Financial Outlook for the Metropolitan Transportation Authority

Thomas P. DiNapoli
New York State Comptroller

Kenneth B. Bleiwas
Deputy Comptroller

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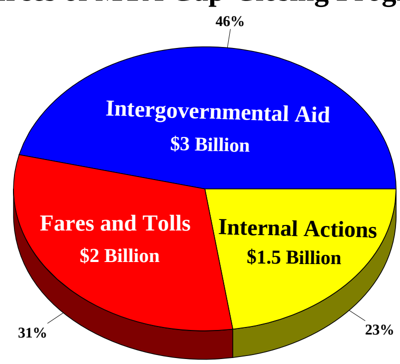
- **Subway, bus, and commuter railroad use reached the highest level in decades in 2007 and grew by 4 percent through May 2008.**
- **The MTA has raised fares and tolls by nearly 33.9 percent since 2002—52 percent faster than the inflation rate. If the increases planned for July 2009 and January 2011 are enacted, fares and tolls will have grown 63 percent faster than the inflation rate.**
- **After peaking in 1992, the value of government subsidies has eroded, on an inflation-adjusted basis, by $383.1 million.**
- **The number of managerial, supervisory, professional, technical, and clerical employees increased by 568 employees between December 2004 and May 2008, and the agencies are authorized to fill another 818 vacancies by the end of the year.**
- **The gap-closing program would cut central administration by only 59 employees by the end of 2009, while maintenance staff would decline by 351 employees.**
- **Debt service grew from $848 million in 2004 to $1.4 billion in 2007, and will reach $2 billion by 2012 just to finance capital programs from 2005-2009 and earlier.**
- **Debt service consumed about 12 percent of total revenues between 1996 and 2005, but will consume 21 percent of revenues by 2012—an increase of 75 percent—and 37 percent of fare and toll revenue.**
- **Health and welfare costs will reach $1.4 billion by 2012—double the 2004 level. Pension contributions peaked in 2008 at $961 million, which is $652 million more than the 2003 level.**

The Metropolitan Transportation Authority (MTA) is facing a serious fiscal crisis. In its July 2008 financial plan (the "July Plan"), the MTA projects operating budget gaps, on a cash basis, of $1.1 billion in 2009, $1.9 billion in 2010, $2.1 billion in 2011, and $2.3 billion in 2012. These gaps represent 11 percent of revenue in 2009 and more than 22 percent of revenue by 2012. In addition, the MTA's 2010-2014 capital program has a funding gap of at least $15 billion.

To balance the 2009 operating budget and to narrow the out-year gaps, the MTA has proposed a $6.4 billion gap-closing program that relies heavily on outside assistance (see Figure 1). More than three quarters of the resources would come from intergovernmental aid ($3 billion) and higher fares and tolls ($2 billion). Less than one quarter would come from internal actions, and 37 percent of those savings remain unspecified**.**

Figure 1
Sources of MTA Gap-Closing Program



Sources: Metropolitan Transportation Authority; OSC analysis

Even though New York State and New York City are experiencing their own financial difficulties, the MTA is seeking a $3 billion increase in intergovernmental aid. The MTA also proposes to raise fares and tolls by 8 percent in July 2009—just 15 months after the last hike—and by an additional 5 percent 18 months after that, in January 2011. These increases will place a heavy burden on riders who are already under financial pressure from recent fare hikes, higher energy costs, and inflation.

After a comprehensive review of the MTA's finances, the State Comptroller concludes that while the MTA presented reasonable estimates of its projected budget gaps in July 2008, the gaps have grown by $381 million now that the State has lowered its forecast of dedicated transit taxes. In addition, recent Wall Street developments have increased the potential for further revenue shortfalls and job losses that could ripple through the regional economy, resulting in lost ridership.

The MTA's gap-closing program, moreover, is too risky because it relies so heavily on actions that are either outside its direct control or are still unspecified. The turmoil on Wall Street has created serious fiscal challenges for the State and City, which will likely limit their ability to provide additional financial assistance to the MTA.

After assessing the gap-closing program and other risks, the MTA still faces remaining operating budget gaps that could total $522 million in 2009, $1.4 billion in 2010, $1.6 billion in 2011, and $1.8 billion in 2012. Even if the gap-closing program is fully successful, a budget gap of $250 million would still remain in 2010—the equivalent of an unplanned fare and toll increase of 5 percent.

The MTA's capital budget is also at a crossroads. Last February, during the debate over congestion pricing, the MTA proposed a $32 billion capital program—the largest in its history. The proposed program, however, had a funding gap of $13.8 billion and did not move forward after congestion pricing failed to win approval. The current capital program ends in December 2009, and the 2010-2014 capital program is expected to have a funding gap of at least $15 billion.

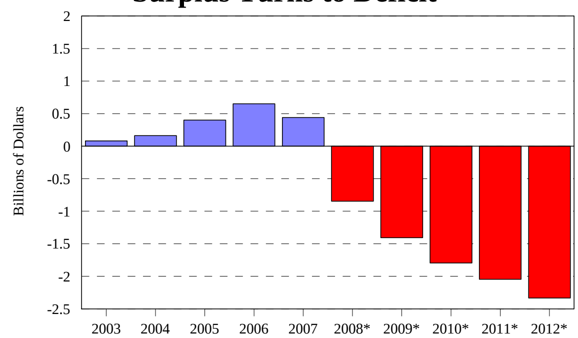
History shows that the size of the capital program and how it is financed has a direct impact on the MTA's operating budget—and hence fares and tolls. The Governor has appointed a 13-member commission to identify new sources of revenue to help finance the MTA's operating and capital budgets for the next ten years. The commission will release its findings by December 5, 2008, shortly after the MTA issues its November financial plan. Placing the MTA on sound long-term financial footing is critically important to the regional economy.

Projected Budget Gaps

On an accrual basis of accounting, which is the best way to discern long-term trends, the MTA generated positive cash balances during calendar years 2003 through 2007 (see Figure 2), primarily from extraordinary collections from taxes on real estate transactions.[1] (During this period the MTA also raised fares and tolls, and the State increased its assistance.) Overall, revenues grew at an average annual rate of 9.4 percent while spending grew by 7.5 percent each year.

