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BASELINE REPORT

FINANCIAL CAPACITY ASSESSMENT OF THE SAN FRANCISCO MUNICIPAL RAILWAY SAN FRANCISCO, CALIFORNIA

THIRD STREET LIGHT RAIL PROJECT

PREPARED FOR

U.S. DEPARTMENT OF TRANSPORTATION

FEDERAL TRANSIT ADMINISTRATION

UNDER

CONTRACT: **DTFT60-01-D-00001**

PROJECT: **MD-90-5003**

TASK ORDER: **2**

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Table of Acronyms

Term	Definition
ADA	Americans with Disabilities Act
CAC	Citizens' Advisory Council
Caltrans	California Department of Transportation
CIP	Capital Improvement Plan
CMA	Congestion Management Agency
CMAQ	Congestion Mitigation and Air Quality
CPI	Consumer Price Index
CS	Central Subway – Third Street LRT, Phase 2
CTC	California Transportation Commission
CTP	San Francisco Countywide Transportation Plan
D&A	Deva & Associates, P.C.
DOT	U.S. Department of Transportation
DPT	Department of Parking and Traffic
FCA	Financial Capacity Assessment
FFGA	Full Funding Grant Agreement
FTA	Federal Transit Administration
FY	Fiscal Year
IOS	Initial Operating Segment – Third Street LRT, Phase 1
LRT	Light Rail Transit
LRV	Light Rail Vehicle
MME	MUNI Metro East Light Rail Maintenance Facility
MTA	Municipal Transportation Agency
MTC	Metropolitan Transportation Commission
MUNI	San Francisco Municipal Railway
New Starts	FTA §5309 New Starts Funding
O&M	Operating and Maintenance
PMOC	Project Management Oversight Contractor
PTC	Public Transportation Commission
PTD	Public Transportation Department
PUC	Public Utilities Commission
ROD	Revenue Operations Date
RTP	Regional Transportation Plan
SFCTA	San Francisco County Transit Agency
SOGR	State of Good Repair
SRTP	Short Range Transit Plan
STA	State Transit Assistance
STIP	California State Transportation Improvement Program
STP	FTA Surface Transportation Program
TCRP	California Traffic Congestion Relief Plan
TEA-21	Transportation Equity Act for the 21st Century
Third Street LRT	Third Street Light Rail Project
YOE	Year of Expenditure

EXECUTIVE SUMMARY

EXECUTIVE SUMMARY

The **San Francisco Municipal Railway (MUNI)** is the largest transit system in the Bay Area and the seventh largest in the nation. MUNI is currently constructing Phase 1 of the Third Street Light Rail (Third Street LRT) project, the Initial Operating Segment (IOS); and designing Phase 2 of the Third Street LRT, the Central Subway (CS) project. IOS construction of 5.4 miles of surface-level, light rail service began in 2000 with operations scheduled for the winter of 2005/2006. The IOS phase also includes the future construction of a new MUNI Metro East (MME) Light Rail Maintenance Facility to house up to 100 light rail vehicles (LRVs). The CS phase, which is in preliminary engineering, will add 1.7 miles of light rail service extension to Clay Street in Chinatown. Construction of the CS phase is expected to begin in 2009, with a revenue operations date in 2012.

The combined cost of the Third Street LRT project is currently estimated at $1.6 billion ($620.1 million for the IOS phase and $994.4 million for the CS phase). To fund the CS phase, MUNI anticipates requesting $762.2 million in United States Department of Transportation (DOT), Federal Transit Administration's (FTA) §5309 New Starts (New Starts) funding, or 76.6 percent of total estimated costs. On a combined basis, this New Starts funding would be 47.2 percent of combined costs. Non-New Starts funding increases direct federal participation to $815.8 million (50.5 percent). Federal pass through funds of $158.6 million raise the total federal participation to 60.4 percent. Including the pass through federal funds, state funding is budgeted at $298.6 million (18.5 percent). Locally generated revenue will provide the remaining $500.1 million (31.0 percent) of total project costs.

FTA has contracted Deva & Associates, P.C. (D&A) to perform a Baseline Financial Capacity Assessment (FCA) of MUNI to assess MUNI's current financial capacity, the impact of the development and operation of both phases of the Third Street LRT on MUNI's financial capacity, and the ability of MUNI to manage and finance the project. Although MUNI is a department within the City of San Francisco, the Baseline FCA was limited to the financial operations of MUNI. This Baseline FCA includes a forward-looking analysis of MUNI's fiscal capability to construct the proposed CS project. MUNI has prepared a 20-year cash flow projection for operations and capital projects that indicates MUNI has the financial capacity to complete the Third Street LRT and operate the expanded system. D&A analyzed the available project information and identified the following risk factors that impact the financial capacity assessment.

- <u>Farebox Revenue</u> – MUNI's financial projection assumed a 3.4 percent average annual growth rate for farebox revenue based on periodic fare increases. Historical farebox revenue has averaged 4.0 percent for the past 19 years, but only 1.7 percent over the last 10 years, including the first fare increase in over 10 years during fiscal year (FY) 2004. MUNI has included an additional fare increase for FY2006 and future periods. Although the projected increases in farebox revenue were considered reasonable, past history indicates that some risk remains that projected increases may not be realized.

- Dedicated Tax Revenue – MUNI's 20-year cash flow projection assumes an expected annual sales tax revenue growth of 3.9 percent. The expected annual growth equals the actual annual compound growth rate experienced in the past 19 years; however, recent experience over the past five years has been (0.6) percent. The recent experience related to dedicated tax revenue collections indicates risk that MUNI might not be able to realize the projected increases in tax revenue.

- Budget Shortfalls/Cash Reserves – The budgeting/funding process for MUNI's operation, including costs of maintaining the current transit system, does not allow MUNI to accumulate any significant cash reserves. Funding sources are subject to fluctuation-related changes in economic conditions, and certain cost increases cannot be fully controlled by MUNI. Recently, these factors created significant budget shortfalls that have required a major effort to identify additional revenue sources and cost savings each year to balance the budget. MUNI needs a more comprehensive financial plan that provides for some minimal level of cash reserves and identifies contingency funding sources to better manage these funding crises. To date, MUNI has managed to complete this process without major cuts in service levels.

New Starts Compliance Issues - To receive New Starts funding for the CS phase, MUNI expects to request a Full Funding Grant Agreement (FFGA) from FTA during the Final Design phase of the project. This Baseline FCA identified challenges MUNI faces to fulfill its obligations under a FFGA for the CS phase, which includes the ability to continue to operate and maintain its existing transportation services, including other planned improvements.

- Project Budget – The complexity of construction of the CS phase is relatively high, since tunneling and subway stations are included in the project. Based on analysis of prior and existing projects, MUNI has experienced both scope changes and budget issues on less complex projects. In order to minimize the impact of cost increases resulting from scope adjustments, MUNI needs to review its method of estimating project budgets and its methods of controlling project costs to ensure that all major contingencies have been identified and evaluated. This evaluation should be on a continuous basis with analysis to mitigate the cost increases or identify the funding sources for the cost increases. Under a FFGA, FTA does not assume this risk and will not provide funding for cost increases. Any cost increase for the CS phase would require immediate local or state funding or adequate debt capacity to maintain the construction schedule. Adequate debt capacity is defined as fully authorized dedicated financing arrangements that can be activated quickly by MUNI without further outside approval. As a result, MUNI should constantly review and revise the project budget to evaluate the adequacy of project contingencies.

- Funding Sources – MUNI has identified sources of state and local funding for the CS phase. In addition, MUNI has included financing costs in the project budget for potential financing of certain costs of the CS phase. To date, MUNI has not provided any detail plans to support the financing cost computation. Therefore, D&A could not determine the reasonableness of the amount of financing costs. In resolving this issue, MUNI should work with FTA to assure that its financing cost computation is consistent with FTA requirements.

- Contingency/Mitigation Plan – As the CS project continues through preliminary engineering and into final design, MUNI needs to regularly review its project budget and estimates, identify areas of risk, and develop a contingency or mitigation plan in the event that the risks materialize into funding delays or cost increases. Since FTA does not assume risk beyond the amount of New Starts funding requested, MUNI needs to identify funding sources for all project contingencies.

- Maintaining Current Levels of Operations – As stated above, a condition of the FFGA is to maintain the current transit system and level of service. Although MUNI has been able to resolve budget shortfalls without significant cuts in the level of service, cuts in the level of service were considered as a method to mitigate the budget issues. Under FFGA guidelines, MUNI's financial capacity would not be considered adequate unless sufficient revenue sources were available to assure that current service levels are maintained. MUNI needs to develop plans to demonstrate the ability to mitigate these risks with additional state and local funding as required.

Conclusion – The D&A team reviewed the reasonableness of MUNI's financial projections and its underlying financing assumptions, developed models to test the sensitivity of those assumptions, and concluded certain risks exist, which need to be mitigated or minimized before the financial capacity of MUNI would be considered adequate to construct and operate the project. Overall, this testing indicated that MUNI does not have sufficient cash reserves or adequate financing sources available to ensure timely completion of the project if the anticipated federal funding is delayed to future periods or project cost increases are incurred. In addition, the identified risk factors indicate that the growth rates of MUNI funding sources are not certain and MUNI may not have adequate committed funding available to maintain current planned expanded service levels.

If all federal funding is provided in a timely manner as scheduled in MUNI's financial projections, including availability of funds at the beginning of the appropriated year, MUNI anticipates having adequate cash flow to construct the project as scheduled without any significant amounts of financing required. However, MUNI has included approximately $12 million of financing costs in the project budget to primarily fund the potential delays in federal funding. Although this project-financing contingency could be considered appropriate, MUNI has not provided adequate detail support for this requirement.

This FCA has been issued Final using the Draft Report submission date of June 3, 2005, since no information herein has been updated beyond that date.

SECTION 1

SCOPE OF FINANCIAL CAPACITY ASSESSMENT

SCOPE OF FINANCIAL CAPACITY ASSESSMENT

1.1 Background

Deva & Associates, P.C. (D&A) was contracted by the United States Department of Transportation (DOT), Federal Transit Administration (FTA) to perform a Financial Capacity Assessment (FCA) of the San Francisco Municipal Railway (MUNI), in San Francisco, California. The FCA was conducted in accordance with FTA Circular 7008.1A, "Financial Capacity Policy," dated January 30, 2002 and FTA's "Financial Management Oversight Contractors' Guide for Conducting Financial Capacity Assessments," revised July 2002.

The FCA was conducted to evaluate the financial capacity of MUNI's current operations and its capacity to construct and operate both phases of the Third Street Light Rail (Third Street LRT) project. MUNI anticipates requesting a Full Funding Grant Agreement (FFGA) for FTA §5309 New Starts (New Starts) funding to develop Phase 2 of the Third Street LRT project. Although MUNI does not need to be fully compliant with the FFGA requirements until the FFGA is executed, the FCA was conducted to determine the areas where financial capacity cannot be demonstrated and to allow MUNI to develop and implement a plan of corrective actions to mitigate any issues related to financial capacity.

A FFGA limits the exposure of FTA and the federal government to cost increases that may result if project design, engineering, and/or planning are not adequately performed at the local level. FTA is primarily a financial assistance agency and is not directly involved in the design and construction of New Starts projects. While FTA is responsible for ensuring that planning projections are based on realistic assumptions and that design and construction follow acceptable industry procedures, it is the responsibility of project sponsors to ensure that proper planning, design, and engineering have been performed.

The Secretary of DOT, in evaluating a New Starts project, must require that:

- The project funding plan provides contingency amounts that are reasonable to cover unanticipated cost increases;
- The local sources of capital and operating funds are stable, reliable, and available with the project timetable; and
- Local resources are available to operate the overall transit system, without requiring any reduction in existing services in order to operate the proposed project.

