



Board Report

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**FINANCE, BUDGET, AND AUDIT COMMITTEE
FEBRUARY 15, 2023**

SUBJECT: FISCAL YEAR 2024 BUDGET DEVELOPMENT STATUS UPDATE

ACTION: RECEIVE AND FILE

RECOMMENDATION

RECEIVE AND FILE the Fiscal Year 2024 (FY24) Budget Development Status Update.

ISSUE

This is the second in a series of monthly updates to the Board on the FY24 Budget development process, culminating in a planned May 2023 Board Adoption.

BACKGROUND

Metro’s strategic imperatives and priorities established by the CEO and Cabinet leaders will be incorporated into the FY24 Equitable Zero-Based Budget (EZBB) process to help prioritize and benefit our community, including riders, residents, and other stakeholders. In this year’s budget, Metro will strengthen efforts towards providing a reliable, safe, secure, and clean system with strategies and tactical solutions to help protect riders and agency employees. Metro plans to continue to put people and community first while delivering the best-in-class transit service that meets/exceeds customer expectations, maintain capital cost control with effective cost management, and remain financially sustainable with the near-term challenges ahead.

The focus of this report is the following:

- A. Financial Outlook Challenges and the Equitable Zero-Based Budgeting (EZBB) Development Process
- B. FY24 Resource Assumptions
- C. Consumer Inflation and Other Expense Assumptions
- D. Outreach Plan Update

DISCUSSION

A. Financial Outlook Challenges and the Equitable Zero-Based Budgeting (EZBB)

Development Process Update

Transit agencies nationwide face serious challenges as they continue recovering from pandemic-induced changes, struggling to fulfill essential service mandates and return to pre-pandemic ridership levels even after the end of federal stimulus funding. The term “fiscal cliff” is common in the industry and is being discussed as a session topic for the American Public Transportation Association (APTA) Mobility and Rail conferences. Metro is not immune to these financial pressures, making it imperative that every dollar is budgeted and spent wisely. While some transit agencies may be facing immediate fiscal challenges, others may not have the immediate need but are eminent.

In California we are working with transit agencies across the State to address this issue in a comprehensive and collaborative manner. The California Transit Association has gathered agencies together so that we can communicate to the State Legislature the size and scope of the problem as well as urging them to adopt solutions that will ensure the long-term viability of public transit. Through this work the Association will look to implement structural reforms to assist transit agencies and will develop long-term permanent funding solutions.

The federal stimulus funding was essential for transit agencies to continue to provide transit service. For Metro, the funding helped preserve jobs, maintain transit service, and mitigated the loss in fares. At the start of the pandemic, Metro acted quickly and implemented strong cost control measures enabling Metro to maintain financial stability to date. However, with Metro’s federal stimulus funding exhausted and the various efforts to recover from this pandemic ongoing, Metro has financial challenges ahead that require careful prioritization.

The FY24 Budget development process begins with Office of Management and Budget (OMB) estimating the resources available for the upcoming year, taking into account the current economic environment, past historical performance, and projections from leading economic organizations. The budget process will also identify ways to address the heightened security/safety and cleaning efforts as ongoing operational needs as well as plan for sustaining these operational conditions.

The EZBB methodology will help to maintain both an equity focus and cost control pressure on all the services, projects and programs Metro provides. The CEO determines the affordability thresholds by program for the coming fiscal year based on resource availability as well as taking into consideration the near-term financial challenges ahead. The agency is focused on aligning to a common set of strategic imperatives and priorities. Cabinet members will work within their departments and across the agency to evaluate and build their budgets, while considering public comments/feedback. The CEO and leadership team will carefully discuss and make prioritization and tradeoff decisions as necessary. There will also be regular interactions with the Board through Budget Briefings to review each program and any feedback is then integrated into the FY24 Budget before proceeding to the Board for final approval.

As the FY24 Equitable Zero-Based Budget (EZBB) progresses, more detailed budget proposals by program are developed. This month’s report includes the preliminary FY24 Resources Update. The amount of resources available is the starting point in developing the budget. The FY24 Budget is still under development, but we anticipate the areas covered in this report will lead to thoroughly weigh the priorities in curating Metro’s programs and operations in the most optimal way.

