a DAC. The CalEnviroScreen tool requires a statewide definition of a DAC to be used, regardless of whether the tool's criteria is present in each region or if the thresholds vary between regions. This may prevent an investment in what a region may define as its most disadvantaged areas.

Because of the DAC requirements, OCTA has been limited in how it utilizes cap-and-trade funding, including that received for the LCTOP. For the LCTOP formula funds, OCTA has directed most of the funds to transit fare subsidies. Most recently, funding was used for the Santa Ana College Transit Pass Program. In order to fund this program, OCTA was required to demonstrate that at least 50 percent of the students utilizing this program reside in an area considered a DAC, the threshold statutorily required for LCTOP funding. This threshold was barely met even though the college is surrounded by DACs. When analyzing other colleges within Orange County, there are currently no other institutions that would meet this requirement. This is despite the actual income level of the students or financial aid assistance received. If one of the primary drivers of cap-and-trade funding is to boost transit ridership and reduce emissions, the student pass programs can be very effective in allowing for mode shift and attracting new riders. For instance, the survey recently completed for the Santa Ana College Transit Pass Program showed that 88 percent of the students have not used parking on campus since the creation of the pass program. However, the DAC requirements limit the opportunities for such investment. With LCTOP funding expected to grow in future years, this presents an increased challenge for OCTA and other transit agencies.

OCTA also would be limited in funding other transit services that connect DAC residents to major employment centers, educational institutions or healthcare centers, unless the service actually occurs within a DAC. Because most residents of DACs do not stay within their census tract, this presents numerous disadvantages to projects funded by LCTOP and other cap-and-trade programs in meeting the intent to provide residents of DACs transit connectivity benefits. The restrictions the DAC investment requirements present are common issues for many areas of the state, including San Diego, the Bay Area, and the Central Coast area. The topic has been raised numerous times through discussions with the California Transit Association (CTA).

By sponsoring legislation to allow flexibility in the use of cap-and-trade funding for transportation purposes, OCTA can seek opportunities to not only provide additional connectivity options for residents of DACs, but also further reduce emissions. This can include investment in new student transit pass programs; transit connectivity to major centers of employment, healthcare and education; and zero-emission technology. Staff is therefore recommending that the OCTA 2017-18 State Legislative Platform be amended to include the following sponsor legislation principle:

"Sponsor legislation to increase the flexibility in meeting disadvantaged community investment requirements to allow eligibility for projects that improve transit connectivity options."

Initial conversations related to the potential for such legislation have already occurred with Orange County delegation members, CTA, and environmental justice groups. OCTA staff will provide a verbal update of those conversations at the February 15, 2018, OCTA Legislative and Communications Committee meeting.

State Auditor Report Findings on the Local Transportation Fund

Per the direction of the OCTA Board of Directors, and articulated in the 2017-18 State Legislative Platform, on March 3, 2017, Assembly Member Tom Daly (D-Anaheim) and Assembly Member Todd Gloria (D-San Diego) authored a request to the Joint Legislative Audit Committee for the State Auditor to analyze the distribution and assessment of the Local Transportation Fund (LTF), which is imposed under the Bradley-Burns tax as part of the Transportation Development Act. OCTA sought the audit request after observing that the growth rates for LTF revenues, which have historically funded about 50 percent of OCTA's bus operations, were not keeping pace with local transportation sales taxes such as Measure M in Orange County. Since these taxes are assessed differently, it was believed that an increase in internet sales, and potentially other exclusions, could be impacting these rates. Specifically, the audit request asked the State Auditor to analyze the impact the point-of-sale determination for internet sales is having on LTF revenues and how various exemptions and exclusions may be impacting the fund source. The audit request was unanimously approved by the Joint Legislative Audit Committee on March 29, 2017.