The statute further provides that, in assessing the stability, reliability, and availability of local funding, the Secretary of DOT shall consider (among other things) the degree to which financing sources are dedicated to the proposed project and the extent to which the project has a local funding overmatch.

SCOPE OF FINANCIAL CAPACITY ASSESSMENT

1.1 Background (continued)

A FCA is conducted to assess the grantee's financial capacity to meet its obligations under the grant agreements with FTA. A FCA reviews the grantee's financial condition and financial capability to ensure that projects can be completed on schedule and within budget, and that transit service is not interrupted due to a lack of financial capacity on the part of the grantee. The grantee must demonstrate its ability to match and manage FTA grant funds, cover cost increases and/or operating deficits through long-term stable and reliable sources of revenue, and maintain and operate federally-funded facilities and equipment.

1.2 Description of the San Francisco Municipal Railway

MUNI began service in 1912 as one of the first publicly owned transit systems in the United States. From 1932 until 1994, the City of San Francisco's Public Utilities Commission (PUC) governed MUNI. In 1993, Proposition M created the Public Transportation Commission (PTC) and the Public Transportation Department (PTD), removing MUNI from the authority of the PUC. Governance of MUNI was changed again in 1999 with the passage of Proposition E, which created a quasi-independent agency called the Municipal Transportation Agency (MTA). MTA assumed the powers of the PTC on March 1, 2000. MUNI officially became a department of MTA on July 1, 2000. On July 1, 2002, MTA took over the functions of the Department of Parking and Traffic (DPT). MTA is responsible for establishing the basic policies that govern MUNI's operation. A seven member Board of Directors, appointed by the Mayor of San Francisco and confirmed by the City's Board of Supervisors, governs MTA. According to the terms of Proposition E, MTA Directors must have relevant transportation experience and at least four must be regular MUNI riders. MTA Directors are appointed for fixed, staggered terms and serve until reappointed or removed for cause. Proposition E also established a Citizens' Advisory Council (CAC), which serves as an advisory body to MTA. The CAC is composed of fifteen members appointed by the Mayor and the Board of Supervisors. The CAC is divided into four committees: Engineering, Maintenance and Safety; Finance and Administration; Operations and Customer Service; and Planning and Marketing.

Every two years, MUNI produces a Short Range Transit Plan (SRTP) as the transit system's primary planning document. The SRTP describes MUNI's organization, current and planned services, Capital Improvement Program (CIP), and operating financial plan. MUNI staff, the San Francisco County Transit Agency (SFCTA), the Metropolitan Transportation Commission (MTC), FTA, and other agencies use the SRTP to review MUNI's future plans, goals and objectives. The SRTP provides justification, support, and prioritization for MUNI's planned capital projects contained within the San Francisco Countywide Transportation Plan (CTP) prepared by SFCTA and the Regional Transportation Plan (RTP) prepared by MTC.

1.2 Description of the San Francisco Municipal Railway (continued)

In July 2002, MUNI reorganized to better structure the organization for compliance with Proposition E. As a result of the reorganization, MUNI, under MTA, is composed of four divisions: General Manager, Transportation, Maintenance, and Construction. The General Manager reports to the MTA Board and is responsible for directing the operations of MUNI. Overall, MTA/MUNI has more than 4,200 employees. About 4,000 employees are represented by one of 17 labor unions. Work rules and compensation for these employees are governed by collective bargaining agreements between MUNI and the City.

MUNI operates 80 lines, providing bus, trolley coach, light-rail, streetcar, and cable car service. The majority of the bus service and all the light rail/streetcar lines connect to downtown San Francisco. Service hours on most bus and light-rail lines are 5:00 am to 1:00 am. In addition, 12 bus lines run 24 hours a day. MUNI also links passengers to regional transit systems including Caltrain (commuter rail to San Mateo and Santa Clara counties), BART (heavy rail to Alameda, Contra Costa and San Mateo counties), SamTrans (bus service to San Mateo county), Golden Gate Transit (bus service to Marin and Sonoma counties), and Bay Area Ferries (serving Marin, Sonoma, and Alameda counties). MUNI carries over 680,000 daily riders, totaling more than 216 million annual passenger trips, making MUNI the most heavily used transit system in the Bay Area and the seventh largest in the nation.

San Francisco is a charter city, exercising the powers and duties of both a city and county. San Francisco is the fourth largest city in the State of California and the 12th largest in the nation. San Francisco's population increased from nearly 724,000 based on the 1990 census to over 776,000 based on the 2000 census. With an estimated 2004 population of over 792,000, San Francisco has experienced a relatively stable population with less than a one percent average annual increase in population.

San Francisco County's unemployment rate was 4.5 percent in December 2004, the lowest rate since 4.1 percent in May 2001. The San Francisco region lost more than 300,000 jobs from 2001 to 2003, including roughly one-third of all jobs in the technology sector. Based on the annual outlook prepared by the Association of Bay Area Governments, an association of nine counties in the Bay Area region, limited job growth was forecasted for 2004 and 2005, household income was likely to grow at approximately 1.0 percent annually over the next two years, and taxable sales were projected to grow 3.5 percent and 4.3 percent in 2004 and 2005, respectively. Actual sales tax revenue declined 8.2 percent in fiscal year (FY) 2004 with some recovery expected in FY2005. Overall, inflation is not expected to grow rapidly and the Bay Area recovery will lag that of the remainder of the nation.

1.2 Description of the San Francisco Municipal Railway (continued)

Proposition E created a Municipal Transportation Fund for the operation of MTA, MUNI, and DPT. This fund establishes a stable funding base for MTA, based on recent City of San Francisco contributions to the operations of MUNI. Proposition E also initiated a separate budget process for MTA in which the Mayor of San Francisco and the Board of Supervisors have a reduced role. In the new process, the Mayor does not have authority to change the MTA budget sent to the Board of Supervisors, if MUNI does not seek more General Fund support than determined by the Proposition E formula.

The Third Street LRT is comprised of two phases – Phase 1, the Initial Operating Segment (IOS) and Phase 2, the Central Subway (CS) will add more than seven miles of surface and subway-level light rail service to the eastern side of San Francisco. The Third Street LRT project will replace much of the 15–Third Street motor coach line.

The IOS phase is 5.4 miles of new light rail constructed in an exclusive median beginning at a current terminal at Fourth and King Streets and running south to the county line near the Bayshore Caltrain Station. Construction of the IOS phase began in 2000 and will include 19 stations. The revenue operations date (ROD) for Phase 1 is scheduled to begin in the winter of 2005/2006. The IOS phase also includes the construction of the new MUNI Metro East (MME) Light Rail Maintenance Facility, which will store, maintain, and dispatch light rail vehicles (LRVs). The construction of the new maintenance facility has been delayed due to bidding issues. The estimated completion date has not been established.

The CS phase adds 1.7 miles of light rail beginning at the Fourth and King Streets terminal to Chinatown. Several proposed alignments are under consideration. Current proposals incorporate a combined portal for the subway on Fourth Street with three or four subway stations. To minimize public impact during construction of the project, MUNI is considering using deep tunneling techniques for the construction of the subway. Phase 2 is currently in preliminary engineering with a projected ROD in 2012.

1.3 Limitations on Reliability of the Data and Use of this Report

This FCA does not constitute an audit of any financial statements prepared by MUNI. Instead, it is an analysis of MUNI's 20-year financial projection focused on substantive, material issues affecting financial condition and capacity. Since most data provided by MUNI was assumed to be accurate, any inherent limitations, errors, or irregularities that occurred may not be detected. In addition, projection of any evaluation beyond the period of analysis is not appropriate.

SECTION 2

PROJECT OVERVIEW:
THIRD STREET LIGHT RAIL PROJECT

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2.1 Project Description

The Third Street LRT project is currently one of the City of San Francisco's largest infrastructure projects. The project consists of a Phase 1 (IOS) and Phase 2 (CS). Overall, the Third Street LRT project is a seven-mile, dual track light rail transit (LRT) system reestablishing rail service along Third Street between downtown San Francisco and the county line near the Bayshore Caltrain Station. The project also includes the construction of a new LRV maintenance facility on approximately 13 acres at 25th and Illinois Streets to store, maintain and dispatch LRVs.

Construction for the IOS phase of the Third Street LRT project began in 2000. This phase will extend 5.4 miles from a current terminal at Fourth and King Streets, running south along Third Street and Bayshore Boulevard, and ending at the county line at the Bayshore Caltrain Station. This phase will be constructed primarily at-grade in an exclusive median in the street to improve safety and reliability. The IOS includes 19 stations and 15 new LRVs. MUNI originally forecasted the ROD to be in the Fall of 2005. Subsequently, the ROD was tentatively set for December 2005. In May 2005, FTA's project management oversight contractor (PMOC) issued Spot Report 2, Third Street Project Cost and Schedule Assessment. In the spot report, the PMOC concluded that "MUNI will not achieve the December 17, 2005 ROD it has tentatively set, unless MUNI is able to quickly galvanize critical path contractors to rapidly accelerate their work effort… A ROD of April 2006 is more likely at this time… If MUNI fails to address contractor performance, the ROD could easily slip further into the second half of 2006." As additional development along this LRV corridor builds up, MUNI anticipates purchasing an additional 10 LRVs for this line. The MME facility is also included in the IOS phase. MUNI originally anticipated starting construction on the maintenance facility in Fall 2001. Difficulties in the bidding process delayed the start of construction. A second attempt to award a contract, with a projected completion date of May 2007 was ineffective. The project construction is concurrently being rebid. If a contract is awarded, MUNI anticipates a completion date of July 2008. In its spot report, the PMOC expressed concern "that any further slippage in commencing construction and opening the MME facility will hamper MUNI's ability to provide even the level and quality of service it delivers today."

Phase 2 of the Third Street LRT project is currently in preliminary engineering. Several design concepts have been developed. The CS will extend 1.7 miles from the current terminal at Fourth and King Streets to Chinatown. Construction of the CS will begin at-grade at Fourth and King Streets. The CS enters a subway at a combined portal on Fourth Street. The subway portion will be constructed using deep tunneling methods passing under the BART/MUNI Market Street Subway and will incorporate three or four subway stations.

2.1 Project Description (continued)

MUNI has determined that the east side of the City of San Francisco to be served by the Third Street LRT project is undergoing a community revitalization effort supported by numerous City departments, community groups, and other organizations. The objectives of the Third Street LRT are to enhance transit service by improving travel time, reliability, passenger comfort, and travel connections; to support economic development and revitalization in the communities along the corridor; to reduce traffic congestion; and to reduce diesel emissions with the replacement of the 15-Third Street motor coach line.

When the project is complete in 2012, a 14 minute reduction in travel time is expected between Visitacion Valley and Chinatown. Average daily ridership for the IOS is projected to reach 71,000 riders by FY2015. The CS is projected to open in 2012 and carry over 60,000 daily riders by FY2025.

Nearly 46.0 percent of the cost for the Phase 1 (IOS) project will be funded by local Proposition B/K sales tax collected in the County of San Francisco. Other funding sources for the IOS phase include FTA §5309 Rail Modernization, FTA Surface Transportation Program (STP), California Traffic Congestion Relief Plan (TCRP), and California State Transportation Improvement Program (STIP) funds, which are actually federal pass-through funds. MUNI anticipates applying for a FFGA to receive New Starts funds to assist in the funding of the CS phase of the Third Street LRT project. More than 76.6 percent of the project costs for Phase 2 (CS) project will be funded with New Starts funds. Additional funding sources for the CS phase include TCRP, RTP, and Proposition K local sales taxes. MUNI's project plan reflects language included in the FY2004 Federal Omnibus Appropriations Bill (Public Law #108-199) that ensures the investment in Phase 1 serves as part of the non-New Starts contribution for Phase 2 of the Third Street LRT project. The New Starts funding represents 47.2 percent of the total costs of the entire Third Street LRT project.

