CITIZENS BUDGET COMMISSION

BLOG | TRANSPORTATION

Light, at the Beginning of the Tunnel

What to Look for in the MTA 2021 July Financial Plan

July 20, 2021

This week the Metropolitan Transportation Authority (MTA) will release an update to its financial plan. Despite several rounds of federal aid received in 2020, the February 2021 Financial Plan forecasted a cumulative cash shortfall of $8.0 billion through 2024 and included a permanent wage freeze starting in 2022 and steep service cuts starting in 2023.[1]

Subsequent to the February Financial Plan, the MTA's short and mid-term prospects brightened with the passage of the federal American Rescue Plan (ARP) that will deliver $6.5 billion of additional aid, higher dedicated tax receipts and ridership, and lower expenses than projected. In response to the federal aid, the MTA reversed the service reductions and cancelled the wage freeze. It also began to accelerate its capital investment, notably restarting Metro North Penn Station Access and increasing the commitment target for 2021 to more than $7 billion.[2]

These post-February resources and announced actions should result in sufficient cash resources to balance the budget approximately through 2024 by rolling forward federal funds to cover cash shortfalls. However, once the federal funds run out the underlying structural budget shortfall will be exposed. The MTA's July Financial Plan Update will add 2025 to the planning horizon and show the long-term structural deficit, which may well approach $2.5 billion annually.[3]

To address this shortfall, the MTA should improve the efficiency of its operations as CBC's recent "Track to Fiscal Stability" demonstrated. While the path to achieving operating savings is hard, it is much preferable to phase in these savings over the next few years than to have massive fare and toll increases, economically damaging service cuts, or significant increases in dedicated taxes and subsidies.

To better understand the MTA's fiscal outlook, the following elements should be examined when the MTA releases its update this week.

Revenues

- **Higher than Expected Ridership, Tolls, Dedicated Taxes, and Fare Revenue –** In November 2020, the MTA reduced its ridership and fare revenue projection based on the "worst case" McKinsey forecast scenario. However, revenues have outperformed these assumptions; compared to these projections, actual fare revenues are 82 percent, $443 million, higher than planned through May 2021.[4] Likewise, 2021 revenues have come in higher than planned for both tolls ($323 million or 71 percent) and dedicated taxes and subsidies ($383 million or 17 percent).[5] While ridership, economically sensitive dedicated taxes, and especially toll revenue are likely to continue to be higher than the "worst-case scenario," the outlook does face risks, especially for commuter rail.[6] The MTA may alter its farebox, toll, and dedicated tax revenue projections based on the latest experience. Forecast updates should focus on known near-term favorable developments caused by the faster-than-anticipated end of the state of emergency; exercising caution in the out-year forecasts in 2024 and beyond remains appropriate.

- **Fare and Toll Increases –** The February Plan included planned fare and toll increases yielding 4 percent in September and April 2021, respectively. The agency set the final toll increase to yield 6 percent, and the revenue estimate should be updated accordingly. The September transit fare increase has yet to be finalized.

  Decoupling fare and toll increases during the pandemic was appropriate since tolled vehicle traffic has returned to normal, but transit ridership has not. Nonetheless, the MTA should continue its policy of regular biannual increases to help adequately and appropriately fund its operations. Likewise, the City should continue to implement and ensure full uptake of Fair Fares as a key companion policy to assist low-income riders.

- **Elimination of the Local Match for FEMA Reimbursement –** The MTA's February Plan budgeted $220 million in FEMA reimbursement in 2021 for 2020 costs. The typical FEMA 25 percent local match requirement was waived by executive order on February 2, 2021. Eliminating the local match in its Financial Plan Update should increase the FEMA funds for 2020 expenses by $80 million. Furthermore, FEMA reimbursement is likely to be available for eligible expenditures incurred from January 20th, 2021, to September 30, 2021.[7] This additional reimbursement may total $300 million assuming 2021 expenses are similar to those in 2020.

