

A Report to the Maryland General Assembly
Senate Budget and Taxation Committee,
House appropriations Committee, and
House Ways & Means Committee

regarding

Farebox Recovery –
Attainment and Operational Requirements
(Transportation Article, § 7-208(b)(2))

Maryland Transit Administration
Maryland Department of Transportation

December 2013



Maryland Department of Transportation
The Secretary's Office

Martin O'Malley
Governor

Anthony G. Brown
Lt. Governor

James T. Smith, Jr.
Secretary

December 13, 2013

The Honorable Edward J. Kasemeyer
Chair, Senate Budget and Taxation Committee
3 West Miller Senate Office Building
Annapolis MD 21401-1991

The Honorable Norman Conway
Chair, House Appropriations Committee
121 House Office Building
Annapolis MD 21401-1991

The Honorable Sheila Hixson
Chair, House Ways and Means Committee
131 House Office Building
Annapolis MD 21401-1991

Dear Chairs:

Please see the attached report prepared by the Maryland Transit Administration (MTA) concerning *MTA's Farebox Recovery Ratios*. This report was prepared to meet the requirements set forth in the Budget Reconciliation and Financing Act (Chapter 397, Acts of 2011). The Transportation Article, § 7-208 language requires:

“(b)(1) For fiscal year 2009 and each fiscal year thereafter, the Administration shall separately recover from fares and other operating revenues at least 35 percent of the total operating costs for:

- (i) The Administration's bus, light rail, and Metro subway services in the Baltimore region; and*
 - (ii) All passenger railroad services under the Administration's control.*
- (2) The Administration shall submit, in accordance with § 2-1246 of the State Government Article, an annual report to the Senate Budget and Taxation Committee, House Ways and Means Committee, and House Appropriations Committee by December 1 of each year that includes:*
- (i) Separate farebox recovery ratios for the prior fiscal year for:*
 - 1. Bus, light rail, and Metro subway services provided by the Administration in the Baltimore region;*
 - 2. Commuter bus service provided under contract to the Administration in the Baltimore region; and*
 - 3. Maryland Area Rail Commuter (MARC) service provided under contract to the Administration;*
 - (ii) A discussion of the success or failure to achieve the farebox recovery requirement established in paragraph (1) of this subsection; and*

The Honorable Edward J. Kasemeyer
The Honorable Norman Conway
The Honorable Sheila Hixson
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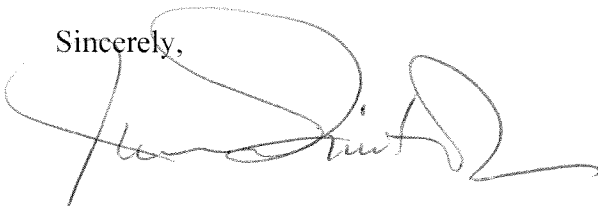
- (iii) *Comparisons of farebox recovery ratios for the Administration's mass transit services and other similar transit systems nationwide; and*
- (iv) *The estimated fare prices necessary to achieve the farebox recovery requirement established in paragraph (1) of this subsection for the next fiscal year."*

For your information, the Baltimore-area Commuter Bus data is provided by MTA contractor invoices showing costs minus revenue collected for service. As farebox recovery is typically calculated using the ratio of revenue compared to cost, MTA's data cannot be verified by FMIS data, which uses the costs figure only with no reference to the revenue collected. In the past, this has been problematic when the Department of Legislative Services has attempted to verify MTA's numbers. To resolve this problem, beginning FY 2014 and going forward, contractor invoices will allow MTA to calculate farebox recovery for Baltimore-area Commuter Bus in way that can be verified in FMIS. Therefore, the Baltimore-area Commuter Bus will have its own section with data verified by FMIS in future reports. For the purposes of this report and using the costs minus revenue collected for service methodology, the MTA estimates the current farebox recovery ratio is approximately 35 percent.