2.2 Project Budget

The Third Street LRT project is currently projected to cost $1.6 billion (including prior expenditures) in year of expenditure (YOE) dollars. The funding plan is summarized below:

Third Street LRT Project Funding Plan (in millions, YOE dollars)				
Source	Phase 1 (IOS)	Phase 2 (CS)	Total	Percentage
New Starts	$ --	$ 762.2	$ 762.2	47.2%
Federal – Other	53.6	--	53.6	3.3
State	192.4	106.2	298.6	18.5
Local	374.1	126.0	500.1	31.0
Total	**$ 620.1**	**$ 994.4**	**$ 1,614.5**	**100.0%**

2.2 Project Budget (continued)

MUNI's financial plan proposes to utilize $762.2 million of federal New Starts funds and $53.6 million of other federal funds for a total of $815.8 million, or 50.5 percent federal funding. The $298.6 million of state funding consists of STIP and TCRP funds and the $500.1 million of local share consists of sales tax and RTP funds. The STIP funds are actually pass-through federal funds of approximately $158.6 million, which brings total federal funds to 60.4 percent of total cost. This funding proposal reflects assumptions made by the grantee, and are not FTA assumptions.

The total project cost estimate of $1.6 billion has not been reviewed by the PMOC since Phase 2 is in preliminary engineering. In May 2005, the PMOC issued Spot Report #2, Third Street Project Cost and Schedule Assessment, reviewing the cost and project history of Phase 1 of the Third Street LRT project. In the report, the PMOC "predicts that the costs will increase another $15 million and perhaps more due to escalation in MME facility costs, additional contingency for potential changes to the MME facility during construction, increase in the cost estimate for system start-up, and extended overhead costs."

2.3 Project Cash Flows

D&A analyzed the cash flow summary for the Third Street LRT project to ensure that funds would be available when needed to pay for project expenditures. Proposed project funding includes New Starts funding, as well as other state and local funding.

MUNI's 20-year financial projection assumes grants will be received for the full federal share of the New Starts project. Actual New Starts funding will depend on FTA funding recommendations and federal appropriations, which are required before any funds will be available to MUNI.

The baseline project cost estimate totals $1.6 billion for both phases of the Third Street LRT project. For further information on the cost of the contract units comprising the total project cost, refer to the most current FTA Project Management Oversight Program's project monthly report.

Potential uncertainties exist in annual federal appropriations for all New Starts projects. Delays in appropriations of federal funds do not constitute a basis for extension of the ROD. As a result, an assessment of MUNI's ability to fund the New Starts project until federal funds committed under the FFGA become available is necessary. MUNI is aware of the potential time lag risk between the need for the federal funds and actual receipt.

2.3.1 Potential Delays in Proposed Project Funding

MUNI has indicated that, as a department of the City, it would be able to utilize financing authority of the City to obtain grant anticipation notes to finance costs due to delays in federal funding or other longer term borrowing, if required. However, these plans have not been formalized, and risk remains that the required financing might not be available when required.

2.3.2 Potential Project Cost Increases

Because of the more permanent nature of substantial cost increases versus funding delays, project costs that substantially exceed budgeted amounts, including available project contingencies, would require additional funding. Major capital projects face the possibility of additional funding requirements not currently anticipated as part of the project and uncertainties affecting project scope and/or cost.

MUNI is committed to completing the Third Street LRT project within the baseline cost estimate. Although MUNI has indicated that long-term debt capacity could be available, MUNI has not specifically developed principal strategies for addressing cost increases or finalizing details of any debt capacity or related use thereof. Consequently, MUNI needs to develop formal financing plans to utilize available debt capacity to provide funding for potential cost increases or funding shortfalls.

Based on recent history of subway projects, the potential risk of significant cost increases would be considered high. Compounding this risk factor is the fact that MUNI has not finalized the CS alignment or updated the cost budget for the planned project revisions.

2.4 Project Status/Revenue Operations Date

The IOS phase of the Third Street LRT project, started construction in 2000 and MUNI expects to start revenue operations in December 2005. MUNI estimates that the IOS phase of the project is currently 85 percent complete. However, the construction of the new light rail maintenance facility included in the IOS phase has been delayed and the schedule for this part of the project is uncertain. The CS phase of the Third Street LRT, is in preliminary engineering, which should be completed in 2006. Final design of the CS portion is expected to begin in 2007 and be completed in 2008. Acquisition of land and right-of-way for the project is budgeted for 2007. Actual construction of the CS project is scheduled to start in 2009 with revenue operations starting in 2012. MUNI continues to incur budget creep for the Third Street LRT with projected cost increases over the last two years of 7.6 percent for the IOS phase. Recently, MUNI also increased the budget for the CS phase of the project by 30.2 percent. MUNI indicated that the cost elements for the CS phase had not been updated since 1999 and the revised estimate includes elements that had been omitted from the earlier estimate. To cover the

2.4 Project Status/Revenue Operations Date (continued)

cost increases, MUNI has estimated an increase in state and local funding of 5.4 percent and federal funding, primarily New Starts, of 40.0 percent. Planned New Starts funding increased from $531.7 million to $762.2 million in the latest budget. This represents 47.2 percent of the current estimated total cost of the Third Street LRT of $1.6 billion. Other federal funding of $53.6 million brings the total federal share to 50.5 percent. However, after adjustment for the $158.6 million of pass-through federal funds included in the committed state funding, the total federal share is actually $974.4 million, or 60.4 percent. The latest PMOC spot report indicated that there was potential for additional budget increases and that identified funding sources may not be adequate or available.

2.5 Project Plan

Every two years, MUNI produces a SRTP as the transit system's primary planning document. The SRTP describes MUNI's organization, current and planned services, CIP, and operating financial plan. The SRTP, however, does not analyze MUNI's cash flows during the projected period. In September 2004, MUNI prepared a 20-year cash flow projection, which combined the operating and state of good repair (SOGR) projections from the FY2004-2023 SRTP and the Third Street LRT project. This projection was subsequently revised in April 2005.

MUNI should implement the following improvements to future project plans to improve compliance with FTA guidelines and New Starts requirements:

- The project plan should include a written plan and a summary cash flow projection. The written plan should include a narrative describing the project, summarizing the project budget, and discussing the assumptions made in the cash flow projection. The summary cash flow projection should include historical data for the past five years and at least 20 years of projected operations and capital program sources and uses. The summary cash flow projection should also include all projected financing proceeds, debt service payments, and ending cash reserves/balances. The project plan should be updated regularly for changes in budgets, close of a fiscal year, changes in assumptions, etc. Revised project plans should be distributed to FTA and the Financial Management Oversight Contractor.

- The summary cash flow projection should be supported by detailed supporting information. Farebox revenue should be computed using passenger or ridership projections and fare rates. Detailed farebox revenue should be projected by service type and segregated by existing and new service. Detailed support for other revenues should be projected by source. Any new revenues projected that require third party or voter approval should be presented separately from existing revenues sources. In addition, any revenues generated from new service (i.e.: IOS or CS phase) should also be presented separately from existing revenue sources.

SECTION 3

MUNI’S FINANCIAL CONDITION AND CAPABILITY

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D&A evaluated the financial condition and capability of MUNI, not only for its ability to complete the proposed New Starts project and other planned projects, but also for its capability to operate and maintain the existing bus, trolley coach, cable car, and light-rail lines and streetcar service. The following discussion presents an analysis of the current financial plan for operating and maintaining the MUNI system, and replacing and expanding capital assets.

The financial condition of MUNI's current cost of transit service is shown in the Baseline Financial Plan in the Appendix (pages A-1 through A-3). The financial plan shows MUNI's operating and capital finances on a fiscal year basis, as well as cumulative "bottom line" amount, between FY2005 and FY2024, the period of analysis.

3.1 Revenue Analysis

This section discusses projections of operating and capital sources of funds. MUNI has four principal sources of operating revenue: farebox revenue, state and local sales tax revenue, parking revenue, and City and County of San Francisco General Fund revenue. Operating revenue for the Third Street LRT project does not assume any new funding sources.

3.1.1 Farebox Revenue

Farebox revenue is the largest component of system-generated revenues, and the second largest source of operating revenue at approximately 24.4 percent of FY2004 operating costs. Farebox revenue is projected to increase at an average rate of 3.4 percent annually over the 20-year projection as a result of fare increases and increased ridership. In FY2006, FY2010, and every three years thereafter, MUNI's 20-year projection incorporates a fare increase based on the projected inflation rate during the period. Ridership increases are also projected in connection with the Third Street LRT project beginning in FY2006.

The table in Appendix C-1 presents MUNI's actual passenger revenue from FY1985 to FY2004. Over 19 years, the average annual increase in passenger revenue was 4.0 percent. This increase included the first fare increase (September 2003) in over 10 years. The following table shows MUNI's projected passenger revenue from FY2005 to FY2024. MUNI assumes that ridership for the IOS phase of the Third Street LRT project will ramp up rapidly in the first two years and the CS phase will ramp up in the first year of operations.

3.1.1 Farebox Revenue (continued)

Fares were increased in FY2004, resulting in a 14.4 percent increase in farebox revenue. This was the first fare increase in over 10 years. Excluding FY2004, the projected annual increase in average passenger revenue included in the projection significantly exceeds the historical experience of the last 10 years, but is based on more frequent fare increases. This growth pattern was considered aggressive and risk exists that this growth might not be achieved.

Projected Farebox Revenue (dollars in millions) - FY2005 to FY2024

Fiscal Year	Total	Percentage Change
2005	$121.9	5.5%
2006	135.1	10.8
2007	135.3	0.1
2008	135.4	0.1
2009	135.6	0.1
2010	155.0	14.3
2011	155.2	0.1
2012	155.4	0.1
2013	170.4	9.7
2014	170.6	0.1
2015	170.8	0.1
2016	187.3	9.7
2017	187.5	0.1
2018	187.7	0.1
2019	205.9	9.7
2020	206.1	0.1
2021	206.3	0.1
2022	226.3	9.7
2023	226.5	0.1
2024	226.7	0.1
	$ 3,501.0	
Average Annual Percentage Change		**3.4%**

Source: MUNI's 20-year Cash Flow Projection, revised April 2005

3.1.2 State and Local Sales Tax Revenue

MUNI receives state and local sales tax revenue to fund its general operations from the following three sources:

- One-quarter of one percent of San Francisco's 8.5 percent sales tax;
- One-half of one percent of sales tax in San Francisco, Alameda, and Contra Costa Counties; and
- State Transit Assistance (STA) derived from the state sales tax on gasoline and diesel fuel.

The sales tax revenue in the 20-year cash flow projection reflects budgeted amounts for FY2005 and FY2006. The revenue projected for FY2007 to FY2013 represents amounts calculated by the MTC. MTC projected a significant increase in sales tax revenues in FY2009 following the end of an annual "off-the-top contribution" from the STA Public Transportation Account to the TCRP. Beginning in FY2014, sales tax revenue grows by the projected inflation rate. The following table details MUNI's projected sales tax revenue for FY2005 to FY2024. A table detailing the historical analysis of sales and use tax revenue from FY1985 to FY2004 is included as Appendix D-1. This table does not identify any changes in the tax basis or details as to specific tax source. MUNI projects sales and use tax revenue to grow at an average compound annual growth rate of 4.5 percent. Historically, the year-to-year percentage change varies widely based on economic conditions.

