STAFF REPORT

MEETING DATE: 8/5/2020 **Staff Report No.** 20-062c

TO:	**AC Transit Board of Directors**
FROM:	**Michael A. Hursh, General Manager**
SUBJECT:	**New Budget Goals, Proposed FY 2020-21 Budgets, Bi-Monthly Review**

ACTION ITEM

RECOMMENDED ACTION(S):

Consider approving a new set of Budget Goals for FY 2020-21; receiving report on the Proposed FY 2020-21 Operating and Capital Budgets; and receiving the bi-monthly budget update for the period of July through June for the Fiscal Year 2019-20.

STRATEGIC IMPORTANCE:

Goal - Financial Stability and Resiliency
Initiative - Financial Efficiency and Revenue Maximization

Adopting updated budget goals will allow staff to better focus budget related efforts. Presenting a proposed budget to the Board allows for further Board review of the budget before final adoption.

BUDGETARY/FISCAL IMPACT:

The Proposed FY20-21 Operating Budget is balanced and includes a both projected operating revenues and expenses of $467.3 million. The budget is summarized in Attachment 3 with more details in Attachment 8.

The Proposed FY20-21 Capital Budget includes a projected spending plan of $81.9 million, composed of $54.8 million in grant funds, $7.8 million in District Capital funds, and $19.3 million of Line of Credit funds for the East Bay Bus Rapid Transit (BRT) Project. It is unchanged from the Draft Capital Budget. The Proposed Capital Budget is shown in Attachment 5.

BACKGROUND/RATIONALE:

Proposed New Budget Goals

The Board adopted a set of budget goals in March (shown in Attachment 1), just before the Bay Area and counties in the District's service area were ordered to shelter-in-place (SIP) due to the coronavirus pandemic. Since then, it has become apparent that the approved budget goals do not match the new economic and social realities of the pandemic.

Attachment 2 proposes a new set of budget goals that respond to the immediate issues the District is now facing for FY2020-21. The first goal and overriding concern of this time is the health and safety of all District employees and riders. The District continues to follow all relevant CDC, state and local health department guidance related to the pandemic. The District is committed to providing the proper safety equipment for our employees. The second goal is to be financially resilient in the recession caused by the pandemic. This means reducing expenses and maximizing all revenues available to the District.

The third goal is to have sufficient operations for the public. Reduced ridership, revenues, and social distancing requirements have forced the District to reduce service and capacity. The District has adapted to the situation during the current Emergency Service Plan and will continue to adapt as service levels are increased. The fourth goal is to enable the mobile workforce. The SIP requirements have forced administrative staff to work remotely. This has meant a quick focus on technology needed to allow administrative staff to continue to be productive from home. It will also mean adapting office environments for transitioning back while keeping the innovations that improve staff productivity.

The fifth goal is to have strong stakeholder, policymaker, and public communications. The pandemic has forced many changes in the District's service and operations. It is more important than ever to keep the lines of communication flowing. Riders and their communities need to know how service is changing and how they can be heard in deliberating those changes. The District must make its needs heard by policymakers and partners. Times of crisis make people hungry for good information, and the District must do its best to supply it.

Staff requests that the Board approve this new set of budget goals. Despite them not having been in effect from the beginning of the budget planning process, the new goals can still serve staff as they continue to work with what will be an evolving budget throughout this fiscal year.

Proposed Operating and Capital Budgets

Overview

The Proposed Operating and Capital Budgets build on what was presented in July for the Draft Budgets. The coronavirus pandemic continues to affect the local, national, and global economy and staff is continuing to watch trends towards the planned adoption of the budget in early September.

The basic revenue assumptions and ranges used to develop the Draft Budget have not changed. Farebox revenue has been reduced due to the estimated re-start of fare collection having been delayed until September. The estimates for property taxes and State Transit Assistance (STA) revenues have increased due to higher than expected returns through the end of FY 2019-20. These higher returns prompted staff to increase the baseline for calculations up while still applying the same overall reduction formulas used in the Draft Budget.

The federal Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law in late March and is providing the District with significant revenue relief. The Metropolitan Transportation Commission (MTC) approved the second allocation of funding in late July after the recommendation of the Blue Ribbon Transit Recovery Task Force. The District received a total of $114.2 million. This funding is crucial to allowing the District to continue functioning and keeping its workforce employed. The District drew on the first $30 million of this funding at the end of FY 2019-20 to fill in the revenue losses experienced, leaving the remaining $84.2 million available for this fiscal year. The Proposed Budget assumes use of all the CARES Act funding in FY 2020-21.

Service level plans for the fiscal year have not changed since the presentation of the Draft Budget and the planned increase to 75% of pre-pandemic levels occurs in August 2020. This balanced Proposed Budget will allow the District to continue with current service levels through the fiscal year without having to plan further service reductions. Staff will continue to operate the current emergency service network with minor adjustments as needed until FY21-22. By early calendar 2021 staff should have a better understanding of the revenue picture for FY21-22 which can then guide any service changes to be implemented that fiscal year. Budget and Planning staff continue to closely collaborate so that service levels can be maximized within available funds.

