

Putting the

Trust

**Back in the
New Jersey
Transportation
Trust Fund**

July 2005

Regional **Plan** Association
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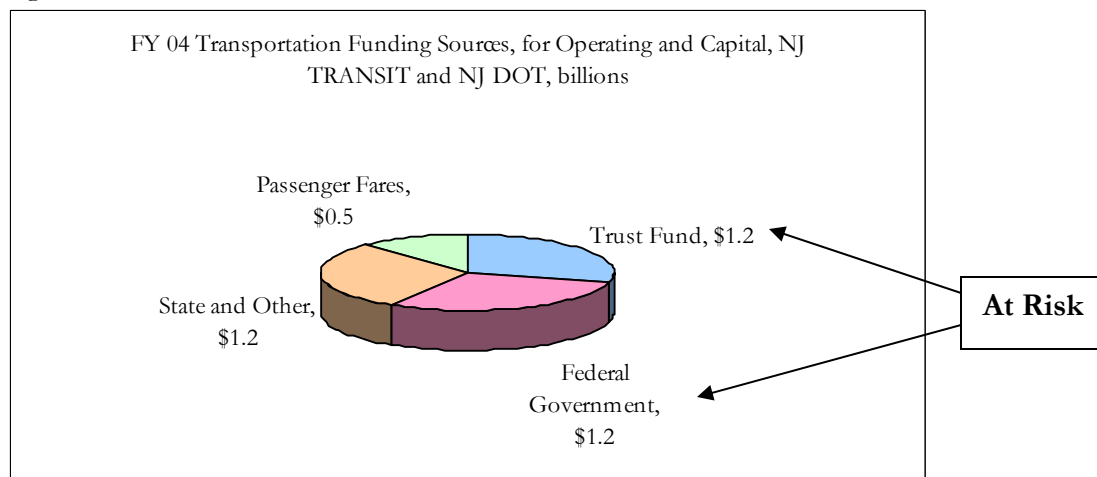
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The Day of Reckoning: June 30, 2006

Though property tax relief and school funding are the fiscal issues that have dominated public debate in New Jersey in recent months, the state’s most pressing financial problem is transportation funding. By June 30, 2006, New Jersey will have exhausted nearly all of the revenue sources it currently uses to pay the capital costs of building and maintaining its roads and mass transit systems. In fact, starting this July (2005), nearly all the state’s gas tax will go towards debt relief. This year, the Trust Fund’s capital generating capacity was stretched to June 30, 2006 through refinancing and GARVEE bonds, further tying up today’s gas taxes and federal funding for future debt service.¹ The State has not sufficiently raised the revenue needed to pay for this past borrowing or to sustain investment going forward. As a result, New Jersey will have to pay for the next generation of infrastructure repair and improvement with new revenue that the Legislature and Governor will have to identify and raise.

Though it seems wildly implausible in the state with the second highest per capita income in the country and annual governmental revenues of many billions of dollars, by the middle of next year, road, bridge, rail, station and tunnel work could be jeopardized in New Jersey. This is a problem of both financing *capital construction* and funding the *operating budgets* of NJ TRANSIT (TRANSIT) and the New Jersey Department of Transportation (DOT). A recently enacted TRANSIT fare increase narrows these gaps, but closing the gaps using only fares and tolls would require abruptly raising them so high as to disallow the ridership needed for a well-functioning transportation system.

Figure 1



In 2004, New Jersey spent about \$4.1 billion on transportation: \$2.7 billion on capital projects, and \$1.4 billion on operations. Thirty percent (\$1.2 billion) of that comes from the Transportation Trust Fund. Another 30% comes from federal sources, many of which require matching funds provided by the Transportation Trust Fund.² The remaining \$1.7 billion comes from a combination of state sources, the Port Authority of New York and New Jersey, fares and other system-generated revenue. In 2006, the Trust Fund will no longer be able to fulfill its mission. Millions in federal matching

¹ Even though its capital generating capacity is quickly approaching \$0, in the first quarter of 2005 the New Jersey Transportation Trust Fund Authority was ranked the number 2 top issuer in the nation, with two bond issues of \$1.7 billion (*The Bond Buyer*, April 4, 2005, page 43).

² These numbers are from the agencies’ FY 2004 adopted budgets, also reported in the Blue Ribbon Transportation Commission report.

dollars are at stake. Much of New Jersey's \$4 billion transportation budget will disappear without the Trust Fund.

Fiscal irresponsibility in Trust Fund management now threatens to end a quarter of a century of unparalleled prosperity and growth in New Jersey. Over the next year, New Jersey will either avoid facing this problem with some patched up financial expedient that, a few years in the future, will leave New Jersey worse off than ever, or take the approach of fiscal responsibility and thoughtful long term investment outlined in this report and spark another quarter of century of growth.

A Transportation-Driven Economy

This issue resonates with all residents of New Jersey, not just government and the transportation industry. Transportation is the driver of New Jersey's economy. There are strong links between accessibility, efficient transportation systems, economic advancement, and standard of living. Everyone has a daily experience with the transportation system, be it on the roads, on train platforms, in bus shelters, or crossing bridges. It impacts the safety of children traveling to and from school, the security of cities served by transit and connected by roads, and the day-to-day speed and ease of life in the state. How people experience the transportation system is critical to the success of the state and the region as a whole. Pot holes, congested trains, infrequent buses, and closed bridges may seem like mere inconveniences in the short term, but in the long term they can add up to economic disaster.

Throughout most of the twentieth century, New Jersey had a nation-leading, highly-competitive transportation system – and a nation-leading economy built upon and supported by that transportation system.³ Today's knowledge-based economy is even more dependent on efficient transportation than in the past. The movement of information in huge quantities and at incredible speeds has generated a need for even more mobility and increased transportation demand.⁴ A key priority of transportation systems is to facilitate the commute of knowledge-based workers, and the key component of the commute is public transportation.

Efficient supply chain management also places enormous demands on transportation systems. Just-in-time inventory control in manufacturing and retailing requires large increases in the volume of truck shipments and deliveries. It is now possible to set very specific daily inventory levels, but the actual adjustment of those inventories requires many more frequent deliveries of smaller quantities than in the past. Roads and bridges are more important to the economy than ever.

**Every increment of economic advancement
demands an equivalent increment
of transportation services advancement.**

The bottom line is that a global economy requires a comprehensive global transportation grid. If New Jersey is not an efficient component of that transportation grid, then it will not continue to be

³ The following section contains excerpts from Hughes, James W. and Seneca, Joseph J. "A Transportation-Driven World-Class Economy: New Jersey at Risk." Issue Paper No. 23, April 2005, attached in Appendix A.

⁴ Initially it was predicted that technological changes would mean people travel less and depend less on transportation infrastructure. These predictions have been proven largely wrong. Similarly, the promise that computerization would create the paperless office was wrong, and paper consumption keeps increasing.

a competitive component of the global economy. A faltering transportation system, like that now faced by New Jersey, will have bleak economic consequences on a very large scale.

New Jersey's Transportation Infrastructure

New Jersey's transportation system is dense, heavily-used, and old. On a per square mile basis there are more miles of highway in New Jersey than in any other state. Its 39,000 miles of highway are more heavily used than any other – on average almost 2 million miles are traveled on each mile of streets and highways in New Jersey, more than doubling in use in the mid-1960s. This intensity of use of New Jersey's road system is more than the surrounding states of New York, Pennsylvania and Delaware, and even more than the auto-oriented states of California, Texas, and Florida.

New Jersey built its highways early. By 1960, four of every five miles of streets and highways in place today were already built (see Appendix B). Most of the system is now 30 to 55 years old, and some of it even older. The state's limited access network (freeway and toll roads) is similarly aging. This 23-year heyday of highway expansion, triggered by funding from the toll roads in the 1950s (the New Jersey Turnpike and Garden State Parkway) and the federal interstate system into the 1970s, has now for all practical purposes ended, the result of a combination of high cost, community opposition and concerns about sprawl. Consequently, this road system – mostly approaching or exceeding a half-century in age – is in constant need of repair, replacement or upgrading.

The average age for New Jersey bridges is 47 years and 40% of all bridges are older than 50 years, the point when major rehabilitation or total replacement typically is in order. Almost one in seven of New Jersey's 2,300 bridges is structurally deficient, with its condition threatened by truck traffic volumes growing and projected to grow by 2.7% per year, which translates into 80% more trucks by 2020 (compared to the base of 1998).