For the 19 years from FY1985 to FY2004, the average annual growth rate was 3.3 percent. In FY2002, the largest annual growth rate of 33.4 percent was realized. In FY1993, the sales and use tax experienced the largest decrease of (20.2) percent. During the past 10 years, the average annual growth rate was 4.5 percent. During the past five years, the state and local sales tax revenue decreased at an annual average rate of (0.6) percent. Although the average projected growth rate is consistent with the average growth rate realized during the past ten years, the annual growth rate assumptions used for projecting future sales and use tax revenue were considered an aggressive growth pattern with some remaining risk that the projected growth might not be achieved.

3.1.2 State and Local Sales Tax Revenue (continued)

Projected State and Local Sales Tax Revenue
(dollars in millions) - FY2005 to FY2024

Fiscal Year	Total	Percentage Change
2005	$ 65.7	(1.6%)
2006	71.9	6.2
2007	81.1	9.2
2008	84.9	3.8
2009	95.4	10.5
2010	99.8	4.4
2011	104.4	4.6
2012	109.0	4.6
2013	113.9	4.9
2014	117.5	3.6
2015	121.3	3.8
2016	125.1	3.8
2017	129.1	4.0
2018	133.3	4.2
2019	137.5	4.2
2020	141.9	4.4
2021	146.5	4.6
2022	151.2	4.7
2023	156.0	4.8
2024	161.0	4.5
	$2,346.5	
Average Annual Percentage Change		**4.5%**

Source: MUNI's 20-year Cash Flow Projection, revised April 2005

3.1.3 Parking Revenue

Parking revenue is the largest source of operating revenue at approximately 27.8 percent of FY2004 operating costs. MUNI receives revenue from parking meters, fines, tax, and garages. The revenue for the current City of San Francisco's 25.0 percent parking tax is split three ways. MUNI and the City of San Francisco's General Fund each receive 40.0 percent of the revenue. The remaining 20.0 percent is allocated to a senior citizens fund.

3.1.3 Parking Revenue (continued)

The parking revenue in the 20-year cash flow projection incorporates a growth rate equal to inflation each year. In addition, the projection includes a one percent increase every three years (beginning in FY2006) to account for other changes in parking policy, including new meters and increased rates. The projection also includes incremental revenues for the proposed increase in the City's parking tax from the current rate of 25 percent to 35 percent. The proposed increase, which requires two-thirds voter approval, would be implemented in FY2006. The incremental revenue from this tax increase is incorporated in MUNI's 20-year cash flow. The following table details MUNI's projected parking revenue for FY2005 to FY2024. A table detailing the historical analysis of parking revenue from FY1995 to FY2004 is included as Appendix E-1. Overall, MUNI projects parking revenue to grow at an average compound annual growth rate of 4.0 percent. Historically, the year-to-year percentage change varied widely based on economic conditions.

Projected Parking Revenue
(dollars in millions) - FY2005 to FY2024

Fiscal Year	Total	Percentage Change
2005	$ 132.4	0.8%
2006	143.3	8.2
2007	153.2	6.9
2008	158.6	3.5
2009	164.1	3.5
2010	171.4	4.4
2011	177.4	3.5
2012	183.6	3.5
2013	191.8	4.5
2014	198.5	3.5
2015	205.5	3.5
2016	214.6	4.4
2017	222.1	3.5
2018	229.9	3.5
2019	240.2	4.5
2020	248.6	3.5
2021	257.3	3.5
2022	268.7	4.4
2023	278.1	3.5
	$3,839.3	
Average Annual Percentage Change		**4.0%**

Source: MUNI's 20-year Cash Flow Projection, revised April 2005

3.1.3 Parking Revenue (continued)

For the nine years from FY1995 to FY2004, the average annual growth rate was 7.0 percent. In FY2004, the largest annual growth rate of 16.6 percent was realized. In FY2003, the revenue experienced a decrease of (1.5) percent. Although the average projected growth rate does not exceed historical rates, the projected parking revenue includes new revenues requiring voter approval and an aggressive growth pattern with some remaining risk that the projected growth might not be achieved.

3.1.4 Local Funding

Proposition E established a base amount of revenue that MUNI receives from the City of San Francisco's General Fund. A formula was created which dictates that the base amount of General Fund support increases and decreases at the same annual percentage rate as overall city discretionary revenues. In addition to a more predictable funding base than previous years, Proposition E required MUNI to streamline its budget process and provided MUNI more control over its budget and fare policy. As long as MUNI does not request more than the formula amount from the City's General Fund in its budget, the Mayor must submit the budget as received to the Board of Supervisors and the Board of Supervisors must accept or reject the budget in its entirety. If MUNI requests support in excess of the formula amount in its budget, the Mayor and Board of Supervisors would conduct a more traditional review process.

MUNI's 20-year cash flow projection assumes the City's discretionary funds will increase with inflation, except for increases of $9.0 million (9.2 percent) in FY2006 and $6.5 million (6.1 percent) in FY2007. These increases are based on funding increases projected by the City of San Francisco, which require voter approval. Overall, MUNI does not seek General Fund contributions in excess of the formula amount in the 20-year projection.

The SFCTA was created in 1989 to administer a one-half percent transportation sales tax program (Proposition B). Proposition B was reauthorized and succeeded by Proposition K in 2003. Since 1990, SFCTA serves as the designated Congestion Management Agency (CMA) for the City and County of San Francisco and the San Francisco Program Manger for grants from the Transportation Fund for Clean Air. In the CMA role, SFCTA is responsible for developing and administering the Congestion Management Program. Through these activities, SFCTA has been able to leverage state and federal transportation dollars to supplement Proposition K monies. In the role, SFCTA approves funding for transportation projects that directly benefit air quality through reduced motor vehicle emissions.

SFCTA has committed $128 million in local Proposition K funds to the CS phase of the Third Street LRT project. These funds were originally intended for use on the IOS phase, however they were exchanged with TCRP funds. The Proposition K funds are from currently authorized

3.1.4 Local Funding (continued)

sales tax and do not require any additional voter approval. However, since SFCTA controls these funds, MUNI can only request additional funding when needed and cannot be assured of support from SFCTA for cost increases or other funding delays.

In addition to sales tax and parking revenues, other sources of local revenue include miscellaneous operating activities, San Francisco's Transit Impact Development Fund, joint real estate lease projects, and bridge tolls.

3.1.5 State Funding

MUNI also receives limited operating assistance from the State of California for various programs including paratransit service.

The California Department of Transportation (Caltrans) is responsible for the administration of a number of state and federal funding programs. One of the primary documents related to the administration of these funds is STIP. MUNI's share of STIP funds is approximately 60.0 percent of the county share. Amounts incorporated in MUNI's 20-year cash flow projection are based on revised MTC RTP projections. SFCTA also administers the STIP funds, which are federal pass-through funds. SFCTA has committed $80 million in STIP funds to the Third Street LRT project.

The California Transportation Commission (CTC) was established in 1978 to assume the responsibilities of four independent bodies: The California Highway Commission, the State Transportation Board, the State Aeronautics Board, and the California Toll Bridge Authority. CTC is responsible for programming and allocating funds for the construction of highway, passenger rail and transit improvements throughout the State of California. CTC approved the Thirds Street LRT project application for TCRP funds. The approval committed $140 million to the project, $126 million to the IOS phase and $14 million to the CS phase.

3.1.6 Federal Funding

Operating assistance is made available through FTA's §5307 Urbanized Area Formula Grants Program. For urbanized areas with populations greater than 50,000, these funds are available for preventative maintenance. The Transportation Equity Act for the 21st Century (TEA-21) eliminated operating assistance to larger urban areas, but preventive maintenance expenses in the operating budget may be considered as "capital" for this purpose. Grantees may elect to use capital resources to fund maintenance. Funds are allocated by statutory formula to all qualifying urbanized areas in the country, with the amount based on federal authorization and appropriation. These formula grants are based on various demographic, level-of-service, and ridership variables.

3.1.6 Federal Funding (continued)

The §5307 funds are distributed by formula each year to larger and smaller urban areas and require a 20.0 percent local matching share. MUNI's 20-year cash flow projection incorporates $15.9 million and $4.6 million in FY2005 and FY2006, respectively.

Under the current federal legislative authorization, these allocations have been subject to a funding guarantee that provides a high degree of assurance future grants will be forthcoming in the amounts anticipated. This legislation is undergoing reauthorization and it is expected that the funding guarantee mechanism will be retained. MUNI's projection anticipates that no operating revenue source will be available after FY2006.

MUNI receives funds from several FTA capital grant programs. The assumptions used in MUNI's 20-year cash flow projection for these programs include:

- §5307 Urbanized Area Formula Grants Program funds were included using MTC projections established in March 2003. MUNI's share of funds is estimated at 50.5 percent of the San Francisco/Oakland urbanized area. FY2004 and FY2005 are based on actual programming. A four percent annual growth rate was determined by MTC for the remaining years.

- §5309 Fixed Guideway Modernization program funds were included using MTC projections established in March 2003. MUNI's share of funds is estimated at 41.7 percent of the San Francisco/Oakland urbanized area. FY2004 and FY2005 are based on actual programming. A four percent annual growth rate was determined by MTC for the remaining years.

- §5309 Bus Acquisition funds were included based on the 1999 TIP and prior year averages. MUNI's share of funds is estimated on replacement needs and fuel path changes.

- STP funds were included using MTC projections. MUNI's share of funds is estimated at 12.1 percent of regional total based on average of FY1991 to FY1998. No funding was included for FY2004 or FY2005 due to shortfalls from FY2003. Funding is held constant for all other years in the 20-year projection.

- TEA-21 appropriations were included based on MTC projections of $1.0 million annually with no escalations and $0.5 million annually for the county program with a 2.0 percent escalation. SFCTA recommended that MUNI assume a 50.0 percent share of the TLC/HIP funds, which was extrapolated for the county program.

- Congestion Mitigation and Air Quality (CMAQ) funds were included based on MTC projections. MUNI's share of funds is estimated at 13.3 percent of region totals for FY1991 to FY1998. No programming for FY2004 or FY2005 due to shortfalls from FY2003. Funds escalate at 2.0 percent for all other years in the 20-year projection.

3.2 Cost Analysis

The cost analysis examines three cost elements: operating and maintenance (O&M) costs; maintaining capital equipment, facilities, and vehicles; and MUNI's expansion plans. MUNI has developed a 20-year cash flow plan that describes their ability to operate the existing transportation system and the Third Street LRT project. MUNI indicated that the LRT project will increase efficiency and enhance MUNI's service network in concert with a community revitalization effort supported by numerous city departments, community groups, and other organizations.

3.2.1 Operating and Maintenance Costs

O&M costs are driven by two components, changes in service and inflation. Through FY2004, MUNI has operated a transit system utilizing bus, LRV, trolley, cable car, and historic streetcars. The only significant service change in MUNI's 20-year projection is the Third Street LRT project. The operating plan for funding incremental costs associated with the Third Street LRT project is quite different from the typical New Starts project. The Third Street LRT project replaces and upgrades existing bus service. MUNI estimated ridership and revenue growth to ramp up quickly over the first two years of operation of the IOS phase and the first year of operation for the CS phase. Full operating costs are projected at the outset.

In FY2003, MUNI operated a revenue fleet of 495 motor coaches, 333 trolley cars, 151 LRVs, 40 cable cars, and 27 historic streetcars. During FY2003, MUNI's fleet delivered 13.8 million, 7.5 million, 5.7 million, and 0.5 million revenue miles from its motor coaches, trolley cars, LRVs and historic streetcars, and cable cars, respectively. MUNI projects a nominal reduction in motor coach service when the OIS phase of the Third Street LRT project begins operations. MUNI anticipates that the motor coaches from the 15-Third Street line will be reassigned to other lines experiencing heavy ridership.

