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**July 17, 2020**

**TO: BOARD OF DIRECTORS**

**THROUGH: PHILLIP A. WASHINGTON** *PAW*  
**CHIEF EXECUTIVE OFFICER**

**FROM: NALINI AHUJA** *Nalini Ahuja*  
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**SUBJECT: FISCAL YEAR 2021 BUDGET DEVELOPMENT PROCESS**

**ISSUE**

On May 28, 2020, the Board approved the Continuing Resolution which allows Metro to develop a fiscally responsible budget plan by re-assessing the financial constraints created by COVID-19. This report sets up the economic environment and resources available for the next fiscal year, followed by a series of updates to the Board to restart the FY21 Budget development process. The FY21 Proposed Budget will be presented in September 2020 for Board consideration for adoption after public input and outreach.

The budget process estimates and allocates resources that are available and eligible to achieve Metro Vision 2028 goals in a manner that is fiscally sound and financially responsible. In the upcoming months, the FY21 Budget development will review key economic factors affecting revenues and expenses, setting program deliverable objectives to operate, expand, plan and fund regional Transit and Transportation systems, while incorporating stakeholder input and demonstrating agency accountability and performance.

**DISCUSSION**

**Background**

In March 2020, the State of California, County and City of Los Angeles issued Safer At Home orders in response to the global pandemic, COVID-19. The outbreak has had a negative impact on the Agency's financials and operations. As a result, the assumptions of resources and revenues upon which the pre-COVID FY21 Budget would have been built has changed significantly. Currently,

major funding sources such as sales tax revenues and fare revenues that fund Metro services and functions have sharply declined.

Metro continues to pursue stimulus and recovery subsidies from FEMA, Federal and State governments. Although the Federal CARES Act signed on March 27, 2020 provides \$1 Billion for LA county transit operators on a reimbursement basis, the CARES Act alone will not cover all of Metro's losses. Furthermore, due to reimbursement eligibility, the CARES Act is unable to meet all the needs of Metro and regional transportation. Metro will experience near term cash flow challenges because of reimbursement timing.

### Sales Tax Revenue Assumptions

Metro relies on sales taxes for more than half of its total revenues. In addition, cities and other transit providers in Los Angeles County plan their operations based on Metro's revenue projections. This fact necessitates a careful evaluation and forecasting to determine the funding levels for FY21.

The COVID-19 pandemic continues to have a devastating impact on retail sales in Los Angeles County. Actual sales tax revenues declined dramatically starting in March, 2020. With so much continuing uncertainty going forward, a different approach was necessary to create a revised forecast.

Since the economic impacts of the pandemic are spread unevenly among economic sectors, the revised forecast is being developed with a bottom-up approach by estimating revenue impacts by sector. The model shown below lists major sectors and the percentage of county sales tax revenues generated by each. The estimated rate of change was developed through 1) independent research of local and industry sales data, 2) information from other agencies in the state that also collect local sales taxes, several of whom are utilizing a very similar approach, and 3) reviews with economic forecasters including UCLA Anderson Forecast and Beacon Economics.

Leisure and hospitality activities are suffering most from the restrictions, so sales tax revenues from restaurants are projected to fall the most. Big ticket consumer purchases are expected to suffer steep declines, so auto sales, furniture, and appliances are reduced dramatically. Non-essential general retail categories like apparel and recreation products are heavily reduced as well. Given the dramatic drop in gasoline prices and consumption, service stations are also hit hard. On the other end, many business to business activities are assumed to see more modest drops. Drug stores are expected to see only modest declines in sales tax revenues, while grocery store sales are expected to hold relatively steady. Finally, miscellaneous retail is also projected to hold steady as many online retailers are included in that category. Projected Year-over-year declines in select categories are highlighted in the table below.