New Jersey's transit network is similarly large and old. TRANSIT was created in 1979 as the nation's only statewide transit agency to assume operation and control of a bankrupt network of private bus and rail companies that were incapable of reinvesting in their infrastructure. New Jersey's public transit network, pieced together from the vestiges of eleven 19th century rail companies and the third largest bus network in the nation, has been the recipient of \$15 billion of capital investment in rolling stock, buses, tracks, signals, stations, parking, and maintenance facilities in the last 25 years. TRANSIT's investment has brought these systems back from near collapse and closer to a state of good repair. The rail system has also been the recipient of funds for several major projects including the Kearny and Montclair Connections, and the Secaucus Transfer that have linked the historically disconnected network, and two new light rail lines.

The transit system today serves multiple functions. Its bus network provides a dense web of routes in urban areas for those without automobiles. In Newark, Jersey City, Elizabeth, New Brunswick, Paterson, Trenton, Camden, Atlantic City, and numerous other cities and towns, buses offer a lifeline of mobility for residents who do not drive or own cars, and often offers a better choice than driving for many. The bus network also delivers thousands of commuters each day to jobs in Newark, Manhattan, and Philadelphia, serving those areas of New Jersey without adequate rail transit.

The commuter rail system is largely geared to delivering commuters to Manhattan, where high paying jobs are made accessible to New Jersey residents and a well educated labor force is made accessible to New York businesses. The newly-built light rail line along the Hudson knits together

the old and newer residential and commercial centers from Bayonne to West New York. South Jersey light rail is intended to spur development in a long-neglected part of the state.

The bus and rail systems, plus the rapid transit systems of PATH in the north and PATCO in the south, are important in removing some cars from the road and relieving congestion. In part due to transit, New Jersey has the fourth lowest vehicle use per capita in the nation after transit-rich New York, highway-poor Alaska and physically-constrained Hawaii. The transit network also benefits the environment by improving air quality, lowering energy consumption, and lessening the pressure to expand highways.

The value of these highway and transit networks is threatened if they cannot provide quality and affordable service. Without adequate resources, disinvestment begins. In the case of the highway network, delays in repairs and stretched-out repaving schedules will force weight limitations on bridges and create bottlenecks at outmoded interchanges. Poor, unreliable driving conditions will diminish the attractiveness of the state to both residents and businesses.

Faced with funding limitations, the transit network can easily fall back to the days of perpetually late trains and buses, as infrastructure is unattended and maintenance schedules are extended. These limitations can slow or stop the expansion of the network into areas now without transit. Lack of funding can also limit peak period (rush hour) capacity where it is most needed, most notably across the Hudson River.

How did the Transportation Trust Fund go broke when millions are collected each year in gas taxes?

**Too many demands;
too few resources;
insufficient accountability.**

The Trust Fund started out in 1984 as an experimental solution to the need for capital investment in transportation. It was intended as an antidote to highly unstable and insufficient funding. The Trust Fund Authority became responsible for issuing bonds and investing Trust Fund revenues, but was not charged with participating in the development or management of the capital programs at DOT or TRANSIT, and was not to be involved with the management of federal funds. The Trust Fund did not address operating costs, leaving those to the General Fund. The Trust Fund was only to be used for capital projects, such as rebuilding bridges, highway rehabilitation and expansion, transit system improvements and new rail cars and buses. Operations, including maintenance and day-to-day personnel costs, were not to be paid for out of the Trust Fund. It was also to function primarily on a pay-as-you-go basis: the revenue coming in to the Trust Fund was to be mostly spent as it was collected, not borrowed against.⁵

At first, the Fund was soundly managed, on a self-replenishing basis, by an investment program that used a fraction of the funds to pay debt service on bonds and the majority for pay-as-you-go transportation investment. Then policy makers directed the Trust Fund to stray from its original intentions quite dramatically. Now, not only has the Trust Fund borrowed against most of its \$805

⁵ Chief Financial Officer. Background Report: History and Status of Transportation Trust Fund Legislation and Financing. New Jersey Department of Transportation, March 2003.

million in revenue sources so that its capital generating capacity is about to end, but it has diverted some of its spending to fill large gaps in operations. The Trust Fund has effectively begun paying for operations. In household terms, New Jersey is taking out a home equity loan to pay for its heating bill.

New Jersey faces the 2006 day of reckoning because while the capital program was growing over the last 20 years, constitutionally dedicated revenues to the Trust Fund were stagnant and statutorily dedicated revenues stopped being appropriated. The capital program was five times larger in 2005 than in 1985. During these 20 years of growth, the State only increased taxes for transportation purposes once (the 2.5 cent gas tax increase in 1988). To make up for the increasing demands and decreasing revenues, the Trust Fund Authority increased its use of bonding, using larger bonds with longer maturities. **The core of the problem was that, starting over a decade ago, leaders chose short-term responses such as tax cuts, one-shot deals, and no toll or fare increases, over long-term solutions.** A race to the bottom ensued and for many years it was thought to be political suicide to be identified as a supporter of revenue increases and other fiscally prudent measures.

Tax cuts were sold as free and painless, not as something that would inevitably require major cutbacks in state government spending. Budgets were balanced by shifting money for capital construction to basic operations. Fares were not allowed to increase to keep pace with inflation and other expenses, for fear of voter backlash. As the bills came due, New Jersey engaged in a series of increasingly dubious fiscal maneuvers including massive borrowing, pushing expenses onto local government, and depleting reserves.

The Transportation Trust Fund, designed to be New Jersey's stable, predictable and sufficient source of transportation investment, was sacrificed. The recession of the early 1990s and New Jersey's increasing needs for transportation investment applied pressure on the Fund's initially prudent management. Borrowing was substantially, but temporarily, increased.

In 1995, the state prepared to embark on an ambitious spending program including three TRANSIT light rail projects. The state government, however, was unwilling to raise taxes or fares and to tell New Jersey residents that the logical consequence of a costly program and no new revenues would eventually be a reduced program and more costly services. The state government departed from using pay-as-you-go funding for transportation capital projects in favor of using most of the Trust Fund revenues to support the issuance of long-term transportation bonds. This switch to long term borrowing allowed the transportation capital program to virtually double, but obscured problems in the TRANSIT operating budget and avoided the need to do what should have been done: increase revenues in an orderly way.

In 2000, Trust Fund renewal gave New Jersey a chance to right the foundering Transportation Trust Fund, but it made no fundamental reforms. Instead, leaders further increased the size of the program, dedicated revenues from the General Fund (raising the constitutionally dedicated annual revenue to \$805 million), continued the diversion of capital into the operating budget and bonded most of the available revenue. As problems mounted in the annual state budgeting process, the state next reduced the appropriated amount of operating assistance to TRANSIT, and ceased appropriating \$114.5 million in statutorily obligated funds to the Trust Fund. During the last four years those policies were not reversed: TRANSIT operating funds remained far too low and the Trust Fund lost a major dedicated revenue source.

The Trust Fund is down to \$0 capital generating capacity.