From FY1985 to FY2004, O&M costs have grown at an average annual rate of about 4.4 percent (from $208.9 million to $472.9 million). During the last five years, O&M costs have grown at an average rate of 6.9 percent. During that time, MUNI incurred significant increases in salaries and fringe benefits, paratransit service, and other operating costs. At the same time, efforts included reorganization of MUNI's operations to Proposition E milestones for service standards and performance measures, as well as service revisions to improve operating efficiency and system utilization.

MUNI's capital program includes ongoing modernization programs intended to yield reductions in out-year maintenance requirements and improvements in service productivity. MUNI service is based on a fleet of over 1,000 vehicles. Replacing the fleet on a regular basis is the most cost-

3.2.1 Operating and Maintenance Costs (continued)

effective way to yield higher productivity and quality service to MUNI customers and to minimize operating requirements. The next element of quality service identified by MUNI is the network of guideways and wayside infrastructure, including stops and platforms. The fleet and infrastructure programs are supported by a system of operations, maintenance, and administrative facilities.

MUNI plans to continue managing O&M costs to keep them in reasonable balance with patronage and operating revenue. MUNI's 20-year cash flow projection reflects budget costs for FY2005 and FY2006. Salaries increase by the projected Consumer Price Index (CPI) rate for FY2007 to FY2024. Fringe benefits for FY2006 and FY2007 are calculated on the known increases per the recent Memorandums of Understanding to the Employer Retirement Contribution and the employer pickup of the Employee Retirement Contribution. For the remaining years, fringe benefits increase by the proposed inflation rate plus one percent. Judgments and claims have not grown with inflation in recent years. These costs have been projected at 50 percent of the proposed inflation rate from FY2006 forward. All other operating costs increase at the projected inflation rate.

3.2.2 Maintaining Capital Equipment, Facilities and Vehicles

Every two years, MUNI prepares a SRTP. The CIP element covers a 20-year period. MUNI issued its current SRTP (FY2004-2023) in FY2004. MUNI's CIP includes major investments in rolling stock or in the physical plant and are costs that would not normally be covered in the operating budget. Some of MUNI's capital projects are programmatic, such as fleet and infrastructure replacement projects that recur on a regular basis. Expansion projects such as the Third Street LRT are developed through major corridor or other planning studies. During the past two SRTPs, MUNI has conducted a Call for Capital Projects, which provides an opportunity for projects to be proposed, reviewed, and ranked in the CIP. The table below summarizes the new MUNI capital projects for FY2004 through FY2023, which are included in MUNI's CIP.

MUNI's CIP – FY2004 - FY2023 (dollars in millions)

	20-year total
Fleet Program	$ 2,499.9
Infrastructure Program	7,871.0
Facilities Program	696.5
Equipment Program	107.0
Other Projects	29.9
Total General Capital Expenses	**$ 11,204.3**

Source: MUNI's Short Range Transit Plan FY2004-2023

3.2.2 Maintaining Capital Equipment, Facilities and Vehicles (continued)

MUNI's fleet program includes rehabilitation and replacement of MUNI's revenue and non-revenue vehicles. Infrastructure programs include rehabilitation, replacement and modification of rail, communications, signals, overhead, subway, stations and cable car systems. In addition, infrastructure includes adding and improving Americans with Disabilities Act (ADA)-mandated Key Stops, accessibility improvements, and transit preferential streets. The facilities program includes development, management and maintaining space for operating, maintenance, administration and storage needs to support MUNI's operations. The equipment program provides the tools needed to continue operation of MUNI's operating, maintenance and administrative functions. Other projects are capital projects not included above.

MUNI's financial projection focuses on SOGR outlays to maintain existing core transit services. Enhancement and expansion projects that are deferrable if not funded or projects that MUNI has not historically undertaken with capital funds are not included in MUNI's 20-year cash flow projection.

3.2.3 Rail and Bus Expansion Plans

The Third Street LRT project is the only bus or rail expansion plan in MUNI's 20-year cash flow projection. The Third Street LRT project is comprised of two phases, the IOS phase and the CS phase. No other bus or rail expansion has been identified, budgeted or funded at this time and, therefore has not been included in the baseline financial plan.

3.3 Financial Condition and Capability Results

MUNI has prepared a 20-year cash flow analysis to demonstrate its financial capacity. This analysis projects the revenues and expenditures, both operating and capital, that MUNI expects to incur in continuing current transit services with the addition of the Third Street LRT project. If the farebox and state and local sales tax revenues can be realized, as illustrated in MUNI's 20-year financial projection included in Appendix A-2 and A-3, MUNI would have the financial resources to eventually fund its existing system and to build, operate, and maintain the Third Street LRT. However, MUNI has not demonstrated adequate debt capacity, available financing arrangements or cash reserves to finance or provide a cushion against unexpected cost increases or delayed federal funding. This debt capacity would also need to provide a cushion against the risks related to slower growth, negative cyclical variations, or reduced revenues. The projection also indicates years with excess funds from operations used to support the capital programs or generate cash reserves. There is no basis to indicate that this is possible under the current funding process for MUNI. Thus, there is significant risk that MUNI's financial capacity might not be adequate to assure project completion and continued operations.

SECTION 4

SENSITIVITY ANALYSIS

SENSITIVITY ANALYSIS

The FCA is based on assumptions regarding trends in future revenues and costs. Because many of these costs and revenues are variables beyond MUNI's control, there is some uncertainty about how these variables, such as sources of revenue or O&M costs, will behave in the future. Therefore, sensitivity testing is conducted to test the assumptions used in the financial plan. These measure the impact of adverse changes to the more important assumptions used in the baseline financial plan. The indicator showing the effect of the sensitivity analysis is the cash balance at the end of FY2024.

4.1 Farebox Revenue

Farebox revenue is the largest component of system-generated revenue and subsidizes approximately 24.4 percent of MUNI's operating expenses. Overall, farebox revenue is the second largest source of operating revenue after parking revenue.

In FY2006, FY2010, and every three years thereafter, MUNI projects a fare increase to match CPI inflation. Proposition E provides MUNI with the authorization to include fare increases in its budget. If MUNI's budget does not request more General Fund support than determined by the Proposition E formula, the Mayor must send the budget to the Board of Supervisors as submitted.

To examine the potential impact of a reduction of farebox revenue as a result of these fare adjustments, a sensitivity test was run to determine the effect a five and ten percent reduction in the projected annual farebox growth rates would have on the operations by the end of FY2024. The tests resulted in a reduction of operating income during the 20-year period of $62.5 million and $123.9 million. For the five percent test, total operating revenue exceeded total operating expenses by $324.1 million. For the ten percent test, operating revenue exceeded operating expenses by $262.7 million.

4.2 State and Local Sales Tax Revenue

Sales and use tax revenue subsidizes approximately 13.0 percent of MUNI's operating expenses. From FY1979 to FY2004, the growth rate in sales tax revenue has averaged 3.3 percent annually. Over the last 10 years (FY1995 to FY2004) and five years (FY2000 to FY2004) the average annual growth rate was 4.5 and (0.6) percent, respectively.

MUNI's financial projection assumes an average annual growth rate of 4.5 percent. The projection assumes that the recent negative trend in sales and use tax revenue will reverse, as there are no additional products or services identified which can be added to the taxing base.

A sensitivity test was conducted to determine the effect on operating income if the projected annual growth rates were reduced by five and ten percent. Based on a five percent reduction

4.2 State and Local Sales Tax Revenue (continued)

in the growth rates, operating revenue during the 20-year period decreased by $67.8 million, reducing total operating revenue over operating expenses during the 20-year period to $318.8 million. A ten percent reduction in the growth rates resulted in a reduction of $133.6 million in operating revenue, resulting in total operating revenue over operating expenses of $253.0 million for the 20-year period.

4.3 Parking Revenue

Parking revenue is the largest source of operating revenue and subsidizes approximately 27.8 percent of MUNI's operating expenses. MUNI projected an annual growth rate equal to inflation and an additional one percent increase beginning in FY2006 and every third year thereafter for changes in parking policy, new meters and increased rates.

A sensitivity test was run to determine the effect a five and ten percent reduction in the projected annual growth rates would have on the operations by the end of FY2024. The tests resulted in a reduction of operating income during the 20-year period of $79.9 million and $158.0 million, respectively. For the five percent test, total operating revenue exceeded total operating expenses by $306.7 million during the 20-year period. For the ten percent test, operating revenue exceeded operating expenses by $228.6 million during the 20 years.

4.4 San Francisco General Fund Contribution

Proposition E established the base amount of revenue that MUNI receives from the City of San Francisco's General Fund. A formula was created which dictates that the base amount of General Fund support increases and decreases at the same annual percentage rate as overall City discretionary revenues. As a result, the City's contribution to MUNI is more predictable than previous years. In FY2004, the City's General Fund Contribution represented 21.0 percent of operating expenses.

MUNI's 20-year cash flow projection assumes the City's discretionary funds will increase with inflation, except for an increase in funds during FY2006 and FY2007, which results from revenue increases proposed by the City of San Francisco requiring voter approval.

A sensitivity test was conducted to determine the effect on operating income if the projected annual growth rates were reduced by five and ten percent. The tests resulted in a reduction of operating income during the 20-year period of $93.9 million and $185.7 million, respectively. For the five and ten year tests, total operating revenue exceeded operating expenses during the 20-year period by $292.7 million and $200.9 million, respectively.

4.5 Other Operating Revenue and Funding

Other operating revenue and funding subsidized approximately 13.8 percent of MUNI's FY 2004 operating expenses. MUNI forecasted other operating revenue and funding at an average annual growth rate of 2.4 percent beginning in FY2008. From FY2005 to FY2007, the growth rate ranges from (19.3) percent to 3.7 percent.

A sensitivity test was conducted to determine the effect on other operating income if the projected annual growth rates were reduced by five and ten percent. Based on a five percent reduction in the growth rates, operating revenue during the 20-year period decreased by $11.5 million, reducing total operating revenue over operating expenses during the 20-year period to $375.1 million. A ten percent reduction in the growth rates resulted in a reduction of $23.0 million in operating revenue, reducing total operating revenue over operating expenses during the 20-year period to $363.6 million.

4.6 O&M Costs

MUNI's 20-year cash flow projection assumes a 3.6 percent average annual inflation rate for O&M costs beginning in FY2007. For FY2005 and FY2006, O&M costs represent the amount budgeted by MUNI. In FY2006, salaries increase from 1.7 percent to 2.0 percent. In FY2006 and FY2007 fringe benefits are calculated based on known increases. All other O&M costs increase based on projected CPI through FY2024.

A sensitivity test was conducted to determine the effect on operating costs if the projected annual inflation rate would be increased by five and ten percent. Based on a five percent increase in the inflation rate, cash flow generated by operations would decrease a total of $277.3 million during FY2005 to FY2024. A ten percent reduction would result in a reduction of $560.9 million in cash flow generated. MUNI maintained a positive cash reserve throughout the entire projection for the five percent test. For the ten percent test, the final four years (FY 2021 – FY 2024) had negative cash reserves and an ending negative cash reserve of ($168.3) million.

4.7 Capital Costs

In MUNI's 20-year cash flow projection, capital and SOGR costs represent the amount budgeted in MUNI's CIP, except for projects that are deferrable if not funded.

A sensitivity test was conducted to determine the effect on projected system capital costs if increased by five and ten percent. Based on a five percent increase, capital costs would increase a total of $162.6 million during FY2005 to FY2024. A ten percent increase would result in an increase of $325.3 million in total capital costs.

