Proposed Principles for Redirecting Funding to Transit Operations for Emergency Response

Subject: As Bay Area public transit operators continue to face financial uncertainty brought on by the COVID-19 pandemic, MTC staff propose several principles to apply when considering shifting funds normally assigned to other transportation expenditures, to transit operations.

Background: Before the onset of the COVID-19 pandemic, Bay Area transit operators generated and collected about $3.7 billion in annual operating revenues. Passenger fares and sales taxes accounted for approximately two-thirds of those revenues. Ridership, and therefore fare revenue, has remained significantly depressed. As of September, ridership across all Bay Area transit systems remained down 80 percent compared to pre-COVID levels. Sales tax revenues data is lagging but based on preliminary data, this revenue source is faring better than expected regionwide, with the exception of the City and County of San Francisco. Other revenue sources relied on by transit operators such as bridge tolls, parking revenue, and city general funds, are also generating significantly less transit operating funds. Uncertainty related to the timeframe and extent of Shelter in Place orders, social distancing requirements, and continued telework practices make it difficult to gauge both the cost of service provision and when demand for service will return.

While the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) of FY 2019-20 provided a $1.3 billion lifeline, Bay Area transit operators will collectively face an operating revenue loss of between $400 and $600 million by the end of the current fiscal year, and without a substantial improvement in the pandemic facilitating a return of ridership and general mobility, the scale of operating revenue losses could approach $1.7 billion in Fiscal Year (FY) 2021-22.

Bay Area operators continue to react and adjust to changes in revenue and ridership demand. Through varied methods of reducing operating costs, Bay Area operators, with one or two exceptions, will likely be able to meet revised operating budget requirements for FY 2020-21 without making involuntary labor force reductions. In FY 2021-22, in the absence of a significant funding package or alleviation of the pandemic that leads to a sharp rebound in ridership, Bay Area operators will face very difficult decisions including significant service and labor force reductions.

<u>Principles</u>
Given the funding streams at its discretion, MTC does not have the ability to subsidize pre-pandemic transit service levels. At best, MTC may be able to provide flexibility to operators to bridge a temporary gap if a subsequent transit operations funding package appears imminent, or to

reduce the abruptness of the "financial cliff" by providing a glide path for operators as they size service appropriately to ridership demand and available resources, once those are known.

Redirecting funds from one intended investment to another is not without significant complexity and difficult trade-offs. The following proposed Principles (included in full detail in Attachment A) are intended to guide Commission decisions related to providing additional flexibility within transit funding streams, and to determine the appropriateness of shifting funds between modes or from capital to operating expenditures. These principles only apply to fund sources that MTC has authority to redirect and should be considered alongside advocacy efforts to secure federal relief funding.

Staff proposes the following principles be applied when considering the redirection of funds to transit operations:

1. **Provides a "Glide Path"** -- Funding should smooth the transition to a correctly-sized transit system based on service demand and available resources.
2. **Opportunity Costs** -- The benefits of redirecting funds to transit operations should outweigh the disbenefits.
3. **Operator Balance** -- The distribution of funds redirected from transit capital priorities to transit operations or preventive maintenance, should promote fairness among Bay Area operators.

<u>Upcoming Opportunity and Preliminary Recommendation</u>
As the designated recipient of certain Federal Transit Administration (FTA) formula funds for the San Francisco Bay Area, MTC develops the Transit Capital Priorities (TCP) program primarily to replace and maintain in a state-of-good-repair transit vehicles (buses, trains, ferries) and fixed guideway infrastructure. These funds can be used, with certain restrictions and limitations, for transit operations and preventive maintenance expenses. MTC programs over $450 million in FTA formula funds annually as part of the process.

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Opportunity and Constraints:
A key consideration is whether a proposal to shift funding to transit operations is "big enough to matter" and will bring stability to the system(s), given the operating revenue gaps that are foreseen especially for FY 2021-22. Another key consideration is the opportunity cost of any redirection of funding. At an annual amount $450 million, the FTA TCP program has the capacity to meet temporary operating demands, so is appropriately scaled with some constraints. However, it is **not** sufficient to sustain a permanent redirection of capital investments away from critical

state of good repair needs. Staff therefore believes that permitting a redirection of FY 2020-21 FTA federal formula funds could be appropriate given the various considerations **under the following conditions:**

- Any shifting of formula capital funding is **temporary**, and would be pursued to ensure that transit operators have an additional tool to stabilize operating budgets through the end of FY 2020-21, when one of two scenarios are expected to take place:
  - The Federal Government comes forward with continuing emergency relief ("CARES 2") that is financially robust enough, and timely enough, to stave off a cumulative annual operating deficit for FY 2021-22 that could be over $1.5 billion for San Francisco Bay Area transit agencies alone.
  - In the absence of such federal intervention, or one meeting equivalent parameters from the State or other sources, MTC funding permits a more metered glide path to structural service changes, including any workforce adjustments, that fit within budgets sized to economic recovery factors at that point in time.
- The amount of transit capital investment to be shifted on an agency basis will be driven by agency specific conditions, and should be initiated by the agency, within the remainder of FY 2020-21 timeframe outlined.

Taking this into account, staff have developed a proposal to allow for the shifting of TCP program funding to transit operations, as needed to bridge to FY 2021-22, by augmenting this flexibility in the existing TCP policy.

