Item #9

Preparation for Initiating the FY25 Budget Development Process

Finance, Budget, Audit Committee

October 18, 2023

Meeting Agenda

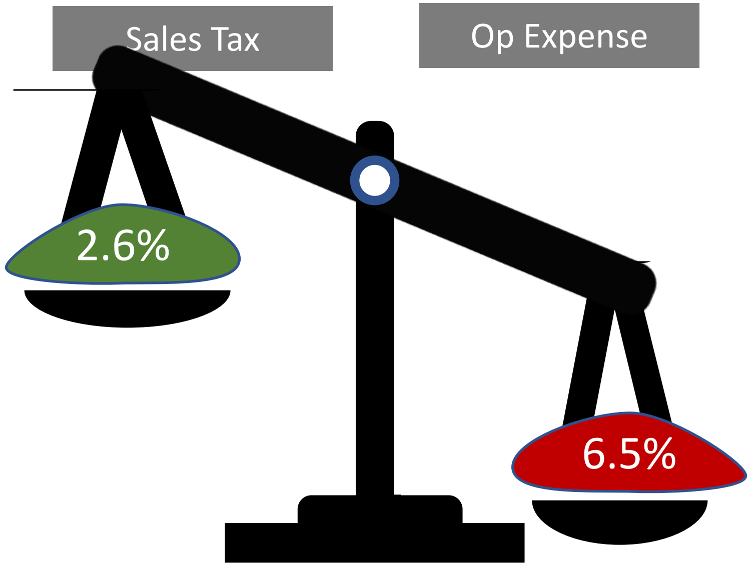
- Metro Transit Cost Growth Drivers
  - Labor
  - Parts, Fuel, Power and Contract Services
  - Insurance Premiums
  - Public Safety, Law Enforcement
  - Cleaning
  - Rail Expansion
  - Electrification
- Transit Infrastructure Construction Risks
- Other Programs Challenges
- Equitable Zero-Based Budgeting (EZBB) & Next Steps

Metro Transit Expense Financial Outlook (FY24 – FY29)

- Exhaustion of one-time federal stimulus funding that was used to balance budgets the last 3 years

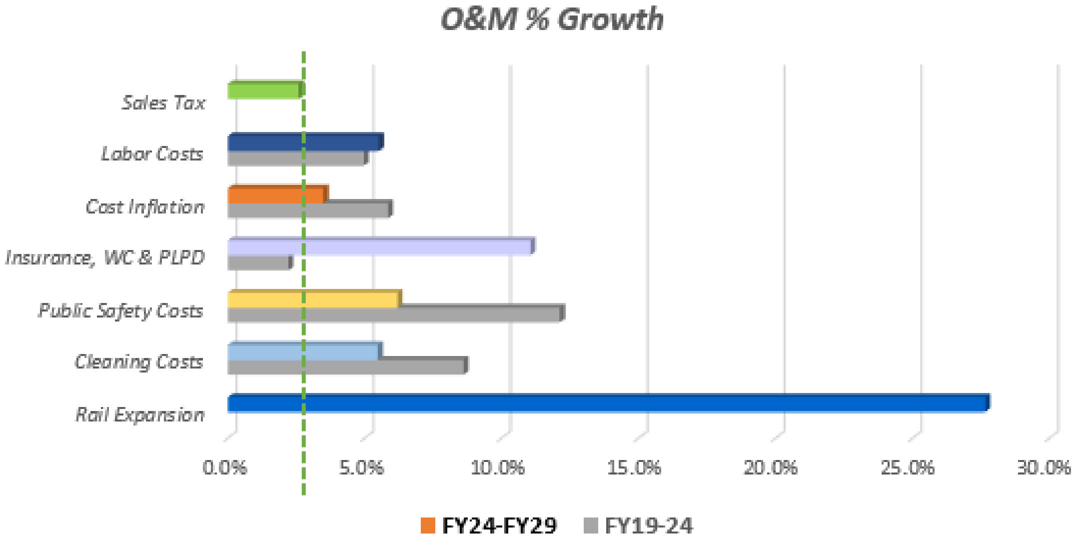
- Operating cost growth (6.5%) is increasing faster than sales tax and operating revenues (2.6%):
  - Escalating labor, insurance and cost inflation to run current level service
  - Operating an expanding rail system
  - Incremental costs for enhancing safety and cleaning with no offsetting cost savings

