South Coast
Air Quality Management District
21865 Copley Drive, Diamond Bar, CA 91765-4178
(909) 396-2000 • http://aqmd.gov

ATTACHMENT B

April 4, 2006

Abstract of Fiscal Year 2006-07 Draft Budget and Draft Work Program
of the
South Coast Air Quality Management District

Attached is the Executive Officer's transmittal letter to the Governing Board and the Budget Options and Summary from the Fiscal Year 2006-07 Draft Budget and Draft Work Program. The Budget Options and Summary is a brief overview of the AQMD and includes program and financial information. The FY 2006-07 Draft Budget and Draft Work Program is also available on our website at http://www.aqmd.gov/finn/financialinformation.htm

If you have any questions about the Fiscal Year 2006-07 Draft Budget and Draft Work Program, please contact Cheryl Wade, Financial Services Manager, at (909) 396-2767.

Attachments

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April 4, 2006

South Coast Air Quality
Management District Board

Transmittal of the Executive Officer's
Draft Fiscal Year 2006-07 Budget and Work Program

This proposed draft Budget and Work Program continues the AQMD's commitment to protecting public health. For Fiscal Year (FY) 2006-07, I am proposing a budget that increases staffing levels by one position and increases expenditures by approximately $3.1 million from the amended FY 2005-06 budget. Due to substantial increases in retirement rates over the past few years, new three-year labor agreements, and the continued reduction in emissions fees revenues reflecting lower emissions as a result of additional emission controls placed on the Basin's largest emitters, the agency's revenues do not recover program costs.

Since FY 1991-92, the AQMD has reduced staffing and program costs despite increased program requirements. This year's proposal is $118.6 million and includes 786 funded positions. Compared to fifteen years ago, this request reflects 32% less staffing and an increase of 5% of budgeted expenditures. Adjusting today's dollar for inflation, this expenditure proposal is 36% less than the FY 1991-92 adopted budget. Despite these reductions and the success of several streamlining measures adopted by the Board, estimated revenues for next year do not recover the cost of AQMD's stationary programs. In order to bring the agency's fee revenues in-line with its program costs and reduce the agency's dependence on one time revenues (penalties) to balance its budget, staff has spent the last year analyzing its program costs and outputs. This analysis builds upon previous work detailed in a 1999 Fee Structure Study performed by Thompson, Cobb, Bazilio and Associates, PC, a Certified Public Accountants and Management Consultants firm, in addition to inputs in 2005 from a Stakeholders Working Group regarding discretionary program expenditures. Based on that analysis, I am recommending a cost recovery fee increase of 10% on permit, annual operating, and emissions fees (3.65% CPI for the remaining fee supported programs) plus an appropriation from the Undesignated Fund Balance of $1.8 million. In addition, I am proposing one other alternative for Board consideration. This alternative is a 3.65% across-the-board fee increase consistent with the 2005 change in the California Consumer Price Index, plus an appropriation from the Undesignated Fund Balance of $5,778,716. Nevertheless, both options may entail further downsizing in future years from the current budget.

The budget is based on the goals and objectives presented to the Governing Board at the February 3, 2006 meeting. These goals emphasize our continued efforts to improve efficiency and productivity, implementation of the AQMP, implementation of the Board's initiatives, implementation of the Fleet Rules, pursuing environmental justice enhancement activities, reduction of air toxics, and continuing to address other priority issues.

The public and the business community have several opportunities to participate in the budget development process. These include meetings of the Budget Advisory Committee; one public workshop to discuss and receive comments on the impacts of the proposed amendments to the fee rule; one public workshop to discuss the proposed budget and work program, and two public hearings.

In summary, while this proposed budget for FY 2006-07 represents an increase from the current amended budget, most of this increase is associated with labor agreements and increased retirement contributions. Estimated revenues for FY 2006-07 are $116,819,069. The AQMD plans to utilize a portion of its reserves over the next few years to make up for the drop in revenues, as we strive to balance revenues and expenditures. The AQMD will continue its efforts to make progress toward attaining the federal and state clean air mandates in the most cost-effective manner possible.

Respectfully,

Barry R. Wallerstein, D.Env.
Executive Officer

BRW:PHP

BUDGET OPTIONS AND SUMMARY

Preface

The following represents the preliminary Draft Budget and Work Program of the South Coast Air Quality Management District (AQMD). This proposal is available for public review and comment during the month of April. Two initial workshops are scheduled to discuss this year's proposal, one for the public on April 12, and one for the Governing Board on April 28.

As part of this year's budget proposal two options are being presented for discussion and consideration by the Governing Board at their April budget meeting. Option I (cost recovery) proposes to increase fee rates for permitting, annual renewals and emissions by 10% (CPI for the remaining fee programs) and specific adjustment to the fee regulation to recover certain other permitting, compliance, and Hot Spot Toxic program costs. Option II (CPI) includes a proposed increase of 3.65%, plus the previous specific adjustments. The cost recovery option represents approximately $4,000,209 in additional revenue and would begin to bring into balance stationary source fee revenues with their associated program costs. This draft budget and the supporting documentation have been prepared reflecting this option. The cost/revenue associated with each option and the effect on the fund balance is detailed below:

	Options	Expenditures	Revenues	Change in Fund Balance
I	**10% Fee Increase**	$118,597,576	$116,819,069	$(1,778,507)
II	**CPI (3.65% Fee Increase)**	$118,597,576	$112,818,860	$(5,778,716)

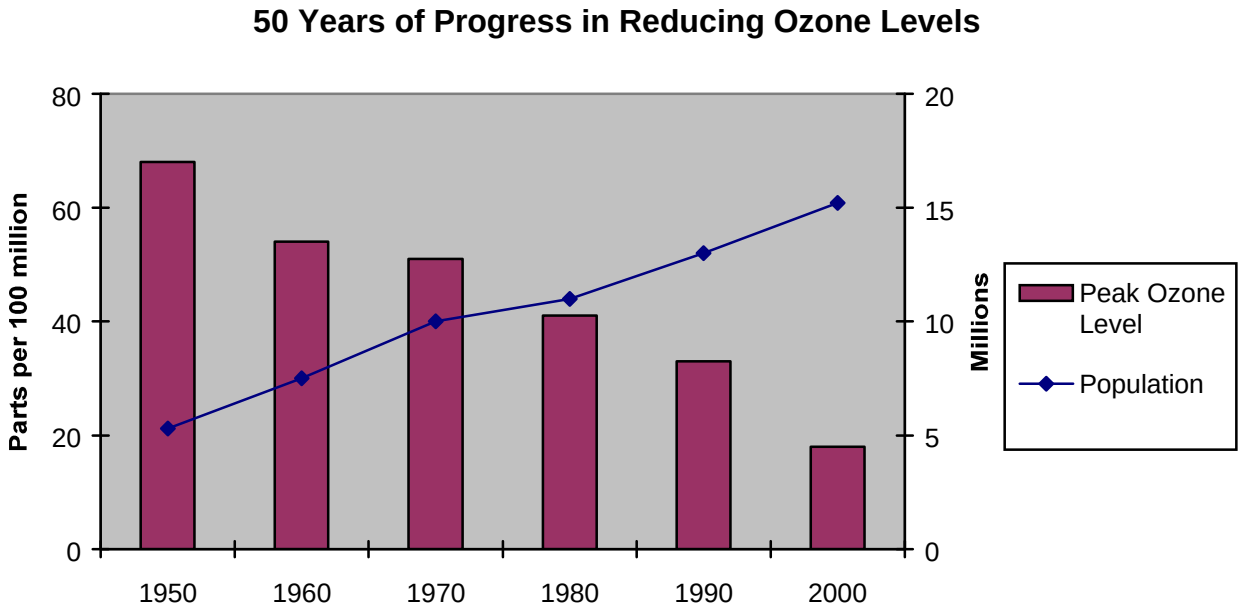
A final Draft Budget and Work Program, which may include changes based on comments from the public and Board, will be presented for adoption at a public hearing scheduled for June 2, 2006.

Introduction

The South Coast Air Basin has suffered unhealthful air since its rapid population growth and industrialization during World War II. While air quality has improved, the residents of the Basin still breathe some of the most polluted air in the nation.

