



**Finance & Administration Committee**

**Information Item IV-A**

**October 13, 2016**

**FY2018 Operating Budget Prep Session**

Washington Metropolitan Area Transit Authority

## Board Action/Information Summary

☐ Action ☒ Information

MEAD Number:  
201795

Resolution:  
☐ Yes ☒ No

### TITLE:

FY2018 Operating Budget Prep Session

### PRESENTATION SUMMARY:

Metro must bridge a significant projected resource gap in order to achieve a balanced operating budget for FY2018. This presentation will set forward a number of key considerations -- including expense growth, fare policy, service reductions, and treatment of preventive maintenance -- for Board discussion and feedback ahead of the formal budget proposal in November.

### PURPOSE:

Staff will present information on preliminary projections for FY2018 operating expenses, revenues, and subsidy to the Committee in preparation for the General Manager/Chief Executive Officer's (GM/CEO) formal operating budget proposal in November. The FY2018 operating budget will support Metro's customer-focused goals of safety, service reliability, and financial accountability.

### DESCRIPTION:

#### Key Highlights:

- Daily ridership on bus and rail declined significantly in FY2016 in response to poor service quality and reliability, and the impacts of SafeTrack are likely to keep ridership at this lower level throughout FY2017 and into FY2018. Metro is also facing broader market challenges related to changing trip-making behavior, lower gasoline prices, and the emergence of transportation alternatives.
- Based on preliminary expense and revenue projections for FY2018, the current funding gap is approximately \$275 million.
- The GM/CEO has already acted in FY2017 to reduce expenses and thus reduce future year subsidy growth, and additional cost reductions and efficiencies are under consideration. However, these actions will not be sufficient to bridge the entire gap. A combination of fare increases, service reductions, subsidy increases, and preventive maintenance (PM) funding will be considered in order to close the remaining gap.

#### Background and History:

FY2018 will begin on July 1, 2017. The operating budget must be adopted in the spring in order to provide sufficient time to incorporate any Board-approved changes to fares,

service, or other major Authority operations, and the current schedule anticipates budget adoption in March 2017. In order to provide sufficient time for public participation and feedback, the budget will be proposed in November 2016. This budget prep session -- following on an earlier strategy session looking at Metro's performance metrics compared to various peers, as well as a workshop examining current trends in transit ridership and regional economic performance -- will present the key decision points for the FY2018 budget to the Committee for consideration and feedback.

## **Discussion:**

### **Budget Context**

After 15 years of consistent growth, total rail ridership peaked in 2009. It held relatively strong in the aftermath of the recession (2010-2012), and then declined in 2013-2015 due to combination of external factors (federal spending pullback, telework, alternative modes, transit benefit instability, lower gasoline prices) and internal factors (weekend trackwork, relatively high rail fares, service quality). Ridership then declined further in FY2016 as a result of poor service quality and high profile disruptions and safety incidents, as riders turned to increasingly available alternatives. Ridership so far in FY2017 is down even further, primarily as a result of closures and service interruptions due to the SafeTrack initiative.

The variability in bus ridership has been different. Bus declined more during and immediately after the recession but had fully recovered by FY2014, with strong ridership on the major Priority Corridor Network routes (especially mid-city and along Columbia Pike, etc.) and relatively weak ridership on lower frequency routes. Ridership was flat in FY2015 but then dropped in FY2016. Some of the decline appears to be a 'spillover' from the rail reliability challenges, as many riders use Metrobus to access rail. Declines in ridership on other local bus providers (e.g., Fairfax Connector, Montgomery County Ride-On, etc.) are also occurring, indicating broader, region-wide challenges.

Through the entire post-recession period, labor costs have continued to rise due to contractually-required wage increases and growing headcount to support service expansion on the Silver Line as well as maintenance on the aging system. As ridership has stagnated or declined, fare increases and subsidy growth have made up the gap between expenses and revenues. One-time sources have also been used to balance the budget -- Transit Infrastructure Investment Fund (TIIF) dollars in FY2016 and increased use of federal grant funds for preventive maintenance (PM) in FY2017.

FY2018 presents a fundamental challenge that cannot be solved through one-time actions. Achieving a balanced FY2018 operating budget will require a range of difficult actions, including additional efficiency savings, fare increases, service cuts, and increased jurisdictional contributions.

### **Management Actions**

Elimination of 500 positions is substantially underway in FY2017, with the total impact expected to be a \$25 million reduction to the operating budget in FY2018. Management has also implemented changes to healthcare benefits for non-represented (NRP) employees, including increased premiums and imposition of deductibles. The expected savings in FY2018 are approximately \$3 million.

Management is now pursuing other efficiencies and outsourcing opportunities to further reduce operating costs or optimize revenue. These actions may include further staffing reductions, privatization of parking (an RFP has already been released), and consolidation of duplicative services. Management will also put additional focus on reducing absenteeism and the costs associated with workers compensation claims. Total savings relative to baseline from management actions are expected to be \$40 million.

### **Pre-Funding of OPEB**

Other post-employment benefits (OPEB) include medical, pharmacy, and life insurance for retired employees. As of January 1, 2017, OPEB will be closed to all new employees except transit police (OPEB for new Local 689 employees was closed in 2010). WMATA funds all OPEB expenses on a pay-as-you-go (PAYGO) basis, with an actuarially estimated expense of \$60 million in FY2018. The most recent actuarial projection estimates WMATA's total unfunded OPEB liability at \$1.8 billion. If WMATA were to create a trust to pre-fund OPEB expenses (similar to the existing pension trusts), annual operating expenses would be higher in the near-term (i.e., PAYGO plus trust contribution), but total expenses would be reduced in the long-term as the trust earned returns to be used to pay future benefits.