- Major investments in Capital Improvement Program (CIP) for electrification efforts



Cost Growth Drivers for Metro Transit Operations

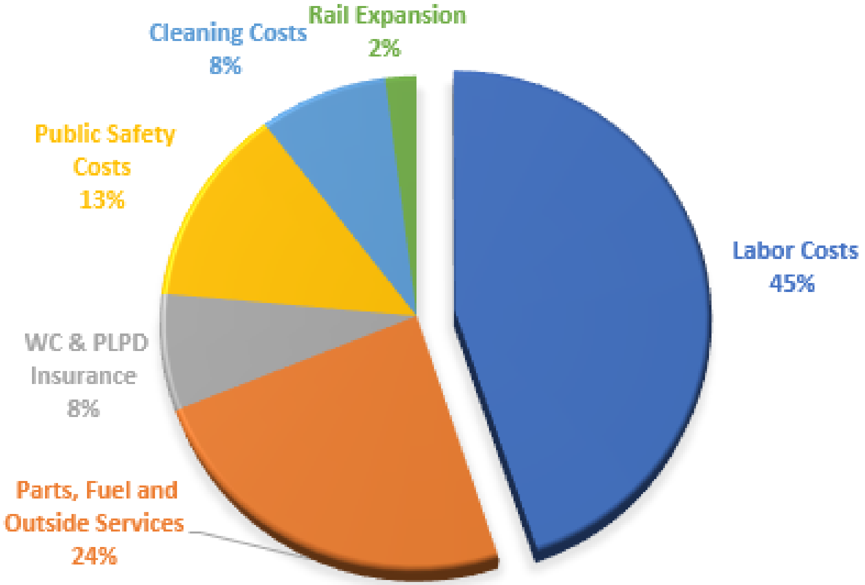
- The Agency's Near-Term Outlook on Metro Transit Operations & Management (O&M) includes significant cost growth drivers:
  - Labor costs
  - Cost inflation for parts, fuel, power and contract services
  - Insurance, Workers' Comp and PLPD
  - Public safety
  - Cleaning
  - Rail expansion



- Historical growth rates have been on the high side and expected to continue the trend over the next five years. The forecast includes recent cost control measures from EZBB
- Every cost growth driver is anticipated to grow at a faster rate than sales tax revenues

Cost Growth Driver - Labor Costs

- Total operating labor costs make up 45% of total Metro Operations costs
- Labor costs have had a historical growth of 5% per year
- Labor cost inflation assumptions include the latest SMART contract from July 2022
- A projected trend for growth is anticipated for the next 5 years and subject to change based on the upcoming negotiations for the remaining Collective Bargaining Agreements

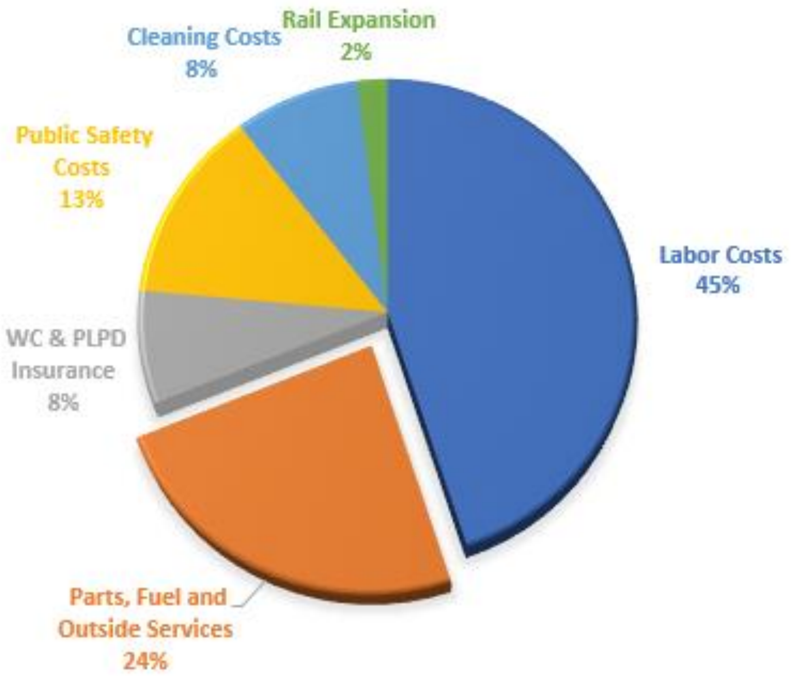


Cost Growth Driver - Parts, Fuel and Outside Services

- Total operating costs for parts, fuel, power and contract services make up 24% of total Metro Operations costs