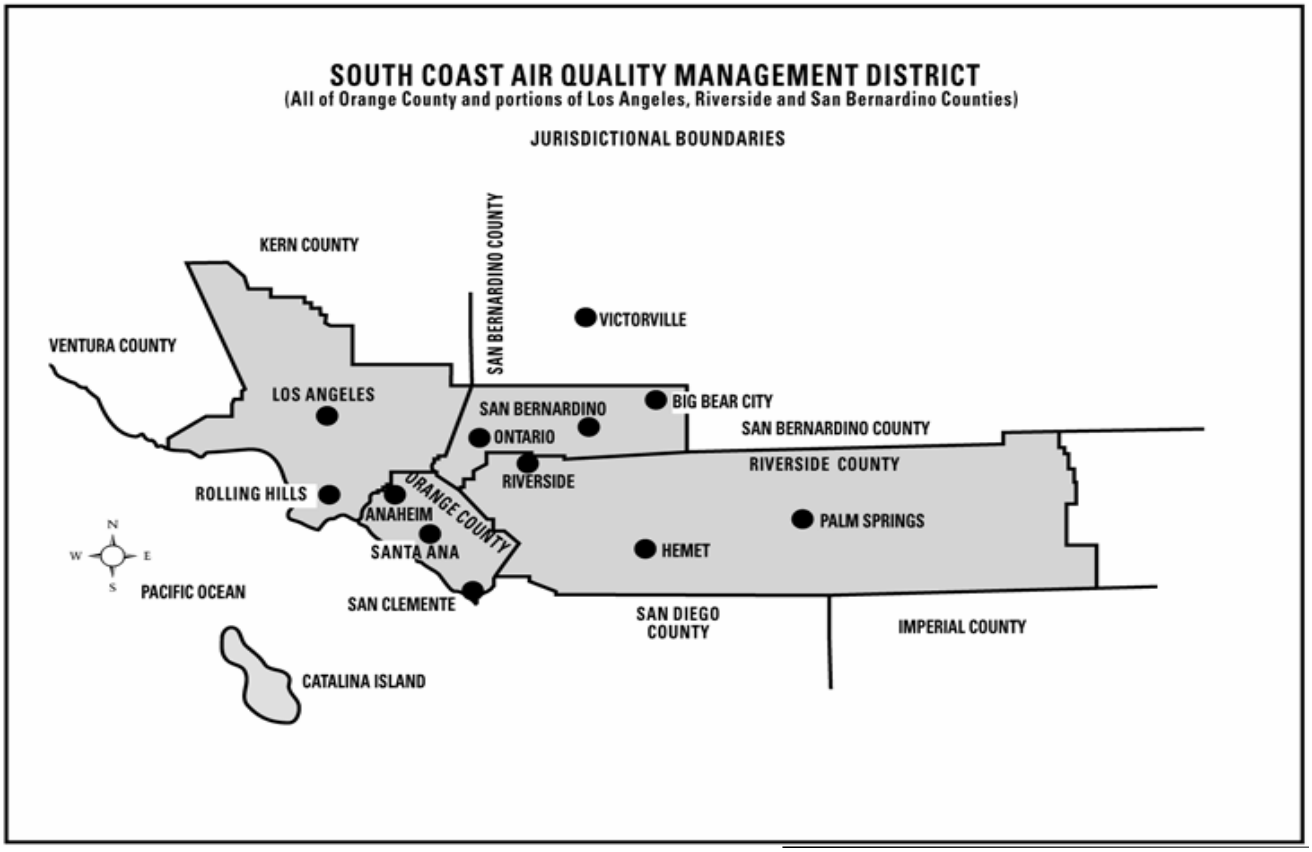
The 50-year history of the region's air pollution control efforts is, in many ways, one of the world's key environmental success stories. Peak ozone levels have been cut by almost three-fourths since air monitoring began in the 1950s. Population exposure was cut by 50% during the 1980s alone.

Since the late 1940s when the war on smog began, the region's population has tripled from 4.8 million to over 15 million; the number of motor vehicles more than quadrupled from 2.3 million to 9.7 million; and the area has grown into one of the most prosperous regions of the world. This phenomenal economic growth illustrates that pollution control and strong economic growth can coincide.



Government

The South Coast Air Quality Management District (AQMD) began operation on February 1, 1977 as a regional governmental agency established by the California Legislature pursuant to the Lewis Air Quality Management Act. The AQMD encompasses all of Orange County and parts of Los Angeles, San Bernardino and Riverside Counties, representing over 16 million citizens. It succeeded the Southern California Air Pollution Control District and its predecessor four county air pollution control districts, of which the Los Angeles County Air Pollution Control District was the oldest in the nation, having been formed in 1947. The AQMD Governing Board is composed of 12 members, including four members appointed by the Boards of Supervisors of the four counties in AQMD's jurisdiction, five members appointed by cities in the AQMD's jurisdiction and three members appointed by the Governor, the Speaker of the State Assembly and the Rules Committee of the State Senate, respectively. The members appointed by the various Boards of Supervisors and cities consist of one member of the Board of Supervisors of Los Angeles, Orange, Riverside, and San Bernardino Counties, respectively, and a mayor or member of the city council of a city within Orange, Riverside and San Bernardino Counties. Los Angeles County cities have two representatives, one each from the western and eastern portions of the county.



Mission

The mission of the AQMD is to protect public health from air pollution while being sensitive to the economic needs of the Basin's businesses. It does this through a comprehensive program of planning, regulation, education, enforcement, compliance incentives, technical innovation and promoting public understanding of air quality issues. Over the past several years the AQMD has implemented a policy of working with regulated businesses to ensure their participation in making the rules which will impact them. This cooperative approach has resulted in greater business support for achievement of air that is healthful to breathe.

To carry out its mission the AQMD has developed a set of Goals and Objectives, which is evaluated and revised annually and presented at a public hearing. The following Goals have been established for FY 2006-07:

I. Ensure expeditious progress toward meeting clean air standards and protecting public health.
II. Ensure equitable treatment for all communities.
III. Operate efficiently and in a manner sensitive to businesses.

These goals are the foundation for the AQMD's Work Program. Each goal is supported by multiple activities, which target specific areas of program performance. A public hearing to receive input on the Goals and Objectives for FY 2006-07 was held on February 3, 2006.

Budget

The AQMD's annual appropriated budgets are adopted for the general fund. Budgets are adopted on a budgetary basis that includes encumbrances as expenditures. All annual appropriations lapse at fiscal year end to the extent they have not been expended or encumbered. Amendments to increase the budget must be approved by the Governing Board.

To meet its financial needs, the AQMD utilizes a system of evaluation fees, annual operating fees, emission fees, Hearing Board fees, contracts, penalties/settlements and investments that generate approximately 72% of its revenues. The remaining 28% of its revenue are from an Environmental Protection Agency grant, California Air Resources Board subvention, and California Clean Air Act Motor Vehicle fees. Beginning with its Fiscal Year 1978-79 Budget, the AQMD no longer received any property tax moneys.

The draft budget consists of two volumes. The first volume is the Draft Budget and Draft Work Program that presents the primary information regarding proposed program revenues and expenditures for the new fiscal year and a forecast for the second and third years. The second volume is the Supporting Documentation, which contains detailed expenditure and program justifications supporting the draft budget and work program requests. The budget is a line-item budget structured by office. The budget is supplemented with a work program which estimates staff resources and expenditures along program and activity lines.

This draft budget and work program is scheduled for adoption by the South Coast Air Quality Management District Governing Board at its June meeting. The period covered by this budget is Fiscal Year 2006-07, which ends on June 30, 2007.

