CITIZENS BUDGET COMMISSION

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How Will The MTA Fight Its Four-Alarm Fire?

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At the Metropolitan Transportation Authority's (MTA) June 24 Board meeting Chairman Patrick Foye aptly characterized the authority's fiscal condition as a four-alarm fire. The MTA faces huge gaps in funding for its operating and capital budgets. Recent estimates are that the operating budgets for 2020 and 2021 are short between $8.4 billion and $12.6 billion and the capital plan also will fall short of billions in revenue that supports its investments.[1] At the upcoming July 22 Board meeting the authority's leaders are expected to present an updated financial plan that should indicate how they will fight this potentially devastating fiscal fire.

Federal aid should be a significant contributor to solving this crisis. Yet, even if the MTA receives all the aid it has requested, its leaders face hard choices about how to manage the resources they control. Among five strategies three should have high priority, one be considered carefully, and one should be a last resort:

- The three high priority approaches are to pursue greater efficiencies to lower operating expenses, which in large part require working collaboratively with labor unions; to prioritize planned capital investments to lower debt service costs, including postponing expansions and possibly slowing accessibility improvements; and to optimize service levels by continually adjusting capacity to current demand and safety requirements.
- The option to be considered carefully is revision of fare and toll policies that seek more revenue from fares and to raise tolls proportionally more than fares.
- The last resort, to be minimized and used only when other options are exhausted, is to borrow for operating expenses in order to sustain vital services during the crisis period.

Why Are Things So Bad?

The current dire situation is primarily attributable to consequences of the COVID-19 pandemic that began early this year. However, before the pandemic the MTA's financial position was already weak. Its February 2020 four-year financial plan counted on continued economic growth, substantial savings from a likely optimistic, largely unspecified (and subsequently delayed) Transformation Plan, and additional optimistic assumptions about staffing levels, overtime control, and the pattern of collective bargaining settlements. Even under optimistic assumptions, the plan projected a deficit at the end of 2023.[2]

The pandemic and resulting economic shutdown have hurt the MTA in multiple ways. These impacts are concentrated in 2020 and 2021, but also will reduce economically sensitive revenues in 2022 and beyond. The fire alarms include:

1. Mass transit ridership has dropped precipitously with an accompanying decline— almost disappearance— of fare revenues. Revenue from tolls on bridges has fallen less dramatically but is still far short of pre-pandemic levels.[3]

2. Dedicated subsidies for operations from payroll, sales, and other taxes, which were counted on for more than 40 percent of the operating budget, are down from previously expected levels and are likely to continue to be weak well into 2021 and perhaps beyond.[4] The New York City Independent Budget Office projects cumulative shortfalls below MTA plan projections of $2.7 billion in 2020 to 2022.[5] In addition, some portion of these revenues could be diverted by the State to address its own major budget shortfall.

3. Newly authorized revenues initially intended to support debt service for the capital plan, including real estate transaction and sales taxes, are yielding less than was counted on to underwrite the planned investments; a congestion pricing system expected to yield $1 billion annually for debt service starting in 2021 has been delayed by federal inaction and the pandemic.[6]

4. Despite some curtailment of service, including stopping overnight subway service, operating expenses are rising due to added cleaning costs required during the pandemic for safety.[7]

Federal Aid: Welcome, Appropriate, and Needed, but Inadequate

A well-established national strategy for coping with economic recessions and regional disasters is federal aid and targeted support for heavily affected sectors. Multiple programs following this

pattern have been enacted by Congress in recent months including increased aid to states and funds earmarked for mass transit agencies. The MTA has received $3.8 billion in such federal aid.[8]

However, the federal funding to date is woefully insufficient to offset the pandemic impacts. An MTA-commissioned analysis by McKinsey & Company estimates that after taking into account the $3.8 billion in aid, the MTA's operating shortfall over the 2020 and 2021 period will be between $8.4 and $12.6 billion.[9] Using a midpoint of the range in the first year of this analysis the MTA has requested $3.9 billion in additional aid for 2020.[10] Congress has not yet acted on the additional request, but many political analysts predict some action to aid further transit agencies and other public entities in the coming months. Yet even if this prognostication proves correct, the new legislation is likely to leave the MTA with a continuing problem. The additional aid may be less than the requested $3.9 billion, and aid to deal with the 2021 shortfall is not even under discussion in Washington. Assuming $3.9 billion in new aid is authorized, the MTA will still face a 2020-2021 cumulative deficit of $4.5 billion to $8.7 billion in its operating budget. Additional shortfalls in revenue initially devoted to the capital plan worsen the problem.

