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**Consultant**  
Cynthia Alvarez  
David Storza

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CHAIR

**Committee Secretary**  
Karla J. Mendoza

1020 "N" Street, Suite 112  
(916) 319-2093

Tuesday, May 21, 2019  
1:30 p.m. -- State Capitol, Room 4202

## OVERSIGHT HEARING

### **Review of the California High-Speed Rail Authority 2019 Project Update Report**

Tuesday, May 21, 2019  
State Capitol, Room 4202

## Background

### **Introduction and Purpose of Hearing**

The purpose of today's hearing is to review the California High-Speed Rail Authority's (Authority's) recently released 2019 Project Update Report (PUR). The Authority is statutorily required to submit a Project Update Report on March 1<sup>st</sup> every odd-numbered year, as approved by the Secretary of Transportation, to the budget and policy committees of the Legislature. The PUR is required to include an update on the development and implementation of intercity high-speed train service, specifically a program wide summary, as well as details by project segment, with all information necessary to clearly describe the status of the project.

The PUR is not as extensive as the Authority's Business Plans, which are completed every even-numbered year and detail funding, financing, and ridership estimates for the entire project. However, this version of the PUR takes on new significance as it reflects Governor Gavin Newsom's new vision for the high-speed rail program. Additionally, the PUR includes work conducted by the Early Train Operator (ETO), a private sector rail operator from Germany, who was tasked with studying ridership and costs of interim service options for both the San Francisco Bay Area and Central Valley as described in the 2018 Business Plan.

The PUR shifts the focus of the high-speed rail program from the northern oriented Initial Operating Segment (IOS) from the Silicon Valley to the Central Valley, outlined in the 2018 Business Plan, the so-called "Valley to Valley" Line, to adopting a "building blocks" approach of completing a high-speed rail line from Merced to Bakersfield, the so-called "Central Valley Line." The report, "focuses limited resources the state has identified to get a working section that can demonstrate the viability of the broader project." The Authority has defined this new Central Valley Line as a 171-mile long segment to operate high-speed trains from Merced to the F Street Station in Bakersfield by 2028 at a cost of \$18.3 billion. The line would be coordinated with increased service from the San Joaquins inter-city passenger rail and the Altamont Corridor Express (ACE) service to the Bay Area.

Additionally, the Authority continues its commitment to fund the bookend projects in the Bay Area and Los Angeles, and complete environmental work on the entire planned Phase I system for a total cost of \$20.4 billion. The costs estimates include an additional \$1.8 billion in cost increases for the current Central Valley construction from \$10.6 billion outlined the 2018 Business Plan to \$12.4 billion.

Finally, the PUR details the funding available to the Authority to complete the Central Valley Line, including federal funding, Proposition 1A bonds, and revenues from the state's cap-and-trade program. The Authority estimates the total funding available between \$20.4 billion and \$23.4 billion by 2030, depending on cap-and-trade fluctuations. Recent actions by the federal government have put this funding scheme in jeopardy. The Federal Railroad Administration (FRA), the Authority's federal funding and project partner, announced its intention to de-obligate nearly \$1 billion from the project and possibly claw back \$2.6 billion in funds already expended on construction. Additionally, the FRA has ceased participation in day-to-day interactions with the Authority, including ongoing environmental reviews.

The high-speed rail program is facing its biggest challenge to date. The Authority remains committed to completion of a high-speed operating segment, as costs continue to increase and schedules continue to slip. Additionally, as this committee heard in an oversight hearing in November 2018, the Authority continues to have internal management issues. However, the PUR does not provide the Legislature with alternative options for completion of segments or future service. There are hard decisions on the very short horizon for Legislators. The purpose of today's hearing is to provide an opportunity for Legislators and the public to gain a full understanding of the costs, funding sources, and associated risks in completing the proposed Central Valley Line, the situation with the FRA, and the ongoing investments in significant projects in bookends in the Bay Area and Southern California.

