Memorandum

MIAMI-DADE COUNTY

Date: September 2, 2008

Agenda Item 12(B)1

To: Honorable Chairman Bruno A. Barreiro
and Members, Board of County Commissioners

From: George M. Burgess
County Manager

Subject: Resolution R-302-08 -Orange Line New Starts Application Review- Interim Status Report

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On March 18, 2008 the Board of County Commissioners adopted Resolution No. R-302-08, sponsored by Commissioner Dorrin D. Rolle, directing the County Mayor to utilize an independent financial consultant to examine the development of the New Starts North Corridor application. Enclosed is a copy of the subject report as well as the Executive Summary for your review.

Assistant County Manager

Orange Line New Starts Application Review
Interim Status Report Summary

This document provides a summary of the IMG Team's review of the local funding provisions for the proposed Orange Line Phase II – North Corridor Metrorail Extension New Starts application, presented in our Interim Status Report dated April 11, 2008.

On March 18, 2008, a resolution by the Board of County Commissioners directed the County Manager to engage an independent financial consultant to examine the New Starts North Corridor application. The resolution directed the consultant "to examine the capital financial plan, and all supporting documents used to prepare the New Starts North Corridor application, and provide recommendations to secure the required local funding necessary to satisfy the Federal Transit Administration New Starts requirements." The review would need to be completed within fifteen (15) days of the effective day of the resolution.

To fulfill our responsibility we have undertaken the following tasks:

1. Review of the FY 2009 New Starts Financial Plan, submitted to FTA in September 2007, and FTA's Financial Assessment, to determine the specific areas that were highlighted as needing improvement
2. Review of the FY 2008 New Starts Financial Assessment, prepared by FTA in November 2006, to examine differences between the submittal to FTA in September 2006 for the Orange Line Phase 2: North Corridor Metrorail Extension Project and the most recent MDT submittal
3. Examination of available elements of the proposed submittal for July 2008
4. Review of the MDT operating and financial plan
5. Determination of the likelihood that the local funding provisions of the revised submittal would meet FTA criteria
6. Development of recommendations to achieve a satisfactory level of confidence of meeting FTA's criteria for local funding.

To date we have conducted work tasks one, two, and six listed above. Work on the remaining task could not commence because we have not received any draft documentation of the proposed July 2008 submittal. Our Interim report, delivered on April 11, provides more details on the specific findings. The principal conclusions presented in the report are as follows:

We have found that the rating by FTA is not primarily associated with issues regarding the North Corridor, or even the Orange Line, but rather with MDT's financial capacity in several key areas: 1) MDT is operating more service than it can financially afford with its current revenue streams; 2) dedicated PTP tax revenue is being applied to support MDT's existing service and, leaving insufficient funds to support the capital program; 3) MDT does not have a funding source to support its infrastructure replacement program from 2014 and beyond; and 4) the net proceeds of the surtax, after allocations to the

municipalities and Public Works projects, may not be sufficient to support projected levels of transit service and transit capital projects.

In order for our team to fulfill our responsibility we will need to examine the New Starts application that MDT is preparing for submittal to FTA, determine the likelihood that the local funding provisions of the revised submittal will meet FTA criteria, and develop recommendations to achieve an improved rating for the Orange Line Phase 2: North Corridor Metrorail Extension Project.

MDT and its consultants have indicated that they are working on addressing the issues raised by the FTA and incorporating into the new submittal a financial and operational plan that will respond to FTA's concerns. As soon as the draft new application is provided, we will review it and provide a technical memorandum with our findings and recommendations.

MEMORANDUM

TO: Nan Markowitz and Maria Johnson, CITT

FROM: Lou Wolinetz, Infrastructure Management Group

DATE: April 11, 2008

SUBJECT: Orange Line New Starts Application Review – Interim Status Report

This memo summarizes the work conducted to this point on our review of the local funding provisions for the upcoming Orange Line Phase II – North Corridor Metrorail Extension New Starts application. In addition to describing the background and scope of the task, we describe our accomplishments to date, our preliminary findings, and a discussion of the next steps in the project. We are continuing to request and analyze data, and will present our final conclusions in a later document.

The information presented below was the result of work conducted by IMG and Planning and Economics Group. The principal team members from IMG are Sahan Mukherji, Tom Rubin, Sasha Page, and myself. The principal team members from Planning and Economics Group are Isabel Gonzalez-Jettinghoff and Bill Hutchinson.

A. Background and Scope

On March 18, 2008, a resolution by the Board of County Commissioners directed the County Manager to utilize an independent financial consultant to examine the development of the New Starts North Corridor application. The resolution further directed the consultant "to examine the capital financial plan, and all supporting documents used to prepare the New Starts North Corridor application, and provide recommendations to secure the required local funding necessary to satisfy the Federal Transit Administration New Starts requirements." The review would need to be completed within fifteen (15) days of the effective day of the resolution.