- An average 6.0% growth per year over the last five years attributed to:
    - Historical high rates on CNG fuel and propulsion power
    - Parts and supplies growth due to supply chain constraints
    - Contract services from labor shortage challenges and record high inflation

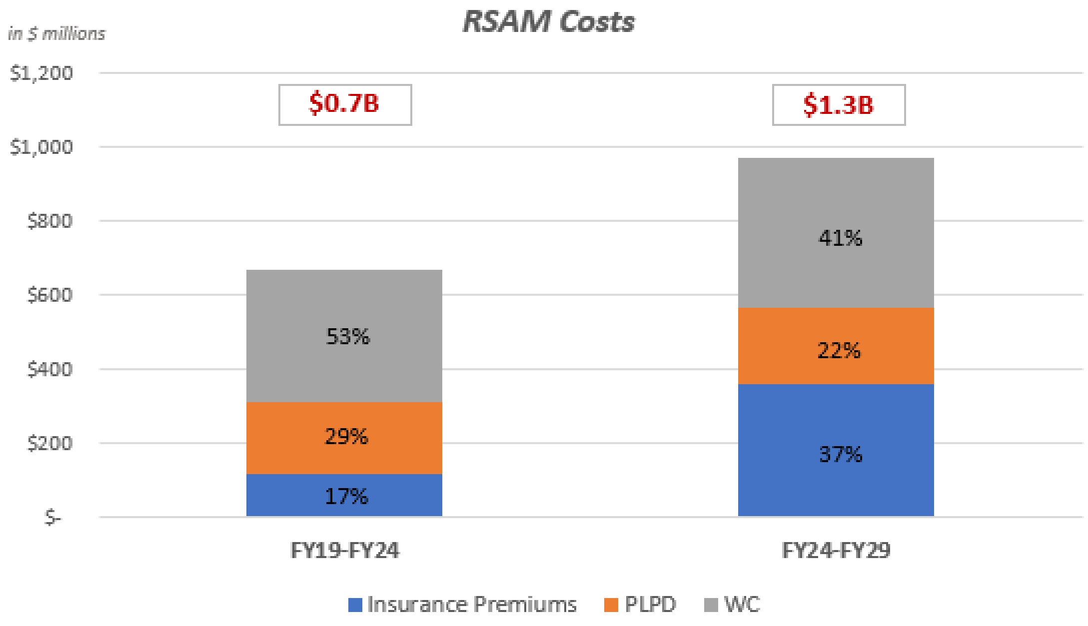
- An average 3.5% future growth per year for the next five years due to new rail service, station maintenance, and CPI cost increases



Cost Growth Driver – Insurance, Workers’ Comp and PLPD

- Total insurance, workers’ compensation and PLPD costs make up 8% of total Metro Operations costs

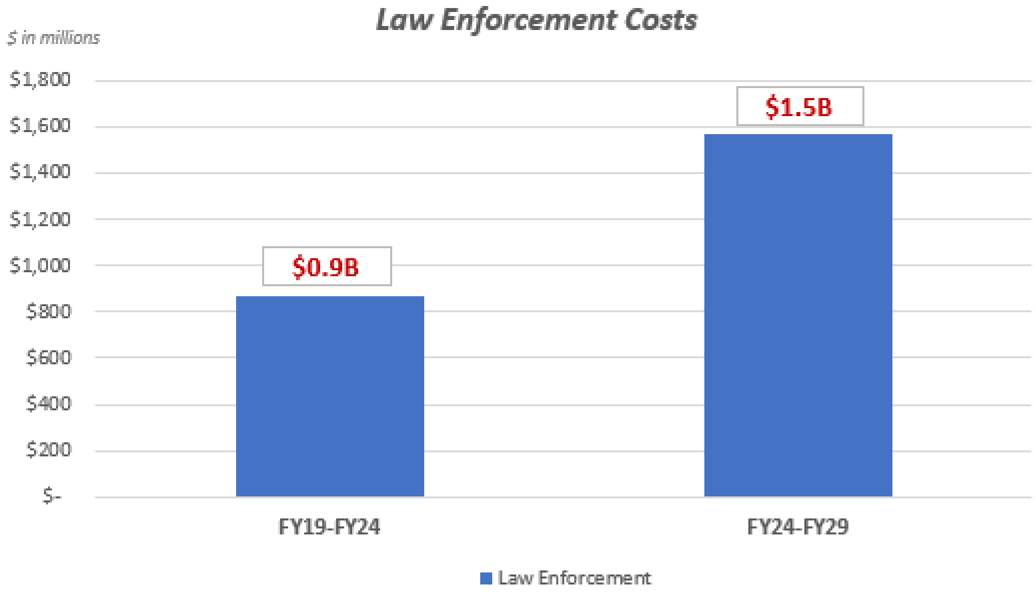
- Insurance premiums have experienced a double-digit growth per year over the last five years due to:
  - Insurance market industry has hardened due to string of natural disasters and extensive losses experienced
  - Additional assets to insure due to an expanding rail system



