Finance & Administration Committee

Information Item IV-D

September 10, 2015

FY2017 Budget Guidance

Washington Metropolitan Area Transit Authority

Board Action/Information Summary

Action	Information	MEAD Number: 201656	Resolution: Yes	No

TITLE:

FY2017 Budget Guidance

PRESENTATION SUMMARY:

Staff will kick off the FY2017 budget development and approval process by presenting the Board with high-level information on the challenges and opportunities facing Metro's operating and capital budgets.

PURPOSE:

The Board will receive budget and strategic information from staff on the challenges and opportunities facing Metro in the development of the FY2017 operating and capital budgets.

DESCRIPTION:

Key Highlights:

- Metro's current FY2016 combined operating and capital budget is approximately $3.0 billion. That investment of passenger fares, local and state government funds, and federal funds produces over 340 million trips annually on Metrobus, Metrorail, and MetroAccess.
- The critical challenge facing Metro in FY2017 is to improve transit service in the Washington region by investing more in safety, service quality, customer service, funding of long-term liabilities, and increased capacity, while at the same time staying within jurisdictional budget constraints.
- Operating expense growth is currently greater than operating revenue growth, leading to substantial projected long-term increases in jurisdictional subsidy. Sustainable jurisdictional subsidy growth will require that expense growth be reduced from its current trend, including both personnel and non-personnel areas across the Authority.
- In the capital budget, competing needs for future funding as well as uncertainty regarding future federal funding must be addressed in the context of a renewal of the Capital Funding Agreement (CFA), which expires at the end of FY2016.

Background and History:

The annual budget process usually begins in October each year, with the goal of adoption in early spring (March or April) in order to begin the new fiscal year on July 1. However, given the various challenges currently facing Metro, and thus the need for additional time to consider options and strategies, the FY2017 budget process is kicking

off early.

A Board work session was held on July 30, 2015, to discuss the current status of Metro's *Momentum* strategic plan as well as to discuss capital programming and the need to renew the Capital Funding Agreement (CFA) that provides the legal and policy framework for the region's capital investment in Metro. This 'FY2017 Budget Guidance' item follows on that work session and highlights the challenges and opportunities facing Metro in both the operating and capital budgets. In particular, one goal is to identify current trends that may be unsustainable and to initiate discussion on the necessary actions -- by both staff and the Board -- to shift the budget towards a more sustainable path.

Discussion:

Metro's adopted FY2016 combined capital and operating budget is $3.0 billion -- $1.8 billion for operating and $1.2 billion for capital. These resources fund Metrobus ($960 million), Metrorail ($1.9 billion), and MetroAccess ($130 million), which together generate over 340 million trips annually across the Washington region.
Budgeted operating revenues (primarily passenger fares) account for $938 million of the $1.8 billion operating budget, for an operating cost recovery ratio of 52 percent.

Metro faces a number of challenges as it kicks off the development of the FY2017 budget. Most critically, in light of recent safety failures (including the L'Enfant smoke incident in January and the Blue/Orange/Silver derailment in August) as well as declining customer satisfaction (as evidenced in recent Key Performance Indicators), Metro must improve its transit services on a number of dimensions -- safety, service quality, and customer service -- while also funding long-term liabilities and investing for future capacity increases. Yet Metro must achieve these improvements while staying within jurisdictional budget constraints and reducing the growth of local operating subsidies.

In the operating budget, the lack of growth in Metrorail ridership raises significant challenges. The jurisdictions are essentially "leveraged," so that when fare revenue growth falls behind expense growth, subsidy increases rapidly. At the current 50 percent cost recovery, a year of six percent expense growth and one percent revenue growth leads to a ten percent increase in subsidy. Some jurisdictional representatives have made it clear that they cannot sustain such high levels of subsidy growth year over year given their own revenue growth and competing needs for investment in schools, public safety, and other priorities.

In addition to diverging overall trends in cost and revenue growth, Metro must also address sustained projected growth in MetroAccess usage (with its high per-trip cost), and must also address unfunded liabilities in both Other Post-Employment Benefits (OPEB) and pensions of $1.5 billion and $1 billion, respectively.