- **Congestion Pricing –** MTA delayed the congestion pricing launch to 2023, citing federal delays on the required environmental review. Recent federal approval of an expedited environmental assessment eliminated the roadblock originally cited, but the MTA has not provided an updated timeline. Congestion pricing remains urgently needed and the MTA should expedite its implementation.

Expenditures

- **Favorable Current Operating Expenses –** Operating expenses in 2020 and through May 2021 have been approximately 2 percent below the February plan.[8] If the MTA expects this trend to continue, it should be reflected in an updated forecast.

  Savings from temporary commuter rail schedule reductions have contributed to the favorable operating expense variance. Metro-North Railroad (MNR) has been running about 63 percent of normal service, with plans to resume 83 percent after Labor Day. On February 1, 2021, the Long Island Railroad (LIRR) initially reduced service to close to 75 percent of normal, but delivered 81 percent of normal service after public protests.[9] Temporary service reductions yield only modest savings because most rail operating costs are fixed in the short run. Still, some service "right-sizing" tailored to the new patterns of peak and off-peak commuting would remain appropriate.

- **Unidentified Transformation Plan Savings –** The MTA must sustain and advance the progress in administrative and back-office streamlining. From the beginning, it was not clear that the MTA would be able to achieve its full Transformation Plan goal announced in 2019. As measured by its 2024 value in the February Plan, roughly 30 percent, $150 million annually, of the ongoing Transformation Plan's $475 million annual savings target has yet to be identified and achieved.[10] The savings may be modified in the update and should be monitored.

- **COVID Cleaning Expenses –** The 2020 November Financial Plan reclassified COVID cleaning expenses into the baseline budget, thus removing the detail of annual costs in ongoing plan updates. The previously itemized annual expenditures were planned to be $379 million in 2021, declining to $377 million in 2024. While enhanced cleaning has been well received in rider surveys and will likely be reimbursed by FEMA through September 2021 based on the federal emergency declaration, the agency may adjust such spending in the long run.

- **Updated Capital Plan and Borrowing Actions –** The 2020-2024 Capital Plan has been incrementally unfrozen this year, most notably with the reactivation of the Penn Station Access project for MNR. The decline in operating revenue last year rendered pay-as-you-go and new borrowing for capital investment for the current capital plan fiscally unfeasible. Nearly all commitments in 2020 and 2021 have thus far been drawn from the capital plans predating 2020. After initially removing the MTA's $9.8 billion contribution to 2020-2024 plan from its out-year debt issuance schedule in the February Plan, the MTA reportedly now intends to restore $6.9 billion of the original $9.8 billion, reflecting a reduction equivalent to its borrowing $2.9 billion from the Federal Reserve's Municipal Liquidity Facility (MLF).[11] However, no capital plan amendments have been adopted.

Federal MTA operating budget relief, continued favorable MTA revenues and expenses, federal funding for the 2nd Avenue Subway, and more stable State and City budgets may allow additional capital spending. Resources available and the MTA's capacity to implement projects, however, will not be sufficient to complete the full 2020-2024 Capital Plan and outstanding projects from prior plans by 2024. It is critical that the MTA focus its investment on the highest priority state of good repair and normal replacement work and make publicly available its project schedules and costs.

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ENDNOTES

[1] Metropolitan Transportation Authority, *2021 Adopted Budget*, *February Financial Plan 2021-2024* (February 2021), p. I-1, https://new.mta.info/document/30186.

[2] Verbal Commentary of Janno Lieber, President of MTA Construction and Development, at the Metropolitan Transportation Authority, MTA June 2021 Board Meeting (June 23, 2021), https://youtu.be/NM4emUJTf50?t=6022.

