SECTION 4

TRANSIT FUNDING & FINANCE

A. INTRODUCTION

In 2000, some 9.4 billion rides were taken on public buses and trains, the highest number of trips taken by Americans in 40 years, since the inauguration of federal transit funding under President Kennedy.[1] In fact, as of 2000 transit usage is growing faster than highway usage.[2] Between 1995 and 2000, public transportation trips grew 21 percent, a growth rate faster than the U.S. population (4.8 percent), highway use (11 percent), and domestic air transportation (19 percent).[3] According to former FTA Acting Administrator Nuria Fernandez, "I believe the biggest challenge facing transit agencies all across the country…is finding the resources to meet the increased demand for transit and assuring that transit infrastructure is up to the task."[4] Since the fare box covers only a portion of operating and capital expenses, the funding of transit is of critical importance to its sustainability.[5]

Before the San Francisco Bay Area Rapid Transit (BART) system opened in 1972, the last major transit system had been built in Cleveland in the 1920s. BART was followed by several New Starts, including the Washington Metropolitan Transit Authority (WMATA) in 1976, and then Atlanta, Miami, Buffalo, and Baltimore.[6]

Section 3 of the Urban Mass Transportation Act of 1964[7] authorized discretionary federal grants and loans to states or local public agencies for up to 80 percent of the cost of (1) construction, acquisition, or improvement of mass transit facilities and equipment, (2) coordination of mass transit services with highways and other transportation, and (3) establishment and organization of public transit corridor development corporations.[8] The Federal Highway Act of 1973 opened up the Highway Trust Fund for urban mass transportation projects for the first time, and increased the federal share from two-thirds to 80 percent of the net project cost. ISTEA authorized states to transfer National Highway System funds to the Surface Transportation Program, which can include, *inter alia,* construction and rehabilitation of transit and capital projects eligible under Chapter 53 of Title 49 of the United States Code.

Most of transit's federal funding now comes from the Mass Transit Account of the Highway Trust Fund and is derived from 2.86 cents of the 18.4 cent per gallon tax on gasoline and the 24.4 cent per gallon tax on diesel fuel.[9] ISTEA provided some $600 million annually for new transit starts.

Under TEA-21,[10] a $217 billion authorization bill (the largest infrastructure bill in U.S. history), Congress significantly increased funding for CMAQ (by 35 percent), as well as for transit (by 50 percent). TEA-21 authorized $36 billion through 2003 in guaranteed funding for a variety of transit programs, including financial assistance to states and local governments to develop, operate, and maintain transit systems. Other federal funds are available to develop, plan, or construct transit facilities through DOT's highway and transit formula and federal loan programs.[11] For fiscal year 2001, FTA had some $6.3 billion available for transit programs, of which $60 million was earmarked for the 2002 Winter Olympic Games in Utah, primarily for the construction of temporary transportation facilities.[12]

Relative to demand, however, transit remains severely underfunded. The FTA estimates that the $5 billion in transit capital investment from all sources is approximately $2 billion less than required to maintain current conditions. One-third of public transport facilities are in fair or poor condition. Federal gasoline taxes and general funds support 47 percent of transit costs nationwide. State sales taxes and general funds cover less than a third of operating expenses. Approximately

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[1] One of the most authoritative sources on the subject of transit finance is MARY COLLINS, REPORT ON INNOVATIVE FINANCING TECHNIQUES FOR TRANSIT AGENCIES (Transit Cooperative Research Program, Legal Research Digest No. 13, 1999), a publication highly recommended to the reader.

[2] *Testimony of FHWA Administrator Kenneth Wykle Before the U.S. House Comm. on Transportation & Infrastructure* (Mar. 8, 2000).

[3] *Public Transportation Ridership on the Rise for Fifth Straight Year,* U.S. NEWSWIRE, Apr. 16, 2001.

[4] *Testimony of Nuria Fernandez Before the Subcomm. on Gov't Management, U.S. House Comm. on Government Reform* (Oct. 6, 2000).

[5] *See, e.g.,* WAYNE BOYLE, EIGHT WAYS TO FINANCE TRANSIT: A POLICYMAKER'S GUIDE (1994). PAUL MARX, THE VALUE OF INNOVATIVE FINANCING TO TRANSIT IN THE U.S. (Global Mass Transit Systems 101, 1999). COLLINS, *supra* note 1; FED. TRANSIT ADMIN., FINANCIAL INNOVATIVE FINANCING HANDBOOK (1995); INST. FOR URBAN TRANSPORTATION, INDIANA UNIV., FINANCIAL MANAGEMENT FOR TRANSIT: A HANDBOOK (1985).

[6] *Testimony of Gladys Mack Before the Subcomm. on Gov't Management, Comm. on Government Reform* (Oct. 6, 2000).

[7] Currently 49 U.S.C. § 5309 (2003).

[8] 49 U.S.C. § 5309 (2003); PAUL DEMPSEY & WILLIAM THOMS, LAW & ECONOMIC REGULATION IN TRANSPORTATION 314 (Quorum 1986).

[9] Thomas Howard, *Highway Finance Information,* PUB. ROADS, Nov. 1, 1999, at 40.

[10] Pub. L. No. 105-178 (1998).

[11] GEN. ACCOUNTING OFFICE, MASS TRANSIT: CHALLENGES IN EVALUATING, OVERSEEING AND FUNDING MAJOR TRANSIT PROJECTS 3 (2000).

[12] Department of Transportation and Related Agencies Appropriations Act for Fiscal Year 2001, Pub. L. 106-346 (2001). 66 Fed. Reg. 4900 (Jan. 18, 2001). The actual transfer of funds is handled under U.S. Department of Treasury regulations, "Rules and Procedures for Funds Transfers," 31 C.F.R. pt. 205 (2003), that implement Section 5(b) of the Cash Management Improvement Act of 1990, as amended, 31 U.S.C. § 6503(b) (2003). U.S. Department of the Treasury Circular 1075, pt. 205, "Withdrawal of Cash from the Treasury for Advances Under Federal Grants and Other Programs." 31 C.F.R. § 102.13(i)(2) (1999).

42–44 percent of operating costs are covered by the fare box in conventional buses,[13] while only 27 percent is recovered on light rail.[14] This shortfall requires innovative financing techniques.[15] Leveraged funding, as a bridge financing mechanism, becomes increasingly necessary as the arrival of federal dollars fails to keep pace with the current needs and expansion of the transit system.[16]

At the outset, a distinction must be drawn between capital expenses and operating expenses. Capital funds fund capital projects. The operating expense shortfall from farebox revenues is entirely the responsibility of the transit system, and is typically covered by either a subsidy from the transit system's general fund or from a dedicated funding source, such as a percentage of the state/local gas tax or sales tax. Except for paratransit operations, the FTA does not permit capital funds to be used for most operating expenses—capital cost of maintenance and capital leases notwithstanding.[17]

B. PLANNING

Federal financial support for transit planning is available from several sources, including the Metropolitan Planning Program[18] and the State Planning and Research Program,[19] as well as flexible funding available through the planning programs administered by FHWA.[20] Additionally, FTA Urbanized Formula Funds[21] and flexible funding under the STP and the CMAQ may also be allocated to certain planning activities.[22]

However, FTA does not support the use of New Starts funding[23] for initial planning activities.[24] In assessing New Starts applications, FTA considers the degree to which initial planning was supported with funding from sources other than the New Starts program.[25] Moreover, Congress has specified that no more than 8 percent of New Starts funding may be used for purposes other than final design and construction.[26]

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[13] MARX, *supra* note 5, at 101; Maya Bell, *Elusive Goal, Rail Line that Works,* ORLANDO SENTINEL, Mar. 5, 2000, at A1. The percentage of operating costs recovered by transit providers at the fare box differs significantly between jurisdictions. In London, London Transport covers 66 percent of conventional service and 12 percent of paratransit from the fare box. Chip Martin, *Bus Service Deserves Budget Hike*, LONDON FREE PRESS, Nov. 29, 1999, at A3. In San Diego, fare box recovery is estimated to be 50 percent. *Transportation Planning is Misguided*, SAN DIEGO BUS. J., Aug. 27, 2001, at 39. Milwaukee's trolleys are estimated to cover 12 percent from the fare box. *Transit: Don't Let Cute Cars Take You for a Ride,* MILWAUKEE J. SENTINEL, Aug. 14, 2001, at 14A. Denver's fare box recovery is reported to be 20 percent. Kevin Flynn, *RTD Pushes 4-Year Fare Increase,* ROCKY MOUNTAIN NEWS, July 24, 2001, at 16A. In California, Santa Clara's VTA recovers 17 percent, while "SamTrans, the public transit agency for San Mateo County, has a fare box recovery of about 27 percent; Alameda Contra Costa Transit District, less than 25 percent; and San Francisco Municipal Railway, 33 percent. Bay Area Rapid Transit is one of the most efficient in the nation, operating at about 64 percent." Alastair Goldfisher, *VTA Bus, Light Rail Fares Expected to Increase in July,* BUS. J., Dec. 19, 1998, at 16.

[14] Stacey Higgenbothem, *Light Rail Can Reap Many Benefits, Despite Risks,* BOND BUYER, June 21, 2000, at 30. However, San Diego's South Line covered 90 percent of operating costs in its inaugural years from the fare box. Marlon Boarnet & Nicholas Compton, *Transit Oriented Development in San Diego County,* J. AM. PLAN. ASS'N, Jan. 1, 1999, at 80, 81.

[15] As we shall see below, FTA has embraced innovative financing techniques to leverage federal funds and federally-funded assets. 60 Fed. Reg. 24682 (May 9, 1995).

[16] Yvette Shields & Mary Wisneiwski, *Are Leveraged Federal Grants the Future of Transit Projects?*, BOND BUYER, Apr. 10, 2001, at 36.

[17] *But see* note 57, *infra,* for a complete list of eligible capital projects.

[18] 49 U.S.C. § 5303 (2003). This program supports funding to support the cooperative, continuous, and comprehensive planning program in metropolitan areas, as required by 49 U.S.C. §§ 5303–5306 (2003). State DOTs and MPOs may receive funding to support the economic vitality of the metropolitan area. Funds are apportioned according to a formula that takes into consideration, *inter alia,* the state's urbanized area population in proportion to the urbanized area population for the United States as a whole. Each state can receive no less than .5 percent of the amount apportioned. These federal funds are sub-allocated by the state to MPOs under a formula that considers each MPO's urbanized area population, their planning needs, and a minimum distribution. FED. TRANSIT ADMIN., THIS IS THE FEDERAL TRANSIT ADMINISTRATION 10 (2000).

[19] 49 U.S.C. § 5313(b) (2003). This program provides funding to states for statewide planning and other technical activities; planning support for nonurbanized areas; research, development and demonstration projects; fellowships for training in the public transportation field; university research; and human resource development. Funds are allocated under a formula based on the last census, and the state's urbanized areas compared with the urbanized areas of all states. A state must receive not less than .5 percent of the amount apportioned under this program. FED. TRANSIT ADMIN., *supra* note 18, at 11.

[20] Unless highway funds are actually "flexed," they are prohibited by law from being used on highway projects.

[21] 49 U.S.C. § 5307 (2003).

[22] 65 Fed. Reg. 76868 (Dec. 7, 2003). CMAQ funds may be used for project planning or other activities that lead directly to the construction of facilities or new programs improving air quality, such as preliminary engineering, major investment studies, preparation of environmental NEPA documents, and related air quality development activities. However, general planning or environmental activities or documents, such as economic or demographic studies, that do not directly support air quality improvement, are ineligible for CMAQ funding. 61 Fed. Reg. 50884 (May 9, 1995).

[23] 49 U.S.C. § 5309 (2003).

[24] New Starts funding is discussed in greater detail below. For present purposes, New Starts are FTA capital investments or loans for fixed guideway systems or extensions to existing systems. 49 C.F.R. § 611.1 (1999).

[25] 65 Fed. Reg. 76868 (Dec. 7, 2000); 49 U.S.C. § 5309 (2003).

[26] 49 U.S.C. § 5309(m)(2) (2003).

C. URBANIZED AREA FORMULA PROGRAM

The Urbanized Area Formula Grants Program allocates funds to urbanized areas[27] for capital, operating, and planning costs associated with mass transit.[28] Eligible projects include planning, engineering design and evaluation of transit projects, capital investments in bus and bus-related projects, construction and maintenance of passenger facilities, capital investments in new and existing fixed guideway systems, preventive maintenance, and some ADA complementary paratransit service costs.[29] Under this program, 9.32 percent is allocated to small urbanized areas (population 50,000 to 199,999), while the remaining 90.68 percent is allocated to large urbanized areas (population 200,000 and above).[30] For small urbanized areas, the formula apportionments are based on two factors: (1) population, and (2) population times population density. For larger urbanized areas, the formula also breaks down into two tiers: the Fixed Guideway[31] Tier (33.29 percent) and the Bus Tier (66.71 percent).[32] Operating assistance is not an eligible expense for large urbanized areas under this program. In these areas, not less than 1 percent of program funding must be dedicated to transit enhancement activities, such as historic preservation, landscaping, public art, pedestrian access, bicycle access, and enhanced access for the disabled.[33]

Large urbanized areas receive their formula apportionments directly from the federal government, through a designated recipient agency within the urbanized area. But for small urbanized areas that are not in a TMA,[34] the Governor of their respective state acts as the designated recipient.[35] FTA publishes an annual notice of apportionments and allocations in the Federal Register. The notice also includes program guidance and any requirements imposed by Congress.[36]

The grantee must adhere to certain public participation requirements[37] and specified reporting requirements,[38] and must submit to an annual review, audit, and evaluation to determine whether the recipient has carried out the project in a timely and effective way, and has used federal funds in a lawful way. Moreover, at least every 3 years, FTA reviews and evaluates the recipient's performance in carrying out the funded program, and its compliance with statutory and regulatory requirements.[39] Triennial Review is a comprehensive review of the performance of the grantee as well as a review of its compliance with FTA's program requirements.

D. NONURBANIZED AREA FORMULA PROGRAM

The Nonurbanized Area Formula Program provides assistance to states to support public transportation in

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[27] An "urbanized area" is an incorporated area of 50,000 or more that is so designated by the U.S. Census Bureau.

[28] 49 U.S.C. § 5307 (2003). Grants may be made "for capital projects and to finance the planning and improvement costs of equipment, facilities, and associated maintenance items for use in mass transportation, including the renovation and improvement of historic transportation facilities with related private investment." 49 U.S.C. 5307(b)(i) (2003).

[29] FED. TRANSIT ADMIN., *supra* note 18, at 11–12. Unless it has determined that it is not necessary to expend 1 percent of the amount of federal assistance it receives for the fiscal year for transit security projects in accordance with 49 U.S.C. § 5336, a recipient of FTA funds must expend at least 1 percent of the amount of that assistance for transit security projects, including increased lighting in or adjacent to a transit system, increased camera surveillance of an area in or adjacent to that system, emergency telephone line or lines to contact law enforcement or security personnel in an area in or adjacent to that system, and any other project intended to increase the security and safety of an existing or planned transit system. 49 U.S.C. § 5307(d)(1)(J) (2003). Capital grant funds are also available for crime prevention and security. 49 U.S.C. § 5321 (2003).

[30] 49 U.S.C. § 5307 (2003) (formerly Section 9 of the Federal Transit Act).

[31] Fixed guideway system means a mass transportation facility which utilizes and occupies a separate right-of-way, or rail line, for the exclusive use of mass transportation and other high occupancy vehicles, or uses a fixed catenary system and a right of way usable by other forms of transportation. This includes, but is not limited to, rapid rail, light rail, commuter rail, automated guideway transit, people movers, ferry boat service, and fixed-guideway facilities for buses (such as bus rapid transit) and other high occupancy vehicles. A new fixed guideway system means a newly-constructed fixed guideway system in a corridor or alignment where no such system exists.

49 C.F.R. § 611.5 (1999). 49 U.S.C. §§ 5309(e), 5304(2) (2003).

[32] 49 U.S.C. § 5336 (2003).

[33] FED. TRANSIT ADMIN., *supra* note 18, at 12. Recipients of funds apportioned under Section 5336 that serve a population of 200,000 or more must make 1 percent of their funds available for transit enhancement activities. 49 U.S.C. § 5307(k) (2003).

[34] Transportation management area (TMA) means an urbanized area with a population over 200,000 (as determined by the latest decennial census) or other area when TMA designation is requested by the Governor and the MPO (or affected local officials), and officially designated by the Administrators of the FHWA and the FTA. The TMA designation applies to the entire metropolitan planning area(s).

23 C.F.R. 500.103 (2003). TMAs are discussed in greater detail in Section 2—Transportation Planning.

[35] 64 Fed. Reg. 37193 (July 9, 1999).

[36] The FY 2001 notice of apportionments and allocations can be found at 66 Fed. Reg. 4958 (Jan. 18, 2001), and is also listed on the FTA Web site at www.fta.dot.gov (visited April 21, 2003).

[37] 49 U.S.C. § 5307(c) (2003).

[38] 49 U.S.C. §§ 5307, 5335(a), FTA Regulations, "Uniform System of Accounts and Records and Reporting System," 49 C.F.R. pt. 630 (2003).

[39] 49 U.S.C. § 5307(i) (2000). Failure to adhere to applicable legal requirements may result in the imposition of criminal sanctions. 49 U.S.C. §§ 1001, 5307 (2000). However, grantees work hard to maintain good standing with FTA. In the overwhelming number of Triennial Reviews, the grantee is informed of shortcomings, and is provided technical assistance that will enable the grantee to return to compliance.

areas of less than 50,000 in population.[40] These funds may be used for capital, operating, administration, and project administration expenses for state agencies, local public bodies, and nonprofit organizations, as well as operators of public transportation services. Funds are apportioned so that each state receives an amount equal to the total appropriation multiplied by a ratio equal to the population of nonurbanized areas divided by the population in nonurbanized areas in the United States.[41] A state must also use 15 percent of its annual apportionment under this program to support intercity bus service, unless the Governor certifies that such needs are being adequately satisfied.[42] Projects dedicated to ADA compliance, the Clean Air Act, or bicycle access, may be funded at 90 percent federal match, but operating expenses may be funded only at the 50 percent level.[43]

E. THE RURAL TRANSIT ASSISTANCE PROGRAM

The Rural Transit Assistance Program[44] (RTAP) provides assistance for projects involving the design and implementation of training and technical assistance projects, as well as other support services designed to meet the needs of transit operators in nonurbanized areas. The program provides an annual allocation to each state to develop and implement technical assistance and training programs, and provides funds to support the development of information and materials for use by states and local transit operators and to support research and technical assistance projects of national interest. There is no requirement for a local match.[45]

F. THE RURAL TRANSPORTATION ACCESSIBILITY INCENTIVE PROGRAM

The Rural Transportation Accessibility Incentive Program funds incremental capital and training expenses incurred in meeting the requirements of the DOT's Over-the-Road Bus Accessibility Rule.[46] It may be used to fund wheelchair lifts for new or existing vehicles and for training. The federal share is 90 percent.[47]

G. THE ELDERLY AND PERSONS WITH DISABILITIES FORMULA PROGRAM

The Elderly and Persons with Disabilities Program provides formula funding and loans[48] to states[49] to assist nonprofit organizations and governmental authorities[50] in meeting the transportation needs[51] of individuals who are elderly or who have disabilities, whenever existing transportation services are inadequate to their needs.[52] Funds are apportioned according to a formula that takes into consideration each state's share of the population of the elderly and disabled.[53] States submit statewide grant applications identifying the projects for which funding is sought. Upon FTA approval, the state administers the program and allocates funds to subrecipients (including private nonprofit transportation providers and certain public bodies) within the state.[54] The federal share for this program is 80 percent.

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[40] 49 U.S.C. § 5311 (2003) (formerly § 18 of the Federal Transit Act). (DEMPSEY & THOMS, *supra* note 8, at 318.) Transportation projects must be embraced within a state program of mass transportation service projects. 49 U.S.C. § 5311(d) (2003). State procedures are set forth in FTA Circular 9040.1E. DOT may approve such programs only if "the Secretary finds that the program provides a fair distribution of amounts in the State, including Indian reservations, and the maximum feasible coordination of mass transportation service assisted under this section with transportation service assisted by other United States Government sources." 49 U.S.C. § 5311(b) (2003).

[41] 49 U.S.C. § 5311(c) (2003). No more than 15 percent of a state's funds may be spent on administration and technical assistance to a recipient. 49 U.S.C. § 5311(e) (2003).

[42] A recipient of FTA funds must spend at least 15 percent of its funds authorized for 49 U.S.C. § 5311 for intercity transportation projects, unless the State's chief executive officer has certified to FTA that the State's intercity bus service needs are being adequately met.

[43] FED. TRANSIT ADMIN., *supra* note 18, at 12. *See* FTA Circular 9040.1E, available at FED. TRANSIT ADMIN., NON-URBANIZED AREA FORMULA PROGRAM GUIDANCE AND GRANT APPLICATION INSTRUCTIONS (Oct. 1, 1998), http://www.fta.dot.gov/library/policy/circ9040_1E/9040face.htm.

[44] 49 U.S.C. § 5311(b)(2) (2003). This statute is discussed at http://www.fta.dot.gov/research/implem/rtap/rtap.htm (visited April 21, 2003).

[45] 49 U.S.C. § 5311(b) (2003). FED. TRANSIT ADMIN., *supra* note 18, at 13.

[46] 49 C.F.R. pt. 37 (1999). 64 Fed. Reg. 6165 (Feb. 8, 1999); 64 Fed. Reg. 46224 (Aug. 24, 1999); 66 Fed. Reg. 8060 (Jan. 26, 2001). Incremental capital costs eligible for funding include adding lifts, tie downs, moveable seats, doors, and installation thereof, as well as retrofitting vehicles with such components. 65 Fed. Reg. 2772 (Jan. 18, 2000).

[47] FED. TRANSIT ADMIN., *supra* note 18, at 21. Rural transit assistance is discussed at Fed. Transit Admin., *Rural Transit Assistance Program* (visited Aug. 13, 2003), http://www.fta.dot.gov/research/implem/rtap/rtap.htm.

[48] 49 U.S.C. § 5310(e) (2003).

[49] State procedures are set forth in FTA Circular 9070.1E.

[50] Eligible recipients are defined in 49 U.S.C. § 5310(a)(2) (2003).

[51] Among such needs that may be funded is meal delivery service to homebound individuals. 49 U.S.C. § 5310(h) (2003).

[52] 49 U.S.C. § 5310 (2003) (formerly § 16 of the Federal Transit Act).

[53] 49 U.S.C. § 5310(b) (2003).

[54] FED. TRANSIT ADMIN., *supra* note 18, at 13–14; Transit Express v. Ettinger, 246 F.3d 1018 (7th Cir. 2000), held that a complaint brought by a private transportation provider that it was unlawfully excluded from participating in this program does not raise present federal question jurisdiction.

H. THE CAPITAL INVESTMENT PROGRAM

The Capital Investment Program provides assistance for three activities: (1) new and replacement buses and facilities; (2) modernization of existing rail systems, and (3) new fixed guideway systems. (The latter program is discussed in a separate section below). Eligible recipients are public bodies and agencies (such as transit authorities), including states and their political subdivisions, and certain public entities created under state law.[55] Federal funding may cover up to 80 percent of the net project cost[56] of an eligible capital project.[57] "Net project cost" is the part of the cost that cannot be financed with revenue.[58] Most of these funds are allocated by FTA on a discretionary basis.[59] FTA may also make loans for such purposes.[60] Although this program has been called discretionary, in reality it has been entirely earmarked by Congress in recent years. The New Starts program has seldom provided more than 50 percent of project costs in recent years and may be statutorily set at 50 percent in the next Congressional reauthorization.