B. FY24 Resource Assumptions

Sales Tax Revenues

Metro uses multiple approaches and sources to project and validate estimated sales tax revenues including an economic sector model, regression analysis, long term and short term historical actual receipts, and leading professional forecasts of economic trends.

The local economy and labor market remain strong in the first quarter of FY23, with sales tax receipt actuals at 15% above the Q1 Budget totaling \$271.5 million per ordinance. FY23 Budget is re-estimated from \$1,031.8 million to \$1,158.0 million per ordinance given Q1 actual accounts for roughly 23% of the year-end total historically, a 6.1% projected increase from the FY22 Actual of \$1,091.5 million per ordinance.

To tame decades-high inflation, the Federal Reserve has been imposing aggressive measures to slow the economy and additional interest rate hikes are anticipated in calendar year 2023. Economic growth is expected to respond correspondingly and stabilize from the rapid pandemic recovery growth rates. These assumptions are factored into Metro’s economic sector and regression models which FY24 sales tax revenue projections reconcile closely at \$1,200.0 million per ordinance, a moderate increase of 3.6% from the FY23 Reforecast of \$1,158.0 million. Figure 1 displays Metro’s historical sales tax revenue actuals and latest projections for FY23 and FY24.

Figure 1:

	FY21 Actual	FY22 Actual	FY23 Reforecast	FY24 Assumption
1 (\$ in Millions)				
1 Sales Tax Revenue per Ordinance ⁽¹⁾	\$ 911.7	\$ 1,091.5	\$ 1,158.0 ⁽²⁾	\$ 1,200.0
2 % Change	10.5%	19.7%	6.1%	3.6%

⁽¹⁾ Proposition A , Proposition C, Measure R and Measure M. Transportation Development Act (TDA) sales tax revenue is approximately 50% of the other ordinances.

⁽²⁾ The FY23 Reforecast of \$1,158.0 million per ordinance is 12.2% above the FY23 Adopted Budget of \$1,031.8 million per ordinance.

Figure 2 compares Metro’s historical and current budget estimates to actual receipts and leading regional forecasts. FY24 sales tax revenue projections from UCLA, Beacon Economics and Muni Services are between \$1,103.8 million to \$1,232.4 million per ordinance, and Metro’s estimate of \$1,200.0 million falls within range.

Figure 2:

Sales Tax Revenue per Ordinance Forecast Comparison

(\$ in Millions)

Forecast Source	FY19	FY20	FY21	FY22	FY23 Reforecast	FY24 Assumption
1 Actual	\$ 846.8	\$ 824.7	\$ 911.7	\$ 1,091.5	\$ 1,158.0 ⁽¹⁾	
2 Metro- Adopted	\$ 844.0	\$ 873.0	\$ 778.1	\$ 865.0	\$ 1,031.8	\$ 1,200.0 ⁽²⁾
3 UCLA	\$ 863.6	\$ 838.1	\$ 770.2	\$ 794.4	\$ 1,058.1	\$ 1,103.8
4 Beacon Economics	\$ 835.4	\$ 843.5	\$ 892.3	\$ 896.7	\$ 1,013.4	\$1,091.7 - \$1,232.4
5 Muni Services	\$ 827.7	\$ 868.1	\$ 737.3	\$ 881.7	\$ 1,017.1	\$ 1,145.1

⁽¹⁾ FY23 Sales Tax Revenue per Ordinance Reforecast as shown in Figure 1.

⁽²⁾ FY24 Assumption.

Other Resources

Toll, Advertising and Other

Toll revenues are projected to be \$65.5 million in FY24 which include ExpressLanes usage and violation fees from the existing I-10, I-110. Advertising revenue is expected at \$28.3 million which is based on anticipated contract modifications that will address long-term depressed ad sales from the pandemic impact as well as decrease in commercial sponsorships. Other revenues include bike program, Union Station, park and ride, lease, film, Service Authority Freeway Emergencies (SAFE), auto registration fees, transit court fees, federal Compressed Natural Gas (CNG) tax credit, Low Carbon Fuel Standard (LCFS) credit sales, investment income, and other miscellaneous revenues are anticipated at a total of \$89.2 million in FY24.