- An average 20% growth per year for the next five years for insurance premium costs is projected due to the trend of the insurance market industry, making up 37% of the total costs in the next five years

Cost Growth Drivers - Public Safety, Law Enforcement Costs

- Public safety costs make up 13% of total Metro Operations with law enforcement costs as the biggest driver (about 65% of the total)
- Last five-year contract value of $870M vs. a possible estimated $1.5B for next five years based on the historical cost growth by continuing existing practice
- Total law enforcement costs will nearly double the next five years vs. last five years



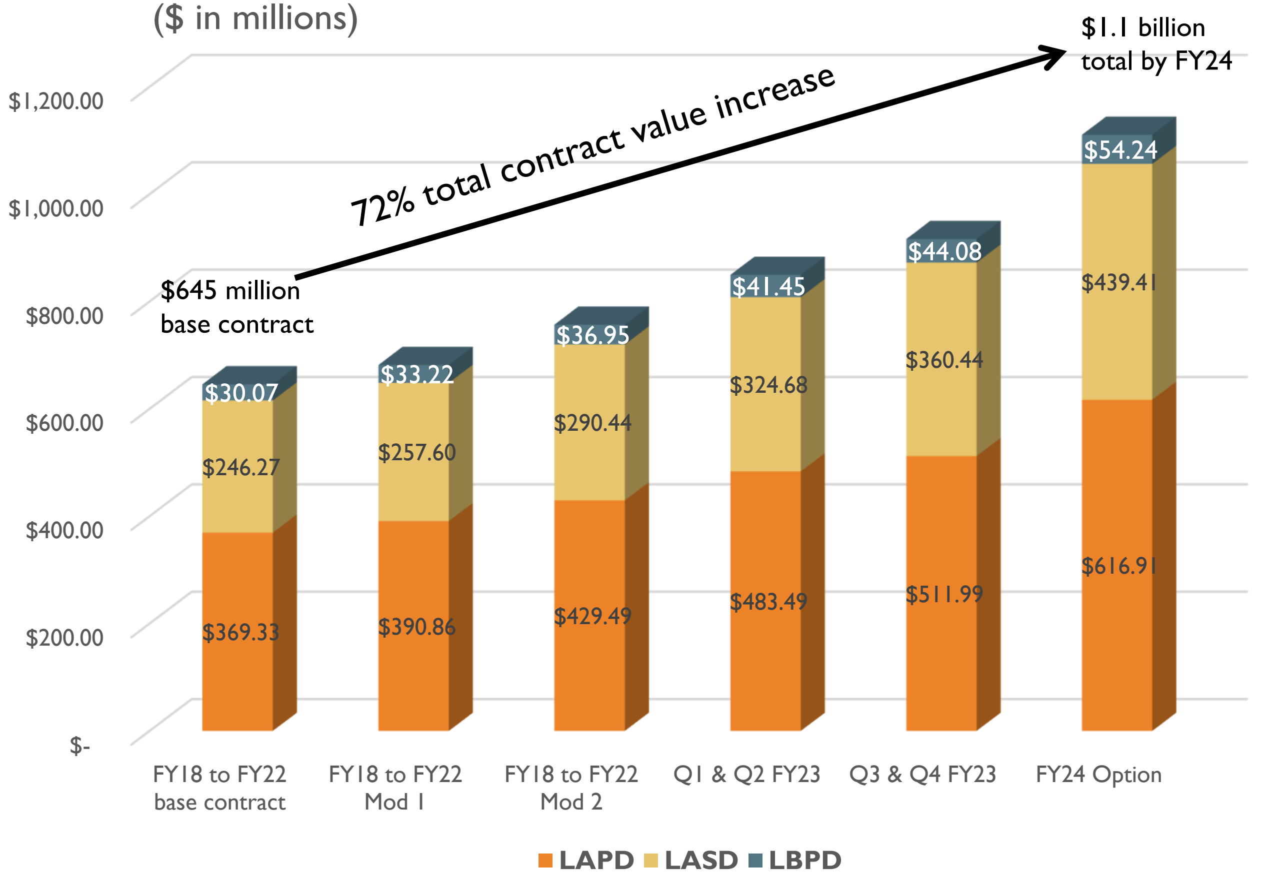
LAW ENFORCEMENT CONTRACT VALUE FY18 TO FY24 BY AGENCY

