

**MTA-WIDE FINANCIAL PLAN
FOR 2004-2007**

AND

FINAL PROPOSED BUDGET FOR 2004

**MTA Finance Committee
MTA Board**

**October 28, 2003
October 28, 2003**



Metropolitan Transportation Authority

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Acknowledgment

This Presentation is dedicated in memory of:

David J. Casella

**Deputy Director of Budgets & Financial Planning
Subways and Buses**

In appreciation for your years of unwavering service, friendship and
dedication.

I. INTRODUCTION



Metropolitan Transportation Authority

State of New York

October 28, 2003

Members of the MTA Board:

This document represents the Final Proposed 2004 Budget for the MTA Board's consideration and includes a Four Year Financial Plan for 2004 through 2007. The budget remains balanced through 2004 with a small surplus of \$36.2 million projected at the end of 2004 due to favorable revenue receipts. Adoption of the 2004 Budget will fulfill the Board's pledge to hold service, fare and toll levels through the end of 2004.

Deficits, however, are projected for 2005 (\$839 million), 2006 (\$1.34 billion) and 2007 (\$1.45 billion). These deficits represent structural imbalances in the MTA budget stemming primarily from the following areas:

- Rising Debt Service Costs
- Increasing Pension, and Health and Welfare Expenses
- Depletion of Non-Recurring Resources

HOW WE GOT HERE

The projected deficits in 2005 through 2007 while significant are not surprising given the MTA's growth in capital needs, shrinking financial support from its funding partners and the reduced availability of non-recurring revenues.

The structural imbalances are evident in comparing the 2004 Final Proposed Budget and the 2005 Plan. The 2004 Final Proposed Budget estimates a net cash balance of \$36.2 million at year-end. The 2005 Plan, however, projects an end-of-year cash deficit of \$839.7 million, a worsening of \$875.9 million from 2004. As the table below demonstrates, this deterioration in the cash balance results from extraordinary increases in debt service and pension costs, a reduction in subsidy revenues, the elimination of non-recurring favorable 2004 cash adjustments and the loss of prior year surpluses as reflected in the lower 2005 opening cash balance.

The table further demonstrates that normal operating expenses (excluding pension and health and welfare) grow by a modest 2.8 percent in 2005, less than the 3.24 percent projected growth in inflation as measured by the regional CPI. Health benefit costs, reflecting national trends, are expected to increase by 8.2 percent in 2005. The operating expense and health benefit increases are offset in the Plan by an assumption of 5.0 percent growth in 2005 in passenger and toll revenue yield -- an increase less than the projected inflation rate from 2003. An additional 5.0 percent increase in passenger and

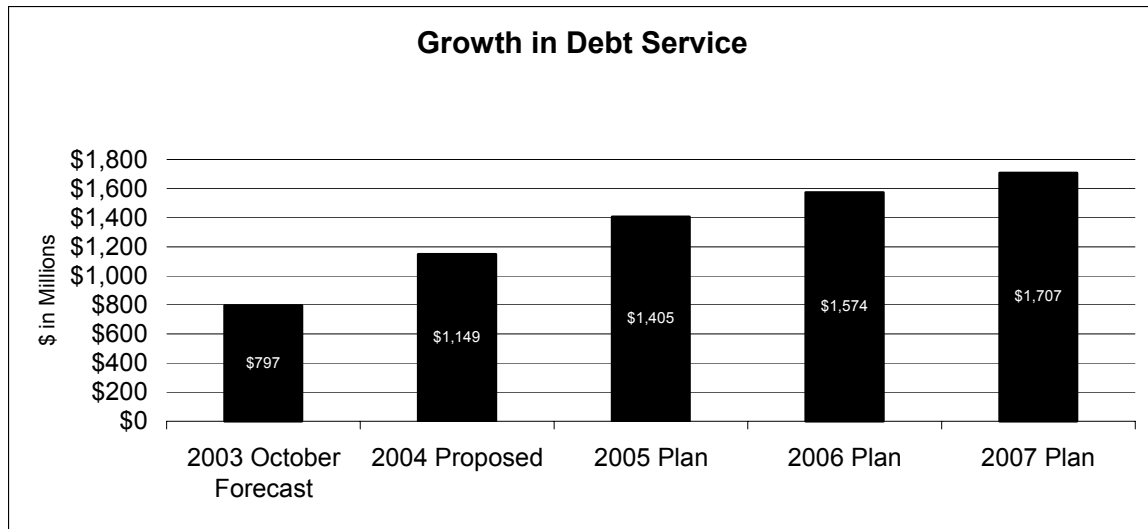
toll revenue yield is also assumed in 2007 to partially offset growth in normal operating expenses between 2005 and 2007.