1. Bus and Bus-Related Projects

Eligible bus projects include

> fleet and service expansion, bus maintenance and administrative facilities, transfer facilities, bus malls, transportation centers, intermodal terminals, park-and-ride stations, acquisition of replacement vehicles, bus rebuilds, bus preventive maintenance, passenger amenities such as passenger shelters and bus stop signs, accessory and miscellaneous equipment such as mobile radio units, supervisory vehicles, fareboxes, computers, shop and garage equipment, and costs incurred in arranging innovative financing for eligible projects.[61]

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[55] 49 U.S.C. § 5309 (2003).

[56] 49 U.S.C. §§ 5307(e), 5309(h) (2003).

[57] Eligible capital projects are:

> (A) acquiring, constructing, supervising, or inspecting equipment or a facility for use in mass transportation, expenses incidental to the acquisition or construction (including designing, engineering, location surveying, mapping, and acquiring rights-of-way), payments for the capital portions of rail trackage rights agreements, transit-related intelligent transportation systems, relocation assistance, acquiring replacement housing sites, and acquiring, constructing, relocating, and rehabilitating replacement housing; (B) rehabilitating a bus; (C) remanufacturing a bus; (D) overhauling rail rolling stock; (E) preventive maintenance; (F) leasing equipment or a facility for use in mass transportation, subject to regulations that the Secretary prescribes limiting the leasing arrangements to those that are more cost-effective than purchase or construction; (G) a mass transportation improvement that enhances economic development or incorporates private investment, including commercial and residential development, pedestrian and bicycle access to a mass transportation facility, and the renovation and improvement of historic transportation facilities, because the improvement enhances the effectiveness of a mass transportation project and is related physically or functionally to that mass transportation project, or establishes new or enhanced coordination between mass transportation and other transportation, and provides a fair share of revenue for mass transportation that will be used for mass transportation—(i) including property acquisition, demolition of existing structures, site preparation, utilities, building foundations, walkways, open space, safety and security equipment and facilities (including lighting, surveillance and related intelligent transportation system applications), facilities that incorporate community services such as daycare or health care, and a capital project for, and improving, equipment or a facility for an intermodal transfer facility or transportation mall, except that a person making an agreement to occupy space in a facility under this subparagraph shall pay a reasonable share of the costs of the facility through rental payments and other means; and (ii) excluding construction of a commercial revenue-producing facility or a part of a public facility not related to mass transportation; (H) the introduction of new technology, through innovative and improved products, into mass transportation; or (I) the provision of nonfixed route paratransit transportation services in accordance with section 223 of the Americans with Disabilities Act of 1990, 42 U.S.C. § 12143 (2003), but only for grant recipients that are in compliance with applicable requirements of that Act, including both fixed route and demand responsive service, and only for amounts not to exceed 10 percent of such recipient's annual formula apportionment under sections 5307 and 5311.

49 U.S.C. § 5302(a)(1)(i) (2003). They also include the following:

> (A) capital projects for new fixed guideway systems, and extensions to existing fixed guideway systems, including the acquisition of real property, the initial acquisition of rolling stock for the systems, alternatives analysis related to the development of the systems, and the acquisition of rights of way, and relocation, for fixed guideway corridor development for projects in the advanced stages of alternatives analysis or preliminary engineering; (B) capital projects, including property and improvements (except public highways other than fixed guideway facilities), needed for an efficient and coordinated mass transportation system; (C) the capital costs of coordinating mass transportation with other transportation; (D) the introduction of new technology, through innovative and improved products, into mass transportation; (E) capital projects to modernize existing fixed guideway systems; (F) capital projects to replace, rehabilitate, and purchase buses and related equipment and to construct bus-related facilities; (G) mass transportation projects planned, designed, and carried out to meet the special needs of elderly individuals and individuals with disabilities; and (H) the development of corridors to support fixed guideway systems, including protecting rights of way through acquisition, construction of dedicated bus and high occupancy vehicle lanes and park and ride lots, and other nonvehicular capital improvements that the Secretary may decide would result in increased mass transportation usage in the corridor.

49 U.S.C. § 5309(a)(1)(h) (2003).

[58] 49 U.S.C. § 5309(h) (2003). "Net Project Cost" is defined by 49 U.S.C. § 5302(a)(8) (2003). Certain expenses must be applied to reduce the net project cost. For example, if the recipient sells a building built in 1912 and deposits the funds in a reserve account, when it subsequently selects the site on which to build a new facility with FTA financial assistance, it must apply the sales proceeds to reduce the net project cost, notwithstanding that the city may still owe bond indebtedness on the original purchase of the 1912 building.

[59] FED. TRANSIT ADMIN., *supra* note 18, at 14.

[60] 49 U.S.C. § 5309(b) (2003). Loan purposes may include acquiring rights-of-way, station sites, and related purposes, as well as reconstruction, renovation, property management, and relocation costs if the property is required for a transit system and will be used for such purpose within a reasonable period of time. *Id*.

[61] FED. TRANSIT ADMIN., *supra* note 18, at 15.

2. Fixed Guideway Modernization

A fixed guideway is

> any transit system that uses exclusive or controlled rights-of-way or rails, entirely or in part. The term includes heavy rail, commuter rail, light rail, monorail, trolleybus, aerial tramway, inclined plane, cable car, automated guideway transit, ferryboats, that portion of motorized bus service operated on exclusive or controlled rights-of-way, and high-occupancy-vehicle (HOV) lanes.[62]

Eligible purposes are capital projects that are designed to improve or modernize existing fixed guideway systems. Such projects include the purchase and rehabilitation of rolling stock, track, equipment, signals, power equipment, substations, passenger stations and terminals, security equipment and systems, maintenance facilities and equipment, computer hardware and software, system extensions, and preventive maintenance. These funds are allocated according to a formula to urbanized areas with rail systems in operation for 7 years or longer.[63]

I. THE NEW STARTS PROGRAM

The major Capital Investment Program is the New Starts Program.[64] This program funds major new fixed guideway (separate and exclusive rights-of-way) rail, bus, or trolley transit systems, or extensions to existing fixed guideway systems.[65] Eligible projects include construction or extension of light rail, heavy rail, commuter rail, monorail, automated fixed guideway systems, and busway/high-occupancy vehicle corridors.[66] TEA-21 authorized $8.2 billion in New Starts transit projects through FY 2003.[67] FTA was authorized to make New Starts funding commitments for nearly $10 billion during fiscal years 1998–2003.

1. Historical Development of the New Starts Program

In 1976, in its first policy statement on the subject, the FTA introduced a process-oriented approach requiring that New Starts projects be subjected to an analysis of alternatives, including a Transportation System Management (TSM) alternative that used no-capital and low-capital measures to make optimum use of the existing transportation system. The statement also required that projects be cost effective.[68]

The Surface Transportation and Uniform Relocation Assistance Act of 1987 (STURAA)[69] set forth criteria New Starts projects had to meet in order to be eligible for federal discretionary grants. Projects had to be "cost-effective" and "supported by an adequate degree of local financial commitment." In evaluating the local commitment, FTA must determine whether: (1) the proposed plan provides for contingencies in order to cover unanticipated cost increases; (2) each proposed local source of capital and operating funds is stable, reliable, and available within the timetable for the proposed project; and (3) local resources are available to operate the overall proposed mass transit system without requiring a reduction in existing services.[70] ISTEA expanded the original requirement that a project be "cost-effective" by specifying that projects be "justified, based on a comprehensive review of its mobility improvements, environmental benefits, cost-effectiveness, and operating efficiencies."[71]

In 1994, President Clinton issued an Executive Order requiring a systematic analysis of the costs and benefits of proposed investments, and calling for efficient management of infrastructure, including a focus on the operation and maintenance of facilities, as well as the use of pricing to manage demand.[72]

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[62] FED. TRANSIT ADMIN., *supra* note 18, at 15. A fixed guideway is a mass transportation facility "(A) using and occupying a separate right-of-way or rail for the exclusive use of mass transportation and other high occupancy vehicles; or (B) using a fixed catenary system and a right-of-way usable by other forms of transportation." 49 U.S.C. § 5304(2) (2003). 49 C.F.R. § 611.5 (2003). 65 Fed. Reg. 76864 (Dec. 7, 2000). It falls under the capital investment grants and loans program of 49 U.S.C. § 5309 (2003).

[63] FED. TRANSIT ADMIN., *supra* note 18, at 15; Circular 9300.1A, ch. IV, available at: http://www.fta.dot.gov/library/policy/9300.1A/chp4.htm (visited April 21, 2003).

[64] 49 U.S.C. § 5309 (2000). "New start means a new fixed guideway system, or an extension to an existing fixed guideway system." 49 C.F.R. § 611.5 (1999). *See* FTA Circular 9300.1A, ch. V, available at: Fed. Transit Admin., *Capital Program: Grant Application Instructions* (visited Aug. 13, 2003), http://www.fta.dot.gov/library/policy/9300.1A/toc.htm.

[65] 49 U.S.C. §§ 5309(e), 5304(2) (2000). 49 C.F.R. § 611.5 (2003). Proposed projects are exempt from these requirements if the amount of Section 5309 assistance being sought for the project is less than $25 million. 49 U.S.C. § 5309(e)(8) (2003); 49 C.F.R. 611.7 (2003). Projects of less than $25 million in total funding under 49 U.S.C. § 5309, and projects specifically exempt by statute, do not have to satisfy the New Starts regulatory criteria. However, they still must satisfy the planning requirements of 23 C.F.R. pt. 450 (1999), and the environmental review requirements of 23 C.F.R. pt. 771 (1999).

[66] FED. TRANSIT ADMIN., *supra* note 18, at 16.

[67] U.S. GEN. ACCOUNTING OFFICE, FTA'S PROGRESS IN DEVELOPING AND IMPLEMENTING A NEW STARTS EVALUATION PROCESS (1999).

[68] 41 Fed. Reg. 41512 (Sept. 22, 1976). This was followed by a *Policy on Rail Transit,* which reiterated the alternatives analysis requirement, imposed requirements for local financial commitments, established the Full Funding Grant Agreement, and required that local governments take land use actions. 43 Fed. Reg. 9428 (Mar. 7, 1978). This, in turn, was followed by a *Statement of Policy on Major Urban Transportation Capital Investments,* which established a rating system for making comparisons between competing projects. 49 Fed. Reg. 21284 (May 18, 1984).

[69] Pub. L. 100-17 (1987).

[70] 67 Fed. Reg. 76864 (Dec. 7, 2000).

[71] 49 U.S.C. § 5309(e) (2003).

[72] Executive Order 12893, 59 Fed. Reg. 4233 (Jan. 31, 1994).

TEA-21[73] left much of past law and policy regarding New Starts intact, including the basic project justification criteria and the multiple-measure method of project evaluation. However, significant changes were introduced:

• *Major Investment Study*—Integration of the Major Investment Study (MIS) requirement into the FTA/FHWA planning and environmental regulations,[74] elimination of the MIS as a separate requirement,[75] and streamlining of the environmental process.[76]

• *Project Ratings*—The requirement for FTA to establish overall project ratings of "highly recommended," "recommended," or "not recommended." FTA must submit a report annually to Congress of projects with their respective ratings.[77]

• *FTA Approval*—The requirement for FTA approval for a project to advance to the final design stage of the project development process; TEA-21 requires that at the completion of the alternative analysis phase,[78] the local project sponsor must submit the locally preferred alternative New Starts project justification to FTA, and request FTA's approval to enter into the preliminary engineering[79] phase. Only when preliminary engineering is completed may a local project sponsor request FTA approval to enter into final design.[80]

• *Regulations*—FTA must publish regulations on the manner in which proposed projects will be evaluated and rated; and

• *Other changes* included a required evaluation of the cost of sprawl, infrastructure cost savings due to compact land use, population density and current transit ridership in a corridor, and the technical capacity of the grantee to undertake the project. TEA-21 expressly prohibits FTA from considering the dollar value of mobility improvements.[81]

2. Criteria for Approval

The FTA uses several criteria to evaluate candidate New Starts projects[82] and to determine which projects to propose to Congress for funding.[83] They are:

1. Mobility improvements—The forecast time savings from the New Start project vis-à-vis the baseline alternative predicated on a multi-modal measure of perceived travel times faced by all users of the transportation system, as well as the number of low income

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[73] Pub. L. No. 105-178 (June 9, 1998).

[74] 23 C.F.R. pt. 450 and 23 C.F.R. pt. 771 (2003).

[75] *See* Section 1308 of TEA-21.

[76] *See* Section 1309 of TEA-21. A multimodal MIS must be prepared for all major transit and highway expansions before they are included in the transportation plan or TIP. 61 Fed. Reg. 67094 (Dec. 19, 1996). The transportation planning process is described above, in Section 2—Transportation Plannning.

[77] 67 Fed. Reg. 76864 (Dec. 7, 2000).

[78] "Alternatives analysis is a corridor level analysis which evaluates all reasonable mode and alignment alternatives for addressing a transportation problem, and results in the adoption of a locally preferred alternative by the appropriate State and local agencies and official boards through a public process." 49 C.F.R. § 611.5 (2003). Moreover,

> (1) To be eligible for FTA capital investment funding for a major fixed guideway transit project, local project sponsors must perform an alternatives analysis.
> (2) The alternatives analysis develops information on the benefits, costs, and impacts of alternative strategies to address a transportation problem in a given corridor, leading to the adoption of a locally preferred alternative.
> (3) The alternative strategies evaluated in an alternatives analysis must include a no-build alternative, a baseline alternative, and an appropriate number of build alternatives. Where project sponsors believe the no-build alternative fulfills the requirements for a baseline alternative, FTA will determine whether to require a separate baseline alternative on a case-by-case basis.
> (4) The locally preferred alternative must be selected from among the evaluated alternative strategies and formally adopted and included in the metropolitan planning organization's financially-constrained long-range regional transportation plan.

49 C.F.R. § 611.7 (2003).

[79] "Preliminary Engineering is the process by which the scope of the proposed project is finalized, estimates of project costs, benefits and impacts are refined, NEPA requirements are completed, project management plans and fleet management plans are further developed, and local funding commitments are put in place." 49 C.F.R. § 611.5 (2003). Moreover,

> 1) A proposed project can be considered for advancement into preliminary engineering only if:
> (i) Alternatives analysis has been completed;
> (ii) The proposed project is adopted as the locally preferred alternative by the Metropolitan Planning Organization into its financially constrained metropolitan transportation plan;
> (iii) Project sponsors have demonstrated adequate technical capability to carry out preliminary engineering for the proposed project; and
> (iv) All other applicable Federal and FTA program requirements have been met.

49 C.F.R. § 611.5 (2003).

[80] This requirement enables FTA to control the bottleneck in enabling projects to proceed to a full funding grant agreement [FFGA].

[81] *See* Section 3010 of TEA-21.

[82] 49 U.S.C. § 5309(e)(1)(B) (2003). These measures have been developed according to the considerations identified at 49 U.S.C. § 5309(e)(3) (2003), and Executive Order 12893. 49 C.F.R. § 611 App. A (1999).

[83] U.S. GEN. ACCOUNTING OFFICE, *supra* note 11, at 1. In making annual funding proposals to Congress, the FTA gives highest priority to projects having federal grant agreements, and secondary preference to projects rated highly recommended, or recommended and ready to proceed to final design and a FFGA within the forthcoming fiscal year. For example, in the 2001 fiscal year budget process, FTA evaluated 48 projects, rated 32 as highly recommended or recommended, and proposed that 15 receive FFGAs. *Id*. at 2. In FY 2002, FTA evaluated 40 new projects, and developed ratings for 26 of them. Twenty-three rated "highly recommended" or "recommended," but only four received FTA's recommendation for an FFGA because they met the agency's "readiness" criteria. The majority of the remaining 19 did not meet the FTA's "readiness" or technical capacity criteria. U.S. GEN. ACCOUNTING OFFICE, MASS TRANSIT: FTA COULD RELIEVE NEW STARTS PROGRAM FUNDING CONSTRAINTS 3 (2001).

households and existing jobs within a half mile radius of the boarding points;

2. Environmental benefits—The anticipated change in pollutant and greenhouse gas emissions and energy consumption attributable to the New Start vis-à-vis the baseline alternative;

3. Operating efficiencies—The forecast change in operating cost per passenger mile for the entire transit system compared to the baseline;

4. Cost-effectiveness—The transportation system user benefits[84] based on a multimodal measure of travel times for the forecast year divided by the incremental cost of the proposed project;

5. Land Use—Existing and transit supportive land use policies and future patterns must be rated according to how likely the project is to foster transit supportive land use;[85] and

6. Other Factors—Including the extent to which the policies and programs are in place as specified in the forecasts, project management capability, and additional factors relevant to local and national priorities and the project's success.[86]

Each of the first five criteria is ranked by FTA as "high," "medium-high," "medium," "low-medium," or "low." Factors identified in the last criterion are reported as appropriate.[87]

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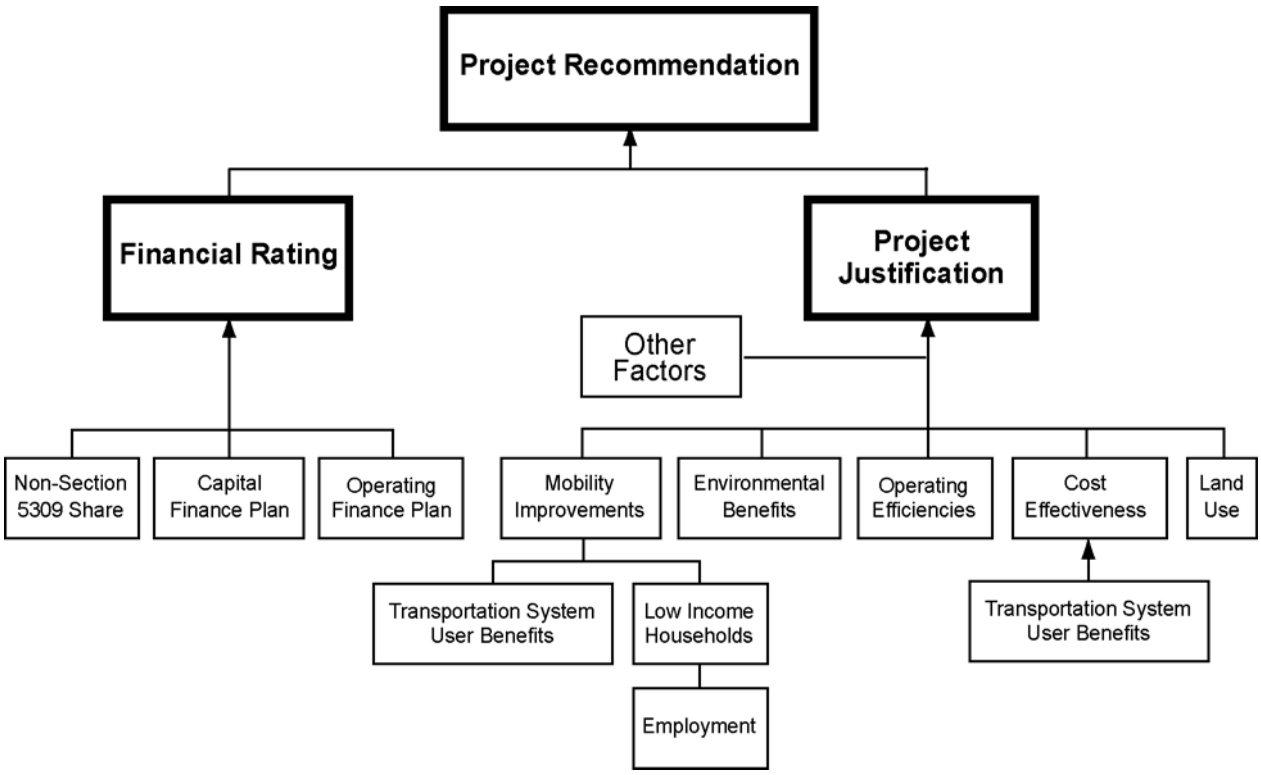
[84] Formerly, the FTA evaluated the "cost per new rider" as a measurement of cost effectiveness. The "transportation system user benefits" focuses on the potential reduction in travel time and out-of-pocket costs that riders would incur in taking a trip. U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 2.

[85] According to FTA, "Transit-supportive land use, whether it is a factor of existing patterns, existing local policies, or planned future development which targets development around the Federally-assisted project, has been an important indicator of future project success. Additionally, TEA-21 added two new land-use-related considerations to the project evaluation process: The reduction in local infrastructure costs achieved through compact land use development, and the cost of suburban sprawl." 65 Fed. Reg. 76872 (Dec. 7, 2000) (citing 49 U.S.C. §§ 5309(e)(3)(B), (C) (2003)). In evaluating land use, FTA looks at eight factors: (1) existing land use; (2) impact of proposed New Starts project on land use; (3) growth-management policies; (4) transit-supportive corridor policies; (5) supportive zoning regulations near transit stations; (6) tools to implement land use policies; (7) the performance of land use policies; and (8) existing and planned pedestrian facilities, including access for pedestrians with disabilities. 65 Fed. Reg. 76884 (Dec. 7, 2000).

[86] 49 C.F.R. pt. 611, App. A (1999). Other factors given consideration include multimodal emphasis of the project; environmental justice; opportunities for increased access by low-income persons; livable community initiatives; alternative land use development scenarios; innovative financing; procurement and construction techniques; and empowerment zones. *Id*.

[87] 65 Fed. Reg. 76871 (Dec. 7, 2000).

Figure 4.1—New Starts Rating Process



New Starts projects must be carried out under an FFGA[88] executed by FTA based on the results of a rating and evaluation process,[89] the technical capability of the sponsor, and a determination that no outstanding issues might interfere with successful completion of the project.[90] FFGAs are negotiated between FTA and recipients. As the name implies, in the event of cost overruns, the recipient is contractually and legally obligated to complete the project and may not request additional funds from FTA. The FFGA covers the project's scope and schedule, the length of the system, number of stations, and its cost.[91] FFGAs are used in all New Start projects requiring more than $25 million in Section 5309 New Start funds.

To obtain New Start funding, the grantee must first perform a local or regional review of alternatives, develop preliminary engineering plans, and secure FTA approval for final design.[92] The ratings developed by FTA for each of the project justification criteria and for local financial commitment form the basis for the overall rating for each project. FTA assigns overall ratings of "highly recommended," "recommended," and "not

[88] A Full Funding Grant Agreement (FFGA) is an instrument that defines the scope of the project, the FTA contribution to it, and other terms and conditions. 49 C.F.R. § 611.5 (2003). An FFGA "establishes the terms and conditions for federal participation, including the maximum amount of federal funds available for the project, which cannot exceed 80 percent of its estimated net cost. The grant agreement also defines a project's scope, including the length of the system and the number of stations; its schedule, including the date when the system is expected to open for service; and its cost. To obtain a grant agreement, a project must first progress through a local or regional review of alternatives, develop preliminary engineering plans, and obtain FTA's approval for final design." (U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 4).

See FTA Circular 5200.1.

[89] To be funded, the project must be rated by FTA as "recommended" or "highly recommended." 49 C.F.R. § 611.7(d)(3)(i) (2003).

[90] 49 C.F.R. § 611.7(d) (2003).

[91] U.S. GEN. ACCOUNTING OFFICE, MASS TRANSIT: STATUS OF NEW STARTS TRANSIT PROJECTS WITH FULL FUNDING GRANT AGREEMENTS 2 (1999).

[92] U.S. GEN. ACCOUNTING OFFICE, *supra* note 11, at 4.

recommended," to each proposed project.[93] FTA submits an annual report to Congress of project ratings. Note, however, that a rating of "recommended" or higher does not ensure a federal funding recommendation. Those proposals that have been rated "highly recommended" or "recommended," and have been sufficiently developed for consideration of an FFGA are eligible for FTA recommendation to Congress of funding.[94] The purpose of the project rating process is to bring greater uniformity to the New Start grantmaking process. Historically, FTA lacks sufficient appropriations to fully fund all of the projects that are ready for New Starts designation; in many instances, the then existing grantmaking process was circumvented by "earmarks." "Earmarks" are provisions contained in legislation by which Congress directs that federal funds be directed, or "earmarked," for a specific local project. Congress became concerned that implementation of transit projects depended too greatly upon the Congressional delegation of the local project sponsor to earmark funds and too little upon an objective grantmaking process.