Hard Choices: Finding the Right Mix of Five Options

MTA leaders have five options for addressing the unprecedented fiscal disaster. The best strategy for this firefight will be a combination of these actions that maximizes the benefits each can provide and minimizes adverse impacts.

Achieve greater efficiencies

The most desirable way to balance any agency's budget is to achieve greater efficiency in service delivery. This benefits the customers while reducing costs. This strategy should be the highest priority.

The February 2020 Plan included a Transformation Plan that seeks more than $500 million annually in savings largely from reorganization and administrative efficiencies and other measures to reduce spending by better managing staff levels and overtime. With the onset of the pandemic, implementation of the Transformation Plan was delayed and some expenditure controls could not be achieved. A new financial plan should restart the Transformation Plan and should include additional efficiencies from operational changes, most of which require changes in union agreements about work rules and compensation. Notable examples include changes to bus driver schedules to reduce overtime, one-person train operation, and lower fringe benefit costs.

In pursing greater efficiencies the MTA leadership should recognize that its workforce demonstrated praiseworthy commitment and heroism in serving essential workers and all New Yorkers during the pandemic. Their efforts have generated calls for federally funded bonus pay. This extraordinary performance warrants recognition, but it is not a justification for work rules that are inefficient and divert funding from better service. Workers and their union representatives should collaborate in revising work practices so that the MTA's financial survival, and their job security, is protected well into the future. The current collective bargaining agreement with the Transport Workers Union Local 100 has provision for joint labor-management committees to explore efficiencies in some departments; even better structured and targeted arrangements should be developed for mass transit operations and be extended to the commuter railroads. The new financial plan should set a substantial target for savings from negotiations with the major unions.

Prioritize planned capital projects

The MTA's current plans call for at least $64 billion in capital commitments in the next five years; this includes $54.8 billion in the 2020-2024 capital plan and $8.8 billion in work remaining from earlier plans in 2020 and 2021.[11] These plans are unrealistic and well-defined priorities should guide their revision to lower planned spending in the 2020-2024 period, and shift other projects to the future.

The ambitious plan simply will not happen because its previous record suggests the MTA is not capable of implementing projects at the anticipated pace; because the pandemic has already caused delays in work scheduled for 2020; and because the previously noted loss of revenue to support the new plan means it is no longer affordable. Priorities should be set to determine which of the many planned projects will actually be implemented in the coming years; lower priority projects should be postponed until after 2024.

Selecting the right priorities is important, and has two benefits. First, it will save money by reducing future debt service. Savings initially are modest because borrowing supports actual capital expenses not the full commitment amount for the initial contract award; nevertheless, savings are still meaningful. For example, the projected debt service for projects in the first five years of the new plan grows from $31 million to $466 million annually for a cumulative total of $742 million.[12]

Prioritizing also is desirable because it gives the capital plan greater transparency. The MTA should be honest about what it truly expects to accomplish rather than have the capital plan be a wish list that appears to please all constituencies but ultimately disappoints them.

The highest priorities should be for projects needed to achieve or maintain a state of good repair for existing assets; those that improve systems in need of updating, notably the signal and communications systems; and investments in plant and equipment that will reduce maintenance expenses such as replacing aged subway cars with frequent breakdowns with new equipment. Sustaining and improving current core services and their productivity is critical to the New York economy.

Desirable, but lower priority, projects are those that expand the system. The major expansion projects scheduled for coming years are the second phase of the Second Avenue Subway line from 96th Street to 125th Street and the Penn Station Access project which brings MetroNorth to Penn Station and adds four stations in the Bronx. The combined cost of these projects is about $7.9 billion with a majority of the Second Avenue Subway cost financed by federal grants.[13] Another desirable, but at least partly deferrable, set of projects are those proposed in accord with the MTA's recent policy to expand and accelerate the accessibility of subway and commuter rail stations. The cost of these multiple projects affecting at least 70 stations is about $6 billion.[14] This planned volume of work could be slowed and extended beyond the current five-year pan period to permit a balance with the need for other investments to promote a state of good repair and overcome previous neglect of needed repairs and replacement. Deferring the lower priority projects would enable the MTA to make its capital plan more realistic, transparent, affordable, and effective in making vital operations safe and reliable.