Figure 2

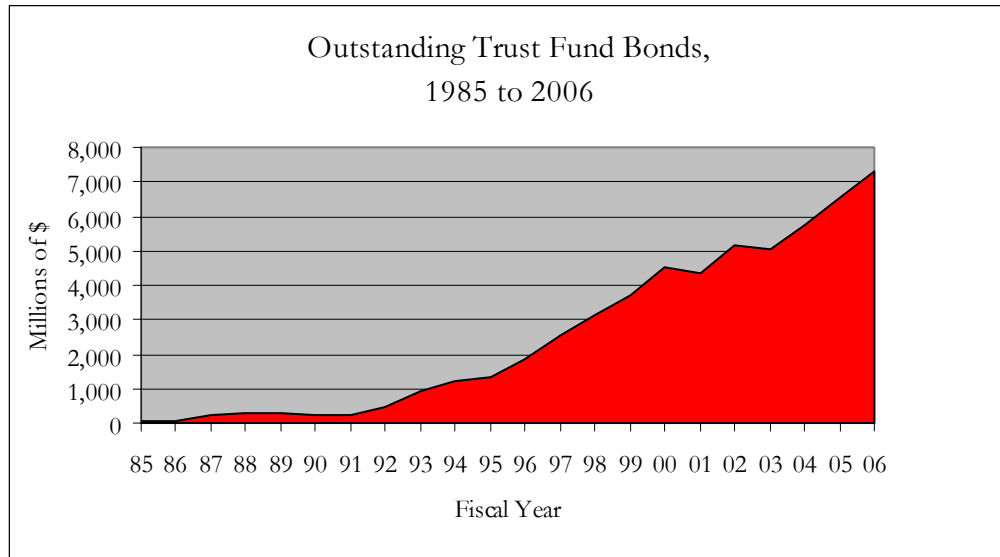
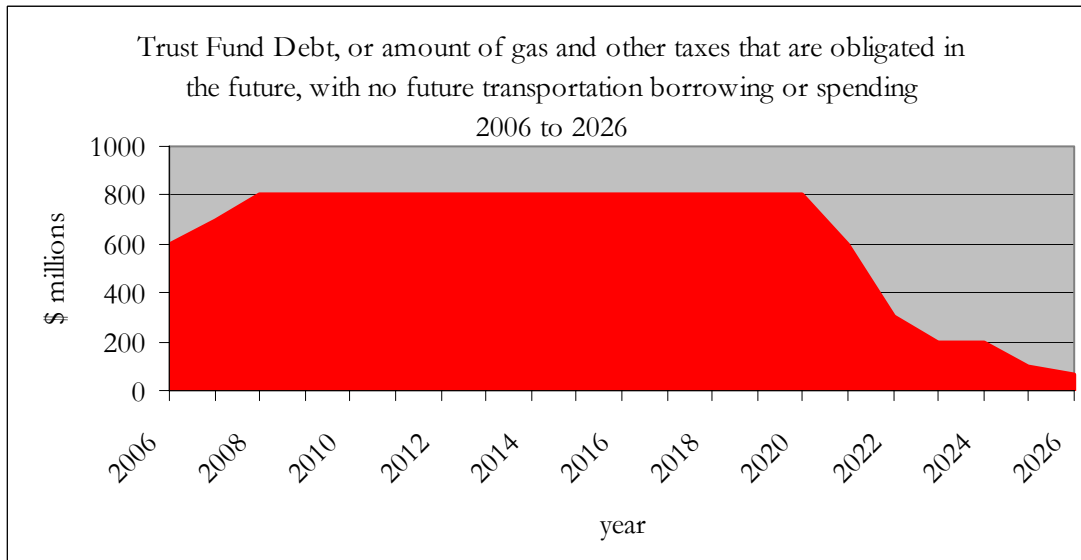


Figure 3



Now, with all of the Trust Fund's revenues pledged to repay bonds, New Jersey is stuck with an \$805 million dollar a year bill for debt service that must be paid faithfully through 2021, leaving no money for new transportation investment.

The simple fact is that the responsibility for New Jersey's transportation funding crisis is bipartisan, just as is the responsibility for fixing it.

The day of reckoning is just around the corner. The Transportation Trust Fund will be bonded out at the end of this fiscal year, June 30, 2006. An attempt to increase the gas tax to add new funds at the end of 2003 was unsuccessful despite a forceful and sobering report from the Governor's Blue Ribbon Transportation Commission. The Trust Fund remains broke, and the clock is ticking towards transportation investment shutdown and abrupt and painful increases in TRANSIT fares.

An Honest Assessment

New Jersey's transportation system is under assault from a massive fiscal cancer. Treating it will require facing painful and difficult choices. But ignoring it will be so much worse.

If New Jersey is to maintain the transportation infrastructure that was the foundation of its prosperity in the last quarter century, it must invest billions of dollars over the next ten years. This means major new revenue sources must be identified and put in place to support transportation – both operations and capital programs. But just as tax cuts come with an obligation to face the issue of spending cuts, revenue increases impose a commensurate obligation: to prioritize proposed expenditures strategically and insure they are spent productively, so that proposed revenue increases are balanced against needs and kept affordable and reasonable. Sacrifices have to be made, and decisions should be based not on anxiety about the next election but on what will provide the most benefits for New Jersey taxpayers at the least cost in the long run.

To win public confidence in such an undertaking, advocates of revenue increases must offer a credible program for safeguarding the financial management of these resources. Considerable public skepticism exists about the political leadership's past management of the Transportation Trust Fund. DOT and TRANSIT have been expected to meet too many demands with too few resources. Structural reforms are a necessary, integral part of that Trust Fund reauthorization. To restore the long-term fiscal health of New Jersey's transportation system, fiscal and programmatic accountability reforms must be put in place. Mechanisms should assure that the Trust Fund's capital-generating capacity is sustained, that sound projects are selected for investment and that operating expenses are properly addressed. To be effective, those mechanisms must be transparent and sufficiently independent from political pressures.

How to Approach the Crisis

The three most important elements are restoring long term bondability to the Transportation Trust Fund, eliminating the use of capital funds for operating expenses, and providing for clear financial transparency and accountability.⁶

The task at hand is not as simple as raising the gas tax to finance the \$1.2 billion per year provided by the Trust Fund in Fiscal Year 04. The question needs to be first, what reforms would assure the public that its tax money is being managed responsibly this time around; and second, what level of transportation spending is necessary to maintain New Jersey's transportation operations and economic vitality.

**Without reform, the Trust Fund can
easily empty out to \$0 again,
even after taxes are increased.**

The Trust Fund is managed with insufficient oversight and accountability. The transportation budgeting processes are not connected to the capacity of the Trust Fund. Ambitious capital programs have been approved alongside structurally deficient operating budgets. The public does not know how much is collected from its gas and other transportation taxes, nor how the taxes are spent.⁷ Improved accountability is necessary to prevent the Trust Fund Authority from repeating the cycle and once again incurring enough debt to propel the Trust Fund to functional insolvency.

⁶ New Jersey was ranked second to California in having confusing accounting for its transportation resources, according to a study from Rutgers University: Glenn Beamer. "A Comparative Analysis of New Jersey Transportation Funding And Debt Management." Draft February 14, 2005.

⁷ While some information is available about expenditures of a portion of the gas tax, auto sales tax and other related taxes, the full amount collected and its use is not clearly reported.

How NOT to Approach the Crisis⁸

(1) No New Taxes: What happens if New Jersey waits out the current crisis?

To highlight the need for new revenue and reform, let's assume that in 2006, New Jersey fails to raise revenues and waits for its current debt obligation to ease up so that current taxes once again become feasible sources of new spending. DOT and TRANSIT lose all but their system-generated revenues such as fares, fees and advertising. Billions of federal matching dollars are lost. System reliability and quality of operations declines. Since a large part of transportation operations are still relying on Trust Fund transfers, DOT is reduced to simple snow removal; bridges and roads badly in need of maintenance begin to crumble, some fail entirely and many are closed to traffic. TRANSIT cuts back service substantially and increases fares sharply. The roads become even more clogged as many would-be transit users are forced back into their cars by an unreliable, overpriced, infrequent transit system. Capital projects all but cease for the next ten years. Huge numbers of construction, logistics and other jobs are lost, and the economy suffers the hit. Needed expansion projects such as the Trans-Hudson Express Tunnel are delayed, and the region's businesses begin to look elsewhere for opportunities to grow. In short, the region backslides into an era of disinvestment and neglect, harming New Jersey's economy and quality of life. After 15 years, when the debt obligations finally ease, the Trust Fund can bond out all its resources, as it has done in the past, and once again ensure that New Jersey's transportation system will be stymied in the future.

(2) Business As Usual: What happens without structural and institutional reform?