Proposals for FTA capital investment funds[95] for new transit fixed guideway systems and extensions to existing systems must be based on the results of alternatives analysis and preliminary engineering.[96] The *alternatives analysis* (also known as an MIS or multimodal corridor analysis) evaluates several modal and alignment options for satisfying mobility demands in a corridor, and examines information on the costs, benefits, and impacts of alternative strategies to address a transportation problem in a particular corridor.[97] The alternative analysis is performed by a contractor; it includes a public participation process and is submitted to FTA. The alternative strategies evaluated must include a no-build alternative, a baseline alternative, and build alternatives.[98] Local funding sources for building and operating the project must be identified. Competition for New Starts funds is sharp; hence, FTA looks very closely at the proposed local match. Despite the much enhanced transit funding provided by Congress, New Starts funding remains a competition for very scarce federal funds. The lower the proposed federal share, the better position a grantee is in to obtain

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[93] 49 U.S.C. § 5309(e)(6) (2003); 49 C.F.R. § 611.13 (2003).

[94] 46 Fed. Reg. 87687 (Dec. 7, 2000).

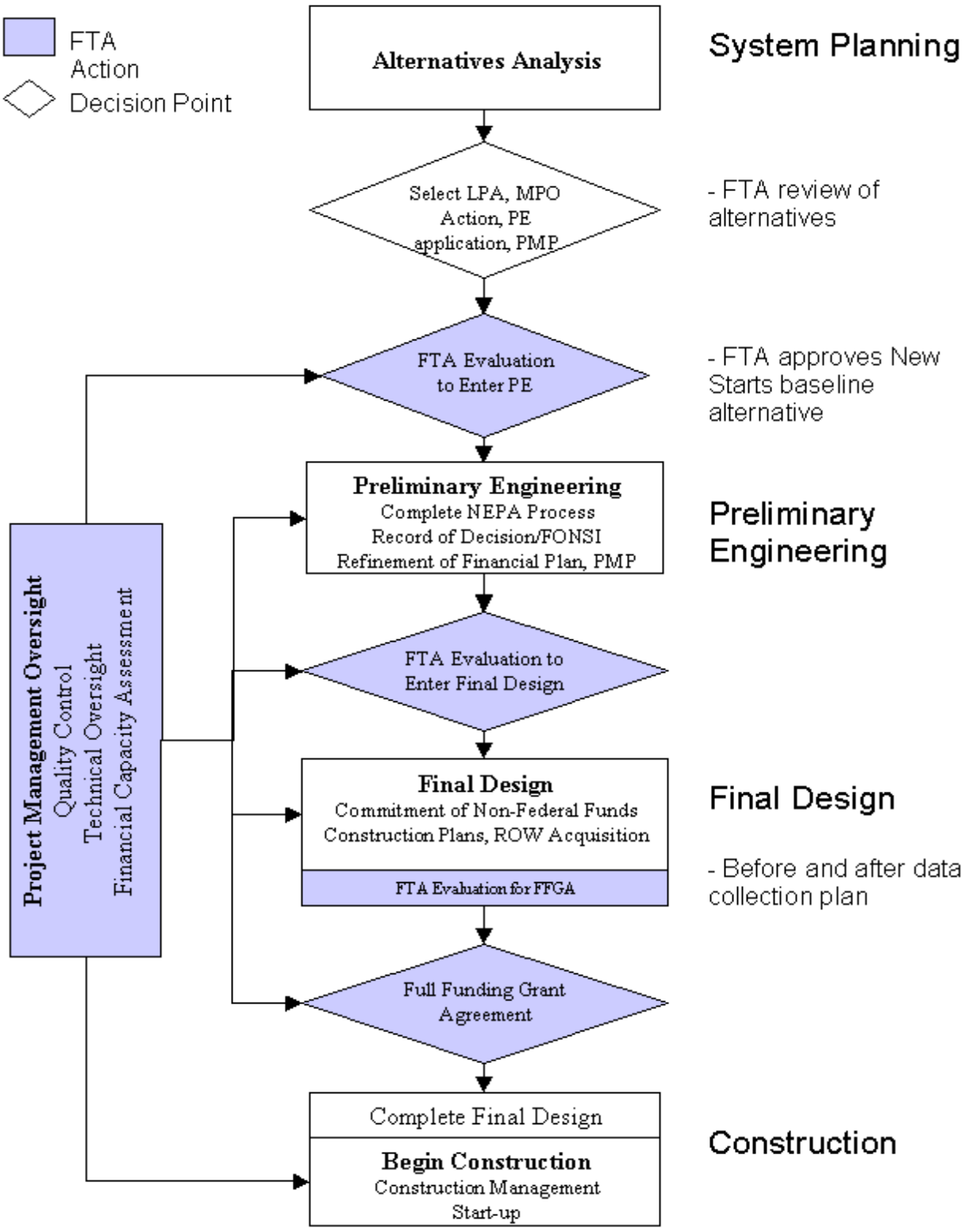
[95] 49 U.S.C. § 5309 (2003).

[96] 49 C.F.R. § 611.7 (2003).

[97] 65 Fed Reg. 76868 (Dec. 7, 2000). "During the preliminary engineering phase, project sponsors refine the design of the proposal, taking into consideration all reasonable design alternatives—which results in estimates of costs, benefits, and impacts." U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 2.

[98] ALI TOURAN, RISK ASSESSMENT IN FIXED GUIDEWAY TRANSIT SYSTEM CONSTRUCTION (1994).

Figure 4-2—FTA New Starts Planning and Project Development Process



approval. FTA looks for ways to stretch/leverage the funds provided by Congress, and a project with a proposed 51 percent federal share has a better chance of advancement than does a proposed project with a 59 percent federal share. A wide range of stakeholders, including the public, should be involved in the process. The alternatives analysis may include preparation of a Draft EIS or EA. The alternatives analysis is complete when local decisionmakers settle on a locally preferred alternative and it is included in the MPO's[99] financially constrained long-range regional transportation plan.[100]

At this point, the project sponsor may ask the FTA regional office for permission to initiate preliminary engineering. The proposal must include information that proves the project's readiness to proceed, including adoption of the project in the metropolitan transportation plan, and the programming of the preliminary engineering study in the TIP,[101] as well as the sponsor's technical ability to undertake the preliminary engineering. The proposal must also address project justification and local financial commitment. At this point in the process, it may be sufficient merely to demonstrate a reasonable financial plan that identifies potential sources of local funds adequate to construct the project.[102] As a practical matter, a financial plan that does not include a dedicated funding source sufficient both to maintain and operate the completed New Start project is doomed. However, FTA approval[103] to move the project to preliminary engineering does not constitute a commitment to federal funding of either the final design or construction.[104]

The *preliminary engineering* may proceed only after the transit agency has completed the alternatives analysis, the MPO has adopted the proposed project into its long range plan, FTA has determined that the sponsor has adequate technical ability to carry out the preliminary engineering, and all other statutory and regulatory requirements have been met.[105] Preliminary engineering is ordinarily funded with 49 U.S.C. §§ 5303 and 5307 funds, local revenue, and flexible funding under CMAQ[106] and STP.[107] During preliminary engineering, the sponsors refine the project's design, taking into account all reasonable design alternatives. They estimate the project's cost, and complete the EIS, if necessary,[108] and project and fleet management plans, and secure local funding commitments. At this point, nearly all of the local funds should have been committed, and provisions should have been made for cost overruns. FTA will not issue a final approval and will not enter into an FFGA until it is satisfied that the grantee has arrangements in place to complete and operate the project, even in the face of cost overruns.

The evidence of a local funding commitment should include identification of stable and dependable funding sources to construct, maintain, and operate the proposed project.[109] The sponsor's Finance Plan must identify the amounts to be funded by the New Starts funding,[110] as well as federal formula and flexible funds. It should identify both the 20 percent local match required by federal law as well as additional nonfederal capital funding ("overmatch"), and the degree to which initial planning has been concluded without New Starts funds.[111]

"Overmatch" was added as a statutory consideration by TEA-21. An abundance of "overmatch" can help tilt the scales in favor of a project, since FTA seeks to fund a large number of New Starts projects with limited economic resources, and enhanced funding suggests a project will not encounter financial problems jeopardizing the federal contribution. In recent years, the average prevailing federal share has been around 50-55 percent, which demonstrates the extent to which local sponsors are willing to put up their own funds in order to obtain federal funds. Hence, in many ways, it is a bidding war among applicants seeking FTA funding. Sponsors are also encouraged by FTA to consider policies and actions that would advance the benefits, the financial feasibility, and the safety of the project.[112]

After the NEPA process has been completed, the project sponsors have demonstrated adequate technical capability to carry out the final design, and all other legal requirements have been satisfied, the FTA may authorize the project sponsor to proceed to a final design of the project.[113] At this point, the FTA issues an ROD.[114] As noted above, in Section 3—Environmental

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[99] In Section 2—Transportation Planning, we discuss the critical role of the MPO. Also included in that discussion are two critical facts: (1) no project can be funded unless it is included in the long-range regional transportation plan; and (2) projects must be implemented in the priority listed in the planning process.

[100] 49 C.F.R. § 611.7(a)(4) (2003); 65 Fed. Reg. 76868-69 (Dec. 7, 2000).

[101] The TIP is described in detail in Section 2—Transportation Planning, above.

[102] 65 Fed. Reg. 76870 (Dec. 7, 2003).

[103] 49 U.S.C. § 5309(e)(6) (2003).

[104] 65 Fed. Reg. 76869 (Dec. 7, 2000).

[105] 49 U.S.C. §§ 5309(e)(6), 5328(a)(2) (2003); 49 C.F.R. § 611.7(a) (2003).

[106] 23 U.S.C. § 149 (2003).

[107] 23 U.S.C. § 133 (2003). 65 Fed. Reg. 76869 (Dec. 7, 2000). The Surface Transportation Program (STP) is the largest source of funds available from FHWA. The federal share is up to 80 percent, and funds may be used for all FTA programs except operating assistance.

[108] *See* Section 3—Environmental Law, above.

[109] 49 U.S.C. § 5309(e)(1)(C) (2003).

[110] 49 U.S.C. § 5309 (2003).

[111] 65 Fed. Reg. 76874-75 (Dec. 7, 2000).

[112] 65 Fed. Reg. 76869 (Dec. 7, 2000).

[113] 49 C.F.R. § 611.7(c) (2003). "Final design is the last phase of project development before construction and may include right-of-way acquisition, utility relocation, and the preparation of final construction plans and cost estimates." (U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 4.)

[114] 65 Fed. Reg. 76869 (Dec. 7, 2000).

Law, in order for the project to go forward, where appropriate, an EIS must be prepared, or a FONSI made.

The last phase of the project, *final design,* includes acquisition of the necessary rights-of-way, relocation of the utilities, and preparation of final construction plans (including construction management plans), detailed specifications, cost estimates, and bid documents.[115] Final design is eligible for New Starts funding.[116]

Federal funding may cover no more than 80 percent of the estimated total net cost of the project (though because New Starts funds are oversubscribed, and dependent on annual Congressional appropriations, they rarely reach the 80 percent ceiling). State or local sources must augment the federal share to cover the total project cost.[117] The grantee is responsible for covering all cost overruns,[118] unless the funding agreement is amended.[119] Examples of projects that have exceeded their budgets include:

- The South Boston Piers transitway project was 28 percent over budget, primarily because of the project's early design, which subsequently required modification, as well as unanticipated construction delays.
- The BART's extension to San Francisco International Airport was 27 percent over budget, primarily because of higher than anticipated construction costs due to an overheated Bay Area economy.
- San Juan's Tren Urbano rapid transit line was 34 percent over budget because of major scope changes and higher than anticipated contract costs.[120]

Various projects have had to restructure their funding in order to avoid collapse.

An example is the Massachusetts Bay Transportation Authority's (MBTA) 1.5-mile underground transitway to connect its existing transit system with the South Boston Piers area. In 1994, FTA entered into an FFGA with MBTA under which the federal government would pay $331 million (80 percent) of the projected total first phase cost of $413 million. But by 2000, schedule delays and design changes had put the project 3 years behind schedule, and projected costs had bloated to $601 million, or 46 percent more than the original cost. Congressional concern over the project's cost was expressed in the Conference Report accompanying the Department of Transportation and Related Agencies Appropriations Act of 2000, which made funds contingent on MBTA's completion of a finance plan. MBTA proposed to use the original $331 million in New Starts funding to cover 55 percent of the project's cost, supplemented with $150 million from the Formula Grant Program to cover 25 percent, putting the federal share back up to 80 percent of the project's new projected cost. The remaining $120 million, or 20 percent, would be covered in state or MBTA bonds; to cover unanticipated expenses, MBTA established a $50 million capital reserve bond fund.[121]

3. Project Management Plans

The statute requires a grantee under the Federal Transit Act or the National Capital Transportation Act to prepare and utilize a "project management plan" approved by the Secretary if it is undertaking a "major capital project."[122] The plan must contain a wide variety of items that are intended to demonstrate the grantee's ability to carry out the project efficiently and cost-effectively.[123] The FTA will notify the grantee as to

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[115] 65 Fed. Reg. 76869 (Dec. 7, 2000).

[116] 49 U.S.C. § 5309 (2003). *See* 65 Fed. Reg. 76864 (Dec. 7, 2000); 64 Fed. Reg. 17062 (Apr. 7, 1999).

[117] In assessing the stability of a project's local financial commitment, FTA assesses the project's finance plan for evidence of stable and dependable financing sources to construct, maintain, and operate the proposed system or extension. In evaluating this commitment, FTA is required to determine whether (1) the proposed project's finance plan incorporates reasonable contingency amounts to cover unanticipated cost increases; (2) each proposed local source of capital and operating funds is stable, reliable, and available within the timetable for the proposed project; and (3) local resources are available to operate the overall proposed mass transportation system without requiring a reduction in existing transportation services.

(U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 5).

[118] Cost overruns typically are caused by higher than anticipated construction costs, schedule delays, and/or project scope changes and system enhancements. (U.S. GEN. ACCOUNTING OFFICE, *supra* note 91, at 2.)

[119] U.S. GEN. ACCOUNTING OFFICE, *supra* note 11, at 4.

[120] U.S. GEN. ACCOUNTING OFFICE, *supra* note 91, at 3–4.

[121] Letter from GAO Director Phyllis Scheinberg to Hon. Richard Shelby and Hon. Frank Wolf (Nov. 9, 2000).

[122] 49 U.S.C. § 5327(a) (2003). Strangely, the statute does not require recipients of funds under 23 U.S.C. § 103(e)(4) to submit a plan, although it does permit the Secretary to use funds for oversight of a project developed under 23 U.S.C. § 103(e)(4). 49 U.S.C. § 5327(c) (2003). The FTA's own regulations, however, mandate that a 23 U.S.C. § 103(e)(4) funding recipient provide such a plan. 49 C.F.R. § 633.3(b) (2003). The regulation defines a "major capital project" as a project that: (1) involves the construction of a new fixed guideway or extension of an existing fixed guideway; (2) involves the rehabilitation or modernization of an existing fixed guideway with a total project cost in excess of 100 million dollars; or (3) the Administrator determines is one for which a project management oversight program will benefit the FTA or the recipient. 49 C.F.R. § 633.5(1) through (3) (2003). Projects that fall within the latter point will typically be any expected to have a total cost in excess of $100 million or that are of a sort that have previously been shown to benefit from the program. 49 C.F.R. § 633.5(3)(i) (2000). This particularly includes projects using new technologies or that are of a "unique nature" for the grantee. 49 C.F.R. § 633.5(3)(ii) through (iv) (2003). Also, if "past experience" with the grantee "indicates…the appropriateness" of applying the program, the Administrator may choose to employ it. 49 C.F.R. § 633.5(3)(v) (2003).

[123] The items that must be included or shown are: (1) adequate staff organization with well-defined reporting relationships, statements of functional responsibilities, job descriptions, and job qualifications; (2) a budget covering the project management organization, appropriate consultants, property acquisition, utility relocation, system demonstration staff, audits, and miscellaneous payments the recipient may be prepared to justify; (3) a construction schedule for the project; (4) a document control procedure; (5) a change order procedure that includes a documented, systematic approach to the handling of construction change orders; (6) organizational structures,

when it should submit the project management plan.[124] This notification will usually be made during the grant review process, but may come at any time once the grantee has initiated a federally financed project.[125] The regulations offer some finesse on the statute's description of the review process, giving the Administrator the power to ask the grantee to modify its plan to address any concerns the FTA may have, rather than simply accepting or rejecting the entire plan.[126]

Once the plan has been submitted, the Secretary has 60 days to approve or deny it.[127] In the event that the Secretary rejects the plan, an explanation for the reasons behind the rejection must be given to the grantee.[128] A grantee submitting a plan must agree to give the FTA or its chosen contractor access to the relevant construction sites and records pertaining to the project to the extent reasonably necessary.[129]

Finally, once the Administrator approves the plan, the grantee must begin its implementation.[130] If a grantee makes modifications to an already approved plan, it is required to submit the proposed changes, and an explanation for their necessity, to the Administrator for approval.[131] A grantee is obligated to provide periodic updates of the plan to the Administrator.[132] It is important that the grantee prepare the periodic reports carefully, for in the event of a cost overrun that results in a request to the FTA for additional funds, the FTA will scrutinize the reports to determine whether the grantee properly managed the project, could or should have detected the possibility of the overrun, and took appropriate measures to prevent or minimize the additional costs.

4. Project Management Oversight

In the 1980s, a number of FTA New Starts projects encountered quality, cost, and schedule problems.[133] Because it was vulnerable to fraud, waste, abuse, and mismanagement, the FTA's federal grants oversight program was placed on the U.S. General Accounting Office's high-risk list, though it has since been removed.[134] Congress addressed this concern in a periodic transit reauthorization bill, STURAA,[135] which authorized the FTA's project management oversight (PMO) program and established a funding mechanism for overseeing major capital projects.[136] PMO consists of monitoring major capital projects to determine whether they are on time, on budget, in conformity with design criteria, constructed according to approved plans and specifications, and are otherwise being efficiently and effectively implemented.[137] By 2000, the PMO program was overseeing construction of more than 100 major capital projects (defined by FTA as those costing more than $100 million) totaling more than $47 billion.[138]

The Secretary ordinarily may use only one-half of 1 percent of the project's funding to finance a contract for overseeing a construction project within the statute's purview.[139] The duties of a PMO contractor may include reviews or audits for purposes of determining safety,

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management skills, and staffing levels required throughout the construction phase; (7) quality control and quality assurance functions, procedures, and responsibilities for construction, system installation, and integration of system components; (8) materials testing policies and procedures; (9) internal plan implementation and reporting requirements; and (10) criteria and procedures to be used for testing the operational system or its major components. 49 U.S.C. § 5327(a)(1) through (10) (2003).

[124] 49 C.F.R. § 633.21(b)(1) (2003).

[125] *Id*. In either instance, once notification has been given, the grantee has a minimum of 90 days to prepare and submit the plan. 49 C.F.R. § 633.21(b)(2) (2003).

[126] 49 C.F.R. § 633.21.

[127] 49 U.S.C. § 5327(b)(1) (2003). If the Secretary is unable to completely review the plan in that time, the recipient must be notified of the reason for the delay and be provided an estimate of when the review will be completed. 49 U.S.C. § 5327(b)(1) (2003).

[128] 49 U.S.C. § 5327(b)(2) (2003).

[129] 49 U.S.C. § 5327(d) (2003).

[130] 49 C.F.R. § 633.27(a) (2003).

[131] 49 C.F.R. § 633.27(b) (2003).

[132] These shall include, but not be limited to: (1) the project budget; (2) the project schedule; (3) the status of both operating and capital financing; (4) ridership estimates with an operating plan; and (5) the status of local efforts to enhance ridership when estimates are contingent upon the success of such efforts. 49 C.F.R. § 633.27(c)(1) through (5) (2003). In addition to the aforementioned updates, the recipient must submit a report to the Administrator on a monthly basis, reflecting the project's status in regard to budget and schedule. 49 C.F.R. § 633.27(d) (2003).

[133] In 1983, the UMTA (now the FTA) conducted a review of the manner in which it provided oversight for grantees' major capital projects. This review led to the development of a national project management oversight program [the PMO program] that relied on independent contractors for its administration. However, because Congressional appropriations had not been allocated to support it, funding the PMO program proved difficult. Thus UMTA was obliged to divert funds from other activities to perpetuate the PMO program. Eventually, UMTA was able to convince Congress of the benefits of the system in terms of reducing costs and increasing efficiency in its grantees' project. After stopgap funding, a 1987 reauthorization bill included project management oversight as a regular part of the UMTA grant program. 54 Fed. Reg. 36708 (1989). The legislation amending the Act was the Surface Transportation and Uniform Relocation Assistance Act of 1987, Pub. L. No. 100-17 (1987). Since 1987, the PMO program has been effectively unchanged. 49 C.F.R. § 633.1 (2000).

[134] U.S. GEN. ACCOUNTING OFFICE, *supra* note 11, at 2.

[135] Pub. L. 100-17.

[136] Funding is described in 49 C.F.R. § 633.19 (2003).

[137] 49 C.F.R. § 633.5 (2003).

[138] U.S. GEN. ACCOUNTING OFFICE, MASS TRANSIT: PROJECT MANAGEMENT OVERSIGHT BENEFITS AND FUTURE FUNDING REQUIREMENTS 4 (2000).

[139] 49 U.S.C. § 5327(c)(1) (2003). An additional one-quarter of 1 percent of funding may be used if the project is being developed under 49 U.S.C. § 5309 (principally fixed guideway systems and related projects).

procurement, management, or financial compliance with the approved plan, as well as providing technical assistance to the grantee to correct deviations from the approved project management plan.[140] The federal government must cover the entire cost of the PMO contract.[141] The statute requires grantees whose projects have an estimated cost of $1 billion or more to submit an annual financial plan for the project to the Secretary.[142] The plan is to be based on "detailed annual estimates" of the cost to complete the remaining parts of the project and on reasonable assumptions of future increases in costs necessary to bring the project to completion.[143]

Once the FTA has determined the program is applicable, project management oversight services should be initiated as soon as is practical.[144] The program will thus be ordinarily put into effect during the preliminary engineering phase, but the Administrator has the ability to determine at any time that a project is a "major capital project."[145] Any person or entity may be used to render project management oversight services, with only two significant exceptions: (1) a grantee may not provide such services for its own project, and (2) a person or entity may not provide such services where a conflict of interest exists.[146] The FTA must use ordinary federal procurement procedures for obtaining PMO transit services.[147]

The FTA lacks sufficient personnel to perform PMO in-house. Accordingly, PMO is performed by third party contractors retained and trained by FTA. PMO usually begins during the preliminary engineering phase of the project. The PMO program is designed to assure that grantees that are constructing major capital projects have the qualified staff and procedures necessary to successfully complete the project according to accepted engineering principles. FTA contracts with engineering firms, which provide PMO services under the guidance of the FTA, to augment its technical staff.[148] The oversight contractor reviews the grantee's plan for managing and constructing the project as early as the project design phase. The process measures how well projects remain on schedule and budget once FFGAs have been signed, and the success of New Starts projects once they are up and running.[149]

From the practical perspective of the grantee, PMOs can be trouble. They justify their existence by finding problems, and they tend to find them. Though not involved in the "acceptance" of project elements, PMOs can recommend that FTA not accept the project for payment until they're satisfied, sometimes making life difficult for both the grantee and its contractors, and subjecting the grantee to delay claims because, at the PMO's insistence, the grantee will not accept the work as satisfactorily completed. Even where a transit recipient's counsel insists there is no basis for a contractor claim, the FTA may hold up grant funds because the PMO is unhappy with how the project is proceeding. Hence, PMOs have enormous discretion that transit recipients may be powerless to resist.