Figure 2

Surplus Turns to Deficit



Note: Estimates exclude depreciation. * MTA forecast
Sources: Metropolitan Transportation Authority; OSC analysis

The continued rapid growth in debt service and fringe benefits, combined with a slowdown in real estate transaction tax collections and a rise in energy costs, will cause spending to outstrip projected revenue growth beginning in the current calendar year. Even though the MTA raised fares and tolls in March 2008, spending will exceed revenues, on an accrual basis, by $847 million in 2008. To balance the 2008 budget, the MTA will draw upon its cash reserves. Despite increases in utilization, the disparity between revenues and expenditures will widen in subsequent years.

Overall, spending will grow at an average annual rate of 4 percent during calendar years 2008 through 2012, while revenues are projected to grow by only 0.8 percent each year. The disparate growth rates result in budget gaps of $1.4 billion in 2009, $1.8 billion in 2010, $2 billion in 2011, and $2.3 billion in 2012.

[1] The estimates in this report exclude depreciation and the long-term liability associated with fringe benefits other than pensions (i.e., OPEBs).

The major factors that contribute to the budget gaps are debt service and health insurance costs, which together are projected to grow almost five times faster than inflation. The growth in these costs accounts for more than half of the 2012 budget gap. At the same time, collections from taxes on real estate transactions are expected to drop by $544 million in 2008.

Utilization Trends

The use of mass transit services (i.e., subway, bus, and commuter railroads) grew by 2.8 percent in 2007 to reach the highest level in decades. The July Plan assumes ridership will rise by another 2.1 percent in 2008, stagnate in 2009, and then grow by 1 percent per year. So far, gains have been greater than expected, but ridership could drop in the second half of 2008 as job losses mount on Wall Street.

Bridge and tunnel crossings are expected to drop by 3 percent in 2008 and again in 2009 because of higher gasoline prices before increasing slightly in 2010. Figure 3 shows utilization trends for each service since 1990 (also described below).

New York City Transit: In 2007, subway ridership reached its highest level since 1951. Through May 2008, ridership was up 5 percent. Bus ridership is 50 percent higher since 1996, but levels have stayed relatively flat since 2003.

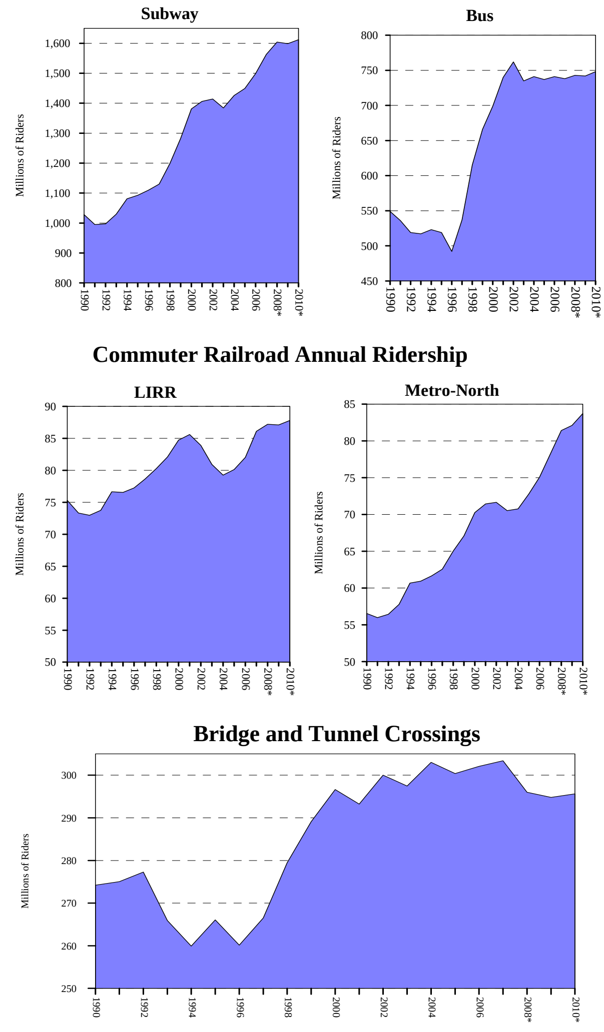
Long Island Rail Road (LIRR): The LIRR has recovered from ridership losses that occurred after the terrorist attacks of September 11, 2001. In 2007, the LIRR recorded its highest ridership since 1949, and through May 2008 ridership was up 4 percent.

Metro-North Railroad: In 2007, Metro-North recorded the highest ridership since its creation in 1982, and through May 2008 ridership was up 5 percent.

Bridge and Tunnel Crossings: Crossings increased by 17 percent between 1996 and 2007, but were lower by 1.4 percent through May 2008 in response to higher gasoline prices.

Figure 3

New York City Transit Ridership

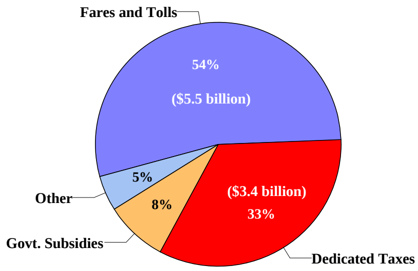


Sources: Metropolitan Transportation Administration; OSC analysis

Revenue Trends

In 2008, more than half of the MTA's revenue (54 percent) will come from fare and toll collections from subways, buses, railroads, tunnels, and bridges (see Figure 4). One third of the revenue will come from taxes imposed by the State on the 12 counties that make up the MTA transportation district (e.g., sales taxes and real estate transaction taxes), and also from taxes and fees effective throughout the State (e.g., petroleum business taxes and motor vehicle registration fees). The balance of the MTA's revenue will come from State and local government subsidies (8 percent), and from advertising and other sources (5 percent).

Figure 4
Sources of Revenue
2008= $10.2 billion



Sources: Metropolitan Transportation Authority; OSC analysis

Fare and Toll Collections

The MTA did not raise fares and tolls between 1995 and 2002, but raised them by 25 percent in 2003, 5 percent in 2005, and by 3.85 percent in March 2008. To help address the projected budget gaps, the MTA has proposed raising fares and tolls by 8 percent in July 2009 and by another 5 percent in January 2011.