What might happen if, in 2006, New Jersey raises the gas tax but does not implement any reforms? Let's assume that New Jersey raises the gas tax by 12.5 cents in 2006 and constitutionally dedicates it to the Trust Fund. The increase of 12.5 cents would raise about \$562 million per year. Assuming that the agencies' spending level remains at \$1.2 billion again as it was in FY 04 and increases at the rate of inflation, the 12.5 cent increase would only fund the transportation system for six years. In 2011, it would have to be increased substantially again. In reality, it would probably run out much sooner. Without reforms, at least part of the \$562 million would leak into the General Fund. Without an independent entity such as the recommended five person Financial Policy Review Committee, the Trust Fund Authority could bond nearly all new revenue as it became available to support higher spending levels. Revenue might be less than expected: imposing a large increase in the gas tax all at once would likely deter some driving. In addition, since the tax is collected per-gallon, improved fuel efficiency might lead to lower revenue streams over time and an even greater share of the gas tax going to cover old debt. Over \$300 million per year would continue to be diverted to cover operating costs. The statutorily dedicated funds of \$114.5 million per year which were originally dedicated to the Trust Fund would continue to leak out into the General Fund. Without reports from the Director of the Division of Taxation, the public would still have no clear picture of how much their gas taxes raise. The increase of 12.5 cents would be fully obligated to pay debt until 2035.

Neither of these options is acceptable.

⁸It is assumed that gas consumption holds steady at 2003 levels, that the Trust Fund bonds out for 20 years at 1/10 debt service ratio, that inflation is 4% each year. All numbers on this page are rough estimates.

Guidelines

The management of the Trust Fund needs to be dramatically reformed in its next reauthorization. The way financing takes place and the amount and method of revenue collection also must be overhauled. There are several major points that will stand out as this report details its recommendations:

- The Trust Fund should not require a major overhaul again for at least 25 years.
- The operations structural deficit, particularly at TRANSIT, must be addressed, or it will undermine the capital budget. Public funding for the operations needs should be significantly expanded in the short term and continued for the long term
- A diversity of revenue sources should be used, not just the gas tax, to ensure adequate revenue levels and distribute the burden of paying for the transportation system more widely across the state.
- The TRANSIT rider must be part of the solution. TRANSIT fare increases should be predictable and related to normal growth in expenditures.
- Wherever feasible, transportation users who impose higher environmental, social, and economic costs should pay a higher share of the transportation costs.

The Bright Side

New Jersey's investment in transportation infrastructure over the last 20 years has been tremendously beneficial. If the leadership fixes the Trust Fund now, New Jerseyans can expect an improved quality of life in the short and long term. In the short term, new revenues supporting the Trust Fund will translate to better roads and bridges, more buses and trains, cleaner facilities and a safer system overall. In the long term, New Jersey residents will see an improved quality of life, with less road congestion, an expanded transit system, a healthier environment, and a thriving economy.

A fully-funded transportation system can help New Jersey sustain even greater economic growth by promoting smarter settlement patterns. New Jersey is fortunate to have accepted, for the most part, the tenets of smart growth. Anti-sprawl sentiment is fairly strong, and even non-transit riders acknowledge the importance of investing in a strong transit network. State Transportation Commissioner Jack Lettiere has been awarded the 2005 New Jersey Future Smart Growth award, in recognition of the "significant shift in transportation decision-making toward the use of modern, community-friendly and environmentally sound solutions to New Jersey's transportation problems."⁹ Fixing the Trust Fund now can make New Jersey one of the nation's most desirable locations for residents and employers 20 years down the road.

Voters have shown they are willing to pay for better transportation infrastructure.

In November 2004, voters in 11 states faced local ballot initiatives to fund transportation. They overwhelmingly voted in favor of spending more on transportation, be it through taxes or tolls, toward transit or road improvements. Voters approved billions of dollars for light rail in Miami, commuter rail in Austin, and a monorail in Seattle, to name a few. The *USA Today* headline read, "Red state or blue, Americans sick of gridlock." A closer examination of the ballots reveals that

⁹ See NJ Future's website at <<http://www.njfuture.org/articles/SGAs.htm>>

well-balanced proposals meet with success even where the public has rejected proposals in the past. In California, for example, local ballot initiatives need a supermajority of 2/3 to prevail. The strict requirement forces pro- and anti-growth parties to negotiate on ballot measures and bring high quality proposals to the people. Prior to the supermajority requirement, only half the ballot measures in California passed. Now that the bar has been raised, Californians are more often voting yes on the taxes and tolls put before them. Why is this good news for New Jersey? It shows that voters in a diverse state with a diverse set of transportation needs will support taxes and tolls when they know the money is going directly to their transportation system.

What do the agencies need?

New Jersey's transportation needs are substantial. New revenue is needed for both capital construction and day to day operations. Over the last 15 years, New Jersey saw increasing demands put on its aging roads, bridges and rails as well as the continuing need to replace and expand its transit fleet. Over the next 20 years, more can be expected; New Jersey's population and labor force are expected to grow significantly, leading to increases in travel demand. This growth needs to be absorbed in a state with a dense, old, and very heavily used transportation system.

Some of the 10-year needs are listed here. The full capital needs statements can be found in Appendix C, the Capital Improvement Strategy (March 2005). The Transportation Trust Fund has typically provided for about half the cost of the capital programs and projects. Operating needs are not stated in any official document, but can be estimated based on past expenditures, anticipated deficits and system-wide shortfalls.

Capital Needs

Roads: Less than half of the highway pavement in New Jersey is rated "acceptable," below the national average as well as the ratings for New York, Pennsylvania, Connecticut and Delaware. The Blue Ribbon Transportation Commission two years ago concluded that, absent substantial new investment, the current 47% acceptable rate will wither to 10% within a decade. The need at that time was identified as one billion dollars a year for 10 years.

Bridges: When the Blue Ribbon Transportation Commission completed its work in 2003, 87% of the state's bridges were rated as in "acceptable" structural condition; two years later, DOT reports that inventory has dropped to 83%. Even if funding is maintained at the current rate of \$300 million per year, the number of acceptable bridges will continue to decline to 81% within a decade. Without further investment, the number will fall to 73% over that same time, according to DOT. The Blue Ribbon Transportation Commission identified the bridge need number at \$7 billion over 10 years.

Municipalities: Largely funded by the Transportation Trust Fund, the Local Aid program has made many local road improvements possible. Local Aid applications now far outstrip funding. For example, in FY 05 DOT was able to approve less than half the 829 municipal aid funding applications it received and award less than one third of the \$198.5 million in funding requested. The Safe Streets to School program drew 227 applications for \$37.7 million in funding; DOT could award only \$4 million for 45 proposals. Without renewal of the Transportation Trust Fund, county and municipal governments will have to rely on local property taxes to undertake such projects or abandon them altogether. These projects are estimated to cost \$3.7 billion over ten years.

Transit: Over the next ten years, TRANSIT will need over \$6 billion to bring its system to a state of good repair and maintain it at that level. This includes replacing 13 miles of track each year, working on a backlog of bridges and other structures that need repair or replacement, updating the signaling system, modernizing the bus and rail fleet, and rehabilitating stations. An additional \$9 billion is needed to increase and expand core system capacity. Much of this will come from the federal government and other sources, but only if the Transportation Trust Fund can provide matching funds.

Other: DOT also has substantial ten year capital needs to continue and enhance program areas including pedestrian and bicycle, safety, maritime and aviation, and rail freight. TRANSIT has safety and customer service/technology needs as well. Both agencies have mandatory expenses, such as equipment and rolling stock leases, that will increase over time.

Operating Needs

Both TRANSIT and DOT have severe operating deficits. The TRANSIT practice of using capital funds to fill the gap has weakened its ability to meet its capital objectives. DOT's operating budget shortfalls have serious consequences on routine maintenance and basic operations. For example, the drainage system for roads and bridges should be cleaned once annually, but, given DOT's low operating budget, only 10% of the system is cleaned annually, usually when severe flooding occurs. The failure to perform adequate preventative maintenance has a multiplier impact on capital infrastructure repair and rehabilitation costs: as operations are under-funded, capital needs increase. For DOT, using capital funding for operations often leads to the use of more expensive contractors and fewer agency employees. The total net need for operations at DOT and TRANSIT, including ceasing the practice of capital-to-operating transfers, will be \$8.3 billion over ten years.

The capital and operating needs of both agencies are summarized in Table 1.