In the capital budget, the challenges are different, but no less real. In the short term (which may include amendments to the current FY2016 budget), Metro must fund the critical safety investments that are identified by the National Transportation Safety Board (NTSB) and the Federal Transit Administration (FTA) following the two recent safety incidents. The region must also reach agreement on a renewal of the six-

year Capital Funding Agreement (CFA), which will expire at the end of FY2016. The CFA provides the legal and policy framework for Metro's capital program and is necessary to ensure continued funding of major long-term investments.

Operating Trends

Beginning in the mid-1990s and extending through the late 2000s, Metro experienced sustained annual growth in Metrorail ridership and revenue. During that period, annual expense growth of approximately six percent was offset by overall operating revenue growth of approximately five percent. This, combined with relatively strong growth in local jurisdictional tax revenues, kept the subsidy contributions to WMATA at a sustainable level.

Since the recession, however, revenue growth and expense growth have diverged, leading to substantial increases in jurisdictional subsidy. Given current trends, this subsidy growth appears likely to continue if no changes are made, but some jurisdictional representatives have been clear that large year-over-year funding increases to Metro cannot be supported. Therefore, in order to keep subsidy growth at three percent if revenue growth is likely to stay in the one to three percent range annually, Metro staff and the Board must undertake significant actions to keep expense growth in the range of two to three percent annually.

These actions are likely to include major reductions in non-personnel expenses (such as services, materials and supplies, and miscellaneous expenses) as well as actions to reduce personnel costs. Personnel costs in the near term may be reduced through efficiency measures, while long-term costs will be affected more directly by staffing levels, benefits packages, and upcoming collective bargaining agreements. The Board workplan being initiated in conjunction with the outside consulting firm will also play a major role in these decisions.

The Board must also weigh potential fare changes as part of the FY2017 budget. Metro's revenue needs (and the ability to raise revenue through higher fares) must be weighed against the overall environment, including economic, political, and service quality factors. The Riders Advisory Council (RAC) is expected to propose certain measures to simplify fares, and staff will provide additional market-specific analyses (e.g., differential increases for bus vs. rail trips or long vs. short trips). Staff will also be looking at non-fare sources of revenue, such as advertising and retail concessions.

Capital Budget Outlook

As discussed at the July 30 work session, in addition to the procedural steps necessary to complete the renewal of the CFA, substantive decisions must be made regarding the competing needs for Metro's future capital funding. These needs include:

- Safety requirements from NTSB and FTA SMI
- Replacement of the 2000 and 3000 series railcars
- Expansion railcars and power upgrades
- Station access/capacity improvements
- Additional Buses for Priority Corridor Network
- Other Metro 2025 projects

At the same time, the region must also address the uncertainty over future levels of

federal funding. This includes short-term annual risks associated with the appropriation of formula and PRIIA funding as well as medium-term (i.e., within the six-year window of the CFA) risks associated with the reauthorization of the federal surface transportation legislation and grant programs as well as the expiration of the ten-year PRIIA authorization.

FUNDING IMPACT:

No immediate funding impact - information item only.	
Project Manager:	Thomas J. Webster
Project Department/Office:	CFO/OMBS

TIMELINE:

Previous Actions	July 2015 - Board work session on Momentum and Capital Programming
Anticipated actions after presentation	October 2015 - Discussion of ridership and fare policy November 2015 - Budget preview December 2015 - GM/CEO budget proposal and agreement in principle on CFA January-March 2016 - Board discussions and public hearings/outreach April 2016 - Budget adoption

RECOMMENDATION:

No Board action required - information item only.