According to the most recent data from the National Transit Database, the farebox ratios for the MTA's subways, buses, and commuter railroads (i.e., the percentages of fare revenues that cover operating expenses) were already among the highest in the nation in 2006.

In 2006, subway and bus fares covered 58.9 percent of New York City Transit's operating expenses—the highest in the nation among comparable transit agencies (see Figure 5). Philadelphia, Chicago, and Atlanta each had farebox operating ratios under 40 percent. Metro-North had the highest farebox operating ratio of the five largest commuter railroads in the nation, at 60.6 percent, and the LIRR was fourth, at 46.9 percent (see Figure 6). Farebox operating ratios declined in 2007 to 54.8 percent for NYC Transit, 45.1 percent for the LIRR, and 57 percent for Metro-North, and are projected to decline again in 2008 even though fares were raised in March 2008.

The MTA estimates that, overall, its farebox ratio was 52.1 percent in 2007 and will be 49.8 percent in 2008. The State Comptroller recommends that the MTA and its funding partners establish, as a matter of public policy, a target range for the maximum share paid by riders to make fare increases more predictable and less contentious.

Figure 5
Transit Operators
2006 Farebox Operating Ratios
(in millions)

	Fare Revenue	Expenses	Ratio
NYCT	$2,722.0	$ 4,621.9	58.9%
Wash. DC	504.2	1,112.5	45.3%
Phila.	215.3	584.6	36.8%
Chicago	462.0	1,311.3	35.2%
Atlanta	96.1	294.7	32.6%

Sources: National Transit Database; OSC analysis

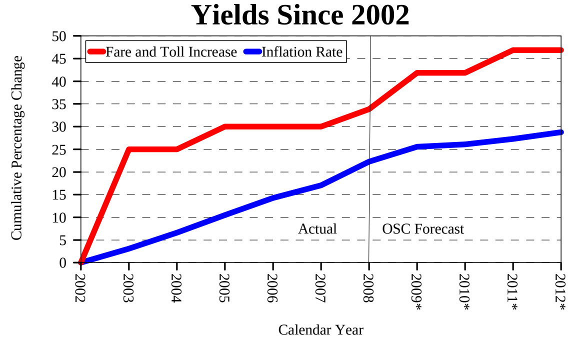
Figure 6
Commuter Railroads
2006 Farebox Operating Ratios
(in millions)

	Fare Revenue	Expenses	Ratio
Metro-North	$ 454.4	$ 749.2	60.6%
Philadelphia	97.0	182.2	53.3%
NJ Transit	351.6	685.2	51.3%
LIRR	457.4	975.3	46.9%
Boston	104.3	223.8	46.6%

Sources: National Transit Database; OSC analysis

While average fares are slightly lower today than they were in 1996 as a result of discounts and bonus programs, the MTA has raised fares and tolls by nearly 33.9 percent since 2002—52 percent faster than the inflation rate (see Figure 7). After the implementation of planned fare and toll increases in July 2009 and January 2011, fares will be 46.9 percent higher than the 2002 level—63 percent higher than the inflation rate.

Figure 7
Cumulative Change in Fare and Toll Yields Since 2002



Sources: Metropolitan Transportation Authority; OSC analysis

Dedicated Transit Taxes

Since 1980, the State has imposed taxes and fees on both a regional and a statewide basis to benefit mass transit. The majority of the proceeds (90 percent) is allocated to the MTA and the balance is distributed to other transit systems. In 2008, the MTA will receive $3.4 billion from taxes dedicated to mass transit.

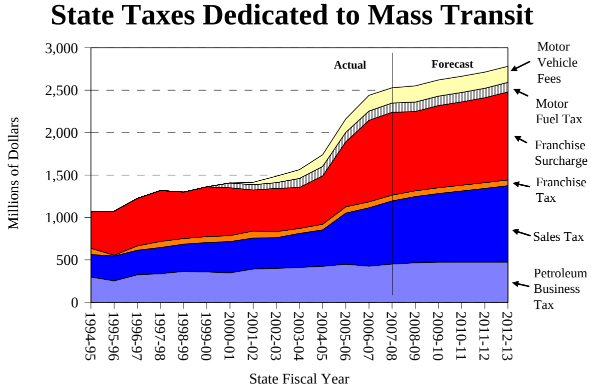
As we have pointed out in the past, the State has used a portion of these resources (since 1995) to fund up to 90 percent of its statutory obligation to subsidize the MTA's operating budget, rather than using General Fund revenues as originally intended. Consequently, the MTA has been shortchanged by $2.2 billion since 1995, and will lose out on $709 million during calendar years 2009 through 2012. In addition, the State intends to divert resources intended for the MTA's operating budget to fund transit capital projects.

Revenues from dedicated transit taxes have grown by 76 percent between State fiscal year (SFY) 2000-2001 and SFY 2007-2008 (see Figure 8). Some of the taxes, such as the franchise surcharge and the sales tax, have performed exceptionally well over the past few years, while others, such as the petroleum business tax, have lagged behind.

Given the current economic slowdown, the potential for revenue shortfalls is increased**.** The MTA's tax estimates are based on the enacted State budget for the current fiscal year, but those estimates were recently updated. Based on the latest forecast from the State Division of the Budget, tax collections are likely to be lower than assumed in the July Plan by $139 million over the next 18 months, and by $77 million in 2010, $86 million in 2011, and $78 million in 2012.

Figure 8

State Taxes Dedicated to Mass Transit



Sources: Metropolitan Transportation Authority; OSC analysis

Dedicated Transit Taxes and Fees

Sales Tax: A 0.375 percent sales tax is assessed on most sales transactions in the 12-county MTA district. The tax was raised from 0.25 percent in June 2005.

Petroleum Business Tax (PBT): Assessed on petroleum businesses in New York State. The tax rate rises and falls annually as the Producer Price Index for refined petroleum products changes, but State law has capped any change in the rate at 5 percent. The MTA receives about one third of the State's PBT revenue.