As it has done in the past, the MTA planned to include comparisons to similar nationwide systems in their Annual Performance Indicators (API) report, which is prepared separately from the farebox recovery report. Due to the October Federal government shutdown and subsequent delays in receiving the required data from the Federal Transit Administration's (FTA's) National Transit Database (NTD), the NTD still does not contain FY 2012 information necessary. Without the FY 2012 NTD data, MTA would essentially be resubmitting last year's report, which would not provide any meaningful information. MTA continues to monitor the NTD daily. Once the NTD data is received, MTA will complete and submit the API report as required.

Please feel free to contact Mr. Robert Smith, MTA Administrator, at 410-767-3943 if you have questions. Of course, you should always feel free to contact me directly.

Sincerely,



James T. Smith, Jr.
Secretary

cc: Members of the Budget Committees
Mr. Robert Smith, Administrator, MTA

Farebox Recovery – Attainment and Operational Requirements (Transportation Article, § 7-208(b)(2))

Introduction

This report was prepared to meet the requirements set forth in Transportation Article, § 7-208(b)(2), which directs:

“(b)(1) For fiscal year 2009 and each fiscal year thereafter, the Administration shall separately recover from fares and other operating revenues at least 35 percent of the total operating costs for:

(i) The Administration’s bus, light rail, and Metro subway services in the Baltimore region; and

(ii) All passenger railroad services under the Administration’s control.

(2) The Administration shall submit, in accordance with § 2-1246 of the State Government Article, an annual report to the Senate Budget and Taxation Committee, House Ways and Means Committee, and House Appropriations Committee by December 1 of each year that includes:

(i) Separate farebox recovery ratios for the prior fiscal year for:

1. Bus, light rail, and Metro subway services provided by the Administration in the Baltimore region;

2. Commuter bus service provided under contract to the Administration in the Baltimore Region; and

3. Maryland Area Rail Commuter (MARC) service provided under contract to the Administration;

(ii) A discussion of the success or failure to achieve the farebox recovery requirement established in paragraph (1) of this subsection;

(iii) Comparisons of farebox recovery ratios for the Administration’s mass transit services and other similar transit systems nationwide;¹ and

(iv) The estimated fare prices necessary to achieve the farebox recovery requirement established in paragraph (1) of this subsection for the next fiscal year.”

Background

Historically, the Maryland Transit Administration (MTA) has been subject to requirements that a certain percentage of operating expenses for its system be recovered from farebox revenue.

Chapter 684, Acts of 2008 (HB 1185) amended the farebox recovery requirement to 35 percent and explicitly added farebox recovery data to MTA’s annual performance report.

¹ MTA usually includes farebox recovery comparisons to similar systems nationwide in its Annual Performance Indicators (API) report, which is prepared separately from the farebox recovery report. Unfortunately, the API report that is due on December 1, 2013 is still not complete because it requires the MTA to use data from the Federal Transit Administration’s (FTA) National Transit Database (NTD). The FTA was delayed from updating the NTD by the October shutdown of the Federal government. As of December 1, 2013, the NTD still does not contain FY 2012 information. Without the FY 2012 NTD data, MTA cannot make any meaningful comparisons with peer systems. MTA continues to check the NTD for updated data on a daily basis.

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Chapter 397, Acts of 2011 (HB 72) provided MTA “may not reduce the level of services provided by the Administration for the purpose of achieving the farebox recovery requirement.”

Chapter 429, Acts of 2013 (HB 1515) required the MTA to increase base fares prices and the cost of multiuse passes to the nearest 10 cents for all transit services, except for commuter rail and commuter bus service, by the same percentage as the biennial increase in the Consumer Price Index for all urban customers, as determined from January 1, 2012 to December 31, 2013, and each subsequent 2-year period for which the amount is being calculated. HB 1515 also required MTA, every five years, to increase one-way zone fare prices and the cost of multiuse passes to the nearest dollar for commuter rail and commuter bus service by at least the same percentage as the 5-year increase in the Consumer Price Index as determined from January 1, 2009 to December 31, 2013 and each subsequent 5-year period for which the amount is being calculated. Finally, HB 1515 allowed the MTA, when increasing commuter bus and rail fares, to consider other factors affecting commuting costs applicable to the jurisdictions in which the Administration provides commuter service, including: monthly parking fees, the retail price per gallon of motor fuel, the amount of any federal subsidy, fare prices for intercity rail service and any other relevant commuting costs. These “additional costs” can be used to determine the amount of a commuter bus or rail fare increase over and above the amount of the five-year increase in consumer prices.