The Board previously authorized creation of an OPEB Trust and included \$5 million to fund it in the FY2015 budget, but the Board did not establish the trust as planned. The Pensions Subcommittee has recently recommended that the proposed FY2018 budget include a pre-funding OPEB trust contribution; however, current estimates of the FY2018 funding gap do not include an OPEB trust contribution.

If the previous OPEB funding plan were implemented starting in FY2018, pre-funding contributions would begin at \$5 million and increase by \$5 million each subsequent year (\$10 million in FY2019, \$15 million in FY2020, etc.) up to \$40 million and remain at that level until the trust is sufficiently funded such that asset returns begin reducing required contributions. If an OPEB trust is not created, WMATA will continue to pay OPEB expenses on a PAYGO basis and report on the unfunded liability.

### **Pension Plan Funding**

As reported to the Pension Subcommittee this month, WMATA's five defined benefit pension plans have total accrued liabilities of \$4.6 billion and total plan assets of \$3.6 billion, resulting in a funded ratio of 78 percent and an unfunded liability of \$1.0 billion. The estimated WMATA contribution to these five pension plans in FY2018 is \$158 million. While the funded ratio can vary depending on certain assumptions (particularly investment returns and mortality rates), WMATA's plans are in the normal range for similarly-sized public agencies.

### **Fare Increases**

WMATA's last broad-based fare change was implemented in FY2015. It included an approximately 3 percent increase in rail fares, a base bus fare increase from \$1.60 to \$1.75 (with elimination of the cash surcharge), a \$0.10 parking fee increase, and a reduction in the MetroAccess max fare from \$7.00 to \$6.50.

The Board's current policy, as adopted in 2007, is to consider fare changes every other year and to benchmark increases against inflation. The goal is for fare increases to be modest and predictable. However, WMATA chose to forego any fare increases for

FY2017 due to service and ridership challenges.

Metrorail fares are generally perceived to be high relative to large-city peer agencies, particularly in the peak, though the restoration of the federal transit benefit to parity with the parking benefit helps mitigate that for some riders. A round-trip commute with parking from terminal stations like Vienna and Shady Grove to downtown can cost more than \$15 per day.

Bus fare at \$1.75, by contrast, is relatively low – most big-city transit peers charge \$2.00 or more for bus trip. However, many agencies have more generous bus-rail transfers than WMATA, so that mitigates the low price somewhat. If WMATA is going to continue accepting cash fare payment and allow on-board cash loading of SmarTrip cards, staff recommend that all further bus fare increases be in quarter increments (\$2.00, \$2.25, etc.) in order to reduce change-handling at the farebox.

One fare change proposal currently under consideration would generate approximately \$48 million (\$31 million rail, \$17 million bus), but scenarios with lower rail fare increases are also under consideration. The higher scenario maintains the current base fare, increases the peak per-mile charge by \$0.07 (for 3-6 miles) and \$0.10 (for miles 6+), and increases the peak max fare from \$5.90 to \$6.00. Bus fare would increase from \$1.75 to \$2.00, with a premium fare of \$2.25 for MetroExtra services. Total daily ridership loss is estimated at 24,000 trips total (1 percent reduction on rail and 4 percent reduction on bus). No changes to parking fees are currently under consideration, due to the active RFP regarding a potential parking concession, but parking fees could be re-evaluated following the completion of that process. The MetroAccess fare structure (twice the fastest comparable fixed-route trip) would remain the same, though the minimum fare would increase with the bus fare from \$3.50 to \$4.00.

The risk to ridership on bus appears relatively low, since \$2.00 still represents a good value proposition for most services. The risk to rail ridership is higher, as customer dissatisfaction with service reliability is substantial, and current estimates of price elasticity may not fully capture the potential customer reaction.

### **Service Reductions**

Rail service reductions would allow for a matching of service to current levels of demand or to realities of ongoing maintenance. Metro's current service standards call for maximum headways of six minutes during the peak at all stations except Arlington Cemetery. By providing six-minute service at terminal stations such as Vienna and Glenmont, riders at most closer-in stations see a train every three minutes (e.g., on the Orange/Silver Lines east of West Falls Church, or on the Red Line between Silver Spring and Grosvenor). Given current lower levels of demand, Metro could increase maximum headways from six to eight minutes, so that riders at the closer-in stations would instead have service every four minutes.

In the off-peak (particularly on weekends), Metro is not achieving scheduled service levels due to interruptions for maintenance requirements. Weekend schedules could be officially modified to account for this work and better align scheduled service and associated staffing levels to the service actually provided. Metro could also consider off-peak (midday, evening, weekend) closures of stations with low ridership.

Bus service reductions on bus could be achieved through three different but complementary approaches: (a) eliminating unproductive services (i.e., routes with low ridership); (b) eliminating or transferring services to the local operators which are inefficient for Metro to operate (i.e., significant deadhead time); (c) “thinning out” services that require a large number of buses in the peak and have the highest-cost operator shifts.

Staff is currently assessing options for a combination of service reductions that would result in \$25 million in subsidy savings (i.e., total cost savings less the expected ridership/revenue loss due to the change).

Although fare increases are unpopular, surveys generally indicate that service cuts are even more unpopular with riders. Proposed cuts to specific bus routes always will be met with public opposition, and proposed service reductions on rail are likely to be broadly unpopular, especially if service reliability in the peak does not improve and the reduction would lead to significantly worsened crowding.