### **Background**

Development of high-speed rail in California began more than 20 years ago. SB 1420 (Kopp), Chapter 796, Statutes of 1996, created the Authority to direct development and implementation of intercity high-speed rail service that would be fully coordinated with other public transportation services. The Authority reports to the California State Transportation Agency and is governed by an eleven-member Board of Directors. The Governor appoints five members of the board, the Senate Rules Committee appoints two, and the Assembly Speaker appoints two. Additionally, the board includes two ex-officio, non-voting members, one member of the Assembly and one member of the Senate.

Assembly Bill 3034 (Galgiani), Chapter 267, Statutes of 2008, placed before the voters the Safe, Reliable High Speed Passenger Train Bond Act for the 21st Century (Proposition 1A) in the fall of 2008. California voters approved the initiative, which authorized \$9.9 billion in general obligation bonds for two distinct purposes: \$9 billion to develop and construct a high-speed rail system connecting San Francisco Transbay Terminal to Los Angeles Union Station and Anaheim; and \$950 million for connecting intercity and commuter rail systems that would enhance those systems' capacity, safety, or connectivity to the high-speed rail system.

At the time of the passage of Proposition 1A, estimates for the cost of the system varied. The analysis by the Legislative Analyst's Office (LAO) that accompanied the ballot measure referenced a 2006 estimate from the Authority that the total cost to develop and construct the entire high-speed rail system would be about \$45 billion. However, the Authority's 2008 Business Plan, released after the passage of Proposition 1A estimated the cost at \$33 billion, financed by a mix of bond funds, federal, local, and private funds.

Proposition 1A prescribes specific route and design requirements for the high-speed rail system including that it must be electrified, be capable of sustaining speeds of no less than 200 miles per hour, and have the capacity to achieve travel times between San Francisco and Los Angeles of 2 hours and 40 minutes. Additionally, Proposition 1A requires a 50 percent match of all bond funds and lays out specific requirements the Authority must meet in order to access and spend the bond funds, including submission of

detailed funding plans to the Legislature and Department of Finance. Furthermore, Proposition 1A requires high-speed rail to operate without government subsidies.

Overall, the project is to be built in two phases, with Phase I covering roughly 500 miles from San Francisco to Anaheim. Phase II would extend the system to Sacramento in the north and San Diego in the south. The delivery of the project is broken into segments, including an Initial Operating Segment (IOS), which over the years has changed from a southern-focused route to Los Angeles, to the current norther-focused route from San Francisco to Bakersfield.

In July 2012, the Legislature approved SB 1029 (Committee on Budget and Fiscal Review), Chapter 152, Statutes of 2012, that appropriated nearly \$8 billion in federal and state funds to begin the construction between Madera and Bakersfield. SB 1029 funded three components of the project, including:

- 1) Initial Operating Segment: SB 1029 provided \$5.8 billion to fund construction of the high-speed rail "backbone" in the Central Valley with approximately 130 miles of right-of-way and track bed from Madera to the northern outskirts of Bakersfield. Of this amount, \$3.2 billion was from federal grants (both American Recovery and Reinvestment Act (ARRA) funds and a Fiscal Year (FY) 2010 grant), and \$2.6 billion was from Proposition 1A bonds.
- 2) Connectivity: SB 1029 appropriated \$819 million of Proposition 1A bonds for "connectivity" projects on existing regional and inter-city rail systems throughout California to improve the connectivity to the future high-speed rail system.
- 3) Bookends: SB 1029 also appropriated \$1.1 billion of Proposition 1A funds for improvements in the Los Angeles Basin and in the San Francisco Peninsula, referred to as the "bookends." These funds were for near-term improvements to these existing rail segments that will facilitate the eventual use of the segment for high-speed rail and also improve service for existing riders.

Of this amount, \$500 million was dedicated to fund projects in the Los Angeles Basin as reflected in the 2012 Memorandum of Understanding (MOU) signed with the Southern California Association of Governments (SCAG) and its regional transportation members, and \$600 million for electrification of the Caltrain system in the San Francisco Bay Area.

Additional federal funds and Proposition 1A funds were authorized for ongoing administrative, planning and environmental work on the project.

Furthermore, a 2014-15 state budget trailer bill [SB 862 (Committee on Budget and Fiscal Review), Chapter 36, Statutes of 2014], continuously appropriated 25 percent of the revenues derived from the state's Cap-and-Trade program to the project. Additionally, in July 2017, the Legislature extended the state's cap-and-trade program through 2030, in AB 398 (Garcia), Chapter 135, Statutes of 2017. The Authority estimates that this equates to a range of \$500 to \$750 million annually in funding for the program.