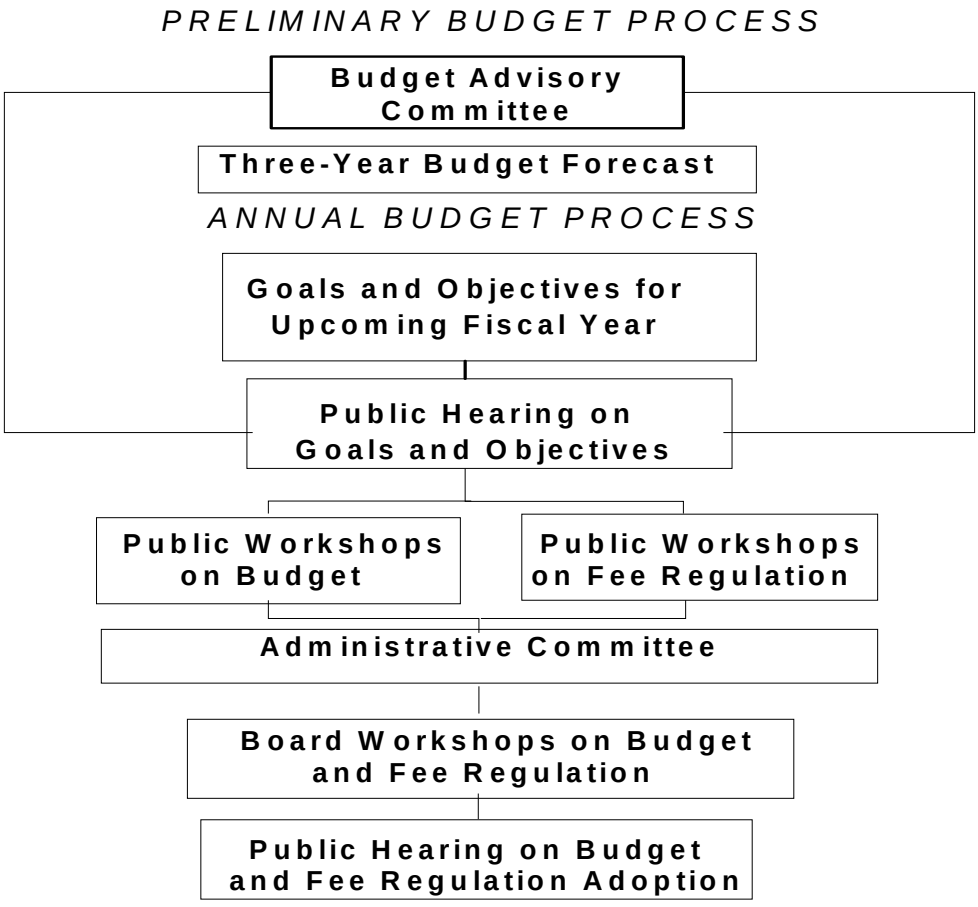
Budget Process

The AQMD has a comprehensive budget process, which establishes goals and objectives and monitors progress in meeting those goals and objectives.

Up to and including the budget adoption hearing by AQMD's Governing Board, the public and the business community have several opportunities to participate in the budget process. The opportunities include:

- meetings of a budget advisory committee made up of business and environmental representatives
- several public workshops—to discuss proposed changes to the fee rule and to discuss the proposed budget
- two public hearings—one on the Goals and Objectives and one on the proposed budget

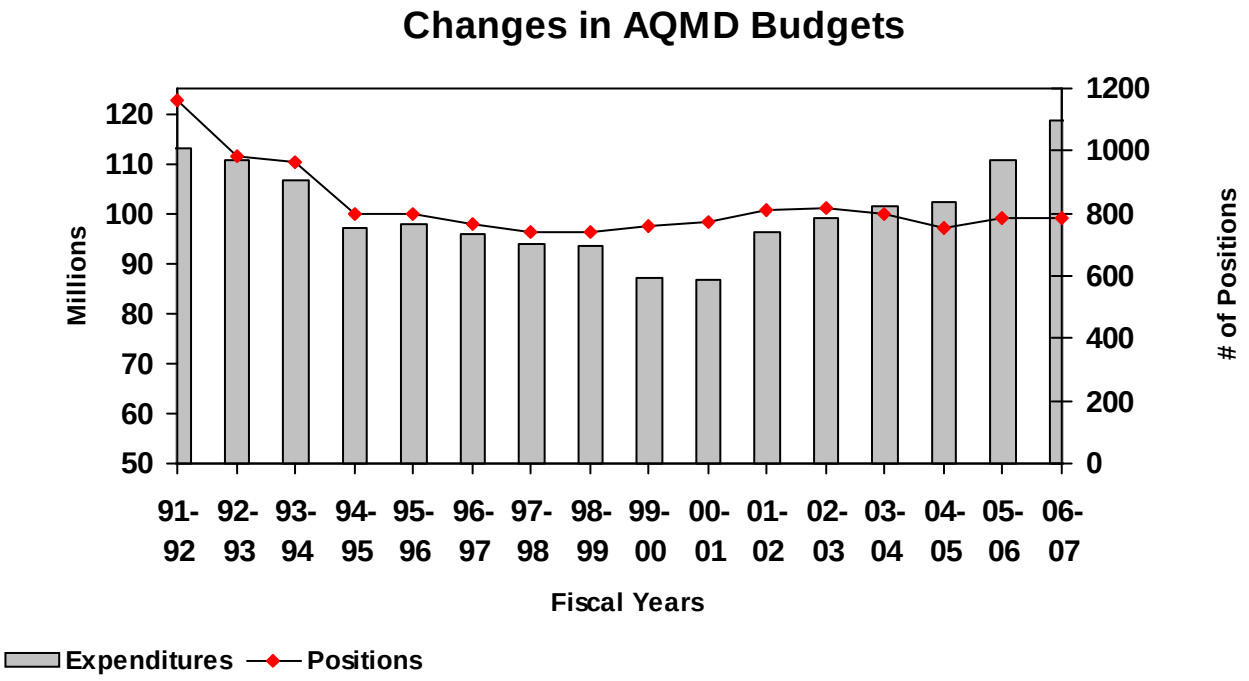
The following flow chart represents the major milestones that take place in the development of the AQMD budget.



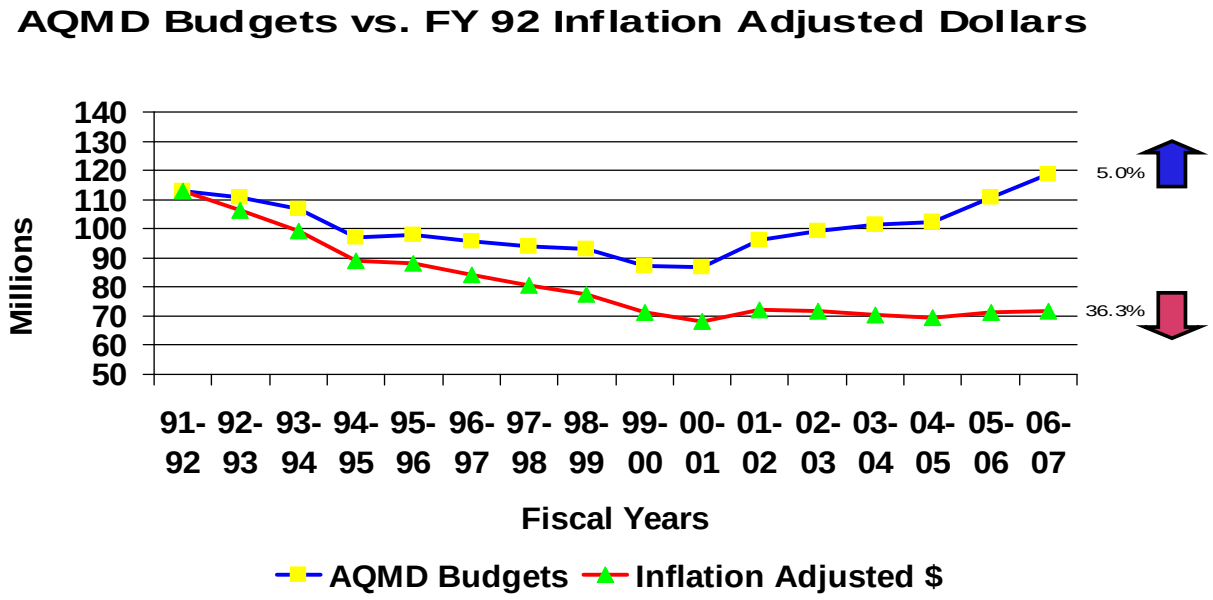
Following input from the public, Budget Advisory Committee, and Governing Board the draft budget for the ensuing fiscal year is prepared and made available in early April. In June the AQMD Governing Board holds a public hearing on the adoption of a final proposed operating budget, including final fee schedules. The adopted budget becomes operative on July 1.