Motor Fuel Tax: Paid by distributors of motor fuel in the State and passed on to consumers. The MTA receives about 20 percent of statewide motor fuel tax revenue, an increase from the initial 11 percent that the State devoted to the MTA in 2000.

Franchise Tax and Surcharge: Two taxes on the stock and earnings of transportation and transmission companies, such as trucking and phone companies, a portion of which is allocated to the MTA. The MTA also receives revenue from a 17 percent surcharge on the franchise tax paid by corporations, banks, utilities, and insurance companies in the MTA region. These sources provided $ 1 billion to downstate mass transit in 2007.

Motor Vehicle Fees: The MTA receives about 20 percent of statewide motor vehicle registration and driver license fees. The percentage devoted to the MTA has increased from 4 percent in 2001, the first year such fees were allocated to the MTA.

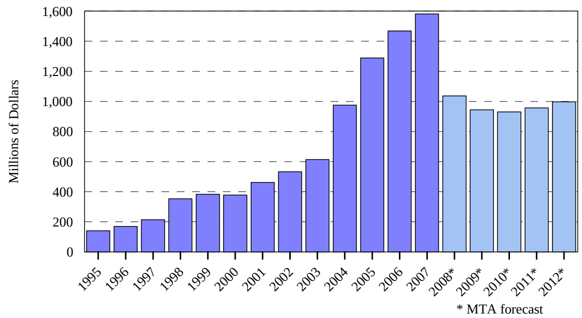
Mortgage Recording Tax: The MTA receives 30 cents for every $100 of outstanding principal for all mortgages recorded in the MTA transportation district. It also receives 25 cents for every $100 of outstanding principal (paid by the lender) for one- to six-family houses in the district.

Urban Tax: The MTA receives 62.5 cents for every $100 of outstanding principal of all commercial mortgages over $500,000 in New York City, as well as 1 percent of all commercial sales in the City over $500,000.

In recent years, the MTA has greatly benefited from the regional real estate boom, especially the commercial market in Manhattan. Collections from taxes on real estate transactions averaged $370 million during calendar years 1998 through 2000, and then reached a record $1.6 billion in 2007 (see Figure 9). The July Plan assumes that collections will decline by $544 million in 2008 from the record 2007 level due to a weakening real estate market. Although collections were stronger in July and August than in the two prior months, it is too soon to determine whether these results represent a longer-term trend.

Figure 9

Annual Real Estate Transaction Tax Collections

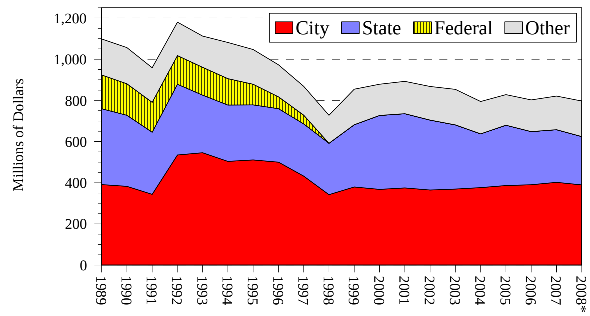


Sources: Metropolitan Transportation Authority; OSC analysis

Figure 10

MTA Government Subsidies

Inflation-Adjusted



Sources: Metropolitan Transportation Authority; OSC analysis

Government Subsidies

Besides State-authorized taxes and fees, the MTA benefits from subsidies from its governmental funding partners. In 2008, the MTA will receive a total of $797 million in subsidies. Of this amount, $390 million comes from the City, $231 million comes from the State, and the remaining $176 million comes from other MTA localities. (The MTA will also receive, from the City, $252 million to cover the deficit of the seven private bus companies for which, at the City's request, the MTA assumed operational responsibility.)

Almost half of the subsidies ($382 million) will come from a State program that requires the localities in the MTA region to match, in the aggregate, the State contribution of $191 million. The MTA also receives subsidies from local governments to maintain commuter railroad stations; from Nassau County for Long Island Bus; and from Connecticut for Metro-North's New Haven line. NYC Transit receives subsidies from the State and the City to provide free and reduced fares to the City's schoolchildren and elderly and disabled passengers.

Since 2000, State and local subsidies have remained level at about $600 million. When measured against inflation, the erosion in the value of these subsidies becomes clear. The MTA will receive $383.1 million less in government subsidies in 2008 compared with the peak received in 1992 (see Figure 10).

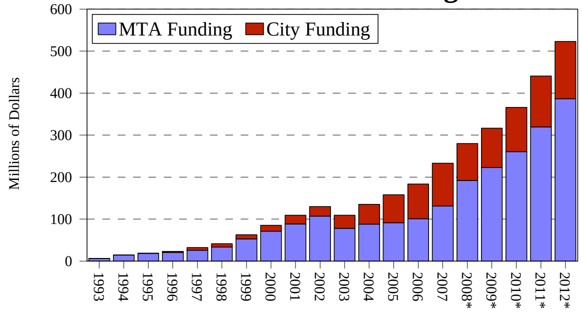
More than one third of the decline comes from the federal government's decision in 1998 to stop providing operating budget subsidies to large mass transit agencies and to focus on capital funding instead. U.S. Senator Clinton and Congressman Nadler have sponsored recent bills that would provide the MTA with $237 million in additional assistance over a two-year period. If such assistance were used to balance the operating budget, the MTA would be prohibited from raising fares during the period. The City's annual contribution has eroded by $156.4 million since it peaked in 1993, and the State's contribution has eroded by $134.2 million since it peaked in 1989.

Moreover, the subsidies paid by the State and the City do not pay the full cost of services provided by the MTA. For example, the State and the City each contribute $45 million annually to transport 1.3 million schoolchildren, but, based on the average fare, the MTA places the value of the service at $179 million—nearly twice the value of the combined subsidy.

In 1993, the MTA assumed responsibility for New York City's paratransit program, which provides transportation services to people who are unable to access the subways, buses, or commuter railroads. The cost of the program has grown from $6 million in 1993 to $280 million in 2008, and the cost is projected to reach $522.9 million by 2012 (see Figure 11). In 2008, the City contributed $88.2 million toward the cost of this program, but the MTA contributed more than twice that amount—$191.8 million. The MTA has suggested that the MTA and the City split the cost of this program evenly.

