A REVIEW OF BAY AREA PUBLIC TRANSPORTATION FINANCING

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EXECUTIVE SUMMARY

Since 1974 the Legislature has enacted several measures intended to improve the financial condition of Alameda-Contra Costa Transit (AC Transit), the San Francisco Municipal Railway (MUNI) and the Bay Area Rapid Transit District (BART). When BART began operations in 1973, it was clear that the system would not be able to fund its operating budget entirely from fare revenues. With this in mind, the Legislature enacted Chapter 1417, Statutes of 1974, permitting BART to use revenues from a special 1/2 percent sales tax in Alameda, Contra Costa, and San Francisco counties to fund a portion of its operating costs while the Legislature studied alternatives for addressing the problem on a more permanent basis.

In 1975 and 1977, we issued reports pointing out the need to provide additional financial stability for AC Transit, BART and MUNI. We noted that operating expenses for all three operators were increasing more rapidly than revenues, and were rising more rapidly than prices generally, while fare revenues were not being fully utilized by the three operators as a source of financing for their costs.

In 1977, the Legislature enacted Ch 1204/77 (AB 1107) to promote the financial stability of AC Transit, BART, and MUNI. It did so by (1) making the special 1/2 percent sales and use tax in the three BART counties permanent, (2) providing for the allocation of tax revenues among the three operators, and (3) requiring operators to achieve specified ratios of farebox revenue to operating cost. Specifically, the act allocated 75 percent of the special sales tax revenues--now commonly referred to as AB 1107 funds--to BART in order to provide it with a financial base comparable to what AC Transit and MUNI enjoyed. The Legislature authorized the Metropolitan Transportation Commission (MTC) to allocate the remaining 25 percent of the AB 1107 revenues among all <u>three</u> operators in order to finance <u>service improvements</u>.

Proposition 13/1978, by reducing the amount of property tax revenues available to the three transit operators, threatened to reduce transit services in the Bay Area. In response, the Legislature enacted Ch 264/79 (AB 842), which <u>removed</u> the requirement that MTC allocate the 25-percent discretionary portion of the AB 1107 funds to provide for service <u>improvements</u>. Instead, the act allowed the MTC to allocate these fund to continue vital transit services, using criteria set forth in the MTC's financial management plan and in consultation with the three operators.

<u>The AB 842 Process</u>. MTC has established what has come to be known as the "AB 842 process" (described on page 13) for allocating the 25-percent portion of AB 1107 revenues among AC Transit, BART, and MUNI.

MTC seeks to provide each operator with sufficient resources to maintain current service levels. In the event the resources available to the operators, together with regional funds, are not adequate to achieve this objective, MTC expects the operators to increase fares in a coordinated manner. MTC allocates regional funds <u>assuming</u> that each operator increases fares in line with its coordinated fare recommendation. <u>We believe that this procedure for allocating regional funds is sound, and</u>

that it is consistent with the Legislature's intent to maintain vital transit services.

Nevertheless, we believe that the process can be improved. Lengthening the MTC's planning horizon from one year to five years would assist the operators in developing their annual budgets and short-range plans. Furthermore, by identifying the need for coordinated fare increases well in advance, a five-year plan would give both the operators and the MTC adequate time to carefully consider pricing options and develop the required coordinated fare structure. Finally, by requiring that the plan be consistent with capital commitments, the Legislature would help ensure that the operating costs of planned projects are fundable.

Therefore, we recommend that the Legislature enact legislation requiring the MTC to adopt, and update annually, a five-year financial management plan which identifies committed service levels in each of the five years and is consistent with planned capital improvements in the Regional Transportation Improvement Program. We further recommend that the MTC use this plan as the basis for allocating funds to AC Transit, BART, and MUNI under the AB 842 process.

Financial Projections

To determine whether regional resources are adequate to fund vital transit service levels in the coming years, we compared the projection of operating expenses developed by each operator in its most recent short-range plan with our own projection of revenues.

Assuming that state and federal operating assistance remains at current levels, we project that AC Transit and MUNI will incur an operating deficit during the five-year period 1985-86 through 1989-90. However, if inflation remains at current levels and if the operators restrict growth in operating expenses to the general rate of inflation, the deficit probably would be negligible. In contrast, we project that BART will realize an operating surplus of $46 million during the same five-year period.

It is almost certain that federal operating assistance will be reduced in the future as a result of efforts to reduce the federal deficit. If federal operating assistance were phased out during the next three years, AC Transit and MUNI could face a combined revenue shortfall for the five-year period 1985-86 through 1989-90 totaling $42.9 million more than the deficit projected if federal funding levels remain constant. Adding to this problem, it is likely that the amount of State Transportation Assistance funding available to MUNI and AC Transit each year in the future will be $1 million or more below current levels.

These trends present much more of a threat to MUNI and AC Transit than they do to BART. This is because BART is not dependent upon state and federal operating assistance, though it does depend upon capital assistance.

Options. We discuss six basic options (page 49) for responding to the pending reductions in federal and state operating assistance on which the operators depend:

- The operators could cut their costs of providing service.

- The operators could reduce their services to the public.
- AC Transit could seek financial help from municipalities in its service area (as MUNI has done).
- The Legislature could expand state assistance to transit operators on a statewide basis.
- The Legislature could authorize a surcharge on bridge tolls to fund transit capital or operating needs. Short of this action, the Legislature could make current net toll bridge revenue available for transit operating, as well as capital, purposes.
- The Legislature could reallocate AB 1107 funds.

We recommend that the Legislature enact legislation to : (1) increase the portion of AB 1107 funds that the MTC is able to allocate on a discretionary basis and (2) establish broad priorities to guide the MTC's allocation of these funds.

Given the change in circumstances surrounding Bay Area transit since AB 1107 was enacted (the passage of Proposition 13 and the pending cutbacks in federal operating subsidies), we believe a change is warranted in the way AB 1107 funds are allocated. While the change we recommend would reduce BART's guaranteed allocation (from 75 percent to 65 percent), it would still leave BART with the ability to fund over 95 percent of its operating expenses from its financial base. BART also would be able to compete with the other operators for its share of the increased discretionary amount. More importantly, this change would help to ensure that AB 1107 resources are allocated to fund those services or improvements which are of the highest priority to the region as a whole.

There are at least three potential drawbacks to this change which the Legislature should carefully consider in making its decision.

First, BART has used its 75-percent allocation of AB 1107 funds wisely, and reallocation of AB 1107 funds could be viewed as penalizing BART for fiscal responsibility.

Second, by reallocating funds to AC Transit, the Legislature might weaken the incentives for this operator to (1) identify services and service levels which are truly vital and (2) implement needed restructuring of its routes and services. <u>To avoid this drawback, we recommend that the Legislature direct MTC to consider the extent to which AC Transit has studied and restructured its routes when making its allocation decisions</u>.

Third, our recommended change might weaken the incentives for AC Transit to develop potential sources of local support.

These drawbacks are real and should be carefully considered. Nevertheless, we believe they are outweighed by the benefits to be gained from added flexibility in the allocation of AB 1107 funds. Without this flexibility, the services offered by AC Transit could be imperiled to an unacceptable degree.

INTRODUCTION

On three occasions, the Legislative Analyst's office has reported to the Legislature on the financial condition of the Bay Area Rapid Transit District (BART), the San Francisco Municipal Railway (MUNI), and the Alameda-Contra Costa Transit District (AC Transit).[1] Since our last report, which was prepared in 1980, the level of both state and federal operating assistance to transit agencies has declined. Further reduction in federal assistance appears likely, given the passage of the Gramm-Rudman-Hollings Amendment to the Federal Debt Limit Bill. State assistance also is expected to decline.

The purpose of this report is to review the financial condition of these three Bay Area transit operators in light of recent developments and current trends.

The current report consists of four chapters. Chapter I provides a brief overview of the three operators and discusses the Legislature's past actions to address their financial needs. Chapter II evaluates the extent to which the Legislature's objective of providing financial stability for AC Transit, BART, and MUNI has been achieved and projects the future

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1. AC Transit consists of two special service districts. The provisions of statute discussed in this report pertain only to AC Transit Special Transit Service District 1 (STSD1). Therefore, all references to AC Transit in this report refer to STSD1 unless otherwise indicated.

financial condition of the operators assuming continuation of current levels of state and federal transit funding. Chapter III discusses the impact of anticipated reductions in state and federal funding. Finally, Chapter IV presents our overall conclusions and recommendations.

The report was prepared by Mark Taylor under the supervision of Wayne Keithley.

CHAPTER I

PUBLIC TRANSPORTATION IN THE BAY AREA

AC Transit and MUNI each serve jurisdictions within the larger three county area--Alameda, Contra Costa, and San Francisco--which comprises the BART district.

