# MBTA 2011 Operating Budget Board Action

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STAFF SUMMARY SHEET
(MBTA PROCEDURES NO. 1)

| TO | | FOR | | FROM: | | |
|---|---|---|---|---|---|---|
| 1 | GM | | Approval / Signature | Dept.: Budget | Author: Mary Runkel | Tel Ext.: 3285 |
| 2 | BD | | Vote / Info | Subject: FY2011 Operating Budget | | Date: March 3, 2010 |

Implications: (The implications checked below are involved in this action, are discussed below or in a separate enclosure, and have been considered in the final recommendation.)

- [ ] Capital Budget
- [x] Operating Budget
- [ ] Legal
- [ ] Other

## PURPOSE

To request that the Board of Directors approve the Authority's budget of current operating expenses and debt service costs for the twelve-month period of fiscal year 2011 (July 1, 2010 through June 30, 2011) and to direct the General Manager to submit the approved budget to the MBTA Advisory Board.

## DISCUSSION

The Authority's financial challenges have been daunting over the past several years, exacerbated greatly by the pervasive malaise affecting the local, state, national, and global economies. Transit systems in the United States, indeed many local and state governments, are facing unprecedented budget gaps this year. One has only to read the press to see the number of large transits which are imposing service cuts, fare increases, and the use of federal stimulus money to plug budget holes.

In many ways, the Authority is fortunate when compared with its peers because it receives dedicated revenues (sales tax and assessments) of $917.2 million and, as a result of Transportation Reform last year the Authority now receives contract assistance from the Commonwealth in the amount of $160 million annually to support vital transportation services. Nonetheless, in constructing a budget for fiscal year 2011, the Authority was faced with a $73 million deficit. Because the Authority began the FY 2011 budget process with largely depleted reserves and declining revenues, the reserves and own source revenues were not sufficient to cover a projected deficit of this magnitude.

Since Forward Funding took effect on July 1, 2000, the Authority has experienced a cumulative underperformance of sales tax—its primary revenue source—and now faces an upcoming fiscal year in which the sales tax guaranteed revenue amount will provide no revenue increase for the second consecutive year. The Authority's other dedicated revenue source—local assessments—will also not increase. The Authority's own source revenues will actually decrease by $5.1 million (primarily driven by lower anticipated fare revenue and parking receipts) for a net overall decrease in revenue of $5.1 million.

With total revenues declining by $5.1 million, the Authority considered several options to achieve a balanced budget: operational efficiencies and personnel reductions, service efficiencies, service reductions, debt restructuring, and the depletion of the Capital Maintenance Fund. The Authority elected not to recommend service reductions because of the hardships they would impose on those who depend on the services provided by the MBTA. The Authority also rejected the use of further draws on the $15.4 million remaining in the Capital Maintenance Fund to balance the operating budget because it would compromise desperately needed funds for state of good repair projects. Though the Authority has a Stabilization Fund, which currently has a balance of $19.3 million, using it is not an option because the Authority is statutorily precluded from accessing these funds for budgeting purposes.

So to continue to provide essential transportation services to our customers and to meet our contractual and statutory obligations, the Authority offset the increase in operating costs by cost savings flowing from Transportation Reform efficiencies that will deliver the same level of service at a lower cost, and with a debt restructuring of $67.9 million. Going forward, the use of shared services within the MassDOT family should help relieve some pressure on rising MBTA operating costs.

In addition, and pursuant to Section 11 of Chapter 161A of Massachusetts General Laws and the reporting requirements contained therein, the Authority has established a target net operating investment per passenger mile ratio that it expects to achieve in FY 2011: 36.4 cents, in conjunction with the preparation of this operating budget request. This is a target and not legislatively mandated.[1] The legislation stipulates that beginning in FY 2006, the Authority shall seek to achieve and maintain a target ratio of not more than 20 cents for any fiscal year. This target is not achievable in FY 2011 given the decline in operating revenues and cost escalation in operating expenses.

