IBO

New York City Independent Budget Office

Inside the Budget

NewsFax

Number 112 January 16, 2003

NYC Transit's Budget Gap: Reviewing the Numbers

Forthcoming from IBO...

Budget Options for New York City

...a new edition

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NYC Transit, a component agency of the Metropolitan Transportation Authority (MTA), faces an estimated budget gap of $235 million in calendar year 2003 and $476 million in 2004, according to an IBO review of publicly available MTA financial documents, including the recently-released MTA-Wide Financial Plan for 2002-2004. The financial plan also indicates that NYC Transit's budget gap comprises nearly the entire MTA gap in 2003 and two-thirds of its 2004 gap. The commuter railroads effectively face no budget gap in 2003, and a $240 million gap in 2004. The MTA has proposed three broad options for closing its budget gap, all of which include an increase in the basic subway and bus fare to either $1.75 or $2.00 as well as commuter railroad fare increases.

MTA gap projections. The MTA-Wide Financial Plan 2002-2004, released last month, projected a budget gap of $1.085 billion in 2003 and $1.699 billion in 2004 for all of the MTA. These figures were widely reported in the press. But these were projections of the budget gap *before* taking the steps outlined in the financial plan to confront the shortfall. Following its plan for debt restructuring and cost-cutting, the MTA estimated its remaining gap—before any fare increases—to be $236 million in 2003 and $716 million in 2004.

Some observers have wondered why the agency, which had been in sound fiscal position in recent years, seemed to so quickly develop any shortfall at all.

In fact, the budget for 2002 would have had a significant gap if not for a series of extraordinary measures. Most notable among these was the commitment of the Governor and the state Legislature to plug any gap remaining after other revenue-enhancing and cost-cutting measures were taken. The aid came in the form of what is known in budget circles as a "spin up"—advancing the schedule of state aid payments. The spin up provided roughly $350 million of additional revenue to close the anticipated shortfall in 2002: $250 million for NYC Transit, and $100 million for the commuter railroads.

Revenue and expense estimates. Driving the MTA's shortfalls are stagnant fare revenues and subsidies and steadily increasing labor and debt service costs.

Total NYC Transit revenues are projected to increase 2.1 percent in 2003, and scarcely at all in 2004. With no fare increase, NYC Transit fare revenues are actually projected to decrease slightly in 2003, and rise by 0.6 percent between 2002 and 2004. Fare revenues for the commuter railroads are projected to do better—up by 2.8 percent and 2.5 percent respectively in 2003 and 2004. Total revenues for the commuter railroads, however, are forecast to increase by 5.8 percent in 2003 but then fall by 2.5 percent in 2004.

The main factor buoying 2003 revenues for the transit agencies is the projected rise in surplus toll revenues transferred from MTA Bridges and Tunnels (B&T). NYC Transit is expected to receive $199 million in toll revenues in 2003, $78 million more than in 2002. For the commuter railroads surplus B&T revenues are projected to increase from $166 million to $231 million. By the same token, however, the toll surpluses fall off dramatically in 2004, leading to the overall poor revenue performance.

The reason why the B&T surplus transferred to the transit agencies rises in 2003 and falls in 2004 has to do with the MTA's capital program and debt restructuring. The MTA projects that the total amount of bridge and tunnel toll revenue collected will *decline* by almost 3 percent in 2003. But debt service payments on bonds supported by toll revenues—some of which are used for B&T projects and others for transit and commuter rail projects—are expected to fall even more sharply. This decline in debt service, a result of the MTA's debt restructuring, means that the amount of toll revenue available as a cash transfer to NYC Transit and the commuter railroads increases in 2003. In 2004, the situation is reversed: Toll revenues are projected to increase about 1 percent over the prior year, but rising debt service on toll-backed bonds reduces the amount of the surplus available for transit.

Projected Revenues and Expenses, NYC Transit and Commuter Railroads
Dollar in millions

	2002	2003	2004
NYC Transit			
Fare revenues	$2,131	$2,116	$2,144
Operating assistance	316	316	316
Tax supported subsidies	1,016	1,027	1,195
Bridge and tunnel surplus toll revenues	121	199	0
Other revenues	194	201	211
Total revenues	*3,778*	*3,859*	*3,866*
Labor expenses	2,995	3,125	3,239
Debt service	350	294	436
Other expenses	853	907	867
Total expenses	*4,198*	*4,326*	*4,542*
Total revenues minus total expenses	(420)	(467)	(676)
Adjustment to cash flow balance, including additional state aid	410	217	200
Cash balance from previous year	25	15	0
Ending net cash balance, NYC Transit	**$15**	**($235)**	**($476)**
Commuter Railroads			
Fare revenues	689	708	726
Operating assistance	58	58	58
Tax supported subsidies	519	535	566
Bridge and tunnel surplus toll revenues	166	231	124
Other revenues	254	251	264
Total revenues	*1,686*	*1,783*	*1,738*
Labor expenses	1,162	1,211	1,278
Debt service	161	99	205
Other expenses	774	857	915
Total expenses	*2,097*	*2,167*	*2,398*
Total revenues minus total expenses	(411)	(384)	(660)
Adjustment to cash flow balance, including additional state aid	354	374	420
Cash balance from previous year	67	9	0
Ending net cash balance, commuter rail	**$10**	**($1)**	**($240)**
Total revenues, NYC Transit plus commuter rail	5,464	5,642	5,604
Total expenses, NYC Transit plus commuter rail	6,295	6,493	6,940
Adjustment to cash flow balance, NYCT plus CR	764	591	620
Cash balance from previous year, NYCT plus CR	92	24	0
Ending net cash balance, NYCT plus commuter rail	***$25***	***($236)***	***($716)***

SOURCES: IBO; MTA-Wide FInancial Plan 2002-2004.