Once the PMO plan has been approved, the oversight contractor monitors the project to assess whether it is being performed on schedule, within budget, and according to approved plans and specifications.[150] As a result of its less-than-satisfactory experience with the Los Angeles subway project,[151] in 1998 the FTA ex-

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[140] 49 U.S.C. § 5327(c)(2) (2003).

[141] 49 U.S.C. § 5327(c)(3) (2003).

[142] 49 U.S.C. § 5327(f) (2003).

[143] *Id*.

[144] 49 C.F.R. § 633.13 (2003).

[145] *Id*. Factors that may lead to the conclusion that something is a "major capital project" include: (1) the construction of a new fixed guideway or extension of an existing fixed guideway; (2) the rehabilitation or modernization of an existing fixed guideway with a total project cost in excess of 100 million dollars; or (3) the Administrator determines the project is one for which a project management oversight program will benefit the FTA or the recipient. 49 C.F.R. § 633.5(1) through (3) (2003). Projects that fall within the latter point will typically be any that might be expected to have a total cost in excess of $100 million or which are of a sort that have previously been shown to benefit from the program. 49 C.F.R. § 633.5(3)(i) (2003). This especially includes projects using new technologies or that are of a "unique nature" for the grantee. 49 C.F.R. § 633.5(3)(ii) through (iv) (2003). Also, if "past experience" with the grantee "indicates…the appropriateness" of applying the program, the Administrator may choose to employ it. 49 C.F.R. § 633.5(3)(v) (2003).

[146] 49 C.F.R. § 633.17(a)(1) and (2) (2003).

[147] 49 C.F.R. § 633.17(b) (2003). See Section 5—Procurement, for a discussion of general federal procurement procedures.

[148] These contractors are selected through the competitive bidding process. Typically, these PMO contracts authorize 5 years and 90,000 hours of work. (U.S. GEN. ACCOUNTING OFFICE, *supra* note 138, at 5).

[149] U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 2.

[150] FTA requires that the oversight contractor provide monthly reports containing any corrective action that may be needed. (U.S. GEN. ACCOUNTING OFFICE, *supra* note 138, at 5.)

[151] In 1997, management and financial difficulties with the Los Angeles subway project caused FTA to require the grantee to prepare a recovery plan. FTA's review of that plan found that the grantee's revenues projected in the plan would be much lower than expected and insufficient to complete the project and operate the rest of the transportation system. Subsequently, the grantee had to suspend the construction of two planned extensions to the subway for which FTA had already committed funds through a full funding grant agreement.

(U.S. GEN. ACCOUNTING OFFICE, *supra* note 138, at 8). By 2001, two segments of the Los Angeles New Starts project had been suspended for more than 3 years, and the FTA informed the project's sponsors that it no longer had sufficient funding to cover the suspended segments. (U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 3). "After opening almost 60 miles of rail lines in the last decade and being forced by a federal court consent decree to improve its long-neglected bus service, the MTA faces a massive $438-million operating deficit over the next decade." Jeffrey Rabin, *MTA Strike Has Deep Roots in Agency's Past Mistakes,* LOS ANGELES TIMES, Sept. 19, 2000, at A24.

panded its review to include an assessment of a grantee's current and future financial ability to undertake and complete a new project and cover operating costs, and the financial impact of the project on the recipient's total transit system.[152] For fiscal year 2002, the FTA more strictly scrutinized the ability of the grantees to build and operate proposed projects in an attempt to assure that there were no outstanding issues that might jeopardize the project once an FFGA is signed.[153] However, FTA is not involved in the inspection and acceptance of construction work; that is the responsibility of the grantee.[154]

J. THE JOB ACCESS AND REVERSE COMMUTE PROGRAM

An unconventional provision of TEA-21, Section 3037, creates a special grant system for "job access" and "reverse commute" projects by transit agencies.[155] The motivation behind this new grant system was the broad reform of federal welfare programs in 1996, which would require many aid recipients to find employment following the termination of government benefits.[156] As a result of changes in urban development in the preceding decades, the majority of new job growth took place in suburban areas, while the majority of aid recipients lived in urban areas.[157] Compounding the problem further, a sizeable portion of aid recipients neither owned cars nor had access to transit service that would enable them to reach sites of new job creation.[158] Consequently, Congress decided to formulate a system designed to compensate for these imbalances.[159]

The Act authorizes the formation of a grant system for "job access" and "reverse commute" projects.[160] A job access project is designed to transport welfare recipients and other eligible low-income individuals[161] to and from jobs and activities related to their employment.[162] A reverse commute project is designed to transport the general public to suburban employment venues.[163] Grants funded under these programs may not be used for planning and coordination activities, and may not supplant existing funding sources.[164] Funds are provided on a discretionary basis as follows: 60 percent to urbanized areas above 200,000 in population; 20 percent to areas under 200,000 in population; and 20 percent to nonurbanized areas. These caps were removed by appropriations laws beginning in fiscal year 2001.

Grants for these types of projects may only be given to "qualified entities."[165] Qualified entities are required to submit applications for funding to the Secretary, who must evaluate them in light of a number of factors for consideration.[166] Grantees are to be selected on a competitive basis.[167] A grant given for either type of project may not exceed 50 percent of the total project cost.[168]

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[152] U.S. GEN. ACCOUNTING OFFICE, *supra* note 138, at 2.

> In assessing financial condition, the financial consultants consider historical trends and current financial information contained in the grantees' audited financial statements and other relevant reports. In assessing financial capacity, the consultants consider the nature of funds pledged to support the grantees' operating deficits and capital programs while considering the grantees' capital, operating, and maintenance costs. These assessments are also designed to identify issues that could affect projects in the future.

Id. at 8–9.

[153] U.S. GEN. ACCOUNTING OFFICE, *supra* note 83, at 2.

[154] U.S. GEN. ACCOUNTING OFFICE, *supra* note 138, at 4.

[155] Transportation Equity Act for the 21st Century (TEA-21), Pub. L. No. 105-178, 112 Stat. 107 (1998).

[156] TEA-21 § 3037(a)(7).

[157] TEA-21 § 3037(a)(1).

[158] TEA-21 § 3037(a)(2) and (5).

[159] Information on the job access and welfare-to-work program can be found at Fed. Transit Admin., *Job Access/Reverse Commute Program* (visited Aug. 13, 2003), http://www.fta.dot.gov/library/reference/statsum01/jarc.html.

[160] TEA-21 § 3037(b)(2)(A).

[161] An "eligible low-income individual" is a person whose family income is at or below 150 percent of the poverty line as defined by 42 U.S.C. § 9902(2). TEA-21 § 3037(b)(1).

[162] TEA-21 § 3037(b)(2)(B). Such grants may be used for capital projects and operating expenses related to offering transit service, promoting the use of transit by workers with nontraditional schedules, and encouraging use of transit vouchers and employer-provided bus passes. TEA-21 § 3037(b)(2)(B)(i) through (iv).

[163] TEA-21 § 3037(b)(2)(C). These grants may be used for subsidizing the cost of operating a reverse commute route, purchasing or leasing a vehicle specifically for the purpose of transporting employees to a particular site, and otherwise facilitating the provision of mass transportation services to suburban employment opportunities. TEA-21 § 3037(b)(2)(C)(i) through (iii).

[164] 63 Fed. Reg. 60168 (Nov. 6, 1998).

[165] The term "qualified entity" embraces two categories: (1) applicants that have proposed an eligible project in an urbanized area with a population of at least 200,000, and have been selected by the appropriate metropolitan planning organization, that meets the requirements of TEA-21; or (2) applicants that have proposed an eligible project in an urbanized area with a population of at least 200,000 or an area other than an urban area, and have been selected by the chief executive officer of the state in which the area is located, that meets the requirements of TEA-21. TEA-21 § 3037(b)(4)(A) and (B).

[166] Factors include, but are not limited to: (1) the percentage of the population in the area to be served by the applicant that are aid recipients; (2) if the application is for a job access project, the need for additional services in the area to be served by the applicant to transport welfare recipients and eligible low-income individuals to and from specified jobs, training, or other employment support services, and the extent to which the proposed services will address those needs; (3) the extent to which the applicant demonstrates an innovative approach that is responsive to identified service needs; and (4) the extent to which the applicant demonstrates that the community to be served has been consulted in the planning process. TEA-21 § § 3037(f)(1), (2), (5), and (7).

[167] TEA-21 § 3037(g).

[168] TEA-21 § 3037(h)(1).

The remainder of the project's cost must be provided by cash sources other than farebox revenue, but may include amounts received under a service agreement or from a department or agency of the federal government other than the DOT.[169] All conditions on grants and planning that otherwise apply to funds made available under Section 5307 of the Federal Transit Act also apply to funds provided for either sort of project.[170]

The Job Access and Reverse Commute Program is designed to develop transport services that transport low income individuals and welfare recipients to and from jobs, and facilitate suburban employment opportunities. These funds may be used to finance capital projects and operating costs of equipment, facilities, and capital maintenance expenditures incurred in providing access to employment, promoting use of transit with employees having nontraditional work schedules, promoting use of transit vouchers for welfare recipients and eligible low income individuals, and promoting employer-provided transportation. Under this program, the federal share is 50 percent.[171]

K. THE FLEXIBLE FUNDING PROGRAM

ISTEA provided for flexible funding to support multimodal planning and project development. Stated in simplest terms, "flexible funding" means that FHWA funds can be used by FTA grantees for certain eligible projects, and FTA funds can likewise be "flexed" by FHWA grantees for certain eligible projects. To date, significantly more highway funds have been transferred for transit projects than have transit funds for highway projects. Though only $6 million was transferred from the highway trust funds to transit in the year preceding promulgation of ISTEA, by 1995, transfers grew to $802 million, and a record $1.6 billion was transferred to transit in 2000.[172] TEA-21 continued the flexible funding program. Many transit projects are eligible for flexible funding programs, including the CMAQ,[173] STP,[174] and, in some instances, the National Highway System Program (NHS).[175]

ISTEA tied use of CMAQ funds to projects designed to improve air quality and manage traffic congestion.[176] The principal purpose of the CMAQ program is to fund improvement projects that will enable nonattainment and maintenance areas to reduce transportation emissions.[177] Projects are funded that reduce transportation-related emissions in air quality nonattainment and maintenance areas under the Clean Air Act of 1990 for ozone, CO, and PM10.[178] CMAQ funds are apportioned to states according to a formula that takes into account the severity of their air pollution problems.[179] States are required to use CMAQ funds in nonattainment and maintenance areas.[180] More than $1 billion in CMAQ funding is authorized each year.

Projects and programs eligible for CMAQ funding must be derived from a conforming transportation plan and TIP and be included in the statewide program. The projects must be consistent with the air quality conformity provisions of the Clean Air Act[181] and NEPA, be included in the statewide program, and meet the eligibility requirements for funding set forth in Titles 23 and 49 of the U.S. Code.[182] FTA gives highest priority to those projects and programs set forth in the SIP as a TCM[183] likely to produce air quality benefits.[184]

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[169] TEA-21 § 3037(h)(2)(A)(1) and (2).

[170] TEA-21 § 3037(i) and (j).

[171] FED. TRANSIT ADMIN., *supra* note 18, at 18. Revenue from service agreements constitutes an eligible match, but revenue derived from fares is ineligible for match. Non-DOT federal transportation funding may serve as local match. 63 Fed. Reg. 60168 (Nov. 6, 1998).

[172] U.S. DEP'T OF TRANSPORTATION, INTERMODAL SURFACE TRANSPORTATION EFFICIENCY ACT: FLEXIBLE FUNDING OPPORTUNITIES FOR TRANSPORTATION INVESTMENTS 4 (1996).

[173] 23 U.S.C. § 149 (2003).

[174] 23 U.S.C. § 133 (2003).

[175] 23 U.S.C. § 103(b) (2003).

[176] RUSSELL LEIBSON & WILLIAM PENNER, LEGAL ISSUES ASSOCIATED WITH INTERMODALISM (Transit Cooperative Research Program, Legal Research Digest No. 5, 1996).

[177] 61 Fed. Reg. 50891 (Sept. 27, 1996).

[178] PM10 are fine particulate matters that may be inhaled deeply into the lungs. States wishing to use CMAQ funds in PM10 nonattainment or maintenance areas must consult with and consider the views of the relevant MPOs and obtain their concurrence, and the concurrence of the EPA regional office. 61 Fed. Reg. 50891 (May 9, 1995). These issues are discussed in greater detail above in Section 3—Environmental Law.

[179] Fed. Transit Admin., *supra* note 18, at 17.

[180] 61 Fed. Reg. 50891 (Sept. 27, 1996).

[181] Clean Air Act § 176(c) (2000).

[182] Decisions over which programs and projects to fund should be made cooperatively by the state Department of Transportation, the relevant MPOs, and state and local air quality agencies. They must be included in TIPs developed by the MPO in cooperation with the state and the local transit provider. 61 Fed. Reg. 50899 (Sept. 27, 1996). 23 C.F.R. § 450.300 (2003).

[183] These issues are discussed in greater detail in Section 3—Environmental Law.

[184] 61 Fed. Reg. 50891, 50892 (Sept. 27, 1996). TCMs set forth in the Clean Air Act of 1990, § 108(f)(1)(a), are the types of projects intended for CMAQ funding. They include:

- Programs for improved public transit;
- Restricted lanes for passenger buses or HOVs;
- Employer-based transportation management plans;
- Trip-reduction ordinances;
- Traffic flow improvement plans that reduce emissions;
- Fringe and transportation corridor parking facilities serving multiple-occupancy vehicle programs or transit service;
- Programs that limit or restrict vehicle use in downtown areas or other areas of emission concentration, particularly during peak periods;
- Provision of high-occupancy, shared-ride services;
- Nonmotorized or pedestrian corridors;
- Bicycle lanes and storage facilities;
- Programs to control extended idling of vehicles;

CMAQ funds may be used for new or expanded air quality improvement projects for the good of the general public. In most instances, this will consist of a capital investment in transportation infrastructure or creation of a new demand management strategy, though operating assistance is also available under certain circumstances.[185]

Examples of eligible projects include Intelligent Transportation Systems [ITS], improved transit, cleaner fuels, and bicycle and pedestrian programs.[186] CMAQ funds also may be used to create HOV lanes, provide ridesharing incentives,[187] and improve transit facilities. CMAQ eligibility hinges on whether the transit project represents an expansion or enhancement—if it is a system/service expansion, it is eligible; if it is a reconstruction or rehabilitation, it is not.[188] Eligible capital projects include new transit stations, terminals, centers, malls, intermodal transfer facilities, bus/HOV lanes, and park-and-ride facilities adjacent to a transit stop.[189] New transit buses, vans, locomotives, and rail cars for fleet expansion and augmented service, and alternative fuels refueling infrastructure are also eligible.[190] Public/private initiatives, such as joint ventures, and other innovative activities designed to improve air quality may also be eligible for CMAQ funding.[191] The determination of eligibility is handled by FTA on a case-by-case basis.[192] Among examples of how transit agencies have used CMAQ funds are:

- On smog alert days, the Rhode Island Public Transit Authority puts bags over the fare collection boxes in its buses and provides free service;[193]
- In Chicago, an additional vessel has been added to the RiverBus fleet;[194]
- In Worchester, Mass., the Union Station was renovated;[195]
- In Milwaukee, Freeway Flyer service has been provided to ethnic festivals, and the Milwaukee County Transit System purchased 10 trolleys;[196]

- Employer-sponsored flexible work schedule programs;
- Programs and ordinances to facilitate non-automobile travel and mass transit, and to reduce SOV travel; and
- Pedestrian and other nonmotorized paths, tracks, or areas.

[185] Operating assistance must be limited to new or expanded services. It should not displace other funding mechanisms, such as fees for services. Operating assistance should be limited to start up viable new services that improve air quality, and will eventually be able to cover their costs from other sources. In any event, CMAQ funding is available for operating assistance only for a maximum period of 3 years. 61 Fed. Reg. 50891, 50893 (Sept. 27, 1996). Examples include shuttle service feeding a transit station, circulator service in an activity center, and fixed-route service linking an activity center. According to FTA, "The intent is to support demonstrations of new transit or paratransit service to try to tap new markets and increase transit use. Service demonstrations will usually involve buses or vans since the service should be relatively low-cost and easily terminated if sufficient ridership is not achieved." 61 Fed. Reg. 50893-94 (Sept. 27, 1996). Operating assistance may be used for the start up of major new infrastructure projects (e.g., rail lines, bus/HOV lanes, and extensions to existing systems). Operating assistance under CMAQ is funded at an 80 percent federal share, though CMAQ funds may not replace previously committed funding from other sources. 61 Fed. Reg. 50894 (Sept. 27, 1996).

[186] *Testimony of FHWA Administrator Kenneth Wykle Before the U.S. House Comm. on Transportation & Infrastructure* (Mar. 8, 2000).

[187] "New or expanded rideshare programs, such as new locations for matching services, upgrades for computer matching software, etc. continue to be eligible and may be funded for an indefinite period of time." Moreover, the purchase price of a publicly-owned vehicle for a vanpool service need not be repaid to the federal government. 61 Fed. Reg. 50895 (Sept. 27, 1996).

[188] FTA notes that there are "gray areas," such as, for example, the reconstruction of an underutilized railroad terminal in conjunction with a new park-and-ride. In such circumstances, FTA focuses on whether it is reasonable to expect a significant increase in ridership as a result of the project. 61 Fed. Reg. 50893 (Sept. 27, 1996).

[189] In the latter instance, in CO or PM10 nonattainment or maintenance areas, air quality analysis may be required to ensure that no local "hot spot" violations are likely to occur. 61 Fed. Reg. 50893 (Sept. 27, 1996).

[190] One-for-one vehicle replacements are also eligible in CO and PM10 nonattainment and maintenance areas. Automobiles used by the transit provider are ineligible for CMAQ funding. 61 Fed. Reg. 50893 (Sept. 27, 1996). The conversion of individual conventionally-powered vehicles to alternative fuels is not eligible for CMAQ funding, unless the conversion or replacement is of centrally-fueled fleets, and provided that the fleet conversion is in response to a specific Clean Air Act requirement (e.g., the clean fuel program required of "serious" and worse ozone nonattainment areas), or the fleet conversion is identified in the SIP as an emissions reduction strategy in a nonattainment area of the maintenance plan. 61 Fed. Reg. 50894 (Sept. 27, 1996).

[191] 61 Fed. Reg. 50894 (Sept. 27, 1996).

[192] For example, "Major system-wide upgrades, such as advanced signal and communications systems which improve speed and/or reliability of transit service will likely be eligible, whereas in-kind replacements will not be." Generally speaking, transit-oriented development (retail and other services located in or around transit facilities) is ineligible for CMAQ funding. However, a child-care center adjacent to a transit stop could be funded as an experimental pilot project. 61 Fed. Reg. 50893 (Sept. 27, 1996). Proposals for CMAQ funding should include a precise description of the proposed project (including its size, scope, and timetable), and an assessment of the proposal's anticipated emissions reduction. States must also submit annual reports specifying the activities conducted under the CMAQ program during the preceding fiscal year. 61 Fed. Reg. 50898 (Sept. 27, 1996).

[193] Brian Jones, *Ride Out the Heat for Free,* PROVIDENCE J. BULL., Jul. 23, 2001, at 1A.

[194] *Chicago River Provides Alternative to Wacker Drive Construction,* PR NEWSWIRE, Jan. 31, 2001.

[195] Andi Esposito, *Mission Remains Clouded,* SUNDAY TELEGRAM, Dec. 10, 2000, at E1.

[196] Linda Spice, *County May Cut Festivals,* MILWAUKEE J. SENTINEL, Dec. 7, 2000, at 3B.

• Dallas and Fort Worth converted their public sector vehicles to alternative fuels;

• The Philadelphia Bicycle Network designed and constructed a city-wide network of bicycle routes; and

• New York City purchased a ferry and provides operating assistance for freight operations to remove 54,000 truck trips annually from the New York and New Jersey streets.[197]

The STP provides for the greatest flexibility in the use of funds. STP funds may be used for public transportation capital improvements, carpool and vanpool projects, fringe and corridor parking facilities, intercity and intracity bus terminals, enhancement related transit capital costs, bicycle and pedestrian facilities, safety, and facility enhancement, as well as transit research and development.[198] They may also be used for wetland mitigation and environmental analysis, as well as most TCMs. Some STP funds are made directly available to MPOs in urbanized areas; some are set aside for nonurbanized areas.[199] STP funds have been used to fund a wide variety of projects. Examples include:

• Chicago built the Main Street Rebuilding Project;[200]

• Little Rock has funded trails, sidewalks, and an electric streetcar system;[201]

• The Los Angeles MTA received STP funds to cover 13 percent of the cost of building the Union Station Gateway Center, a multimodal transfer facility;[202] and

• Norman, Oklahoma, upgraded its railroad station.[203]

L. INTERMODAL FACILITIES AND EQUIPMENT

Congress has declared that among the transportation policies of the United States is "to encourage and promote development of a national intermodal transportation system…to move people and goods in an energy-efficient manner, provide the foundation for improved productivity growth, strengthen the Nation's ability to compete in the global economy, and obtain the optimum yield from the Nation's transportation resources." [204] In creating the U.S. Department of Transportation, Congress gave it a mission to "make easier the development and improvement of coordinated transportation service…."[205]

In ISTEA, Congress set forth a detailed national policy to establish a National Intermodal Transportation System "that is economically efficient and environmentally sound, provides the foundation for the United States to compete in the global economy, and will move individuals and property in an energy efficient way."[206]

ISTEA required that the state and MPO planning process include consideration of facilitating intermodal transportation. [207] TEA-21[208] reaffirmed and retained the

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[197] U.S. ENVTL. PROTECTION AGENCY, DOMESTIC PROGRESS ON CLIMATE CHANGE: INTELLIGENT COMMUTING (2000).

[198] TRANSP. RESEARCH BD., FUNDING STRATEGIES FOR PUBLIC TRANSPORTATION, VOLUME 2, CASEBOOK 69 (Transit Cooperative Research Program Report No. 31, 1998).

[199] FED. TRANSIT ADMIN., *supra* note 18, at 16.

[200] Denise Linke, *Main Street Funds Could Come Early,* CHI. TRIB., Jun. 28, 2001, at 6D.

[201] Jake Sandlin, *Money Jumps from Roads to River Rail,* ARK. DEMOCRATIC-GAZETTE, Apr. 26, 2001, at A1.

[202] TRANSP. RESEARCH BD., *supra* note 198, at 13.

[203] *City Earns Depot Grant,* SUNDAY OKLAHOMAN, Feb. 25, 2001, at 1.

[204] 49 U.S.C. § 302(e) (2003). Congress has decreed that,

> A national intermodal transportation system is a coordinated, flexible network of diverse but complimentary forms of transportation that transports passengers and property in the most efficient manner. By reducing transportation costs, these intermodal systems will enhance the ability of the industry of the United States to compete in the global marketplace.

49 U.S.C. § 47101(b)(3) (2003). Further, Congress has recognized that,

> An intermodal transportation system consists of transportation hubs that connect different forms of appropriate transportation and provides users with the most efficient means of transportation and with access to commercial centers, business locations, population centers, and the vast rural areas of the United States, as well as providing links to other forms of transportation and intercity connections.

49 U.S.C. § 47101(b)(5) (2003). Congress also has decided that the U.S. "must make a national commitment to rebuild its infrastructure through development of a national intermodal transportation system." 49 U.S.C. § 47171(b)(8) (2003).

[205] 49 U.S.C. § 101(b)(2) (2003). The Secretary of Transportation is required to coordinate federal policy on intermodal transportation, and promote creation and maintenance of an efficient U.S. intermodal transportation system. 49 U.S.C. § 301(3) (2003). The Secretary is also obliged to consult with the heads of other federal agencies to establish policies "consistent with maintaining a coordinated transportation system…." 49 U.S.C. § 301(7) (2003).