Measurement

The farebox recovery ratio is the ratio of gross revenue to adjusted expenses and measures only the subsidy level of transit service operated, not efficiency or cost-effectiveness. The numerator of the ratio is gross revenue, which is the total of fare revenue plus an allocated share of certain non-passenger operating revenue. The denominator is adjusted expense, which is the gross expense less certain capital and in addition to allocated administrative costs. Tables 1 and 2 summarize the revenue and expense components of the measure.

Table 1: Expense inclusions & exclusions, MTA farebox recovery

Include	Exclude
Insurance	Paratransit and commuter rail service expenses
Changes in inventory levels	Past pension service liabilities
Pro-rated share of administrative costs	New services for the first 36 months of service
	Capital costs, including 20 percent of revenue vehicle maintenance costs

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Table 2: Revenue inclusions & exclusions, MTA farebox recovery

Include	Exclude
Passenger fare revenues	Paratransit and commuter rail revenues
Advertising revenues	New services revenues for the first 36 months
Lease and rental income	

Factors in Revenue and Expenditure Growth

MTA's operating revenue is entirely a function of ridership, which itself is a function of the level of service provided and economic factors, such as employment levels and gas prices. In terms of influences on expense, MTA relies heavily on three factors to operate and maintain transit service:

- 1) *Union labor*: Approximately 75 percent of MTA's workforce is represented by unions and works under the terms of collective bargaining agreements, which set wages, hours, conditions of employment, and fringe benefit arrangements. In May 2013, MTA settled a 2-year contract with its union, Amalgamated Transit Union (ATU) Local 1300, representing approximately 2,500 MTA operations employees, including all operators and mechanics covering FY 2013-2014. The settlement provided union members with a 2.5 percent salary increase in FY 2013 retroactive to July 1, 2012 and a 2.5 percent salary increase effective July 1, 2013. Table 3 illustrates the increasing share of MTA's budget attributable to union wage and benefit costs.

Table 3: MTA Union Labor as Share of Operating Expense (\$000)

	FY 2010	FY 2011	FY 2012	FY 2013	Projected FY 2014
Union Labor Cost	\$214,980	\$236,676	\$238,184	\$237,817	\$257,880
Annual Growth	5.7%	10.1%	0.6%	-0.1%	8.4%
Total Operating Expense	\$610,286	\$621,917	\$646,795	\$665,843	\$689,072
Annual Growth	3.1%	1.9%	4.0%	3.0%	3.5%
Union % Of Total	35.2%	38.1%	36.8%	35.7%	37.4%

- 2) *Diesel fuel*: MTA is the largest purchaser of diesel fuel in State government, and the second largest purchaser in the State. In FY 2013, MTA purchased approximately 8.5 million gallons of diesel fuel, costing a total of \$27.2 million. MTA has begun to move its fleets to hybrid-electric buses and increase the use of biodiesel to improve fuel efficiency, but fluctuations in service levels and per gallon prices still present a large cost to MTA. While diesel prices dropped from FY 2008 through FY 2010, they began to increase through FY 2011 and FY 2012. While the average cost per gallon in FY 2013 is the same as FY 2012, there were wide fluctuations in the monthly prices ranging

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from a low of \$2.96 in July to a high of \$3.40 in February. MTA’s price per gallon for diesel fuel increased 49 percent from FY 2010 to FY 2013. Table 4 below shows diesel fuel price fluctuations in recent years.