Major Reasons for Change in Net Cash Balance 2004 vs 2005 Favorable/(Unfavorable)		
		<i>(\$ in millions)</i>
Operating Expense Growth-excluding Pension, Health and Welfare and Debt Service - 2.8% Growth		\$(161.1)
Health and Welfare Expense - 8.2% Growth		(62.6)
Passenger, Toll and Other Operating Revenue Improvement		18.3
Increased Fare and Toll Yields – 5.0%		<u>227.0</u>
<i>Sub-Total</i>		<i>\$21.6</i>
Debt Service Costs - 22.3% Growth		(255.9)
Pension Costs – 32.6% Growth		(150.9)
Subsidy Change		(162.1)
Non-Recurring Cash adjustments		(139.7)
Reduced Opening Cash Balance (prior year cash balance)		<u>(188.9)</u>
<i>Sub-Total</i>		<i>\$(897.5)</i>
<i>Total Change in Net Cash Balance</i>		<i>\$(875.9)</i>

Although 2005 operating expense growth is held below projected inflation, the plan provides for the maintenance of 2004 service levels, improvements in safety and security for employees and customers and the continuation of high reliability and maintenance standards.

RISING DEBT SERVICE COST TO SUPPORT CAPITAL PLAN

The largest cause of expense growth is the payment of debt service for the Capital Plan. This single expense is projected to grow from \$1.15 billion in 2004 to \$1.71 billion in 2007 - - a 49 percent increase.