[206] 49 U.S.C. § 5501(a) (2000). The National Intermodal Transportation System shall:

• "consist of all forms of transportation in a unified, interconnected manner…to reduce energy consumption and air pollution while promoting economic development and supporting the United States' preeminent position in international commerce";

• include the Interstate highway system and the principal arterial roads;

• include public transportation;

• provide improved access to seaports and airports;

• give special emphasis to the role of transportation in increasing productivity growth;

• give "increased attention to the concepts of innovation, competition, energy efficiency, productivity, growth and accountability";

• be adapted to new technologies wherever feasible and economical, giving special emphasis to safety considerations; and

• be the centerpiece of a national investment commitment to create new national wealth.

49 U.S.C. § 5501(b)(8) (2003). All DOT employees are required to be given a copy of the National Intermodal Transportation System Policy, and it is required to be posted prominently in all offices of the Department. 49 U.S.C. § 5501(c) (2003).

[207] Intermodal Surface Transportation Efficiency Act of 1991, Conference Report, H.R. No. 404, 102d Cong. (Nov. 27, 1991).

[208] Pub. L. No. 105-178.

planning provisions and MPO structure of ISTEA, with its emphasis on federal-state-local cooperation and public participation, though significant changes were made in funding levels.[209] TEA-21 established seven factors to be considered in TIP preparation, one of which is to "Enhance the integration and connectivity of the transportation system, across and between modes, for people and freight."[210]

In ISTEA, Congress also required DOT to promulgate regulations for state development, establishment, and implementation of a system for managing its intermodal transportation facilities and systems.[211] States are required to devote 2 percent of federal highway appropriations to planning and research of, *inter alia*, "highway, public transportation, and intermodal transportation systems."[212] Emphasizing the importance of highway, public transport, and intermodal systems, Congress decreed that not less than 25 percent of such funds expended by the state shall be devoted to research and development of these systems.[213]

Intermodal transfer facilities and equipment explicitly are included within the term "capital project" for which federal money may be spent for mass transportation.[214] The Secretary is also instructed to encourage various governmental and private institutions to develop plans to convert rail passenger terminals into intermodal transportation terminals.[215] Grants may also be made to preserve existing rail terminals if such facilities are reasonably capable of conversion to intermodal facilities.[216] DOT may provide financial assistance to states seeking to build rail intermodal freight terminals.[217] Loans and loan guarantees may be made by DOT to finance the acquisition, improvement, rehabilitation, development, or establishment of intermodal equipment or facilities,[218] or to preserve or enhance intermodal service to small communities or rural areas.[219] DOT may provide up to 50 percent of the costs incurred by a public agency for high-speed rail corridor planning.[220] Among the eligible corridor planning activities are intermodal terminals.[221]

The promotion of rail passenger terminal conversion projects is at least as much one of historic preservation as it is one of facilitating transportation. The Secretary is to provide financial, technical, and advisory assistance for:

1. Conversion of rail passenger terminals into intermodal transportation terminals on a feasibility demonstration basis;

2. Preservation of rail passenger terminals that are reasonably likely to be converted to other uses pending preparation of plans for their reuse;

3. Acquisition and use of space in suitable buildings of historic or architectural significance, but only where use of the space is feasible and prudent in comparison to available alternatives;[222] or

4. Encouragement of state and local governments, transportation authorities, common carriers, philanthropic organizations, and others to develop plans to convert rail passenger terminals into intermodal transportation terminals and civic and cultural activity centers.[223]

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[209] William Vantuono, *Uncomplicated Answers for Complicated Questions,* RAILWAY AGE, Sept. 1, 1998, at 16; AMERICAN PUB. TRANSIT ASS'N, TEA 21: A SUMMARY OF TRANSIT RELATED PROVISIONS 6 (1998). For example, under the $217 billion authorization bill (the largest infrastructure bill in U.S. history), funding was significantly increased for the Congestion Mitigation and Air Quality Program (by 35 percent) as well as for transit (by 50 percent). Bud Shuster, *Shuster Applauds Gore's "Better America Bonds,"* PRESS RELEASE, Jan. 11, 1999.

[210] Metropolitan planning organizations are required to develop transportation systems and facilities "that will function as an intermodal transportation system for the metropolitan area and as an integral part of the intermodal transportation system for the state and the United States." 23 U.S.C. § 134(a)(3), 49 U.S.C. § 5303(a)(2) (2003). State plans and programs must do the same. 23 U.S.C. § 135(a)(3) (2003). The states' long-range 20-year transportation plan must provide for the development and implementation of the intermodal transportation system of the state. 23 U.S.C. § 135(e)(i) (2003). The Secretary of Transportation shall make grants to the states to develop model state intermodal transportation plans, which shall include systems for collecting data related to intermodal transportation. 49 U.S.C. § 5504(a) (2003).

[211] 23 U.S.C. § 303(a) (2003).

[212] 23 U.S.C. § 505(a)(5) (2003).

[213] 23 U.S.C. § 505(b)(1) (2003). A state's intermodal management system

> shall provide for improvement and integration of all of a state's transportation systems and shall include methods of achieving the optimum yield from such systems, methods for increasing productivity in the state, methods for increasing use of advanced technologies, and methods to encourage the use of innovative marketing techniques, such as just-in-time deliveries.

23 U.S.C. § 303(e) (2003).

[214] 49 U.S.C. § 5302(i) (2003). ISTEA also allocated resources for federal funding of up to 80 percent of at least three demonstration projects for conversion of rail passenger terminals into intermodal transportation terminals. 49 U.S.C. § 5562(a)(1) (2003). To be eligible for federal funding, such terminals needed to include, as appropriate, facilities to handle motorbus transportation, mass transit, and airline ticket offices and passenger terminals providing direct access to area airports. 49 U.S.C. § 5563(a)(1) (2003).

[215] 49 U.S.C. § 5562(a)(4) (2003).

[216] 49 U.S.C. § 5564(c)(1)(A) (2003).

[217] 49 U.S.C. § 22101(a)(3) (2003).

[218] 45 U.S.C. § 822(b)(1) (2003).

[219] 45 U.S.C. § 822(c)(6) (2003).

[220] 49 U.S.C. § 26101(a) (2003).

[221] 49 U.S.C. § 26101(b)(1)(J) (2003). Amtrak was given eminent domain power to build an intermodal transportation terminal at Washington, D.C.'s Union Station. 49 U.S.C. § 24311(a)(1)(B) (2003).

[222] The Secretary may only acquire this type of space after consulting with the Advisory Council on Historic Preservation and the Chairman of the National Endowment for the Arts. 49 U.S.C. § 5562(c) (2003).

[223] 49 U.S.C. § 5562(a)(1) through (4) (2003). "Civic and cultural activities" are defined as including, *inter alia*, libraries, musical and dramatic presentations, art exhibits, adult education programs, public meeting places, and other facilities for

The Secretary may provide funds for conversion of a rail passenger terminal to an intermodal transportation terminal only if certain conditions are met.[224] Funding is permissible where the terminal is capable of being converted to accommodate other modes of transportation the Secretary "decides are appropriate."[225] If its transportation use can be combined with other "civic and cultural activities," the Secretary is also given discretion to finance the terminal's conversion.[226] Where a terminal conversion is to be funded on the grounds of architectural preservation or civic activities, the Secretary is obligated to employ independent architectural consultants for the purpose of evaluating the conversion plan.[227] Only if the consultants agree that the conversion will meet the desired goal may the Secretary release funds for the project.[228] FTA funds may not make up more than 80 percent of the total cost of converting the terminal to intermodal transportation use.[229]

The Secretary may provide financial assistance to a person or entity[230] for the preservation of a terminal where the Secretary has determined that the terminal has a reasonable likelihood of being converted to intermodal transportation use, [231] and/or a civic/cultural center, [232] and planning activity for such conversion has commenced and is "proceeding in a competent way."[233] If the Secretary does decide to fund a conversion project under these guidelines, the grant may not be for more than 80 percent of the total cost of maintaining the terminal for a period no longer than 5 years.[234]

Among the aviation statutes is a declaration that it is the policy of the United States "to develop a national intermodal transportation system that transports passengers and property in an efficient manner."[235] The Wendell H. Ford Aviation Investment and Reform Act for the 21st Century of 2000 amended this provision to provide for the encouragement and development "of intermodal connections on airport property between

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carrying on an activity any part of which is supported under federal law. 49 U.S.C. § 5561 (2003). The designation of a terminal for conversion under this section does not bar the allocation of funds for the same purpose from other programs. 49 U.S.C. § 5562(b) (2003). Regardless of percentage spending caps identified below, the Secretary may not allocate more than $15 million for demonstration conversions or acquiring space in historical/architecturally significant buildings, $2.5 million for maintenance of terminals pending conversion, or $2.5 million for encouraging conversion of terminals to dual transportation/civic activity use. 49 U.S.C. § 5568(a)(1) through (3) (2003). These amounts, once appropriated, will persist until expended. 49 U.S.C. § 5568(b) (2003).

[224] 49 U.S.C. § 5563(a) (2003).

[225] 49 U.S.C. § 5563(a)(1) (2003). Types of "appropriate" transportation include motorbuses, mass transit via rail or rubber, and airline ticket offices and passenger terminals providing transportation to area airports. 49 U.S.C. § 5563(a)(1)(A) through (C) (2003). If the terminal is listed on the National Register of Historic Places, the "architectural integrity" of the terminal is to be preserved. 49 U.S.C. § 5563(a)(2) to (3) (2003).

[226] 49 U.S.C. § 5563(a)(2) through (4) (2003). In the case of using the terminal for civic and cultural activities, the Secretary must make that determination only after consulting with the Advisory Council on Historic Preservation and the Chairman of the National Endowment for the Arts to develop criteria for the conversion. 49 U.S.C. § 5563(a)(5) (2003).

[227] 49 U.S.C. § 5563(b) (2003).

[228] 49 U.S.C. § 5563(b) (2003).

[229] 49 U.S.C. § 5563(c) (2003).

[230] The funding recipient must be a party that is "qualified, prepared, committed, and authorized by law" to preserve the terminal. This includes being able to prevent the demolition or dismantling of the terminal. 49 U.S.C. § 5564(a) (2003).

[231] 49 U.S.C. § 5565(c)(2) (2003). Recipients of financial assistance under any of the terminal conversion categories must keep records as required by the Secretary. 49 U.S.C. § 5566(a) (2003). At minimum, these records must show: (1) the amount and disposition of the funds received; (2) the total cost of the project for which the funds were given or used; (3) the amount of the project cost that was supplied by other sources; and (4) any other records that will "make an effective audit easier." 49 U.S.C. § 5566(a)(1) through (4) (2003). For 3 years following the completion of a project, the Secretary and the Comptroller General may audit and inspect any records of the recipient that the Secretary or Comptroller General decides may be relevant to the financial assistance. 49 U.S.C. § 5566(b) (2003).

[232] The intended recipient must: (1) be prepared to develop practicable plans that meet zoning, land use, and other applicable requirements of the state and locality where the terminal is located; (2) incorporate into the proposed designs and plans for the conversion features that "reasonably appear likely" to attract private investment for the planned conversion and its subsequent operation and maintenance; and (3) complete the designs and plans for the conversion within the period of time prescribed by the Secretary. 49 U.S.C. § 5565(a)(1) through (3) (2003). The Secretary is required to give preference to applicants whose designs and plans will be implemented within 3 years after their completion. 49 U.S.C. § 5565(b) (2003).

[233] 49 U.S.C. § 5564(b)(1) and (2) (2003). This statute is actually in contradiction with the statute under which it purports to be giving guidance. According to 49 U.S.C. § 5562(a)(2) (2003), the Secretary may provide financial assistance to "preserve rail passenger terminals that reasonably are likely to be converted or maintained *pending preparation of plans for their reuse*." [emphasis supplied]. Yet 49 U.S.C. § 5564 (2003), while stating that it gives guidelines "to preserve a rail passenger terminal under section 5562(a)(2) of this title," also requires that "planning activity directed toward conversion or reuse *has begun and is proceeding in a competent way*." 49 U.S.C. § 5564(b)(2) (2003) [emphasis supplied]. As of March 7, 2001, this contradiction has not been the subject of litigation, but it would appear to be rife with possibilities. This discrepancy can be resolved, however, if 49 U.S.C. § 5562(a)(2) is interpreted as permitting assistance pending *completion* of plans for the terminals' reuse. Funds appropriated for this purpose are to be allocated in the manner most likely to maximize the preservation of rail passenger terminals that are: (1) reasonably capable of conversion to intermodal transportation terminals; (2) listed in the National Register of Historic Places; or (3) recommended on the basis of architectural integrity or quality by the Advisory Council on Historic Preservation or the Chairman of the National Endowment for the Arts. 49 U.S.C. § 5564(c)(1)(A) through (C) (2003).

[234] 49 U.S.C. § 5564(c)(2) (2003).

[235] 49 U.S.C. § 47101(b)(1) (2003).

aeronautical and other transportation modes to serve air transportation passengers and cargo efficiently and effectively and promote economic development."[236]

The Federal Aviation Act requires that public airports accepting Airport Improvement Program (AIP) funding agree that all revenue generated by the airport be used exclusively for the capital or operating costs of the airport, the local airport system, or facilities owned or operated by the airport directly and substantially related to the air transportation of persons or property.[237] The question has arisen whether airport funds spent on building or operating transit or rail lines or stations are to be owned or operated by the airport and directly and substantially related to the air transportation of passengers.[238]

Federal Aviation Administration (FAA) regulations provide that airport access projects must preserve or enhance the capacity, safety, or security of the national air transportation system, reduce noise, or provide an opportunity for enhanced competition between carriers.[239] Such projects must also be for exclusive use of the airport patrons and employees, be constructed on airport-owned land or rights-of-way, and be connected to the nearest public access of sufficient capacity.[240] The FAA insisted that AIP funds be limited to the airport landside area, "which encompasses the area from the airport boundary where the general public enters the airport property to the point where the public leaves the terminal building to board the aircraft. Typical eligible landside development items include such things as terminal buildings, entrance roadways and pedestrian walkways."[241] As we shall see, more recent interpretations by the FAA have liberalized this rather constricted view of the types of landside projects that are appropriate for federal airport funding.

In 1996, the FAA approved the request of the Port Authority of New York and New Jersey to use Passenger Facility Charges (PFC) funds to extend Newark Airport's light-rail line 4,400 feet to an Amtrak/New Jersey Transit station off airport grounds.[242] The airlines opposed this decision on grounds that the funds should only be used for direct airport and terminal projects, not to benefit off-site transportation. The fact that the FAA expanded its perspective as to what were legitimate off-airport uses of aviation trust funds made this a landmark policy change. Among the largest intermodal projects approved by the FAA for PFC funding was a 1998 rail line that cost $1.5 billion linking New York's John F. Kennedy International Airport with the Long Island Rail Road and the E, J, and Z subway lines to Manhattan at Jamaica Station, and to Howard Beach.[243] The FAA concluded that PFC expenditures on the JFK rail link would satisfy its statutory and regulatory requirements by alleviating ground congestion on airport roadways and terminal frontages, by enhancing the efficient movement of airport employees, by freeing up capacity on the roadways for additional passengers, and by improving the airport's connection to the regional transportation network. The FAA noted that, "Where ground access is shown to be a limiting factor to an airport's growth, a project to enhance ground access may qualify as preserving or enhancing capacity of the national air transportation system."[244] The FAA found that the rail line would enable an additional 3.35 million passengers to use JFK annually by the year 2013, and "therefore must be construed to have a substantial capacity enhancement effect on JFK, as measured in air passengers accommodated by the airport."[245] The FAA concluded that the rail link would "serve to preserve or enhance the capacity of JFK and the national air transportation system…."[246] The $3 per ticket PFC would generate about $45-50 million a year, enabling the airport to pay off the cost of the line in 20 years.[247]

Rail lines at Atlanta, Chicago, Cleveland, and Washington, D.C., airports have been financed by transit systems rather than airports. The ISTEA legislation included a special appropriation for extension of BART to San Francisco International Airport (SFO). The FTA committed $750 million, or about 64 percent of the $1.2 billion project. The remaining $417 million comes from state and local funding sources.[248] The FAA approved airport funding for construction of a BART station at

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[236] 106 Pub. L. 181; 114 Stat. 61 (Apr. 5, 2003).

[237] 49 U.S.C. § 47107(b) (2003).

[238] 49 U.S.C. § 47107(b) (2003); 14 C.F.R. pt. 158 (2003); FAA Order 5100.3A, para. 553(a), AIP HANDBOOK (Oct. 24, 1989); PHILIP S. SHAPIRO, INTERMODAL GROUND ACCESS TO AIRPORTS: A PLANNING GUIDE 16, 202 (1996). More recent interpretations by the FAA have liberalized this rather constricted view of the types of landside projects that are appropriate for federal airport funding. Federal funding of an airport with the surrounding highway, rail, or transit networks can come from the FAA, FHWA, or FTA.

[239] 14 C.F.R. pt. 158.

[240] FAA Order 5100.3A, para. 553(a), AIP HANDBOOK (Oct. 24, 1989).

[241] *Quoted in* SHAPIRO, *supra* note 238.

[242] *Stalled Train to Kennedy Airport,* N.Y. TIMES, Jan. 30, 1998, at A20. Letter from FAA Associate Administrator Susan Kurland to Port Authority Executive Director George Marlin (Nov. 6, 1996).

[243] The Port Authority of New York and New Jersey alleged that the line would create "a more efficient vehicular flow at the airport by removing buses, shuttle vans, and private autos currently used by air passengers, airport visitors, and airport employees at JFK…," and that without the line, "ground access congestion would constrain projected O&D passenger growth at JFK and adversely affect the national air transportation system." Letter from FAA Associate Administrator Susan Kurland to Port Authority Executive Director Robert Boyle of Feb. 9, 1998, at 20.

[244] *Id*. at 21.

[245] *Id*. at 24.

[246] *Id*.

[247] Matthew L. Wald, *U.S. Approves Plan To Build Kennedy Airport Rail Link*, N.Y. TIMES, Feb. 10, 1998, at A20.

[248] U.S. GEN. ACCOUNTING OFFICE, SURFACE INFRASTRUCTURE: COSTS, FINANCING, AND SCHEDULES FOR LARGE-DOLLAR TRANSPORTATION PROJECTS 18 (1998).

SFO.[249] The 8.7-mile extension, the largest since BART was built in the early 1970s, will have four stations. About 68,000 riders a day are expected to use the line.[250]

FTA also committed to 72 percent of the construction costs of the $399 million extension of the St. Louis Metrolink to Mid-America Airport in St. Clair County, Illinois. This light rail system already connects to St. Louis Lambert International Airport.[251]

As noted above, ISTEA and TEA-21 provided for flexible funding to support multimodal planning and project development.[252] Flexible funding allowed the various federal, state and local transportation units to coordinate development of the Miami Intermodal Center, for example, which seeks to facilitate seamless passenger connections between air, rail, bus, and ferry modes.[253]

FHWA is financing 80 percent of the $11.6 billion, 7.5-mile highway/tunnel extension of the Interstate highway link to Boston Logan International Airport.[254] Federal and state highway departments have partnered successfully with airport authorities to connect road networks with airports at many cities, including Las Vegas and Pittsburgh. More than $300 million in PFC funding was approved for building an access road and tunnel at Las Vegas McCarran International Airport, while NHS funds were used to construct the highways outside the airport property.[255] In summary, federal funding of an airport with the surrounding highway, rail, or transit networks can come from the FAA, FHWA, or the FTA. ISTEA's effort to foster more cooperation among these agencies has had limited, but significant, success.

M. AUDIT, ACCOUNTING, REPORTING, AND CERTIFICATION REQUIREMENTS

Recipients of federal funds are subject to a host of reporting,[256] accounting,[257] and auditing[258] requirements. They must also sign the FTA Master Agreement and Annual Certifications and Assurances for FTA Grants,[259] Part II of the grant contract between FTA and the recipient setting forth most of the legal obligations imposed upon the grantee.[260] Recipients of capital

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[249] Letter from FAA Associate Administrator Susan Kurland to SFO Airport Director John Martin (Oct. 18, 1996).

[250] Benjamin Pimentel, *BART's 4-Year Trip to SFO Starts Today,* SAN FRANCISCO EXAMINER, Nov. 3, 1997, at 1.

[251] U.S. GEN. ACCOUNTING OFFICE, *supra* note 248, at 40.

[252] U.S. DEP'T OF TRANSP., INTERMODAL SURFACE TRANSPORTATION EFFICIENCY ACT: FLEXIBLE FUNDING OPPORTUNITIES FOR TRANSPORTATION INVESTMENTS 4 (1996).

[253] *Id*. at 13.

[254] U.S. GEN. ACCOUNTING OFFICE, *supra* note 248, at 57.

[255] SHAPIRO, *supra* note 238, at 16, 203.

[256] The Federal Transit Act provides that DOT shall "maintain a reporting system, by uniform categories, to accumulate mass transportation financial and operating information and a uniform system of accounts and records. The reporting and uniform systems shall contain appropriate information to help any level of government make a public sector investment decision." 49 U.S.C. § 5335(a) (2003). Prepared under the Uniform System of Accounts and Records, a recipient must file: (1) a capital report; (2) a revenue report; (3) an expense report; (4) nonfinancial operating data reports; (5) miscellaneous auxiliary questionnaires and subsidiary schedules; and (6) data declarations. 49 C.F.R. pt. 630 (2003). Grant reporting requirements are set forth in FTA Circular 5010.B, and require: (1) milestone/progress reports; (2) quarterly financial reports; (3) quarterly disadvantaged business enterprise reports; and (4) reports of significant events. FTA uses the Financial Status Report to monitor the use of federal funds through either the electronic grant making system or via SF-269A.

[257] FTA provides for two information-gathering analytic systems: a Uniform System of Accounts and Records, and a Reporting System for the collection and dissemination of public mass transportation financial and operating data. 49 C.F.R. pt. 630 (2003). Recipients of FTA funds must comply with Section 15, Uniform System of Accounts and Records. 49 C.F.R. § 430.4 (2003); 58 Fed. Reg. 4888 (Jan. 15, 1993); § 111, Pub. L. 93-503, 88 Stat. 1573 (49 U.S.C. § 1611 (2003)); § 303(a) and 304(c), Public Law 97-424, 96 Stat. 2141 (49 U.S.C. § 1607 (2000)); and 49 C.F.R. § 1.51 (1999). Congress earmarked funds for the Section 15 reporting system to be updated.

[258] U.S. DOT A-133 Compliance Supplement (May 1998). A recipient of FTA funds must perform the financial and compliance audits required by the Single Audit Act amendments of 1996, 31 U.S.C. 7501 *et seq*. (2000), and OMB Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations and Department of Transportation Provisions of OMB A-133 Compliance Supplement, April 1999. The purpose of the audit is to determine whether the grantee has prepared financial statements that fairly present its financial position in accordance with generally accepted accounting principles, has in place internal accounting and other control procedures and systems to assure it is managing its financial assistance programs in compliance with federal law, and has complied with federal laws and regulations that may effect its financial statements and each of its federal assistance programs. Audit costs are described in OMB Circular A-87, Revised; OMB Circular A-21, Revised; OMB Circular A-122, Revised, or 48 C.F.R. ch. I, subpt. 31.2 (1999). As noted above, recipients of FTA urbanized formula grants must submit to a DOT audit at least every 3 years, during which FTA reviews and evaluates completely the recipient's performance in carrying out the funded program, and its compliance with statutory and regulatory requirements. Failure to adhere to applicable legal requirements may result in the imposition of criminal sanctions. 49 U.S.C. §§ 1001, 5307 (2003). Specific pre-award and post-delivery audits are required of rolling stock purchases, focusing on such issues as Buy America and safety certification. 49 C.F.R. pt. 663 (2003).

[259] The annual list of certifications and assurances is very important to transit lawyers, who must sign the certifications. *See, e.g., Federal Transit Administration Fiscal Year 2001 Annual List of Certifications and Assurances for Federal Transit Administration Grants and Cooperative Agreements.* The most recent list can be found at the FTA Web site at http://www.fta.dot.gov/library/legal/federalregister/2002/fr102302.html (visited April 21, 2003).