The need for re-submittal of the application comes from the medium-low rating provided by the Federal Transit Administration's (FTA) 2009 New Starts Report to Congress for the Orange Line Phase II – North Corridor Metrorail Extension. This rating means that for this cycle the North Corridor is not recommended for funding and therefore cannot proceed to final design. Miami Dade Transit (MDT) will have an opportunity to present a New Starts North Corridor application for review by FTA in July 2008.

To fulfill our responsibility we have undertaken the following tasks:

1. Review of the FY 2009 New Starts Financial Plan, submitted to FTA in September 2007, and FTA's Financial Assessment, to determine the specific areas that were highlighted as needing improvement

2. Review of the FY 2008 New Starts Financial Assessment, prepared by FTA in November 2006, to examine differences between the submittal to FTA in September 2006 for the Orange Line Phase 2: North Corridor Metrorail Extension Project and the most recent MDT submittal

3. Examination of available elements of the proposed submittal for July 2008

4. Review of the MDT operating and financial plan

5. Determination of the likelihood that the local funding provisions of the revised submittal would meet FTA criteria

6. Development of recommendations to achieve a satisfactory level of confidence of meeting FTA's criteria for local funding.

B. Preliminary Findings

To date we have conducted work on the first two of the six tasks listed above. The following paragraphs summarize the activities we have conducted and preliminary findings.

1. Financial Plan

We have found that FTA's conclusions and recommendations relating to MDT's FY 2009 New Starts submission are largely similar to those of the FY 2008 submission.

Yet, the FY 2009 application received a "medium-low" rating as opposed to the "medium" rating received by the FY 2008 submission.

The key concern behind the "medium-low" rating by FTA is MDT's financial capacity or its ability to continue to operate and maintain its existing rail, metromover, STS, and bus service. Operations and maintenance (O&M) costs have been outpacing revenues in prior years, and are expected to increase in the future. The PTP surtax funds have been used in part to fill this gap. Until MDT identifies revenue enhancements and/or cost control measures to balance its operating budget and invest in renewal and replacement of its existing assets, it will be very difficult to convince FTA to invest in additional service.

We found no significant weaknesses with the FY 2009 Financial Plan submittal other than the lack of local financial capability or commitment. Documentation appears to be complete and all key points are addressed. The reason for the "medium-low" rating is a reflection of the financial and operational realities facing MDT. In other words, significant new revenues or reductions in costs will be needed to improve the FTA rating.

The following is a summary of key issues regarding the financial plan:

- **Existing infrastructure funding needs:** One major issue not included in the FY 2008 plan that was added in the FY 2009 update is $1.1 billion in capital expenses for the Infrastructure Replacement Program. MDT did not identify a funding source for this capital expense in the FY 2009 plan.

  Furthermore, this estimate may be understated; conversations with MDT and its consultants revealed that the actual requirement is on the order of $80 to $100 million per year in 2008 dollars. This means costs could reach between $2 and $3 billion in current dollars over the next 30 years.

- **O&M Costs:** Current assumptions show O&M costs rising at lower rates than historical rates. According to the FY 2009 plan, this is achievable only with major reductions in existing service that would reduce ridership 17% by 2011. FTA considers O&M costs in the FY 2009 financial plan to be optimistic.

  It is important to note that service reduction to correct operating deficits is a strong signal that MDT is not in good financial condition and may be unable to fund a major expansion in rail service. Finally, there is little

discussion about how to control or reduce operating expenses. While there are major hurdles to reducing O&M costs, particularly since fuel and labor costs are difficult to control (at least in the short term), a short and long-term plan to control costs would help MDT make its case for Orange Line funding. This plan could include looking at work rules to reduce labor expenses, lower wages and salaries, or outsourcing.

MDT's consultants noted that a key factor for the increase in bus operating costs is that more service will be needed to maintain current headways as traffic congestion increases in the future and bus speeds drop from 12 miles per hour today to about 10 in the future. An alternative to more buses would be fairly modest investments to retain bus speed, such as using signal preference and/or expansion of express/limited stop service.

Another issue is that the 3.5% increase in the County's maintenance of effort (MOE) lags behind the scheduled O&M increase of 4.5% annually.