In 2015, the Authority broke ground on the first construction segment in the Central Valley, starting work on 119 miles from Madera to Poplar Avenue outside of Shafter. This work was reflected in the Authority's grant agreement with the FRA, to spend the federal and state monies appropriated in SB 1029. However, the Authority faced ongoing litigation on the issuance and expenditure of the Proposition 1A bonds. To begin construction work in the Central Valley and move forward on the other project sections, the Authority negotiated its funding agreement with the FRA to allow a "tapered match"—i.e., to allow federal dollars to be spent first and state matching dollars to be spent later. The FRA grant agreements require the Authority to complete construction of this section by December 2022.

### *2018 Business Plan*

In June 2018, the Authority approved the 2018 Business Plan which details an implementation and delivery strategy for the IOS from San Francisco to Bakersfield, or the Silicon Valley to Central Valley (Valley to Valley) Line. The Valley to Valley Line would run from 4th and King Streets in San Francisco to Bakersfield across the Pacheco Pass at a cost of \$29.5 billion to be completed by 2029. Additionally, the plan reflects work directed by the Authority's Board of Directors in 2017 for a comprehensive review of the current Central Valley construction contracts and cost estimates for the Valley to Valley Line and full Phase I of the system. This new cost review was first unveiled in November 2017, when the Authority revealed that costs for the Central Valley segment had risen over \$2.8 billion from previous estimates, due primarily to right-of-way acquisition delays and so-called third party agreements with freight railroads and utilities. The new cost estimates are reflected in the plan. The updated cost for full Phase I of the system is \$77.3 billion.

As noted, the focus of the 2018 Business Plan is the development of the Valley to Valley Line. The funding estimate for Valley to Valley includes everything needed to construct the line and start revenue service, including rolling stock, maintenance facilities, stations, and all necessary rail systems. The Authority acknowledged the funding gap to complete Valley to Valley, specifically the tunnels through the Pacheco Pass, which is estimated to cost roughly \$12.6 billion. The Authority detailed a funding package for Valley to Valley which includes existing sources of Proposition 1A bonds, federal funds, continued cap-and-trade pay-as-you-go funding and a cap-and-trade financing scheme.

### *Bookend Projects*

As previously described, the so-called bookend projects were defined and funding was appropriated by SB 1029 in 2012. Specifically, the Legislature appropriated \$600 million in Proposition 1A bond funds to the Northern California project, the electrification of Caltrain. Additionally, the Authority committed some of its allocation of state cap-and-trade funds to the project for a total commitment of \$713 million. The Caltrain electrification project, which is scheduled to be completed by 2022, will electrify and upgrade Caltrain's commuter rail service between San Francisco and San Jose. Additionally, a component of the project is to install Positive Train Control (PTC) in the corridor, which is now required by federal law. The improvements will allow high-speed trains to utilize the corridor as part of the blended system. The total cost of the Caltrain project is estimated at \$1.98 billion.

In Southern California, two projects have been identified for funding from the \$500 million in Proposition 1A bond funds appropriated in SB 1029. Specifically, in early 2017, \$76 million was approved for the Rosecrans/Marquardt grade separation project. The Rosecrans/Marquardt grade separation is in Santa Fe Springs on the BNSF mainline tracks at the intersection of Rosecrans and Marquardt Avenues. The intersection is also on the Los Angeles/San Diego/San Luis Obispo (LOSSAN) corridor, which is utilized by Amtrak and Metrolink. The intersection sees more than 112 freight and passenger trains per day and has been rated by the California Public Utilities Commission (CPUC) as the most hazardous grade crossing in California. The total cost of the project is \$155.3 million.

The remainder of the Proposition 1A bonds funds for Southern California, \$423.3 million, is dedicated to Los Angeles Union Station (LAUS) for the Link Union Station (Link US) project in downtown Los Angeles. The Link US project will extend up to 10 rail tracks at LAUS to the south of the station over U.S. Highway 101, including platforms and tracks for use by future high-speed rail. The project allows trains at LAUS to "run through" the station rather than head in and back out through a single entrance. The project is planned for two phases of construction with the cost of Phase A estimated at \$950.3 million, (including Proposition 1A bond funds), and the cost of Phase B estimated at \$1.14 billion. The project is expected to be completed in 2027.