Expenses are projected to rise more rapidly than revenues. Both NYC Transit and the commuter railroads project substantial increases in labor costs in both years—4 percent per year for NYC Transit, and 5 percent per year for the commuter railroads.

The MTA's debt restructuring, which was completed last year, has allowed the authority to take advantage of lower interest rates as well as stretch out the payments on existing debt. NYC Transit debt service declines from $350 million in 2002 to $294 million this year. Debt service paid from the commuter railroads' operating budgets falls from $161 million to $99 million. But as the authority begins issuing new debt, debt service rises sharply in 2004.

Simply subtracting total expenses from total revenues gives large deficits for both NYC Transit and the commuter railroads, in 2003 as well as in 2002 and 2004. But when these deficits are adjusted for actual cash flow and the previous year's ending cash balance, a somewhat different picture emerges.

The cash flow adjustment, which lowers the gap, has three components. First, there is an adjustment for the timing of receipts and payments. Second, the MTA includes the additional state aid payments received in 2002 (the spin up) as part of its cash flow adjustment. Finally, in the commuter railroads' budgets there is an adjustment for depreciation. Depreciation is included in total expenses, but it does not involve an actual cash outlay.

The reason for the sharp decline in NYC Transit's cash flow adjustment in 2003 is that the spin up cannot be repeated. The commuter railroads will not receive another spin up, either, but due to the depreciation component their cash flow adjustment is greater in 2003 than in 2002.

When the cash flow adjustment and the previous year's cash balance are applied to "total revenues minus total expenses," the result is an ending cash balance of -$236 million for the MTA in 2003. In absolute value, this deficit is considerably smaller than the $350 million one-time spin up received in 2002. In short, without the spin up the MTA would have had to close an even larger budget gap last year.

Proposed union settlement. When the MTA released a preview of its 2002-2004 financial plan in November 2002, the authority made clear that its expense projections included money for a labor settlement. But actual numbers were not available until the day of the settlement. According to press reports, the recent labor settlement with the Transport Workers Union (TWU) will add up to $400 million to NYC Transit's labor costs over the next two years. NYC Transit has budgeted for a $130 million increase in labor costs in 2003, and a $244 million increase in 2004, for a total of $374 million in additional labor expenses over the next two years. A portion of the budgeted increase will pay for higher pension costs and additional staff to expand service, not for higher pay and benefits. The budgeted increase in labor costs thus appears adequate to accommodate a share of the total contract cost, but not the entire amount.

Additional fiscal considerations. The MTA's financial plan assumes PEGs (Programs to Eliminate the Gap— essentially cost-cutting measures) with a combined savings of just over $1 billion in 2003 and 2004. These PEGs are not explained in detail. Typically the MTA uses "incremental budgeting," and assumes in its baseline budget that current expenses will continue into the future. If a particular expense is nonrecurring, the elimination of that expense in the following year is defined as a PEG. It is likely that the MTA's PEGs include many such nonrecurring expenses that are relatively easy to achieve. But even when spread over two years, $1 billion is a significant portion of the agency's expenditures and the MTA has not released detailed information on how this target will be met.

The MTA projects that the total amount of tax-supported subsidies available to NYC Transit and the commuter railroads will rise from $1.535 billion in 2002 to $1.562 billion in 2003, an increase of 1.8 percent. These subsidies are projected to increase an additional 5 percent in 2004, growing to $1.64 billion. The MTA's forecast of tax revenues used to support transit are generally more pessimistic than those of the city's Office of Management and Budget. The city is expected to revise its projections downward, however.

In addition, the MTA's financial plan anticipates $121 million in increased governmental assistance for NYC Transit in 2004. Given the state and city's current fiscal difficulties, this aid may not materialize.

Fair reporting? The MTA has faced criticism in the past year over its budget and financial reporting practices. Some critics feel that the MTA has presented its budget in a way that, intentionally or not, has confused and misled the public.

IBO's review relies solely on the MTA's publicly available fiscal documents. While the public budget documents present a substantial amount of information on the MTA's projected revenues and expenses, they do not provide details on the assumptions underlying their fiscal projections. Although there have been warnings for over a year that the authority was facing future budget shortfalls (see IBO's April 2001 *NYC Transit: Can It Stay on Fiscal Track?*), an independent evaluation of the assumptions underlying the current projections is not possible without more information.

Responding to the calls for more transparency in the MTA's financial reporting, the City Comptroller's office will conduct an audit of the MTA's books that should provide additional details. A one-time audit, however, is not a permanent solution for the accountability gap that some observers perceive. While interest in the details of the authority's financial condition tends to wane in years when it is not proposing a fare increase, instituting some further requirements for MTA financial reporting now could help avoid a repeat of the recent controversy.

Written by Alan Treffeisen