## FY 2011 Revenue

Total revenue from all sources is projected to decrease by $5.1 million to a total of $1.622 billion. The major revenue categories follow:

### Operating Revenue

Total Operating Revenue is projected to decrease by $7.7 million (-1.5%) to a total $518.6 million in FY 2011. The decrease is due to declines in a number of the Authority's revenue streams from operations:

| | Increase/(Decrease) |
|---|---|
| • Fare Revenue | ($2.3 million) |
| • Advertising | ($1.6 million) |
| • Parking | ($6.3 million) |
| • Other Real Estate Operations[2] | $2.5 million |
| Net Decrease: | ($7.7 million) |

[1] See tab C for a history of the net operating investment per passenger mile ratio since the advent of forward funding.

[2] Includes income from Transit Reality Associates real estate operations on behalf of the Authority, South Station Bus Terminal, Commuter Rail Right-of-Way (B&M Access and Downeaster Service), North Station, Massport Airport Shuttle/Silver Line Boardings, and other real estate initiatives.

The Authority's projected fare revenue budget of $451.2 million represents a one half of one percent reduction over this year's budget. The sustained economic recession in Massachusetts has affected ridership and, therefore, fare revenue and parking income, the latter of which is budgeted at $6.3 million less in FY 2011. The Authority's proposed fare revenue budget achieves a fare recovery ratio of 37.1%—slightly lower than the FY 2010 fare recovery ratio of 38.4%.

Advertising revenue has also been problematic for the Authority. Not surprisingly, the prolonged economic downturn has had a direct effect on the market for advertising, and correspondingly, a situation arose in which Titan, the provider of advertising services for the majority of the Authority's stations and revenue vehicles, was unable to make their minimum annual guaranteed payment due the Authority, instead paying only the revenue share of net billings.

**Non-Operating Revenue**

The Authority's Non-operating Revenue is comprised of two major categories—miscellaneous income and revenue from dedicated sources. Non-operating Revenue will increase by $2.6 million to a total of $1.103 billion.

**Miscellaneous Income**

The Authority's increase in Non-operating Revenue all comes from miscellaneous income. The Authority anticipates an increase in other income of $2.3 million, which includes natural gas excise tax rebates and structured lease income. The Authority will use an additional $2.0 million in federal operating assistance grant funding, increasing the draw down from $10.0 million this year to $12.0 million in FY 2011. Property sales and interest income will decrease because of the economy and lower interest rates on the Authority's investments.

| | Increase/(Decrease) |
|---|---|
| • Other Income | $2.3 million |
| • Funds from Federal Government | $2.0 million |
| • Property Sales | ($0.2 million) |
| • Interest Income | ($1.5 million) |
| Net Increase: | $2.6 million |

The Authority's projected total own source revenue, i.e. all revenue except dedicated revenue, achieves a revenue recovery ratio of 44.7%—slightly under the FY 2010 revenue recovery ratio of 46.5%.

## Revenue from Dedicated Sources

Revenue from dedicated sources will not increase in FY 2011. Consistent with Forward Funding,[3] assessments (funds from local government) will not increase this year because of lack of inflation. This represents a revenue shortfall of $3.7 million. Revenue receipts from sales tax will also remain at the FY 2010 level of $767.0 million. The budget request includes the state contract assistance that was appropriated in FY 2010 in the amount of $160.0 million again this year.

## FY 2011 Operating Expenses

Operating expenses will increase by 3.0% in FY 2011. The need for $35.4 million in additional resources falls into two categories: (1) ongoing operations and quality of service and (2) contractual and statutory obligations. The Authority has generated significant cost reductions, which have helped minimize the overall operating expense increase.

### Ongoing Operations and Quality of Service

The Authority will require $11.4 million in additional funds in FY 2011 for the following, largely non-controllable, costs:

- $8.6 million for Purchased Commuter Rail Service which include $3.2 million in commuter rail contract capital maintenance work, $3.5 million for a commuter rail rolling stock extended life program, $1.4 million for MBCR incentive payments for on-time performance and improved equipment mean distance between failures, and $0.5 million for fixed price scope changes

- $1.3 million for services which include $0.7 million for the software maintenance agreement with Scheidt & Bachmann for automatic fare collection support, $0.3 million for software licensing support costs for the Office of Transportation Access (THE RIDE), and $0.3 million for a capital spares warehouse