### **Preventive Maintenance (PM)**

FTA guidance specifically allows transit agencies to utilize capital grant funds (e.g., Section 5307 Urbanized Area Formula Program) for certain eligible “preventive maintenance” (PM) expenses that would otherwise be funded through the operating budget. WMATA Board policy had limited PM to approximately \$31 million annually prior to FY2017. Staff generally has identified costs associated with bus and railcar vehicle maintenance as the eligible expenses to be funded with FTA grants. However, the total amount of vehicle maintenance expenses that could qualify for PM funding is in excess of \$100 million annually, and the total pool of eligible PM expenses – given WMATA’s extensive ongoing rail system maintenance efforts – is potentially hundreds of millions of dollars annually.

For FY2017, the Board increased the amount of eligible PM expenses that could be funded with FTA grants from \$31 million to \$95 million. The starting point for bridging the funding gap in FY2018 is a return to the previous PM funding amount of \$31 million.

The Board’s decision on the use of PM will not materially change the total amount of funding (operating plus capital) that the jurisdictions will need to invest in WMATA over the long term. If eligible PM expenses are funded with FTA grants, then additional local capital contributions (either debt or system performance) will be needed to replace those grant funds; conversely, if PM is zeroed out and all FTA grants are used only for capital projects, then additional operating subsidy will be required to support those necessary maintenance activities.

Maximizing the use of PM would have positive side-effects – it would simplify the management of WMATA’s FTA grant program, and it would reduce procurement constraints in the capital program for those projects now being funded by local funds rather than FTA grant funds. However, the House Appropriations Committee has warned WMATA in report language that accompanied the THUD bill that given Metro’s capital backlog and ongoing requirements, federal funding – both PRIIA and formula – should be used to address those capital needs.

### **Jurisdictional Subsidy**

Jurisdictional subsidy was held constant from FY2016 to FY2017 at \$845 million (not

including debt service), despite Metro's commitment to also not increase fares or cut service. With farebox recovery at approximately 50 percent, the jurisdictions are leveraged – if expenses were to go up 3 percent (for example) while revenues stayed flat, the subsidy increase would be approximately 6 percent. Achieving a sustainable subsidy growth requires both constraining expenses and maintaining consistent revenue growth through a combination of ridership growth and fare increases.

Given then current ridership challenges, a substantial subsidy increase will be nearly impossible to avoid unless a decision is made to substantially cut service. The GM/CEO proposal will attempt to balance the impacts among riders (through fare increases and service cuts), jurisdictions (through subsidy), and employees (through headcount reduction, reduced benefits, etc.), while also pursuing efficiencies that allow Metro to operate more cost effectively.

### **Labor Negotiations**

WMATA is in negotiations with its largest union (Local 689) on issues of wages, benefits, pensions, and work rules. The outcome of the negotiation is uncertain, but it is important to understand that while constraining labor cost growth is critical to long-term sustainability, a favorable outcome in this negotiation will not be sufficient to bridge the FY2018 funding gap. For example, if the outcome of the current negotiation regarding wages is similar to the previous negotiation, the expected expense growth in FY2018 could be up to \$30 million higher than if the new agreement reflects management's position.

### **Risks & Contingencies**

Historically, Metro's operating budget has not included any explicitly defined contingencies. If Metro faces unexpected expense increases or revenue decreases due to weather, emergency, or other unplanned changes to operations, any resulting year-end deficit that cannot be offset by other spending reductions must be covered by the jurisdictions.

However, Metro faces significant additional uncertainty in FY2018 related to the potential continued need for enhanced rail system maintenance activities after the completion of SafeTrack; the return of rail ridership following SafeTrack; and the need for funding for continued implementation of CARE Plan activities. If such contingency amounts are not included in the budget, then the initial required jurisdictional subsidy for FY2018 will be lower, but the risk of finishing the fiscal year with a deficit increases.

### **Reimbursable Projects**

WMATA undertakes certain projects and activities with funding from outside partners (often the funding jurisdictions, but sometimes other federal or regional public sector agencies, as well as private sector firms such as railroads and utilities) that are not included in the subsidized operating budget or the Capital Improvement Program (CIP). These are known as reimbursable projects.

Current operating reimbursable projects in FY2017 include the management of the DC Circulator bus contract on behalf of the District of Columbia; certain MTPD and security activities funded by Department of Homeland Security (DHS) grants; and Joint Development and Adjacent Construction (JDAC) activities, where WMATA reviews proposed third-party projects that are adjacent to WMATA property to ensure that our assets and operations are not negatively impacted. Current capital reimbursable

projects in FY2017 include Silver Line Phase 2 in conjunction with the Metropolitan Washington Airports Authority (MWAA) and the Purple Line light rail in conjunction with the Maryland Transit Administration (MTA).

As part of a comprehensive update to WMATA's budget policies, management proposes to merge all reimbursable projects and activities, regardless of funding source, into the operating budget or the CIP. This will improve management and oversight of these projects and ensure consistent reporting on all funds being provided to Metro and all activities being undertaken. This will have no impact on the net contributions from the jurisdictions, since the reimbursable projects are fully funded from independent sources.