On November 30, 2017, the State Auditor released an audit on "The Bradley-Burns Tax and Local Transportation Funds." An official summary of this audit is included as Attachment A. Overall, the audit found the LTF revenue statewide has been steadily increasing, but that some counties disproportionately benefit because of existing state law, with counties who have more warehouses or distribution centers receiving more revenue. The audit's primary finding is that changing the allocation structure for Bradley-Burns taxes would result in a more equitable distribution of local transportation funding, primarily due to the "point-of-sale" assessment structure and the impact from an increase in internet sales. The audit recommends that the state amend the Bradley-Burns tax law to allocate revenues from internet sales the same way they are allocated for local measures, such as Measure M, which is based on the destination of sold goods rather than their place of sale. The findings of the audit predict that, without a change in the law, the current inequities will only grow going forward due to the projected increase in e-commerce. The audit also makes several other recommendations to help increase LTF revenue and ensure compliance with existing law, including the following:

- The Legislature should routinely review and evaluate tax exemptions and other expenditures, eliminating those that are outdated or ineffective. With 160 existing exemptions and exclusions, the audit notes that about $22.5 billion in potential statewide revenue could be put to use. As part of this effort, the audit also recommends that the Franchise Tax Board and Department of Finance should include in their annual report on tax expenditures, the estimated costs of those expenditures before implementation, compared to actual forgone revenues to date.

- Increase the tax base by taxing digital goods and taxing services. The report notes that existing state law is not clear as to whether digital goods are exempted. If it were to be interpreted that they were not exempted, this would produce a minor tax revenue boost. However, the biggest impact to tax revenues would be to tax services, which would result in an extra $3.5 billion in LTF revenue annually statewide.

- In order to increase compliance with existing laws, the California Department of Tax and Fee Administration (Tax Administration) should develop a pilot program to determine the cost-effectiveness of providing monetary incentives to individuals who provide information about businesses with unpaid sales and use tax liabilities.

Many of the recommendations from the State Auditor would require a two-thirds vote due to their classification as a tax increase, including efforts to tax digital goods and services, or remove existing tax exemptions. Other recommendations would require funding being appropriated by the annual state budget, including the recommendation for the Tax Administration to develop a pilot program to report businesses who have unpaid sales and use tax liabilities.

In regards to the State Auditor's primary recommendation to change the situs determination for the assessment of Bradley-Burns tax revenue, this may prove very controversial in some parts of the state that stand to lose revenue. If looking at Bradley-Burns as a whole, this would include revenues for not only the LTF, but also the one percent Bradley-Burns directed to local governments. Currently, it is unclear which cities and counties would benefit or lose by a change in the rules, creating the potential for strong opposition which could handicap a legislative effort.

Potentially, a legislative change could be solely focused on LTF revenues, removing some potential opposition and controversy from local government. However, in discussing the results of the state audit on LTF revenues, the State Auditor noted that in producing the report, they only reviewed data from six different counties and could not produce results for all 58 counties due to strict confidentiality rules associated with this data. In order to assess the viability of a legislative option, more data would be needed to determine which counties could benefit from a change in law. OCTA staff is therefore seeking methods to obtain more information about the other 52 counties. This can be done through two avenues, including providing information to individual counties on how they can obtain the data for their jurisdiction and attempting to seek this information through the Legislative Analyst's Office. Staff will provide updates to the OCTA Board of Directors as different options are analyzed and pursued, including the potential for legislation to be pursued.

Innovative Clean Transit Regulatory Proposal

In 2000, the ARB first issued the fleet rules for transit agencies, mandating large transit agencies with over 200 buses to reduce overall nitrous oxides (NOx) and particulate matter (PM) emissions based on two different fuel paths: the alternative fuel path or the diesel fuel path. Those agencies choosing the alternative fuel path were required to begin converting their fleets to non-diesel fuels, including natural gas, hybrid, hydrogen, or electric, while also reducing overall NOx and PM emissions. Those on the diesel fuel path were not required to purchase alternative fueled buses, but were subject to more accelerated NOx and PM emission reduction standards and were subject to implementation of zero-emission bus (ZEB) pilot programs. In the Southern California region, the South Coast Air Quality Management District opted to have all transit agencies within their jurisdiction proceed under the alternative fuel path, including OCTA.