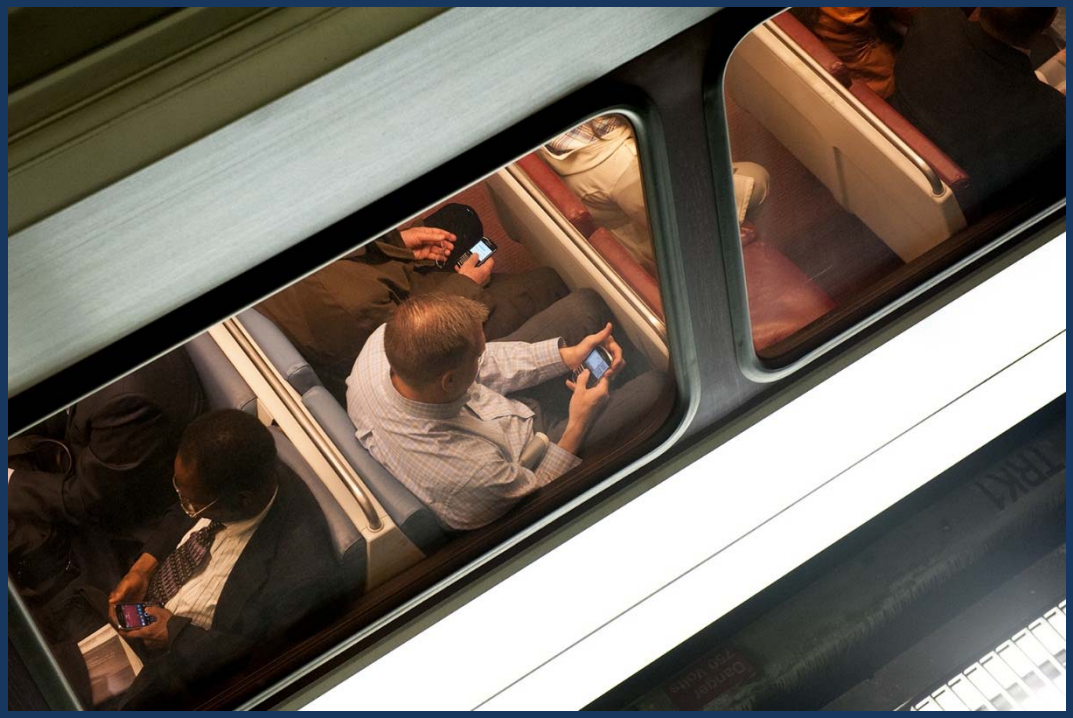
Washington Metropolitan Area Transit Authority

FY2017 Budget Guidance

Finance & Administration Committee
September 10, 2015

Purpose

Kick off FY2017 operating and capital budget development and review challenges and opportunities facing Metro



FY2016 Resource Overview

TOTAL BUDGET OF $3.0 BILLION

OPERATING $1,814 million

CAPITAL $1,165 million

Operating: $634 million

Capital: $327 million

Operating: $1.06 billion

Capital: $827 million

Operating: $121 million

Capital: $11 million

Revenue and Cost Recovery

Operating Revenue	$938
Operating Expenses	$1,814
Operating Cost Recovery	**52 %**

Operating Revenue	$938
Total Expenses	$2,979
Total Cost Recovery	**31 %**

figures in millions

Operating: 29 %

Total: 19 %

Operating: 71 %

Total: 40 %

Operating: 7 %

Total: 6 %

What Do Those Resources Support?

- 340 million trips/year on all modes
  - 17 percent of regional commute trips on transit – 3x national average
  - In core, figure rises to 43 percent
- 6 percent of new households and 14 percent of new jobs near Metro stations
- Over $200 million annually in additional tax revenue as a result of Metro
- Without Metro: worsened congestion, lower property values, more air pollution