#### **FUNDING IMPACT:**

Information item only - no funding impact.	
Project Manager:	Thomas J. Webster
Project Department/Office:	CFO/OMBS

#### **TIMELINE:**

<b>Previous Actions</b>	<p>July 2016 - Comparative Metrics</p> <p>September 2016 - Panel Discussion on Economic and Ridership Trends</p>
<b>Anticipated actions after presentation</b>	<p>November 2016 - GM/CEO Proposal of FY2018 Operating Budget</p> <p>December 2016 - GM/CEO Proposal of FY2018 Capital Budget and Six-Year Capital Improvement Program (CIP); Request for Budget Public Hearing</p> <p>January/February 2017 - Public hearing and outreach process</p> <p>March 2017 - Adoption of FY2018 Operating and Capital Budgets</p>

#### **RECOMMENDATION:**

No Board action required - information item only.





Washington Metropolitan Area Transit Authority

# FY2018 Operating Budget Prep Session

Finance Committee  
October 13, 2016



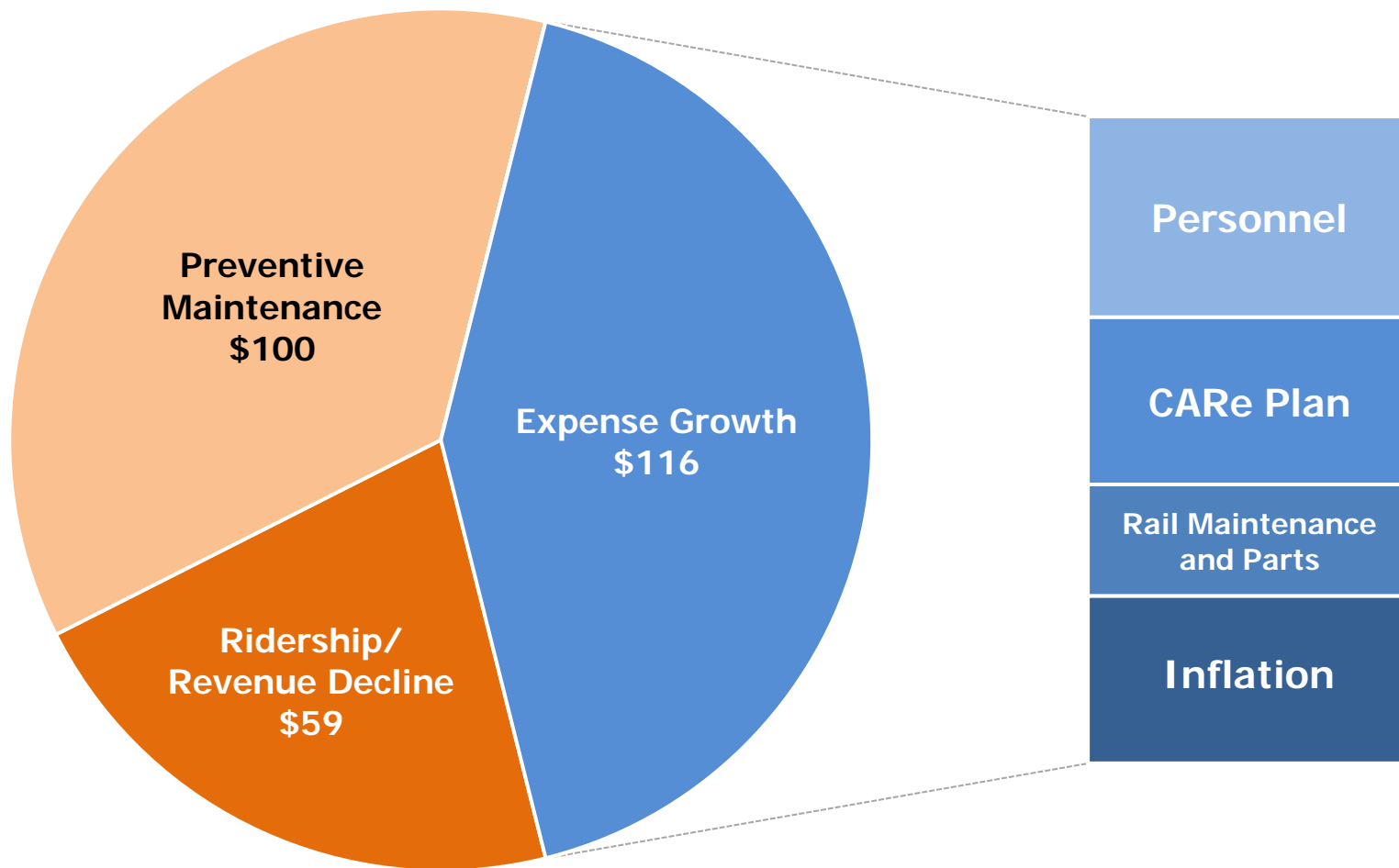
# FY2017 Operating Budget Recap

- No fare increase, no service cuts, flat subsidy
- Increased FTA grant funding for preventive maintenance to \$95 million
- Lower rail and bus ridership due to:
  - ✓ Service/reliability
  - ✓ Changing demand
  - ✓ Market competition

(millions)	FY2016	FY2017	Chg.
Revenues	\$938	\$900	-4%
Expenses	\$1,783	\$1,745	-2%
Subsidy	\$845	\$845	0%



# Estimated Budget Gap for FY2018: \$275 million





# Closing the Gap: Extreme Options

- **Management Reductions:** 2000-2500 positions in addition to 500 in process – 20-23% of all employees
- **Fares:** 35% increase on all modes including Access and parking with no ridership loss
- **Service:** 20-25% elimination of service on all modes plus associated personnel reductions
- **Use FTA Grants:** Utilize over 70% of formula grant funding (including match) for PM
- **Subsidy:** Additional \$100+ million each for DC and MD, \$70 million for VA