The District's cost structure is heavily based on how many people it employs, with bus operators being the largest employee group by far. The balance of the Proposed Budget depends on natural attrition of staff to gradually reduce labor costs over the fiscal year so that expenses end up within the forecasted revenue levels.

While this Proposed Budget is balanced, initial projections of the following budget years (FY21-22 and FY22-23) show significant deficits. This is primarily due to the uncertainty of further state or federal aid.

Revenues

The Proposed Operating Budget includes total revenues of $467.3 million, which is $2.0 million more than shown in the Draft Budget. Staff did not change the trend assumptions/calculations for the revenue sources but adjusted the baseline for those calculations in a few situations based on updated information. Changes from the draft are as follows:

- Farebox revenues are $24.9 million down from $26.7 million (-$1.8 million). This is due to the restart of fare collection being pushed back from August to September because of delays in the installation of operator virus shields. This is nearly 60% reduced from pre-pandemic levels.
- Property tax revenues are $147.3 million up from $144.7 million (+$2.5 million). Preliminary results from FY19-20 for property taxes are over budget by this amount, so staff adjusted the flat forecast by the same amount.
- STA revenues are $22.8 million up from $20.7 million (+$2.1 million). The 25% reduction forecast is now calculated from the actual results. As several counties are moving to the next phase of recovery, restrictions are being lifted, allowing stores to open. And since STA funds are derived from diesel sales taxes, trucking being the main contributor; staff feels that truck delivery traffic will hold up against any further reductions.
- CARES Act funds are reduced by $842,538 to match the actual approved allocation from the $115 million estimate.
- Cap & Trade Low Carbon Transit Operations Program (LCTOP) funds for BRT Operations are increased by $51,000 to match the actual allocation from the estimate.

Expenses

The Proposed Operating Budget is balanced, so expenses are also $467.3 million, which is $3.2 million less than shown in the Draft Budget. Staff continued to refine calculations and work with department managers to optimize their budgets, so there are many small changes that went into the Proposed Budget. The more significant ones are as follows:

- Labor expenses are $338.5 million down from $341.9 million (-$3.4 million). Labor is 72.4% of the total expense budget, which is down slightly from 72.6% from the Draft Budget. The major reasons for the change are:
    - Updated labor costing model - staff used the Prophix budgeting system to comprehensively model labor costs after starting with a simpler model for the Draft Budget. This includes increased expected savings from attrition and vacancies for the fiscal year.
    - Included 11 new positions at an ongoing cost of $1.2 million per year. The proposed new positions are shown in Attachment 4. The included positions were agreed upon by staff and the General Manager as crucial to the District despite the difficult budget situation. The rationale for the additions is discussed further in the report.
    - Increased healthcare costs of $1.9 million based on the updated costing model incorporating the new rates from Kaiser and HealthNet.
- Non-Labor expenses are $128.8 million up from $128.6 million (+$200,000). The major contributors to this change are:
    - East Bay Paratransit - reduced expense estimate by $2.6 million. Based on the recent analysis from staff on East Bay Paratransit usage the Proposed Budget is using the “moderate” estimate with an additional 10% contingency.
    - Staff increased the budget for the Salesforce Transit Center (STC) operating contribution (+$600,000) to match the final budget issued by the Transbay Joint Power Authority (TJPA). The District is facing an overall bill of $5.5 million to support the STC and Bus Storage Facility this fiscal year, a 25% increase from last fiscal year.
    - The professional services budget was reduced by $500,000 as budget and department staff worked to reducing requests to the essentials.
    - The District’s Clipper expense estimate was reduced by $300,000 based on further analysis. The transition to Clipper 2 has complicated the cost model for Clipper, along with the changing timeline for the elements that make up Clipper 2.
    - Staff increased its estimate for utility expenses by $280,000.

Positions/Headcount

Staff is proposing to reduce the budgeted headcount from 2,268 to 2,209. The number of budgeted bus operator positions would drop to 1,280 from 1,350. The District only has 1,274 bus operators on staff as this was written, so all positions removed are currently vacant. The headcount also includes the 11 new positions.

The proposed new positions are listed in Attachment 4. There is need for an additional Finance Administrator to reduce the extremely heavy workload on current payroll staff and ensure timely and correct employee pay. Four of the proposed new positions are due to the added infrastructure maintenance needs of the Tempo Bus Rapid Transit line: two Bus Stop Maintenance Workers; one Journey Facility Maintenance Mechanic; and one Senior Electronic Technician. And finally, staff is proposing to add six new Janitorial positions to help implement the enhanced cleaning protocols developed to combat the spread of the coronavirus.

Capital Budget

The Proposed Capital Budget is shown in Attachment 5. There are no changes to the Draft Capital Budget since its presentation.