[3] The MTA's February Plan annual deficit in 2024 was forecast at $2.4 billion, with no cash balance transfer from prior years available to close it. The following estimated updates to this based on recent experience, as described in this blog, would change this 2024 projection. The reversal of the planned wage freeze and service reductions would add $322 million and $559 million, respectively. Using the McKinsey Midpoint farebox forecast to estimate the impact of higher than budgeted fare revenue that has been recently realized plus the higher than budgeted toll increase would reduce the deficit by $476 million and $43 million, respectively. Assuming the $148 million in Transformation Plan savings are not realized would increase the deficit, while sustaining a one percentage point savings in operating expenses—half the current underspending rate—would reduce it $163 million. These estimates would increase the deficit to $2.8 billion. However, in the intervening years these same changes plus the $6.5 billion received from the ARP would provide sufficient resources to close annual deficits in 2021 through 2023 and likely provide sufficient

resources to cover the 2024 cash deficit. Assuming the resources available to roll forward essentially are depleted in 2024 leaves 2025 with that structural mismatch of revenues and expenses and little or no remaining cash to cover it.

[4] The "worst case" forecast was adopted to minimize down-side financial risk. The forecast anticipated a COVID resurgence in winter and spring 2021. Instead of a new 2021 lockdown, however, vaccination levels have achieved the level necessary to end the official state of emergency.

[5] The lockbox revenue diversion budgeted for this year has been cancelled; it is being redirected out of the operating budget to fund the capital plan reactivation. See: Metropolitan Transportation Authority, *Budgetwatch June 2021 Flash Report* (June 2021), https://new.mta.info/document/42386.

[6] Near-term performance over plan is likely to continue unless COVID resurgence and related activity reverse the trend of increased economic activity, which could negatively affect ridership, tolls, and tax revenue. Currently, tolled crossings are close to pre-pandemic levels; subway and bus ridership have roughly halfway recovered; and commuter rail remains deeply depressed. See: Metropolitan Transportation Authority, "Day-by-Day Ridership Numbers" (accessed July 10, 2021), https://new.mta.info/coronavirus/ridership.

[7] Federal Emergency Management Agency, "COVID-19 Pandemic: Safe Opening and Operation Work Eligible for Public Assistance (interim guidance document, (February 3, 2021) www.fema.gov/sites/default/files/documents/fema_covid-19-pandemic-safe-opening-operation-work-eligible-public-assistance-interim-policy.pdf.

[8] Reported expenses were 7 percent below plan both in 2020 and 2021 through May, but the MTA reports that 70 percent of this year's underspending is due to work that will be done later in the year. Net of this timing shift, expenses would be approximately 2 percent favorable. See: Metropolitan Transportation Authority, *Budgetwatch June 2021 Flash Report* (June 2021), https://new.mta.info/document/42386.

[9] Patrick Foye, "Op-ed | MTA sensing optimism over the reopening of NYC," *AM New York*, (June 17, 2021) www.amny.com/oped/op-ed-mta-sensing-optimism-over-the-reopening-nyc/.

[10] Of the $475 million Transformation savings intended by 2024 in the November Plan, $325 million has been included in the baseline of the operating budget in the February Plan, with the remaining $150 million unidentified savings remaining a "below-the-line" plan adjustment until the savings can be identified. See: Metropolitan Transportation Authority, *2021 Adopted Budget*, *February Financial Plan 2021-2024* (February 2021), p. II-4, https://new.mta.info/document/30186; and Metropolitan Transportation Authority, *2021 Final Proposed Budget*, *November Financial Plan* (November 2020), Volume 1, p. II-3, https://new.mta.info/document/24126.

[11] The removal of the $9.8 billion debt issuance is visible on page III-28 of the February 2021 Financial Plan and discussed in the NYS Comptroller's April report but has not been accompanied by a capital plan amendment. MTA informed the State Comptroller in April that it intends to reduce its capital plan bonding by the amount of its MLF debt, but it has not yet amended its capital plan. Netting out MLF debt would leave $6.9 billion of the original $9.8 billion contribution. See: Office of the New York State Comptroller, "DiNapoli: $2.9 Billion Hole Threatens MTA's Capital Program" (press release, April 20, 2021), www.osc.state.ny.us/press/releases/2021/04/dinapoli-29-billion-hole-threatens-mtas-capital-program.