Also put in place under the initial ARB regulations was a purchase requirement for ZEBs, which mandated those transit agencies following the alternative fuel path to have 15 percent of their purchase and lease agreements be ZEB starting in 2012. This same requirement applied to those agencies opting for the diesel fuel path starting in 2011. However, in July 2009, the ARB deferred the ZEB purchase requirement with a recommendation to first establish technology performance metrics that could be used to assess the commercial readiness and trigger a future purchase requirement. This deferral largely resulted from the advocacy of CTA and its member agencies, including OCTA, who pointed to the lack of technological readiness in broader use, and no identified funding resources at a time where transit agencies were already taking action to cut services and increase fares due to state funding cuts.

Since that time, discussions have continued between ARB staff, transit agencies, technology manufacturers, and other stakeholders regarding the appropriate metrics and path forward that would provide broader integration of ZEBs. Working with the CTA, OCTA and other transit agencies have advocated for a performance-based approach which focuses on actual emission reductions, while also considering funding availability, cost efficiency, and the potential for further technology demonstrations. This approach would also clearly allow for transit agencies to opt out of any requirements due to financial hardship, or if the technology was not performing as needed. While previously ARB staff entertained the potential for a performance-based approach, they have recently moved towards a more aggressive ZEB purchase requirement.

In December 2017, ARB released the Innovative Clean Transit (ICT) Regulation Discussion Document. The ICT proposal seeks to impose an expedited ZEB purchase requirement on all transit agencies within the state, with the goal of achieving fully zero-emission fleets by 2040. Attachment B includes an outline of the requirements proposed under the ICT. While previous iterations of a ZEB purchase requirement were limited to larger urban buses, the ICT would apply to all transit buses, including those used for paratransit service. The regulation would also no longer be limited to transit agencies with 200 buses and over, instead applying to smaller fleets as well. Under the proposed ICT regulation discussion draft, transit agencies would be required to do the following:

- Abide by an accelerating ZEB purchase requirement which takes effect in 2020 for larger fleets with over 100 buses, requiring 25 percent of any bus purchase be ZEB. By 2029, a 100 percent purchase requirement would apply to all fleets.
- Large transit agencies with 100 or more buses would be required to purchase renewable fuels when diesel or natural gas contracts are renewed.
- Include low NOx engines when new bus purchases are made, if available in areas that do not meet federal NOx air quality standards.

While provisions are provided for off-ramps, where an agency can request a one-year extension for compliance, there is not an option for a transit agency to put compliance on hold if the requirements would lead to a reduction in service or other extreme financial hardship, or if funding reductions occur or funding for the increased costs associated with ZEBs is not identified. In addition, while the discussion draft acknowledges the potential for a future performance based option, this is not to occur until after the requirements are already in effect.

OCTA has made significant steps towards the integration of new technology within its transit fleet, including the purchase of ten hydrogen buses and associated fueling infrastructure, addition of low NOx engines on over 100 buses by the end of 2018, and conversion to renewable natural gas for the entire active fixed-route fleet. In addition, OCTA has recently sought funding opportunities to integrate battery electric buses into its fleet, seeking additional methods to test the technology and determine its appropriate use within OCTA's transit system. Despite this progress, the ICT seeks to accelerate the adoption of this technology beyond what is currently in use.

If the ARB adopts the ICT, it would create extreme financial implications for OCTA's transit system. It is currently expected that OCTA will proceed with its next large transit bus procurement after 2020, subjecting the procurement to the new purchase requirements. It is expected that almost 300 buses will be procured at that time. If the ZEB purchase requirement is in place, this could increase procurement costs by as much as $114 million. Overall, to replace our entire fleet with ZEBs, including paratransit, it would cost at least an additional $442 million in current dollars. These estimates assume that there would need to be an expansion of the fleet due to range limitations with existing ZEBs; however, these estimates do not include the costs of infrastructure and potential for increased fueling costs. This would significantly impact OCTA's ability to maintain existing services and could translate to a service reduction of over 20 percent if the additional funding were not identified. Furthermore, there are several technology challenges that continue to exist for these buses, including the inability to meet existing transit bus range requirements, lack of commercially available ZEBs to replace paratransit vehicles, and no guarantee that existing technology will meet necessary warranties to fulfill federal useful life requirements.