Table 4: MTA Diesel Fuel, Average Price per Gallon, FY 2008-2013

	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>
Jul	\$2.26	\$3.96	\$1.81	\$2.16	\$3.20	\$2.96
Aug	2.23	3.42	2.01	2.23	3.12	3.26
Sep	2.39	3.32	1.92	2.24	3.15	3.34
Oct	2.48	2.93	2.05	2.41	3.04	3.32
Nov	2.78	2.17	2.14	2.49	3.22	3.33
Dec	2.78	1.66	2.10	2.65	3.09	3.26
Jan	2.79	1.58	2.23	2.77	3.18	3.21
Feb	2.79	1.48	2.16	2.94	3.28	3.40
Mar	3.28	1.37	2.28	3.22	3.42	3.17
Apr	3.52	1.58	2.37	3.40	3.36	3.00
May	3.80	1.60	2.32	3.23	3.20	2.99
Jun	4.00	1.90	2.19	3.12	2.85	2.97
Annual	<u>\$2.92</u>	<u>\$2.25</u>	<u>\$2.13</u>	<u>\$2.74</u>	<u>\$3.18</u>	<u>\$3.18</u>

- 3) *Repair parts:* MTA’s bus fleet has an average age of 6.8 years and average annual mileage in excess of 34,000 miles. The most-used buses in the fleet cover approximately 45,000 miles per year on average. MTA’s Light Rail fleet is over 20 years old, and the Metro subway fleet was purchased and put in service nearly 30 years ago. Both rail fleets increase total mileage annually, and all MTA fleets operate in the full spectrum of weather conditions. The annual mileage accumulated by MTA’s aging fleets requires a regular maintenance regimen and a significant inventory of spare parts, many of which have to be re-engineered as several parts manufacturers have gone out of business. The cost of these parts escalates each year, and newer, more sophisticated buses and trains often require more expensive parts.

Because these three cost elements increase annually due to inflation and market factors, the cost to provide the same level of service in the Baltimore area from year to year increases automatically.

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The revenue side of the farebox recovery equation is dependent on ridership and fare prices. Ridership is a function of service provision and quality, employment, population, and economic factors including gas and parking costs. Research has established that ridership increases are driven first by service availability and quality, and second by economic factors such as the relative cost of transit compared to other modes of travel.

Maintaining a *constant* farebox recovery ratio means that ridership (and thus fare revenues) must *increase at the same rate as expenses* each year. To *improve* farebox recovery, ridership and revenue growth must *exceed* the rate of growth in spending, or spending growth must be lower than ridership and revenue growth. Because of the spending factors cited above, MTA would typically need a 4-6 percent annual increase in Baltimore-area ridership to keep farebox recovery *constant at current levels*. In order to accommodate the 4-6 percent ridership increase, a corresponding increase in capital would also be required, equating to an additional \$8-10 million annually. This growth in costs is typical of the transit industry and properties nation-wide face the same issues in providing consistent, quality service while trying to attain sufficient revenues.

Historical farebox recovery expense and revenue totals for Baltimore local service and MARC are shown in Table 5². Note that in FY 2009, MTA saw low diesel prices combined with record growth in ridership, decreased expense and increased revenue. This combination had the effect of increasing the farebox recovery ratio for Baltimore local service. FY 2010 saw record snowstorms that decreased revenues along with the arbitrators ruling on the previous ATU 1300 contract, which significantly increased costs, and resulted in a lower farebox recovery. There was a recovery in ridership in FY 2011 and MTA continued to manage costs resulting in a slight increase in farebox recovery.

Table 5: MTA Farebox Recovery Expense and Revenue, FY 2009-2013 (\$000)

	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
Baltimore-area local service					
Total farebox expense	277,953	282,798	272,639	309,923	307,492
Annual increase	-3%	2%	-4%	14%	-1%
Total farebox revenue	85,163	80,060	79,960	84,452	84,985
Annual increase	1%	-6%	0%	6%	1%

² The farebox recovery rate for the Baltimore-area Commuter Bus is not included in this report, as it has not been for the last several years. The reason for this is that, although the MTA has a rough estimate of farebox recovery for this service (approximately 35 percent), the data on which the ratio is based cannot be verified through the State's Financial Management Information System (FMIS) due to the way the Commuter Bus contractors invoice MTA for their services. Currently and in prior years, Commuter Bus contractors invoice MTA by sending a document that shows gross costs minus revenue collected. This has been problematic in the past because the amount shown in FMIS makes no reference to the revenue collected. However, for FY 2014 and going forward, contractors will be invoicing in a way that will allow MTA to calculate farebox recovery for the Baltimore-area Commuter Bus similarly to MARC and MTA's other operating modes, and next year's report will contain this information.