### *Changes since the 2018 Business Plan*

In November 2018, the California State Auditor released a comprehensive audit of the high-speed rail program and found that flawed decision making and poor contract management contributed to billions in

cost overruns and construction delays. The auditor reiterated that the Authority does not have the funding to complete the system, and highlighted concerns over possible future cost increases. Additionally, the auditor made numerous recommendations to increase oversight of the project, focusing on the delivery of the Central Valley segment currently under construction, by strengthening internal Authority controls, such as contract management. The auditor also recommended increasing transparency and reporting. Specifically, one of the recommendations was for the Authority to develop a quarterly update to the Legislature on progress in the Central Valley to better inform policymakers and the public. Additionally, the auditor recommended the Authority develop a contingency plan for the Central Valley construction in case it is unable to meet its federal grant requirements. In November 2018, this committee joined the Joint Legislative Audit Committee to conduct an oversight hearing regarding the state audit.

In February 2019, Governor Newsom delivered his State of the State address and he appeared to signal a change in the project, shifting emphasis to completing a workable rail line in the Central Valley, but casting doubt over the completion of the full Phase I. Specifically, Newsome noted, “the project, as currently planned, would cost too much and take too long. There’s been too little oversight and not enough transparency.” He outlined a new Central Valley construction plan, including extending the current line north to Merced and south to Bakersfield, stating, “High-Speed Rail is much more than a train project. It’s about economic transformation and unlocking the enormous potential of the Valley.”

In response to Governor Newsom’s address, the FRA issued a letter stating that it plans to “de-obligate \$929 million in federal funding for the project.” The letter details what the FRA contends is the Authority’s failure to comply with the terms of the federal grant agreement for the FY 2010 funds. Specifically, the state must meet certain agreements under the federal grant agreement, including fully spending its state match to the ARRA funds prior to spending the FY 2010 and completing all environmental work on the full Phase I project by 2022. The FRA contends that the Authority has “materially failed to comply, with the terms of the agreement, and has failed to make reasonable progress on the project.” The FRA also stated it is exploring all legal options, which could put the roughly \$2.6 billion already expended also in jeopardy.

The Authority responded with a rebuttal letter in March 2019, reaffirming Governor Newsom’s commitment to the full Phase I project and detailing the Authority’s progress and its compliance with the grant agreement. On May 16, 2019, The FRA sent a letter formalizing its plan to de-obligate the \$929 million, stating that the letter provides a final decision on the matter and that the FRA is terminating the FY 2010 cooperative agreement with the Authority.

It is unclear what recourse the State of California may have regarding this issue. The ongoing disengagement of the federal government and the subsequent risk to the project is detailed in the PUR.

### **2019 Project Update Report**

On May 1, 2019, the Authority released the 2019 PUR. As mentioned, the PUR is not normally as extensive of a document as the Business Plan, which is released every even-numbered year. However, the 2019 PUR takes on special significance as it is the first detailed public plan of the Newsom Administration. When Governor Newsom took office, he outlined his vision for the project in the State of the State. His speech, as detailed above, initially caused confusion about the future of the full high-speed rail project. Subsequent to the State of the State, Governor Newsom has reiterated his support for the completion of the project; however, he has focused the work of the Authority on completing an initial “building block” of a high-speed system in the Central Valley.

To help realize his vision, Governor Newsom appointed a new Chairman of the California High-Speed Rail Board of Directors, his chief economic advisor, Mr. Lenny Mendonca. Chair Mendonca states very clearly in the PUR that, “this report focuses the limited resources the state has identified to get a working section that can demonstrate the viability of the broader project.” Further that abandoning the project, “would leave California having spent \$5 billion, with nothing but lawsuits, job losses, and billions of IOUs with nothing to

show for our debts.” The PUR represents a plan to fund and deliver a high-speed rail line in the Central Valley.