4.8 Federal Funding of Third Street LRT

The proposed FFGA New Starts funding of $762.2 million is subject to the successful negotiation of a FFGA and the future availability of budget authority from Congress. Federal funding from the New Starts program, including annual appropriation levels, will be established as part of the FFGA between MUNI and FTA. Annual appropriations are subject to the federal budget process. Through FY2003, MUNI received $1.5 million of New Starts funds, which represents less than 0.1 percent of total project costs. MUNI's 20-year cash flow projection assumes the remaining New Starts funding will be received through FY2016, with more than 90.0 percent of New Starts funding projected evenly from FY2008 to FY2016.

A sensitivity test was conducted to determine the effect on project cash flows if one-half of the projected federal funding for FY2008 to FY2016 were delayed. The result of the test indicated that federal funding would extend until FY2025. During FY2008 through FY2024, MUNI would need to identify alternate funding sources or financing to fund cash shortfalls.

4.9 Financing Costs

MUNI has included $12 million of financing costs in the CS phase project budget. This finance cost contingency was budgeted to provide for financing costs incurred to fund project costs due to potential delayed federal funding. MUNI has not provided the basis for this estimate or the source of the related debt capacity.

The D&A analysis of project financing costs indicates that MUNI has not addressed the need for funding cost increases or operating deficits. The financing plan was not considered adequate.

4.10 Stress Case Scenarios

An analysis of the reasonableness of financial assumptions is only a starting point to an assessment of overall financial capacity. It is also important to include an analysis of continued financial viability in the event that one or more of the assumptions are not realized as projected. Accordingly, sensitivity analysis subjects the baseline financial plan assumptions to more rigorous tests. This analysis first isolates the impact of changes to individual assumptions that most affect financial results. Sensitivity analysis demonstrates the relative importance of each assumption to financial viability. Once the most significant factors have been identified individually, the stress case scenario assumes that adverse changes to those major assumptions occur simultaneously.

Two stress case scenarios were applied to MUNI's 20-year cash flow projection. The first stress case assumes a reduction in projected annual growth rates by five percent on the revenues and

4.10 Stress Case Scenarios (continued)

funding and an increase in projected annual inflation rates by five percent on expenditures and capital costs assumed for the 20-year cash flow projection. A summary of the assumptions used by MUNI is located in Appendix A-4 to A-8.

From FY2005 to FY2024, MUNI would incur 12 years with negative cash reserves during the five percent stress case scenario. At the end of FY2024, MUNI would have negative cash reserves of ($363) million.

The second stress case assumes a reduction in projected annual growth rates by ten percent on the revenues and funding and an increase in projected annual inflation rates by ten percent on expenditures and capital costs (except the SCLRP) assumed for the 20-year cash flow projection.

The ten percent stress case scenario resulted in negative cash flow from operations during 15 years and negative ending cash reserve balances throughout the 20-year period. At the end of FY 2024, MUNI would have negative cash reserves of ($1.1) billion. Under this stress case, MUNI would not be able to maintain a balanced operating budget or maintain its existing system.

Similar tests of capital expenditures indicated shortfalls in the ability of MUNI to maintain the SOGR. These stress tests have demonstrated a high risk that MUNI does not currently have the financial capacity to handle adverse increases in expenditures or reductions in revenue. However, MUNI's long operating history indicates that MUNI has been able in the past to obtain local support and funding to continue operations, even with adverse economic conditions.

SECTION 5

CONCLUSION

CONCLUSION

If all funding sources identified in the financial projections prepared by MUNI are realized, and no cost increases are incurred, MUNI would have the financial capacity to complete the construction of the Third Street LRT project and continue to operate the transit services as detailed in the latest financial plan. The result of this FCA indicates that there are risk issues with the growth rates of farebox and other revenue sources, including dedicated sales taxes that MUNI is highly dependent upon, both for capital and operations funding. The projected funding increases also include amounts that require voter or outside approval of the source before they can be realized. Although available funding resources might provide coverage of the current committed level of MUNI expansion plans, MUNI has no complete plans for funding cost increases or addressing delays in funding sources. These risk issues are primarily highlighted by the fact that there was an actual decrease in dedicated sales tax revenue during the last three years. This decrease was consistent with the economic downturn experienced by most of the country, but for MUNI the decrease was more moderate than that experienced by most of the country. These risks are somewhat mitigated by the recovery trend noted in the San Francisco area. However, MUNI continues to incur unexpected cost increases in capital areas and budget deficits in operations. So far MUNI has been able to obtain additional funding without significant service reductions. Risk exists that MUNI may not be able to continue these successful mitigation efforts.

In summary, the result of this FCA indicates that MUNI may not have the financial capacity to construct the remaining Third Street LRT project in a timely manner, as reflected in the latest financial plan, since MUNI has not identified adequate funding sources or debt capacity to fund cost increases and delays in funding until additional funding is available. A major concern is that significant shortfalls in available funding or substantial cost increases could result in reduced or delayed capital projects and service level reductions, which would not comply with the FFGA requirements. In addition, MUNI has significant plans for capital improvement projects (over $7 billion) that were excluded from the financial projection, since they are not committed and could be deferred. There is some risk that these deferred projects would be funded from available reserve funds and result in reserve deficits in later periods.

APPENDICES

MUNI'S BASELINE FINANCIAL PLAN SUMMARY

SAN FRANCISCO MUNICIPAL RAILWAY

ACTUAL CASH FLOWS (FY2000-FY2004)

(dollars in thousands)

	2000	2001	2002	2003	2004	Total
Operating Revenues						
Fares	102,103	100,716	98,181	100,960	115,547	517,507
Parking	103,635	104,174	114,254	112,604	131,339	566,006
State & Local Sales Tax	67,916	65,232	87,034	73,304	67,272	360,759
SF General Fund	82,780	100,411	94,305	100,792	99,264	477,551
Other Revenues	22,642	45,724	45,457	62,265	65,388	241,476
Total Operating Revenues	**379,076**	**416,258**	**439,231**	**449,925**	**478,810**	**2,163,299**
Operating Expenditures						
Employee Salaries & Benefits	267,702	290,643	317,656	326,854	345,330	1,548,185
Material & Supplies	35,030	34,682	31,619	30,797	26,847	158,975
Workers' Compensation	19,155	18,800	19,422	18,213	21,119	96,709
Paratransit	13,691	15,176	17,889	18,763	18,203	83,722
Other Expenditures	43,498	56,955	52,647	55,298	61,353	269,751
Total Operating Expenses	**379,076**	**416,258**	**439,231**	**449,925**	**472,851**	**2,157,341**
Cash Flow from Operations	**-**	**-**	**-**	**-**	**5,958**	**5,958**
Capital Revenues (State of Good Repair Projects only)						
Federal	135,970	83,083	96,585	75,032	96,848	487,519
State	3,150	16,540	51,344	67,522	12,534	151,091
Local	74,308	21,816	23,108	33,105	70,553	222,889
Total Capital Revenues	**213,428**	**121,439**	**171,037**	**175,659**	**179,935**	**861,500**
Capital Expenditures (State of Good Repair Projects only)						
Fleet	84,939	79,599	68,675	9,311	19,268	261,791
Infrastructure	115,198	38,909	94,132	140,464	132,193	520,895
Facilities	13,292	2,929	8,122	9,019	18,333	51,695
Equipment				27	-	27
Other Projects	-	2	109	16,839	10,141	27,091
Total Capital Expenses	**213,428**	**121,439**	**171,037**	**175,659**	**179,935**	**861,500**
Annual Surplus/Shortfall	**-**	**-**	**-**	**-**	**-**	**-**
Cash Balance						
Beginning Cash Balance	-	-	-	-	-	-
Change to Cash Balance	-	-	-	-	5,958	5,958
Ending Cash Balance	**-**	**-**	**-**	**-**	**5,958**	**5,958**

SAN FRANCISCO MUNICIPAL RAILWAY

PROJECTED CASH FLOWS (FY2005-FY2014)

(dollars in thousands)

MUNI Operating Forecast	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Total 2005-2014
Operating Revenues											
Fares	121,927	135,119	135,304	135,444	135,589	155,044	155,198	155,358	170,410	170,579	$1,469,972
Parking	132,350	142,955	149,245	154,021	160,490	165,625	170,925	178,104	183,804	189,685	1,627,204
State & Local Sales Tax	65,665	71,894	81,068	84,949	95,435	99,831	104,357	109,009	113,855	117,498	943,561
SF General Fund	98,859	98,882	138,435	142,865	147,437	152,155	157,024	162,048	167,234	172,585	1,437,524
Other Revenues	67,817	63,277	51,037	52,232	53,151	54,099	55,077	56,418	57,803	59,281	570,191
Total Operating Revenues	**486,618**	**512,128**	**555,088**	**569,511**	**592,101**	**626,754**	**642,581**	**660,938**	**693,105**	**709,630**	**6,048,454**
Operating Expenditures											
Employee Salaries & Benefits	342,454	366,115	377,622	390,831	404,510	418,676	433,346	448,540	464,275	480,572	4,126,941
Material & Supplies	29,113	33,317	34,317	35,415	36,548	37,718	38,925	40,170	41,456	42,782	369,761
Workers' Compensation	20,500	23,105	23,798	24,631	25,493	26,385	27,309	28,264	29,254	30,278	259,016
Paratransit	20,074	20,074	20,676	21,338	22,021	22,725	23,453	24,203	24,977	25,777	225,318
Other Expenditures	74,477	69,517	76,659	78,813	80,923	83,194	98,725	101,519	105,078	106,903	875,806
Total Operating Expenses	**486,618**	**512,128**	**533,072**	**551,027**	**569,495**	**588,698**	**621,757**	**642,696**	**665,040**	**686,312**	**5,856,842**
Cash Flow from Operations	**-**	**-**	**22,017**	**18,484**	**22,606**	**38,056**	**20,825**	**18,242**	**28,065**	**23,318**	**191,612**
MUNI Capital Forecast											
Capital Revenues (State of Good Repair Projects only)											
Federal	97,791	73,889	49,348	132,553	141,417	179,623	168,501	171,124	131,062	165,532	1,310,839
State	523	-	-	-	-	-	-	-	-	-	523
Local	259,497	37,995	35,186	57,321	37,383	89,189	44,829	58,456	7,802	8,306	635,963
Total Capital Revenues	**357,811**	**111,884**	**84,534**	**189,874**	**178,800**	**268,811**	**213,331**	**229,580**	**138,863**	**173,838**	**1,947,325**
Capital Expenditures (State of Good Repair Projects only)											
Fleet	110,201	22,675	2,508	7,627	9,773	46,642	41,733	94,975	28,617	63,592	428,343
Infrastructure	209,406	75,480	54,190	181,200	167,980	221,122	170,247	133,559	109,200	109,200	1,431,584
Facilities	23,116	9,098	27,789	-	-	-	304	-	-	-	60,308
Equipment	-	-	-	1,000	1,000	1,000	1,000	1,000	1,000	1,000	7,000
Other Projects	15,088	4,631	47	47	47	47	47	47	47	47	20,091
Total Capital Expenses	**357,811**	**111,884**	**84,534**	**189,874**	**178,800**	**268,811**	**213,331**	**229,580**	**138,863**	**173,838**	**1,947,325**
Annual Surplus/Shortfall	-	-	-	-	-	-	-	-	-	-	-
Cash Balance											
Beginning Cash Balance	5,958	5,958	5,958	27,975	46,459	69,064	107,121	127,946	146,187	174,253	5,958
Change to Cash Balance	-	-	22,017	18,484	22,606	38,056	20,825	18,242	28,065	23,318	191,612
Ending Cash Balance	**$ 5,958**	**$ 5,958**	**$ 27,975**	**$ 46,459**	**$ 69,064**	**$ 107,121**	**$ 127,946**	**$ 146,187**	**$ 174,253**	**$ 197,570**	**$ 197,570**