- $1.5 million for power and utilities

### Contractual and Statutory Obligations

The Authority will require $33.5 million in additional funds in FY 2011 as a result of fringe benefits and payroll costs and existing contractual and statutory obligations as follows:

- $14.2 million for contract rate increases, fuel costs, and higher ridership for the Authority's paratransit service THE RIDE[4]

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[3] Legislation passed in 1999 changing the funding structure of the Authority, including the dedication of a percentage of the state-wide sales tax, excluding meals

[4] The cost of THE RIDE has grown from $21.4 million in FY 2000 to $85.9 million in the FY 2011 budget.

- $12.2 million for the Commuter Rail contractual fixed price contract increase with MBCR

- $4.5 million in pension costs which include an anticipated Authority contribution rate increase for the MBTA Retirement Fund

- $2.3 million for the 4% wage increase for four unions[5] which deferred the arbitrated 4% wage increase in FY 2010 and the fourth and final year of the Building and Construction Trades' contract which expires at the end of FY 2011

- $0.3 million for unemployment insurance

It is important to note the FY 2011 budget request contains no provisions for wage increases for any of the unions with contracts expiring June 30, 2010. These contracts cover the majority of unionized employees.

**Cost Reductions**

Offsetting the requested budget increases associated with ongoing operations and quality of service and contractual and statutory obligations are cost reductions largely attributable to Transportation Reform, which total $9.5 million:

- $6.6 million in wage savings from the elimination of 111 operating budget positions some of which derive from service efficiencies (e.g. single person train operations and station staffing) described below[6]

- $2.0 million for decreased healthcare expenses as a result of non-union employees and non-union retirees transferring to the Group Insurance Commission (GIC) and three unions whose contracts expire on June 30, 2010.[7]

- $0.4 million FICA

- $0.2 million in lower Commuter Rail train fuel costs

- $0.1 million in lower diesel and gasoline costs primarily used in Bus Operations

- $0.1 million for scheduled contractual subsidy decreases for the Authority's commuter boat services (Hingham, Hull/Quincy, and Inner Harbor)

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[5] Local 105 Technical Engineers, Local 453 Office and Professional Employees, Local 651 Blacksmiths, and Local 717 Electrical Workers

[6] The operating budgeted headcount declines from 5,866 positions in FY 2010 to 5,755 positions in FY 2011. The average per capita wage savings of $59,043.

[7] The healthcare savings are the result of the transferal of MBTA employees into the Group Insurance Commission (GIC). MBTA non-union employees and non-union retirees went into the GIC January 1, 2010. Unionized employees and unionized retirees will go into the GIC as their collective bargaining agreements expire.

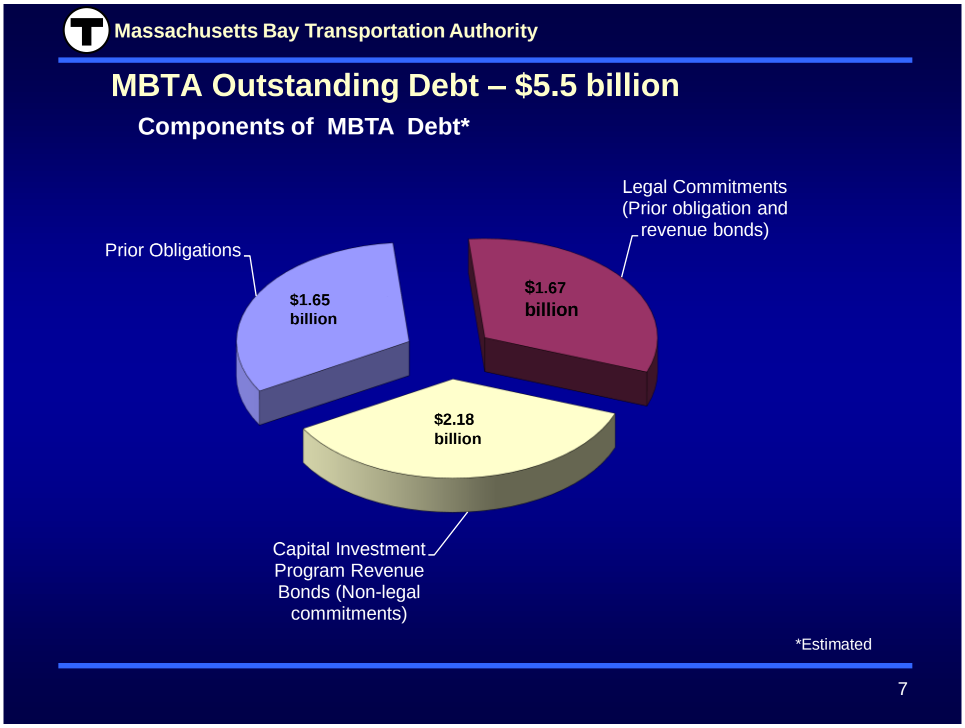
- $0.1 million for casualty and liability insurance premiums