Budget Changes

To minimize the financial impacts of AQMD programs on industry, the agency, since the early 90's, has reduced program expenditures as well as significantly downsizing agency staff.



To meet its program commitments, despite new federal and state mandates and increased workload complexity, the AQMD has continued to streamline many of its operations reducing the cost of its programs. Compared to FY 1991-92, this year's proposal reflects staffing levels that are 32% (377 FTEs) below 1991-92 levels and expenditures ($5.6 million) that will exceed the 1991-92 budget for the first time in 15 years. When adjusted for inflation, this year's expenditure request is 36.3% less than FY 1991-92.



This year's request proposes the use of approximately $1.8 million from the Fund Balance along with estimated revenues of $116.8 million to balance a requested expenditure budget of $118.6 million. Despite a proposed fee increase of 10% to recover the program costs associated with permitting, annual operating and emissions, and increased revenue from specific fee adjustments to recover certain permitting, compliance, and "Hot Spot" Toxic program costs, an average 9% increase in retirement contribution rates and increases associated with recently concluded labor negotiations will continue to impact the cost of AQMD programs.

To continue our progress toward meeting federal and state health standards, the AQMD has implemented several programs in recent years such as market-based incentives (RECLAIM), permit streamlining, source education, business assistance, and technology advancement. For FY 2006-07 emphases will be on implementing the Fleet Rules; implementing the Board's initiatives; implementing the 2003 AQMP; developing the 2007 AQMP; MATES III; pursuing environmental justice activities; reducing air toxics; and continuing to address other priority issues.

The following table compares AQMD budgets to actual/amended expenditures and revenues for Fiscal Years (FY) 2004-05 and 2005-06 and proposed for 2006-07.

	FY 04-05 BUDGET	FY 04-05 ACTUAL	FY 05-06 BUDGET	FY 05-06 AMENDED	FY 06-07 PROPOSED
Program Cost	$109.6	$102.2	$110.6	$115.5	$118.6
Revenues	$103.6	$112.9	$104.3	$107.8	$116.8

This draft budget request reflects an increase of $3.1 million in expenditures from the FY 2005-06 amended budget and an $8 million increase over the budget adopted last June. In the current budget (2005-06) the agency was able to realize significant one-time savings through negotiations with its employee's to delay for the majority of its workforce annual cost of living increases until mid-year (January). The FY 2006-07 budget request includes the full cost increases associated with new labor agreements, which in the long-term will reduce the agency's overall retirement cost by shifting a portion of the retirement cost to its employees and reducing retirement benefits for new employees. This proposal also includes one additional position to replace a long-term temporary, bringing the total staffing request to 786 funded positions.

Air Quality

The four-county Southern California region, designated for air quality purposes as the South Coast Air Basin, has the dirtiest air in the United States. The federal government has designated six pollutants that are pervasive enough across the nation to warrant national health standards. Called "criteria pollutants," these are: ozone (O_3); nitrogen dioxide (NO_2); particulates (PM_{10}); fine particulates ($PM_{2.5}$); carbon monoxide (CO); lead (Pb); and sulfur dioxide (SO_2).

In addition, the State of California through the CARB sets ambient air quality standards for these same pollutants. California's standards generally are tighter than the federal Environmental Protection Agency's, reflecting the conclusion on CARB's part that the federal standards are not adequate to protect public health in this region. Toxic compounds also are a potential problem. More toxic pollution is emitted into the air in the South Coast Basin than in any other region in California. The Basin's large number of cars and small sources—including small businesses and households using ozone-forming consumer products and paints—compounds the problem.

Air Quality Trends

Ozone levels have fallen by about three-quarters since peaks in the mid-1950s. Lead, nitrogen dioxide, and sulfur dioxide levels have gone down from nonattainment to full attainment of federal health standards. In 2005, the Basin continued the trend shift signaled in 2004 where days exceeding the federal one-hour standard were the lowest total recorded. In 2005, EPA replaced the one-hour standard with the eight-hour ozone standard. The federal eight-hour standard is more protective and although the standard was exceeded on 84 days, 2005 was the cleanest year on record for the Basin.

In 2004 the AQMD continued to meet the criteria specified in the federal Clean Air Act for attainment of carbon monoxide and the CARB redesignated the Basin as attainment. The request for federal redesignation is currently being evaluated by EPA. Particulate levels have also decreased in the past decade but not to the degree which ozone has improved. While our air quality is getting better it remains the most unhealthful in the nation.

Mandates

The South Coast AQMD is governed and directed by several state laws and a comprehensive federal law which provide the regulatory framework for air quality management in this Basin. These laws require the AQMD to take prescribed steps to improve air quality. Among the major statutes are:

State Laws

Under state law, the AQMD must develop and submit to the state at least every third year an Air Quality Management Plan (AQMP) demonstrating how the region will achieve state and federal ambient air quality standards, or at a minimum demonstrate that all feasible measures are being carried out to meet state air quality standards. To date, the AQMD's Governing Board has adopted such plans demonstrating attainment in 1989, 1991, 1994, 1996, 1999 (amendments to plan adopted in 1996) and 2003. Earlier plans in 1979 and 1982 did not show attainment and predicted continued unhealthful air well into this century. The AQMD is currently developing its 2007 revision to the AQMP to address achieving the new standards for $PM_{2.5}$ and eight-hour average ozone.

Generally speaking, AQMD is responsible for stationary sources such as factories and businesses. The CARB is primarily responsible for motor vehicles. The AQMD and CARB share responsibilities with respect to area sources. The AQMD and Southern California Association of Governments (SCAG) share some responsibilities with CARB regarding some aspects of mobile source emissions. Control of emissions from sources such as airports, harbors, and trains is shared by the federal EPA, CARB and the AQMD.

California Clean Air Act (AB 2595) requires air districts in California to adopt plans to expeditiously meet state ambient air quality standards. It mandates that AQMD's attainment plans meet several specific requirements including:

- a 5% per year reduction in emissions (the plan can achieve less than 5% annual reduction if it includes every feasible measure and an expeditious adoption schedule);
- Best Available Control Technology (BACT) for new and modified sources;
- Best Available Retrofit Control Technology (BARCT) for existing sources;

Lewis-Presley Air Quality Management Act (SB 151) specifies additional, more stringent requirements for air quality plans in the South Coast area. It specifies that AQMD has responsibility to prepare the plan in conjunction with SCAG, which must prepare the portions of the plan relating to demographic projections, land use, and transportation programs.

State law also includes the following measures:

- authorizes AQMD to adopt market incentives such as the emissions trading program known as RECLAIM as long as they achieve reductions equivalent to command-and-control regulations;
- requires AQMD to establish a program to encourage voluntary participation in projects to increase the use of clean-burning fuels;
- requires AQMD to adopt and enforce rules to ensure no net emission increases from stationary sources;

Air Toxics "Hot Spots" Information & Assessment Act (AB 2588) requires facilities that emit significant quantities of pollutants to prepare health risk assessments describing the impact of toxic contaminants on neighboring areas. If the AQMD determines that the toxic emissions create a significant risk, the public must be notified, and facilities must reduce emissions to below significant levels.

Tanner Air Toxics Process (AB 1807) requires CARB to adopt air toxic control measures to limit emissions of toxic air contaminants from classes of industrial facilities. Local air districts are required to enforce these regulations or adopt equally stringent regulations of their own.

Federal Law

The Clean Air Act. Under federal law, the AQMD must develop and submit to CARB for review and submittal to the federal EPA, an element of the State Implementation Plan (SIP) demonstrating how the region will achieve federal ambient air quality standards. In the case of ozone the plan was required to be submitted by November 15, 1994 and for fine particulates, PM_{10}, the plan was required to be submitted by February 8, 1997. Plans for other pollutants were submitted in earlier years. In 1997, EPA adopted new ambient air quality standards for $PM_{2.5}$ and for ozone measured over an eight-hour period. Plans to attain these federal standards are due to EPA in June, 2007. The South Coast Air Basin must attain the new federal standard for $PM_{2.5}$ by 2015 and the eight hour standard for ozone by 2021. The federal Clean Air Act mandates that sanctions be imposed on an area if a suitable plan is not adopted. These sanctions can include loss of key federal funds and more stringent requirements on new or expanding industries. Specific requirements for our air quality management plan include stringent requirements plus LAER and offsets for major new sources. Federal law also requires an operating permit program for major stationary sources, known as Title V, which must be supported by permit fees. Also, air toxics regulations adopted by EPA pursuant to Title III must be implemented by AQMD.