Table 1

\$ Billions	Operating		Capital		Total
10 Year Gross Needs, after eliminating capital-to-operating transfers					
DOT		4.50		26.60	31.10
TRANSIT		17.10		14.70	31.80
Total		21.60		41.30	62.90
Anticipated and Recommended Non-Trust Fund Resources					
DOT	Anticipated State aid & fees	1.17	Anticipated Federal aid	8.83	10.90
	Anticipated Federal aid	0.90			
TRANSIT	Fares & other system-generated revenue	7.05	Port Authority, for Trans-Hudson Express Tunnel	4.07	19.69
	Recommended fare increases	1.35	Anticipated Federal aid	4.43	
	Anticipated State aid	2.79			
Total		13.26		17.33	30.59
10 Year Needs, Net of Anticipated non-Trust Fund resources listed above.					
DOT		2.43		17.77	20.20
TRANSIT		5.91		6.20	12.11
Total		8.34		23.97	32.31

Non-Trust Fund Revenue

The agencies will not rely exclusively on the Transportation Trust Fund over the next ten years. They can anticipate support from the federal government, the state, the Port Authority, fares and other system-generated revenue, and other sources. TRANSIT anticipates federal sources including full funding grant agreements, formula funds, and CMAQ¹⁰ funds will bring in \$4.43 billion for its capital program over ten years. TRANSIT also optimistically anticipates another \$4 billion from the Port Authority of New York and New Jersey for the Trans-Hudson Express Tunnel (ARC) project. On the operating side, TRANSIT can count on revenue from fares and other system-generated revenue. Another optimistic assumption, given state budget deficits, is that the state will contribute \$2.8 billion over ten years from casino revenues and the General Fund for TRANSIT operations. DOT anticipates federal funding will cover \$8.8 billion of the capital program.¹¹ On the operating side, federal funds are anticipated to cover \$900 million, the state General Fund is expected to cover \$1.07 billion, and fees and other sources will cover \$108 million.¹²

The operating budget needs are estimated to be considerably higher than current appropriations. This is due to the addition of \$200 million to DOT's long-starved operating budget and the elimination of over \$300 million in capital-to-operating transfers. It is assumed that this report's recommended TRANSIT fare increases are implemented, decreasing the gap by approximately \$135 million per year.

These program levels are much higher than they have been in the past. The table below shows average yearly expenditures since 1997.

Table 2

Past Programs, average year (in 2004 dollars, billions)	
DOT Operating	\$ 0.28
DOT Capital	\$ 1.49
TRANSIT Operating	\$ 1.13
TRANSIT Capital	\$ 0.99

There are several reasons the next ten years of transportation spending will be higher than in the past. First, past programs incorporated capital-to-operating transfers. Their strong bias toward capital and away from operating skewed the actual size of the programs; operations were starved, and future programs should not continue this pattern. Second, there have been, from time to time, influxes and contractions of revenue that affected the size of programs, making it difficult to compare past and future programs. Third, future programs are consistently larger because they include continuing expenditures for the multi-year projects initiated in past programs. Some projects requiring one-time large expenditures were started and finished within the last 10 years. Other large expenses are expected to occur over the next ten years, including major bridge repair costs and a need for new capacity crossing the Hudson as the region continues to grow (the Trans-

¹⁰ Congestion Mitigation and Air Quality program

¹¹ \$8.8 billion assumes federal contributions will remain at the levels anticipated in the State Transportation Improvement Plan for 2006 through 2008.

¹² These estimates, \$900 million state general fund contribution and \$108 million contribution from fees and other sources, are based on average past NJ DOT operations revenue, 1994 to 2004.

Hudson Express Tunnel). The final reason is debt – a mandatory expense pushed into future years, making future program needs larger.

Financing for Fiscal Responsibility

This report recommends the capital program be initially financed with short-term bonds, with a switch several years out to a mix of pay-as-you-go and longer term bonds.¹³ This report further recommends that capital-to-operating transfers are eliminated. Assuming these two recommendations are implemented, and substantial non-state funding is available for the Trans-Hudson Express Tunnel project, **a stable and sufficient capital program can be achieved over the next 10 years with an average of \$2 billion in new revenue annually.**

Note on the Trans-Hudson Express Tunnel: Four billion dollars of TRANSIT's gross capital need is for the Trans-Hudson Express Tunnel (also known as Access to the Region's Core, or ARC). This project is critical to the economy of New Jersey and has been demonstrated to be in the interest of the state to "spend money to make money". Regional Plan Association has written two reports that detail the value for a new passenger rail tunnel.¹⁴ The full case will not be repeated here; in short, the new tunnel is the only means to gain the capacity for New Jersey to tap into the huge and continually growing economic engine of Manhattan. TRANSIT's consultants concluded that the tunnel will generate \$15 billion of economic benefit by 2025 and \$25 billion by 2035, equally divided between New York and New Jersey.¹⁵

\$8.35 billion is needed for operating expenses over the next ten years. These are divided between DOT's need of \$2.4 billion and TRANSIT's of \$5.9 billion. This full amount will have to come from pay-as-you-go sources. Fiscal prudence dictates that operating expenditures should not be met with borrowed funds. The Blue Ribbon Transportation Commission has recommended that 50% of the capital program be met with pay-as-you-go funds. However the Blue Ribbon Transportation Commission report did not fully account for operations. This analysis recommends meeting all actual operating expenditures with pay-as-you-go funds, and completely eliminating capital to operating transfers. This alone would make the Trust Fund more fiscally responsible than ever.

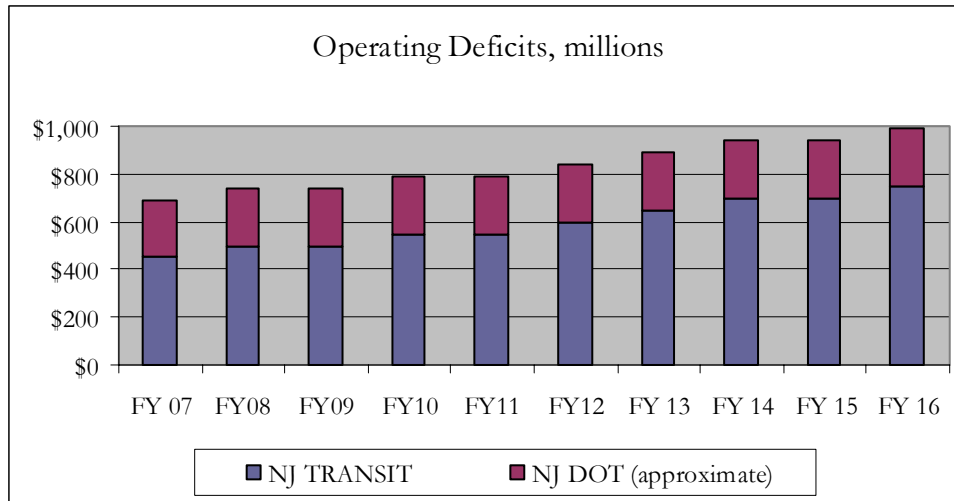
As shown in Figure 4, the cumulative operating needs are projected to grow over time, so that the revenue demand would be lower in the earlier years of the 10-year period and higher in the out years. In FY 07 the new revenue need for transportation operations is projected to be \$740 million.

¹³ It is assumed that the Trust Fund uses 10 year bonds for the first five year with a 0.14 debt service ratio and then switches to 20 year bonds with a 0.083 debt service ratio, and that 20% of the capital program will be funded with pay-as-you-go sources starting in 2016.

¹⁴ *The Case for a New Passenger Rail Tunnel Under the Hudson River*, December 2003 and *Connecting Workers to Jobs: the Port Authority's Role*, March 2005.

¹⁵ Economic and Fiscal Impacts of the ARC Project, Economic Research Associates, November 10, 2004

Figure 4



In summary, the new transportation revenue need begins at \$2.69 billion annually in FY 07, increasing to \$2.99 billion in FY 16.

Taking all the non-Trust Fund anticipated revenue sources into account, New Jersey will still have a gap of \$32.31 billion over the next ten years. This estimate assumes the capital-to-operating transfers are eliminated, uses optimistic estimates of ARC, federal, and state General Fund funding, and assumes this report’s recommended fare increase.