Optimize service levels

One of the most dramatic steps the MTA has already taken is to eliminate subway service between 1 a.m. and 5 a.m. This was not simply a response to the reduced ridership; it is intended to allow thorough cleaning of cars and stations and to prevent the trains from becoming a de facto overnight shelter for homeless individuals.

As the local economy seeks to reopen, mass transit will play a critical role in getting people back to their offices and other work locations. Successful reopening requires a complex balancing of lowering service capacity in line with lower ridership in order to keep operating costs reasonable and maintaining or even increasing capacity in order to build rider confidence that the system can avoid unsafe crowding and provide reliable and convenient service. In order to strike the right balance MTA leaders should constantly monitor and assess ridership on each rail, subway, and bus route to identify times and routes when and where service may need to be adjusted. Some routes may reasonably have service reduced in selected periods, while others may require added service in peak hours. The fiscal implications of this optimization cannot be known in

advance, but it is an opportunity to achieve savings as well as essential for providing quality service.

Reconsider fare and toll policies

For the past decade the MTA has followed a policy of regular (every two years) fare and toll increases averaging 4 percent. The current financial plan continues this policy with increases scheduled for 2021 and 2023. However, the crisis caused by the pandemic suggests careful consideration should be given to two significant deviations that could generate additional revenue.

First, larger increases for mass transit may be appropriate. On subways and buses fares in 2019 covered only about 36 percent of the cost per ride, and due to monthly and weekly Metrocards averaged well below the nominal $2.75 fare.[15] The CBC has long advocated increasing the share of cost coved by fares to 50 percent and movement in this direction could increase revenue. Moreover, the establishment in 2018 of a Fair Fares program granting half fare discounts for low-income New York City residents makes any added fare increase much less burdensome for this group.[16]

Larger fare increases on the commuter railroads also may be appropriate with the share of these trips' costs covered by fares lower than on mass transit for the Long Island Railroad (30 percent) and somewhat higher on MetroNorth (41 percent).[17] In the near term, fare hikes on these railroads may be counterproductive in the effort to raise ridership and have trains compete more effectively with autos for commuters, but in the longer run new fare policies can be pursued with less risk to ridership.

A second break with current policy to be considered is to unlink the size of fare increases from toll increases. Significantly larger percentage toll increases should be considered. The evidence from other global cities is that during reopening periods many former rail commuters shift to autos; significant toll increases could help reduce this shift and support the commuter lines with resources for their efforts to avoid crowding. In addition, the now indefinite delay of congestion pricing beyond January 2021 means the $1 billion annual revenue from the charges probably will not be available to the MTA in 2021 and perhaps longer. Consideration could be given to temporary large toll increases on MTA tunnels connecting directly to the central business district during the period of delay, since they could have the dual benefits of reducing auto traffic into the central business district and providing substitute revenue for the capital plan. For example, increasing the current in-bound toll on these facilities by $11 (the projected amount of the

congestion charge in some analyses) could yield about $250 million annually based on 2019 traffic, but likely would be somewhat less due to the impact of the higher toll on utilization.

Borrowing for operating expenses

To the extent federal aid and the other four options are insufficient to close the gap, the MTA will have to rely on borrowing for operating expenses if it is to sustain its vital services. This option should be viewed as a "last resort" and kept to a necessary minimum. Such borrowing is generally considered fiscally imprudent because it passes the cost of current services onto future generations and its repayment squeezes future budgets. Nonetheless, exceptions may be made in response to disastrous situations such as the current pandemic.

The amount of borrowing in public markets can be reduced by "borrowing" from the capital plan "lockbox," a set of revenues from real estate transactions, sales taxes, and congestion pricing intended to support debt service for the 2020-2024 capital plan. While lockbox revenues will be lower than initially planned, they likely will in the near term exceed the amounts needed for current debt service (especially if the capital plan is prioritized). These "surplus" lockbox revenues can be used for operations and repaid to the lockbox in future years when they may be needed.