AC Transit is a statutorily created transit district which provides service within Alameda and Contra Costa counties, as well as transbay service to San Francisco. It utilizes a fleet of approximately 850[1] buses and carries an average of 189,000 passengers daily[2] (69 million per year). The district's financial base consists of revenues from passenger fares, a districtwide property tax, and Transportation Development Act (TDA) revenues.[3] These revenues are supplemented by allocations from the special 1/2 percent sales tax ("AB 1107" funds) which is imposed in the three BART counties, and by other state and federal funds.

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1. In identifying each operator's "financial base" we have included those revenue sources which are directly controlled by the operator (fares, property tax) or which are available for allocation to the operator on a reasonably predictable basis (TDA).

2. Total fleet for Special Transit Service Districts 1 and 2.

3. STSD1 only.

MUNI serves the City and County of San Francisco. It carries approximately 723,000 riders daily[1] (264 million per year) on a vehicle fleet consisting of 527 motor coaches, 341 trolley coaches, 130 light rail vehicles and 41 cable cars. MUNI's primary function is to provide local travel within San Francisco. Unlike AC Transit and BART, MUNI is not a separate transit district; it is a municipal operation under the San Francisco Public Utilities Commission (PUC). As such, MUNI has access to funding from San Francisco's general fund. This revenue source, along with passenger fare revenues and TDA revenues, provides MUNI's financial base. These revenues are supplemented by regional allocations of AB 1107 funds, as well as by other state and federal assistance.

BART is a 34-station, 71-mile heavy rail transit system connecting major communities in Alameda and Contra Costa counties with each other and, via the transbay tube, with San Francisco. BART operates a fleet of 419 rail cars and carries 167,000 passengers per day (61 million per year). We estimate that during the peak hour, BART carries approximately 15,000 passengers into San Francisco through the transbay tube. This is equal to about 62 percent of the number of persons carried on the Oakland-San Francisco Bay Bridge during the same period.

BART's financial base consists of revenues from (1) passenger fares, (2) a statutory allocation equal to 75 percent of the special 1/2 percent sales tax (discussed below) imposed in the three BART counties, and (3) property taxes. These funds are supplemented by minor amounts of TDA and

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1. Boardings.

state operating assistance. BART receives virtually no federal operating assistance. Most revenues derived from the property tax are pledged to meet debt service requirements on long-term general obligation bonds issued by the district. The bonds were issued to pay the costs of constructing BART prior to the commencement of operations.

Past Legislative Action

Since 1974 the Legislature has enacted several measures that were intended to address financial problems faced by AC Transit, MUNI and BART. These problems emerged in 1973 when BART began operation. It quickly became apparent that, contrary to the earlier view of the project sponsors, BART would not be able to fund its operating budget entirely from fare revenues. Consequently, the Legislature enacted Chapter 1417, Statutes of 1974, as an interim measure permitting BART to use revenues from the special 1/2 percent sales tax to fund a portion of its operating costs through 1977. Subsequently, the Legislature studied alternatives for a long-term solution.

Chapter 1204, Statutes of 1977. We issued reports in 1975 and 1977 on Financing Public Transportation in the San Francisco Bay Area. These reports pointed out the need to provide additional financial stability for AC Transit, BART and MUNI. At the time, operating expenses for all three operators were increasing more rapidly than revenues, and were rising more rapidly than prices generally. We pointed out that fare revenues were not being fully utilized by the three operators as a source of financing for the higher costs.

In 1977, the Legislature addressed these problems by enacting Ch 1204/77 (AB 1107). Its primary objective in passing this measure was to promote financial stability for AC Transit, BART, and the MUNI, by (1) making the special 1/2 percent sales and use tax in the three BART counties permanent, (2) providing for allocation of the tax revenues among the three operators, and (3) requiring operators to achieve specified ratios of farebox revenue to operating cost. Specifically, the act allocated 75 percent of the tax revenues--now commonly referred to as AB 1107 funds--to BART. The Metropolitan Transportation Commission (MTC) was given the responsibility to allocate the remaining 25 percent of the AB 1107 revenues among the three operators in order to finance service improvements beyond the levels of transit services provided in January 1978.

As a further step toward achieving financial stability for the three transit operators, the Legislature declared its intent that the operators:

- Stabilize farebox returns,
- Control operating costs, and
- Improve operating efficiency and effectiveness.

To promote these objectives, Ch 1204 required that each operator achieve a ratio of farebox revenues to operating costs equal to at least 33 percent in order to receive AB 1107 revenues. (This provision was amended by Ch 264/79 so as to require that the three operators jointly achieve a 33 percent farebox ratio. Still later, Ch 115/85 allowed operators in calculating farebox ratios to count as fare revenues increases in local contributions.)

Chapter 1204 imposed the further requirement that each operator participate in a transit operator coordinating council which the MTC established to coordinate routes, schedules, fares, and transfers among Bay Area transit operators and to explore the potential for joint ventures in such areas as marketing, maintenance and purchasing.

Chapter 264, Statutes of 1979. Proposition 13/1978 (Article XIIIA of the California Constitution) reduced the amount of property tax revenues available to the three transit operators. (In the case of MUNI, the reduction took place indirectly, through the measure's effect on San Francisco's general fund.) These revenue losses threatened to bring about a reduction in transit service within the entire Bay Area.

In response, the Legislature enacted Ch 264/79 (AB 842). This act was intended to "continue vital transit services." Specifically, AB 842 removed the requirement that MTC allocate the 25-percent discretionary portion of the AB 1107 funds to provide for service improvements. Instead, it allowed the MTC to allocate these funds to continue vital transit services, using criteria set forth in its financial management plan and in consultation with the three operators. As a result, MTC has established what has come to be known as the "AB 842 process" for allocating the 25-percent portion of AB 1107 revenues among AC Transit, BART, and MUNI.

The MTC Role and the AB 842 Process

The Metropolitan Transportation Commission (MTC) is a nine-county regional agency established by Chapter 891, Statutes of 1970, to provide comprehensive regional transportation planning and project programming for the Bay Area. It is responsible for updating on an annual basis the regional transportation plan and for approving transportation projects--including highway and transit projects--proposed for the region. In addition to these planning and programming duties, MTC is responsible for allocating funds that are derived from a variety of sources for transportation operating and capital outlay purposes. Of primary significance in this context are the funds allocated from the following sources:

- The Federal Urban Mass Transportation Act (UMTA).
- The State Transportation Assistance Program (STA).
- The State Transportation Development Act, local transportation funds (TDA).
- Certain net toll bridge revenues (discussed below) for capital purposes only.
- The AB 1107 discretionary funds (25 percent portion of 1/2 percent sales tax in BART counties).

In addition to pursuing its primary objective of maintaining vital transit services, MTC has sought to achieve the following secondary objectives through the AB 842 process:

- To establish and maintain a coordinated fare structure among the three operators.
- To encourage efficiency and effectiveness of transit services.
- To utilize fare revenues as an important source of operating revenue.

o To maintain local tax contributions as a source of operating revenue.

To guide the AB 842 process, MTC has established an AB 842 Policy Committee consisting of policy representatives from each operator and the MTC Commissioners from each BART county (two commissioners per county).

AB 842 Allocation Procedure. In making 25 percent of the AB 1107 funds available to "continue vital transit services," the Legislature did not provide specific criteria to guide the allocation of the funds. Consequently, the MTC, using the AB 842 process, has adopted criteria which consider vital transit services to be the committed service level--that is, the level of services provided, or to which the operator was committed--as of July 1979. The level of services is measured in terms of the total revenue vehicle miles or revenue vehicle hours supplied to the public by each operator. MTC staff indicate that, in the future, the AB 842 Policy Committee will recommend annual amendments to the "vital transit service" level as appropriate. The procedure which MTC uses to allocate AB 1107 funds is basically as follows:

1. MTC staff estimates the amount needed by each operator to provide the defined level of "vital transit services." It does so by determining the operator's eligible expenses as shown in its latest audited report, and then increasing this amount using rates adopted by the AB 842 Policy Committee.

2. If the three operators' resources, including available regional, state, and federal assistance, are not sufficient to fund the expenditure

requirements, MTC staff propose a coordinated fare increase to fund the aggregate deficit.

3. Regionally allocated funds--TDA, STA, and UMTA funds--are allocated to the operators, based on statutory requirements and MTC policy.

4. AB 1107 funds are allocated to each operator as needed to fully fund estimated operating needs on the <u>assumption</u> that each operator raises fares and achieves fare revenue increases as anticipated by the AB 842 Committee.