Programs

During the past 12 months, AQMD actively pursued the following programs.

Goods Movement & Air Quality Issues

Chairman's Clean Port Initiative

AQMD's Clean Port Initiative, announced by Chairman William Burke at a special Board meeting in Long Beach in November 2005, includes four guiding principles and seven action items outlining steps that the AQMD, along with federal and state agencies and local and international ports can take to help reduce port pollution in the region. A work plan to carry out the new initiatives was adopted by the Board in January 2006. The plan calls for the development and adoption this year of AQMD "backstop" rules that would take effect if the ports and other agencies did not take sufficient actions in a timely manner to reduce emissions. Such AQMD rules could:

- Prohibit emissions increases from new or expanded port facilities unless state-of-the-art pollution controls are used and compensating emission reductions are obtained from other port sources;
- Limit cancer and other health risks from port facilities; and
- Reduce port-related emissions to levels needed to achieve air quality standards.

Locomotive Efforts

AQMD adopts groundbreaking rules to address locomotive emissions. During the past year AQMD adopted three rules to address emissions from locomotives. In October 2005 the Board adopted Rule 3503 – Emissions Inventory and Health Risk Assessment for Railyards – to require the 19 freight railyards in the Los Angeles Basin to conduct detailed studies of the cancer risks posed to nearby residents from their toxic emissions.

Two other rules adopted by the Board in February 2006 address pollution from idling trains. Under Rule 3501 railroads will be required to keep records of all locomotive idling lasting more than 30 minutes. These records will provide information on the amount of emissions from idling trains and assist in identifying ways to reduce these emissions. Trains equipped with an anti-idling device or using alternative technology are exempt from the rule requirements. Rule 3502 is designed to eliminate air pollution from unnecessary idling by prohibiting unattended locomotives from idling more than 30 minutes for crew changes, meal breaks, queuing in railyards or performing maintenance or testing that does not require the train to operate.

AQMD opposes CARB's voluntary agreement with BNSF Railway Co. and Union Pacific. In June 2005, without any public input or public meetings, CARB announced a voluntary memorandum of understanding (MOU) with Union Pacific Railroad Co. and BNSF Railway Co. to reduce locomotive emissions. Since adoption of the MOU, AQMD has expressed ongoing, serious concerns about weak and vague provisions in the MOU and its overall lack of enforceability. At a January 2006 meeting AQMD encouraged the CARB Board to reject the MOU and instead renegotiate a stronger one with public participation from community groups and other air quality agencies. The CARB Board rejected the request but directed its staff to report back in six months with an update on implementation of the MOU.

AQMD co-sponsors legislation to measure locomotive emissions. Governor Schwarzenegger signed Assembly Bill 1222 (Jones) in October 2005. The bill establishes a pilot program to determine emissions from locomotives using remote sensing devices. AQMD Board members and staff worked throughout 2005 to encourage passage of the bill as part of an overall series of efforts to reduce diesel emissions from rail operations. CARB will design and conduct the pilot program. Program costs will be shared by AQMD, BNSF Railway Co. and Union Pacific.

In addition to the rules mentioned above, AQMD's Board adopted several other significant measures, including:

- Rule 1118 – Emissions from Refinery Flares – to reduce sulfur emissions from vent-gas flaring at refineries and other facilities in the basin. Changes to Rule 1118 are expected to reduce SOx emissions from about 2 tons per day in 2003 to less than 0.5 tons per day by 2012;
- Rule 1401.1 to place more stringent requirements on toxic air emissions from new facilities located near schools. The new rule will reduce the potential cancer risk to students near such facilities by requiring that new facilities locating within 500 feet of a school (or 1,000 feet in certain cases) not create a total cancer risk greater than one in 1 million; and

- ♦ Rule 1156 to require the two cement manufacturing plants in the region to cut their particulate emissions in half by 2010 through better housekeeping practices and other cost-effective measures.

Significant Court Cases & Settlements

Railroad Lawsuit

In February 2005, Union Pacific and BNSF filed a lawsuit against AQMD in an effort to invalidate AQMD's three railroad rules. The suit in federal court alleges that AQMD lacks the authority to adopt and enforce the rules. AQMD's position, backed by extensive legal research, is that AQMD does have the authority to enforce the rules and that they do not interfere with railroad safety or operations.

Landmark BP Settlement

In March 2005 AQMD and BP settled a lawsuit AQMD filed against BP for violations at BP's Carson refinery. Under the terms of the $81 million settlement, BP paid the AQMD $25 million in cash penalties; $6 million in past emission fees; and will provide $30 million over 10 years for community programs directed at asthma diagnosis and treatment and $20 million in new refinery improvements aimed at reducing emissions. Outside of the formal settlement, BP also agreed to spend approximately $25 million to replace a process tank that was the source of repeated, egregious nuisance violations.

Following public and Board member input, AQMD staff will bring a funding proposal for the $6 million to the Board in spring 2006.

Fleet Rules Case

Following a federal court ruling in May 2005, the AQMD resumed enforcement of its clean fleet rules for privately owned fleets under contract with public agencies. Starting August 1, 2005, school bus, transit bus, refuse collection, airport ground-access, and street sweeper rules now apply not only to public fleets but also to private fleets under contract to or operating under an exclusive license with state or local public agencies, including the State of California, counties, cities and special districts.

Rule 1105.1

In March 2006, the state appeals court rejected arguments by oil companies and upheld AQMD's Rule 1105.1 that requires the region's six major oil refineries to reduce their PM_{10} and ammonia emissions from their fluid catalytic cracking units by the end of 2006. The Western States Petroleum Association had argued that emission reductions required in the rule were not technically feasible, that the rule was not cost-effective and that AQMD did not prepare an adequate environmental assessment under the California Environmental Quality Act. The judge rejected all three arguments. Rule 1105.1 is expected to reduce direct PM_{10} emissions by 0.5 tons per day and ammonia emissions by 1.5 tons per day.

Technology Advancement/Accelerated Fleet Turnover

Remote Sensing Program for Passenger Cars

In September 2005 the Board approved a program to conduct remote sensing of one million vehicles in the region. The program will then provide incentives to the owners of the most highly polluting vehicles to either repair, scrap, or replace them. Beginning in 2006 remote sensing devices will be placed in multiple locations throughout the region to measure a vehicle's emissions. An independent foundation will contact owners of the dirtiest vehicles tested. Residents who meet state low-income guidelines will be eligible to qualify for additional funding. The program is expected to last about 12 months.

Five Cities Hydrogen Demonstration Project
AQMD dedicated the region's first municipal hydrogen fueling stations along with hydrogen-powered Priuses in the first half of 2006. Five cities in the region are partnering with AQMD to demonstrate five hydrogen fueling stations and a total of 30 hybrid Priuses with internal combustion engines that have been modified to burn gaseous hydrogen. The cities include Burbank, Ontario, Riverside, Santa Ana and Santa Monica. Each city and AQMD will operate five hydrogen-fueled Priuses for five years. The five cities program is aimed at stimulating demand for hydrogen fueling, accelerating the expansion of the region's hydrogen fueling network, and educating the public on hydrogen-fueled vehicles. The cities will use the vehicles in everyday city fleet driving as well as showcase them to community groups, neighborhood associations and schools. All five stations are expected to be open by spring 2006.

Lawn Mower and Leaf Blower Exchange Programs
Since 2003, the AQMD has annually conducted a series of lawn mover exchange events, where residents of the South Coast air basin exchanged their operable gasoline-powered lawn mowers for zero-emission cordless electric lawn mowers. A total of 11,500 mowers have been exchanged. The AQMD plans to exchange another 4,000 lawn mowers at seven events planned for spring 2006.

