

## **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 2014 (July 1, 2013 through June 30, 2014) and to direct the General Manager to submit the approved budget to the MBTA Advisory Board.

## **DISCUSSION**

At the March 13<sup>th</sup> Board meeting, the Authority presented a preliminary budget for fiscal year 2014 which contained a deficit of \$118.1 million. Down from an initial deficit of \$140 million, the preliminary budget represented yet another year in a series of recent MBTA budget deficits which have been increasingly impossible to fix without resorting to major fare increases, service cuts, and additional financial assistance from the Commonwealth.

For example, the FY 2013 budget formation began with a \$185 million deficit, which required one-time infusion of funds from the state as well as a fare increase and modest service reductions in order to have a balanced budget. The FY 2012 budget had a \$127 million gap which required a parking garage lease, parking revenue securitization, and a debt restructuring to close the gap. The Authority faced a \$73 million deficit in the FY 2011 budget and ultimately balanced the budget with a \$67.9 million debt restructuring. The FY 2010 budget required for the first time additional Commonwealth contract assistance of \$160, which has required recurring, annual appropriations.

After the Board vote on March 13<sup>th</sup>, the Authority met twice more with the Board Standing Committee on Finance and Audit and on March 28<sup>th</sup> presented a recommendation to balance the budget deficit of \$118.1 million with additional state assistance currently under consideration by the Massachusetts legislature in the Governor's *Way Forward: A 21<sup>st</sup>-Century Transportation Plan*. The budget proposal incorporates that recommendation to close the gap in order to have a statutorily required balanced budget.

The Authority also presented the Finance Committee with a plan in the event that there was no Way Forward funding by July 1<sup>st</sup>. The Authority laid out \$77.7 million in one-time contingency gap funding as follows: federal preventive maintenance funds (\$48.1 million), projected FY 2013 operating budget surplus (\$12.9 million), capital program elimination (\$9.5 million), deferring a contribution to OPEB (Other Post Employment Benefits) liability (\$5.0 million), and placing a freeze on administrative positions (\$2.2 million). The Authority's one time gap funding would have a detrimental impact to the Authority's capital program by diverting \$48.1 million in federal preventive maintenance funds to the operating budget and eliminating \$9.5 million of capital maintenance funding by using those funds on the operating budget. The use of the FY 2013 projected \$12.9 million operating budget surplus would necessitate more bond funding to support the capital program thus increasing an already overburdened debt structure.

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With an adjusted budget deficit of \$40.4 million after gap funding, the Authority would have no recourse than to plan for fare and or service changes after July 1<sup>st</sup> with a likely implementation around December 2013 or January 2014. While the Authority remains hopeful that it will not have to initiate gap funding and service and fare changes, it is planning for this contingency in the event that the FY 2014 budget cannot be balanced as proposed in the FY 2014 Statement of Revenue and Expenses (see Tab B).

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 2014: 43.2 cents, in conjunction with the preparation of this operating budget request. This is a target and not legislatively mandated. 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 2014 given the cost escalation in operating expenses.

### **FY 2014 Revenue**

Total revenue from all sources is projected to increase by \$100.3 million to a total of \$1.867 billion (see graphic of revenue sources in Tab D). The major revenue categories follow:

#### **Operating Revenue**

The Authority's Operating Revenues come from Revenue from Transportation (fare revenue) and Other Operating Revenue (advertising, parking, and income from real estate operations). Total Operating Revenue is projected to increase by \$35.2 million (6.1%) to a total \$614.6 million in FY 2014. The increase is due to the following:

	<u>Increase/(Decrease)</u>
• Fares	\$32.3 million
• Advertising	\$1.8 million
• Other Real Estate Operations	\$1.3 million
• Parking	( <u>\$0.2 million</u> )
Net Increase:	\$35.2 million

The Authority's proposed fare revenue budget of \$569.2 million achieves a fare recovery ratio of 40.0%—just slightly lower than the FY 2013 budgeted fare recovery ratio of 40.4%. The fare budget represents a 6.0% increase over FY 2013 and recognizes that because ridership did not fall off after the July 1, 2013 fare increase as predicted in the *Potential MBTA Fare Increase and Service Reductions in 2012: Impact Analysis*, fare revenue has exceeded budget through the first 8 months of FY 2013 by 5.8% or \$20.4 million. The FY 2014 fare budget is based on projected FY 2013 fare revenue of \$563.6 million with a 1% increase for ridership growth in FY 2014.