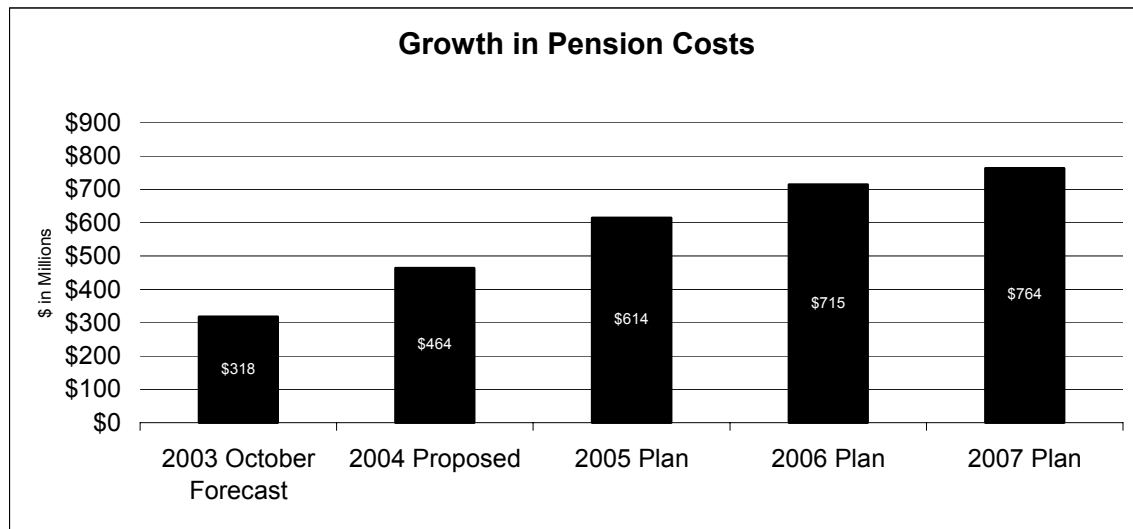


The debt service costs associated with the MTA's current 2000-2004 Capital Plan form the bulk of this increase. This has long been anticipated and was discussed when the Plan was approved by the State's Capital Program Review Board in May 2000. These costs were exacerbated by the defeat of the Transportation Bond Act of 2000 - - from which the MTA was scheduled to receive \$1.6 billion to support its Capital Plan. Although the loss of the Bond Act money was partially offset by the greater than expected savings generated by the MTA's debt restructuring initiative, those additional savings would have otherwise been used to reduce MTA's debt burden. In addition, the increase in debt service costs would have occurred earlier and would have been greater than currently projected absent the successful debt restructuring initiative.

The debt service projections for 2005-2007 also anticipate a small amount of debt service related to the start up of the next five (5) year capital plan, which by statute, must be submitted for CPRB review by October 2004. Since this program is only in its initial stages of development, the size, composition and funding for the 2005-2009 capital program is currently not known. It is, however, assumed that bonds will be issued to support a portion of the next Capital Program. Therefore, as a place holder, the October 2003 financial plan assumes a 2005-2007 base capital program level consistent with the currently approved capital program, plus inflation, and assumes a funding profile similar to the current capital funding plan (38% of core capital work is funded by new debt). Beyond this base capital program, the operating plan assumes the projected commitment plan for the next stages of the MTA network expansion projects - - Second Avenue Subway and East Side Access (assuming a 50% federal match for these projects) - - plus additional funding for its security program. It is significant to note, however, that most of the assumed increases in debt service attributable to the next Capital Plan will not be fully realized until after 2007.

GROWTH IN PENSION, HEALTH AND WELFARE BENEFIT COSTS

The MTA pension costs are projected to increase from \$463.6 million in 2004 to \$763.6 million in 2007 an increase of \$300 million or 65 percent.



The \$300 million increase from 2004 to 2007 includes \$263 million for New York City Transit. The balance of the increase from 2004 to 2007 is spread over the other defined benefit plans maintained by the MTA. The large increase in projected pension costs is essentially due to a decline in the earnings for the pension systems – a trend which is mirrored in state and local pension systems throughout the country. During the late 1990's when the equity returns of the systems were booming, employer pension costs declined significantly. As additional benefits were legislatively enacted for the majority of the employees, such as permanent retiree cost of living adjustments and reductions in contribution by the employees covered by the plans, the pension systems became more expensive to support. Because the improved benefits continue, additional employer contributions will be required until the earnings begin a sustained growth.

In order to develop consistent assumptions for the growth in health and welfare costs, the Financial Plan assumes an inflation rate for this category of expenditure of 15 percent in 2004 and 8.2 percent in years 2005 through 2007. These estimates were based on discussions with the State and an analysis of historical information. Based on these assumptions health and welfare costs are projected to increase \$50 million in 2004; \$63 million in 2005; \$69 million in 2006 and \$75 million in 2007.

DEPLETION OF NON-RECURRING FINANCIAL INITIATIVES

The MTA prior year budgets from 2002 through 2004 relied on various non-recurring budgetary actions. Those actions included a one-time acceleration of State subsidy payments totaling \$368 million as well as operating savings generated from MTA's debt restructuring initiative of \$631 million. These non-recurring resources allowed the MTA to avoid a fare and toll increase in the months following the tragic events of September 11th, and to absorb offsets in revenues caused by the downturn in the economy as well as increased costs in the area of security and police expenses necessary to protect customers, workers, and the physical assets of the system. As these one-time resources disappear, the strain on the budget is inevitable.

The MTA has faced significant deficits in the recent past and managed to close them. We addressed these gaps through management efficiencies and maximizing resources - with only one fare increase over eight (8) years. While the current Financial Plan anticipates increases in the yield from revenues generated by fares and tolls in 2005 and 2007 respectively to offset normal operating expense growth, those increases do not offset the major structural imbalances in the underlying budget for 2005 through 2007. It is clear that additional financial support from outside the MTA will be necessary to manage these imbalances.