AQMD held its first leaf blower exchange program in February and March 2006 where professional landscapers and gardeners exchanged their gas-powered, backpack blower for a new gas-powered, 4-cycle, low-emission, low-noise model. A total of 1,500 blowers were exchanged at seven locations throughout the region. The new blowers are nearly five times cleaner than CARB's standard for new blowers.

Multiple Air Toxics Exposure Study III (MATES III)
The AQMD started collecting air samples in 2004 for some two dozen toxic air contaminants and four other substances as part of its follow-up to the landmark MATES II study conducted in 1998-1999. The goal of MATES III is to update toxic air pollution levels and toxic emission inventories, and then, through computer modeling, determine the cancer, as well as non-cancer, health risk from air toxics across the region. The study investigates potential toxic "hot spots" in communities. The monitoring frequency during MATES III is double that of MATES II. In addition a number of compounds related to vehicle emissions are also being measured as possible tracers of exhaust. Monitoring has been ongoing since 2004. However, due to unusually wet weather during the fall and winter months of sampling, the monitoring was extended for one additional year to compare results with a more typical year's meteorology. A draft report is expected by the end of 2006.

Conferences
Asthma Conference
AQMD hosted a one-day conference in February 2006 titled *"Asthma Impacts of Air Pollution-Healthier Solutions Today for our Children's Tomorrow"* at the Millennium Biltmore Hotel in downtown Los Angeles. The conference brought together an unprecedented breadth and depth of policy makers and health experts from Los Angeles Mayor Antonio Villaraigosa to medical researchers responsible for the region's largest study on air pollution and children's health. Participants examined the impact of air pollution on asthmatics and reinforced the need to do everything possible to reduce the risks.

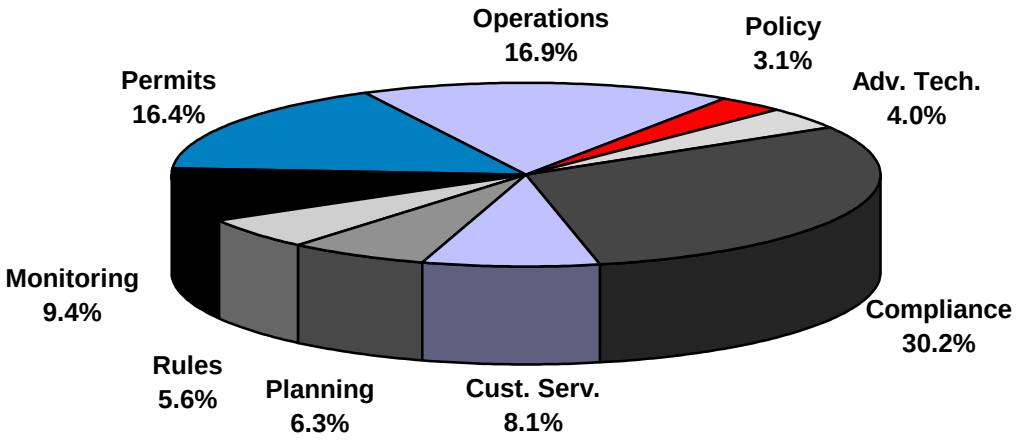
Faster Freight-Cleaner Air Conference
AQMD co-sponsored a three-day conference in January titled *Faster Freight – Cleaner Air 2006* held at the Long Beach Convention Center**.** The event showcased solutions and resources available to improve operations and reduce air emissions from the goods movement industry while creating healthy communities. The event also included an expo highlighting the innovative programs, policies and technologies now being implemented in ports around the nation to improve efficiency and reduce air emissions.

Work Program

AQMD expenditures are organized into nine Work Program Categories which describe its program activities. These categories are: Policy Support; Monitor Air Quality; Develop Programs to Achieve Clean Air; Develop Rules to Achieve Clean Air; Advance Clean Air Technology; Timely Review of Permits; Ensure Compliance with Clean Air Rules; Maintain a Program of Customer Service; and Operational Support.

Each activity within the Work Program falls into one of the above categories. The Work Program ties the goals and objectives of the agency to each of its program activities, identifying resources, performance measures/outputs and legal mandates. A complete description of each program category along with a detailed work program sort by program is included in the section on Work Program. The justifications in support of each activity are contained in the second volume of the Draft Budget Supporting Documentation. The pie chart that follows represents proposed budgeted expenditures by program for FY 2006-07.

Program Expenditures



The following table compares budgeted AQMD Work Program activities by category for FY 2005-06 and proposed for FY 2006-07.

Program Categories	FY 05-06	Proposed FY 06-07
Advance Clean Air Technology	$3,835,768	$4,706,585
Ensure Compliance with Clean Air Rules	33,482,134	35,824,314
Customer Service	9,361,909	9,666,423
Develop Programs to Achieve Clean Air	7,360,833	7,499,446
Develop Rules to Achieve Clean Air	6,236,296	6,640,529
Monitoring Air Quality	10,278,250	11,125,744
Operational Support	19,071,632	20,045,651
Permit Review	17,961,018	19,364,487
Policy Support	3,039,404	3,724,397
Total	$110,627,245	$118,597,576

Developing solutions to the air quality problem involves highly technical processes to meet the legal requirements of California and federal laws.

Monitoring

The first step is simply to determine the smog problem by measuring air pollution levels. AQMD today operates 34 monitoring stations throughout its four-county jurisdiction. These range from full-service stations that measure all criteria pollutants, as well as some toxic pollutant levels, to those which measure fewer pollutants in critical areas. These measurements provide the basis for our knowledge about the nature of the air pollution problem and for all planning to address this problem.

Pollution Sources

The AQMD in cooperation with CARB and SCAG estimates the sources of emissions causing the air pollution problem. Nature itself causes a small portion of the emissions and must be considered. In general, the AQMD estimates stationary and natural sources of emissions. SCAG develops the information necessary to estimate population and traffic, and CARB develops the information necessary to estimate mobile- and area-source emissions using the SCAG traffic data. This data is then pulled together in the AQMP for use in developing the necessary control strategies.

Computer Modeling

The AQMD's planners take monitoring data and estimates of pollution sources and enter it into state-of-the-art computer programs to model the movement and peak locations of smog. Through a series of "what if" questions, planners can look at different control scenarios to determine what strategies best reduce air pollution at the least cost.

Due to the nature of air pollution, these models can be very complex. Some pollutants are not emitted directly into the air but are products of photochemical reactions in the atmosphere. For example, VOCs mix with nitrogen dioxide (NO_2) and "cook" in sunlight to form ozone; similarly, nitrogen oxide gases from tailpipes and smokestacks can be transformed into nitrates or particulates (PM_{10}). The planners thus must take into account the location and size of each source, how the wind carries the emissions, how different emissions react to one another once they are in the atmosphere, and where the pollution is eventually carried. This means considerable weather data must be collected along with the emissions data.

Planning

With emissions data and an air quality model in place, planners can develop possible control strategies and scenarios. As mentioned earlier, for the most part, strategies to reduce driving are developed by SCAG, while mobile source control standards are developed by CARB. The AQMD focuses most of its effort on stationary source controls.

Once a plan of emission controls to achieve federal standards is outlined, the AQMD is required to hold multiple public meetings to present the proposed control strategies and receive public input. The AQMD also conducts a socioeconomic analysis of the control program. The AQMD maintains an ongoing and independent advisory group of outside experts for both its air quality and socioeconomic modeling.

To meet federal air quality standards, the 2007 AQMP calls for significant reductions from projected baseline emissions (2015 for $PM_{2.5}$ and 2021 for eight-hour ozone). These reductions, while meeting federal standards, will still not result in attainment of all California air quality standards since these are more stringent than federal standards. The attainment plan is estimated to cost $3.2 billion dollars per year to achieve and will provide more than $6.6 billion per year in benefits relative to achieving the federal standards.

The AQMD is in the process of implementing the 2003 revision to the AQMP including the development of a number of specific control strategies. In addition, the AQMD is working on improving the emissions inventory and modeling techniques to address the new federal $PM_{2.5}$ and 8-hour ozone air quality standards for the next AQMP revision, expected in 2007.

Rulemaking

The regulatory process, known as rulemaking, takes the concepts of control measures outlined in the AQMP and turns them into proposed rule language. This process involves extensive research on technology; site inspections of affected industries to determine feasibility; typically a year or more of public task force and workshop meetings; in-depth analyses of environmental, social and economic impacts; and thorough review with appropriate Governing Board Committees.