Figure 11

NYC Transit Paratransit Program Sources of Funding



Sources: Metropolitan Transportation Authority; OSC analysis

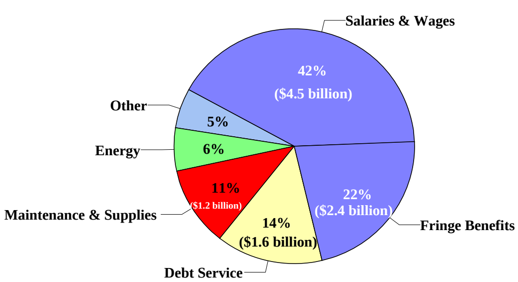
Expenditure Trends

In 2008, the MTA budget is projected to total $10.9 billion. Nearly two thirds of the MTA's resources in 2008 are allocated to personal services costs, including salaries, overtime, health insurance, pension contributions, and other fringe benefits (see Figure 12). Another 14 percent is allocated to debt service; 11 percent is allocated to maintenance and supplies; and 6 percent is allocated to energy costs, including electricity to run the subways and fuel to operate the buses.

Figure 12

Allocation of Resources

2008=$10.9 billion



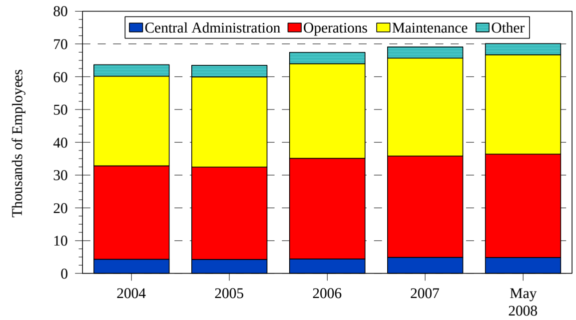
Sources: Metropolitan Transportation Authority; OSC analysis

During the past five years, spending has grown at an average annual rate of 7.5 percent, more than twice the regional inflation rate. The major factors behind the growth in spending have been the rising costs for debt service, health insurance, and pension contributions. Payroll costs have grown at an average annual rate of 3.6 percent during this period—only slightly faster than the regional inflation rate—reflecting collective bargaining costs and an expanding workforce.

Staffing levels reached 70,113 in May 2008, or 6,436 employees higher than the December 2004 level, including the addition of 3,409 employees of the private bus companies that were recently taken over by the MTA (see Figure 13). The agencies are authorized to fill another 559 positions by the end of December 2008, but the MTA expects some of these positions to remain vacant.

Figure 13

MTA Staffing Levels



Note: The MTA's estimates for operations and maintenance include indirect service personnel, such as managers and clerks.
Sources: Metropolitan Transportation Authority; OSC analysis

Central administrative staffing has grown by 373 employees during this period (including 100 associated with MTA Bus), and the agencies are authorized to fill another 303 positions by the end of the year. The number of employees in managerial, supervisory, professional, technical, and clerical titles rose by 568 employees between December 2006 and May 2008, and the agencies are authorized to fill another 818 by the end of the year.

The gap-closing program would cut central administration by only 59 employees by the end of 2009, while maintenance employees would decline by 351. (Another 103 positions are scheduled to be eliminated, but the MTA has not allocated the reduction into any specific headcount category.)

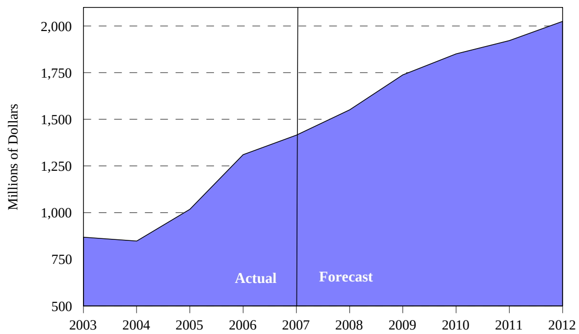
Overall, the July Plan assumes that spending will rise from $10 billion in 2007 to $10.9 billion in 2008—an increase of 9.6 percent—and then grow steadily to nearly $12.8 billion by 2012. This represents an average annual growth rate of 5.2 percent. Moreover, spending will exceed the July 2005 forecast for calendar years 2007 through 2009 by a cumulative total of $1.6 billion.

Major spending trends are discussed below.

Debt Service: Debt service grew from $848 million in 2004 to $1.4 billion in 2007 (see Figure 14)—an increase of 66.9 percent. (In 2007, the MTA made a $297 million debt service prepayment that benefited 2008 by $38 million and 2009 by $283 million.) Debt service will reach $2 billion by 2012—44 percent higher than the 2007 level—just to fund the current and past capital programs, and will average $2.2 billion through 2025. If the MTA were to borrow another $9 billion to help fund the 2010-2014 capital program (an amount similar to the contribution to the current program), debt service would increase by another $600 million annually by 2020.[2]

Figure 14

Debt Service



Sources: Metropolitan Transportation Authority; OSC analysis

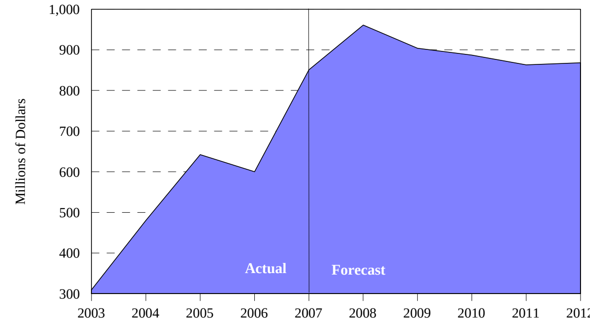
Debt service consumed about 12 percent of total revenues between 1996 and 2005, but will consume more than 20 percent of revenues by 2012—an increase of 75 percent—and 37 percent of fare and toll revenue. Also, for the first time, debt service as a percent of pledged revenue will exceed 50 percent for dedicated tax fund bonds and for Triborough Bridge and Tunnel Authority general revenue bonds.