KPIs Are Clear – Metro Must Improve

Metrobus

On-Time Performance

Fleet Reliability

Customer Satisfaction

Metrorail

On-Time Performance

Fleet Reliability

Customer Satisfaction

System-wide

Customer Injury Rate

Employee Injury Rate

Crimes

Escalator Availability

Elevator Availability

Color of bar reflects performance vs. target

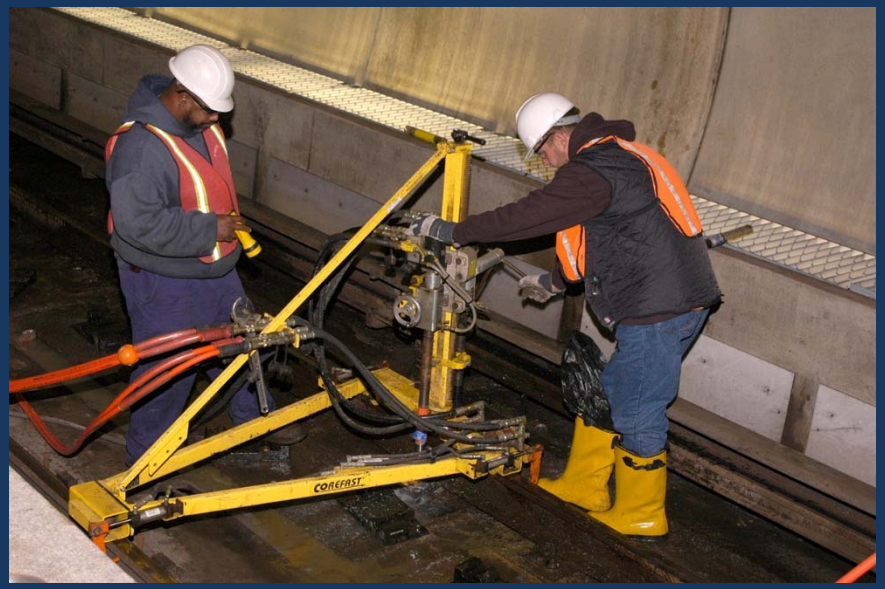
Qtr2 2015

Target

Critical Challenge Facing Metro

Must work within jurisdictional budget constraints while also investing in:

- Safety
- Service quality
- Customer service
- Long-term liabilities
- System capacity