SAN FRANCISCO MUNICIPAL RAILWAY

PROJECTED CASH FLOWS (FY2015-FY2024)

(dollars in thousands)

MUNI Operating Forecast	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	Total 2005-2024
Operating Revenues											
Fares	170,754	187,298	187,485	187,677	205,860	206,065	206,277	226,262	226,487	226,720	$3,500,858
Parking	197,652	203,977	210,504	219,345	226,364	233,608	243,420	251,209	259,248	270,136	3,942,669
State & Local Sales Tax	121,258	125,139	129,143	133,276	137,540	141,942	146,484	151,171	156,009	161,001	2,346,524
SF General Fund	178,108	183,808	189,689	195,760	202,024	208,489	215,160	222,045	229,151	236,484	3,498,241
Other Revenues	60,906	62,427	63,997	65,618	67,290	69,079	71,047	72,885	74,782	76,740	1,254,963
Total Operating Revenues	**728,679**	**762,649**	**780,819**	**801,675**	**839,079**	**859,182**	**882,387**	**923,573**	**945,677**	**971,080**	**14,543,255**
Operating Expenditures											
Employee Salaries & Benefits	497,451	514,933	533,040	551,795	571,222	591,344	612,188	633,780	656,146	679,316	9,968,157
Material & Supplies	44,151	45,564	47,022	48,527	50,080	51,682	53,336	55,043	56,804	58,622	880,593
Workers' Compensation	31,337	32,434	33,569	34,744	35,960	37,219	38,522	39,870	41,265	42,710	626,647
Paratransit	26,602	27,453	28,331	29,238	30,174	31,139	32,136	33,164	34,225	35,320	533,099
Other Expenditures	110,299	113,765	117,305	120,920	124,814	128,589	132,746	136,890	141,422	145,587	2,148,143
Total Operating Expenses	**709,840**	**734,149**	**759,268**	**785,225**	**812,250**	**839,973**	**868,928**	**898,746**	**929,863**	**961,555**	**14,156,639**
Cash Flow from Operations	**18,839**	**28,500**	**21,551**	**16,451**	**26,830**	**19,209**	**13,460**	**24,827**	**15,814**	**9,525**	**386,616**
MUNI Capital Forecast											
Capital Revenues (State of Good Repair Projects only)											
Federal	218,669	188,694	93,483	140,809	89,029	84,373	110,990	126,645	107,552	132,358	2,603,441
State	-	-	-	-	-	-	-	-	-	-	523
Local	45,211	58,341	9,003	16,853	49,790	63,265	10,642	10,868	45,260	61,322	1,006,518
Total Capital Revenues	**263,880**	**247,035**	**102,486**	**157,662**	**138,819**	**147,638**	**121,632**	**137,513**	**152,811**	**193,680**	**3,610,482**
Capital Expenditures (State of Good Repair Projects only)											
Fleet	153,634	154,867	72,239	127,615	108,772	109,092	83,086	98,967	114,265	156,134	1,607,013
Infrastructure	109,200	91,121	29,200	29,000	29,000	37,500	37,500	37,500	37,500	37,500	1,906,605
Facilities	-	-	-	-	-	-	-	-	-	-	60,308
Equipment	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	1,000	-	16,000
Other Projects	47	47	47	47	47	47	47	47	47	47	20,556
Total Capital Expenses	**263,880**	**247,035**	**102,486**	**157,662**	**138,819**	**147,638**	**121,632**	**137,513**	**152,811**	**193,680**	**3,610,482**
Annual Surplus/Shortfall	-	-	-	-	-	-	-	-	-	-	-
Cash Balance											
Beginning Cash Balance	197,570	216,409	244,908	266,459	282,910	309,740	328,949	342,408	367,235	383,048	5,958
Change to Cash Balance	18,839	28,500	21,551	16,451	26,830	19,209	13,460	24,827	15,814	9,525	386,616
Ending Cash Balance	**216,409**	**244,908**	**266,459**	**282,910**	**309,740**	**328,949**	**342,408**	**367,235**	**383,048**	**392,574**	**$ 392,574**

OPERATING ASSUMPTIONS

Explanation of Assumptions
SRTP refers to the FY2004-FY2023 Short Range Transit Plan that was approved by the Municipal Transportation Agency Board of Directors at its September 16, 2003 meeting.

The "Three Year Budget Projection" is a report prepared by the Mayor's Office, the Controller's Office, and the Budget Analyst, and sent to the Mayor and the Board of Supervisors on March 19, 2004. It includes projections on future expenditures and revenues.

FY2005 Approved Budget
Figures come from the revised FY2005 amounts included in the Proposed FY2006 budget approved by the MTA Board on February 28, 2005.

FY2006 Budget
Figures come from the Proposed FY2006 budget approved by the MTA Board on February 28, 2005.

Growth Assumptions
Unless noted in the text below, the growth rates are those noted for the fiscal year. However, in some cases and as detailed below, experience shows that growth will not be consistent with CPI.

For FY2007, the report uses 4.4 percent revenue growth, which is from the "Three Year Budget Projection." That report predicts tax revenue growth of 4.4 percent. The SRTP used 3.5 percent, which was from an earlier estimate by the California Department of Finance. For FY2007, the report uses 3.0 percent expenditure growth.

For FY2008 and beyond, the report uses 3.2 percent. The U.S. Congressional Budget Office long-range CPI forecast for the United States estimates CPI growth at 2.2 percent per year from FY2007 through FY2015. Per the SRTP, the Bay Area CPI growth rate has historically been one percentage point higher than that of the U.S. The SRTP used 3.7 percent, which was an extrapolation of the last year available from the California Department of Finance.

Fare Revenues
From FY2007 forward, the revenues are derived from a revised version of the fare model developed for the SRTP. There is a fare increase in FY2006, and the next increase is in FY2010, and then every three years thereafter. The model assumes that all fares, except for cash discount fares, will be increased every three years by the CPI over that three year period (i.e., 1.032 x 1.032 x 1.032). The model assumes that there will be no growth in ridership, nor that there will be any elasticity of demand.

OPERATING ASSUMPTIONS

Parking Revenues
The model assumes that parking revenues will increase by CPI each year, and by CPI plus 1.0 percentage point every three years. This is to account for changes in parking policy, including new meters and fee increases. Because there is an increase in FY2006, the next assumed increase occurs in FY2009.

States Sales Tax and Fuel Tax Assistance
The report uses figures provided by the MTC for the SRTP for FY2006 through FY2013. Then the figures grow by CPI.

RM-2 Bridge Tolls
This is capped at $2.5 million per year per statute in support of the Third Street LRT, with no inflator. There is also funding available for owl service beginning in FY2006.

Mission Steuart Lease Revenues
The report uses figures from the contract with the developer.

Fund Balance
It is assumed that there are no fund balances after FY2005.

Dedicated Paratransit Funding
There is a source of Paratransit funding from the local Transportation Authority, that will remain level at $9,670,000. The rest of Paratransit revenues are assumed to grow by CPI.

Other Revenue Transfers and Non Operating Revenue
TIDF fee increases were approved. The report assumes that after a slow period of five years of level funding, TIDF revenues increase by CPI.

Transfers In
Beginning in FY2006, this reflects the fact that the MTA is comprised of both MUNI and DPT. However, from an accounting and budgeting perspective, they are two separate departments, so additional revenues must be transferred into MUNI.

Other Salaries
For FY2007, the report assumes salaries increase by 2.3667 percent. For the remainder of the forecast, the report increases wages by CPI.

Fringe Benefits
Fringe benefits FY2007 are calculated on the known increases per the recent MOUs to the Employer Retirement Contribution and the Employer pickup of the Employee Retirement Contribution. For FY2008 forward, the report assumes fringe benefits will increase by CPI plus 1.0 percent.

OPERATING ASSUMPTIONS

Judgments & Claims
Judgments and claims have not grown with inflation in recent years. The cost for this item is assumed to increase by 50.0 percent of CPI from FY2007 forward.

Paratransit Contract
While historically Paratransit expenses have grown beyond the rate of inflation, that appears to be slowing. For FY2006, no growth is predicted, for example. For the remainder, the report assumes that Paratransit costs will increase by inflation.

Fast Pass on BART
This report holds Fast Pass on BART expenditures constant, with the assumption that the advent of Translink and the demand for the extension of Fast Pass use on BART to seniors and disabled will result in a restructuring of the agreement between BART and MUNI.

Net Service Changes
These figures have been updated from the SRTP to reflect FY2003 NTD rates. The figure is a net of new expenses for the Third Street LRT Project, minus savings due to associated bus changes.

CAPITAL PROGRAM ASSUMPTIONS

FUND SOURCE	ASSUMPTIONS
Federal Sources	
Sect. 5307	FY2005-FY2013 based on MTC projections. FY2014-FY2024 uses 4.0 percent per year growth rate (as determined by MTC staff). MUNI share estimated at 50.5 percent of San Francisco/Oakland Urban Area. FY2005 and FY2006 based on actual programming.
Sect. 5309-FG	FY2005-FY2013 based on MTC projections. FY2014-FY2024 uses 4.0 percent per year growth rate (as determined by MTC staff). MUNI share estimated at 41.7 percent of San Francisco/Oakland Urban Area. FY2005 and FY2006 based on actual programming.
Sect. 5309-NS (Discretionary)	FY2005-FY2013, equal to federal amount needed for Third Street LRT Phase 2-Central Subway ($10-$80M/year). Funds for other projects not assumed at this time. Regional share based on MUNI staff estimate.
Sect. 5309-BAF (Discretionary)	FY2005-FY2023 based on 1999 TIP and prior year averages. MUNI share based on estimates for replacement needs and fuel path changes. No change from FY2002 projections.
Sect. 5303-Planning	MUNI share projected at current levels with no increase.
Federal STP	FY2005-FY2023 based on MTC projections. MUNI equals 12.1 percent of regional total based on average of FY1991-FY1998. No change from FY2002 projections. Assumes funding levels will remain at a constant level due to many unknowns with reauthorization. Also, projection is based on the old San Francisco/Oakland Urban Area prior to the 2000 Census. No programming in FY2005 due to OA shortfalls from FY2003. MTC is not revising the projections for these funds until after TEA-3 adoption.
TEA (Federal Enhancement)	Based on MTC projections of $1,027,225 per year. No escalation for the TLC/HIPTEA program, and $513,613 per year at 2.0 percent escalation for the County TEA program. SFCTA recommended that MUNI assume a 50.0 percent share of the TLC/HIP funds. From this, 50.0 percent was extrapolated for the County TEA.
Federal CMAQ	FY2005-FY2021 escalated at 2.0 percent per year based on MTC projections. MUNI equals 13.3 percent of regional total based on average of FY1991-1998. No change from FY2002 projections. Many uncertainties regarding first cycle STP/CMAQ programming and reauthorization. No programming in FY2005 due to OA shortfalls from FY2003. MTC is not revising the projections for these funds until after TEA-3 adoption.
State Sources	
State STIP	Programmed/planned funds for FY2005-FY2007 from 2002 STIP (regional funds do not include TCRP & Prop. 42-MUNI TCRP is included); MTC projections for FY2008-FY2024 (includes TCRP and Prop. 42). MUNI share is 60.0 percent of County, same as in FY2004. Projections for FY2008-FY2024 based on revised MTC RTP projections, received 1/10/2003. MTC is not revising projections for these funds until after TEA-3 adopted.