Current multi-agency law enforcement contract value changes from FY18 to FY24:

Increase $ in millions	LAPD	LASD	LBPD	Total
FY18 to FY22 base contract	$ 369.33	$ 246.27	$ 30.07	$ 645.7
FY18 to FY22 Mod 1	$ 21.53	$ 11.33	$ 3.15	$ 36.0
FY18 to FY22 Mod 2	$ 38.63	$ 32.84	$ 3.73	$ 75.2
Q1 & Q2 FY23	$ 54.00	$ 34.24	$ 4.50	$ 92.7
Q3 & Q4 FY23	$ 28.51	$ 35.76	$ 2.63	$ 66.9
FY24 Option	$ 104.92	$ 78.98	$ 10.16	$ 194.1
Total Contract Value	**$ 616.91**	**$ 439.41**	**$ 54.24**	**$ 1,110.6**
Total % increase	**67%**	**78%**	**80%**	**72%**

Metro System Increase	FY18 to FY24
Law Enforcement Contract CAGR (Compound Annual Growth Rate)	9.5%
All other Metro Contract CAGR	5.7%
Bus and Rail Operating Budget CAGR	5.9%

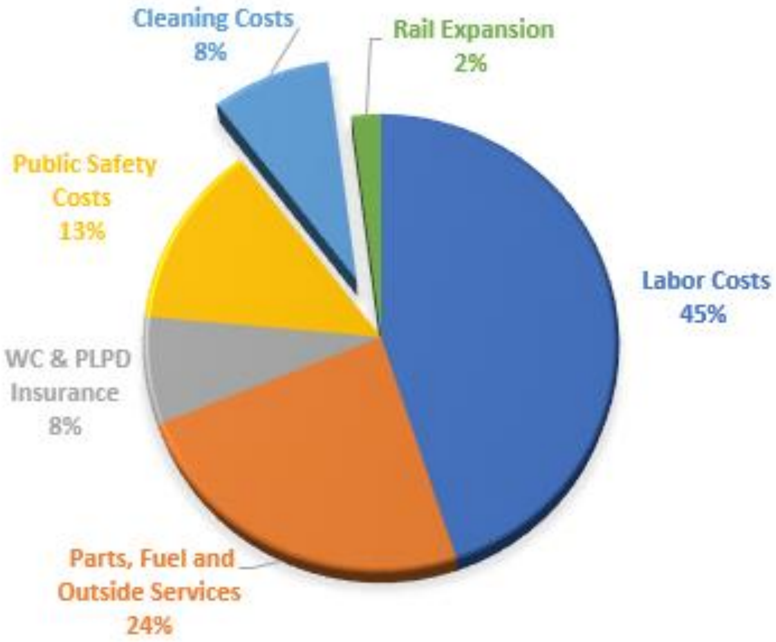
Total contract value by agency
($ in millions)