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Farebox recovery ratio	31%	28%	29%	27%	28%
MARC service					
Total farebox expense	84,415	91,557	76,085	74,974	79,070
Annual increase	29%	8%	-1%	-1%	5%
Total farebox revenue	37,181	43,840	42,001	43,183	43,534
Annual increase	8%	18%	-1%	3%	1%
Farebox recovery ratio	44%	48%	55%	58%	55%

Current Projections

MTA's latest estimate of farebox recovery is shown in Table 6. FY 2015 projections include the anticipated revenues as a result of fare increases mandated by Chapter 429, Acts of 2013 (HB 1515). Farebox recovery ratios for Baltimore-area continue to fluctuate around 30 percent, ending FY 2013 at 28 percent. MARC farebox recovery is projected to remain well above the 50 percent requirement specified in the Transportation Article, §7-208 through FY 2015.

Table 6: Farebox recovery ratios, FY 2012 - 2015 (Est.)

	Actual FY 2012	Actual FY 2013	Estimated FY 2014	Estimated FY 2015 ³
Baltimore area service	27%	28%	27%	29%
MARC	58%	55%	53%	61%

³Assumes fare structure in accordance with Chapter 429, Acts of 2013 (HB 1515) will be implemented January 1, 2015

MARC expenses are driven by the level of service and the contracts MTA holds with Amtrak and CSX/Bombardier, who operate MARC service using MTA-owned rail equipment. Previously, CSX provided operations of trains and stations along their tracks, but CSX requested MTA provide this service. In FY 2013, Bombardier replaced CSX as the third-party operator of the Camden and Brunswick lines. Amtrak runs the Penn line and is still responsible for the operations of trains and stations along their tracks. Track access fees typically escalate annually; however, in FY 2012 the ARRA index was lower resulting in an increase in farebox recovery for that year. FY 2012 was a one-time event and the index increased approximately 6 percent in FY 2013 and is expected to do the same in future years, adding expense without increasing service.

Because of this imbalance in expense and revenue growth, farebox recovery on MARC service is projected to decline through FY 2014, though it will remain well above the statutory requirement of 50 percent.

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Attaining Required Farebox Recovery Ratios

Tables 7, 8, and 9 outline the actions required to meet the 35 percent Baltimore-area ratio through either fare increases or cuts to existing service levels, beginning in FY 2015 and continuing through FY 2019. Prior to implementing fare or service changes, public hearings and input for both fare increases and service adjustments are required, taking approximately 6 months to implement. Additionally, since the recently signed contract with ATU ends June 30, 2014, MTA will soon start negotiating with its largest union. The new contract could have additional cost implications. Due to these factors, implementing either solution in FY 2014 is not feasible.

While HB 1515 requires MTA to increase base fares prices and the cost of multiuse passes to the nearest 10 cents for all transit services, except for commuter rail and commuter bus service, by the same percentage as the biennial increase in the Consumer Price Index for all urban customers in FY 2015 and on a biennial basis, this is insufficient to achieve the mandated farebox recovery of 35 percent for core service.

In addition to increases required and planned for FY 2015, reaching the prescribed ratio would require a further fare increase to \$2.20 (+38 percent) assuming MTA is able to negotiate a cost neutral union contract. If the union contract is not cost neutral, higher fares would be required in order to match increased labor costs. Subsequent fare increases would be required to maintain the 35 percent farebox recovery level. Fare and revenue amounts shown below are rounded and are based on the proposed scenario currently under consideration.