### *Central Valley Line*

The new Central Valley Line is a 171 mile high-speed rail line from Merced to Bakersfield, with stations planned for Merced, Madera, Fresno, Kings/Tulare (future), and Bakersfield F Street. The Central Valley Line includes all of the current Central Valley construction, with extensions to Merced and Bakersfield. The PUR outlines updated cost estimates for the current Central Valley construction and the new Central Valley Line. Specifically, the Central Valley Line is estimated to cost \$18.3 billion and be up and running by 2028. The Central Valley Line estimates include the additional scope in the north and south, all track and systems, new high-speed trains, and several maintenance facilities.

The new line would be operated by an interim passenger rail operator and the Authority anticipates the Central Valley Line would require an operating subsidy. Together with completion of all of Phase I environmental work, as required by the FRA grant agreement, and construction of the book end projects, the PUR outlines a total cost of \$20.4 billion to complete the “building blocks.”

### *How did we get here?*

In 2017, the Authority brought on DB Engineering and Consulting USA as the ETO to assist in analyzing the operations and financing of possible early interim service prior to full build out of the Valley to Valley Line. The ETO was tasked with studying two options for interim service, a Central Valley Line with various station options and Bay Area service on the peninsula sharing tracks with the Caltrain system going from San Francisco to Gilroy.

The ETO concluded that the best scenario to pursue for interim service is a high-speed line from Merced to Bakersfield. The line would connect, cross platform, with the existing San Joaquins intercity passenger rail (Amtrak) service and ACE at Merced. In the south, the high-speed rail line would connect with Amtrak bus service to Southern California. The ETO measured possible ridership in this corridor and concluded that revenues would be 2.8 times higher than what are currently forecasted for the San Joaquins and ACE, and that roughly 90 minutes would be shaved off travel times.

To bring this all together, the current Central Valley construction would be extended north to Merced and south to Bakersfield. Additionally, the plan relies on the completion of the current construction and service plans envisioned by the San Joaquins/ACE Valley Rail Plan. Specially, the Valley Rail Plan is an extension of ACE between Sacramento and Merced and implements two new daily round-trips for the Amtrak San Joaquins service to better connect the Central Valley with Sacramento. The Valley Rail Plan anticipates the ACE extension to Ceres would be completed in 2023 and the ACE extension to Merced would be completed by 2026. According to the San Joaquin Regional Rail Commission (SJRRRC), who operates both the San Joaquins and ACE, the Valley Rail Plan is fully funded, but work will still be required to reach agreements with freight railroad operators to authorize increased travel on their corridors.

The PUR envisions that SJRRRC could be the operator of the new high-speed service and that it would no longer operate “competing” Amtrak rail service south of Merced. It is unclear what this specifically means, or how it would work in practice. Additionally, it is unclear whether this type of interim service would violate Proposition 1A, which requires “planned passenger train service to be provided by the Authority, or pursuant to its authority,” to operate without a subsidy. Currently, the San Joaquins is one of the busiest Amtrak routes in the United States, connecting the Central Valley to Sacramento and Oakland, with bus connections south to Los Angeles. ACE connects nearly 1.5 million commuters per year to the Bay Area.

### *Costs Continue to Increase*

The ETO was also tasked with reviewing cost estimates for the current Central Valley construction, and incorporate these new estimates with the full cost of the newly envisioned Central Valley Line. Additionally, the Authority performed a financial risks analysis to recast cost estimates to reflect a 70

percent level of confidence, or a P70, that the project will stay within its budget baseline. Prior Business Plans reflected only a 10 percent level of confidence, or a P10.

These analyses determined that the current Central Valley construction contracts have again increased in costs, by \$1.8 billion, over the 2018 Business Plan for a total of \$12.4 billion. The Authority indicates that this primarily reflects the inclusion of a larger contingency to meet this new P70 level. This amount is reflected in the overall \$18.3 billion price tag for the Central Valley Line. The ETO did not, however, conduct a similar analysis on the Valley to Valley Line.

#### *Where will the money come from?*

The Authority identifies numerous existing sources of funding to complete the Central Valley Line.