[260] Federal Transit Administration Master Agreement (FTA MA) (7) October 1, 2000; The Master Agreement applies to federal assistance authorized by federal transit laws codified at 49 U.S.C. §§ 5301 *et seq*. (2000); or Title 23, United States Code (Highways); or TEA-21, Pub. L. 105-178, June 9, 1998, 23

funds must certify that they have conducted a meaningful public participation process, for example.[261] Major capital projects require the submission of a project management plan.[262] Before FTA may award a Federal grant or cooperative agreement, the applicant must provide to FTA all certifications and assurances required by federal laws and regulations. These issues are addressed in greater detail in Section 5—Procurement.

N. LOCAL FINANCIAL COMMITMENT

1. Introduction

As noted above, in order to approve a grant or loan under 49 U.S.C. § 5309, the FTA must find that the proposed project is supported by an acceptable degree of local financial commitment.[263] The federal commitment is up to 80 percent of capital expenses, while the local contribution is at least 20 percent (though in fact, most New Starts projects are funded only at about a 50 percent federal share). Typically, the local "match" for capital and operating expenses comes from four sources: (1) taxes (e.g., general fund appropriations, property taxes, sales taxes, gasoline taxes, utility taxes, special assessments); (2) fees (e.g., transit charges, parking charges, central area charges, impact fees, development exactions); (3) debt (e.g., bonds); and (4) operating revenue (e.g., advertising and concessions).[264] However, though farebox revenue can be used to back bonds financing transit improvements, it generally cannot be used as local match,[265] and nationally covers only about 36 percent of operating expenses.[266] In some instances, like-kind exchanges or services qualify as local match.[267] A significant contribution of funds or like-kind services by the private sector can impress FTA as to the extent of local commitment to a proposed project, and many recipients secured FTA discretionary funds or New Starts funds during the 1990s by forming "public-private partnerships." As discussed above, overmatch (i.e., the recipient's proposal to fund more than the 20 percent nonfederal share of eligible project costs) can be highly important in the competition for FTA New Starts discretionary funds.

The FTA uses the following three measures to evaluate the local financial commitment to a proposed capital project: (1) the proposed local share of project costs; (2) the strength of the proposed capital financing plan; and (3) the ability of the local transit agency to fund operation of the system as planned once the fixed guideway project is built.[268]

U.S.C. § 101 note (2000), as amended by the TEA-21 Restoration Act, Pub. L., 105-206, July 22, 1998, 23 U.S.C. § 101 note (2000). Federal Transit Administration Grant Agreement (FTA G-7, October 1, 2000). Federal Transit Administration Supplemental Agreement (Attachment to FTA G-7, October 1, 2000), Federal Transit Administration Cooperative Agreement (FTA C-7, October 1, 2000). FTA issues a revised Master Agreement every year.

[261] An Applicant seeking federal assistance under 49 U.S.C. ch. 53 for a capital project that will substantially affect a community or the community's transit service must certify that it has, or before submitting its application, will have: (a) provided an adequate opportunity for a public hearing with adequate prior notice of the proposed project published in a newspaper of general circulation in the geographic area to be served; (b) held that hearing and provided FTA a transcript or detailed report summarizing the issues and responses, unless no one with a significant economic, social, or environmental interest requests a hearing; (c) considered the economic, social, and environmental effects of the project; and (d) determined that the project is consistent with official plans for developing the urban area. 49 U.S.C. § 5323(b) (2000).

[262] The project management plan is a document that identifies all the tasks necessary to complete a major capital project. 49 C.F.R. pt. 633 (1999). This is discussed in greater detail elsewhere in this Section.

[263] 49 U.S.C. § 5309(e)(1)(C) (2000); 49 C.F.R. § 611.11 (1999). A recipient may not use a grant or loan to pay ordinary governmental or nonproject operating expenses. 49 U.S.C. § 5323(h)(1) (2000).

[264] Operating revenue may be derived from several resources, including fare box receipts, advertising (revenue derived by leasing space for advertising or rights-of-way on transit property), and concessions on transit property.

[265] "All local and State revenues generally eligible for inclusion in the local match with the exception of farebox revenues." 45 Fed. Reg. 56742 (Aug. 25, 1980). With respect to fare increases or service reductions, local transit providers must have a locally developed process to solicit and consider public comment before raising fares or implementing a major reduction of transportation. There have been lawsuits over fare increases and service reductions. The initial lawsuits were brought under Section 5(i)(3) of the Urban Mass Transportation Act, which has since been repealed. In the mid 1990s, Los Angeles was one of two large urban transit properties embroiled in major litigation. The suit was based on Title VI, with the basic contention being that the transit agency was increasing fares illegally for bus riders in the inner city while providing rail/subway service to the affluent suburbs. There was also Title VI fare increase litigation in New York City, which in substantial part was based upon alleged shortcomings in the public participation process. In New York Urban League v. New York, 71 F.3d 1031 (2d Cir. 1995), the Second Circuit dismissed a Title VI complaint on grounds that plaintiff failed to prove disparate treatment. Summary judgment on these claims was also granted defendants in Committee for a Better North Phila. v. SEPTA, 1990 U.S. Dist. Lexis 10895 (E.D. Pa. 1990).

[266] Fed. Highway Admin., *Innovative Finance* (last modified Mar. 13, 2003), http://www.fhwa.dot.gov/innovativefinance. The farebox at Denver's RTD covers only 20 percent of operating costs. Jeffrey Leib, *Rate Hike in Works for Most RTD Fares,* DENV. POST, Jul. 24, 2001, at A1. All transit systems require an operating subsidy. Jennifer Dixon, *Tab for Detroit-Area Bus System Could Top $400 Million a Year,* DET. FREE PRESS, Jun. 4, 2001.

[267] Contributions, donations, and exchanges are assets (e.g., land, rights-of-way, or easements) given by a private entity to a transportation agency in exchange for a future benefit or access to transportation facilities.

[268] 49 C.F.R. § 611, App. A (1999).

The FTA permits grantees to defer payment of the local share of transit projects, as for example when the local funds are invested in a short-term security or otherwise encumbered. TEA-21 permits the local share to vary from year to year, so long as the final contribution of federal funds does not exceed the maximum level authorized for the project.[269] This "tapered match" (or delayed local match) allows the level of local match to vary over the course of the project. Thus, in its initial years, the federal share may be 100 percent, tapering off to zero as the project is completed. This may enable the project to begin before the local agency has secured bonds, capital market financing, or collected revenue from a recently enacted tax. The use of tapered match is confined to circumstances where project completion will be expedited and project costs will be reduced.

State and local governments may also use the fair market value of third party donated funds, locally funded contracts, land, material, or services as part of their local match.[270] The value of publicly-owned property donated to a project may also be used as local match.[271]

Toll revenues on public roads and bridges may also constitute the local match, provided that the toll revenues are used for capital investment and there is no carryover of toll revenue to subsequent years.[272] But this avenue is not applicable to most transit systems.

For transportation enhancement projects, the recipient may apply funds of federal agencies other than FTA to the nonfederal match.[273] Some transit recipients have used imaginative means of securing local matching funds. For example, the Pee Dee Regional Transportation Authority (PDRTA) attempted to dedicate $600,000 it received from the South Carolina Department of Social Services (DSS) (a U.S. Department of Health and Human Services recipient) as part of a $989,000 local match to secure nearly $4 million in federal money for 9 transit centers, 25 buses, and 100 vans. DSS agreed to pay the $600,000 during the 1998-99 fiscal year, though it would receive discounts on the bills it pays PDRTA for transportation of DSS clients over the next 5 years.[274] However, questions were raised as to the legitimacy of DSS funds as a local match. The state DOT offered to allow Pee Dee to use DOT operating funds as a match, and the FTA released $2.2 million it had held up while the state determined whether there were sufficient funds to provide the local match.[275]

2. Local Funding Sources

• *Dedicated funding sources.* A dedicated funding source is a tax or fee dedicated in whole or in part to a particular project or purpose. Unlike annual appropriations from a state or local government, which can vary greatly from year to year, dedicated local taxes provide a relatively stable funding source. The most common disadvantage of local taxes serving as a dedicated funding source is that the revenues may be static and may not keep track with inflation (e.g., a one-cent per gallon share of the gasoline tax generates about the same amount of revenue regardless of the cost of gasoline, unless the price rises so high or drops so low that the amount of gasoline sold significantly increases or decreases). Local taxes may be used to replace declining federal funding, build major capital projects, or cover operating revenue shortfalls. However, only about half of local transit providers receive dedicated local tax revenue.[276] This is particularly important as a greater number of recipients seek New Starts funds for commuter rail and similar projects. FTA's evaluation criteria make it clear that a recipient applying for New Starts funds has virtually no chance of achieving a "Highly Recommended" or "Recommended" rating without a dedicated funding source; FTA views a recipient without a dedicated funding source as not having a stable revenue stream to maintain and operate a New Starts project over its anticipated useful life. The categories of dedicated local taxes listed below are examples.

• *Sales taxes.* Several transit providers, such as BART, MARTA, and Denver's Regional Transportation District (RTD) have dedicated sources of funding. The most common type of locally dedicated revenue to support transit is a portion of the sales tax dedicated exclusively for use by transit. Sales and use taxes (commonly known as sales taxes) are applied to the gross revenue earned on goods and services sold in a specified area.[277]

For example, Atlanta's MARTA collects a one-cent sales tax in the two counties (i.e., DeKalb and Fulton) in which it operates. MARTA leverages the tax by using bonds to fund operations and construction projects. The tax has been extended by the Georgia legislature to run through 2047.[278] But a slowing economy can adversely impact a transit provider relying on sales taxes, as

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[269] TEA-21 § 1302. Prior to TEA-21, local match was required of each federal payment to the state. Removal of this requirement allowed FTA to adjust federal match during the life of the project. Beginning in 1992, the local share could be deferred.

[270] Section 322 of the NHS Designation Act of 1995; 23 U.S.C. § 323 (2000).

[271] TEA-21 §§ 1301, 1303.

[272] ISTEA § 1044; TEA-21 § 1111(c).

[273] TEA-21 § 1108(b)(2)(C)(ii).

[274] David Milstead, *PDRTA May Not Have Funds to Repay DSS,* ROCK HILL HERALD, Mar. 3, 2000, at 1B.

[275] Sarah O'Donnel, *U.S. Unfreezes PDRTA Grant to Build Transit Hub,* ROCK HILL HERALD, Aug. 18, 2000, at 1B. Pee Dee had its FTA funds suspended when it purchased $170,000 of buses on an Internet auction site, and then tried to collect full value reimbursement from the federal government. James Scott, *PDRTA Begins Payment on Federal Debt,* ROCK HILL HERALD, Dec. 16, 2000, at 1B.

[276] TRANSP. RESEARCH BD., *supra* note 198, at 33.

[277] TRANSP. RESEARCH BD., *supra* note 198, at 11.

[278] *Marta's Ford Shares Vision of Excellence,* PROGRESSIVE RAILROADING, Jul. 2001, at 36.

Denver's RTD learned when it was forced to trim its 2001 budget by $8 million as the recession emerged. RTD collects a 0.6 percent sales tax in its metro Denver operating area.[279] Thus, sales taxes receipts are related to the local cost of living and require a strong local retail base in order to serve as a reliable and effective funding source.[280] Moreover, such taxes often require voter approval, which may be difficult to attain.[281]

• *Utility taxes.* Because of the inability to levy an effective sales tax, Pullman, Washington, successfully sought state and voter approval for a ballot measure to impose a 2 percent tax on utility (telephone, water, electric, sewer, and garbage) bills. Because the state of Washington historically matched dedicated funding sources on a 1:1 basis with revenue derived from the State Motor Vehicle Excise Tax, Pullman was able to double the revenue generated by the utility tax.[282]

• *Ad valorem taxes.* Certain transit authorities have been authorized to collect a mill levy on real property. Others collect an ad valorem tax on automobile sales.[283] Mortgage recording taxes also have been dedicated to transit.[284]

• *Special assessment districts.* In a special benefit assessment district, transportation is supported by a special property tax in the area in which, for example, a transit stop is built. A benefit assessment is a tax levied upon the envelope of real property that benefits from public development. Nearly all states allow for tax-increment financing. In Washington, for example, the local government creates a special assessment district—as little as a few square blocks—and dedicates 75 percent of additional property tax increases over a specified period of years to finance public projects.[285] For example, Los Angeles used benefit assessment to fund Metro Rail on land around the transit stations.[286] As the stations are opened, the value of surrounding property increases, and that appreciation is, in turn, partially recaptured via the assessment.

• *Transit impact fees.* Transit impact fees are charges imposed on developers to compensate for the impact of the developer's project in terms of creating transportation infrastructure demand. For example, San Francisco passed an ordinance requiring the collection of a one-time Transit Impact Development Fee from developers of office space to compensate for the burden such development places on the San Francisco Municipal Railway (MUNI) transit system in terms of capital expansion and operating costs.[287] Such exactions have survived court challenges where the improvement paid for by the fee directly benefits the development.[288]

• *Fuel taxes.* The federal tax on gasoline and diesel fuel is diminishing in terms of real dollars, to such an extent that the DOT recognizes a serious shortfall in funds for FHWA projects. The Miami Dade Transit Authority (MDTA) depends on appropriations from the Florida and local governments, supplemented with a minor amount from a dedicated tax on gasoline. In Michigan, some transit providers have received state gasoline tax infusions.[289]

• *Mixed taxing sources.* A number of transit providers are able to generate local financial support from several different taxing sources. For example, BART funds its capital and operating programs from a myriad of formula or dedicated and discretionary federal, state, and local sources. The federal funds are for capital projects only. California supports BART with general taxes, transit-dedicated taxes, and a variety of activity-dedicated bond sources for such things as construction, vehicle acquisition, and rehabilitation. Locally, BART collects a half-cent sales tax in the three-county district, property assessments, and other locally programmed funds.[290] In Tampa, the operating expenses for the street car system were provided by a combination of rider fares, income from an endowment fund, and a special taxing district approved by the Tampa City Council, as well as a 3-year start-up grant from the FTA.[291]

• *General fund appropriations.* Sometimes a local or state government will appropriate money for transit from its general funds. The metropolitan St. Louis Bi-State Development Agency [Bi-State] enjoys a sales tax

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[279] Jeffrey Leib, *RTD to Cut Budget $8 Million,* DENV. POST, Aug. 22, 2001, at 36.

[280] TRANSP. RESEARCH BD., *supra* note 198, at 33, 51.

[281] For example, Tacoma, Washington's, Pierce Transit was funded by a 0.3 percent county sales tax. So as to avoid having to reduce service by 40 percent, it sought an increase in the sales tax by public referendum. *How High a Sales Tax for Pierce Transit?,* NEWS TRIB., Oct. 7, 2001, at B10. The increased tax was necessary because Pierce Transit lost 40 percent of its operating funds once the motor vehicle excise tax ended. Unfortunately, the increased sales tax would leave Tacoma and other Pierce County jurisdictions with the highest tax rate—8.9 percent—in the state. *Pierce County Sales Tax,* SEATTLE-POST INTELLIGENCER, Dec. 6, 2001, at B1.

[282] TRANSP. RESEARCH BD., *supra* note 198, at 47–49.

[283] Mark Uhlig, *Cuomo, In a Shift, Agrees a Tax Cut Should Begin in '87,* N.Y. TIMES, Mar. 10, 1987, at A1.

[284] *Cuomo Plans $700 Million for Highways,* BOND BUYER, Feb. 13, 1987, at 1.

[285] Howard Buck, *Legislature: Increment Taxing Plan Approved,* THE COLUMBIAN, Apr. 22, 2001, at C1.

[286] Nancy Zamora, *Comment: New Financing Strategy for Rapid Transit: Model Legislation Authorizing the Use of Benefit Assessments to Fund the Los Angeles Metro Rail,* 35 UCLA L. REV. 519 (1988).

[287] TRANSP. RESEARCH BD., *supra* note 198, at 12, 57–65. A TIDF can be found in the San Francisco Administrative Code, available online at http://www.amlegal.com (visited April 21, 2003).

[288] TRANSP. RESEARCH BD., *supra* note 198, at 57. *See, e.g.,* Russ Bldg. Partnership v. City and County of S.F., 199 Cal. App. 3d 1496 (1987); Russ Bldg. Partnership v. City of S.F., 44 Cal. 3d 839 (1988).

[289] Dixon, *supra* note 266.

[290] Testimony of Nuria Fernandez Before the Subcomm. on Gov't Management, Comm. on Gov't Reform (Oct. 6, 2000).

[291] Jan Smith, *Hart Seeks Route that Will Cause Least Pain,* TAMPA TRIB., Dec. 15, 2001, at 17.

in the City of St. Louis, but relies on appropriations from St. Louis County (capped at $33.5 million annually) and Missouri ($3.9 million).[292] But in 2001, though St. Louis increased its contribution, Missouri failed to pass a transportation bill extending funding.[293] WMATA has no dedicated funds, and relies on FTA funds for capital assistance and state and local jurisdictions for both capital and operating funds.[294] The federal government funded two-thirds of the $9.4-billion, 103-mile WMATA Metro rail subway (from direct appropriations from the general fund), while the District of Columbia and the states of Maryland and Virginia picked up the remaining third.[295] Usually a transit agency relies on the state legislature to pass a statute, or the city or county to pass a local ordinance either creating a taxing mechanism to fund transit, or allowing the transit agency to levy a tax. Most recipients do not have power to levy taxes, and in most instances the recipient is powerless to increase the tax rate.

O. INNOVATIVE FINANCING: AN OVERVIEW

At the outset, it should be emphasized that the Transit Cooperative Research Program and the FTA have published several highly useful documents addressing innovative financing issues, which the transit attorney is encouraged to consult.[296]

The traditional "pay-as-you-go" system of tax collection following project inauguration has the advantages of simplicity and no interest costs. Nonetheless, it produces hidden costs in terms of inflation and foregone economic development, as well as costs associated with transportation congestion, delay, and environmental pollution.[297] In 1994, the FTA announced a policy of encouraging private-sector investment in transit infrastructure so as to bring market-oriented and results-driven management approaches to bear in satisfying the nation's transit infrastructure needs. Such a policy was designed to take maximum advantage of existing private capital markets and strategies for leveraging transit dollars.[298] The FTA supports the use of innovative financing techniques that enhance the effectiveness of transit investment either by generating additional financial resources or reducing project costs.[299] This includes leveraging federal funds received under the Urbanized Area Formula Program[300] and flex funding programs (CMAQ and STP). Usually, New Starts Program,[301] Nonurbanized Area Formula Program,[302] and Elderly and Persons with Disabilities Program[303] funds can also be leveraged in innovative financing forms. The FTA can issue Pre-award Authority to all formula and flexible funds, allowing transit recipients to undertake lease and debt transactions in anticipation of federal reimbursements for eligible project costs.[304]

Proposals for innovative financing should describe:

- *Project Specifics*—What is being purchased, constructed, and financed.
- *Project Funding*—Federal aid, by type, and other funding sources, including funding resulting from capturing external benefits from project financing;
- *Construction Financing*—The mechanisms being used to finance construction;
- *Intermodal Impacts/Benefits*—The degree to which transit innovations benefit or are enhanced by other modes of transportation;

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[292] *Going the Distance,* PROGRESSIVE RAILROADING, Jul. 2001, at 32.

[293] *The Road to Irrelevance,* ST. LOUIS POST-DISPATCH, Jun. 17, 2001, at B2.

[294] Testimony of Nuria Fernandez Before the Subcomm. on Gov't Management, Comm. on Gov't Reform (Oct. 6, 2000).

[295] Testimony of Gladys Mack Before the Subcomm. on Gov't Management, Comm. on Gov't Reform (Oct. 6, 2000).

> WMATA's funding comes from a variety of federal, state, and local sources. Unlike most other major urban transit systems, WMATA does not have dedicated sources of **tax** revenues, such as local sales tax revenues, that are automatically directed to the transit authority. WMATA receives grants from the federal government and annual contributions by each of the local jurisdictions that WMATA serves, including the District of Columbia and the respective local jurisdictions in Maryland and Virginia. For example, in its fiscal year 2002 proposed operating budget totaling $796.6 million (for rail, bus, and paratransit' services), WMATA projects that approximately 55 percent of its revenues will come from passenger fares and other internally generated revenues, and 45 percent will come from the local jurisdictions served by WMATA. In its capital program for infrastructure renewal, WMATA projects that about 47 percent of its proposed 2002 budget will come from federal government grants, 38 percent from federally guaranteed financing, and 15 percent from the local jurisdictions and other sources. WMATA has also, received funding directly through the congressional appropriations process over the past 30 years totaling about $6.9 billion—for construction of the originally planned subway system. WMATA did not have to compete against other transit agencies for this funding, which ended in fiscal year 1999.

Testimony of Jayetta Hecker Before District of Columbia Subcomm. of the U.S. House Comm. on Gov't Reform (Sept. 21, 2001).

[296] *See, e.g.,* COLLINS, *supra* note 1, at 6; BOYLE, *supra* note 5; MARX, *supra* note 5; INST. FOR URBAN TRANSP., INDIANA UNIV., *supra* note 5; TRANSP. RESEARCH BD., *supra* note 198, at 15, 81–84. There is also a highly useful Web site: http://www.fhwa.dot.gov/innovativefinance/ (visited April 21, 2003).

[297] Fed. Highway Admin., *supra* note 266.

[298] 59 Fed. Reg. 46878 (Sept. 12, 1994).

[299] Innovative financing is a broad term encompassing various techniques to augment traditional funding sources and methods. It includes such measures as new or nontraditional sources of revenue, new financing mechanisms designed to leverage existing resources, new funds management techniques, and new institutional arrangements. Fed. Highway Admin., *supra* note 297.

[300] 49 U.S.C. § 5397 (2003).

[301] 49 U.S.C. § 5309 (2003).

[302] 49 U.S.C. § 5311 (2003).

[303] 49 U.S.C. § 5310 (2003).

[304] 63 Fed. Reg. 34505 (June 24, 1998). Pre-award authority allows the project to proceed without securing a Letter of No Prejudice from FTA. However, it does not relieve the recipient of reporting or documentation requirements.

• *Clearances*—The status of federal and state sign-offs;

• *Innovation*—The financing innovation and how its use could apply to other regional or national projects;

• *Incentive*—The incentive required, such as fast-tracking, reprogramming, additional funding, or administrative or regulatory flexibility or relief;

• *Leverage*—How the proposal will leverage federal, state, local, and private transit investment; and

• *Timetable*—The timetable for advancing the project, including milestones.[305]

Projects are judged on the basis of their current project status (in planning, preliminary or final engineering, environmental clearance, or commencement of construction), the likelihood of near-term completion of the project, and the level of federal funding required.[306] However, the process of approval is largely unwritten, and can be political as well as legal. Typically, a proposal goes through multiple iterations in email exchanges, telephone conferences, and correspondence between the recipient and the FTA Chief Counsel's Office in Washington, which may bring changes to the loan agreement. The final legal opinion tends to mask the disagreements that led to the consensual result.