This extensive process of public and policymaker participation encourages consensus in development of rule requirements so that affected sources have an opportunity for input into the rules which will regulate their operations. Once the requirements are developed, the proposed rule, along with an environmental impact report and a socioeconomic report, is presented to the Governing Board at a public hearing. Public testimony is presented and considered by the Board before any rule is adopted.

Enforcement and Education

The AQMD issues permits to construct and operate equipment to companies to ensure equipment is operated in compliance with adopted rules. Follow-up inspections are made to ensure that equipment is being operated under permit conditions.

Technical Innovation

In the late 1980s, AQMD recognized that technological innovation, as well as rule enforcement, would be necessary to achieve clean air standards. So it created the Technology Advancement Office to look for and encourage technical innovation to reduce emissions. The Legislature supported this effort by providing a $1 surcharge on every DMV registration fee paid within the AQMD. These funds have been matched at a ratio of approximately three-to-one with funds from the private sector to develop new technologies such as low-emission vehicles, low-NO_x burners for boilers and water heaters, zero-pollution paints and solvents, fuel cells and other innovations.

An additional $4 vehicle registration fee was authorized by the state legislature in 1990. These fees are administered through the AQMD with $1.20 going to the AQMD for mobile source emissions reductions, $1.60 subvened directly to cities and counties to support their air quality programs, and $1.20 to the Mobile Source Reduction Review Committee. This outside panel established by state law makes the decisions on the actual projects to be funded from this portion of the revenue.

Public Education

In the end, AQMD's efforts to clean up the air will be successful only to the extent that the public understands air quality issues and supports and participates in our cleanup effort. Thus, the AQMD strives to involve and inform the public through the Public Affairs office, public meetings, publications, the press, and—to the extent limited funds are available—free and paid public service announcements.

Fiscal Year 2006-2007 Budget

Comparison of Expenditures

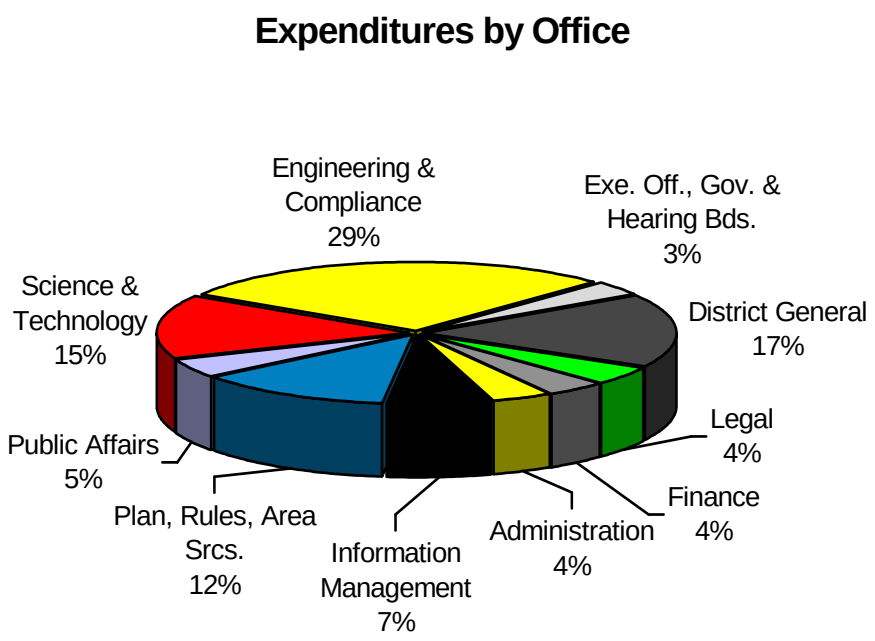
The following table compares the 2005-06 adopted budget to the proposed budget for 2006-07. The middle column is the current 2005-06 budget that includes Board-approved midyear adjustments through March.

Expenditures	FY 05-06 Adopted Budget	FY 05-06 Amended Budget	FY 06-07 Proposed Budget
Salaries/Benefits	$80,331,109	$80,484,580	$87,206,793
Insurance	1,211,400	1,220,400	1,250,000
Rents	747,886	791,716	712,290
Supplies	2,433,585	2,867,008	2,478,076
Contracts and Services	7,756,983	10,701,741	7,962,822
Maintenance	1,106,336	1,382,866	1,261,124
Travel/Auto Expense	447,300	605,641	478,620
Utilities	1,669,240	1,677,839	1,853,619
Communications	628,600	638,620	629,529
Capital Outlay	738,000	1,516,028	974,000
Other	881,740	953,249	970,399
Building Remodeling	0	0	0
Debt Service	12,675,066	12,675,066	12,820,304
Total	$110,627,245	$115,514,754	$118,597,576

The proposed budget for FY 2006-07 represents an increase of approximately $3.1 million from current budgeted expenditures. The amended budget includes midyear increases associated with Photochemical Assessment Monitoring System (PAMS) and $PM_{2.5}$ air monitoring; Low-level pollutant program; litigation matters; Remote Sensing-Locomotive emissions; MATES III; AQIP Lawnmower Buy Down program; clean fuels projects; Asthma Conference; two new positions to support Carl Moyer program requirements; and hybrid vehicle purchases.

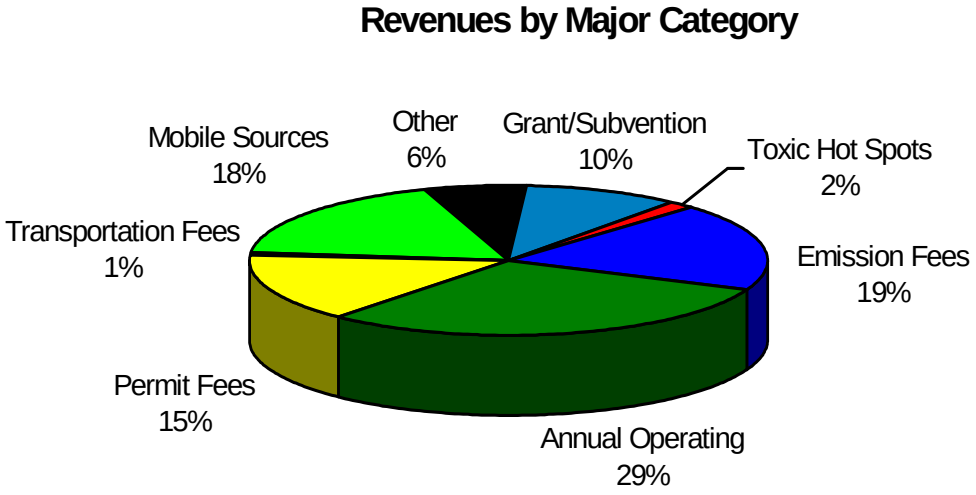
Comparing the FY 2006-07 budget request to the FY 2005-06 adopted budget, this request represents an increase of approximately $8 million over last year's adopted budget.

The pie chart below represents proposed expenditures by office for FY 2006-07.



Comparison of Revenue

Each year, in order to meet its financial needs, the AQMD Governing Board adopts a budget supported by a system of permit evaluation fees, annual operating and emission fees, Hearing Board fees, toxic "hot spots" fees, and transportation plan fees which are estimated to generate approximately $77.6 million or about 66% of AQMD revenues. Other sources, which include contracts, penalties/settlements, investment, and miscellaneous income, generate approximately 6% of total revenues. The remaining 28% of revenue will be received in the form of EPA grants, CARB subvention, and California Clean Air Act motor vehicle fees.



The following table compares the 2005-06 adopted revenues to the proposed revenues for 2006-07. The middle column is the adjusted revenues for 2005-06 that include Board-approved midyear changes.