#### Federal Funds

- \$2.55 billion ARRA
- \$929 million FY 2010

#### State Funds

- \$7.46 billion Proposition 1A (non-bookends)
- \$1.1 billion Proposition 1A (bookends)
- \$2.42 billion Cap-and-Trade received through December 2018
- \$6 billion -- \$9 billion Cap-and-Trade future revenue through 2030

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### **\$20.45 -- \$23.45 billion total funding available**

This funding scheme assumes the Authority is able to retain all of the federal funds, including the \$929 million the FRA is currently threatening to de-obligate, access to the remaining Proposition 1A bonds, and continued allocation of Cap-and-Trade funds at a certain level per year.

#### *Funding and Project Risks*

- **Federal Disengagement** -- It remains unclear how and when the funding and project situation with the federal government will be resolved. As noted, and discussed extensively in the PUR, the FRA has systematically disengaged with the Authority. The Authority identifies this as the most significant risk facing the project. This disengagement is not only reflected in the FRA letter, but in day-to-day activities usually conducted by a funding partner. Specifically, since July 2018, the FRA has not acted as required to complete environmental reviews by withdrawing from its responsibilities under the National Environmental Policy Act (NEPA). Additionally, the FRA is not participating in meetings with other federal environmental agencies.

The environmental disengagement represents huge problems for the project. In the near term, two critical project sections will be indefinitely delayed – the Central Valley Wye, north of Madera, and the Bakersfield Station Locally Generated Alternative. The Authority must environmentally clear these sections to complete the Central Valley Line. Additionally, the current FRA grant agreement requires full environmental clearance on all segments of full Phase I of the project by 2022. The FRA actions could also impact the bookend project at LAUS as FRA is part of the NEPA review for that project. Both the Authority and Los Angeles County Metropolitan Transportation Authority (LA Metro) are pursuing a “CEQA-first” strategy, completing environmental reviews under the California Environmental Quality Act (CEQA) to try to keep the projects on schedule.

According to the Authority, “if the FRA has not engaged by May 2019, the Authority will incur additional delays in completing a Merced-Fresno-Bakersfield operating section, as well as incur additional costs increases, delaying the start of operations within the Central Valley.”

- Possible Litigation – As mentioned, the Authority must clear a number of hurdles required by Proposition 1A to not only fully access funding for the Central Valley Line but also commence operations of a high-speed interim service. Specifically, the Authority must submit a detailed funding plan to gain access to the remaining \$4.1 billion of Proposition 1A bond funds. The funding plan informs the Legislature prior to a vote to appropriate the funds. This issue was litigated after the passage of SB 1029, however, it was ultimately unsuccessful. The Authority anticipates coming forward with this funding plan in the Fall of 2019, with possible consideration by the Legislature next Spring. Additionally, as discussed, there could be possible litigation over the Central Valley high-speed interim service plan as it would need a state subsidy to operate.

### **Conclusion**

Unquestionably, the Authority's task - to build a high-speed passenger rail system - is a daunting one. The sheer size of the program combined with uncertain funding, rigidly prescribed design criteria, constant legal threats, weighty environmental concerns, and difficult engineering challenges seemingly jeopardize accomplishment of the task at every turn.

Now the Authority, and the State of California, face even tougher challenges as the ongoing dispute with the federal government throws the project into serious, immediate jeopardy. It is clear that the PUR outlines the vision of the new Administration, to build a workable line with the funding we have and hope to demonstrate both the technology and the benefits of high-speed rail. However, this approach still raises many questions that the Legislature must consider:

- Does the plan serve the transportation needs of the state?
- Can the Central Valley Line be built at the current cost and schedule?
- Will all of the other pieces, such as the ACE/San Joaquins build out, come together on time and provide the level of service anticipated?
- Would the envisioned interim high-speed service conform to state and federal requirements?

The Legislature will be expected to take action on aspects of the new plan in the coming year. At today's hearing, representatives of the Authority Board of Directors and the Authority will discuss the details of the PUR and the new direction. The LAO will discuss its findings and highlight issues for the Legislature to consider, as will the independent High-Speed Rail Peer Review Group. Next, the committee will hear from the Authority's regional partners who will discuss the implications of the plan on their regions, including the partner at the heart of the PUR, the ACE/San Joaquins. Finally, members will have an opportunity to hear from the public regarding the project.