Metro

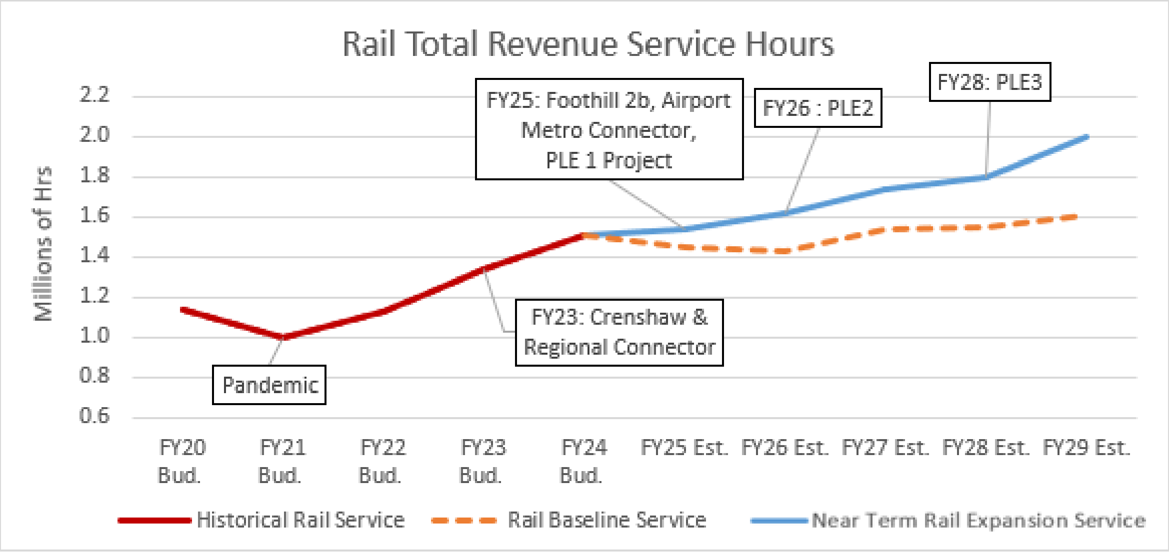
Cost Growth Driver - Cleaning

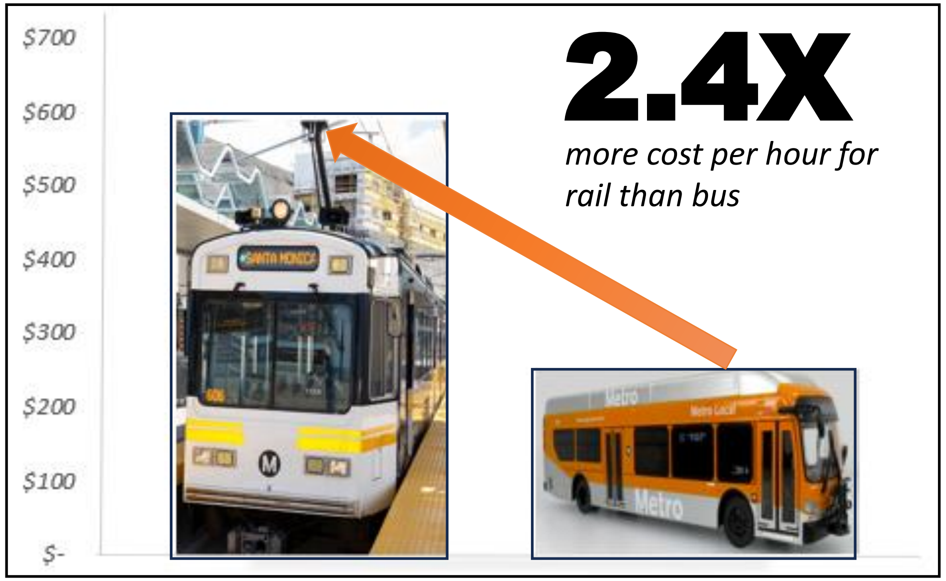
- Cleaning costs make up 8% of total Metro Operations costs
- An average 8.6% growth per year over the last five years attributed to homeless crisis and opioid epidemic challenges, along with the pandemic.
    - Roving cleaning teams
    - Custodial staff
    - Part-time custodial Room to Work participants
    - Frequent “in-line” and mid-day bus interior cleaning
    - End of line cleaning on rail, station hotpots and other activities
- An average 5.5% growth per year for the next five years is projected due to continuing to deliver a cleaner system and improve customer experience