# Closing the Gap: Proportional Scenario

- **\$55 million from each option to generate \$275 million in total:**
  - ✓ **Management Reductions:** 300-400 positions in addition to 500 in process – 6-7% of all employees
  - ✓ **Fares:** 10% increase on all modes including Access and parking, loss of ~10 million trips
  - ✓ **Service:** 5-10% service reduction plus associated personnel reductions, loss of 15-30 million trips
  - ✓ **Use FTA Grants:** Utilize \$55 million of formula grant funding (including match) for PM
  - ✓ **Subsidy:** Additional \$20-21 million each for DC and MD, \$14 million for VA



# Management Actions

- Actions already underway, fully realized in FY2018:
  - ✓ Elimination of 500 positions (\$25 million)
  - ✓ Changes to non-rep healthcare (\$3 million)
- Additional actions under consideration (\$12 million):
  - ✓ Staffing reductions
  - ✓ Parking privatization
  - ✓ Absenteeism and workers comp
  - ✓ Work consolidations and efficiencies
  - ✓ Contracting out





# Increase Fares

- Bus fares low relative to peers – \$0.25 increase to \$2.00 (14%) would generate ~\$15 million
- \$0.04 to \$0.05 increase on per-mile charge for rail would raise ~\$20 million (increase of 5-10% for most trips)
- Access would increase with rail/bus
- No change to parking pending RFP outcome
- Increased fare enforcement





# Reduce Service

- Rail options (est. \$15 million):
  - ✓ Increase max peak headway from 6 to 8 minutes
  - ✓ Reduce scheduled off-peak service (already a reality on most weekends), close station entrances, etc.
- Bus options (est. \$10 million):
  - ✓ Inefficient service (far from garage, too much deadhead): transfer to locals or eliminate
  - ✓ Unproductive service (few riders): restructure or eliminate
  - ✓ High peak-to-base ratio: thin out, eliminate most expensive operator shifts







# Illustrative: Eliminate Bus Routes with Highest Subsidy per Rider

Bus Line Descriptions				Performance Criteria Ranking					Annual Data	
Line Name	Route(s)	Regional/ Non-Regional	State	Weekday Daily Riders	Cost Recovery	Subsidy/ Rider	Riders per Rev Trip	Riders per Rev Mile	Riders	Subsidy
Springfield Circulator	S80,91	Non-Reg	VA	420	1.4%	\$14.11	5.7	0.9	106,804	\$1,506,757
George Mason Univ-Tysons Corner	15M	Reg	VA	267	8.2%	\$13.10	8.9	0.8	67,356	\$882,146
Pimmit Hills-Falls Church	3T	Reg	VA	616	8.2%	\$13.04	8.9	1.0	166,018	\$2,165,018
Arlington-Union Station	13Y	Reg	VA	0	8.4%	\$12.72	8.4	1.1	6,726	\$85,582
Indian Head Express	W19	Non-Reg	MD	311	20.5%	\$12.34	11.4	0.5	78,933	\$974,110
Kings Park	17A,B,F,M	Non-Reg	VA	417	20.6%	\$12.27	9.0	0.5	105,423	\$1,293,904
South Capitol St Limited	W9	Reg	DC	161	10.3%	\$10.18	8.9	2.0	40,512	\$412,346
Greenbelt-BWI Airport Express	B30	Non-Reg	MD	370	40.3%	\$9.14	7.6	0.3	132,250	\$1,209,160
Springfield	18E,F	Non-Reg	VA	200	26.0%	\$9.09	11.1	0.8	50,460	\$458,767
Tysons Corner-Dunn Loring	2T	Reg	VA	505	11.8%	\$8.78	9.9	1.2	161,831	\$1,421,585
I-270 Express	J7,9	Non-Reg	MD	326	26.8%	\$8.73	9.9	0.6	82,080	\$716,616
Burke Centre	18P,R,S	Non-Reg	VA	676	27.1%	\$8.58	11.2	0.9	170,709	\$1,464,804
Greenbelt-Prince George's Plaza	R3	Non-Reg	MD	235	12.8%	\$7.98	9.4	1.1	59,268	\$473,106
Metroway - Potomac Yard	MW1	Non-Reg	VA	1,633	13.1%	\$7.74	6.4	2.0	453,382	\$3,507,693
Wisconsin Avenue Limited	37	Reg	DC	599	13.7%	\$7.37	27.2	4.1	150,900	\$1,112,008
Bock Road	W13,14	Reg	MD	658	32.0%	\$6.77	19.2	1.3	167,541	\$1,133,613
Oxon Hill-Fort Washington	P17,18,19	Reg	MD	1,167	32.3%	\$6.68	21.3	1.3	296,228	\$1,977,655
Fair Oaks-Fairfax Blvd	1C	Reg	VA	973	15.1%	\$6.57	18.5	1.3	320,729	\$2,107,075
Chain Bridge Road	15K,L	Reg	VA	486	15.2%	\$6.51	16.8	1.3	122,580	\$798,091
Fair Oaks-Jermantown Rd	2B	Reg	VA	916	15.3%	\$6.48	18.0	1.3	257,612	\$1,668,943