Some of the cost reductions from the elimination of operating budget positions are the result of several operating efficiencies. Subway Operations plans to implement single-person train operation on the Orange Line, which will eliminate the door attendant position aboard Orange Line trains, leaving the motorperson with the duties of operating the train and doors and making announcements. Subway is also eliminating inspector positions on the Blue Line, leaving trains staffed by a single motorperson. In addition, Subway plans to reduce weekday Customer Service Agent coverage in subway stations by 20%. The reductions will be at low ridership stations or off-peak times of day, such as midday and evenings.

## FY 2011 Debt Service

### Interest and Principal Expenses

The FY 2011 budget continues to reflect increases in principal and interest payments as the bill on the Authority's $5.5 billion in outstanding debt comes due. This $5.5 billion in outstanding MBTA debt originates directly from three sources: "prior obligation debt" inherited by the MBTA at the onset of Forward Funding in 2000, projects required to be built and funded by MBTA as legal commitments associated with the Central Artery project permitting process, and the Authority's commitment to act as a good steward of the system and fund at least $470 million per year in capital investment necessary to maintain the current $2.7 billion dollar backlog in much needed State of Good Repair projects. The Authority's share of this capital investment continues to be drawn from bond funds due to the persistent lack of growth in sales tax revenues and the corresponding scarcity of available pay-as-you-go capital. The following chart summarizes the components comprising the MBTA's overall outstanding debt.