Passenger Fares

Passenger fares are assumed to grow as transit ridership continues to increase as the pandemic subsides, some telecommuters return and use transit, service is restored, the homelessness issues and safety on the rail system improve. It is also anticipated that opening of the Regional Connector and the K Lines attracts new fare paying riders.

Passenger fares has been reforecasted to \$118.5 million, based on actual FY23 Q1 and Q2 revenues, which is 10.8% over the FY23 budget. The FY24 budget estimates fare revenues at \$146.8 million. This amount assumes the implementation of the Board approved fare policy changes and fare capping and is planned to launch by Summer 2023. Additionally, Transit operations projects a modest increase in ridership of 3%, which is 72% of pre-pandemic ridership levels.

State Transit Assistance (STA)/Senate Bill 1 (SB1) Revenues

STA and SB1 are sales tax revenues dependent on actual consumption and the price of diesel and gasoline. The FY24 assumption is \$214.6M, which is based on The State Controller’s Office (SCO) February 2023 estimates.

STA funding is partly apportioned by revenue share (qualifying revenues reported by transit

agencies) across the state. The use of federal stimulus funding over the last few years to support transit operations may impact STA apportionments, as these are not qualifying local revenues. Apportionments will be dependent on the use of federal stimulus funding throughout the state and the revised estimates that factor in the qualifying revenues will be available in August, after budget adoption.

Grant Resources

Local, state and federal grant resources are used to support Metro's transit planning, operating, State of Good Repair and construction activities. FY24 includes the first full year of funding from the Federal Infrastructure Investment and Jobs Act (IIJA), which significantly increases federal funding provided by the Fixing America's Surface Transportation (FAST) Act.

Governor Newsom's recently proposed budget is a mixed bag for transportation in general and transit in particular. Outside of increases in federal funds that flow through the state budget, the Governor's proposal provides flat to declining revenues for transit. Advocacy efforts are already underway statewide to highlight the needs of public transit at the state level.

Metro staff continue to aggressively pursue discretionary grant opportunities at both the state and federal levels. Metro's significant local funding can be used as matching funds to leverage our local commitment to continue providing safe and efficient transit operations and maintain momentum on the Measure R and M programs.

Bond Proceeds and Prior Year Carryover

Debt issuance is authorized by applicable federal and state legislation and the local sales tax ordinances. The Board-adopted Debt Policy establishes parameters for the issuance and management of debt that follow best practices and set affordability limits. New debt issuance will be used as a last resort to mitigate the shortfalls in State of Good Repair, transit construction and highway activities.

In FY23, \$1,174.3 million of debt proceeds and prior year carryover are available for transit expansion, highway, State of Good Repair and Transit Improvement/Modernization projects. The debt amounts for FY24 will be determined at a later stage as we finalize the FY24 expense budget and are subject to CEO approval.

Resource Assumption Summary

Refer to Figure 3 below, the 3.6% projected growth in sales tax and TDA revenues are offset by the decrease in federal stimulus funding related to the pandemic. The American Rescue Plan Act (ARPA) is ending in FY23 and no additional federal stimulus funding is assumed in FY24. Line 6 in Figure 3 represents a total decline of 14.6% in overall revenues excluding Grants, Bond Proceeds and Prior Year Carryover.

Figure 3:

Resources (\$ in Millions)	FY23 Reforecast	FY24 Assumption	% Change
1 Sales Tax and TDA Revenues ⁽¹⁾	\$ 5,211.0	\$ 5,400.0	3.6%
2 STA and SB1 Revenues ⁽²⁾	225.6	214.6	-4.9%
3 Passenger Fares ⁽³⁾	118.5	146.8	23.9%
4 Toll, Advertising and Other ⁽⁴⁾	169.0	183.0	8.3%
5 ARPA ⁽⁵⁾	1,239.5	-	-100.0%
6 Subtotal Resources	\$ 6,963.6	\$ 5,944.4	-14.6%
7 Grant Resources ⁽⁶⁾	1,180.7	TBD	
8 Bond Proceeds and Prior Year Carryover ⁽⁶⁾	1,174.3	TBD	
9 Total Resources	\$ 9,318.6	TBD	

Note: Totals may not add due to roundings.