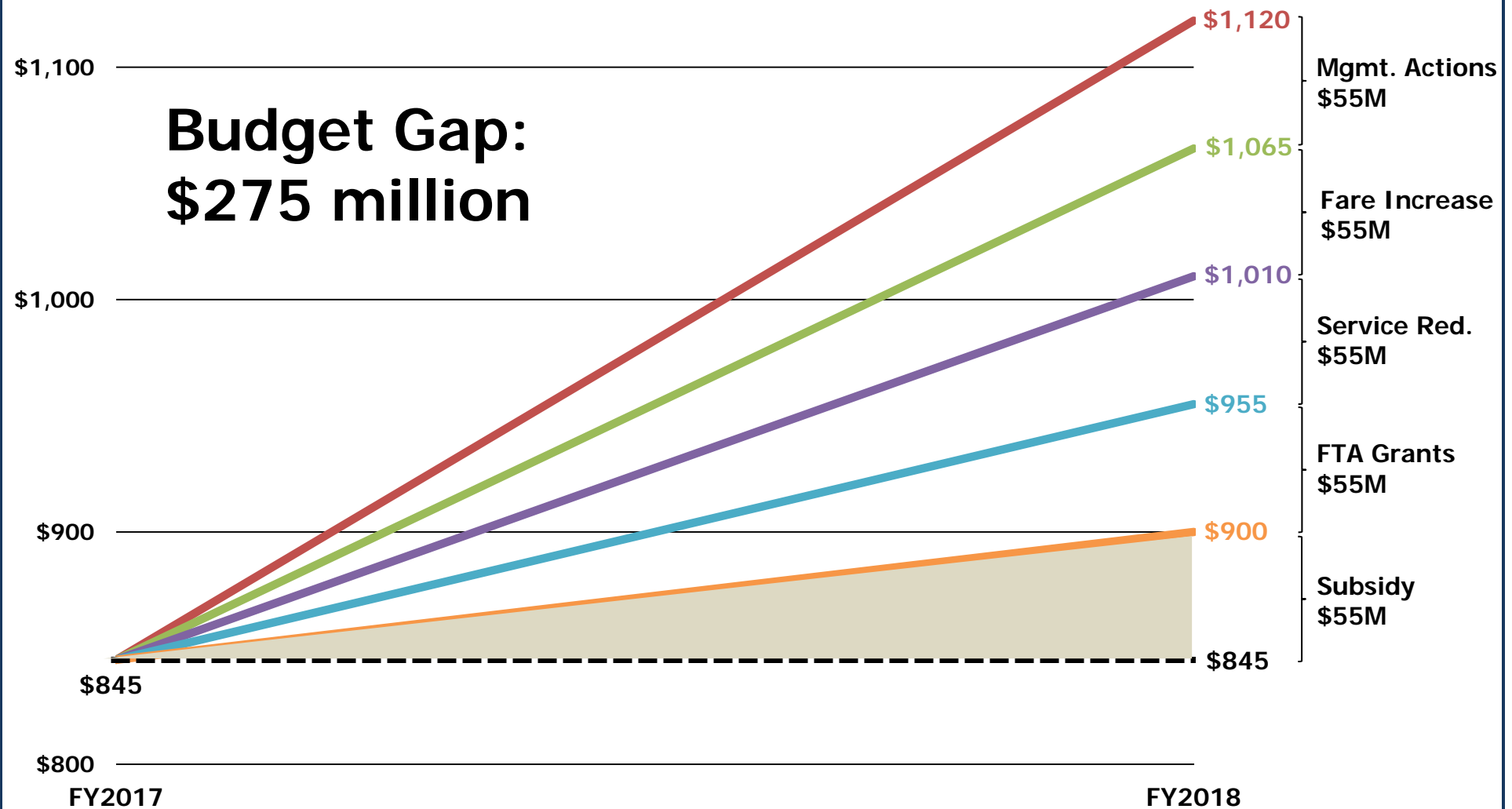
# Use FTA Grants

- Pre-FY2017 – Board limited use of FTA grants for eligible preventive maintenance (PM) expenses to \$31 million
- FY2017 – increased to \$95 million
- FY2018 – return to \$31 million of PM expense unless Board provides alternative guidance