CHAPTER II

FINANCIAL STABILITY OF THE TRANSIT OPERATORS

In this chapter we examine the extent to which the Legislature's objective of providing financial stability for AC Transit, BART and MUNI has been achieved. We look in turn at (1) farebox ratios, (2) operating cost trends, (3) indicators of operator efficiency and effectiveness, and (4) the ability of operators to maintain "vital transit services." We also consider the ability of each operator to finance operating costs from its "financial base," as defined in Chapter I.

Farebox Ratio

Prior to the enactment of AB 1107, AC Transit and MUNI experienced a significant decline in farebox revenues as a percentage of operating costs. Between 1972-73 and 1977-78, fare revenues as a percentage of total operating costs declined from 58 percent to 27 percent for AC Transit, and from 51 percent to 32 percent for MUNI. BART, which began operations in 1973-74, saw its farebox ratio rise from 18 percent to 36 percent by 1977-78.

During this period, both the controllable and noncontrollable operating costs incurred by AC Transit and MUNI increased at rates exceeding the inflation rate. It is evident, however, that the governing boards of these two operations were reluctant to increase fares in order to finance their increased costs. Much of this reluctance undoubtedly stemmed from the growth in federal and state operating and capital subsidies which occurred during the 1970s.

In AB 1107, the Legislature required each of the three operators to maintain a ratio of fare revenues to operating costs exceeding 33 percent in order to be eligible for revenues from the special 1/2 percent sales tax. This requirement was relaxed by AB 842, which permits the MTC to allow a credit of up to 5 percent on the farebox ratio requirement for any operator when the MTC determines that "special operating characteristics," such as transfer or special fare policies, warrant such a credit. The act required, however, that the combined farebox ratio for the three operators be at least 33 percent, even though each individual operator no longer had to achieve this ratio.

Under provisions of Chapter 115, Statutes of 1984 (AB 2337), MTC also may consider increases in local support as "fare revenues" for purposes of calculating an operator's farebox ratio if the commission finds that this will enable the operator to maintain or improve vital transit services within a coordinated fare structure. This provision became effective on July 1, 1984.

Table 1 summarizes the performance of each operator since 1979 in attempting to achieve a stable ratio of fare revenues to operating costs.

Table 1

Farebox Revenues as a Percentage of Total Operating Costs
1978-79 to 1984-85

	AC Transit	BART[a]	MUNI	Total
1978-79	39.4	24.5	31.2	30.1
1979-80	38.0	22.0[b]	32.3	29.3
1980-81	37.6	35.1	36.1	36.0
1981-82	32.3	36.4	30.5	33.1
1982-83	37.4	39.9	31.0	35.7
1983-84	37.8	39.7	29.3	34.7
1984-85	33.8	37.8	27.2[c]	32.5

a. Operating costs include interest expense on debt. Excluding such expenses, BART's ratio was 45.9 percent in 1984-85.
b. Reflects work stoppage September 1 - November 25, 1979.
c. Under Ch 264/79, MUNI's required farebox ratio is 28 percent. Ch 115/84 allows increases in local revenue above the base level, as determined by MTC, to be counted as farebox revenue for purposes of calculating the farebox ratio.

Since passage of AB 1107, AC Transit's farebox ratio has been stabilized, and BART's farebox ratio has increased. The farebox ratio of MUNI, however, has been allowed to decline in accordance with the provisions of AB 842 and AB 2337 discussed above. The reduction in MUNI's farebox revenues has been offset by increases in MUNI general fund support.

Operating Costs

Although the primary reasons for the decline in farebox ratios appear to be the operator's increased dependence on federal and state operating subsidies and their reluctance to raise fares, rapidly rising operating costs also contributed greatly to the decline. Prior to passage of AB 1107, the operating costs for the three Bay Area transit operators were increasing at rates substantially greater than the rate of increase in the Bay Area consumer price index (Table 2).

Table 2

Growth in Transit Operating Costs Prior to Passage of AB 1107
1972-73 through 1977-78
(dollars in millions)

	1972-73	1977-78	Percent Increase
AC Transit	$25.9	$50.2	94.6%
BART	--[a]	78.2	130.6[b]
MUNI	48.9	79.1	61.8
Bay Area CPI	--	--	47.9

a. BART commenced operations in 1973-74 with operating costs of $33.9 million.
b. Increase from 1973-74 through 1977-78.

As noted in our 1980 report, "Financial Stability of Bay Area Transportation," some of the increase in operating costs during this period was due to expansions in service. Nevertheless, we concluded that "even allowing for such expansions...operating costs were rising at a rate faster than the rate of inflation." In particular, we found that salaries and wages, which constituted between 60 and 70 percent of transit expenditures, were growing faster than the CPI. While the Bay Area CPI increased by 48 percent between 1972-73 and 1977-78, the top hourly wage rates of (1) AC

Transit bus drivers increased 63 percent, (2) BART train operators increased 92 percent, and (3) MUNI operators increased between 46 percent and 62 percent, respectively.

Table 3 presents data on the growth in operating costs during the period since enactment of AB 1107.

Table 3

Growth in Transit Operating Costs After Passage of AB 1107
1980-81 through 1984-85
(dollars in millions)

	1980-81	1984-85	Percent Increase
AC Transit	$70.2	$89.6	27.6
BART[a]	103.3	147.1	42.4
MUNI	126.3	204.6	62.0
Bay Area CPI[b]	251.9	327.5	30.0

a. Excludes interest expenses on outstanding debt.
b. As measured in October.

The table shows that between 1980-81 and 1984-85, AC Transit operating costs grew at a slower rate than the CPI. During the same period, BART operating costs grew by 42 percent, or about 1.4 times the rate of inflation, and MUNI costs grew by 62 percent, or about twice the increase in prices.

The increase in operator costs directly reflect the increase in wage, salary and fringe benefit costs. During the period 1980-81 through 1984-85, these costs rose 21 percent, 52 percent, and 58 percent, respectively, for AC Transit, BART, and MUNI.

Efficiency and Effectiveness

One of the Legislature's goals is to promote efficiency and effectiveness in the delivery of transit services by the three Bay Area operators. Table 4 provides two measures of the operators' progress in achieving these goals.

Table 4

Trends in Operator Cost Efficiency
1980-81 through 1984-85

	1980-81	1981-82	1982-83	1983-84	1984-85	Percent Increase 1980-81 to 1984-85
Cost per vehicle hour						
AC Transit	$37.45	$43.26	$44.84	$44.81	$47.87	27.8
BART	100.29	113.05	117.57	122.94	130.92	30.5
MUNI	42.14	50.91	54.44	58.65	69.75	65.5
Cost per passenger						
AC Transit	0.93	1.05	1.16	1.18	1.28	37.6
BART	2.10	2.18	2.30	2.37	2.42	15.2
MUNI	0.49	0.54	0.55	0.54	0.78	59.2
Bay Area CPI	251.9	297.0	302.4	305.7	327.5	30.0

Source: Metropolitan Transportation Commission and Department of Commerce, Bureau of Labor Statistics.

The table shows that both AC Transit and BART have held increases in the unit cost of providing transit service--as measured by cost per vehicle hour of service--to a rate which is below the rate of growth in consumer prices during the period 1980-81 through 1984-85. Thus, the real, or inflation-adjusted, unit costs of these operators has fallen since 1980-81. In contrast, AC Transit's cost per passenger has increased in both nominal and real terms, as a result of reduced ridership. Because BART's ridership has been growing, its nominal costs per passenger has grown by only 15.2 percent, which translates into a substantial reduction in inflation-adjusted dollars.

Both MUNI's cost per vehicle hour and its cost per passenger increased during the 1980-81 through 1984-85 period. Since there was little change in ridership or service hours between the beginning and end of the period, these increases simply reflect the growth in MUNI's operating costs (discussed above).

Table 5 indicates trends in the effectiveness--or the degree of utilization--of each operator's services, as measured by the number of passenger boardings and passengers per vehicle hour of service.

Table 5

Trends in Operator Effectiveness
1980-81 through 1984-85

	1980-81	1981-82	1982-83	1983-84	1984-85	Percent Increase 1980-81 to 1984-85
Passenger boardings (millions annually)						
AC Transit	75.3	76.1	70.6	68.7	69.0	-8.4
BART	49.2	54.4	54.8	56.5	60.8	23.6
MUNI	254.5	281.3	298.5	313.1	264.0	3.7
Passengers per vehicle hour						
AC Transit	40.1	41.4	38.8	38.0	37.3	-7.0
BART	47.8	51.8	51.2	51.8	54.1	13.2
MUNI	86.3	94.4	98.8	108.3	90.0	4.3

Source: Metropolitan Transportation Commission.

BART's effectiveness increased substantially during the period 1980-81 through 1984-85, as indicated by the increase in passenger boardings (24 percent) and passengers per vehicle hour (13 percent). MUNI's passenger boardings and passengers per vehicle service hour increased through 1983-84 but declined in 1984-85, so these measures were only slightly higher at the end of the period than they were at the beginning.