Pension Contributions: These costs are projected to peak in 2008 at $961 million, which is $652 million more than the 2003 level (see Figure 15). Contributions have grown rapidly to make up for pension fund investment shortfalls, unfunded liabilities, and benefit enhancements. Contributions are projected to decline slightly in 2012, to $868 million. These estimates do not reflect investment performance in 2008, which is likely to fall short of expectations and increase future contributions.

[2] The July Plan assumes that the MTA will borrow $15 billion to help finance the next capital program, and that external resources are identified to fund $11 billion of this amount.

Figure 15

Pension Contributions

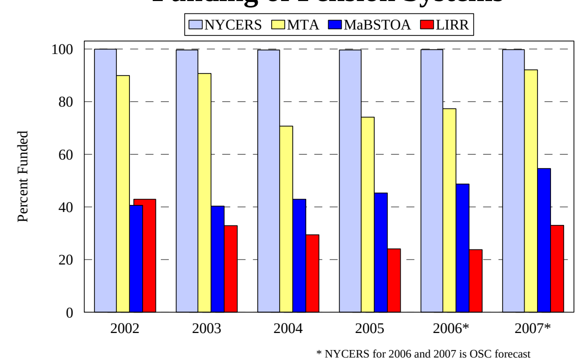


Sources: Metropolitan Transportation Authority; OSC analysis

The New York City Employees' Retirement System (NYCERS) manages the pension funds for the employees of NYC Transit and Bridges and Tunnels. This system is virtually fully funded, assuming an 8 percent return on future investments, but the pension systems managed by the MTA are not as well-funded (see Figure 16).

Figure 16

Funding of Pension Systems



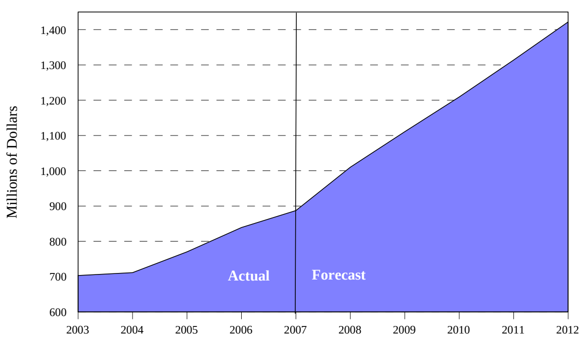
Sources: Metropolitan Transportation Authority, New York City 2007 CAFR; OSC analysis

The MTA pension system, which includes the employees of the seven private bus companies taken over by the MTA in 2006, is 92 percent funded. The pension systems for the LIRR and the Manhattan and Bronx Surface Transportation Operating Authority (MaBSTOA) are far less well-funded. The LIRR pension system has sufficient assets to cover only 33 percent of its accrued liabilities, and MaBSTOA is only 55 percent fully funded. Together, these two systems have unfunded accrued liabilities of $1.9 billion. (These estimates reflect a one-time contribution of $464 million, which was funded with a portion of the real estate transaction tax collection windfall.)

Health and Welfare: These costs are projected to reach $1.4 billion by 2012—double the 2004 level (see Figure 17) because health insurance premiums have risen far faster than inflation. The July Plan assumes that premiums will rise by 10 percent in 2009 (the same as the State rate) and by 7 percent annually during the 2010-2012 period. These estimates include the cost, on a cash basis, of post-employment benefits other than pensions, such as health insurance benefits for retirees. These costs are projected to rise from $270 million in 2007 to $465 million in 2012.

Figure 17

Health and Welfare Costs

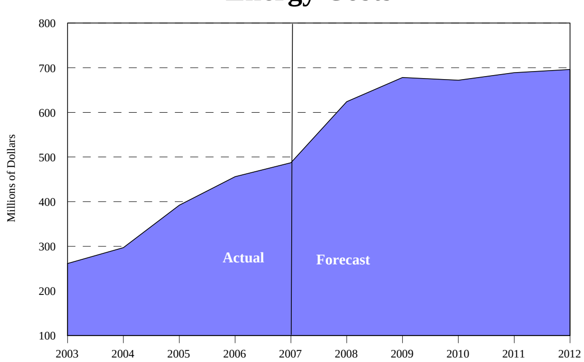


Sources: Metropolitan Transportation Authority; OSC analysis

Energy: These costs have more than doubled over the past five years, growing from $261 million in 2003 to $624 million in 2008, reflecting the higher cost of petroleum products. The July Plan assumes that energy costs will reach $678 million in 2009—39 percent higher than the 2007 level (see Figure 18).

Figure 18

Energy Costs



Sources: Metropolitan Transportation Authority; OSC analysis

The July Plan assumes that oil prices will average $147.60 per barrel during the last five months of 2008—a conservative assumption now that prices have fallen below $100 per barrel—and that prices will average $139.87 in 2009 and $98.58 during the 2010-2012 period. The latest Global Insight forecast suggests that while energy costs may be lower than forecast by the MTA in the short term, costs could be higher during the 2010-2012 period.

Closing the Projected Budget Gaps

The MTA has outlined a gap-closing program that relies heavily on higher fares and tolls, and additional intergovernmental assistance (see Figure 19). The three major components of the program are described below.

1. Higher Fares and Tolls: The MTA proposes to raise fares and toll revenue by 8 percent in July 2009 to raise $202 million in 2009 and more than $400 million annually thereafter. Eighteen months later (January 2011), the MTA would raise fares and tolls by another 5 percent for an additional $272 million in 2011 and $282 million in 2012.

2. Intergovernmental Assistance: The MTA is seeking assistance from its governmental funding: $342 million over the next 18 months, $802 million in 2010, $873 million in 2011, and $955 million in 2012—nearly $3 billion during the entire financial plan period. Most of the assistance would come from the State and City, although the MTA is also seeking some federal assistance.

The MTA has proposed a menu of actions that could be taken by the State and local governments, including higher reimbursement rates for services provided at their request (e.g., reduced-fare services for schoolchildren and paratransit), and tighter tax codes. Although the MTA did not specify the source, it has suggested that the State create a new revenue stream for the MTA that would generate $364 million beginning in 2010.