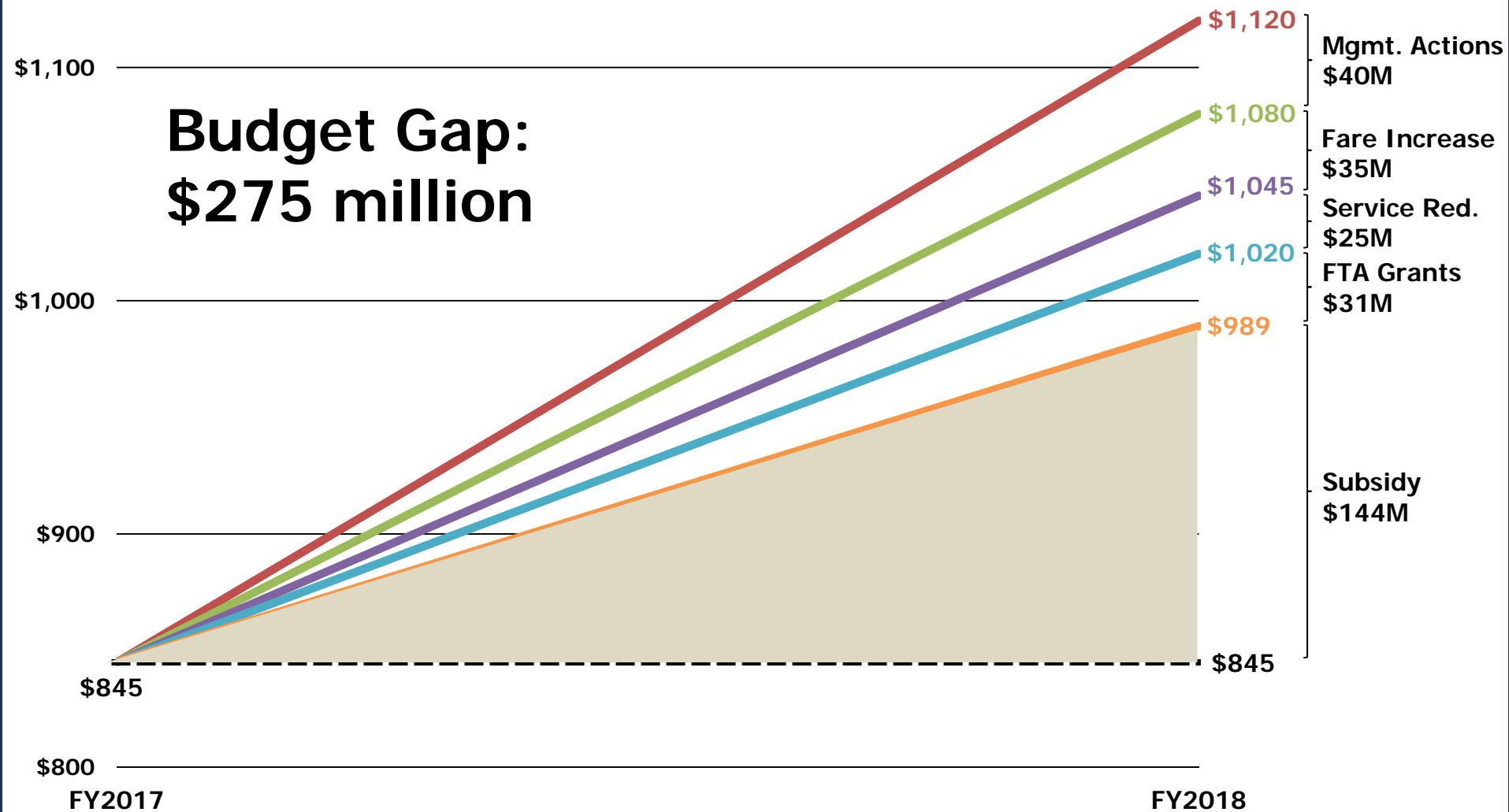


# Summary: Proportional Scenario





# Summary: Alternate Approach



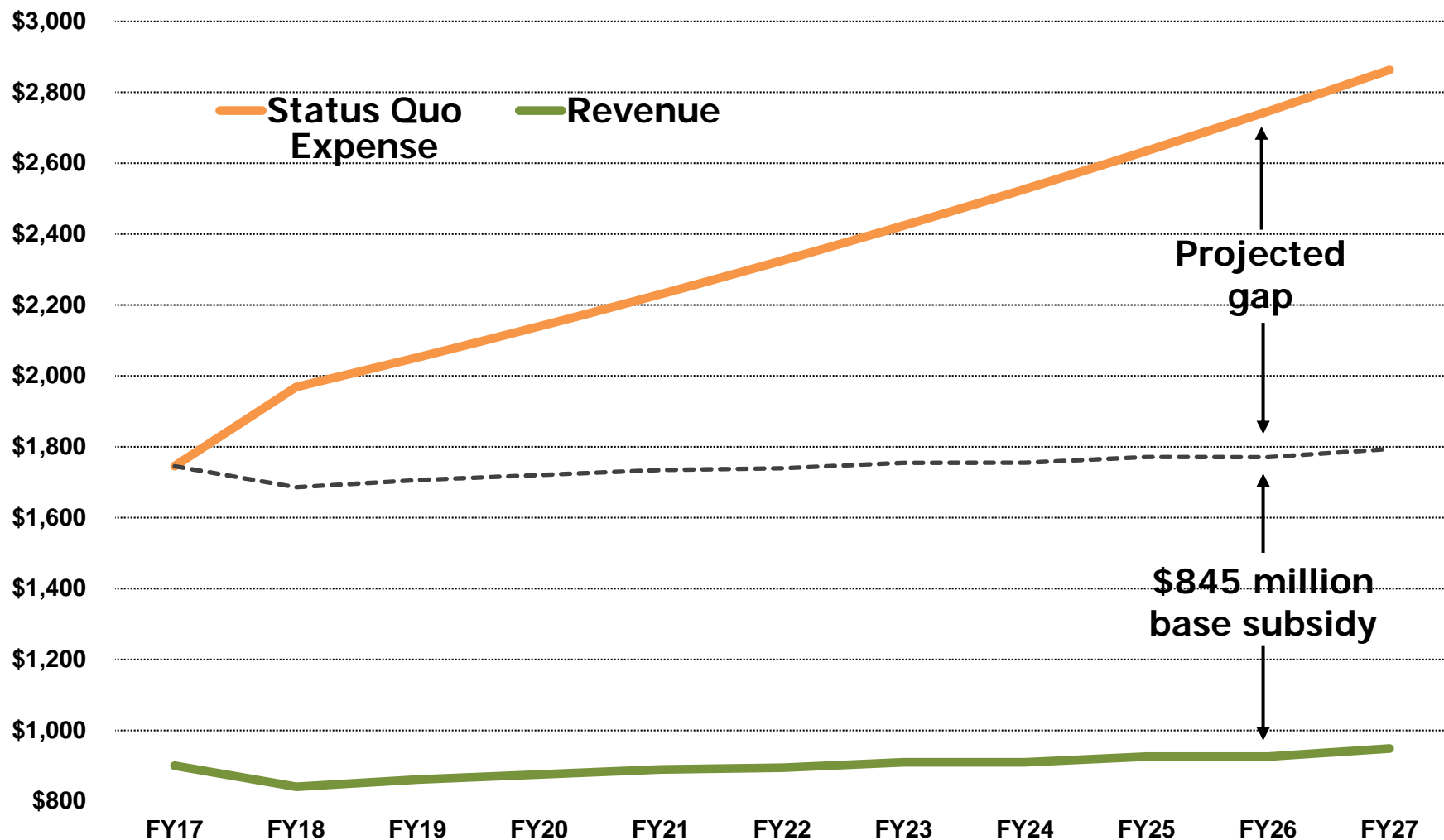


# Risks and Contingencies

- Ridership return following SafeTrack and service impacts from ongoing maintenance
- Safety directives
- Collective bargaining outcome
- Continued changes in rider behavior, trip-making and transportation market (telework, alternate modes, gas prices, etc.)
- Budget contingencies for additional track maintenance efforts and CArE Plan actions