Table 3

Annual Net Needs, millions	Operating		Capital	Total
	NJ TRANSIT	NJ DOT (approximate)	New revenue needed given bonding (approximate)	New revenue needed
FY 07	\$450	\$240	\$2,000	\$2,690
FY08	\$500	\$240	\$2,000	\$2,740
FY09	\$500	\$240	\$2,000	\$2,740
FY10	\$550	\$240	\$2,000	\$2,790
FY11	\$550	\$240	\$2,000	\$2,790
FY12	\$600	\$240	\$2,000	\$2,840
FY 13	\$650	\$240	\$2,000	\$2,890
FY 14	\$700	\$240	\$2,000	\$2,940
FY 15	\$700	\$240	\$2,000	\$2,940
FY 16	\$750	\$240	\$2,000	\$2,990

To meet this new revenue demand, New Jersey's leaders and its citizens will be faced with hard choices.

**Before considering how the revenue will be raised,
the public needs assurance that
this crisis will not recur in the future.**

Major reforms are necessary to restore trust to the Trust Fund. DOT and TRANSIT should be able to assure the public, the Trust Fund Authority and the recommended five-person Financial Policy Review Committee that their needs statements include fully funded operating budgets. DOT and TRANSIT should use a 'fix it first' principle, which they have indeed been moving toward, to bring the system closer to a state of good repair. DOT should limit road capacity expansion to truly smart growth projects. While TRANSIT should not avoid meeting capacity needs with projects such as the Trans-Hudson Express tunnel (ARC), it must carefully consider stretching out or postponing projects past the 10-year forecast period. TRANSIT needs to determine what projects cannot be demonstrated to meet an immediate need or to be cost effective if built in the next ten years. Bond-ability should be permanently restored to the Trust Fund. The public should know exactly how much is collected from its taxes and how it is being spent.

REFORM

There are four main reasons the Trust Fund went astray. These substantiate the need for the recommended reforms.

- 1. Growth of capital program without commensurate increases in revenue,**
- 2. Insufficient funding from non-Trust Fund sources for operations,**
- 3. Leakage of Trust Fund revenue sources into the General Fund,**
- 4. Lack of accountability and independent oversight.**

1. Growth of capital program without commensurate increases in revenue

The size of the DOT and TRANSIT capital programs has increased dramatically in the last 20 years. The portion funded by the Transportation Trust Fund has grown from \$250 million in 1985 to \$1.2 billion in 2005, five times its original size. This is despite the fact that the Trust Fund reauthorization in 2000 envisioned a \$950 million annual program.

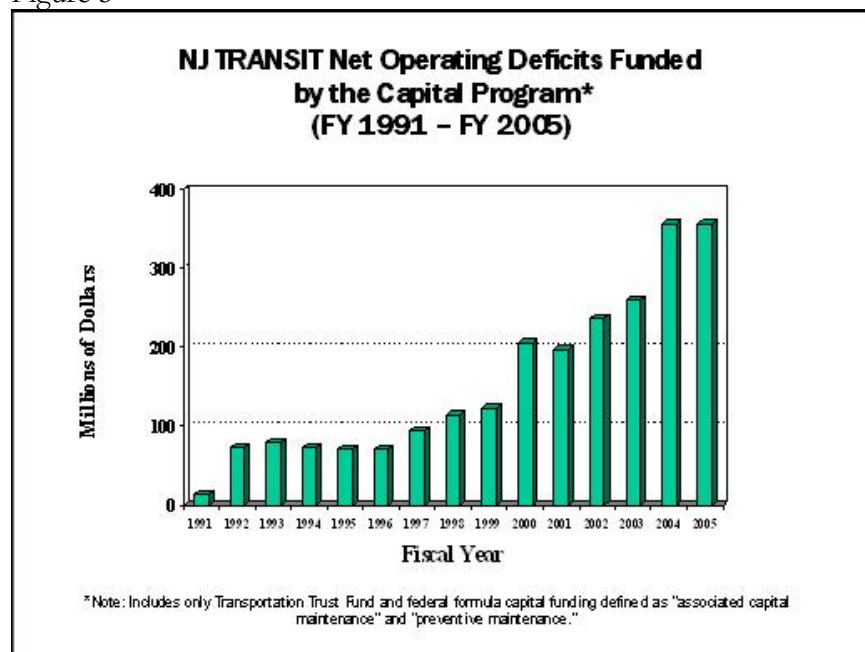
In New Jersey, capital plans are adopted without oversight from the Trust Fund Authority. Nonetheless, programs are routinely adopted that maximize use of revenue available from the Trust Fund. Over the years, a series of reauthorizations increased the bonding capacity and lengthened the terms of bonds that could be issued by the Trust Fund Authority, thus providing more and more revenue for capital programs. The TRANSIT New Starts program developed at this time was very ambitious, and the DOT capital programs grew steadily as well. However capital expansion leads to increases in operating and maintenance expenditures. The agencies did not account for the full future cost of the capital programs adopted in the last 10 years. Revenues were not increased; while capital and operating needs grew, fares remained static and only one new constitutionally dedicated revenue sources increased (the gas tax, by 2.5 cents, in 1988). Instead of new revenue sources, the Trust Fund Authority used longer bond terms to issue more money, tying more of it up in the future. While costs went up, the capital generating capacity of the Trust Fund went down.

TRANSIT capital program growth offers a good example. In 1999 and 2000, a major source of operating funds was terminated by federal mandate.¹⁶ Operating deficits grew, and instead of being filled with fare increases or legislative appropriations, they were filled with diverted federal and state capital funds. This depleted the amount of capital funds actually available for capital projects substantially (about 30%). TRANSIT was incurring debt on the capital side to pay for rolling stock acquisitions, further restricting \$100 million per year in capital funds, and depleting the amount available for capital projects. With only 50% of capital funds left for capital projects, and no programmatic oversight from the Trust Fund Authority, TRANSIT approved several expensive light rail projects including the South Jersey Light Rail and the Hudson-Bergen Light Rail. These New Starts were premised on optimistic anticipated revenue estimates and TRANSIT believed they would not take much away from the rest of the capital program. In the end the anticipated revenue came up short, and the light rail projects cost nearly \$2 billion – much more than anticipated, mostly due to the South Jersey Light Rail – in state and federal funds that could have been used on other capital projects. More than 2/3 of capital funds had been spent on supporting the operating budget, paying for debt, and funding ambitious new projects based on flawed assumptions. The Trust Fund Authority was not established with the intention of overseeing programmatic decisions, and without this oversight TRANSIT’s program grew even as it was becoming increasingly consumed with debt and mounting operating deficits.

2. Insufficient funding from non-Trust Fund sources for operations

TRANSIT anticipates it will need to move \$310 million per year from its capital resources to subsidize operations if the current transportation funding structure remains unchanged. This is a conservative estimate. (Note that approximately one-half of this money has come from federal formula funds, not the Transportation Trust Fund.) TRANSIT’s capital-to-operating transfers have increased over time, as shown in Figure 5.

Figure 5¹⁷



¹⁶ Leveraged leasing proceeds

¹⁷ Source: Blue Ribbon Transportation Commission report, 2003.

TRANSIT recognizes that using funds intended for capital programs on operations is problematic, and its current plans cap the amount that can be transferred from capital to operating. For its operations needs, DOT receives a small contribution from the state General Fund, and another small portion from the Federal Highway Administration for permitted operating expenses related to specific capital projects. DOT's operating budget has used between \$50 and \$80 million per year of Trust Fund revenue. Even at this level, however, DOT's operations are under-funded. This affects the system as a whole. The failure to perform adequate preventative maintenance has a multiplier effect on capital infrastructure repair and rehabilitation costs: as operations are under-funded, capital needs increase.

Capital-to-operating transfers are both against the original intention of the Trust Fund and inefficient. From an operations point of view, using capital funding often leads to use of more expensive contractors and fewer regular employees. From a budgeting point of view, the true operating cost of the system is obscured by the use of capital funds; fare-setting, legislative appropriations and other policies that should be based on true operating costs get skewed by the practice. Finally the public trust is lost by using Trust Fund monies for other-than-intended purposes. The public is justified in its suspicion that its contributions to the Trust Fund, mainly paid at the pump, are not dedicated to bringing the system to a state of good repair or for expanding it to provide more services.

Part of TRANSIT operations is currently funded with fares and other system-generated revenues such as advertising. Fares are not indexed to inflation, operating expenses, or any other metric, and were in fact frozen for 11 years. As a result, fares have been raised irregularly and somewhat steeply. The cost recovery ratio – ratio of fare and other TRANSIT revenue to operating expenses – will be about 47% when fare increases are implemented in July 2005.