3. Internal Actions: The gap-closing program assumes that MTA internal actions (described below) will generate $465 million in savings over the next 18 months, $411 million in 2010, $225 million in 2011, and $361 million in 2012—a total of nearly $1.5 billion. More than one third of this amount remains unspecified, and more than one fourth is nonrecurring.

2006 Surplus Recovery: In 2006, the MTA set aside $150 million of the 2006 surplus in an off-budget account to fund capital security projects and other nonrecurring expenses. The MTA reports that it has not committed $120 million of these resources, and it now intends to use those funds to help balance the operating budget. In 2007, the MTA set aside

$150 million to prefund energy contracts. To improve transparency, the State Comptroller recommends that the MTA deposit surplus resources into a Fare Stabilization Account, which would remain part of its financial plan, and that the MTA draw down the resources as commitments are made.

OPEB Loan: Like New York City, the MTA has taken prudent steps to pay down its unfunded liability for post-employment benefits other than pensions (known as OPEBs). While the MTA had previously planned to reserve $500 million by the end of 2010 for this purpose, the MTA now plans to borrow $270 million of this amount to help balance the budget in 2009 and 2010. Although the July Plan assumes that the $270 million will be repaid by the end of 2012, the State Comptroller believes that to draw upon these resources—which were intended to improve the MTA's long-term financial position—before exhausting other options is ill-advised and short-sighted. (The MTA faces an estimated unfunded liability of $13.4 billion.)

The July Plan also assumes that $117 million from the OPEB reserve will be used to reimburse NYCERS and MaBSTOA for refunds to certain employees pursuant to the labor agreement with the Transport Workers Union and State law. NYCERS has already amortized the cost, and in the opinion of the City Actuary, there is no statutory authorization that would permit the MTA to make the planned $99 million reimbursement to NYCERS.

2009 Agency Program: The agencies expect to save $98 million over the next 18 months and about $80 million in each subsequent year (about twice the size of last year's program). More than half of the savings would come from changes in subway, bus, and LIRR maintenance practices, which would eliminate about 351 jobs. Although these actions are not intended to affect services, they could have unintended consequences. Subway service has already deteriorated when measured by on-time performance; by the average mean distance between failure (which declined by 12 percent in 2006 and by another 4.5 percent in 2007); and by a recent survey performed by the Straphangers Campaign. Administrative actions would save $20 million annually and would eliminate 62 positions.

In 2006, the MTA realized only $12.3 million in savings from monitored management actions—59 percent less than anticipated—and achieved another $24 million in 2007—25 percent less than anticipated. The 2008 cost-reduction program, which is also modest at $36 million, fell 20 percent short of its first-quarter target. In 2006, for example, the MTA failed to obtain $12 million more in lease payments for its right of way.

2010 Agency Program: MTA agencies will reduce controllable expenses by 1.5 percent each year for annual savings of $275 million beginning in 2012. The MTA has identified only $1 million in savings so far.

Figure 19
MTA Gap-Closing Program
(in millions)

	2008	2009	2010	2011	2012
Accrual Forecast	**$ (684)**	**$(1,123)**	**$ (1,794)**	**$ (2,045)**	**$ (2,316)**
Cash Adjustments	397	42	(24)	44	53
GASB Cash Contribution	(58)	(62)	(64)	(67)	(70)
2007 Cash Carry-Over	495	- - -	- - -	- - -	- - -
Current-Year Cash Forecast	**150**	**(1,143)**	**(1,882)**	**(2,068)**	**(2,333)**
Internal Actions:					
2006 Surplus Recovery	120	- - -	- - -	- - -	- - -
2009 Agency Program	16	82	80	88	79
2010 Agency Program	- - -	- - -	97	174	275
OPEB Loan	- - -	135	135	(135)	(135)
Labor Contribution	- - -	53	82	85	86
Other Actions	18	40	17	13	56
Subtotal	**155**	**310**	**411**	**225**	**361**
Intergovernmental Aid	**40**	**301**	**802**	**873**	**956**
Higher Fares and Tolls	**- - -**	**202**	**405**	**687**	**699**
Total Gap-Closing Program	**194**	**813**	**1,618**	**1,785**	**2,016**
Cash Transfer	- - -	344	15	- - -	- - -
Net Cash Surplus/(Deficit)	**$ 344**	**$ 15**	**$ (250)**	**$ (283)**	**$ (318)**

Sources: Metropolitan Transportation Authority; OSC analysis

Labor Contribution: The July Plan assumes that wages will increase by 2 percent annually based on an inflation projection for the metropolitan region that was performed by the forecasting service Global Insight in May 2008. The July Plan further assumes that the MTA's unions will agree to a wage increase of one half of the projected inflation rate in the first year of a new contract, which will generate savings of $53 million in 2009 and about $85 million in subsequent years. Inflation has been growing faster than expected due to higher energy and food prices. In fact, Global Insight recently raised its inflation forecast to 5 percent in 2008 and 3 percent in 2009.

Other Actions: The MTA has proposed the following actions that would yield a net of $58 million over the next 18 months, $30 million in total during 2010 and 2011 and $56 million in 2012.

- *Business Service Center:* Spend $210 million during the financial plan period (including $145 million for consulting fees) to create a business service center that would streamline certain adminstrative operations, such as human resources transactions, payroll, and some accounting transactions. While the MTA will realize benefits beginning in 2009, the first savings ($29 million) are not expected until 2012—eight years after the State Comptroller identified the potential for such savings.
- *MTA Reorganization:* Review other back-office operations to generate additional savings of $3 million in 2009 and $13 million annually thereafter. The MTA was unable to document the savings estimates for this initiative.
- *Recapture E-ZPass Revenues:* Charge City, State, and county vehicles for bridge and tunnel crossings to generate $10 million annually.
- *Long Island Bus:* Obtain $4 million in annual subsidies from Nassau County, which have gone unpaid in the past.
- *Other Administrative Reductions:* The MTA would save $15 million in 2008 and $30 million in 2009 by slowing hiring and by reducing nonrevenue vehicle mileage and costs for travel, catering, professional memberships, subscriptions, and telecommunications. The MTA, however, could not document the savings estimate or the impact on services. The initiative will not generate any recurring savings.