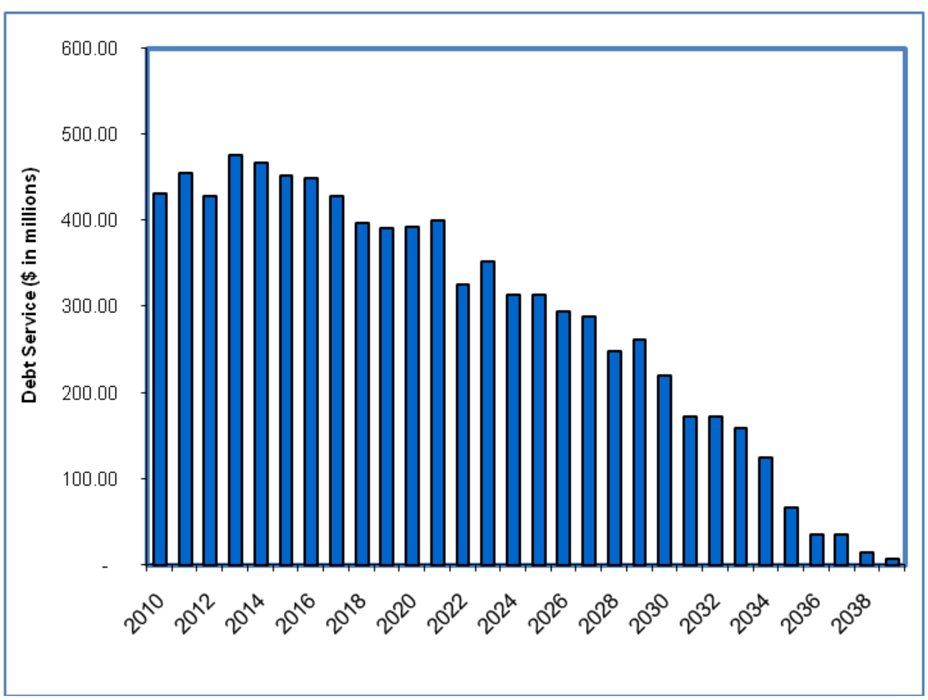

Currently, no dedicated funding source exists to pay for the Authority's portion of the Capital Investment Program. As a result, sales tax, assessment, and the Authority's own source revenues must cover both operating and capital expenses. The Authority's five-year Capital Investment Program is funded by five sources: revenue bonds, federal grants, state infrastructure funds, grant anticipation notes, and pay-as-you-go capital. In FY 2011, as in past years, the MBTA's non-federal portion of the capital program will be funded primarily by the issuance of new revenue bonds which will only further contribute to the unsustainable pattern of escalating principal and interest costs.

Since FY 2001, the MBTA has attempted to implement a "pay-as-you-go" capital funding structure, but that has been made impossible due to the limited growth in sales tax revenues. It is unlikely that the Authority will be able to increase "pay-as-you-go" funding in the future given the economic outlook for both the overall economy and sales tax revenue growth. The Authority is committed to a minimum investment of $470 million per year to the State of Good Repair program and to allocate at least 95% of the Capital Investment Program toward State of Good Repair investments in the core system even in light of the organization's financial condition. Failure to invest at least this amount would result in degradation of the core transit system and a deterioration of service. Such an outcome would likely result in lower ridership and other real economic costs given the importance of transit to the overall local economy.

The MBTA plans to implement a restructuring of debt service due in FY 2011 (principal payments only) of $67.9 million to address its significant operating deficit and achieve a balanced budget in FY 2011. This will necessarily involve the issuance of bonds, and delaying these principal payments will increase their cost over time to the MBTA.

Without a restructuring of debt service in FY 2011, the total debt service that would otherwise be due (excluding leases) is $454.9 million, which represents an increase of approximately $30.6 million over the FY 2010 debt service budget (excluding leases) of $424.3 million. Assuming a proposed debt restructuring of $67.9 million in principal payments, total principal and interest payments due in FY 2011 are projected at $387 million (excluding leases). Therefore, following the execution of the proposed restructuring, this will represent a decrease in FY 2011 of $37.3 million in total principal and interest costs budgeted (as compared to FY 2010). However, principal and interest costs will continue to consume almost 24% of the Authority's FY 2011 projected operating revenues, leaving fewer funds available to provide vital transit services. Furthermore, principal and interest will continue to increase and remain high over the next several years – see chart below which reflects only existing principal and interest without any new borrowing. Much of the current debt has been refinanced at a lower cost over the past ten years, but those savings opportunities no longer exist.

As there is no dedicated funding source for capital spending, continued reliance on bonds to finance the Authority's portion of the Capital Investment Program will only further exacerbate this situation, illustrated in the chart below, which shows significant and increasing debt service requirements even without the issuance of any new bonds for the continued funding of the Capital Investment Program. Therefore, as noted above, in order to address the backlog in deferred maintenance projects of $2.7 billion, the MBTA would need to issue more bonds than is planned in the Capital Investment Program – contributing more substantially to the Authority's debt burden and the burgeoning costs associated with maintaining even current levels of service.



The following table summarizes the FY 2011 principal payments and interest expense:

| Bond Issue | Principal Payment | Interest Expense |
|---|---|---|
| Prior Obligations | $32.6 million | $45.1 million |
| Revenue Bonds | 95.4 million | 201.9 million |
| New Revenue Bonds/CIP* Funding | | 3.2 million |
| Commercial Paper | | 5.7 million |
| Liquidity and Remarketing Fees | | 3.7 million |
| Derivative Income | | (0.7) million |
| **Total** | **$128.0 million** | **$259.0 million** |

* *Capital Investment Program*

**Lease Payments**

Lease payments for revenue and non-revenue vehicles will decrease by $3.2 million to $17.8 million. These payments provide funding for tax-exempt vehicle leases that support vehicle purchases for THE RIDE program, the MBTA's police department, system-wide maintenance, and service delivery.