Cost Growth Driver - Rail Expansion

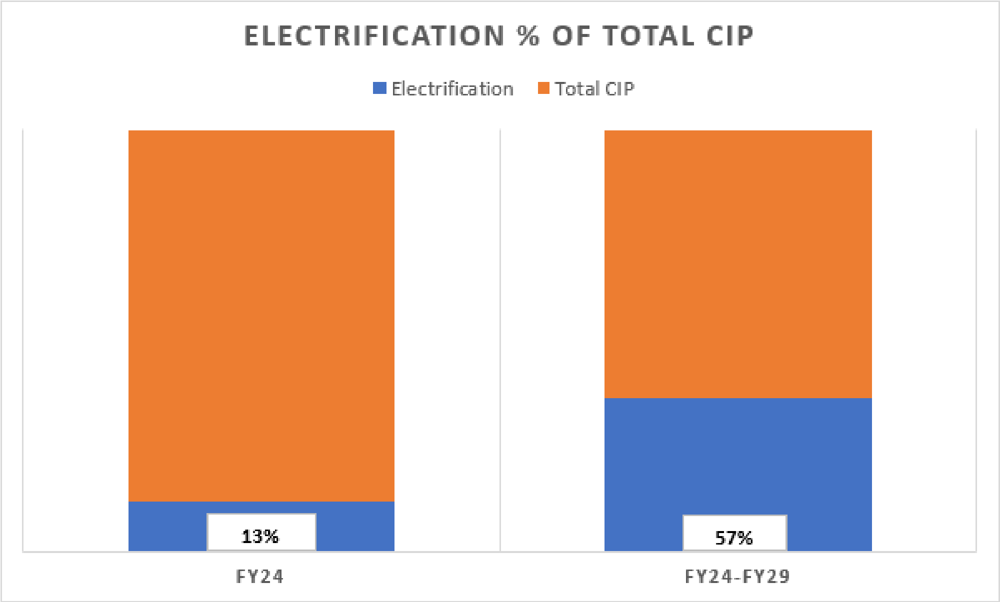
- Metro is undergoing a major rail expansion network with the anticipated opening of Foothill Phase 2B, Airport Metro Connector, Purple Line Extensions 1, 2, and 3
- Anticipated operating and maintenance cost of integrated regional facilities (i.e., Airport Metro Connector (AMC))
- The cumulative incremental cost for the expansion is projected at $342 million, or 27.6% per year average growth from FY24 through FY29
- The average cost of running 1 hour of rail is 2.4x more than operating 1 hour of bus service





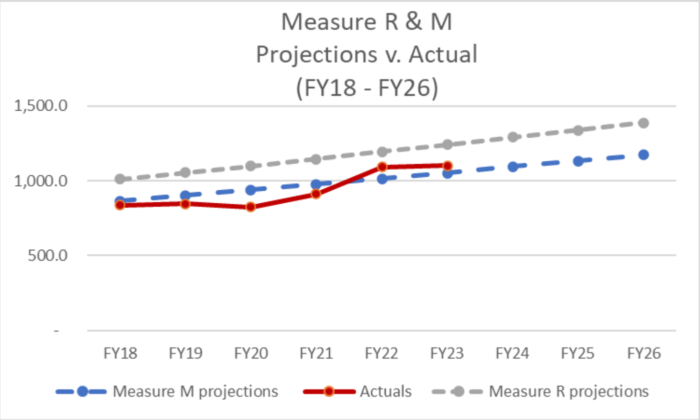
Major Investments in Capital Improvement Program (CIP)

- Electrification Goal
  - The implementation of the zero-emission bus program is a significant capital cost to meet the State of California's 2040 mandate for eliminating the use of hydrocarbon fueled buses
  - Metro's Near-Term Outlook assumes an accelerated goal of achieving a zero-emission fleet by 2030, which includes procuring zero-emissions Battery Electric Buses (BEB) and related electric charging infrastructure
  - This effort will require a minimum investment of $4.3 billion in buses and charging infrastructure through 2030
  - In today's budget, electrification makes up 13% of the total CIP program and that would need to grow to be 57% over the next five years to meet the 2030 goal. Note: external funding has not been secured and would require deficit spending
  - New zero emission bus acquisitions and supporting infrastructure development will proceed as available technology and funding permit



Transit Infrastructure Construction Risks

- Metro recognizes the additional financial risks stemming from Transportation Infrastructure Development (TID) as Metro continues to build out the ordinance approved major construction projects