Table 7: Fare increases required to meet the 35% farebox recovery ratio - Baltimore core service (\$000)⁴

	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Core riders (projected)	93,111	93,349	92,380	95,101	93,936
<i>% increase previous year</i>	0.6%	2.9%	0.7%	2.9%	-1.2%
Core expense (projected)	\$319,686	\$329,213	\$339,023	\$349,126	\$359,530
<i>% increase previous year</i>	2.1%	3.0%	3.0%	3.0%	3.0%
Fares @ 35% FBR	\$111,890	\$115,224	\$118,658	\$122,194	\$125,835
New fare required	\$2.20	\$2.40	\$2.40	\$2.40	\$2.50
Required annual increase	38%	9%	0%	0%	4%

⁴ Proposed fares do not include any additional costs for the union contracts, which expire in FY 2014 and are currently under negotiations.

Estimated service cuts to meet the 35 percent farebox recovery level are shown in Table 8. The size of the required service cut shown in Table 8 would necessitate layoffs of both union and management employees, as well as the sale or retirement of large portions of MTA's bus fleet in advance of their useful life cycle, requiring repayment of federal funds to the Federal Transit Administration. Table 8 assumes all costs are variable for demonstration purposes.

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Table 8: Service cuts required to meet the 35% farebox ratio – Baltimore core service (\$000)

	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Core riders (projected)	93,111	93,349	92,380	95,101	93,936
Fare revenue (projected)	\$84,771	\$93,905	\$96,480	\$99,332	\$115,902
Projected expense	\$319,686	\$329,213	\$339,023	\$349,126	\$359,530
Expense @ 35% FBR	\$242,202	\$267,157	\$275,657	\$283,806	\$331,150
Required annual service cuts to meet FBR	-22%	-19%	-19%	-19%	-8%

It is an understatement to say that a 22 percent reduction in service would affect MTA’s customer base and the future success of Baltimore-area transit operations. Fully 55 percent of MTA’s Baltimore-area riders are dependent on transit as their primary mode of transportation. Reducing service and reliability so extensively would virtually guarantee that riders would be driven away from transit options, reducing revenue and requiring further cuts to meet the farebox recovery ratio. This “vicious cycle” of declining service and declining ridership should be avoided at all costs.

Table 9, below, shows the impact on the Transportation Trust Fund of both the fare increase and service reduction options.

Table 9: Impacts to the Transportation Trust Fund, FY 2015-2019 (\$000)

	FY 2015	FY2016	FY2017	FY2018	FY2019
MTA fare increases					
Revenue to TTF	\$27,119	\$21,720	\$22,178	\$22,862	\$9,933
MTA service reductions					
Savings to TTF	\$77,484	\$62,056	\$63,366	\$65,320	\$28,380

MTA has made great strides in increasing the efficiency, cost-effectiveness, and productivity of its operations in the last four years. In FY 2013, 92 percent of MTA’s operating budget went directly to operating Statewide transit service. Recent efforts to make MTA more cost-effective include reducing overtime use, implementing a new absenteeism policy, and developing internal systems to track MTA’s efficiency and productivity with regular reviews of data and results.

Additionally, MTA has reduced its management workforce by 15 percent and deferred system-wide service expansions since FY 2009. Because of the large fixed cost of operations as well as MTA’s commitment to maximizing ridership and available service, gains from efficiency are not sufficient enough to impact significantly the farebox recovery ratio.

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Conclusion

MTA's farebox recovery ratio is to a large extent affected by external factors that the MTA cannot influence. The current statutory requirement reflects the collective wisdom of the legislature in recognizing that an arbitrarily high recovery rate could lead to fare increases that would disproportionately affect transit-dependent persons and lower-income individuals. These individuals cannot easily adjust their personal budgets to accommodate higher transportation costs.

Farebox recovery provides a good snapshot of changes to MTA's revenue in comparison to expenses, but should only be used to evaluate the MTA's effectiveness and efficiency in the broader context of the performance measures MTA reports annually to the General Assembly and of the MTA's overall mission. MTA was created to meet the need for a public service that could no longer be provided profitably by private enterprise. With that mission, the MTA works continuously to strike the delicate balance between reducing expenses and providing high quality transit service to attract a growing number of riders. MTA is committed to acting as a prudent steward of the taxpayers' resources that provide the majority of its funding, at a time when demand for transit service and the associated stress on the existing system continues to rise.