## Projected Sales Tax Revenue Declines by Economic Sector

	% of total	FY20-Q3	FY20-Q4	FY21-Q1	FY21-Q2	FY21-Q3
<b>General Retail</b>	27.18%					
<b>Apparel Stores</b>	<b>5.78%</b>	<b>-20%</b>	<b>-60%</b>	<b>-55%</b>	<b>-30%</b>	<b>0%</b>
<b>Department Stores</b>	<b>7.43%</b>	<b>-20%</b>	<b>-40%</b>	<b>-30%</b>	<b>-20%</b>	<b>10%</b>
<b>Furniture/Appliance</b>	<b>3.55%</b>	<b>-20%</b>	<b>-60%</b>	<b>-55%</b>	<b>-30%</b>	<b>0%</b>
Florist/Nursery	0.33%	0%	-25%	-15%	-5%	5%
Miscellaneous Retail	8.15%	0%	-10%	-5%	0%	5%
<b>Food Products</b>	20.01%					
<b>Restaurants</b>	<b>14.85%</b>	<b>-25%</b>	<b>-80%</b>	<b>-60%</b>	<b>-30%</b>	<b>0%</b>
Liquor Stores	0.65%	-3%	-20%	-20%	-10%	0%
Food Processing, Equip	0.57%	-5%	-30%	-20%	-20%	0%
<b>Transportation</b>	19.15%					
<b>Auto Sales - New</b>	<b>7.91%</b>	<b>-15%</b>	<b>-60%</b>	<b>-55%</b>	<b>-40%</b>	<b>0%</b>
<b>Auto Sales - Used</b>	<b>1.31%</b>	<b>-15%</b>	<b>-60%</b>	<b>-55%</b>	<b>-40%</b>	<b>0%</b>
<b>Service Stations</b>	<b>6.86%</b>	<b>-15%</b>	<b>-40%</b>	<b>-25%</b>	<b>-10%</b>	<b>5%</b>
<b>Construction</b>	8.35%					
Bldg, Matis-Wholesale	5.11%	0%	-20%	-10%	-5%	5%
Bldg, Matis-Retail	3.24%	0%	-20%	-10%	-5%	5%
<b>Business To Business</b>	20.62%					
Office Equipment	3.34%	-5%	-40%	-30%	-20%	0%
Electronic Equipment	1.05%	-5%	-40%	-30%	-20%	0%
Business Services	1.74%	-5%	-40%	-30%	-20%	0%
Energy Sales	1.17%	-20%	-40%	-30%	-20%	0%
Chemical Products	0.78%	-5%	-40%	-30%	-20%	0%
Heavy Industry	3.56%	-5%	-30%	-20%	-10%	5%
Light Industry	4.37%	-5%	-40%	-30%	-20%	0%
Leasing	4.34%	0%	-30%	-20%	-10%	5%
Biotechnology	0.04%	0%	-20%	-20%	-10%	5%
I.T. Infrastructure	0.12%	0%	-20%	-20%	-10%	5%
Green Energy	0.10%	0%	-40%	-30%	-20%	0%
<b>Miscellaneous</b>	2.61%					
Health & Government	1.62%	0%	-20%	-20%	-10%	0%
Miscellaneous Other	0.99%	-10%	-30%	-30%	-10%	0%

While the intensity of the downturn is already evident, the bigger issue in projecting FY21 revenues is the duration and the shape of the recovery. The assumption is a six-quarter economic impact starting in the third quarter of FY20 when the safer-at-home orders began. The largest decline is expected in the fourth quarter of FY20 with only a marginal improvement in the first quarter of FY21. Then a gradual recovery is expected to take hold in the Fall with gradual improvement over the remaining three quarters of FY21.

Combining the impacts from all economic sectors and distributing them over time using the assumptions of the intensity and duration of the downturn, the model generated a sales tax revenue projection as follows:

<b>Fiscal Quarter</b>	<b>Months</b>	<b>Reduction from Budget/Proposed</b>	<b>Key Assumptions</b>
FY20 Q3	Jan-Mar 2020	-11%	Slowing of consumer spending; Safer-at-home orders implemented mid-March
FT20 Q4	Apr-Jun 2020	-41%	Severe economic downturn due to lockdown
FY21 Q1	Jul-Sep 2020	-32%	Marginal improvement as businesses begin to reopen
FY21 Q2	Oct-Dec 2020	-14%	Recovery begins in fall
FY21 Q3	Jan-Mar 2021	-12%	Recovery continues but may slow due to second wave
FY21 Q4	Apr-Jun 2021	-2%	Recovery nearly complete by end of FY21

We are continuing to monitor retail sales trends and sales tax revenues and may revise our estimates as new information becomes available.

#### Other Resource Assumptions

##### Passenger Fares

The large reduction in travel due to the safer-at-home orders, telecommuting and physical/social distancing combined with rear door boarding on Metro buses has severely reduced fare revenues. With passenger boardings expected to follow the same rate of recovery and duration described above and the implementation of reduced pass prices by 50% through December, preliminary estimated FY21 fare revenue will be in the range of \$40-\$80 million. We will continue to monitor fare revenue trends as public health indicators or COVID-19 threat levels improve.

##### Toll, Advertising and Others

All revenue sources are impacted by the pandemic. Toll revenues of \$43.8 million are projected in FY21 which include ExpressLanes usage and violation fees from the existing I-10, I-110. For advertising revenue, \$22.8 million based on new and existing contracts is expected in FY21. Other revenues including bike program, Union Station, park and ride, lease, film, Service Authority Freeway Emergencies (SAFE), county buy down, auto registration fees, transit court fees, CNG credits, investment income and other miscellaneous revenues are anticipated at a total of \$71.6 million in FY21. The total amount of \$138.2 million in this category represents a decline of 18% from FY20 Adopted Budget levels.

## Grant Resources

An overall total of \$1.2 billion in local, state and federal grant resources are projected in FY21 to support Metro's transit planning, operating, state of good repair and construction activities. These are normal transportation grants that Metro receives either by formula or through competitive processes.

Additional grant funding to support continued operations and additional safety measures required as a result of the COVID-19 pandemic is not included in this amount. The only known amount currently is funding received from the CARES Act. A total of \$1.068 billion was apportioned to Los Angeles County, with \$874 million coming to Metro, of which \$102 million was allocated from Metro to other transit operators in the region. It is important to note that the CARES Act does not cover all of Metro's losses in bus and rail operations and provides no funding for transit infrastructure projects.