The existing TCP policy includes provisions that allow operators to request preventive maintenance funding to meet budgetary shortfalls, provided certain requirements are met. In recognition of the current crisis, staff proposes to expand that flexibility with special protocols during this emergency, until removed by the Commission. These protocols are intended to allow for a nimble response to operators' potential budget shortfalls. Protocols include:

- Making operating funding eligible in addition to preventive maintenance, as allowed by FTA rules
- Consider special pandemic factors during staff review of operator requests, and in operator demonstration of fiscal need
- Waive requirement for a board-approved "bridging strategy" to sustain financial recovery for future years, as well as the requirement to enter into an MOU with MTC and other affected operators

- Eliminate the limitation on use of this strategy to two years within a twelve-year period.

Under this concept, operators would have the flexibility to use their share of TCP program funds for either capital purposes or transit operations/ preventive maintenance as deemed appropriate. Staff would work with operators to defer or remove capital projects from the FY 2020-21 program for those who elect to use their funds for operations or preventive maintenance.

Transit operators that could take advantage of this flexibility have expressed support for the adaptation it offers, as current budgetary circumstances in the current fiscal year vary significantly. Some rail capital intensive systems see their share of TCP investments as supporting a redirected, retrained workforce to deliver their capital program, and thus maintain jobs. Other operators, the smaller ones in particular, see their original CARES Act allocations as sufficient to get them through this fiscal year without major service disruptions. Other agencies may want to assess their options of using "flexed" TCP funds, but believe their potential TCP shares may give them the room to do that effectively.

Thus, while this concept does not provide the wholesale operations funding relief over an extended period that some interests may hope for, the benefit of this concept is that capital intensive transit systems could elect to retain their capital investment level, and their attendant capital-related jobs; and any election of a temporary shift to operations on an agency by agency basis should impact the region's state-of-good-repair commitments more modestly.

Staff therefore proposes that the Committee approve an overall set of principles for shifting funds to sustain transit operations be approved as outlined in Attachment A.

Furthermore, we believe that modifications to the existing TCP program can be an effective "bridging mechanism" to deploy in these uncertain times; and we request that the Committee direct staff to develop and present a proposed TCP Program Process and Criteria for FY 2020-21 for review and recommendation for Commission approval in January, including the flexible operating provisions as outlined above.

Issues: To create capacity in the TCP capital pipeline sufficient to accommodate a temporary shift of program funds from capital to transit operating, a concurrent successful financing of the BART replacement vehicles is needed. The replacement of 775 BART cars includes a roughly $1 billion commitment from the TCP program. Staff intends to return to the

Commission and/or BAIFA in early 2021 to request authorization for the financing of this commitment based on a Letter of No Prejudice secured through the FTA. The financing would allow the TCP program to pay for the BART cars over approximately 15 years instead of requiring nearly half of all TCP programming over the next five years. For staff to recommend shifting TCP program funds to support transit operations, and ensure a moderated impact on the capital pipeline that includes essential "state of good repair" investments, a financing commitment would need to be in place that smooths out the BART car replacement project's demand on pipeline capacity.

Recommendation: Refer Principles for Shifting Funds to Transit Operations to the Commission for approval.

Attachments: Attachment A: Principles for Shifting Funds to Transit Operations

Therese W. McMillan

Attachment A – Principles for Redirecting Funds to Transit Operations

These principles apply to fund sources that are under the direct authority of the Metropolitan Transportation Commission to program, allocate, distribute or otherwise control; and that such fund sources allow flexibility to direct to transit operations within existing statutory authorities.

1. Use funding to smooth the transition to a transit system based on service demand and available resources. – A re-direction of funding for transit operations would be intended as temporary relief, not an ongoing subsidy. To ease the disruption to agency labor forces and the public, funding should provide a "glide path" to an optimized system, once the availability of future operating resources and the demand for service are better understood. An expected federal funding relief package, a proposed vaccine roll-out plan, or other similar information could be important factors to right-size the system and establish a transition glide path.

2. The benefits of redirecting funds to transit operations should outweigh the disbenefits. – The opportunity costs or trade-offs involved with re-directing funds from their intended usage to transit operations can include, but are not limited to:
    - Capital job losses
    - Safety and reliability concerns if fund source is normally directed to state of good repair purposes
    - Other pandemic recovery strategies including bicycle/pedestrian, mobility, and regional programs and projects
    - Inability to implement Plan Bay Area /Sustainable Communities Strategy goals, priorities and climate objectives, and meet multiple federal performance requirements
    - Inability to fund county priorities including congestion relief and multi-modal improvements; including loss of leveraged state and federal competitive funds

    Further, the degree of impact that a redirection of a specific funding source might have, given the scale of operations funding need, should be considered. An analysis of the relevant costs and benefits should be conducted prior to the redirection of funding.

3. Specific to the federal transit formula funds programmed within the Transit Capital Priorities (TCP) process, the distribution of funds redirected from transit capital priorities to transit operations or preventive maintenance should promote fairness and balance of need across Bay Area operators. – Funds normally used to improve the state of repair of transit capital assets in the region are distributed based on capital rehabilitation and replacement need, limitations posed by federal Urbanized Area (UA) eligibility, and negotiated agreements related to the distribution of formula funds among eligible operators within UAs. Funding redirected from transit capital priorities to transit operations for any particular operator, should be treated as an advance against future funding shares for that operator.