AC Transit's effectiveness during the period declined by 8.4 percent as measured by passenger boardings, and by 7 percent as measured by passengers per vehicle service hour. The most recent performance audit of the district, completed in March 1984, made several recommendations to improve AC Transit's effectiveness and financial position. One of these recommendations was that AC Transit conduct a comprehensive reevaluation of its routes and service levels. The report noted that while AC Transit reviews the performance of individual routes annually, it has not conducted a system-wide review of routes and service levels since it began operations in 1960. Given the substantial changes in land use and demographics, together with the initiation of BART service, a comprehensive reevaluation is warranted. The district has initiated such a review.

Financial Base

Each operator funds the delivery of transit services from two sources:

- o Its financial base, which we define as those revenues that are either statutorily dedicated to the operator or available on a reasonably predictable basis, and
- o External sources, consisting primarily of federal and state assistance.

Table 6 indicates the percentage of total operating expenses which each operator funds from its financial base.

Table 6

Base Revenues as a Percent of Operating Expenses
1980-81 versus 1984-85

	1980-81	Estimated 1984-85
AC Transit	72.8	71.6
BART	105.0	99.2
MUNI	69.4	85.5

As the table shows, BART is capable of funding nearly all its operating expenses from base revenues. (In BART's case, base revenues include fares, 75 percent of AB 1107 funds, and property taxes.) BART's strong financial base provides it with a high degree of financial independence. In fact, it currently plans to increase service levels on its own, without federal and state operating assistance. (BART is dependent upon capital assistance, as we discuss in the next chapter.) Furthermore, BART's financial base gives it the ability to compete effectively for capital grants and to finance capital improvements by issuing bonds.

MUNI's base revenues fund a smaller percentage of its operating expenses, making MUNI more dependent on allocations of state and federal operating assistance and discretionary AB 1107 funds. Even so, MUNI's access to the San Francisco general fund provides the system with considerable flexibility to respond to changing circumstances. One indication of this relatively broad financial base is the increase in the base revenues/operating expense ratio that occurred between 1980-81 and 1984-85--a period of substantial growth in MUNI operating costs. This increase in the ratio reflects the increased commitment of San Francisco general fund revenues to MUNI. Moreover, the City and County of San Francisco has shown a willingness to fund MUNI improvements and service expansions by imposing fees on developers.[1]

In the current year, San Francisco reduced general fund support for MUNI, in response to a projected general fund deficit, thereby necessitating an increase in MUNI fares.

Of the three operators, AC Transit is the most dependent on external assistance to meet its expenses. Its base revenues consist of fares, TDA revenues, and property tax. The increase in these revenues since 1980-81 has been approximately 26 percent, compared with an increase of 30 percent in the CPI. Nevertheless, the share of operating expenses funded from base revenues has remained constant at about 72 percent, due to the fact that AC Transit's operating costs also grew at a rate below the rate of inflation.

Ability to Maintain Vital Transit Services

Table 7 provides two measures of the service levels delivered by each of the three operators. The table indicates that despite the differences in the ratios of operating expenses to base revenues, the three operators have been able to maintain vital transit services as defined by

1. These fees are being challenged in court.

MTC. This can be attributed to (1) regional allocations of UMTA, TDA and, in particular, discretionary AB 1107 funds, by the MTC through the AB 842 process, and (2) BART's agreement to purchase certain services from AC Transit (discussed below).

The regional allocations for each year are presented in Appendix 1 and summarized in Charts 1 and 2.

Table 7

Operator Service Levels
1980-81 through 1984-85
(millions)

	1980-81	1981-82	1982-83	1983-84	1984-85	Percent Increase 1980-81 to 1984-85
Vehicle service miles						
AC Transit	25.5	25.9	25.5	25.6	25.7	0.8
BART	27.7	28.5	29.2	29.9	30.6	10.5
MUNI	25.4	26.4	25.6	25.9	27.7	9.1
Vehicle service hours						
AC Transit	1.88	1.84	1.82	1.81	1.85	-1.6
BART	1.03	1.05	1.07	1.09	1.12	8.7
MUNI	2.95	2.98	3.02	2.89	2.94	-0.3

No discretionary AB 1107 funds have been allocated to BART under the AB 842 process; instead, the funds have been split between AC Transit and MUNI. Chart 1 shows that each system's share of these funds has varied considerably since AB 842 was enacted. For example, between 1984-85 and 1985-86, AC Transit's share of AB 1107 discretionary funds decreased from

CHART 1

AB 1107 DISCRETIONARY FUNDS
DISTRIBUTION

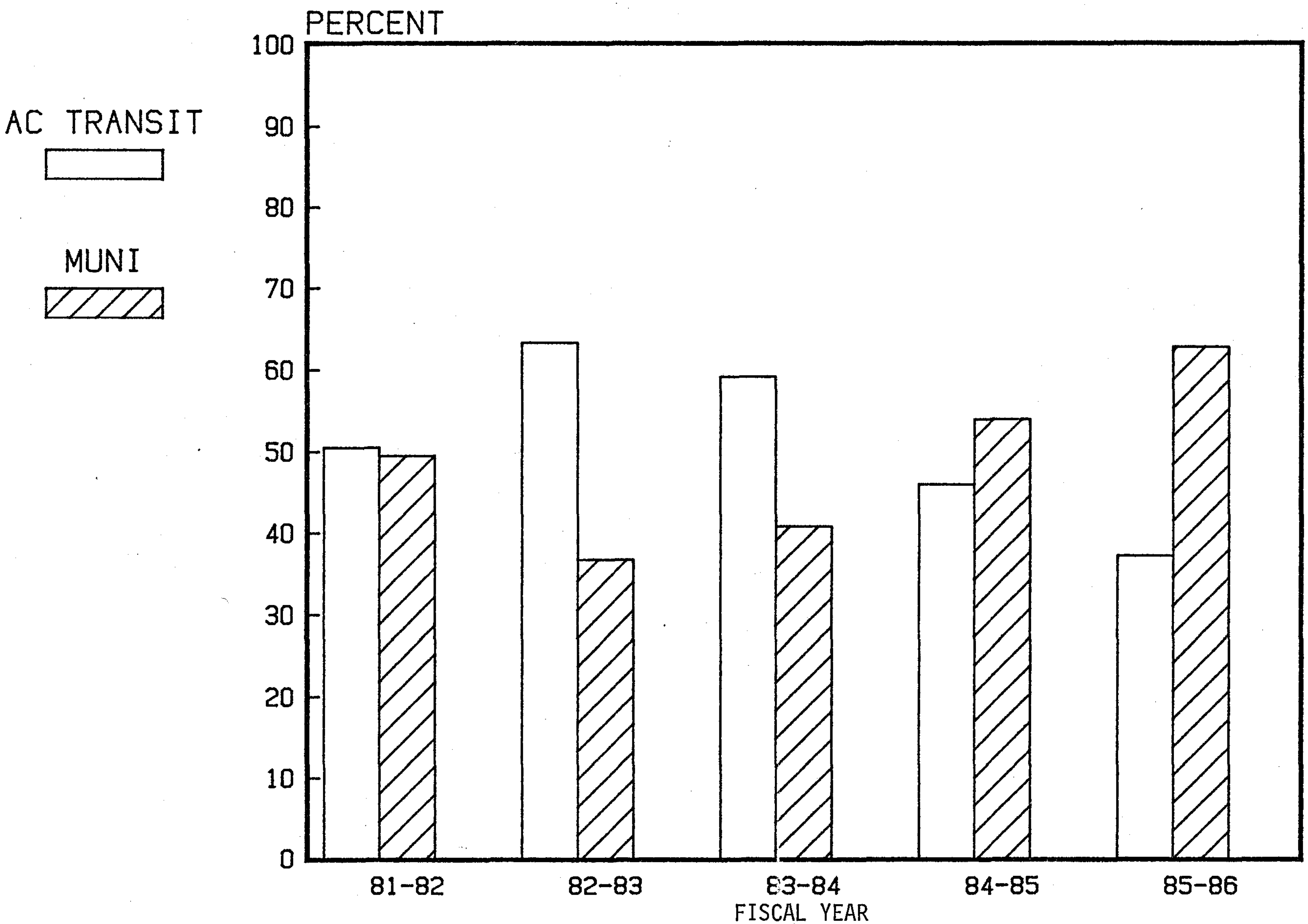
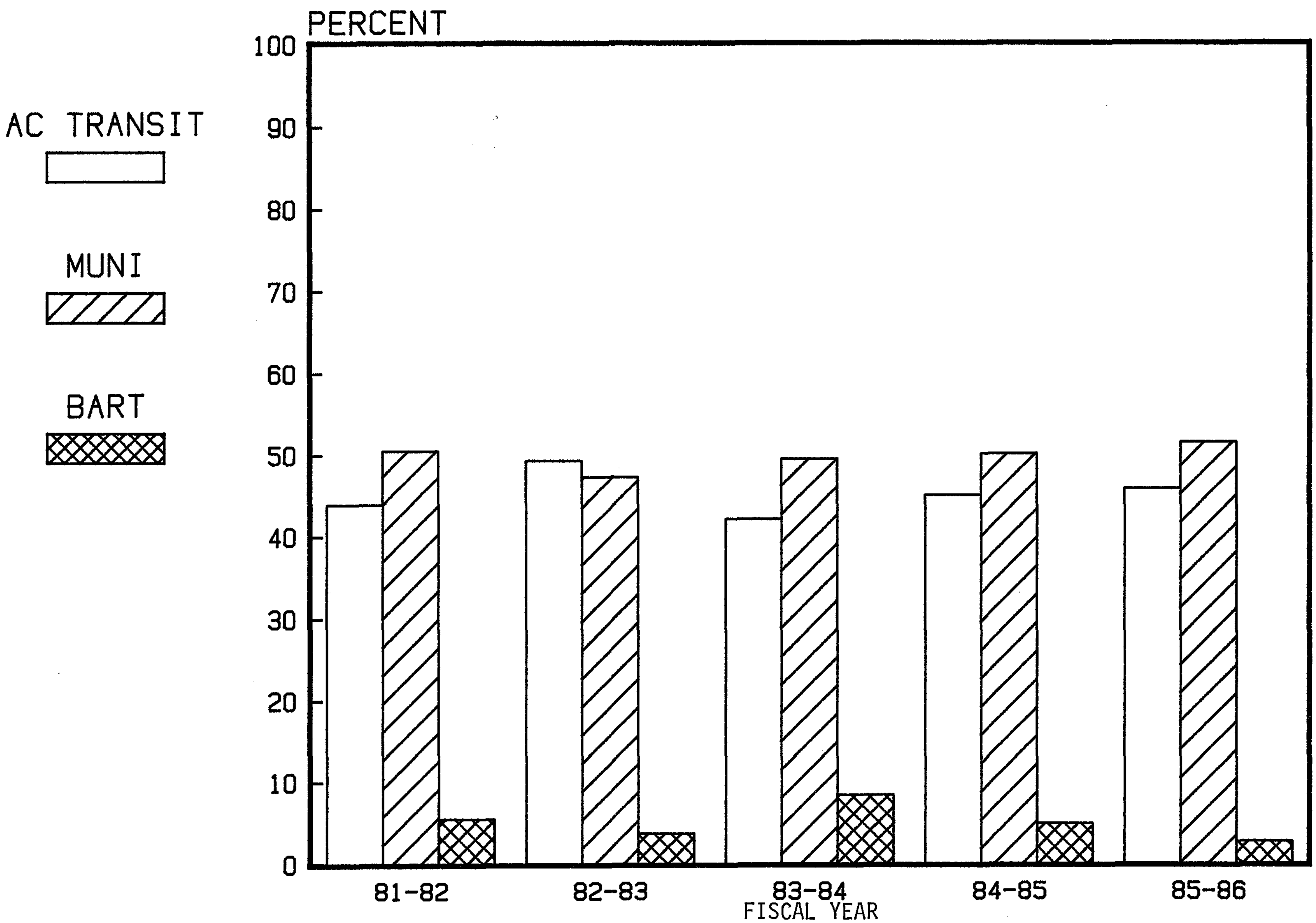