The FTA has identified the following as examples of innovative funding techniques it deems acceptable, several of which are discussed in greater detail below:

• *Leasing*—Urbanized Area Formula Program funds may be used to make lease payments, so long as leasing is more cost effective than purchasing.[307] On a case-by-case basis, FTA allows New Starts Program, Nonurbanized Area Formula Program, and Elderly and Persons with Disabilities funding to be used for lease payments.[308] Structured leasing, through Certificates of Participation or Grant Anticipation Notes, is encouraged, as are other mechanisms that generate net present benefits or cost reductions.[309]

• *Certificates of Participation*—These are bonds used to finance the purchase of transit assets that are paid from the lease of such assets to the transit provider.[310]

• *Joint Development*—New Starts Program, Urbanized Area Formula Program, STP, and CMAQ funding and assets previously acquired with FTA funding may be used to support joint development projects physically or functionally related to a transit project that enhance its effectiveness.[311]

• *Use of Proceeds from Sale of Assets in Joint Development Projects*—Surplus real estate may be sold and the proceeds applied to the purchase of other real estate for transit-supportive development. Proceeds from the sale of real property no longer needed for transit purposes have been authorized to be spent on other real property for a transit-supportive development. If the property is leased, the rental income may be used for any transit purpose. Air rights above land purchased with federal funds may be sold, and the proceeds retained as program income for use in transit projects. Land above or below property owned by the transit provider (such as a transit stop) may be sold or leased to a private business for commercial use. The proceeds may be retained for future use in mass transit.[312]

• *Cross Border Leases*—Transit providers can take advantage of foreign tax treatment by leasing equipment from foreign investors.[313]

• *Capital Cost of Contracting*—A portion of the costs of contracting with a private operator may be designated a capital cost for New Starts funding.[314]

• *Innovative Procurement Approaches*—Multi-year rolling stock procurements, creating consortia to take advantage of bulk or quantity purchases, or using design-build ("turnkey") are all encouraged.[315] "Super turnkey" projects—where a design/build contractor borrows funds for the project—may be paid off over time using federal funds.[316] In such a situation, a project management consortium undertakes to Build/Operate/Transfer (BOT) a facility to the purchasor. The consortium may also arrange financing.[317] However, the legal impediment to design/build in some state laws makes qualifications-based procurement, which is essential to successful design/build, illegal.

• *State Transit Finance Support*—If permitted under state law, FTA funds may be used to support transit-related state financial enterprises, such as transportation banks providing a range of financial options not otherwise available to transit providers, including cross border leases, certificates of participation, and joint procurement. New Starts funding may be used to cover the initial capitalization, but not the ongoing operating costs of the program.[318]

• *Revolving Loan Funds*—Federal funds may be used to support state or local revolving loan funds that could be used to provide loans to transit providers, or to acquire equipment or facilities leased back to it. Payments to retire the loans or service the interest would be used to fund other transit projects. FTA funds may

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[305] 59 Fed. Reg. 46878 (Sept. 12, 1994).

[306] *Id*.

[307] 49 C.F.R. pt. 639 (1999) defines the circumstances under which leasing may be eligible.

[308] 49 C.F.R. § 639.11 (1999).

[309] 59 Fed. Reg. 46878 (Sept. 12, 1994). See discussion below.

[310] See discussion in this Section, below.

[311] See discussion below, and in 62 Fed. Reg. 12266 (Mar. 14, 1997).

[312] *See* The Model Airspace Act. *See Testimony of Danny Alvarez Before the U.S. House Gov't Reform Comm.* (Oct. 6, 2000).

[313] See discussion below.

[314] *See Testimony of Dallas Area Rapid Transit Authority Executive Director Richard Snoble Before the U.S. Senate Comm. on Banking, Housing and Urban Affairs* (Apr. 25, 2000).

[315] 49 U.S.C. § 5326(a) (2003).

[316] *Testimony of FTA Acting Administrator Nuria Fernandez Before the U.S. House Appropriations Comm., Subcomm. on Transportation* (Mar. 8, 2000).

[317] ISTEA § 3019; 49 U.S.C. § 5326 (2003).

[318] See discussion in § 4.08, above.

be used to cover initial capitalization, but not operating costs.

• *Deferred Local Match*—With prior approval, FTA grantees may defer payment of the local share, drawing down 100 percent of the first 80 percent federal share of the project cost.

• *Transfer of Federal Interest*—FTA permits the concentration of the federal interest in a portion of assets acquired, leaving the remainder unencumbered by the federal interest. For example, if 100 buses were acquired with an 80 percent federal/20 percent local share, only 80 buses would be considered having a federal interest. The remaining 20 could be used to leverage additional funds, or to cover debt subordination, or be mortgaged, for example.[319]

• *Like-Kind Exchange*—FTA allows the transfer of the remaining federal interest in an asset to a new asset to facilitate early replacement. Tangible transit property (e.g., vehicles) may be sold before the end of their useful life, and the proceeds may be applied to the purchase of like property. For example, buses that have reached half their projected useful life may be sold and the proceeds dedicated to the cost of replacement vehicles.[320] However, prior FTA concurrence is required.

• *Incidental Nontransit Use*—Federally-funded transit facilities may be used for incidental nontransit purposes. For example, proportionate to the transit use of the facility, FTA funds may be dedicated to a Compressed Natural Gas facility used by transit and other nontransit public vehicles so long as the nontransit use does not detract from or interfere with the transit use of the facility.

• *Transfer of Federally-Assisted Assets*—If prior approval is conferred by the FTA, federally-funded assets may be transferred for another public use when they are no longer needed for transit purposes.[321] For example, a bus garage no longer needed for transit maintenance could be transferred to a local governmental entity in exchange for other local support for transit.

• *Coordinated Urban and Rural Services*—Assets acquired under the Urbanized Formula Program or New Starts Program may be used in a rural area together with assets funded under the Nonurbanized Area Formula Program as part of a coordinated urban/rural system.

• *Corridor Preservation/Advance Right-of-Way Acquisition*–Subject to two conditions,[322] FTA funds may be used to acquire and preserve existing transportation corridors and rights-of-way.[323] If the property value should increase, the property would be acceptable as local match for the federal grant.[324]

FTA emphasizes that these are only representative samples of the types of innovative financing that may be pursued. Recognizing that the demand for transit assistance outpaces the available federal economic resources, FTA welcomes all proposals that may leverage infrastructure investment, or will help reduce infrastructure costs over time, provided that the proposal meets FTA's basic criteria.

What follows elaborates on several of these approaches, and adds several more funding approaches to the list. It too, is far from an exhaustive review of innovative financing techniques.[325] New and different approaches are being designed by creative transit providers, lenders, contractors and manufacturers nearly every day. Such innovation is accelerating transit infrastructure development at a place unrealizable in its absence. Innovative financing may be daunting to those who have never ventured into it, and staff often meets resistance of "we can't afford New York bond counsel and won't make any money after we get through paying the lawyers, the accountants and our lost staff time." But it can be done, FTA really is there to help, and you do not need to be one of the nation's mega-transit systems in order to make good use of these funds.

P. DEBT

1. Introduction

Debt can come in various flavors. Usually, a transit operator must secure authority to issue *general obligation debt* from the municipality or the state. Such bonds are backed by the "full faith and credit" of the issuing governmental institution, meaning that it guarantees to pay the debt to prevent default. *Revenue bonds* pledge repayment from a limited source of revenue, such as taxes or operating revenue.[326] Transportation bonds are

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[319] *See, e.g.,* 60 Fed. Reg. 24682 (May 9, 1995).

[320] 57 Fed. Reg. 39328 (Aug. 28, 1992).

[321] 49 U.S.C. § 5334(g) (2000).

[322] The conditions are that a Major Investment Study must be completed before the project may be programmed for construction funding, and no land acquisition may be made that may prejudice mode and alignment decisions prior to completion of NEPA requirements.

[323] John Keahy, *$150 Million Deal First Stop in Wasatch Transit Plan,* SALT LAKE TRIB., Oct. 18, 2001, at A1; Laurie Blake, *From Rail to Trail?,* MINNEAPOLIS STAR TRIB., Oct. 1, 2001, at 1B.

[324] 60 Fed. Reg. 24682-84 (May 9, 1995); 59 Fed. Reg. 46878 (Sept. 12, 1994).

[325] The reader is encouraged to visit two excellent Web sites for comprehensive information on innovative financing: Fed. Highway Admin., *supra* note 297; Fed. Highway Admin., *Tifia Transportation Infrastructure Finance* (last visited Aug. 13, 2003), http://tifia.fhwa.dot.gov.

[326] The principal legal instrument setting forth the revenue bond structure is the "indenture" or "master resolution," which identifies the revenue stream to pay principal and interest on the debt. A "rate covenant" requires system administrators to assess rates adequate to generate revenue at a designated threshold. The "additional bonds test" evaluates the ability of the issuer's revenue stream to pay existing and proposed debt service. The "debt service reserve fund" creates an adequate fiscal cushion to prevent default when revenue is inadequate to cover debt service. Linda Lipnick et al., *The Determinants of Municipal Credit Quality,* GOV'T FIN. REV., Dec. 1, 1999, at 35.

usually municipal bonds issued by state and local governments to finance projects and expenses. The interest earned is exempt from federal tax and, if issued in the investor's state of residence, exempt from state and local taxes as well. The savings realized by the tax exemption enables governmental institutions to borrow at rates lower than the market rate for private debt instruments. Bonds are written promises to repay borrowed capital on a fixed schedule.[327]

The debt instrument, such as a bond, is ordinarily rated by a bond-rating agency, which effectively determines the cost of capital, or in other words, the interest rate the issuing agency must pay. As noted, tax exempt bonds typically carry lower interest rates than taxable securities. In determining the credit rating for the debt instrument, the bond rating agency usually evaluates four areas:

- *Economic Factors*—Because the economic base generates the revenue to repay the debt, the economic cycle is an important part—but the least controllable—of the four factors;
- *Debt*—With every new debt issuance, the issuer's overall debt is reevaluated in order to determine its impact on credit quality. With the issuance of general obligation tax-supported or general-fund supported debt, all the debt for which the issuer's tax base or citizens are the source of repayment must be evaluated to determine the overall debt burden to taxpayers;
- *Financial Factors*—Beyond operating results and financial statements, an evaluation is made of numerous financial factors, including budgetary planning and projections; budgetary surpluses; the issuer's policies on spending growth, use of surpluses, and shortfall contingency plans; as well as general fund balance as a percentage of revenues; and
- *Management Strategies/Administrative Factors*—This requires an evaluation of such factors as the issuer's organization, its division of responsibilities, professional qualifications, and adequacy of power to perform its functions.[328]

Bonding authority is ordinarily granted by the state government. For example, in 1984, the Florida legislature created the Florida High Speed Rail Transportation Commission and gave it authority to issue tax-free revenue bonds to design, build, and operate a high-speed rail system linking Tampa, Orlando, and Miami.[329] New York's MTA has used its bonding authority to raise several billions of dollars.[330]

In requests for reimbursements of interest or other financing costs of capital projects, an applicant for federal funds must certify that it will not seek reimbursement for interest and other financing costs unless it demonstrates that it has used reasonable diligence in seeking the most favorable financing terms available.[331] In order to demonstrate this to the FTA, the grantee must have performed a financial analysis.

2. Certificates of Participation

The difficulty in securing voter approval for the issuance of general obligation debt coupled with the need to finance politically unpopular projects has led to the increased use of lease debt to finance various infrastructure projects. Because lease debt usually does not require voter approval or count toward debt limits, lease debt can be used as a vehicle to generate capital funds despite limits on the issuance of general obligation bonds.[332] Hence, projects can be financed without technically incurring long-term debt.[333]

Certificates of Participation (COPs) are securities (e.g., tax-exempt bonds) that represent interests in a stream of revenue from an underlying obligation (e.g., lease or installment sale agreement).[334] Typically, the COP process begins when the transit provider has ordered vehicles or contracted for construction of a facility that the Finance Corporation agrees to complete and finance. FTA grants allocated to such equipment or facilities are no longer needed for them, allowing the transit provider to reprogram the funds for other projects.[335] COPs are usually issued by a state-level entity used in financing transit equipment or other facilities (e.g., rolling stock, buses, or stations well suited to lease agreements), sometimes for several transit providers. They may be repaid with revenue derived from rental, lease, or installment sale payments (often from an equipment or facilities lease) from the local transit provider, sales taxes, grants, or any other available source of revenue. Typically, over the 7 to 12 year life of the bonds, title to the assets is held by a trustee as a security interest for the bond holders.[336] Section 308 of the STURAA authorized the use of Section 9 federal transit funds[337] at the 80 percent level when leasing is deemed more cost-effective than purchase or construction.[338] Both the lease payment and imputed interest are eligi-

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[327] Nat'l Coop. Highway Research Program, *Innovative Finance for Surface Transportation* (last visited Aug. 13, 2003), http://www.innovativefinance.org.

[328] Lipnick et al., *supra* note 326, at 35.

[329] Gil Klein, *High Speed Rail System for Florida Gets Boos from Lawmakers,* CHRISTIAN SCI. MONITOR, Jun. 4, 1984, at 12; Alberdo Valdez, *Financing High Speed Rail: Meeting the Challenges of the 1990s,* 18 TRANSP. L. J. 173 (1990). This project was subsequently terminated by Florida Governor Jeb Bush.

[330] BUS. WIRE, Apr. 15, 2002.

[331] 49 U.S.C. §§ 5307(g), 5309(g)(2)(B), 5309(g)(3)(A), and 5309(n) (2003).

[332] Linda Lipnick et al., *supra* note 326, at 35.

[333] COLLINS, *supra* note 1, at 6. The rationale for the proposition that leases do not constitute debt is because the lessee is not obligated to make rental payments throughout the entire term of the lease, but need only pay rent each year to the extent such property is available for use. *Id*.

[334] COLLINS, *supra* note 1, at 6.

[335] Fed. Highway Admin., *supra* note 297.

[336] 60 Fed. Reg. 24682 (May 9, 1995).

[337] 49 U.S.C. § 5207 (2000).

[338] 49 C.F.R. pt. 639; 60 Fed. Reg. (May 9, 1995).

ble for reimbursement at the rate of 80 percent for federal grants and 20 percent for local funds.[339]

As an example, using leases secured by the newly purchased buses, the California Transit Finance Corporation has used COPs to enable the Sunline Transit Commission to replace its entire fleet of diesel buses with buses that run on compressed natural gas. Similarly, transit agencies in Denver, Los Angeles, and New York have used COPs, Equipment Trust Certificates,[340] and Beneficial Interest Certificates[341] to finance bus purchases.[342] The Tri-County Metropolitan District of Oregon has engaged in a number of innovative financing methods. For example, it has issued COPs for lease financing projects and has sold bonds backed by lottery proceeds and payroll taxes.[343]

3. Tax-Increment Financing

Under tax-increment financing, bonds are issued based on projected additional tax revenue on property anticipated to increase in value because of transportation improvements. It allows a city or county to issue bonds on improvement projects it cannot afford in order to attract business. A special tax district is created for a specified geographic region—in some instances only a few city blocks—with the tax increases dedicated to paying down the bonds over a prescribed period of time.[344] For example, Arlington Heights, Ill., built a rail rapid transit station with a combination of funds from state and federal agencies, the local transit provider, and tax-increment financing.[345]

4. Fare Box Revenue Bonds

The issuance of debt by a transit provider secured by a pledge of operating revenue has also been a source of innovative financing. For example, in 2001 Las Vegas broke ground on a $650 million Strip monorail funded by contributions by casinos near transit stops and revenue bonds to be paid by fare box revenue over time.[346]

5. Revolving Loan Funds

Seeking to build on its participation in an FHWA lease-to-buy vanpool program in 1994, and in response to the FTA's request for proposed innovative financing programs, the Arkansas State Highway and Transportation Department (AHTD) submitted a proposal to FTA to establish a new revolving loan fund (RLF) program for transit vehicle purchases. The FTA approved the program, and FHWA allowed AHTD's previously allocated vanpool funds to be used for the RLF. AHTD purchases a large number of vehicles at a volume discount (saving between $2,000 and $5,000 per vehicle), and leases them to the local transit providers. The leases are interest free, require no down payment, last for the life of the vehicle, and have a monthly payment equal to the cost of the vehicle divided by its life. At the end of the lease period, title to the vehicle is transferred to the transit provider. U.S. Department of Health and Human Services funds can be used to lease the vehicles.[347]

6. Grant Anticipation Debt

Grant Anticipation Notes (GANs) involve pledging forthcoming federal formula grants as security to pay off tax-exempt bonds. This allows acceleration of project construction, paying the cost over a period of years, thereby saving inflation costs and acquiring debt at attractive rates. However, federal anti-deficiency requirements prohibit the grantee from providing an enforceable pledge against future federal receipts in advance of their congressional appropriation.[348] They may, however, promise to satisfy debt obligations first out of federal receipts. Creditors may also insist on a reserve fund, or a pledge of local or state revenue.

Tri-County Metropolitan District of Oregon completed the first anticipation financing in the nation.[349] New Jersey Transit (NJT) found that it was impossible to purchase a fraction of the equipment it needed on a "pay-as-you-go" basis, and instead became the first transit system of its kind to leverage federal grants.[350] With only limited debt power (it can only issue debt if backed by an FFGA)[351] and no taxing authority, its 2001 $1.1 billion capital program budget consisted of a $440 million contribution from the federal government, $570

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[339] "The cost of carrying out part of a project includes the amount of interest earned and payable on bonds issued by the State or local governmental authority to the extent proceeds of the bonds are expended in carrying out the part." 49 U.S.C. §§ 5307(g)(3), 5309(n)(2) (2003).

[340] An Equipment Trust Certificate is a lease/finance arrangement typically used for aircraft, rail equipment, and surface transportation equipment. *See* Paul Sweeney, *The Bigger, the Better,* INVESTMENT DEALERS DIGEST, Feb. 26, 2001.

[341] MTA used Beneficial Interest Certificates to lease/purchase 384 buses to be paid off with toll revenues. Aaron Pressman, *New York City's Triborough Authority Tries out Lease Deal with Ironclad Payment Guarantee,* BOND BUYER, Apr 5, 1993, at 1.

[342] Fed. Highway Admin., *supra* note 297.

[343] Deborah Firestone, *Northwest Transit Agencies Get Creative Capital Projects,* BOND BUYER, Nov. 21, 2000, at 4.

[344] Buck, *supra* note 285, at C1.

[345] James Andrews, *Downtown Arlington Heights,* PLAN., Mar. 1, 2001, at 10.

[346] Jan Moller, *City Oks $250,000 for Monorail-Downtown Studies,* LAS VEGAS REV. J., Aug. 16, 2001, at 8B.

[347] TRANSP. RESEARCH BD., *supra* note 198, at 15, 81–84.

[348] 31 U.S.C. §§ 1341, 1342, 1517 (2003).

[349] Deborah Firestone, *supra* note 343, at 4.

[350] Humberto Sanchez, *Fitch Expects More Debt Backed by FTA's New Starts Program*, BOND BUYER, Apr. 20, 2001, at 6.

[351] "Full-funding grant agreement-backed instruments 'provide transit authorities with the opportunity to advance construction and more quickly realize the benefits from new-starts transit projects than the traditional grant reimbursement approach.'" *Id*. at 6.

million from the state, and $120 million from local authorities. In order to accelerate its three new light rail systems, NJT issued two grant anticipation notes. Considering the cost of rights-of-way acquisition, had it waited 10 years to undertake the projects, the projected cost would have increased tenfold.[352] The Denver area's RTD used grant funds to back its debt instruments; the commercial paper portion of the Denver's southeast light-rail corridor is bridge financing for federal grant funds.

7. Tax-Anticipation Debt

Some transit providers have been able to leverage the revenue earned from authorized local taxes to accelerate projects. For example, Denver's RTD secured voter approval in a referendum allowing it to issue $324 million in bonds backed by its sales tax revenue stream in order to build a light rail corridor running along Interstate 25. RTD cooperated in the initiative with the Colorado Department of Transportation, which issued $680 million in GARVEE bonds (grant anticipation notes)[353] backed by future federal highway allocations and $115 million secured on future state sales and use tax revenue to widen Interstate 25.

8. TIFIA

TEA-21[354] created two new federal credit programs for surface transportation projects—the Transportation Infrastructure Finance and Innovation Act of 1998 (TIFIA) and the Railroad Rehabilitation and Improvement Financing Program (RRIF).[355] TIFIA is designed to assist financial markets in developing the capability to supplement the federal government in financing the costs of large projects of national significance.[356] TIFIA does not create new federal funding. And it is a taxable program, unlike the tax-exempt debt offering authority enjoyed by many governmental institutions.[357] TIFIA simply gives transit providers additional flexibility by allowing them to borrow against federal funds under a line of credit guaranteed by the federal government.[358] TIFIA gives transit providers enhanced access to capital markets, flexible repayment terms, and often, more favorable interest rates than those available in private capital markets. These benefits may advance projects that might be jeopardized or delayed because of their size and complexity and the market's uncertainty over timing of funding.[359] DOT established a multi-agency Credit Program Steering Committee and Working Group to coordinate and monitor all policy decisions and implementation actions associated with this federal credit assistance program.[360]

Three types of credit instruments are permitted for public and private sponsors of eligible surface transportation projects under TIFIA: secured (direct) loans,[361] loan guarantees,[362] and lines of credit.[363] To be eligible for assistance under TIFIA, the project must have eligible costs of at least $100 million, or 50 percent of Federal-aid highway funds apportioned to the state. Projects principally involving the installation of an ITS must cost at least $30 million. However, the amount of federal credit assistance may not exceed 33 percent of the cost of the project.[364] To be eligible for assistance, projects must be classified within the following categories:

- *Surface transportation projects* as defined under Title 23 or chapter 53 of Title 49 of the United States Code;
- *International bridge or tunnel projects* for which an international entity is responsible;
- *Intercity passenger bus or rail facilities and vehicles*, including those owned by Amtrak; or
- *Publicly-owned intermodal surface freight transfer facilities,* provided they are located on or adjacent to the NHS, and are not seaports or airports.[365]

The application must be accompanied by a preliminary rating opinion letter from a nationally recognized credit rating agency that indicates the project's overall creditworthiness and the potential of the project's sen-

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[352] Yvette & Wisniewski, *supra* note 16, at 36.

[353] A GARVEE is a Grant Anticipation Revenue Vehicle. A GAN is a grant anticipation note.

[354] Public Law 105-178, 112 Stat. 107, 241.

[355] TIFIA, as amended by Section 9007, Public Law 105-206, 112 Stat. 685, 849, and codified at 23 U.S.C. §§ 181-189 (2000). RRIF authorizes loans and loan guarantees for the acquisition, improvement, development, or rehabilitation of intermodal or rail equipment or facilities. The loans may not exceed a period of 25 years, must be justified by present and future demand, must provide reasonable assurance that the facilities or equipment will be economically and efficiently utilized, and must be reasonably expected to be repaid. Fed. Highway Admin., *supra* note 297.

[356] 64 Fed. Reg. 5996 (Feb. 8, 1999).

[357] Ola Kinnader, *Transportation: TIFIA Aid to 5 Projects Demonstrates Program's Flexibility,* BOND BUYER, Nov. 19, 1999, at 5.

[358] Testimony of Gladys Mack Before the Subcomm. on Gov't Management, Comm. on Gov't Reform (Oct. 6, 2000).

[359] Fed. Highway Admin., *supra* note 297.

[360] 64 Fed. Reg. 29741 (June 2, 1999); 64 Fed. Reg. 5996 (Feb. 8, 1999).

[361] Direct loans offer flexible repayment terms and permit combined construction and permanent financing of the project's capital costs.

[362] Loan guarantees enjoy federal full-faith-and-credit guarantees to institutional investors that make loans for transportation projects.

[363] During the first 10 years of project operations, these standby loans of credit (representing secondary sources of funding in the form of contingent federal loans), may be drawn down to supplement project revenues. 23 U.S.C. §§ 183, 184 (2003).

[364] Fed. Highway Admin., *supra* note 297.