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Footnotes

1. Metropolitan Transportation Authority, "McKinsey Analysis – Financial Impact Assessment on 2020 Revenue of COVID-19" (May 1, 2020), https://new.mta.info/document/16951.
2. Metropolitan Transportation Authority, *MTA 2020 Adopted Budget February Financial Plan 2020 – 2023* (February 2020) p. II-3.
3. Metropolitan Transportation Authority, "Day-By-Day Ridership Numbers" (updated July 6, 2020) https://new.mta.info/coronavirus/ridership and "Finance Committee Meeting Board Book" (June 2020) https://new.mta.info/document/17951
4. Metropolitan Transportation Authority, "Finance Committee Meeting Board Book" (June 2020) https://new.mta.info/document/17951 and *MTA 2020 Adopted Budget February Financial Plan 2020-2023* (February 2020), https://new.mta.info/document/15221.
5. Alan Treffeisen, "Trouble Ahead, Trouble Behind: The Impact of Declining Dedicated Tax Revenue on MTA Finances" (Independent Budget Office, July 2020). Estimates are for New York City fiscal years 2020 through 2022.
6. Metropolitan Transportation Authority, "Finance Committee Meeting Board Book," (June 2020) https://new.mta.info/document/17951 and *MTA 2020 Adopted Budget February Financial Plan 2020-2023* (February 2020), https://new.mta.info/document/15221.
7. COVID-19 related cleaning, testing, and private protective equipment (PPE) related expenses may cost $700 to $800 million annually in 2020 and 2021. See: Metropolitan Transportation Authority, "McKinsey Analysis – Financial Impact Assessment on 2020 Revenue of COVID-19" (May 1, 2020), https://new.mta.info/document/16951.
8. Metropolitan Transportation Authority, "McKinsey Analysis – Financial Impact Assessment on 2020 Revenue of COVID-19" (May 1, 2020), https://new.mta.info/document/16951.

9. Metropolitan Transportation Authority, "McKinsey Analysis – Financial Impact Assessment on 2020 Revenue of COVID-19" (May 1, 2020), https://new.mta.info/document/16951.
10. Metropolitan Transportation Authority, "MTA Issues Emergency Request for $3.9 Billion in Federal Aid as Congress Considers Next COVID-19 Relief Package" (press release, April 16, 2020) http://www.mta.info/press-release/mta-headquarters/mta-issues-emergency-request-39-billion-federal-aid-congress
11. Metropolitan Transportation Authority, *MTA Capital Program 2020 – 2024* (As proposed to CPRB October 1, 2019) and *MTA Planned Commitments for 2020 and 2021 from Prior Capital Plans* (January 2020), https://www.mta.info/sites/default/files/pdf/2020_planned_commitments_from_prior_mta_capital_plans.pdf.
12. Metropolitan Transportation Authority, *MTA 2020 Adopted Budget February Financial Plan 2020-2023* (February 2020), https://new.mta.info/document/15221.
13. Total cost for the Second Avenue Subway Phase 2 includes $1.7 billion in funding from prior capital programs for a total project cost of $6.3 billion. Penn Station Access includes $452 million from prior capital programs for a total project cost of $1.6 billion. See: Metropolitan Transportation Authority, *MTA Capital Program 2020-2024* (September 25, 2019), https://new.mta.info/document/10511.
14. Metropolitan Transportation Authority, *MTA Capital Program 2020-2024* (September 25, 2019), https://new.mta.info/document/10511.
15. Metropolitan Transportation Authority, "Farebox Recovery and Farebox Operating Ratios: 2019 Adopted Budget Final Estimate" (December, 2019) https://new.mta.info/document/13731.
16. Enrollment in the Fair Fares program has been lower than initially expected and has been slowed further by the pandemic and the associated reduced mass transit ridership. The lower enrollment led to a reduction in the program budget in New York City's fiscal year 2021 budget. However, eligibility has not been curtailed and future enrollment and benefits for low-income city residents are not adversely affected.
17. Metropolitan Transportation Authority, "Farebox Recovery and Farebox Operating Ratios: 2019 Adopted Budget Final Estimate," (December, 2019) https://new.mta.info/document/13731