Bi-Monthly Overview for July 2019-June 2020

The Bi-Monthly charts in Attachment 7 shows the District's preliminary and un-audited FY19-20 results, and a second chart shows the results just for the last quarter during the pandemic. A third page shows trends of selected expense categories. The full-year overall result shows an $11.0 million surplus, but this is primarily due to the $30.0 million in CARES Act funds that staff elected to draw down. In late-June when the CARES Act funds became available, staff had to make an estimate of what the year-end deficit would be and how much CARES Act funds to draw down. Revenues ended up coming above expectations, in particular property taxes and STA. And expenses came in lower than expected, particularly non-labor. This reduced the deficit staff expected to need to cover with CARES Act funds.

The CARES Act funds will most likely all be drawn down by the end of the calendar year, so except for the effect on the budgetary results, it is not particularly significant that $30.0 million was drawn down in June versus some other amount. The fact that this analysis shows a surplus for FY19-20 does not change the fact that the District is most likely going to be looking at a significant deficit for the FY2021-22 budget year.

Overall the results show what might be expected given the fourth quarter onset of the economic contraction due to the pandemic. Both revenues and expenses came in under budget, with the fourth quarter showing a particularly steep drop for some categories. Labor costs did not drop very much since all staff were kept on payroll with CARES Act funds. And as illustrated in the charts in Attachment 7, the significant reduction in service hit a few categories - fuel and materials - more than others. Highlights of the results are as follows:

Revenues

- Revenues for the full fiscal year were $13.6 million (-2.9%) below budget. Excluding CARES Act funds, revenues for the fiscal year were $43.6 million (-9.2%) below budget. For the fourth quarter, excluding CARES Act, they were $28.6 million (-24.1%) below budget.
- Farebox revenues were $15.1 million (-25.3%) below budget for the full year.
- Contract Services revenues were $2.1 million (-20.5%) below budget. This is not due to the pandemic, as these revenues were below budget by $1.0 million for the first half of the FY.
- Sales tax revenues were $9.6 million (-4.8%) below budget for the FY, but nearly -25% for the fourth quarter. Assuming that this time period was a low point for revenues, then next year's sales tax projections at -30% are conservatively positioned and should help buffer the District's revenue level.
- Property and parcel taxes came in at $3.5 million (2.4%) over budget for the full Fiscal Year. The final quarter results of $3.3 million over budget show that the overage was mostly all recognized in the final quarter.
- Other federal, state, and local (excluding CARES Act) was $19.9 million (-39.3%) for the full year.

Expenses

- Expenses for the full fiscal year were $21.9 million (4.6%) below budget. For the fourth quarter they were $20.0 million (17.0%) below budget. The major components of the drop in the fourth quarter were salaries and wages - primarily reduced operator overtime - and reduced East Bay Paratransit usage.
- Total Labor expenses were only $2.7 million (0.8%) below budget for the fiscal year. For the fourth quarter they were $5.8 million (6.9%) below budget. This is primarily due to reduced operator overtime in the fourth quarter.

- Fringe benefits were close to budget for both the full fiscal year and the final quarter. While Salaries and Wages dropped in the fourth quarter, Fringe Benefits did not due to the extra charges from the new leave provisions in the Families First Coronavirus Relief Act (FFCRA).
- Pension Expense was over budget by $3.2 million (-5.5%) for the full year. Staff expected this outcome as the budget was based on an early and low actuarial valuation.
- Services were $5.2 million (13.8%) below budget, with more than half of this due to the fourth quarter.
- Fuel and Lubricants were $3.9 million (25.5%) below budget for the year. The bulk of this is from the fourth quarter, but prices had started to decline a bit before the pandemic hit.
- Other Materials and Supplies were $861,000 (4.4%) under budget for the fiscal year. The fourth quarter was $1.6 million (32.5%) under budget due to reduced service levels leading to a reduction in bus parts spending. The fourth quarter was significantly under budget despite increased spending on protective equipment.
- Casualty and Liability was under budget by $1.5 million (9.1%) for the year.
- ADA/Purchased Transportation was under budget for the year by $5.4 million (15.6%), and $5.4 million (62.3%) for the final quarter due to a significant drop in East Bay Paratransit demand.

Going Forward

Staff plans to follow up in the Recommended Budget staff report with an analysis of revenue and expense "signs" they will be looking for as the year progresses.

ADVANTAGES/DISADVANTAGES:

The advantage of adopting new budget goals is to recognize the realities of the current pandemic and how they are having a great effect on the agency. Staff does not see any disadvantage to adopting new budget goals.

ALTERNATIVES ANALYSIS:

Staff considered continuing with the existing budget goals or using the new goals alongside the existing goals but felt that the situation required affirmative actions to acknowledge the changed situation that staff is working in.

PRIOR RELEVANT BOARD ACTION/POLICIES:

SR 20-062 FY 2020-21 Budget Goals & Objectives // SR 20-062a Delay in Adoption of FY20-21 Budget and Continued Spending Authority // SR 20-062b Draft FY20-21 Operating and Capital Budgets

ATTACHMENTS:

1. Adopted Budget Goals
2. Proposed New Budget Goals
3. Proposed Operating Budget
4. Proposed New Positions
5. Proposed Capital Budget
6. Proposed Budget Presentation
7. Bi-Monthly Report

8. Proposed Budget Book

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