[365] *See* Notice of Availability of Funds Inviting Applications for Credit Assistance for Major Surface Transportation Projects, 65 Fed. Reg. 44941 (July 19, 2000).

ior debt obligations (i.e., those obligations having a lien senior to the TIFIA credit instrument) to achieve an investment grade rating.[366] Annual credit evaluations must also be submitted.[367] Unlike other innovative financing alternatives, TIFIA requires a competitive federal application process. Project selection is based on eight criteria:

- Whether the project is nationally or regionally significant (20 percent);
- How creditworthy is the project, and how secure is the financing (12.5 percent);
- Whether it would foster innovative public/private partnerships and attract private debt or equity (20 percent);
- Whether TIFIA assistance would enable the project to proceed more expeditiously (12.5 percent);
- Whether the project would use new technologies (5 percent);
- The amount of money required to fund the TIFIA instrument (5 percent);
- The extent the project helps to maintain or protect the environment (20 percent); and
- The extent to which TIFIA assistance would reduce federal grant assistance (5 percent).[368]

In 2000, WMATA became the first transit agency to receive a loan guarantee under TIFIA.[369] It devoted the $600 million guarantee to expedite upgrading of its original Metrorail segments (some of which were more than 20 years old), and rehabilitate the railcar fleet.[370] Previously, WMATA had to turn to commercial banks for its loans. Using TIFIA, WMATA saved 45 basis points over 10 years, or approximately $20 million.[371] Other examples of TIFIA guarantees include:

- The Tren Urbano rapid rail project in Puerto Rico;
- The Miami Intermodal Center near Miami International Airport; and
- The Farley/Penn Station in New York.[372]

The benefits are varied. The Tren Urbano project eased intense short-term capital needs. In the case of the $1.4 billion Miami Intermodal Center, TIFIA's $432 million guaranteed funding advanced the project by several years. Miami's $269 million TIFIA loan was secured by state fuel taxes, while its $164 million loan was secured by rental car fees.[373] TIFIA's loan and line of credit ensured that the Farley/Penn Station got off the ground.[374] In New York, Staten Island Ferries and Terminals used a $153 million TIFIA loan secured by revenue from the Tobacco Settlement Agreement of 1998 to acquire ferryboats and rebuild intermodal ferry terminals.[375]

States may use FTA funds to establish and operate Revolving Loan Funds to support public and private nonprofit transit providers. States may pool vehicle purchases and lease or sell them to transit providers, or make loans to them for facilities and vehicle acquisitions.[376]

Q. STATE INFRASTRUCTURE BANKS

The National Highway System Designation Act of 1995[377] authorized DOT to enter into cooperative agreements with up to 10 states for the establishment of State Infrastructure Banks (SIBs) or multistate infrastructure banks for making loans to entities implementing eligible projects.[378] As of March 2001, 32 states had entered into 204 loan agreements totaling more than $2.4 billion.[379] Examples of use of SIBs to fund transit include Bi-State transit agency's $5.3 million loan from Missouri's State Infrastructure Bank.[380]

SIBs may use federal and state funds to provide loans; credit enhancements (e.g., loans, loan guarantees, letters of credit, grant anticipation notes, COPs); interest rate subsidies; leases; debt financing securities; and other debt financing mechanisms (when approved by the DOT). SIB support may enable the sponsor to attract private, local, or state financial resources, leveraging the SIB investment into a larger dollar investment. SIB investment may also be used as collateral to borrow in the bond market or create a guaranteed reserve fund.[381] States may capitalize SIBs by using up to 10 percent of their federal-aid highway or transit funding. States are required to match all federal funds, though they are free to fund SIBs at levels beyond the required local match. Once the money is allocated to a specific mode, it may not subsequently be reallocated to a different mode. All disbursements, plus interest, must

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[366] 65 Fed. Reg. 44936 (July 19, 2000).

[367] 49 C.F.R. § 80.11 (2003). Annual project performance reports and audited financial statements are also required. 49 C.F.R. § 80.19 (2003).

[368] 49 C.F.R. § 80.15 (1999).

[369] Testimony of Nuria Fernandez Before the Subcomm. on Gov't Management, Comm. on Gov't Reform (Oct. 6, 2000).

[370] *WMATA Awarded First TIFIA Loan Guarantee*, RAILWAY AGE, Apr. 1, 2000, at 6.

[371] Kinnader, *supra* note 357, at 5.

[372] *Testimony of FHWA Administrator Kenneth Wykle Before the U.S. House Comm. on Transportation & Infrastructure* (Mar. 8, 2000).

[373] Other funding included a state SIB loan, TEA-21 federal highway funds, and CMAQ funds.
Http://www.innovativefinance.org (visited April 21, 2003).

[374] Kinnader, *supra* note 357, at 5.

[375] Fed. Highway Admin., *supra* note 297.

[376] FED. TRANSIT ADMIN., *supra* note 5.

[377] 23 U.S.C. § 101 note (2003); Section 1511 of TEA-21, 23 U.S.C. § 181 note (2000).

[378] TEA-21 extended federal funding for SIBs to four states—California, Florida, Missouri, and Rhode Island.

[379] Fed. Highway Admin., *supra* note 297. *See, e.g.,* CAL. GOV'T CODE § 63010 (2003).

[380] Ken Leiser, *Transit Agency Faces Prospect of Cutting Bus, Light-Rail Service,* ST. LOUIS POST-DISPATCH, Mar. 29, 2001, at B1.

[381] Fed. Highway Admin., *supra* note 297.

be repaid, whereby SIB's capital is replenished and used for a new cycle of transportation projects.[382]

R. LEASING

Section 308 of the STURAA[383] amended Section 9(j) of the Federal Transit Act to allow Section 9[384] recipients to use capital funds to finance the leasing of facilities and equipment on the condition that the leasing arrangements are more cost effective than purchase or construction. A recipient of FTA funds may not use federal assistance to finance the cost of leasing any capital asset until it performs calculations demonstrating that leasing would be more cost effective than purchasing or constructing a similar asset.[385] Though FTA must approve the use of discretionary funds for lease payments, pre-approval is not required for the use of formula funds. However, leases that include provision of maintenance and fuel would fall under the operating assistance cap, for such payments would be regarded as operating expenses.[386]

1. Capital Leases

TEA-21 amended the definition of "capital project" to allow transit recipients to use capital funds to finance the leasing of facilities and equipment whenever leasing is more cost effective than purchasing or construction.[387] Any leasing arrangement that provides for the recipient's use of a capital asset is eligible, irrespective of the classification given the leasing arrangement for tax purposes.[388] All costs directly attributable to the lease are eligible for capital assistance under former Section 9[389] of the Federal Transit Act.[390] In comparing the respective costs of leasing vis-à-vis purchasing, realistic estimates must be made of both the direct and indirect costs of either alternative.[391] If it does not establish a single grant fund from which lease payments are drawn down over the course of the lease, the recipient must certify it will have adequate funds to cover the lease payments should it not receive federal capital assistance funds.[392] If the lease is terminated early, federal funds covering the terminated period must be reimbursed to FTA.[393] If the recipient is unsure whether it qualifies under the leasing regulations, the recipient may request FTA to determine the eligibility of its proposal.[394]

2. Cross-Border Leasing

In 1986, Congress eliminated the safe harbor leasing provision in the Internal Revenue Code (whereby a transit agency arranged for a private sector third party to purchase vehicles and enjoy the depreciated tax benefit the public entity could not utilize). Nevertheless, investors in several nations (including Denmark, France, Germany, Japan, and Sweden) continued to

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[382] TRANSP. RESEARCH BD., *supra* note 198, at 75–77. Issues surrounding interest and other financing expenses are addressed in a number of statutes. For example, the exemption for state governments is set forth in the Debt Collection Act of 1982, as amended, 31 U.S.C. §§ 3701–3720 (2003). Interest requirements for governmental bodies is addressed in Section 5(b) of the Cash Management Improvement Act of 1990, as amended, 31 U.S.C. § 6503(b) (2003). Prejudgment common law interest is addressed by U.S. General Accounting Office/U.S. Department of Justice regulations at 4 C.F.R. § 102.13(i)(2) (1999).

[383] Pub. L. 100-17 (1987).

[384] 49 U.S.C. § 5307 (2003) (formerly Section 9 of the Federal Transit Act).

[385] "Capital Leases," 49 C.F.R. §§ 639.11, 639.15(b)(1), and 639.21 (2003). 49 U.S.C. § 5307 (2003); Section 3037 of TEA-21, 49 U.S.C. § 5309 note (2003); 56 Fed. Reg. 51794 (Oct. 15, 1991).

[386] The FTA provides the following guidance as to what constitutes capital maintenance:

> Preventive maintenance…was established as permanently eligible for FTA capital assistance under TEA-21; therefore, FY 1998 funds and subsequent fiscal year appropriations may be used for preventive maintenance**.** Preventive maintenance costs are defined as all maintenance costs. For general guidance regarding eligible maintenance costs, the grantee should refer to the definition of maintenance in the most recent National Transit Database reporting manual. A grantee may continue to request assistance for capital expenses under the FTA policies governing associated capital maintenance items (spare parts), vehicle overhaul as 20 percent of maintenance, maintenance of vehicle leased under contract, and vehicle rebuilds (major rework); or a grantee may choose to capture all maintenance under preventive maintenance**.** If a grantee purchases service instead of operating service directly, and maintenance is included in the contract for that purchased service, then the grantee may apply for preventive maintenance capital assistance under the capital cost of contracting policy.
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> 63 Fed. Reg. 60054 (Nov. 6, 1998).

[387] 49 C.F.R. §§ 639.3, 639.21 (2003); 49 U.S.C. § 5302 (2003).

[388] 49 C.F.R. § 639.13(a) (2003). However, lump sum leases require prior FTA approval. 49 C.F.R. § 639.13(c) (2003).

[389] 49 U.S.C. § 5307 (2003) (formerly Section 9 of the Federal Transit Act).

[390] Such costs include finance charges (including interest), delivery and installation charges, and maintenance costs. 49 C.F.R. § 639.17 (2003). However, an early termination of the lease may require partial reimbursement of federal funds used. 49 C.F.R. § 639.31 (2003).

[391] 49 C.F.R. §§ 639.23 – 639.27 (2003).

[392] 49 C.F.R. § 639.15 (2003).

> A recipient that wishes to enter into a lease which requires the draw down of a single lump sum payment at the inception of the lease (or payments in advance of the incurrence of costs) rather than periodic payments during the life of the lease must notify FTA prior to execution of the lease concerning how it will ensure satisfactory continuing control of the asset for the duration of the lease. FTA has the right to disapprove any arrangements where it has not been demonstrated that the recipient will have control over the asset. FTA may require the recipient to submit its cost-effectiveness comparison for review.
>
> 49 C.F.R. § 639.13(c) (2003).

[393] 49 C.F.R. § 639.31 (2003).

[394] 49 C.F.R. § 639.13(b) (2003).

enjoy such a depreciation tax benefit under their local law.[395]

By leveraging assets through use of foreign tax laws (whereby the investor enjoys non-U.S. tax benefits from depreciation on the assets), transportation equipment (rolling stock, usually rail cars) can be acquired on a purchase/lease basis. Cross-border leasing can save between 4 percent to 6 percent (3.89 percent on average) of the cost of buses and rail rolling stock. Some leases do not actually finance the purchase of equipment *per se.* Instead, a transaction is concluded under which a foreign entity will take ownership of the vehicles and pay the "lessee" a percentage of the cost of the vehicles to the transit agency for the privilege of entering into the transaction. The foreign entity enjoys favorable tax treatment in its country, and the transit provider enjoys unencumbered revenue that it may use for any purpose.[396] The transactions are usually linked to the country of manufacture.[397]

Typically, they are structured as follows:

- The foreign lessor borrows money from a bank on a nonrecourse note;
- Then the lessor uses the money to purchase the equipment either from the transit provider or the manufacturer; and
- Finally, the foreign lessor leases the equipment to the transit provider. As security for the loan, the lessor assigns sufficient lease payments to repay the loan to the lender.[398]

Examples of these types of transactions include the following:

- In 1991, King County, Washington, used FTA Section 9 funds to complete a $90 million purchase of 360 buses, which it sold to Japanese investors. The cross border lease saved King County 4.5 percent, or $4.24 million, off the original purchase price. FTA accepts cross-border leasing proposals so long as the net benefit exceeds the transaction cost.[399]
- In 1994, Denver's RTD entered into a $25 million leveraged lease financed by CS First Boston (Nederland) N.V. (the lender) from Deutsche Bank AG (the lessor) of 11 light rail vehicles manufactured by Siemens Duewag Corporation.
- In 1995, the San Diego Metropolitan Transit Development Board entered into a defeased[400] cross-border lease of 97 buses from JL Coronado Lease Co., Ltd. (the lessor), financed by the Dai-Ichi Kangyo Bank, Ltd. (the lender).[401]

3. Structural Domestic Lease Transactions

For some time, sale/leasebacks were deemed ineligible for investment tax credits in the United States. However, clever tax attorneys have come up with a sale/leaseback structure they believe results in domestic tax savings, and the FTA recently has approved several of them. This allows recipients to take advantage of tax provisions that treat physical assets as if they were sold by the grantee to third-party investors, and leased back. It involves a "head lease," or a conditional sales contract for tax purposes, and a "true lease," which is a leaseback of assets to the transit provider.

Often after the sale/leaseback, the lessee transit agency purchases defeasance instruments to ensure that the payment stream is available, and then assigns the payments or pledges the defeasance instruments to the lessor company. In this way, there is little to do after closing except make sure that the money is transferred twice a year.

Though the FTA usually requires return of a *pro rata* share of proceeds from the early sale of a transit asset, FTA has recognized that the transit provider is not actually disposing of the asset in a sale/leaseback transaction, and simply requires the transit provider to maintain "effective continuing control" of the asset.[402] From the FTA's perspective, the central issue is not who holds title to the assets, but the issue of continuing control—the grantee must have real and substantial physical control of federally-assisted assets that have a lifespan of more than a year. This includes all buses, trucks, vans, automobiles, tow trucks, emergency responders, light and commuter rail vehicles, and maintenance facilities, but does not include supplies. Thus, a grantee may sell, lease, or otherwise encumber an asset so long as it retains physical possession of it for transit purposes. What one must also remember is that once an asset is tied up in a lease, it is encumbered, and therefore almost impossible to be used for joint development. A sale/leaseback is an exception to FTA's position that the term of a contract shall not exceed 5 years. FTA will evaluate a proposed sale/leaseback on the basis of the rate of return and the grantee's continuing control of the transit asset over both the proposed term of the transaction and the useful life of the asset for transit purposes.

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[395] TRANSP. RESEARCH BD., *supra* note 198, at 109.

[396] COLLINS, *supra* note 1, at 16.

[397] FTA Circular 7020.1, "Cross-Border Leasing Guidelines" (April 26, 1990).

[398] COLLINS, *supra* note 1, at 16–17.

[399] TRANSP. RESEARCH BD., *supra* note 198, at 109–14.

[400] Depending on the jurisdiction and the needs of the lessee, the lease may be defeased or nondefeased. If defeased, the lessee pays an entity (usually the lending institution) an amount equal to that borrowed by the lessor. The lending institution then assumes responsibility for payment of all obligations to the lender. If nondefeased, the lessee has U.S. tax ownership of the equipment, and is ordinarily obliged only to repay the loan to terminate the lessor's interest in the equipment. The nondefeased structure is similar to a leveraged lease. COLLINS, *supra* note 1, at 17.

[401] The latter two studies are discussed in COLLINS, *supra* note 1, at 17.

[402] The statute requires that a grantee maintain "satisfactory continuing control over the use of [federally funded] equipment and facilities." 49 U.S.C. §§ 5307(d)(1)(B), 5309(d)(1), 5310(e)(g) (2003).

4. Lease-In/Lease-Out

Under a lease-in/lease out, the transit provider leases out rolling stock and facilities, then leases them back in a defeased structure maturing between 50–60 percent of the assets' useful life. Though the rules require a straight-line amortization, the investor realizes income statement benefits, while the transit provider enjoys a net present benefit from the defeased transaction.[403]

S. JOINT DEVELOPMENT

Joint development and joint ventures are partnerships between transit providers and private entrepreneurs in the development of mixed-use construction projects, whereby the transit provider shares the risks and rewards of development. The FTA's "Livable Communities Initiative"[404] may support such ventures, so long as they are physically or functionally related to a transit project and they enhance its effectiveness.

Joint development consists of an income-producing activity related to a real estate asset in which FTA has an interest or obtains one as a result of FTA grants (also known as an Assisted Real Estate Asset). It is an income-producing activity involving a third party,[405] taking place on or with an Assisted Real Estate Asset. The FTA has adopted a policy favoring joint development.[406] Joint development projects must meet three tests: statutory definition, financial return, and highest and best transit use.

The statutory definition imposes a requirement that joint development be a transportation project that enhances economic development or the effectiveness of a mass transit project, and is physically[407] or functionally[408] related to that mass transit project (proximate to FTA-assisted capital projects), or establishes new or enhanced coordination between mass transportation and other transportation, and provides a fair share of revenue for mass transportation use. Proceeds derived from a joint development transfer are considered program income,[409] which may be retained by the grantee. In contrast, proceeds from a sale are not program income and must be returned to FTA.[410]

The highest and best use requirement is that the equitable return is based on the appraised market value as represented either by highest and best use of the property,[411] or by highest and best *transit* use of the property.[412]

The FTA offers the example of a rapid rail station that includes 6.3 acres for a "park and ride" area:

> A developer has been approved to build 160 residential units and 17,000 square feet of service retail space on a portion of this area. The transit operator transfers 3.4 acres to the developer for use in the joint development. The development will generate more transit trips and more non-fare revenue than the displaced parking spaces provided. The transit agency will retain the income generated from this land transfer as program income and will be assured of satisfactory continuing control through covenants running with the land. Should the developer re-sell the land in the future, the covenants bind the next owner to a transit-oriented use of the land.[413]

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[403] Internal Revenue Code § 467 (2000).

[404] Fed. Transit Admin., *Livable Communities* (visited Aug. 12, 2003), http://www.fta.dot.gov/research/polplan/susdev/livcom/livcom.htm.

[405] The third party is the source of the income to the grantee, and is the party to whom the property is transferred or the lessee who leases the space.

[406] 62 Fed. Reg. 12266 (March 14, 1997). FTA Circular 9300.1A, App. B.

[407] A joint development project is "physically related" to a capital project if it provides a direct physical connection with transit services or facilities. Physically related development may include projects using air rights over transit stations or projects built within or adjacent to transit facilities.

[408] A joint development project is "functionally related" to an FTA capital project if it is related by its activity and use, and is functionally linked to transit services or facilities, provides a beneficial service to the public, and enhances use of or access to the transit system. Usually, they are within reasonable walking distance to the transit entry point, or within a radius of 1,500 feet from it.

[409] 49 C.F.R. § 19.24 (2003). The FTA considers all "revenue derived from such joint development to be program income as defined in the Common Grant Rule at 49 C.F.R., subtit. A, § 18.25," 62 Fed. Reg. 12266 (Mar. 14, 1997). "Real property that is no longer needed for transit purposes may be sold and the proceeds may then be used to purchase other real property for a transit-supportive development. If the real property is leased, the proceeds are considered program income and may be used for any transit purpose." 60 Fed. Reg. 24683 (May 9, 1995).

[410] 49 C.F.R. § 18.31(c)(2) (2003).

[411] A property's "highest and best use" is the use that results in the highest anticipated selling price.

[412] "Highest and best transit use" consists of that combination of residential, commercial, retail, public, and/or parking space and amenities that will produce the highest level of social, economic, and financial benefit to the transit system and its community, irrespective of the selling price. It consists of that combination of such benefits as increasing ridership, reducing trip durations, or improving connections between trips, that maximizes the value of the asset to transit. 62 Fed. Reg. 12266 (Mar. 14, 1997).

[413] FTA also proffered an example of the transit agency building an "envelope," or rehabilitating an existing transit owned facility. The envelope or building shell consists of load bearing walls, roof, foundation, substructure improvement, site design, and engineering. "Tenant finishes," ineligible for FTA reimbursement, include partition walls, furniture, equipment, shelving, lighting, drapes, floor coverings, and other items specific to the business intended to be operated. FTA noted a case in which

> the local transit authority was allowed to convert an existing office building into a $3 million Neighborhood Travel Center. The center will serve as a terminal for bus lines to industrial jobs and will provide the focus for a downtown redevelopment "campus" including jobs training, child care facilities, and a privately-financed development bank. The tenant finishes for each of these ancillary activities will be paid for with non-grant funds, though grant funds were used to rehabilitate the building itself. The tenants will pay market rate rent to the transit authority.

Joint development does not have a dedicated funding source, but such activities are eligible for funding under all Title 49 capital programs, including the Capital Program,[414] the Urbanized Area Formula Program,[415] the Non-Urbanized Area Formula Program,[416] and the Elderly and Persons with Disabilities Program.[417] CMAQ and STP funds may also be used to support joint development projects.[418] As is the case in all innovative financing techniques, before undertaking a joint development project, transit recipients are encouraged to discuss the proposal with the FTA Regional Office.[419]

In *Town of Secaucus v. Dep't of Transportation*,[420] the Town of Secaucus sought to enjoin New Jersey Transit's construction of a $448 million transportation hub within its city limits. Secaucus argued that the use of $15.7 million to build a foundation upon which a 4.7-million square foot private commercial development would be built over the transit station was not related to mass transportation and was therefore an inappropriate use of federal funds. The court reviewed ISTEA's provisions on joint development and found to the contrary:

> Section 5309(a)(5)—the provision that § 5309(f)(2) supplements—specifically authorizes funding for joint transportation/commercial/residential development projects. By its very terms, § 5309(a)(5), along with § 5309(f)(2)(A), envisions that federal transit dollars will be used to fund such elements as property acquisition, building foundations and utilities to enable the contemplated joint development to get off the ground. Transportation projects that "incorporate private investment, including commercial and residential development" are expressly eligible for funding where they "enhance the effectiveness of a mass transportation project" and are related "physically or functionally" to a mass transportation project.[421]

Woodham v. Federal Transit Administration[422] addressed the issue of whether joint development triggers federal NEPA[423] and National Historical Preservation Act (NHPA)[424] requirements. In 1984, the FTA provided MARTA (Atlanta) nearly $4 million to purchase property for its Lindbergh transit station. Thirteen years later, the FTA granted MARTA an additional $1.6 million to purchase surrounding real estate and to develop and solicit plans for joint development. The FTA approved a plan whereby MARTA would lease 9.6 acres of federally-funded real estate to private developers for the development of office buildings, retail shops, apartments, and condominiums, and retain the lease proceeds as program income.

The court noted that the presence of federal funds does not turn a project into a "major federal action" triggering NEPA, saying

> the joint development plan proposed by MARTA is not a "major federal action" because the FTA had no control or responsibility over material aspects of the project. MARTA created, developed, and implemented the joint development plan, using funds received from private investors. While MARTA used FTA funding to purchase property (9.6 of the 48 total acres) and begin preliminary development of the project, these funds do not transform the joint development plan into a "major federal action."[425]

Neither did FTA's concurrence with the plan. The court also observed that jurisdiction under NHPA's "federal or federally assisted undertaking" requirement is coextensive with NEPA's "major federal action" requirement, and that neither were triggered by the FTA's action in approving this joint development project.[426]

FTA Circular 9300.1A, App. B.

[414] 49 U.S.C. § 5309 (2003).

[415] 49 U.S.C. § 5307 (2003).

[416] 49 U.S.C. § 5311 (2003).

[417] 49 U.S.C. § 5310 (2003).

[418] Flexible funds are discussed at Fed. Transit Admin., *Flexible Funds* (visited Aug. 13, 2003), http://www.fta.dot.gov/library/reference/flex/ffi2.html.

[419] FTA Circular 9300.1A, App. B.

[420] 889 F. Supp. 779 (D. N.J. 1995).

[421] 889 F. Supp. at 779.

[422] 125 F. Supp. 2d 1106 (N.D. Ga. 2000).

[423] 42 U.S.C. § 4332 (2003).

[424] 16 U.S.C. § 470f (2003).

[425] 125 F. Supp. 2d at 1109. *See also* Town of Hingham v. Slater, 98 F. Supp. 2d 131 (D. Mass. 1999), which held that the FTA's discontinuance of preparation of an EIS for which no federal money would be used did not violate NEPA.

[426] Similarly, in South Bronx Coalition for Clean Air v. Conroy, 20 F. Supp. 2d 565 (S.D. N.Y. 1998), the court held that FTA's provision of funds and concurrence in MTA's sale of a bus depot and use of the proceeds to purchase a new facility did not trigger NEPA because FTA had no control over MTA's project decisions.