Additional funding received from FEMA and any future legislative actions will be added to the budget as they become known and realized.

## **Resource Assumption Summary**

### **Fiscal Year 2021 Pre-Covid Versus Post-Covid Estimated Revenues**

<b>Resources (\$ in Millions)</b>	<b>FY21 Pre-Covid Assumption</b>	<b>FY21 Post-Covid Assumption</b>	<b>Pre/Post Covid % Change</b>
Sales Tax and TDA Resources	\$ 4,095.0	\$ 3,487.9	-14.8%
STA and SB1 Revenues	245.9	228.8	-7.0%
Passenger Fares*	281.6	60.0	-78.7%
Toll, Advertising and Others	153.3	138.2	-9.9%
Grant Resources	1,227.1	1,225.2	-0.2%
<b>Total (Excluding New Bond Proceeds)</b>	<b>\$ 6,002.9</b>	<b>\$ 5,140.0</b>	<b>-14.4%</b>

\* For FY21 Post-Covid Assumption, the midpoint of the range of \$40-\$80 million is used

## Budget Process and Schedule

The May 2020 Continuing Resolution adoption by the Board provides an opportunity to reset the financial forecast and allow Metro to develop a fiscally responsible budget plan to deliver FY21 goals within the current economic constraints. In order to meet the financial challenges ahead, the FY21 Budget process is redesigned so that staff can reassess budget expenditures, monitor financial conditions, reforecast available revenues and resources, and provide full transparency with the public and stakeholders. Staff will continue to monitor the evolving economic crisis, and will perform a mid-year adjustment if required.

## Board of Directors Updates

Beginning in June, detailed budget briefings on the revised FY21 Budget are being presented to the Board through Board staff. These briefings are providing an in-depth update of the budget development for every Metro department, as well as a comprehensive look at all revenues, expenses, and project deliverables planned for FY21. In addition to these briefings, staff will continue to update the Board by providing monthly reports.

From Board adoption of the Continuing Resolution in May to final Board Adoption of the FY21 Budget in September, the schedule of topics to be presented is as follows:

Date	Action
May	Board Adoption of Continuing Resolution
June	Board Staff Briefing on Budget Process, Revenues, and Outreach
July	Board Box on Budget Process, Revenue Assumptions and Outreach
August	Board Report and Board Staff Briefings on Budget Status
September	Board and Board Staff Briefings on FY21 Proposed Budget September 16: Public Hearing September 24: Final Board Adoption
December	Board Midyear Budget Amendment (As needed)

## FY2021 Budget Outreach Update

In light of the recent COVID-19 outbreak, the in-person FY21 Budget Outreach was temporarily put on hold in mid-March, while online outreach continued. We are now in the process of resuming all FY21 Budget outreach activities on the virtual platforms; moving forward with engagement and education of the FY21 Budget. Soliciting meaningful input from the public and stakeholders via public workshops, community meetings, the Public Hearing, and public comments from Metro's email comment line to ensure the greatest level of awareness about the budget and engagement possible. Keeping in line with Metro policy on social/physical distancing, all meetings will be held on video conferencing platforms, thus meeting all public involvement and participation requirements during the COVID-19 pandemic.

Additionally, to achieve greater participation, Service Councils, Citizen Advisory Groups and Board appointed subcommittee meetings will be advertised via a digital campaign utilizing the agency's communications channels such as the creation of Facebook (FB) events on Metro's FB page, amplifying budget outreach events on the FB page of ongoing Metro construction projects, Instagram stories, Nextdoor, Twitter posts, TheSource, and e-blasts. These

strategies will drive the public to visit the Metro’s website ([metro.net/myvoice](http://metro.net/myvoice)), to learn about the budget, get current budget information, view the schedule of the various outreach meetings and tell us their priorities by filling out the questionnaire. We will also resume the previously planned marketing strategies on bus posters, messages on hold, and Union Station’s East Portal Ticker.

Finally, the legally required public budget hearing will culminate the public outreach process in September 2020. Staff will provide monthly Board updates on the FY21 Budget Outreach activities.

Below is the tentative schedule of the FY21 Budget Outreach for stakeholders and community meetings.

<b>Stakeholder and Public Outreach Efforts</b>	
Metro FY21 Budget Briefing – Regional Service Councils	Sept. 3
Technical Advisory Committee (TAC)	Sept. 2
Citizens Advisory Council (CAC)	Sept. 4 & 23
Bus Operator Subcommittee (BOS)	Sept. 15
Local Transit Systems Subcommittee (LTSS)	Sept. 17
Streets & Freeways Committee	Sept. 17
Public Hearing	Sept. 16

**NEXT STEPS**

As described earlier in this report, Metro staff will provide regular Budget briefings to Board members and their staff starting this month. Further, we will provide Board Box and Receive-and-file reports on a monthly basis, as previously detailed.