Revenues	FY 05-06 Adopted Budget	FY 05-06 Amended Budget	FY 06-07 Proposed Budget
Emission Fees	$20,352,000	$20,352,000	$22,125,200
Annual Operating Fees	31,408,000	31,408,000	34,798,650
Permit Processing Fees	14,818,133	14,818,133	17,228,702
Mobile Sources	18,778,000	20,345,000	21,018,100
Transportation Programs	769,524	769,524	838,529
Toxic Hot Spots	1,490,000	1,615,000	1,912,000
Grant/Subvention	10,005,500	11,828,955	11,393,700
Other[1]	6,638,800	6,638,800	7,504,188
Total	$104,259,957	$107,775,412	$116,819,069

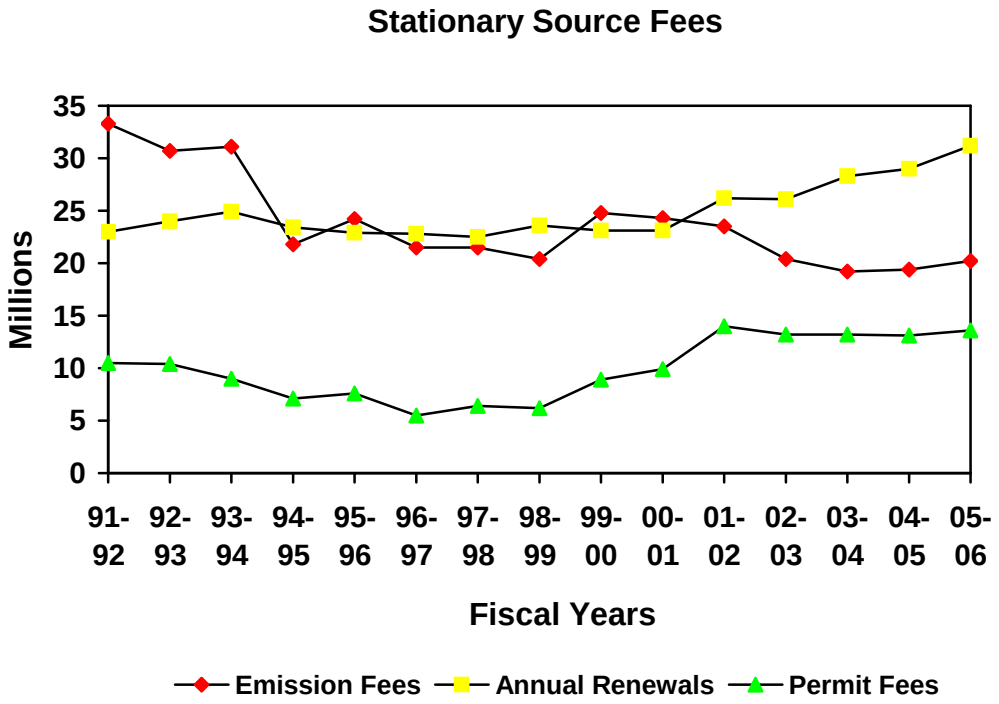
The proposed fee increase of 10.0% (CPI for the remaining fee programs) plus additional specific adjustments to certain permit and "Hot Spot" toxic fees to more fully recover costs are estimated to increase revenues from stationary sources by approximately $7.4 million from current year levels.

Mobile source revenues that are subvened to the AQMD by the Department of Motor Vehicles (DMV) are projected to increase slightly, according to the DMV, over FY 2005-06 revenues. Clean Fuels contract activities and revenues are recorded in a special revenue fund outside the general fund. Clean Fuels program work costs are reimbursed to the General Fund from the Clean Fuels Fund and are recorded in the mobile source revenue account.

Revenue from Environmental Protection Agency 103/105 grants is expected to decrease slightly from current levels as the result of less 105 grant and $PM_{2.5}$ funding. With regards to the State Subvention program, funding at current levels (reduced 33% from FY 2001-02) is expected for FY 2006-07.

Over the past several years, total permit fees (including permit processing, annual operating permit, and annual emissions based fees) collected from stationary sources has dropped 3% (greater if adjusted for inflation) from $66.8 million in 1991-92 to $65.0 million (estimated) in 2005-06.

[1] Includes revenues from Lease Income, Source Testing, Hearing Board, Penalties/Settlements, Interest and Other.



Debt Structure

Installment Sale Revenue Bonds were issued by the South Coast Air Quality Management District Building Corporation (Corporation) in August 1988 and September 1989 for the purpose of financing the building of the AQMD Diamond Bar Headquarters. The bonds are secured by a pledge of the semiannual payments to be made by the AQMD pursuant to an Installment Purchase Agreement between the Corporation and AQMD, whereby the AQMD is required to make the debt service payments on the Corporation's bonds. On December 1, 1992, AQMD's obligation to the Corporation under the installment purchase agreement was refinanced to take advantage of lower interest rates. In August 1998 the AQMD further reduced its debt service through the defeasance of a portion of the debt with proceeds from the sale of its El Monte facility. On June 1, 2002, AQMD again refinanced its obligation to the Corporation to take advantage of lower interest rates, obtaining a present value savings of $1,958,135.

The annual payment requirements under the installment purchase agreement are as follows:

	Annual Debt Service Requirement		
Year Ending June 30	Principal	Interest	Total
2007	4,565,000	1,494,105	6,059,105
2008	4,595,000	1,464,011	6,059,011
2009	4,625,000	1,428,342	6,053,342
2010	4,665,000	1,316,342	5,981,342
2011-2015	25,745,000	2,702,922	28,447,922
Total	$44,195,000	$8,405,722	$52,600,722

Pension Obligation Bonds were issued jointly by the County of San Bernardino and the AQMD in December 1995. In June 2004 the AQMD went out separately and issued pension obligation bonds to refinance its respective obligation to the San Bernardino County Employee's Retirement Association for certain amounts arising as a result of retirement benefits accruing to members of the Association.

The annual payment requirements under the refunding bonds are as follows:

	Annual Debt Service Requirement		
Year Ending June 30	Principal	Interest	Total
2007	3,305,000	3,456,199	6,761,199
2008	3,675,000	3,246,456	6,921,456
2009	4,070,000	3,013,947	7,083,947
2010	4,500,000	2,756,774	7,256,774
2011-2013	12,772,007	8,805,992	21,577,999
2014-2018	16,257,815	19,701,405	35,959,220
2019-2023	22,877,074	14,148,372	37,025,446
Total	$67,456,896	$55,129,145	$122,586,041

Fund Balance

The AQMD is projecting an undesignated fund balance for June 30, 2007 of $33,671,504. Following are the projected Reserves and Designations at June 30, 2007.

Reserve for encumbrances	$5,200,000
Reserve for inventory of supplies	80,000
Designations:	
for self-insurance	2,000,000
for unemployment claims	80,000
for litigation/enforcement	3,000,000
for budget stabilization	8,000,000
for enhanced compliance activities	291,061
for capital equipment replacement	2,000,000
Total	$21,529,061

Reserves represent portions of the fund balance set aside for future use and are therefore not available for appropriation. These reserves are made-up of encumbrances which represent the estimated amount of current and prior years' unperformed purchase orders and contract commitments in process at year-end; and inventory which represents the value at cost of office, computer, cleaning and laboratory supplies on hand at year-end. Designations in the fund balance indicate plans for use of financial resources in future years. The AQMD is self-insured for general liability, workers' compensation, automobile liability, premise liability, and unemployment. These designations have been made to provide for unanticipated judgments against the AQMD, which exceed the budget. The designation for litigation/enforcement provides funding for outside legal support. The designation for budget stabilization provides for revenue shortfalls in future years as revenues are not projected to keep pace with projected program maintenance costs. The designation for enhanced compliance activity is to provide funding for inspection/compliance efforts. The designation for capital equipment replacement is to provide funding for the periodic purchase of costly replacement equipment or systems that have reached the end of their useful life.

As mentioned at the beginning of this section on revenues, the AQMD currently receives the bulk of its funding (66%) from stationary sources and relies on State subventions and federal grants to support a majority of the remaining costs in such program areas as air monitoring, regional modeling, emissions inventory, planning, rule making, public nuisance and emergency response. Over the past fourteen years the AQMD has in all but two year's held its general fee increases to the change in the Consumer Price Index (CPI) and made significant reductions in its workforce and budget to offset declining revenues from Emission Fees. Fortunately, the agency has sufficient reserves to cushion the projected revenue and expenditures impacts for next year. However, future increases in labor and retirement costs coupled with reduced funding will force further staffing and program reductions unless revenues can be brought in line with program costs.