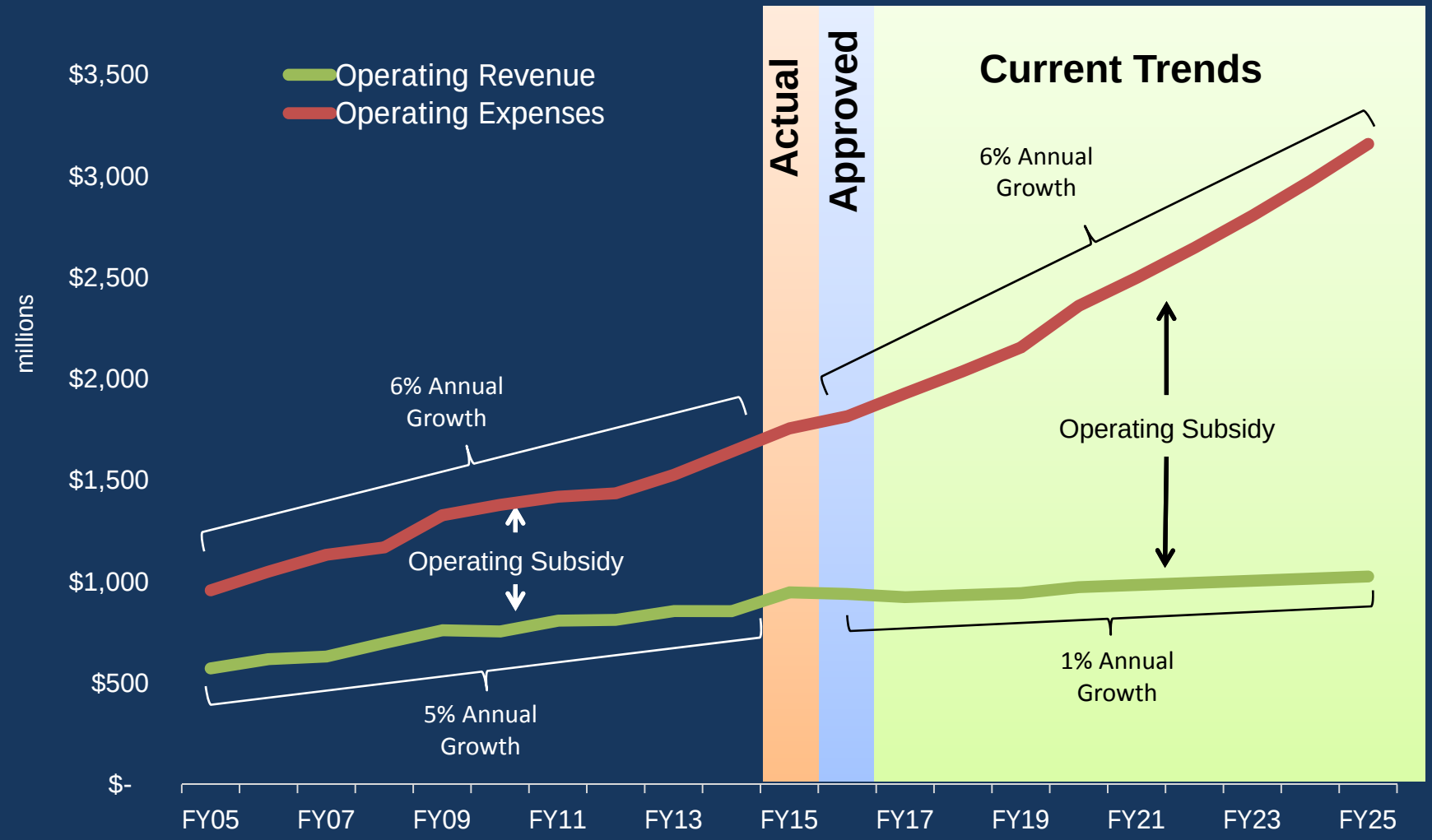


Operating Budget Challenges

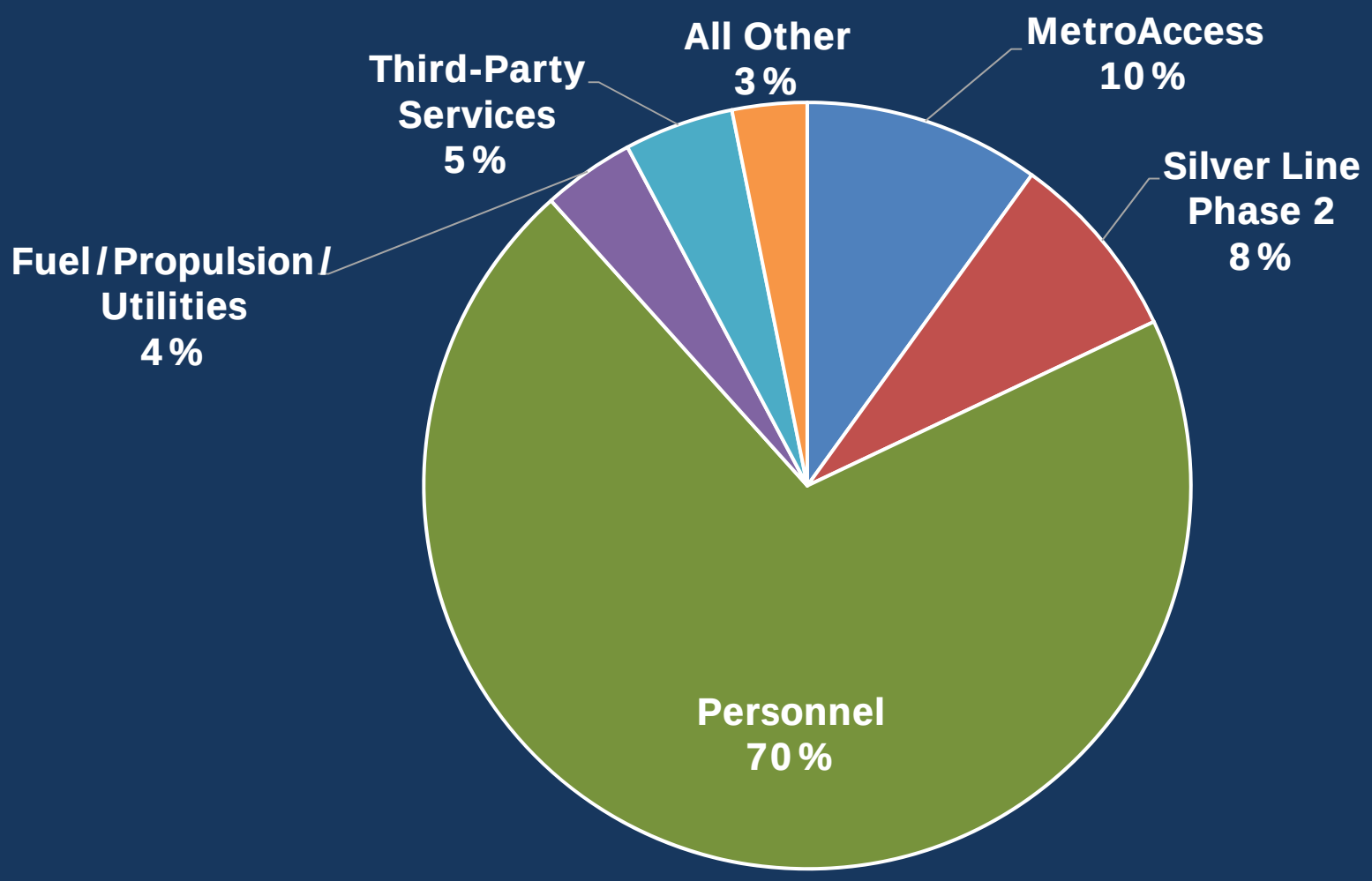
- Lack of revenue growth and leveraged jurisdictional subsidy:
  - At current cost recovery of approximately 50 percent:

    6% expense growth + 1% revenue growth = 10% subsidy increase
- MetroAccess demand continues to grow
- Unfunded liabilities of $1.5 billion for OPEB and $1.1 billion for pensions
- Upcoming Collective Bargaining negotiations

Ten-Year Outlook



What Is Driving Expense Growth?



Which Scenarios Are Realistic?

Average Annual Growth Rates: FY2017 to FY2025

	Current Trend	Scenario 1	Scenario 2	Scenario 3	Scenario 4	Scenario 5
Expenses	6%	2%	3%	4%	5%	6%
Revenues	1%	1%	3%	5%	7%	8%
Local Subsidy	10%	3%	3%	3%	3%	3%

Closing The Gap

- Improved operational efficiency
- Revenue growth
- Service changes

Operational Efficiency

- Personnel – headcount, outsourcing of certain functions, wage and benefit rates
- Non-personnel – services, materials & supplies, utilities
- Initial actions from Board workplan

Revenue Growth

- Current Board policy is to consider fare changes in FY2017:
  - Simplification
  - Market-specific analysis (bus vs. rail, long vs. short trips, etc.)
- Revenue needs must be considered in overall environment (economic, political, and service quality)
- Advertising, retail concessions, other sources

Service Changes

- Potential restructuring related to bus ‘recalibration’ analysis
- Potential targeted service adjustments to improve productivity

Capital Budget Challenges

- Identify and fund key safety requirements
- Achieve regional agreement on renewal of Capital Funding Agreement (CFA)
- Reach consensus on capital needs priority
  - Total inventory of needs exceeds $10 billion
- Address funding risks related to reauthorization of PRIIA and MAP-21