OCTA is currently working with the CTA and other transit stakeholders to respond to the ICT proposal, noting the inaccuracies included in the proposal and impacts to transit systems if enacted. OCTA's comments on the ICT proposal are included as Attachment C. Throughout this process, comments will continue to:

- Emphasize the need for additional capital and operating funding to implement any new technology commensurate with the increased costs, and the technology challenges which could impact service
- Detail the implications on transit service and ridership if implemented as proposed, and the associated vehicle miles traveled and disadvantaged community impacts.
- The need for technological advancement to meet the range and reliability requirements of existing transit systems.
- Potential conflicts with bus axle weight limitations.

ARB staff currently plan on holding workshops through the remainder of Winter and Spring 2018, with the goal of a formal regulation going for approval in Summer 2018. Staff will provide updates as discussions continue, including potential alternative pathways that may be considered.

Legislative Analyst's Office Report on the Extension of Cap-and-Trade

On December 12, 2017, the Legislative Analyst's Office (LAO) released a report entitled, "Cap-and-Trade Extension: Issues for Legislative Oversight." The report was written in response to the passage of AB 398, which extended the cap-and-trade program from 2020 to 2030, to help the state achieve its goal of reducing greenhouse gas (GHG) emissions to 40 percent below 1990 levels by 2030. The report identifies five key implementation decisions for the Legislature to evaluate to ensure consistency with legislative goals and priorities, such as: setting post-2020 caps and banking rules to ensure the state meets its GHG targets, setting a hard price ceiling at a level that balances emissions and costs, setting price containment points to moderate price increases, implementing new offset limits, and determining industry assistance factors through 2020.

In addition, the LAO report also finds that the amount of revenue that will be generated from the extension of cap-and-trade is highly uncertain. The range of future revenues could vary by billions of dollars under different assumptions about future allowance prices. The revenues could range from $2 billion to $4 billion in 2018 and from $2 billion to almost $7 billion in 2030. It is expected that one of the priority policy areas the Legislature will address this year will be how to allocate future revenues, with only 60 percent of existing revenues dedicated to ongoing expenditures. Staff will continue to provide updates as these discussions continue.

Cap-and-Trade Expenditure Plan and the Governor's Executive Order on Zero-Emission Vehicles

On January 26, 2018, the Governor released a cap-and-trade expenditure plan for Fiscal Year 2018-2019. The $1.25 billion dollar expenditure plan provides investments in renewable energy, transit-oriented development, environmental restoration, sustainable agriculture, and zero-emission trucks, buses, and vehicles. Specifically, the expenditure plan includes $160 million to the ARB to provide incentives for clean trucks, buses, and off-road equipment, which will also be available for the Carl Moyer Program. The expenditure plan represents the 40 percent of cap-and-trade revenues available for appropriation on an annual basis.

In addition, on January 26, 2018, the Governor issued Executive Order B-48-18, to increase the supply of zero-emission vehicles and charging stations in California. The executive order calls for a new target of five million zero-emission vehicles in California by 2030. The Administration is also proposing a new eight-year $2.5 billion initiative to help bring 250,000 vehicle charging stations and 200,000 hydrogen fueling stations to California by 2025.

Summary

A sponsor bill is recommended related to disadvantaged communities. Updates are provided on State Auditor findings related to local transit funding and a proposed regulation related to zero-emission buses. An overview is provided on a Legislative Analyst's Office report on the cap-and-trade program, the cap-and-trade expenditure plan and an executive order related to zero-emission vehicles. A verbal update will be provided on the Governor's proposed state budget.

Attachments

A. Fact Sheet: The Bradley-Burns Tax and Local Transportation Funds
B. California Air Resources Board: Innovative Clean Transit Regulation Summary
C. Orange County Transportation Authority Comment Letter on the Innovative Clean Transit Regulation Discussion Document to California Air Resources Board Chair Mary Nichols, dated January 22, 2018
D. Orange County Transportation Authority Legislative Matrix

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