CHART 2

AB 842 TOTAL REGIONAL FUNDS
DISTRIBUTION



46 percent to 37 percent, while MUNI's share increased from 54 percent to 63 percent. Nevertheless, AC Transit and MUNI's shares of total regional fund distributions have remained fairly stable over the entire five-year period (Chart 2). In effect, AB 1107 funds have been used as a balancing item in the overall funding allocations in order to stabilize total regional allocations to the operators. This is consistent with the Legislature's objective of maintaining current service levels offered by the three operators.

In both 1984-85 and 1985-86, BART agreed to purchase service from AC Transit--at a cost of $3.1 million and $5.5 million, respectively. Because the services being purchased were, to some extent, already being provided by AC Transit, the purchases provided additional net revenues to AC Transit, thereby reducing the need for fare increases. The agreement reduced AC Transit's midday transbay service--when excess BART capacity exists--and required improvements in AC Transit's feeder bus services to BART.

Financial Projections

To determine whether regional resources are adequate to fund vital transit service levels in the coming years, we compared the projection of operating expenses developed by each operator in its most recent short-range plan with our own projection of revenues.

Projected Revenues. In projecting revenues to each operator, we first developed a set of assumptions regarding the future. For simplicity, we assumed that federal operating assistance would remain at its 1985-86 level. In fact, it is likely that federal operating assistance will be reduced below this level. Consequently, the projections developed in this chapter regarding the adequacy of regional resources are optimistic. In the next chapter, we discuss the impact that reductions in federal assistance would have on the three operators.

We also assumed that:

- State Transportation Assistance (STA) funding will remain constant at the 1985-86 level.
- Local Transportation Development Act (TDA) revenues will grow at the annual rate of 6.3 percent beyond 1984-85. (Prior-year funds in 1984-85 are reflected as an adjustment to 1985-86 revenues.)
- AB 1107 revenues will grow at the rate of 6.3 percent per year beyond 1984-85. (In the case of AB 1107 funds allocated by the MTC, prior-year funds in 1984-85 are reflected as an adjustment to 1985-86 revenues.)
- Fare revenues in any given year will be either (1) the amount projected by the operator, or (2) the amount necessary to insure that the specified ratio of fare revenues to operating costs is achieved, whichever is greater. The farebox ratio specified for AC Transit and BART is 33 percent; for MUNI it is 28 percent. (BART's projected farebox ratio is well above the 33 percent ratio in each of the five years.)
- Local general fund support for MUNI will grow at the same rate as MUNI operating expenses, thus funding a constant share of such expenses.

Projection Results. Table 8 summarizes the results of our projections for each of the three operators.

Table 8

Projected Operating Expenses and Revenues
(dollars in thousands)

	1985-86	1986-87	1987-88	1988-89	1989-90	Total
Operating Expenses						
AC Transit	$92,100	$98,220	$104,400	$110,980	$117,640	$523,340
BART	163,896	177,020	191,335	207,177	220,410	959,838
MUNI	213,356	228,255	245,976	263,836	280,624	1,232,047
Total	$469,352	$503,495	$541,711	$581,993	$618,674	$2,715,225
Revenues Before AB 1107 Allocations[a]						
AC Transit	$83,154	$83,665	$88,568	$93,827	$99,335	$448,549
BART	173,322	184,929	198,057	215,285	234,413	1,006,006
MUNI	194,793	211,097	222,997	238,065	252,381	1,119,333
Total	$451,269	$479,691	$509,622	$547,177	$586,129	$2,573,888
Surplus (Deficit) Before AB 1107 Allocations						
AC Transit	($10,253)	($14,555)	($15,832)	($17,153)	($18,305)	($74,791)
BART	9,426	7,909	6,722	8,108	14,003	46,168
MUNI	(18,563)	(17,158)	(22,979)	(25,771)	(28,243)	(112,714)
Total	($18,082)	($23,805)	($32,089)	($34,816)	($32,545)	($141,337)
AB1107 Allocation	$28,988	$30,530	$32,453	$34,498	$36,671	$163,141
Surplus (Deficit) After AB 1107 Allocations[b]						
AC Transit/MUNI	$1,480	($1,183)	($6,357)	($8,427)	($9,877)	($24,364)
BART	9,426	7,909	6,722	8,108	14,003	46,168

a. Before allocation by the MTC of the 25-percent discretionary share of AB 1107 funds.
b. AB 1107 funds are applied to meet the deficits of AC Transit and MUNI.

We project that even after the allocation of MTC's discretionary AB 1107 funds, AC Transit and MUNI could face a combined deficit of approximately $24 million over the five-year period 1985-86 through 1989-90. This represents about 1.4 percent of their combined projected operating expenses during this period. The annual deficit in 1989-90 would be nearly $9.9 million, or 2.5 percent of combined operating expenses.

These results, of course, are highly sensitive to the assumptions on which the operators based their projections of operating expenses. AC Transit projects its operating expenses to grow at a rate of approximately 6.3 percent per year, while MUNI anticipates an annual growth in operating expenses of approximately 7.1 percent. In preparing the Governor's Budget for 1986-87, the Department of Finance estimated that the state CPI would increase by 4.6 percent in 1985 and 1986, and by 5.1 percent in 1987. If we assume that the increase in the Bay Area CPI averages 5.0 percent during the period 1985-86 through 1989-90 <u>and</u> that operators restrict the growth in operating costs to the rate of growth in the CPI, the combined AC Transit/MUNI deficit would be $1.4 million during the period.