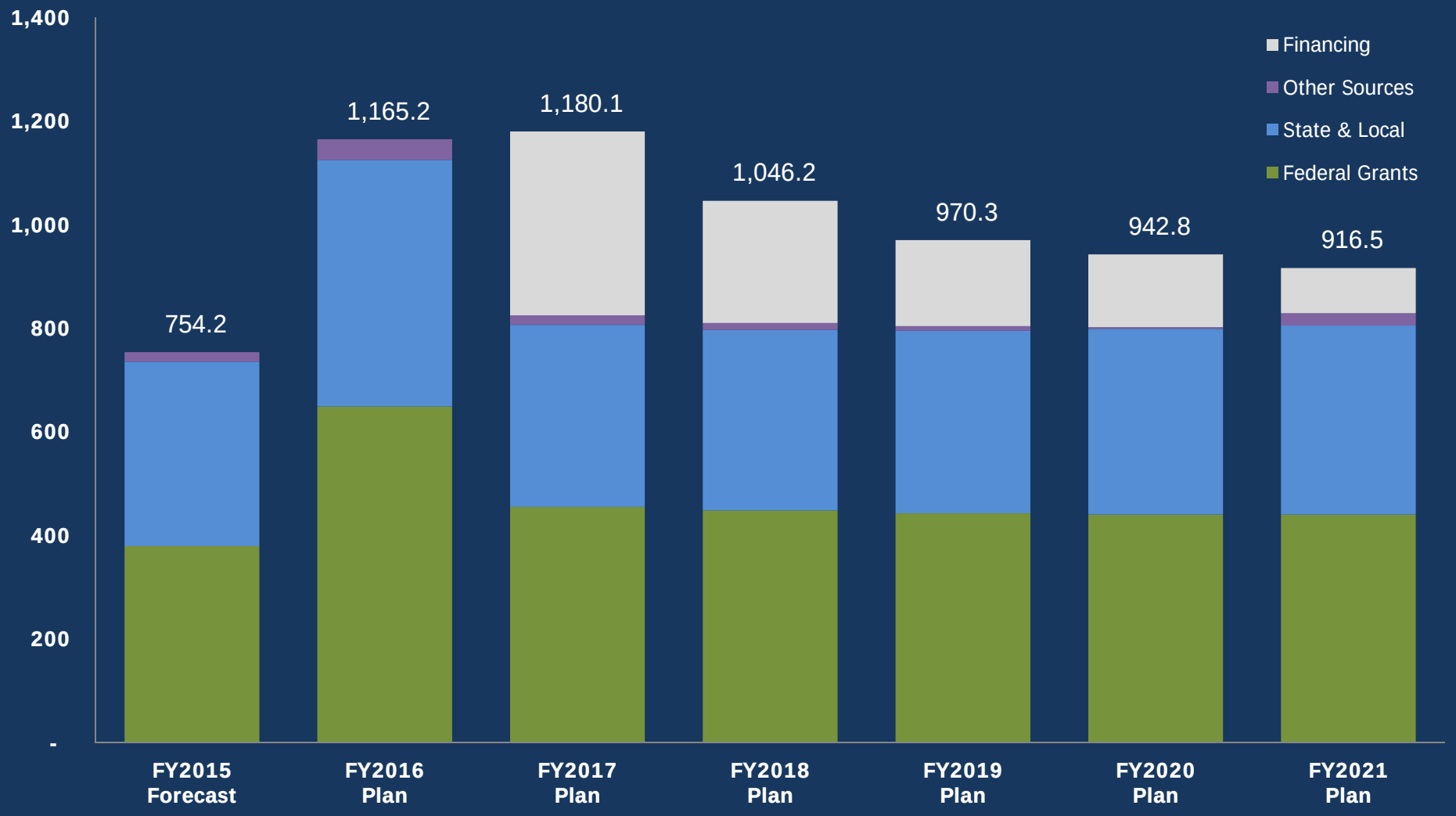
Capital Budget Outlook

- Safety and state-of-good-repair investment will continue to be primary focus:
  - Safety requirements from NTSB and FTA SMI
  - Delivery of 7000 series railcars
  - Bus and MetroAccess fleet replacement
  - Rail system rehabilitation (track and structures, elevators/escalators, yards, platforms, water mitigation, etc.)
  - Bus garage rehab and replacement
- Little programming flexibility for next six years unless new funding identified

Capital Budget Outlook (cont.)

- Competing needs for future funding:
  - Replacement of 2000 and 3000 series railcars
  - Expansion railcars and power upgrades
  - Station access/capacity improvements
  - Additional Buses for Priority Corridor Network
  - Other Metro 2025 projects
- Uncertainty of federal funding:
  - Annual appropriation of formula and PRIIA funding
  - Reauthorization of formula grant programs
  - Expiration of ten-year PRIIA authorization
- Expiration of Capital Funding Agreement

Planned Investment of $6.2 Billion Between FY2016 and FY2021



Next Steps

- **October**: Ridership and fare policy; recap of investment since FY2011
- **November**: Budget preview
- **December**: GM/CEO budget proposal; agreement in principle on CFA
- **January-March**: Board discussions and public hearings/outreach
- **April**: Budget adoption