**Debt Management**

The MBTA refunded over $2.0 billion in debt during FY 2005, FY 2006, FY 2007, and FY 2008 in order to achieve economic savings and reduce principal and interest costs. Debt management also includes defeasance of debt and hedge agreements in order to manage financing costs and volatility in an uncertain economic environment.

With the continuing slow growth in sales tax revenue, principal and interest costs are consuming an ever increasing amount of revenue each year. Unless corrected or mitigated, this will continue to compromise the Authority's ability to provide the anticipated service levels included in the FY 2011 budget and in future years. The Authority could decide to curtail the Capital Investment Program, with the aforementioned negative impact on the system's State of Good Repair. However, since the majority of the debt has been issued this would provide very little relief in the short term.

Last year, the MBTA Board of Directors created a Board Finance Committee. The board has been instrumental in evaluating and assessing capital spending needs. They have also set policy for prioritizing and maximizing capital projects that are eligible for federal funds thus reducing the amount of debt the Authority will have to issue, as well as focusing on projects critical to maintaining a safe transit system.

## SUMMARY

The FY 2011 budget request of $1.622 billion reflects a 0.3% decrease over FY 2010. The decrease is primarily related to a debt restructuring. This debt restructuring is required in order to preserve vital transportation services to our customers. It is difficult to predict what future budgets will look like without growing dedicated revenues and significant debt relief. The FY 2011 budget as proposed will maintain current service levels and will provide the Authority with time to develop a long term solution to the structural deficit.

## RECOMMENDATION

It is recommended that the Board of Directors approve the proposed FY 2011 annual operating budget and authorize the General Manager to submit the budget to the MBTA Advisory Board.

## ATTACHMENTS

| | |
|---|---|
| Tab A | Recommended Vote |
| Tab B | Statement of Revenue and Expenses |
| Tab C | Net Operating Investment per Passenger Mile: FY 2000—FY 2011 |

## COORDINATION

Wesley G. Wallace, Jr., Treasurer/Controller

**RECOMMEND APPROVAL**

Mary E. Runkel
Director of Budget

Date: March 3, 2010

**RECOMMEND APPROVAL**

Jonathan R. Davis
Deputy General Manager and
Chief Financial Officer

Date: ____________________

**RECOMMEND APPROVAL**

Gerald K. Kelley
Acting General Counsel

Date: March 5, 2010

**APPROVAL**

William A. Mitchell, Jr.
Acting General Manager and Acting
Rail & Transit Administrator
Date: March 5, 2010

# RECOMMENDED VOTE

That the Board of Directors approve the Authority's budget of current operating expenses and debt service costs for a one year period—July 1, 2010 through June 30, 2011—in the amount of $1,621,700,706 in the form submitted to this Meeting; and that the General Manager is hereby authorized and directed to submit the same, in the name and on behalf of the Authority, to the MBTA Advisory Board no later than April 15, 2010 in accordance with Section 20 of Chapter 161A of the Massachusetts General Laws.