As Table 8 shows, we project that BART will realize an operating surplus of approximately $46 million over the five-year period. These funds have been programmed for capital replacement and modernization as well as for capacity expansion and rail extension projects. The operating surplus projected for BART reflects (1) the system's strong financial position relative to AC Transit and MUNI and (2) its decision to increase fares to fund its capital program.

Conclusion. Assuming that state and federal operating assistance remains at current levels, we project that AC Transit and MUNI would incur an operating deficit during the five-year period 1985-86 through 1989-90. We believe, however, that this deficit is likely to be small (1.4 percent) relative to the total operating expenses of the two operators. Moreover, if inflation remains at current levels and if the operators restrict growth in operating expenses to the general rate of inflation, the deficit would be negligible. Under these circumstances, reductions in current service levels could be avoided through tighter cost controls and, if necessary, by increasing fares.

In the next chapter, we consider the impact of possible reductions in state and federal funding on the three operators.

CHAPTER III

IMPACT OF FEDERAL AND STATE FUNDING UNCERTAINTY

In the previous chapter, we considered the ability of the three operators to finance current service levels over the five-year period 1985-86 through 1989-90 if federal and state transit funding remains at current levels. In this chapter, we focus on the availability of state and federal funding to the three transit operators in the coming years. Because some state and federal money could be used to fund operations or capital outlay, and because each operator is dependent on state and federal funding for the capital replacement needed to maintain service levels, we will consider the availability of both operating and capital assistance.

State Transportation Assistance (STA)

The State Transportation Assistance (STA) program provides capital and operating assistance to local transportation agencies for public mass transit systems and, in areas where there are no unmet transit needs, for construction and maintenance of local streets and roads.

Thirty percent of STA funding is allocated to operators; the other 70 percent is provided to regional transportation planning agencies, such as the MTC in the San Francisco Bay Area, for allocation on a discretionary basis as operating or capital assistance. The MTC has a policy of allocating STA 70-percent funds on a matching basis for capital outlay projects.

The STA program is funded from 60 percent of retail sales tax revenues transferred under a "spillover" formula to the state's Transportation Planning and Development (TP and D) Account. Between 1983-84 and 1985-86, these revenues fell from approximately $159 million to approximately $114 million (estimated) annually.

In order to provide a measure of stability in the state's Transportation Planning and Development Account, the Legislature enacted Chapter 1600, Statutes of 1985 (SB 300). This act specifies that annual transfers shall be made to the account from (1) the General Fund in 1986-87, or (2) sales and use taxes imposed on diesel fuel, beginning in 1987-88, if such transfers are necessary to bring the account's annual revenues up to $110 million.

It is difficult to project revenues to the TP&D Account, given instability in gasoline and diesel fuel prices. Nevertheless, we believe that the allocation of <u>all</u> revenues from the retail sales and use tax on diesel fuel may not be adequate to provide for an annual funding level of $110 million in the TP and D Account beyond 1986-87. Revenues to the account could be no more than $90 million per year--or even less. Since current law appropriates 60 percent of the revenues received by the Transportation Planning and Development Account to the State Transportation Assistance program, this would imply a funding level for the program of $54 million annually--18 percent <u>less</u> than what we assumed in making our projections. This would mean that AC Transit and MUNI would receive about $1 million less in STA funding annually than what we assumed in Table 8.

Federal Operating Assistance

Since federal fiscal year 1983, operating assistance for local transit has been capped at about $875 million annually. For FFY 1986, the Congress reduced this amount to $870 million. These funds are apportioned on a formula basis to urbanized areas, with approximately $22.8 million going to the San Francisco-Oakland urbanized area on an annual basis.

It is likely that federal operating assistance will be reduced in the future as a result of efforts to reduce the federal deficit. For example, under the "Gramm-Rudman-Hollings Amendment to the Federal Debt Limit Bill," the President and the Congress must meet specified annual deficit targets leading to a balanced budget in FFY 1991. If the President and Congress are unable to agree on a program to meet these targets, the President is required to make across-the-board reductions in federal programs not specifically exempted from provisions of the act. (Transit programs are not exempt.)

The first set of automatic expenditure reductions under the Gramm-Rudman-Hollings amendment took effect on March 1, 1986, cutting transit assistance by approximately 4.3 percent. Because MTC anticipated a cut of 10 percent in its allocation of federal operating assistance, this reduction is reflected in the projections set forth in Chapter II.

The level of federal operating assistance that will be made available in FFY 1987 and beyond is highly uncertain. For FFY 1987, the President has proposed to eliminate operating assistance for all operators except those in rural or small urban areas. Although the Congress rejected a similar proposal last year, it may be more receptive now, given the enactment of the Gramm-Rudman-Hollings Amendment.

If Congress is unable to enact a budget consistent with the deficit target for FFY 1987, operating assistance would be subject to the across-the-board cuts called for by the Gramm-Rudman-Hollings Amendment. These cuts could range from approximately 9 percent to 20 percent of FFY 1986 budget authority. This assumes, however, that (1) the courts do not rule the deficit reduction provisions unconstitutional, and (2) Congress does not act to modify the provisions or delay their effective date.

Impact of Potential Federal Funding Reductions

We believe that, if federal funds are reduced, the resources available to the MTC for allocation will not be adequate to maintain current service levels in future years. For example, if federal operating assistance were phased out over the next three years, AC Transit and MUNI could face a combined revenue shortfall for the five-year period 1985-86 through 1989-90 of $67.3 million. This is $42.9 million more than the deficit that would be incurred if federal funding levels remain constant over the period, and represents 3.8 percent of combined AC Transit and MUNI operating expenses projected for the five-year period. By 1989-90, the deficit would be $24.2 million--6.1 percent of combined AC Transit and MUNI operating expenses after the allocation of available AB 1107 regional sales tax funds. (These estimates assume continuation of state operating assistance at current levels.)

Capital Assistance

Each transit operator also receives capital funding assistance from federal and state sources that is allocated by the MTC. A portion of this assistance is used for capital replacement and, therefore, is necessary to maintain service levels.

The state makes capital funding available on a formula basis for allocation by regional transportation planning agencies (MTC) under the STA program. It also makes capital funding available on a discretionary basis from the California Transportation Commission, under the Transit Capital Improvements Program. Both of these programs are funded from the TP and D Account. As a consequence, funding for them is unlikely to increase, and probably will fall, given the outlook for revenues to this account.

Additional transit capital funding is available under statutory formula from net toll bridge revenues earned on the San Francisco-Oakland Bay, the San Mateo-Hayward and Dumbarton Bridges. Under the statute, the MTC receives "net revenues" in excess of the amount required to pay necessary costs of operations, rehabilitation and safety improvements, to meet the obligations assumed under any bond resolutions applicable to the toll bridges and to repay any advances made from other funding sources for studies and work preliminary to the financing of any toll bridge project. These revenues are available for discretionary allocation by the commission for transit capital improvement in the vicinity of the toll bridges. In 1984-85, approximately $10.4 million was available from such revenues for allocation by the MTC to AC Transit, BART and MUNI.

Federal capital assistance is available from several sources on either a formula or discretionary basis. The Congress reduced federal appropriations for this purpose in FFY 1986 by approximately 12.8 percent, and these appropriations have been reduced by an additional 4.3 percent as a result of the Gramm-Rudman-Hollings amendment. These funds are likely to be cut further in future years, as the federal government seeks to reduce the federal deficit.

Capacity to Respond to Potential Funding Reductions

The impact of reductions in operating and capital assistance varies among the three operators.

BART. BART receives almost no federal operating assistance and, therefore, would feel no direct effects from a reduction in such funding. The system could experience an indirect effect from such a cut, however, if capital assistance available at the regional level, such as the STA 70-percent funds, is used instead to fund the operating needs of other carriers within the region.

A reduction in federal capital assistance, however, would have a direct impact on BART. The system has adopted a five-year capital program (excluding design and construction of any rail extensions) costing approximately $927 million. Approximately $504 million of this amount is already funded, with $184 million (36.5 percent) coming from the federal government. The funded portion of the program includes approximately $340 million for six projects which together will expand the capacity of the current BART system by approximately 50 percent. The $423 million unfunded portion of BART's capital program includes $173 million needed to complete the system capacity expansion projects. Other unfunded capital needs identified in the plan include approximately $106 million for additional parking capacity at BART stations, $80 million for right-of-way acquisitions in anticipation of future BART extensions, and $64 million for other purposes.