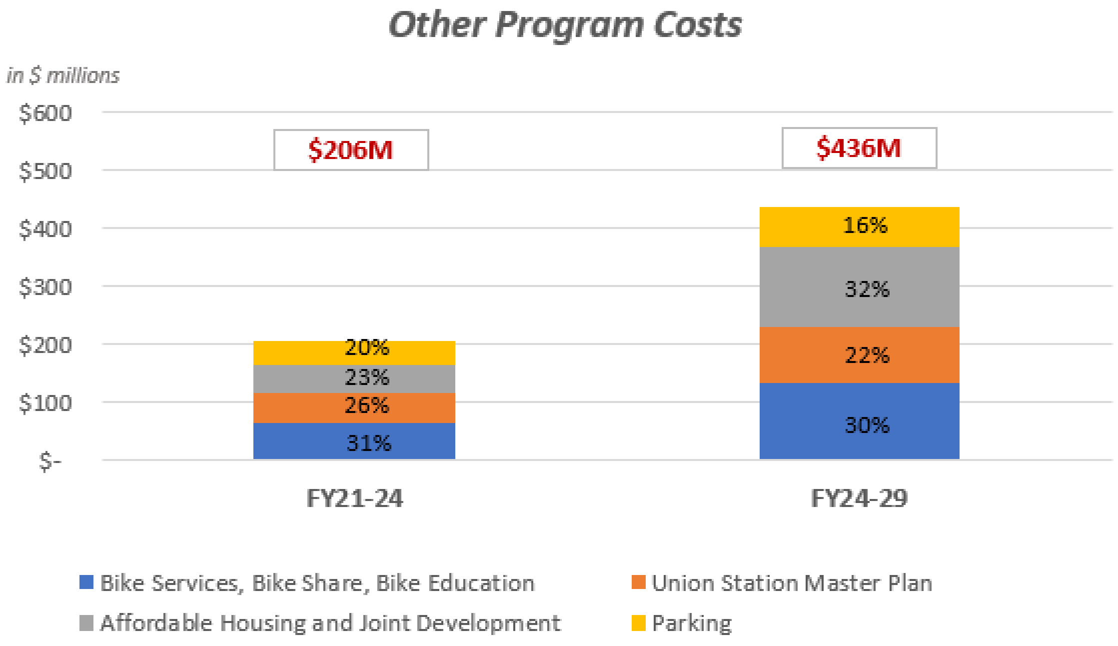
Actual to MR/MM ordinance projections

- Expenditure Plans – specify projects and funding caps
- MR actuals below ordinance projections by $1.9B since inception in FY10
- MM actuals are closer to ordinance projections the largest variance during the pandemic years, falling short by over $200 million from FY18 (inception) through FY22

- Metro continues to compete for capital investment grants, which are not always awarded and often include significant operational and local match funding requirements
- The ongoing financial risks that stem from TID programs may take away funding currently eligible for bus and rail operations, if no alternative funding source is identified. These include:
  - Higher bid prices and cost increases due to a tighter labor market and rising demand for goods
  - Project cost overruns due to scope and schedule changes, and additional close out risks
  - Limited options and funding for cost increases on underground projects
  - Additional debt issuances must be repaid with interest

Other Programs Indirectly Impacting Metro Transit Funding

- Metro utilizes resources for a wide range of activities that support the goal of delivering improved mobility, sustainability, and financial and technical support to Metro's partners throughout the Los Angeles County region
- Programs that do not have sufficient dedicated funding and indirectly compete with Metro Transit for funds include:
  - Metro's Bike and Active Transportation program
  - Operating and maintaining Union Station
  - Affordable housing and joint development efforts
  - Other projects without dedicated funding



- These programs are estimated to grow at a 4.6% average annual rate over the next five years, outpacing sales tax growth of 2.6%

Next Steps

- Metro will continue utilizing the EZBB process to develop the FY25 budget given the near-term outlook challenges
  - Strengthen cost controls and balance the budget by staying within our cost & equity parameters
  - Evaluation of pilot programs based on aligned strategic imperatives and priorities
  - Partner with the Board of Directors to identify mitigation strategies

Near-Term Outlook

Forecasting and Mitigation

Outreach

Early, comprehensive and thorough outreach plan

Equity Review

Equity process through EFC assessment and MBEAT

Financial and Cost Management

Cost control task forces and mitigation and financial accountability through quarterly reviews

Holistic Program Reviews

Program reviews to promote collaboration on prioritization and trade-offs

- The CEO will make prioritization and trade off recommendations to the Board going into the FY25 budget development process
- Regular budget briefings will also be provided to the Board while integrating feedback for the final FY25 Budget approval in May 2024