# Massachusetts Bay Transportation Authority

## Statement of Revenue and Expenses

| REVENUE | FY09 Actuals | FY10 Budget | FY11 Budget Request |
|---|---|---|---|
| **Operating Revenues** | | | |
| Revenue from Transportation | 448,751,949 | 453,447,330 | 451,167,000 |
| Other Operating Revenue | 58,002,689 | 72,874,489 | 67,406,967 |
| **Total Operating Revenue** | **506,754,638** | **526,321,819** | **518,573,967** |
| **Non-Operating Revenues** | | | |
| Dedicated Local Assessments | 146,486,060 | 150,148,212 | 150,148,212 |
| Dedicated Sales Tax | 767,056,684 | 767,019,551 | 767,019,551 |
| Other Dedicated Revenue | 0 | 160,000,000 | 160,000,000 |
| Other Income | 26,167,562 | 23,261,170 | 25,958,976 |
| **Total Non-Operating** | **939,710,306** | **1,100,428,933** | **1,103,126,739** |
| **TOTAL REVENUES** | **1,446,464,944** | **1,626,750,752** | **1,621,700,706** |
| **EXPENSES** | | | |
| **Operating Expenses** | | | |
| Wages | 402,881,583 | 400,613,524 | 396,331,319 |
| Fringe Benefits | | | |
| Pensions | 47,724,676 | 53,960,414 | 58,507,137 |
| Healthcare | 109,528,356 | 115,676,142 | 113,734,455 |
| Group Life | 1,546,281 | 1,469,482 | 1,462,012 |
| Disability Insurance | 62,333 | 63,820 | 60,256 |
| Workers' Comp | 9,819,754 | 10,820,897 | 10,820,897 |
| Other Fringe Benefits | 212,009 | 290,414 | 290,414 |
| **Total Fringe Benefits** | **168,893,409** | **182,281,169** | **184,875,171** |
| Payroll Taxes | | | |
| FICA | 30,271,460 | 30,673,688 | 30,320,393 |
| Unemployment | 2,544,780 | 911,274 | 1,168,764 |
| Total Payroll Taxes | **32,816,240** | **31,584,962** | **31,489,157** |
| Materials, Supplies and Services | 172,911,308 | 183,805,352 | 187,368,831 |
| Casualty and Liability | 14,923,435 | 15,535,693 | 15,435,693 |
| Purchased Commuter Rail Service | 273,461,652 | 280,956,341 | 300,511,485 |
| Purchased Local Service Subsidy | 67,737,669 | 81,525,339 | 95,706,262 |
| Financial Service Charges | 4,368,625 | 5,157,569 | 5,157,569 |
| **Total Operating Expenses** | **1,137,993,921** | **1,181,459,949** | **1,216,875,486** |
| **Debt Service Expenses** | | | |
| Interest | 238,051,078 | 266,965,765 | 258,987,553 |
| Principal Payments | 84,634,312 | 157,325,038 | 128,019,218 |
| Lease Payments | 19,093,168 | 21,000,000 | 17,818,449 |
| **Total Debt Service Expenses** | **341,778,558** | **445,290,803** | **404,825,220** |
| **TOTAL EXPENSES** | **1,479,772,479** | **1,626,750,752** | **1,621,700,706** |
| **Net Revenue** | **(33,307,535)** | **0** | **0** |
| **Deficiency Fund** | **16,000,000** | **0** | **0** |
| **Capital Maintenance Fund** | **17,307,535** | **0** | **0** |
| **NET Revenue in Excess of Expenses** | **0** | **0** | **0** |
| Fare Recovery Ratio | 39.4% | 38.4% | 37.1% |
| Revenue Recovery Ratio | 46.8% | 46.5% | 44.7% |

# Net Operating Investment Per Passenger Mile

## FY00-FY11

| Fiscal Year | Net Investment | Passenger Miles | Investment Ratio |
|---|---|---|---|
| FY 00 | $430,379,097 | 1,677,781,807 | $0.257 |
| FY 01 | $393,749,587 | 1,818,140,290 | $0.217 |
| FY 02 | $436,452,216 | 1,823,179,910 | $0.239 |
| FY 03 | $469,202,961 | 1,874,755,722 | $0.250 |
| FY 04 | $476,062,438 | 1,862,072,081 | $0.256 |
| FY 05 | $507,888,031 | 1,738,697,937 | $0.292 |
| FY 06 | $526,313,048 | 1,767,605,772 | $0.298 |
| FY 07 | $520,007,218 | 1,734,986,303 | $0.300 |
| FY 08 | $537,680,974 | 1,843,528,441 | $0.292 |
| FY 09 | $613,271,036 | 1,880,345,528 | $0.326 |
| FY 10 Budget | $637,876,958 | 1,870,943,800 | $0.341 |
| FY 11 Request | $680,342,543 | 1,870,943,800 | $0.364 |

Note: Section 11 of Chapter 161A of Massachusetts General Laws stipulates that beginning in FY2006, the Authority should seek to achieve and maintain a target ratio of not more than 20 cents for any fiscal year. The legislation instructs the Authority to calculate the ratio using for the values of the variables the data reported each year to the Federal Transit Administration for the National Transit Database. As such, the data in the above chart differs slightly from the Authority's Statement of Revenue and Expenses.