FINAL PROPOSED 2004 BUDGET

The Final Proposed 2004 Budget is being presented to the MTA Board for review, analysis and comment. Each agency has invited public comment and discussed its Preliminary 2004 Budget with their respective Board Committees. Changes resulting from this input and review of updated data for the current year (2003) have been incorporated into the Final Proposed 2004 Budget. Public comment will continue to be solicited at the November Committee and/or Board meetings and a Final 2004 Budget will be adopted by the MTA Board in December.

In July the MTA Board was presented with a mid-year forecast of operating revenues and expenses for 2003 and a Preliminary Budget for 2004. That plan was in balance on a cash basis with projected year-end cash balances of \$186.3 million in 2003 and \$4.1 million 2004. The current reforecast for 2003 and the Final Proposed Budget for 2004 remains in balance on a cash basis with projected year-end cash balances of \$225.1 million in 2003 and \$36.2 million in 2004. Major changes in 2003 and 2004 over the Preliminary budget released in July presented below:

**2004 Net Cash Balance Preliminary Budget – Final Proposed Budget
Favorable/(Unfavorable)**

(\$ in
millions)

<i>2004 Net Cash Balance - Preliminary Budget</i>	<i>\$4.1</i>
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Changes:

Bridges and Tunnels toll revenue	33.1
Passenger fare revenue	11.8
Mortgage Recording Tax yields	42.1
Urban Tax yields	7.6
Debt Service expenses	14.7
Pension cost re-estimate	(32.6)
August 2003 Blackout costs and lost revenue	(20.6)
Health and Welfare inflation re-estimate	(19.0)
Other expense needs	(5.0)

<i>Total Change</i>	<i>\$32.1</i>
<i>2004 Net Cash Balance - Final Proposed Budget</i>	<i>\$36.2</i>

In preparing the Final Proposed Budgets for 2004 as a general rule agencies were permitted to reallocate funding and to restore previously proposed reductions to the extent that the October 2003-2004 projections reflect an overall improvement to the July 2003 plan. As a result, new needs required internal agency funding. One exception involves an unanticipated new need in the LIRR pension system which was subsidized in 2004—however; the plan assumes that the agency will begin to absorb these costs on a graduated basis in 2005 through 2007.

While the 2004 Final Proposed Budget projects a small positive cash balance, this Plan does have risks. The Budget assumes \$121.3 million of increased governmental assistance which has not yet been identified. The continuation of the current sluggish economy or a further downturn, would reduce revenue and subsidy yields. In addition, the Plan includes only a small contingency of \$30 million, less than 0.5 percent of operating expenses for unforeseen events.