# Ten-Year Operating Outlook

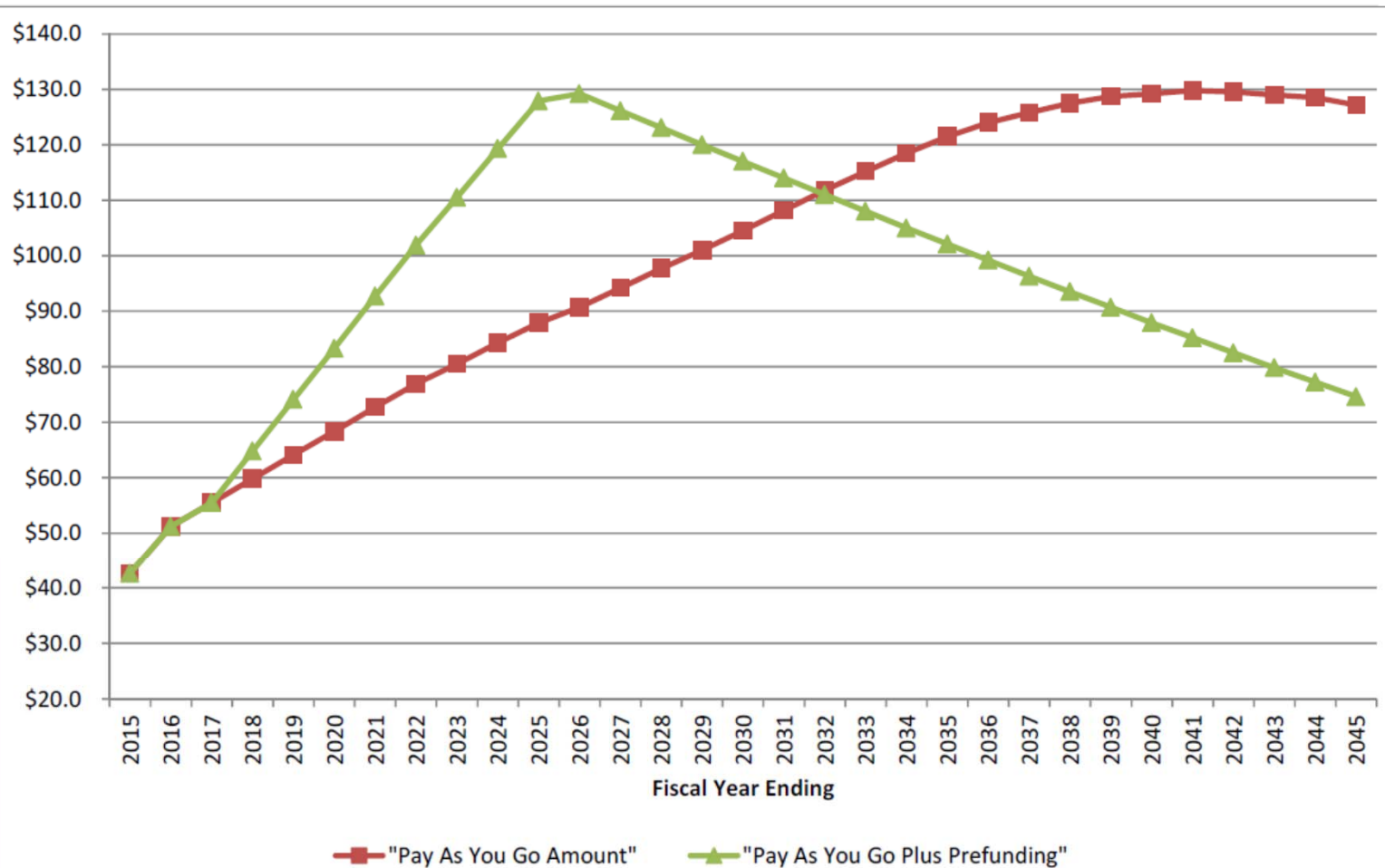




# OPEB Pre-Funding Strategy

## Funding Strategies

### Expected Annual Contributions With and Without Prefunding







## Next Steps

- **November:** GM/CEO Proposal of FY2018 Operating Budget
- **December:** GM/CEO Proposal of FY2018 Capital Budget and Six-Year CIP; Request for Budget Public Hearings
- **January/February:** Public Hearings and Outreach
- **March:** Adoption of FY2018 Budget