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Metro

FINANCE AND BUDGET COMMITTEE
JANUARY 17, 2007

SUBJECT: STRUCTURAL DEFICIT

ACTION: APPROVE PROPOSED STRUCTURAL DEFICIT REDUCTION PLAN

RECOMMENDATION

Approve the attached proposed three-year plan to solve the transit operating and capital structural deficit.

ISSUE

The FY07 ten-year forecast, presented to the Board at the October meeting, shows that under the current assumptions, Metro faces a structural deficit of $1.8 billion over the next ten years. The structural deficit is defined as: "... the result when available revenues designated for transit operating and capital are less than the forecasted expenditures." As part of the CEO's FY07 performance goals, the Board directed that the CEO provide a plan to resolve the transit operating and capital structural deficit in three years.

DISCUSSION

To solve this deficit, we recommend that the Board adopt a strategy that combines reducing costs and increasing revenues, including the use of one-time regional fund balances. A key performance indicator is the "Farebox Recovery Ratio," total fare revenue divided by total operating costs. Increasing the farebox recovery ratio is achieved either by decreasing costs, increasing fare revenues or a combination of these actions. To consistently operate at a balanced budget at the baseline level of capital investment, Metro's farebox recovery ratio needs to be at least 37%.

According to the 2004 National Transit Database, Metro's farebox recovery ratio was approximately 25% (and is budgeted at 24% in FY07) and declines over the ten years of the forecast. New York City Transit Authority reports a farebox recovery ratio of 60%; Washington Metro reports 46%; SEPTA (Philadelphia) reports 43%; New Jersey Transit reports 43%; and Chicago Transit Authority reports 38%.

The proposed "Three-Year Deficit Reduction Plan" (Attachment A) combines reducing costs and increasing fare revenues and shows the effects of improving revenues in the first three years to resolve future year deficits. The proposal assumes that after the three-year period, fare revenues are adjusted annually according to the regional consumer price index, as proposed in the Financial Stability Policy. Specific fare recommendations are not identified.

This plan identifies required revenue increases to balance the budget using minimal regional fund balances.

ALTERNATIVES CONSIDERED

Many different scenarios were considered when formulating our recommendation for solving the transit operating and capital structural deficit. One alternative was to use $114 million of regional fund balances and less fare revenues during the three-year period. It was not recommended because the performance and financial analyses for the 2006 Long Range Transportation Plan (LRTP) that was presented to the Board in May 2006 assumed that this $114 million would be available for regional transit corridor projects, highway projects and/or Countywide Call for Projects funding needs. It should also be noted that the baseline assumption of revenues available in the ten-year forecast assumes the continuation of the MOSIP program for both Metro and the Municipal Operators using approximately $70 million per year of Proposition C40% funds, so any additional use of regional funds would be additive to this amount.

Another alternative was to spread out the solution over a longer period than three years. This alternative increases the use of regional fund balances, which again could be used for other competing regional needs.

There are a myriad of differing combinations of fare adjustments, service adjustments and/or operating efficiencies to eliminate the structural deficit in part or over time. However, implementing an alternative combination that requires more regional funding than the recommended strategy may significantly impact mobility projects and programs in the LRTP.

As more regional funding is used for addressing the deficit, the Board may expect to encounter delays of planned completion dates of some major regional transit and highway capital projects within the next ten years, as well as the continued postponement and/or deletion of several major regional transit and highway capital projects and other Los Angeles County programs planned through 2030. After the approval of a specific alternative strategy, we would return with more detailed analyses that would identify more specifically which projects and programs would be impacted, i.e., delayed, postponed and/or deleted.

FINANCIAL IMPACT

The proposed deficit reduction plan decreases Metro costs by $15 million over a three-year period. The initial fare increase from this plan would begin in October 2007. Fare revenues would increase by $337 million with a resulting farebox recovery ratio of 37% after three years. The plan proposes the use of $45 million of Prop C40% fund balance in FY08 and elimination of the amount equivalent to the cost of purchased transportation (13 lines of contracted bus service) in FY09, for a savings of $33 million per year.

NEXT STEPS

With Board approval, we will incorporate the recommended strategy into the FY08, FY09 and FY10 Business Planning parameters that we will bring to the Board for approval in January 2007.

Attachment

Prepared by: Office of Management and Budget

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Chief Financial Services Officer, and Treasurer

Roger Snoble
Chief Executive Officer

Attachment A

FY07 Ten-Year Forecast Transit Operating and Capital
Proposed Three-Year Deficit Reduction Plan

	$ in millions	**FY08**	**FY09**	**FY10**	**FY11**	**FY12**	**5-YEAR TOTAL**
1	Baseline Deficit	(104.6)	(134.3)	(224.8)	(227.2)	(226.8)	(917.7)
2	Defer Bus Buy and Other Capital	-	-	-	-	-	-
3	Reduce Fuel Estimate	5.0	5.0	5.0	5.0	5.0	25.0
4	Eliminate Purchased Transportation	-	33.0	33.0	33.0	33.0	132.0
5	PC40% Backfill	45.2	-	-	-	-	45.2
6	Increase Fare Revenues	54.4	106.0	177.0	186.6	195.9	719.9
7	Prior Year Fund Balance	-	0.0	9.7	(0.1)	(2.7)	
8	Net Surplus (Deficit)	0.0	9.7	(0.1)	(2.7)	4.4	4.4

9	Baseline Farebox Recovery Ratio	24.3%	24.3%	23.9%	23.2%	23.3%
10	Proposed Farebox Recovery Ratio	29.0%	33.2%	38.1%	37.6%	38.1%

11	Prop Increases to Total Fare Rev	19.5%	15.0%	15.2%	1.2%	1.2%

12	Proposed Annual Service Hrs Reduction (000)	113.5	765	48	71	0	997.5

- Solves deficit in 3 years
- Maintains minimal capital program
- Reduces fuel estimate as per FY07 actuals
- Eliminates Purchased Transportation in FY09
- Service capacity increases with Artic purchases
- Increases fares each year
- Uses PC40% Backfill in FY08 in addition to MOSIP