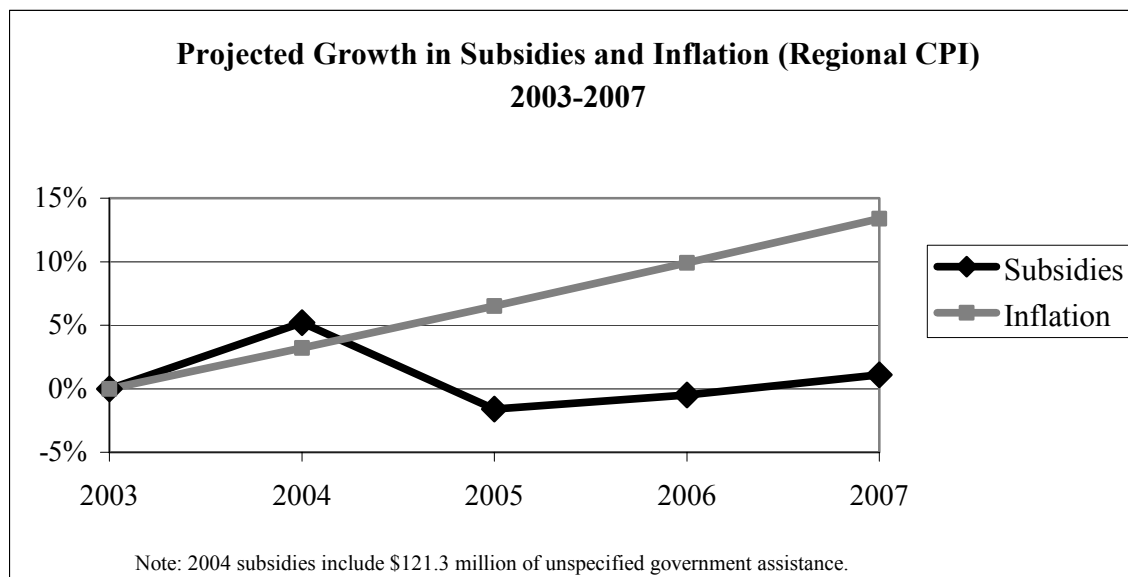
ADDRESSING THE NEEDS – NEXT STEPS

In the months to come, the MTA management team will undertake a two-pronged approach to addressing these out-year deficits. First, extensive analysis will be initiated to determine what cost-cutting measures and cost containment actions can be implemented to minimize projected costs while maintaining existing service levels and without compromising safety, security and reliability standards. These actions will include among other initiatives the proposed organizational restructuring of the MTA to

reduce duplicative expenditures and focus its entities along business lines; reviewing existing procurement and other administrative procedures to enhance efficiencies; and undertaking a review of the management of the MTA's various pension systems.

Secondly, the MTA will seek necessary financial assistance from its governmental funding partners on the Federal, State and local levels to ensure that it receives the subsidies necessary to maintain its existing levels of service. Assistance will be required both on the operating budget and on the next five year Capital Plan.

The inadequacy of current subsidy sources is demonstrated by the fact that the projected growth in existing subsidy resources is far short of keeping pace with estimated regional inflation, as measured by the Consumer Price Index (CPI). Current subsidy sources in 2007, the last year of the Financial Plan, are projected to increase by only 1.1 percent from 2003, compared to a projected inflation increase of 13.4 percent over the same period, as shown on the chart below.



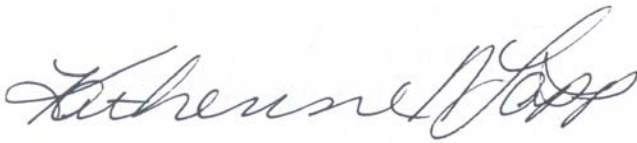
It is important to note that even if subsidy levels kept pace with projected inflation, the resulting yields would not offset the structural budget imbalances projected in 2005 and beyond. The Plan does assume increased yields from passenger fares and tolls to offset in part the inflation-based growth in normal operating expenses; however these yields cannot offset the extraordinary growth in debt service, health and welfare and pension costs.

In addition to strains on the operating budget, the MTA, together with other transit properties throughout the country, is monitoring the developments on the Federal level concerning the reauthorization of TEA-21, which expired in September of this year and was extended for a five (5) month period. The MTA receives \$800 million annually under the current TEA-21 funding formula to support its Capital Plan—a level which

must not only be maintained, but enhanced to maintain the systems and avoid additional debt burdens on the MTA operating budget.

Leaders in business, government and civic associations will be contacted to make the needs of this critical service known and to garner the support necessary to ensure that it not only is maintained but continues to grow and service the mass transportation needs of the metropolitan region. We have issued the Four Year Plan to set forth the financial challenges ahead for the MTA. We have up to a year to work with our funding partners to identify the long-term solutions needed to close these gaps that puts the least amount of burden on our riders.

Sincerely,

A handwritten signature in dark ink, appearing to read "Katherine Lapp". The signature is fluid and cursive, with the first name "Katherine" written in a larger, more prominent script than the last name "Lapp".

Katherine N. Lapp
Executive Director and
Chief Operating Officer