BART estimates that funds will be available from federal, state, and local sources to fund all but $71 million of its unfunded capital program. It expects to raise approximately $65 million of this amount by issuing revenue bonds in 1985-86. This suggests that BART will be able to fund its five-year capital program. On the other hand, we note that BART is counting on receiving approximately $278 million in previously uncommitted federal funds during that period--an amount which represents 66 percent of the system's $423 million unfunded capital program.

If federal capital assistance is reduced, as we expect it to be, BART will need to either (1) compete more effectively for the remaining federal funds, (2) scale back its capital program, or (3) find alternative financing for its projects. BART also will need to consider alternatives for reducing expenditures, such as:

- Reducing or postponing expenditures for rail extension right-of-way acquisition or planning. Approximately $87 million of such expenditures are included within the unfunded portion of the capital plan.
- Reducing or postponing expenditures for expansions in parking

capacity. These represent $106 million of the unfunded program.

- Stretching out the completion of its capacity expansion projects, which represent $173 million of the unfunded program.

None of these alternatives would significantly affect BART's ability to maintain current service levels in the short term. They would, however, limit its ability to increase service levels in order to improve mobility within the region.

BART also may have available alternative ways to finance its capital program. For example, BART recently concluded an agreement with a private developer which permits development of a hotel on BART property at the Pleasant Hill station, in exchange for construction of 2,800 additional parking spaces and annual rental payments, estimated at up to $1 million per year.

MUNI. MUNI funds about $8.2 million, or 3.8 percent of its operating expenses, from federal sources. While the loss of these funds could affect some MUNI services, such impact probably would be minor. Furthermore, MUNI's access to San Francisco's general fund provides it with a degree of financial flexibility that would make it easier to adjust to a reduction in federal funding. On the other hand, a simultaneous reduction in federal funding for other county programs, which is certainly likely, would increase the demands on the San Francisco general fund.

MUNI has a five-year capital program costing approximately $428 million. It estimates that, during this period, between $204 million and $495 million will be available from federal, state, and local sources to fund this program. (Most of the variance is due to uncertainty about the availability of federal funds.)

The loss of federal capital assistance would require adjustments in MUNI's capital program. Some reductions in planned capital expenditures could be made without affecting current service levels. For example, expenditures for the extension of MUNI Metro to Mission Bay ($11.5 million), the construction of the Embarcadero streetcar line ($30.4 million), the construction of the Market Street to Embarcadero streetcar line ($19.3 million), or the extension of cable car lines to the wharf ($3.9 million) could be reduced or postponed. Clearly, however, a reduction in federal capital assistance would limit MUNI's ability to undertake capital improvements to increase service levels.

AC Transit. Federal operating assistance accounts for $6.1 million, or 6.6 percent, of AC Transit's operating expenses. AC Transit's limited financial base and its relatively greater dependence on federal operating assistance means that it is less able to maintain service levels without outside assistance than either of the other two operators. The system would be heavily dependent on MTC to help it adjust to any abrupt loss of federal funds.

We do believe, however, that AC Transit has some capacity to absorb some cuts by improving its efficiency. In particular, the current study of the district's route structure and service levels has the potential to yield significant improvements in system utilization by achieving a better match of system routes with travel needs (including better coordination with BART and other regional operators). Such improvements should reduce costs and increase revenues. In addition, recent improvements to AC Transit's management information system also should assist the district in its efforts to improve system efficiency.

AC Transit is nearing completion on a major facilities improvement program which includes (1) construction, reconstruction or rehabilitation of four of its six operating division facilities (Emeryville, Richmond, Seminary and South Hayward), (2) construction of new maintenance and training facilities, and (3) construction of a new 10-story facility for its general offices. Much of this program already has been completed; the balance will be completed by the end of 1986. This should provide the district with the basis for productivity improvements in the next several years.

AC Transit's five-year capital program totals approximately $71.3 million. Most of this amount ($56.4 million, or 79 percent) represents planned expenditures for bus replacement. The program also includes $7.8 million to complete the facilities improvement program just discussed, $2.2 million for strategic planning and marketing research, $1.8 million for an automatic vehicle monitoring system, and $3.1 million for other projects. On the whole, the capital program provides for vehicle replacement and productivity improvement projects necessary to provide current service levels.

Metropolitan Transportation Commission. In the absence of additional state assistance, any reduction in federal funding will require

MTC to reevaluate its policies for allocating state and federal funds. In doing so, the commission will need to consider whether to make available the STA 70-percent funds, currently reserved for capital purposes, as additional operating assistance. At the same time, the commission will need to determine (1) how to meet capital replacement needs, and (2) how best to allocate capital funds for service improvements.

CHAPTER IV

CONCLUSIONS AND RECOMMENDATIONS

As noted in the previous chapters of this report, the Legislature has enacted several measures designed to promote the financial stability of AC Transit, BART, and MUNI and to maintain vital transit services. So far, we have evaluated the extent to which the Legislature's objectives have been achieved and considered the impact that reductions in state and federal funding for transit operating and capital needs would have on the three operators. This chapter presents our overall conclusions and recommendations.

MTC Allocation Process Appears Consistent

The MTC has adopted a procedure for allocating regional funds which seeks to provide each operator with sufficient resources to maintain current service levels. In the event the resources available to the operators, together with regional funds, are not adequate to achieve this objective, the MTC expects the operators to increase fares in a coordinated manner so as to provide the additional revenue needed. The MTC allocates the regional funds assuming that each operator increases fares in line with its coordinated fare recommendation.

We believe that this procedure for allocating regional funds is sound, and that it is consistent with the Legislature's intent to maintain vital transit services.

A Five-Year Financial Plan Would Improve Decision Making

We recommend that the Legislature enact legislation requiring the MTC to adopt, and update annually, a five-year financial management plan which identifies committed service levels in each of the five years and is consistent with planned capital improvements in the Regional Transportation Improvement Program. We further recommend that the MTC use this plan as the basis for allocating funds to AC Transit, BART, and MUNI under the AB 842 process.

Under current law, the MTC is required to allocate 25 percent of the AB 1107 funds in accordance with a financial management plan which is revised annually in cooperation with the transit operators. To satisfy this requirement, each year the Commission adopts the AB 842 Transit Finance Study, which projects operating expenses and revenues for each of the three operators in the upcoming year, and sets forth the allocation of regional funds--including AB 1107 funds--proposed by the MTC.

While this plan provides a basis for allocating funds in the short run, it does not provide operators with estimates of their allocations in future years nor does it provide adequate lead time for any coordinated fare increases that will be required under the AB 842 process. Moreover, the plan does not anticipate changes in future committed service levels resulting from planned capital improvements.

We believe that lengthening the MTC's planning horizon to five years would assist the operators in developing their annual budgets and short-range plans. Furthermore, by identifying the need for coordinated fare increases well in advance, a five-year plan would give operators and the MTC adequate time to carefully consider pricing options and develop the required coordinated fare structure. Finally, by requiring that the plan be consistent with capital commitments, the Legislature would help ensure that the operating costs of planned projects are fundable.

While a five-year plan would not reduce uncertainty relating to the availability of federal or state funds in the region, it would reduce the uncertainty operators face regarding the way in which available funds will be allocated by the MTC.

Options to Respond to Reduced Federal Funding

As indicated in Chapter III, we believe that reductions in federal operating assistance are likely and that such reductions could pose problems for AC Transit and, to a lesser extent, MUNI. In addition, the amount of STA funding available to MUNI and AC Transit each year in the future is likely to be $1 million or more below current levels.

There are six basic options for responding to the reductions in federal and state operating assistance on which the operators depend:

- o The operators could cut their costs of providing service.
- o The operators could reduce their services to the public.
- o AC Transit could seek financial help from municipalities in its service area (as MUNI has done).
- o The Legislature could expand state assistance to transit operators on a statewide basis.

- o The Legislature could authorize a surcharge on bridge tolls to fund transit capital or operating needs. Short of this action, the Legislature could make current net toll bridge revenues available for transit operating, as well as capital, purposes.
- o The Legislature could reallocate AB 1107 funds.

Cut Costs. As discussed in Chapter II, from 1980-81 through 1984-85, AC Transit's operating costs increased at a rate slightly less than the rate of inflation, while MUNI costs increased at twice the rate of inflation. As noted earlier, these increases are directly related to increases in wage, salary and fringe benefit costs of 21 percent for AC Transit and 58 percent for MUNI.

We believe that AC Transit and MUNI should continue to pursue efforts to reduce costs. Nevertheless, we believe AC Transit's ability to achieve major savings beyond those realized since 1980-81 are limited.