⁽¹⁾ Sales Tax (Proposition A, C, Measure R and M) and TDA Revenues reflect current year revenues only. The percentage change of 3.6% compares the FY24 Assumption of \$1.20 billion per ordinance to the FY23 Reforecast of \$1.16 billion per ordinance. Any (estimated) prior year carryover will be reflected on line 8 which will be revised throughout the remainder of the annual budget process.

⁽²⁾ STA and SB1 STA Revenue estimates from the State Controller's office are reduced by 10% for the revenue base share and population-base share due to anticipated shortfall of FY24 revenue. SB1 SGR revenue estimates from the State Controller's Office is reduced by 5% due to the anticipated shortfall of FY24.

⁽³⁾ The FY23 fare revenues has been reforecasted to reflect the estimated annual FY23 fare revenues, which are based on FY23 Q1 and Q2 actual revenues received. The FY24 amounts assume the implementation of the Board approved Fare Policy changes and assumes a modest 3.0% growth in ridership (about 72% of pre-pandemic ridership).

⁽⁴⁾ Toll, Advertising, and Other FY24 revenue estimates are projected at \$183.0 million, a 8.3% increase from the FY23 Reforecast of \$169.0 million primarily due to extension of federal CNG tax credits for calendar years 2022 and 2023, which offsets the decrease in Advertising revenue and LCFS credit sales.

⁽⁵⁾ No additional federal stimulus funding is assumed in FY24.

⁽⁶⁾ The estimates for FY24 Grants, Bond Proceeds and Prior Year Carryover will be updated when information becomes available.

C. Consumer Inflation and Other Expense Assumptions

Cost Inflation Indicator - Consumer Price Index (CPI)

CPI historical actual and projected growth rates from Metro and regional economic forecasting sources are presented in Figure 4 below. FY23 year-to-date CPI growth rate is 4.59%, a 1.95% decline from the FY22 actual indicating the pace of inflation is slowing. The Federal Reserve has signaled intentions to continue rate hikes into calendar 2023 to tackle the high inflation, and CPI growth is therefore expected to moderate and settle at the UCLA's projection of 3.71% in FY24 (Figure 4). OMB will continue to monitor CPI trends and updates from the economic forecasts as we go through the budget process.

Figure 4:

Annual Change in Consumer Price Index (CPI)

Forecast Source	FY18	FY19	FY20	FY21	FY22	FY23	FY24
1 Actual	3.48%	3.40%	2.48%	2.30%	6.54%	4.59% ⁽¹⁾	
2 Metro	1.75%	2.25%	2.28%	2.30%	2.00%	3.30%	3.71% ⁽²⁾
3 UCLA	2.78%	2.42%	2.60%	2.19%	1.68%	3.78%	3.71%
4 Beacon Economics	2.00%	2.15%	1.83%	2.30%	2.07%	3.86%	2.36%

⁽¹⁾ Reforecasted figure based on FY23 YTD actual. FY23 Adopted Budget is 3.30%.

⁽²⁾ FY24 Assumption.

Other Expenses

Wages and Benefits

Metro's labor and fringe benefit costs will adhere to the respective collective bargaining agreements (CBA).

Growing Cost in Project and Service Deliveries and Other Fiscal Challenges in FY24

Although inflation has been trending down in the recent months, tight labor market, rising demand for goods, and supply chain disruptions continue to push prices in delivery of Metro services and projects above the historical average. Metro also faces other fiscal challenges such as slowing sales tax and other resource growth due to economic slowdown, discontinuation of the federal stimulus funds, higher debt borrowing costs, escalating electrification efforts, heightened security/safety and cleaning efforts, continuation of costs with new lines opening, and incremental costs for new initiatives. These challenges along with the uncertainty caused by the ongoing pandemic have specific financial implications to the available funding for FY24 and may intensify our affordability gap in the near-term. In the upcoming budget development, the trade offs for each program and transit services will be thoroughly reviewed in the monthly reports.