Advertising revenue is projected to increase by \$1.8 million (14.4%) due to the following: station and vehicle advertising (Titan and Clear Channel), on-line advertising, merchandise revenue, and digital billboard advertising.

The \$1.3 million increase in income from other real estate operations is due largely to the fact that the Authority no longer pays MassPort for Silver Line boardings—a savings of \$1.2 million with a corresponding loss in fare revenue. MassPort continues to offer free Silver Line service from Logan Airport.

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The total parking budget for FY 2014 is \$15.7 million. The decrease in parking income at MBTA lots is the result of some underutilization and the fact that the MBTA no longer receives income from the Anderson Regional Transportation Center.

### **Non-Operating Revenue**

The Authority's Non-operating Revenue currently comprises four major categories —dedicated local assessments, dedicated sales tax, contract assistance, and other income. The FY 2014 budget request adds a new category of Other State Assistance, which is the method by which the Authority is offering a balanced budget. In total Non-operating Revenue will increase by \$65.1 million (5.5%) to a total of \$1.252 billion.

#### **Dedicated Local Assessments**

The funds from local government in the MBTA district will increase by 0.8% (\$1.2 million) to a total of \$157.1 million. Assessments can increase by no more than 2.5%. The increase is based upon the Consumer Price Index, which in FY 2012 grew no more than 0.8%.

#### **Dedicated Sales Tax**

Revenue receipts from the state sales tax will increase by 1.6% (\$12.4 million) to a total of \$799.3 million. Actual sales tax receipts for CY 2012 were up 2.6% but because the guaranteed amount increases at the lower of inflation or actual sales tax receipts, the Authority received the inflationary increase.

#### **Contract Assistance**

The budget request assumes an appropriation of state contract assistance in the amount of \$160.0 million.

#### **Other State Assistance**

The amount of \$118.1 million reflects the minimum required from the Commonwealth in the MassDOT proposal for transportation funding, *The Way Forward: A 21<sup>st</sup>-Century Transportation Plan* to have a balanced budget. This assistance will avert the need to use costly, one-time gap funding in FY 2014 which would have a detrimental effect on the Authority's capital program as well as increasing the reliance on bond funding.

#### **Other Income**

The Authority's income line items are a combination of miscellaneous revenue sources, which include interest income, property sales, funds from federal government, utility reimbursements, and "other" which includes natural gas tax rebates. The Authority's budget request of \$17.5 million reflects a dramatic decrease of \$66.7 million from FY 2013 because the following items with an asterisk were one time infusion of funds to help balance the FY 2013 budget:

	<u>Increase/(Decrease)</u>
• MassDOT Motor Vehicle	
Inspection Trust Fund Transfer*	(\$51.0 million)
• MassDOT Snow and Ice Removal	
Surplus Transfer*	(\$5.0 million)
• THE RIDE Federal Reimbursements*	(\$5.0 million)
• Property Sales	(\$5.0 million)

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• Property Sales	(\$5.0 million)
• Other—Gas Rebates and Utility Reimbursements	(\$0.5 million)
Net Decrease:	(\$66.5 million)

The Authority's projected total own source revenue, i.e. all revenue except dedicated revenue including contract and other state assistance, achieves a revenue recovery ratio of 44.4%—lower than the budgeted FY 2013 revenue recovery ratio of 49.4%.