Recommendation: Regularly increase TRANSIT fares to keep pace with expenses.

TRANSIT is preparing to increase its fares in July 2005, and fares should indeed go up as a measured response to increasing needs: TRANSIT's operating costs have been increasingly subsidized with funds intended for capital projects, and as TRANSIT has added services its costs have risen. However the agency should not simply use a one-time fare hike. It should adopt a policy which guarantees fares will increase as expenses increase, and therefore guarantees the Trust Fund capital resources will not be diverted for operating expenses.¹⁸

No transit system in the United States comes close to supporting 100% of its costs with the farebox, and most fund less than half of their operating cost from fares. Recent fare increases have raised the TRANSIT cost recovery ratio to 47%, so that for every \$1.00 it spends to run the trains and buses, it receives 47 cents from fares and other system-generated revenue.¹⁹ With the recommended future steady recovery ratio of about 48%, fare increases should be predictable and based on reasonable

¹⁸ A more thorough recommendation on fares is available from the New Jersey Association of Railroad Passengers in its "Proposal for a Statewide Policy to Fund Public Transportation, A 5 Point Program for an Adequate, Stable and Secure Source of Future Funding," April 2005.

¹⁹ If fares were to remain static for the next 10 years, the share would be reduced to only 39 cents by 2015. The rest of the cost of operations – the other 53 cents per dollar – comes from Federal and State subsidies.

needs, and should keep pace with inflation. Indexing fares to a steady fare box recovery ratio is sound fiscal policy for a transit agency.²⁰

The Math of Operating Deficits

Even if a transit agency’s operating revenues are increasing at the same rate as expenditures, there can still be negative financial consequences. For example, if in a given year an agency’s operating expenses are \$200 million and operating revenues are \$100 million, then the agency has a 50% fare box recovery ratio and an operating deficit of \$100 million. This is a reasonable position for a transit agency; 50% is often considered a target fare box recovery ratio. Let’s say that the next year, the operating revenues and expenses both increase by 5%: the operating expenses are now up to \$210 million while revenue is only up to \$105 million. The fare box recovery ratio is still 50% but the operating deficit is up to \$105 million, an increase of \$5 million from the year prior. **To avoid these increasing absolute operating deficits, operating revenue needs to grow at twice the rate of operating expenses. That means higher fares,** even when it can be claimed that operating expenses and revenues are “increasing in parallel.” When considering how much fares should be raised, it is important to look at absolute numbers as well as rates of change.

Absolute Operating Deficit Grows even as Expenses and Revenues Increase at the Same Rate	Year 1	Growth Rate	Year 2
Expenses	\$200	5%	\$210
Revenues	\$100	5%	\$105
Deficit	\$100		\$105

Other TRANSIT system-generated revenues have been lost over time. Leveraged lease proceeds were tax benefits that TRANSIT sold to investors who took nominal title to property, such as rolling stock, and charged the depreciation against their tax liability. The sale of these tax benefits has been suspended due to federal policy shifts, resulting in a loss of operating revenue of \$20 to \$30 million per year. After the attacks of September 11, 2001, TRANSIT received a \$100 million federal appropriation to fill its operations gap; this funding was for one time only, but the security mandates have required permanently higher levels of operating expenditure and are still in place. Other sources have already been tapped out, including leftover COPs revenue (Certificates of Participation). As TRANSIT officials put it, “We’ve already cleaned out the cupboards. The cupboards are bare.” Both TRANSIT and DOT could not provide regular service – running the

²⁰ Most of the numbers used here are technically cost recovery ratios since they account for all system generated revenue, not just fares.

trains and buses, maintaining the roads, and picking up snow, for example – without substantial pass-throughs from the Trust Fund-funded capital budgets.

Recommendation: Fully fund DOT and TRANSIT operating budgets and eliminate capital-to-operating transfers.

Capital and operating needs are closely interconnected, a fact not fully acknowledged by framers of Trust Fund Authority legislation. The state's failure to plan and appropriate sufficient, predictable operating resources has created a structural deficit in operating funds. The two budgets need to be planned to function together, not in competition. Capital to operating transfers result in forgone rail expansion; the operating deficit results in less routine road, bridge and rail maintenance, and less frequent bus service.

**Without resolving the structural deficit,
the capital budget will continue to appear to under-perform
and the operating side will continue to be starved
and forced to steal from the capital side.**

The Blue Ribbon Transportation Commission report did not fully deal with how to end the operating budget's structural deficit. As New Jersey faces overall budget deficits, the General Fund cannot be relied upon as the only source for filling this crucial need. The practice of using capital funds to pay for operations should be stopped immediately, and the increased revenue required up front should be allocated.

The Blue Ribbon Transportation Commission report and others have recommended a weaning approach to resolving the \$300 million plus capital-to-operating transfers. Some believe that eliminating the capital-to-operating transfers all at once would be too large a fiscal step to take and should be done in stages. However ending capital-to-operating transfers completely, and soon, is essentially an accounting transfer. While it may tighten the fiscal constraints in the short term by requiring the state to borrow for less of its transportation system and use more pay-as-you-go sources, it provides fiscal solvency in the long term. Without ending this practice and solving the operations deficit, the agencies will continue to use funds intended for new train lines and better roads to pay for day to day operations. Agencies should only resort to using capital money for operations in case of severe fiscal emergency; New Jersey's practice has instead caused one.

3. Leakage of Trust Fund revenue sources into the General Fund

By constitutional dedication, the Trust Fund receives \$805 million each year as follows:

- \$200 million from petroleum gross receipts tax, a tax that affects fuel wholesalers;
- \$200 million from a motor vehicles sales tax; and
- \$405 million, or the equivalent of 9 cents of the 10.5 New Jersey state gas tax.

The Trust Fund also has 'statutorily dedicated' revenue sources. These are items which may be appropriated to the Trust Fund, but in times of statewide budget deficit have been appropriated to the General Fund. These funds have not been appropriated to the Trust Fund since 2001. Referred to here as leakage items, they add up to \$114.5 million per year and include,

- \$30 million from heavy truck fees,
- \$24.5 million from the toll road authority, and

- \$60 million from the good driver surcharge.²¹

In addition, one and a half cents of the current 10.5 cent gas tax will no longer be obligated to debt service in the near future. The revenue equivalent of the 1.5 cents, or about \$67 million, is not constitutionally dedicated to the Trust Fund but is intended for transportation purposes.

Recommendation: Constitutionally dedicate all originally intended resources to the Transportation Trust Fund.

With a projected FY 05 deficit of \$3 billion, the state of New Jersey clearly needs all it can get for its General Fund. However these specific sources are guaranteed for transportation purposes. A constitutional dedication of these resources to the Trust Fund would be a clear signal of the state's commitment to restoring financial stability to the transportation system. Such a dedication is also recommended by the Blue Ribbon Transportation Commission and in Assemblyman John Wisniewski and Assemblyman Peter Biondi's proposed Trust Fund reauthorization legislation (A3414, October 2004).

4. Insufficient accountability and independent oversight

One of the main underlying factors behind the current crisis is insufficient oversight of the Trust Fund. A number of questions need to be seriously posed to the Governor, Legislature, TRANSIT and DOT:

- How can the public be assured it is getting the maximum bang for its buck in transportation spending?
- How can DOT and TRANSIT be assured that their planning efforts will be met with stable, sustainable funding into the future?
- How can the taxpayers be assured that the agencies' operating budgets are not in structural deficit?

The system clearly needs added oversight and accountability to instill this kind of assurance. In addition, it needs to be supported by funding sources which will not deplete over time and which are not over-sensitive to recession or inflation.

As it stands now, the Trust Fund Authority is largely powerless. It is comprised of the Commissioner of Transportation, the State Treasurer, and five appointees by the Governor and Legislature. There is no independent accounting arm or balancing oversight measure in place. The Trust Fund Authority, as noted earlier, is not tied into the process of developing or managing the capital programs for which it issues bonds, nor is it part of the management of its resources by the agencies. It is also not part of the management of federal funds, much of which are matching funds unavailable without its resources. The Trust Fund Authority simply bonds out that amount appropriated to it by the State, within legal limits. In the last 10 years, the limits on the amount it can bond and the terms of its bonds have been increased. While the agencies' needs have grown, excessive bonding without independent oversight has led to the current crisis in which all revenue coming into the Trust Fund is obligated to debt for the next 15 years.