Risk Assessment

Our review concludes that while the MTA presented reasonable estimates of its projected budget gaps in the July Plan, the gaps have grown by $381 million now that the State has lowered its forecast of dedicated transit taxes. Moreover, the gap-closing program is inherently risky because it relies so heavily on actions outside of the MTA's direct control.

Aside from higher fares and tolls, only a small portion of the gap-closing program (23 percent) is within the MTA's direct control, and the internal actions proposed by the MTA are modest in size and most remain unspecified. The MTA also has a record of falling short of its cost-reduction targets.

In addition, the July Plan's assumption of limiting wage increases to 1 percent in the first year of a new contract and to 2 percent in subsequent years will be difficult because of growing inflationary pressures and recent agreements between the City and its unions, which granted relatively generous wage increases. The labor agreement with the Transport Workers Union, the MTA's largest union, expires on January 15, 2009.

Our review finds that the remaining budget gaps could total $522 million in 2009, $1.4 billion in 2010, $1.6 billion in 2011, and $1.8 billion in 2012 (see Figure 20). In addition, the July Plan includes a general reserve of only $38 million in 2008 and $75 million annually thereafter (0.7 percent of revenue). New York City, in contrast, has reserves of $1.1 billion in the current fiscal year (2.7 percent of City fund revenue).

Figure 20
OSC Risk Assessment
(in millions)

	2009	2010	2011	2012
MTA Forecast	**$15**	**$(250)**	**$(283)**	**$(318)**
OSC Risk Assessment:				
Intergovernmental Aid	(341)	(802)	(873)	(956)
Tax Revenue	(139)	(77)	(86)	(78)
Labor Savings	(53)	(82)	(85)	(86)
Internal Actions:				
Specified	(32)	(37)	(39)	(37)
Unspecified	- - -	(97)	(174)	(275)
Energy Costs	28	(36)	(51)	(65)
Subtotal	**(537)**	**(1,131)**	**(1,308)**	**(1,500)**
Remaining Gap	**$(522)**	**$(1,381)**	**$(1,591)**	**$(1,818)**

Financing the Capital Program

The way the MTA finances its capital program has a direct impact on the operating budget. In the past the MTA has relied heavily on borrowing to finance its capital program because the State reduced its direct support and because extraordinary sources of funding, such as from the sale of the New York Coliseum, dried up.

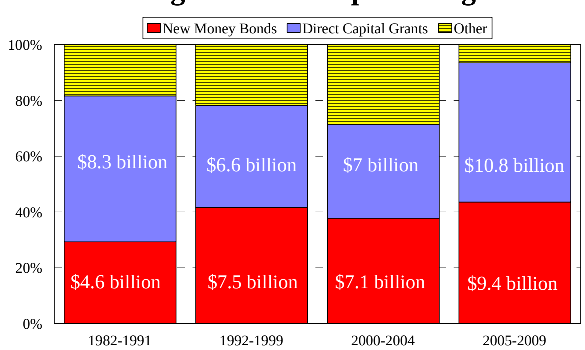
The State contributed $2.4 billion during the 1982-1991 period, but only $104 million in the 1992-2004 period. (The City has contributed less than $100 million each year since 2000, although the contributions in prior years were more generous.) The federal contribution, in contrast, has more than doubled, from $4.2 billion in the 1982-1991 program to $8.9 billion in the 2005-2009 program.

To help finance the 2000-2004 program, the MTA embarked on the largest public debt restructuring in history at that time. The MTA saved $2.8 billion in debt service from 2003 through 2015, but will incur $8.6 billion in higher costs from 2016 to 2032.

The MTA is also depending more on new money bonds to finance its capital needs (see Figure 21). The 2005-2009 capital program relies on new debt to finance $9.4 billion (43.6 percent) of the program—more than twice the amount that financed the 1982-1991 program ($4.6 billion). Since 2000, the MTA has issued $16 billion in debt and plans to issue another $9 billion in support of the current capital program by 2016.

Figure 21

Financing the MTA Capital Program



Sources: Metropolitan Transportation Authority; OSC analysis

The MTA is counting on the sale of real estate assets to generate $1 billion to help finance the 2005-2009 capital program. The MTA has entered into three agreements that have the potential to generate $1.3 billion, but details, including the timing of proceeds, still need to be worked out. The MTA should fully explore opportunities to maximize the return from under-utilized assets.

The current capital program has been characterized by cost overruns and delays, particularly in expansion and new technology projects (see our report 11-2008, *Metropolitan Transportation Authority: Proposed 2008-2013 Capital Program*, for details). The MTA had proposed deferring $2.7 billion in projects from the current capital program, but the proposal was recently withdrawn from consideration by the State Capital Program Review Board.

In February 2008, during the debate over congestion pricing, the MTA proposed a $32 billion capital program for the 2008-2013 period to continue restoring the transit system to a state of good repair; complete existing expansion projects, such as East Side Access and the first phase of the Second Avenue Subway; and to begin new expansion initiatives, such as the next phase of the Second Avenue Subway. Continuing to restore the existing system to a state of good repair must be the first priority, but expanding the system to meet future needs is also critically important.

The proposed program, however, had a funding gap of $13.8 billion. While proceeds from congestion pricing would have reduced the gap to $9.3 billion—still too large for the MTA to finance on its own—the program did not progress after congestion pricing failed to win approval.

The Governor recently appointed a 13-member commission to identify new sources of funding to help finance the MTA's operating and capital budgets over the next ten years. Suggestions for consideration have included tolling the East River bridges; congestion pricing; a millionaire's tax; and collecting taxes on cigarettes sold on Indian reservations. The commission is expected to report its findings by December 5, 2008.

The MTA is accelerating its capital planning process so the commission will have the benefit of an updated 20-year capital needs assessment and a proposed capital program for 2010-2014. The next capital program is expected to have a funding gap of at least $15 billion.

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Office of the State Comptroller, New York City Public Information Office
633 Third Avenue, New York, NY 10017
(212) 681-4840