### **FY 2014 Operating Expenses**

Operating expenses will increase by 7.0% in FY 2014. The need for \$93.5 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 \$50.8 million in additional funds in FY 2014 for the following, largely non-controllable, costs:

- \$18.7 million for materials, services and supplies across all Authority operations for maintenance of an aging fleet and a more progressive preventive maintenance program
- \$16.7 million for Purchased Commuter Rail Service which includes the following: \$9.0 million for mobilization costs associated with a new operating agreement; \$4.6 million for train fuel; \$3.6 million for MBCR right-of-way capital maintenance; and \$2.0 million for other expenses. Offsetting these increases is a reduction in payments to CSX for \$2.5 million.
- \$8.2 million in wages to account for increased vehicle and infrastructure maintenance
- \$4.3 million for casualty and liability: \$4.0 million for injuries and damages, which is an add-back from last year's budget because tort reform didn't receive legislative approval, and \$0.3 million for risk insurance
- \$1.3 million for gasoline and diesel fuel in Bus Operations
- \$0.6 million for additional staffing in the Safety and Diversity departments to address federal oversight requirements
- \$0.6 million for utilities and power
- \$0.4 million for Authority financial service charges

#### **Contractual and Statutory Obligations**

The Authority will require \$56.7 million in additional funds in FY 2014 as a result of wage and payroll costs and existing contractual and statutory obligations as follows:

- \$33.6 million for the Commuter Rail contractual fixed price contract increase with MBCR (includes base contract, Greenbush, and scope changes for the CSX/Worcester right of way maintenance costs)

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- \$8.3 million for 2% pattern bargaining wage increases
- \$5.7 million for pension costs for employer contributions to the MBTA Retirement Fund and the MBTA Police Association Retirement Plan
- \$4.4 million for Water Transportation contracts, largely associated with the MBTA retention of fare revenue and its reclassification to fare revenue and not a direct offset to the Local Service Subsidy line item
- \$2.8 million for State Transportation Building rent, which had been excused in FY 2013 as part of the Authority's FY 2013 balanced budget solution
- \$1.3 million for FICA
- \$0.6 million for Private Carrier Bus

### **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 collectively total \$14.0 million:

- \$11.8 million for decreased healthcare expenses as a result of the remaining unionized employees and unionized retirees transferring to the Group Insurance Commission (GIC) by October 2013
- \$1.7 million in contract cleaning savings from the new contract
- \$0.4 million in THE RIDE due to lower projected ridership
- \$0.1 million for decreased group life insurance expenses as a result of the remaining unionized employees and unionized retirees transferring to the Group Insurance Commission (GIC)
- \$39 thousand in workers' compensation savings
- \$33 thousand for decreased disability insurance expenses as a result of the remaining unionized employees and unionized retirees transferring to the Group Insurance Commission (GIC)
- \$22 thousand for lower unemployment claims

### **FY 2014 Debt Service**

#### **Interest and Principal Expenses**

The FY 2014 budget continues to reflect increases in principal and interest payments as the bill on the Authority's \$5.45 billion in outstanding debt comes due. This \$5.45 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 transit legal commitments associated with the Central Artery project

inherited by the MBTA at the onset of Forward Funding in 2000, projects required to be built and funded by MBTA as transit 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 direct the majority of the Capital Investment Program to 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.

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 2014, 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.

Total debt service in FY 2014 is \$443.8 million, which represents an increase of approximately \$6.8 million over the FY 2013 debt service budget. No debt restructuring is included in the FY 2014 budget. Principal and interest will continue to remain high over the next several years. Much of the current debt has been refinanced at a lower cost over the past ten years, but those savings opportunities no longer exist.

### **Lease Payments**

Lease payments for revenue and non-revenue vehicles will decrease due to expiring leases by \$0.5 million to \$5.1 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.

## **RECOMMENDATION**

It is recommended that the Board of Directors approve the proposed FY 2014 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 2001—FY 2014
Tab D	Chart of FY 2014 Budget Revenues

Chart of FY 2014 Budget Total Expenses—Operating Expenses and Debt Service

## **RECOMMEND APPROVAL**

Mary E. Runkel, Director of Budget

Jonathan R. Davis, Deputy General Manager and Chief Financial Officer

Rachael Rollins, General Counsel

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Beverly A. Scott, Ph.D., General Manager and Rail & Transit Administrator

**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, 2013 through June 30, 2014—in the amount of \$1,866,555,455 in the form submitted at this Meeting; and

That the General Manager is hereby authorized and directed to submit the budget, in the name and on behalf of the Authority, to the MBTA Advisory Board no later than April 15, 2013 in accordance with Section 20 of Chapter 161A of the Massachusetts General Laws.