D. Outreach Plan Update

Engaging our customers, key stakeholders and the public through an equitable, transparent, and comprehensive process is vital to fulfilling Metro’s vision and mission. With our goal of continuously improving the budget outreach process, below is a list of engagement and outreach efforts that have been accomplished in addition to those that will be conducted to continue to show how listening and learning from our customers, key stakeholders, and the public is an integral part of the budget development process.

Telephone Town Hall Meetings

CEO Stephanie Wiggins, Chair Najarian, Director Barger, and SLT members participated in the first two Telephone Town Hall meetings on October 18, 2022 and January 17, 2023. One more is scheduled on March 28, 2023. The public is invited to attend to have their questions answered about

the budget and Metro services. Callers provide thoughts that will help influence how Metro will use public funds when developing the Budget.

My Metro Budget

Through a collaborative effort between all departments and OMB, a new interactive “My Metro Budget” public learning and feedback activity was created. This program was hosted on the Finance and Budget portal (<http://budget.metro.net>). Additionally, unique links that were a part of a new marketing approach using QR codes were distributed digitally, on vehicles, and with blue shirts. See: <http://mybudget.metro.net/>. This allowed for the segmentation and later aggregation of data to identify pain points of our riders in regions and commonly across the system. The responses to these questions and comments will provide keen insight to departments on how Metro should shape its FY24 Budget.

Outreach Efforts

This year, an emphasis is placed on marketing that engages with our Equity Focus Communities (EFC) and has yielded more participation from underrepresented communities and riders than previous years. The FY24 Budget development process will continue to be advertised through multiple modes, including the budget portal, e-blasts, social media campaigns, traditional advertising, advertisements aboard Metro vehicles, and flyer distribution by metro station staff, to reach all Los Angeles County residents. See Attachment A for a list of the public forums and media channels that will be utilized.

DETERMINATION OF SAFETY IMPACT

This recommendation will not have an impact on safety standards at Metro.

EQUITY PLATFORM

The FY24 EZBB development begins with the evaluation process that provides flexibility to focus resources on Metro’s core missions, key initiatives, and priorities. Budget Equity is a top priority in the FY24 Budget development as Metro carries out its initiatives and impacts all communities throughout Los Angeles County. Furthermore, the FY24 Budget will align with principles that highlight how public transit can be equitable, sustainable, economically productive, safe, and Americans with Disabilities Act accessible.

The ongoing Metro Budget Equity Assessment Tool (MBEAT) incorporates equity into the development of the FY24 Annual Budget. Staff also incorporated a more detailed geographic equity measure into budget development by conducting EFC Budget Assessments for both the FY23 approved budget and for the FY24 budget finalized later this year. Implementation of MBEAT and the EFC Budget Assessment will assess equity impacts that will identify access to opportunities and reduce potential barriers or harms. Furthermore, it incorporates three of the four pillars of the Equity Platform, specifically “Define and Measure,” “Listen and Learn” and “Focus and Deliver.”

IMPLEMENTATION OF STRATEGIC PLAN GOALS

Recommendation supports the following Metro Strategic Plan Goal:
Goal # 5: Provide responsive, accountable, and trustworthy governance within the Metro Organization.

NEXT STEPS

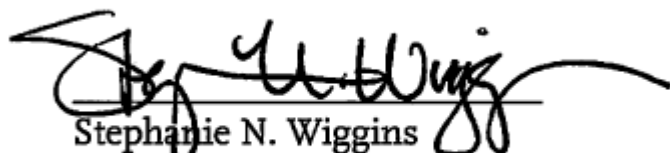
Next month's FY24 Budget process update will address Transit Infrastructure Expansion, Multimodal Highway Investments, Regional Rail, as well as Regional Allocations and Pass-Throughs.

ATTACHMENTS

Attachment A - FY24 Budget Public Engagement and Outreach Forums

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