Reduce Services. We believe that service reductions may be justified where service utilization is low. To determine whether such reductions are warranted, the Legislature should direct the MTC to review service effectiveness annually when establishing the vital transit service levels for each operator. "Committed service levels" should not be maintained if this means continuation of inefficient or ineffective services.

On the other hand, service reductions invariably create hardships for those dependent on public transportation, and these hardships must be taken into consideration by the Legislature.

Local Participation. As a municipal operator, San Francisco MUNI is funded from the San Francisco general fund. This arrangement promotes consideration of MUNI operations and financing within the broader context of urban development in San Francisco. MUNI must be responsive to the needs of the municipality and, in turn, the municipality must act responsibly in placing demands on MUNI.

As a special district, AC Transit does not share the same relationship with the municipalities it serves. AC Transit serves a number of municipalities, rather than a single city/county entity. Nevertheless, with the assistance of the MTC, it should explore the potential of developing increased local funding support from the cities within its service area. While this would be a complex undertaking, it might bear fruit even though not all cities may be responsive. As an inducement to local funding support, AC Transit might offer cities a greater role in determining service characteristics within their borders. Local support might take the form of renewable service contracts between the district and the municipalities served.

Expanded State Assistance. Only the Legislature can decide whether additional state assistance to transit operators is warranted, given other demands on state resources and the limitations on appropriations that the Constitution imposes. In particular, the Legislature should be aware that any increase in funding for transit would probably require offsetting reductions in other state programs.

Since the impact of federal funding reductions also will affect operators in other parts of the state, we believe that the Legislature should consider the needs of AC Transit, BART, and MUNI in the broader context of transit needs generally.

Bridge Tolls. The Legislature could authorize a surcharge on bridge tolls to fund transit capital or operating needs. A surcharge of 25 cents per passenger vehicle would raise approximately $12 million annually. Increased revenues under such a proposal would probably be subject to the constitutional limitation on appropriations. Furthermore, any increase in bridge tolls to fund transit needs could reduce the Legislature's capability to increase tolls in the future to fund bridge projects.

As an alternative to a toll surcharge, the Legislature could make current net revenues from bridge tolls available for transit operating needs. Currently, such revenues equal about $10.4 million annually and are restricted to transit capital purposes.

In 1984, the Legislature passed a measure (AB 3837) which, among other things, authorized MTC to recommend increased tolls to fund transit capital improvements, but the Governor vetoed the bill. The Governor's veto message indicated concern that:

- "There is a large constituency in the Bay Area which feels the bridges should be toll-free once the original indebtedness is paid off,"
- "The toll increases...are, in effect, an added tax on the bridge user and would add millions of dollars annually to the cost of commuting,"

o "A portion of the increased toll revenues...(would go) to transit rather than bridge projects."

AB 1107 Reallocation. Finally, the Legislature could reallocate AB 1107 funds to make a greater share of such funding available to MTC for allocation based on regional priorities. This would reduce BART's guaranteed share of the AB 1107 funds below the 75-percent level, but would serve to provide the MTC with greater flexibility to meet high priority transit needs in the region.

AB 1107 Allocations Should Be Revised

We recommend that the Legislature enact legislation to: (1) increase the portion of AB 1107 funds that the MTC is able to allocate on a discretionary basis and (2) establish broad priorities to guide the MTC's allocation of these funds.

AB 1107 funds have been allocated by the Legislature to achieve two purposes: (1) to provide a financial base for BART, and (2) to maintain vital transit services offered by all three operators. The statutory allocation of AB 1107 funds, however, was enacted at a time when (1) federal operating assistance to MUNI and AC Transit was growing, and (2) AC Transit and MUNI had unrestricted access to growing property tax bases that could be tapped to provide additional operating funds. Both of these conditions no longer exist. Federal assistance has been reduced and further reductions are anticipated. Moreover, Proposition 13 has greatly diminished AC Transit's access to the property tax. As a result, reconsideration of the current financing provisions is warranted.

Our review finds that the 75-percent allocation to BART has, indeed, provided the operator with a solid financial base. This base has proven adequate to fund current service levels and provide for service expansions without the need for federal operating assistance. In contrast, AC Transit and, to a lesser extent, MUNI must depend on federal operating subsidies and MTC discretionary allocations from the remaining 25 percent of AB 1107 funds to maintain current service levels.

Given the relative financial positions of the three operators today, we believe a change in the allocation of AB 1107 funds is warranted. Specifically, we believe that the Legislature should give the MTC discretion over 35 percent, rather than 25 percent, of these funds and allow MTC to allocate the funds for either operating or capital purposes. While this would reduce BART's guaranteed allocation (from 75 percent to 65 percent), it would still leave BART with the ability to fund over 95 percent of its operating expenses from its financial base. BART also would be able to compete with the other operators for its share of the increased discretionary amount. More importantly, this change would help to ensure that AB 1107 resources are allocated to fund those services or improvements which are of the highest priority to the region as a whole.

There are at least three potential drawbacks to this change which the Legislature should carefully consider in making its decision.

First, reallocation of AB 1107 funds could be viewed as penalizing BART for fiscal responsibility. BART has used its 75-percent allocation of AB 1107 funds wisely, and has made good use of farebox revenues to support both current operations and capital improvements. While a reallocation of AB 1107 funds would not threaten BART's ability to deliver current services, it could reduce BART's ability to fund planned capital improvements if the MTC increases allocations to AC Transit and MUNI at BART's expense.

Second, by reallocating funds to AC Transit, the Legislature might weaken the incentives for this operator to (1) identify services and service levels which are truly vital--that is, essential to the local and regional life--and (2) implement the comprehensive restructuring of its routes and services (to which we pointed earlier). To avoid this drawback, it is critical that MTC consider the extent to which AC Transit has studied and implemented route restructuring in making its allocation decisions.

Third, the Legislature might weaken the incentives for AC Transit to develop potential sources of local support.

While these drawbacks are real and should be carefully considered, we believe they are outweighed by the benefits to be gained from the added flexibility that the reallocation of AB 1107 sales tax funds would yield. Without this flexibility, the services offered by AC Transit could be imperiled to an unacceptable degree.

If the Legislature chooses to provide MTC with increased funding authority and responsibility, we believe it should also set broad priorities to guide the commission in allocating sales tax funds. In particular, the guidelines should specify that the AB 1107 funds should be applied first to fund operating costs and replacement capital costs necessary to maintain vital transit services and second to fund service improvements. In setting the guidelines, the Legislature should also direct MTC, in making its allocation decisions, to consider the extent to which AC Transit has studied and implemented route restructuring.

Appendix 1

AB 842 Regional Fund Distributions
To AC Transit, BART and MUNI
(dollars in millions)

	AC Transit	BART	MUNI	Total
FY 1985-86				
TDA	$23.6	$0.6	$17.1	$41.3
UMTA 9	6.0	--	8.1	14.1
UMTA 8	0.1	0.1	0.1	0.3
STA 30%	1.7	1.8	4.0	7.5
AB 1107	10.8	--	18.2	29.0
Total	$42.2	$2.5	$47.5	$92.2
(Percent)	(45.8)	(2.7)	(51.5)	(100.0)
FY 1984-85				
TDA	$17.0	$0.5	$13.9	$31.4
UMTA 9	6.7	--	9.0	15.7
UMTA 8	0.1	--	0.1	0.2
STA 30%	2.4	3.6	5.5	11.5
AB 1107	11.4	--	13.4	24.8
Total	$37.6	$4.1	$41.9	$83.6
(Percent)	(45.0)	(4.9)	(50.1)	(100.0)
FY 1983-84				
TDA	$13.0	$3.4	$16.6	$33.0
UMTA 9	5.9	--	13.9	19.8
UMTA 8	0.1	0.1	0.1	0.3
STA 30%	5.7	4.7	6.4	16.8
AB 1107	16.4	--	11.3	27.7
Total	$41.1	$8.2	$48.3	$97.6
(Percent)	(42.1)	(8.4)	(49.5)	(100.0)
FY 1982-83				
TDA	$15.8	$0.4	$16.8	$33.0
UMTA 9	5.0	--	6.7	11.7
UMTA 8	0.1	0.1	0.1	0.3
STA 30%	2.1	2.4	4.6	9.1
AB 1107	15.7	--	9.1	24.8
Total	$38.7	$2.9	$37.3	$78.9
(Percent)	(49.0)	(3.7)	(47.3)	(100.0)
FY 1981-82				
TDA	$15.0	$3.3	$12.2	$30.5
UMTA 9	7.6	1.3	16.3	25.2
UMTA 8	0.1	0.1	0.1	0.3
STA 30%	--	--	--	0.0
AB 1107	14.5	--	14.2	28.7
Total	$37.2	$4.7	$42.8	$84.7
(Percent)	(43.9)	(5.5)	(50.5)	(100.0)