The financial plan provides for a significant reduction in Metrobus operations from existing levels for several years in the near future and significant increases in Metrorail operations in the out years as the three planned extensions come on line. The operating cost model may be overstating the savings from Metrobus operations reductions in the first years of the plan and overstating the cost of operations from Metrorail operations expansion in the latter years. The basic models for MDT Metrobus and Metrorail operating costs are based on fully allocated cost, or average cost, method of cost estimation; that is, their logic is to take the total cost for Metrobus for a year, divide by the number of units of service provided, such as vehicle revenue hours, and then assume that as service levels change, total costs will change by these factors multiplied by the number of hours added or reduced. In most cases, however, most costs do not change directly proportional to the change in units of service

- **Surtax Revenue Growth:** In the FY 2009 financial plan, FTA considers the projected growth rate of surtax revenues to be slightly optimistic as compared to historical growth. However, in the FY 2008 financial plan, the same average growth rate in surtax revenues was considered by FTA to be reasonable. IMG has previously noted that the growth rates in surtax revenues used by MDT appeared optimistic.

- **New Starts Funding:** The FY 2009 financial plan assumes annual funding of $100 million for 14 consecutive years, an assumption considered by FTA to be optimistic. Even though MDT and its consultants report that FTA has been inconsistent on this point, and has indicated $100 million annually is not unreasonable, it is rare for a transit agency to have two New Starts projects under construction simultaneously. Therefore, we question the likelihood of receiving funding at this level.

- **Revenue Enhancement:** The financial plan includes an aggressive fare increase schedule, with four increases in the next eight years, and then no real increases beyond 2016. The reason for this is to comply with FTA preferences that fare per passenger track inflation over the planning period.

  A second key revenue enhancement is an assumed 15% increase in collections from a new fare collection system MDT is implementing for its rail. No backup is provided for this assumption, which would be strengthened by detailing the experience of other agencies who have implemented the system.

- **Railcar Fleet:** Based on the FY 2009 financial plan, the submission needs to include the most updated assumption regarding whether the existing fleet of railcars will be rehabilitated or replaced. If the decision is to replace, then sufficient funding must be committed and available to purchase the new railcars.

- **Debt Coverage:** According to MDT consultants, the debt service coverage ratio (DSCR) computations reported in the FY 2009 plan are based on gross coverage, meaning that O&M costs are not considered in the computation. The issue with this is that it is not enough to simply cover debt; MDT must also demonstrate funding is adequate to operate the system. A net coverage calculation, while not a legal requirement of bondholders, would provide a more accurate assessment of MDT's projected financial capacity.

- **Financing Costs:** MDT needs to provide detailed analysis to support the financing costs included in the project budget.

- **Traditional Sensitivity Analysis:** MDT needs to provide traditional sensitivity analysis as part of its financial plan submission. A probabilistic analysis was utilized that, while preferred for most purposes, may not provide the information in a format FTA is seeking.

- **Historical Data Presentation:** MDT needs to provide five years of historical data in the same format as the cash flow projection.

It should also be pointed out that since fare elasticity was not explicitly discussed in the financial plan for FY 2009, FTA had mistakenly assumed that no assumption for elasticity was included. Upon review, the IMG Team understands that reasonable fare elasticity assumptions were included in the FY 2009 financial plan and that FTA has been informed. However, this would not change the "medium-low" rating.

2. Operational Plan

Our review of the Orange Line Phase 2 Financial Plan raised issues with the transit operating plan in the design year which had potential financial impacts on both operating and capital costs. We discussed these issues with MDT and its consultants who provided oral responses to our inquiries. To date we have not completed detailed evaluation of this information.

C. Conclusions

In summary, the rating by FTA is not primarily associated with issues regarding the North Corridor, or even the Orange Line, but rather with MDT's financial capacity in several key areas: 1) MDT is operating more service than it can financially afford with its current revenue streams; 2) dedicated PTP tax revenue is being applied to support MDT's existing service, not leaving sufficient funds to support the capital program; 3) MDT does not have a dedicated funding source to support its infrastructure replacement program from 2014 and beyond; and 4) the net proceeds of the surtax , after allocations to the municipalities and Public Works projects, may not be sufficient to support levels of transit service and transit capital projects.

D. Next Steps

The IMG Team is still receiving data and information from MDT and its consultants on the financial and operating plan. In the coming weeks, the IMG team will continue to review this documentation.

In order for our team to fulfill our responsibility we will need to examine the New Starts application that MDT is preparing for submittal to FTA, determine the likelihood that the local funding provisions of the revised submittal will meet FTA criteria, and develop recommendations to achieve an improved rating for the Orange Line Phase 2: North Corridor Metrorail Extension Project.

MDT and its consultants have indicated that they are working on addressing the issues raised by the FTA and incorporating into the new submittal a financial and operational plan that will respond to FTA's concerns. As soon as the new application is prepared we will review it and provide a technical memorandum with our findings and recommendations.