²¹ The so-called 'good driver surcharge' was originally named in context with a safe driving program and is now part of regular motor vehicle registration.

Recommendation: Create an independent Five Person Financial Policy Review Committee.

The Blue Ribbon Transportation Commission Report and legislation proposed by Assemblymen Wisniewski and Biondi have introduced the idea of establishing an independent five member Financial Policy Review Committee.²² The Committee would annually certify that the Trust Fund is not being used for unauthorized expenses and that the Trust Fund Authority is not issuing bonds beyond established limits to maintain stability. If certification cannot be made initially, there is an appeal process by which the Transportation Commissioner can work with the Review Committee to come to consensus on the funding plan.

Recommendation: Issue 6 Month Reports from the Director of the Division of Taxation.

As New Jersey state government does not have a strong auditing arm, another layer of accountability would be provided by requiring 6 Month Reports from the Director of the Division of Taxation on how much is collected from motor fuel and other relevant taxes. This certification would be made to the Review Committee. These are excellent recommendations, and this report calls for added measures to promote oversight and accountability.

The five person Financial Policy Review Committee would be politically independent and provide a balance to the governor's office, the Transit Board and Commissioner. The Wisniewski/Biondi bill proposes the committee be appointed by members of the Executive and legislative branches, as follows:

- One appointment by the Governor with the consent of the Senate (4 year term),
- One appointment by the President of the Senate (3 year term),
- One appointment by the Assembly Speaker (3 year term),
- One appointment by the Senate Minority Leader (2 year term), and
- One appointment by the Assembly Minority Leader (2 year term).

This composition is reasonable and should be adopted, but with changes to the members' terms. This report recommends an alternative structure, to ensure the Committee's independence from the political process. Committee members should have **overlapping terms of five years each**. Initially, the five members would be phased: one would get a one year term, one a two year term, one a three year term, one a four year term and one a five year term. As each retires, a new appointee would get a full five year term. In this way, one new member would retire each year and one would be appointed each year. The five year time frame would protect the Committee from becoming overly concerned with elections. It would also allow Committee members enough time to further develop expertise regarding the issues they face.²³

Appointees to the Committee should have expertise in transportation finance. They should have experience dealing with transportation infrastructure, capital projects, operations, and budgeting, as well as long term financing. Appointees should be professionals who are able to make a five year commitment and lend their full attention to the work of the Committee. No member of the legislature or executive branch should be a candidate for the Committee.

²² Assemblyman Wisniewski and Assemblyman Biondi's proposed Bill A 3414 is attached as Appendix D.

²³ The committee structure and the method of phasing in 5 year terms are similar to that used when the Garden State Preservation Trust was established.

The Committee would function similarly to the New York State Financial Control Board established in 1975 to solve New York City's financial crisis. The Financial Control Board is a helpful precedent for the Committee: it provided review and oversight, it required a new level of accountability from the entity in financial trouble (New York City), and it had the power to restrict implementation of any financial plans and borrowings that it did not approve and certify. Similarly, this report recommends establishing a Committee that would review, oversee and hold accountable all relevant parties to ensure the Trust Fund remains solvent and the transportation infrastructure of the state is stably funded.

The Committee would receive proposed operating budgets from the Commissioner in January of each year and capital budgets in March. These budgets will have already been approved by the Governor and the Metropolitan Planning Organizations (MPOs); the Committee would review the budgets while the legislature is doing the same, for about 4 months. Unlike the transportation budgets reviewed by the legislature, however, the Committee would review budget plans that include all resources – federal and state. At the same time, the Director of the Division of Taxation would make reports to the Committee and the public every six months showing the full amount collected from transportation-related taxes and tolls (gas and diesel, petroleum gross receipts, auto sales, contributions from the New Jersey Turnpike Authority, etc.).

With this information in hand, the politically independent Committee would be empowered to certify that the budgets are sustainable and requests are consistent with resources available from the Trust Fund. Certification would be subject to a reasonable appeals process by the Commissioner, as outlined in Wisniewski/Biondi's proposed legislation. If the Committee cannot certify the budgets as they are presented it would have the power to recommend the Commissioner provide a corrective action plan, which would then be subject to Committee approval. If the Committee further finds it cannot certify the corrective action plan, it can withhold Trust Fund revenue from the agencies for that fiscal year.

The Committee would also certify that the Trust Fund Authority itself is only providing resources at a fiscally responsible and sustainable level, given certain restrictions, including these:

Recommendation: Restore long-term bondability to New Jersey's transportation financing system by limiting bond maturities to ten years until permanent fiscal stability is restored.

Start with Short Term Bonds. The Trust Fund Authority should adhere to certain bonding limits, including a limit on issuing longer term bonds, until bond-ability is restored. An initial analysis shows that the Trust Fund Authority can restore bond-ability by using 10 year bonds for the first 5 years, and then switching to 20 year bonds. The principle of starting short-term should be adhered to, however the exact terms should be further analyzed. The Committee would hold the Authority accountable to these restrictions.

Eventual Pay-As-You-Go/Bonding Ratio. Each year, some portion of the capital program should be funded on a pay-as-you-go basis. However, given the increased pay-as-you-go resources necessitated by the initial elimination of capital to operating transfers, a strict ratio need not be established immediately. Trust Fund reauthorization should lay out when it will implement a pay-as-you-go/bonding ratio for the capital programs, and the Committee should certify that the Trust

Fund Authority is following this ratio. Bondability can be established and maintained with a 20/80 pay-as-you-go/bonding ratio is enacted as early as 2016 given complete elimination of the capital to operating transfers. Like bond term limits, the exact number requires further analysis.

Operations are Fully Funded. Capital-to-operating transfers should be eliminated entirely. The Committee should certify that revenue from the gas tax and other sources is being used on a pay-as-you-go basis to fully fund operations before being used by the Trust Fund Authority to back new bonds. The Committee should also certify that the operating budgets are funded entirely with pay-as-you-go resources, and that the Trust Fund Authority is not providing borrowed funds for capital projects that are being used by the agencies for routine operations. The Committee would receive the full operating and capital budget statements, which would help maintain an honest assessment of operating needs. As noted earlier, TRANSIT fare increases would help to close the operating funding gap.

Conclusion

The Transportation Trust Fund is out of cash as of June 30, 2006. This is the case even though millions in gasoline and other dedicated taxes are collected each year. Reforms are necessary to prevent it from happening again. In addition to reform, significant new revenue will be needed to fund the state's transportation system into the future. This should not come solely from the gas tax; the TRANSIT rider should be part of the solution, and agencies will need to scale back their capital programs significantly. While the overall numbers are daunting – a \$32 billion gap – the impact on individuals and families need not be overwhelming. The transportation system can in fact be saved with only a modest contribution from each resident, but residents need to demand more for their money: more accountability, better oversight, better planning, transparent budgeting, and guarantees that the Trust Fund will not find itself in this crisis again.

To stop the cycle of 'too many demands; too few resources; insufficient accountability,' this report makes the following six recommendations for reform:

1. **Fully fund DOT and TRANSIT operating budgets and eliminate capital-to-operating transfers.** *See pages 17 to 20.*
2. **Regularly increase TRANSIT fares to keep pace with expenses.** *See pages 18 and 19.*
3. **Constitutionally dedicate all originally intended resources to the Transportation Trust Fund.** *See pages 20 and 21.*
4. **Restore long-term bondability to New Jersey's transportation financing system by limiting bond maturities to ten years until permanent fiscal stability is restored.** *See page 23.*
5. **Create an independent Five Person Financial Policy Review Committee.** *See pages 21 to 23.*
6. **Issue 6 Month Reports from the Director of the Division of Taxation.** *See page 22.*

Acknowledgements

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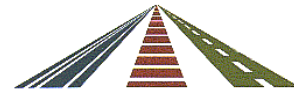
Questions can be directed to Thomas G. Dallessio (732-828-9945) or Alexis Perrotta (212-253-2727 x392) of Regional Plan Association. This report and the Executive Summary can be found on RPA's website: www.rpa.org.



Edward J.
Bloustein School
of Planning and Public Policy



TRI-STATE TRANSPORTATION CAMPAIGN



Mobilizing the Region