CAPITAL PROGRAM ASSUMPTIONS

FUND SOURCE	ASSUMPTIONS
Local Sources	
AB 664-Bridge Tolls	Estimates based on 3/18/2003 MTC projections for the first 10 years. MTC said growth rate of 0.5 percent was used to calculate projections so that rate used for FY2014-FY2024. Reduce MUNI share to 70.0 percent to account for JPB growing claims on funding. There is still no agreement on what the split of the West Bay Share should be between MUNI and the JPB. FY2005 and FY2006 based on actual programming.
RM1-Bridge Tolls	Estimates based on FY2001 RTP projections. MUNI share is 50.0 percent of West Bay share, which is 30.0 percent of regional share. Projections to begin in FY2008.
RM2-Bridge Tolls	Includes $30 million for Metro East, $10 million for Historic Streetcars, and $11.6 million for NextBus.
TFCA	No change in assumptions from FY2002 Projections. Per Mike Murphy BAAQMD-$20 million per year to the region, $12 million per year (60.0 percent) for the Regional program; $780 per year (40.0 percent) return to CMA's for Program Manager funds. Confirmed by Dave Chan SFTCA.
Prop. K	Based on SFCTA Expenditure Plan at an inflation rate of 1.4 percent per year. $22.57 million in FY2005 reflects fund swap with STIP funds due to state budget shortfall.

PROPOSED THIRD STREET LRT PROJECT MAPS

THIRD STREET LRT (PHASE 1) MAP

PROPOSED CENTRAL SUBWAY (PHASE 2) MAP

ACTUAL FAREBOX REVENUE

Actual Farebox Revenue

Fiscal Year	Revenue (in millions)	% Change
1985	$ 55.3	
1986	62.1	12.3%
1987	68.3	10.0
1988	69.6	1.9
1989	76.8	10.3
1990	78.2	1.8
1991	79.8	2.0
1992	82.5	3.4
1993	90.3	9.5
1994	97.3	7.8
1995	93.4	(4.0)
1996	94.6	1.3
1997	98.0	3.6
1998	97.9	(0.1)
1999	97.6	(0.3)
2000	102.1	4.6
2001	100.7	(1.4)
2002	98.2	(2.5)
2003	101.0	2.9
2004	115.5	14.4
Total	**$ 1,759.2**	

Average Annual Percentage Change	
FY 1985 – FY 2004	**4.0%**
Last 10 Years	**1.7%**
Last 5 Years	**3.4%**

Source: MUNI's Historical Revenue & FY2004 SRTP

ACTUAL STATE AND LOCAL SALES TAX REVENUE

Actual State and Local Sales Tax Revenue

Fiscal Year	Revenue (in millions)	% Change
1985	$ 36.4	
1986	39.8	9.3%
1987	37.5	(5.8)
1988	33.0	(12.0)
1989	35.0	6.1
1990	38.5	10.0
1991	49.1	27.5
1992	49.5	0.8
1993	39.5	(20.2)
1994	43.5	10.1
1995	42.0	(3.4)
1996	50.4	20.0
1997	58.3	15.7
1998	58.8	0.9
1999	69.2	17.7
2000	67.9	(1.9)
2001	65.2	(4.0)
2002	87.0	33.4
2003	73.3	(15.7)
2004	67.3	(8.2)
Total	**$ 1,041.2**	

Average Annual Percentage Change	
FY 1985 – FY 2004	**3.3%**
Last 10 Years	**4.5%**
Last 5 Years	**(0.6)%**

Source: MUNI's Historical Revenue & FY2004 SRTP

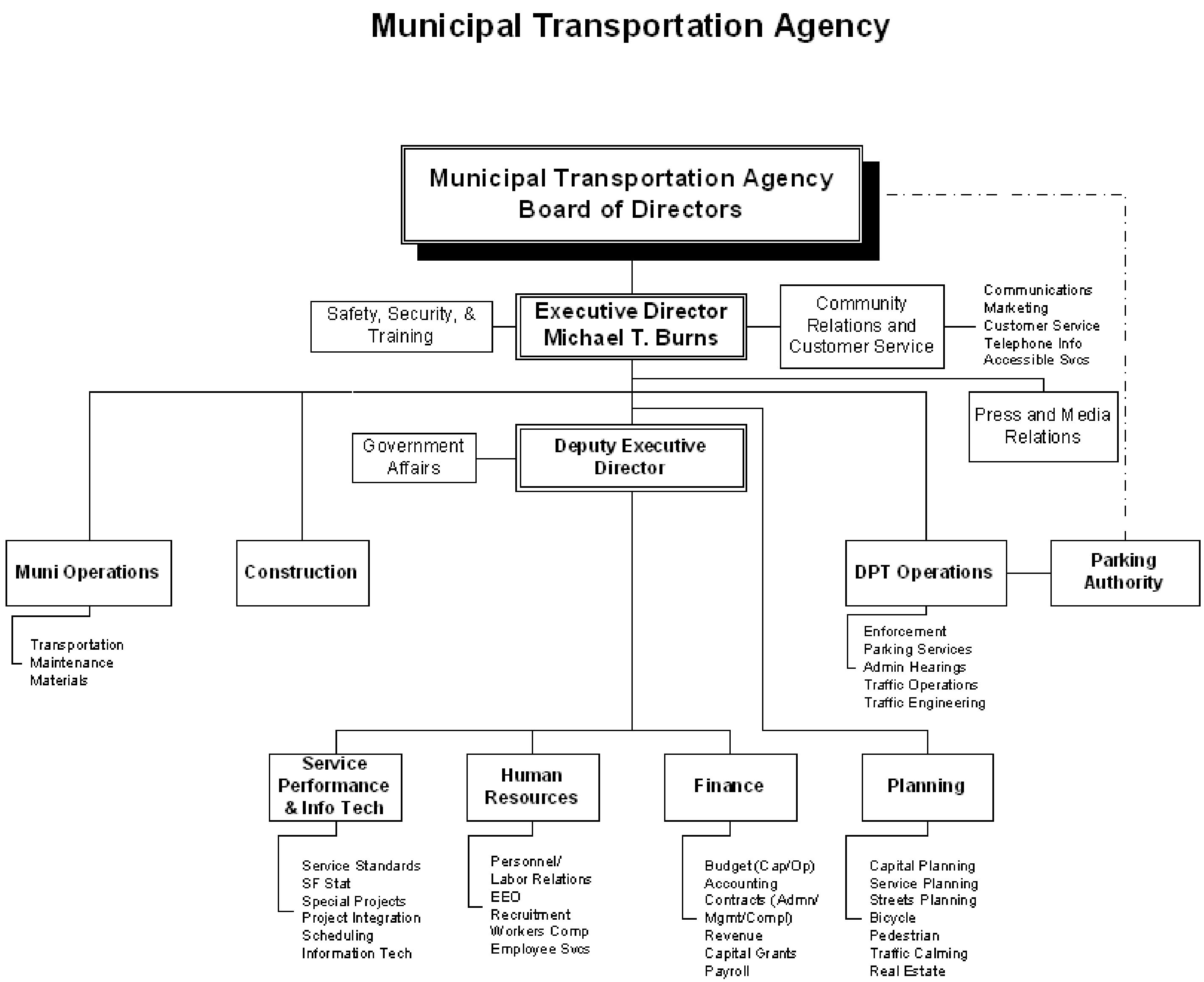
ACTUAL PARKING REVENUE

Actual Parking Revenue

Fiscal Year	Revenue (in millions)	% Change
1995	$ 71.4	
1996	78.7	10.2%
1997	78.9	0.3
1998	83.6	6.0
1999	92.0	10.0
2000	103.6	12.6
2001	104.2	0.6
2002	114.3	9.7
2003	112.6	(1.5)
2004	131.3	16.6
Total	**$ 970.6**	

Average Annual Percentage Change	
FY 1995 – 2004	**7.0%**
Last 5 Years	**7.4%**

MUNI'S ORGANIZATION CHART


Municipal Transportation Agency
Municipal Transportation Agency Board of Directors
Safety, Security, & Training
Executive Director Michael T. Burns
Community Relations and Customer Service
Communications
Marketing
Customer Service
Telephone Info
Accessible Svcs
Press and Media Relations
Government Affairs
Deputy Executive Director
Muni Operations
Transportation
Maintenance
Materials
Construction
DPT Operations
Enforcement
Parking Services
Admin Hearings
Traffic Operations
Traffic Engineering
Parking Authority
Service Performance & Info Tech
Service Standards
SF Stat
Special Projects
Project Integration
Scheduling
Information Tech
Human Resources
Personnel/
Labor Relations
EEO
Recruitment
Workers Comp
Employee Svcs
Finance
Budget (Cap/Op)
Accounting
Contracts (Admn/
Mgmt/Compl)
Revenue
Capital Grants
Payroll
Planning
Capital Planning
Service Planning
Streets Planning
Bicycle
Pedestrian
Traffic Calming
Real Estate

LIST OF PERSONS INTERVIEWED

List of Persons Interviewed

Name	**Title**
MUNI	
Stuart Sunshine	Deputy Executive Director
Kate Breen	Legislative Affairs Manager
Kenneth Jew	Manager of Project Management
Duncan Watry	Manager, Planning and Grants
Alicia Fletcher	Acting Chief Financial Officer
Jerry Levine	Grants Administrator
Taylor Emerson	Special Projects
Monique Dejong	Manager, Capital Grants
Julia Dawson	Budget
Shannon Gaffney	Acting Budget Manager
Peter Straus	Manager of Service Planning
Shahnam Garengi	Manager of Contract Administration
Dennis Tsai	Senior Project Manager – Third Street LRT Project – Phase 1
John Thomas	Senior Project Manager – Third Street LRT Project – Phase 2
Fred Clarke	Former Finance Manager
SFCTA	
Jose Louis Moscovich	Executive Director
Paul Ward	Manager of Capital Projects
Metropolitan Transportation Commission (Metropolitan Planning Organization)	
Alix Bockelman	Senior Transportation Analyst
FTA Region 9 Office	
Jeffrey Davis	General Engineer
STV Incorporated (PMOC)	
Bruce Bernhard	Project Management Oversight Consultant

INVENTORY OF DOCUMENTS REVIEWED

Inventory of Documents Reviewed

MUNI	
20-Year Cash Flow Projection, September 2004	20-Yezr Cash Flow Projection - revised April2005
Organization Structure	MUNI – Background Information FY2002
MUNI Charter	Measures to Reduce FY2005 & FY2006 Operating Budget Deficit
MUNI's Capital Improvement Program – Revised May 2001 (Version 2.1)	2001 Triennial Review Findings & Responses to Findings
MUNI Historical Parking Revenues	Analysis of Historical MUNI Revenues
OTRAK Risk Assessment Questionnaire – FY2002	MUNI – Final FMO Review Report (June 20, 2003)
Active Grants (as of 2/17/2004)	FY2000 Financial Statements (Audited)
FY2001 Financial Statements (Audited)	FY2002 Financial Statements (Audited)
FY2003 Financial Statements (Audited)	FY2004 Financial Statements (Audited)
MUNI Financial Plan (9/30/04)	FY2005 YTD Budget to Actual Compliance - Revenues and Expenditures
2003 TIP Financial Data for Transit Projects at MUNI	2005 TIP – MUNI Projects
2005 TIP (MTC) – MUNI Projects Only	MUNI Light Rail Fleet Management Plan (June 2001)
2001 – 2021 Short Range Transit Plan	2004 – 2023 Short Range Transit Plan
FY2003 Operating Budget	MUNI Capital Improvement Project Estimate (9/17/03)
MUNI Quarterly Project Status Reports of Key Projects (as of 12/31/03)	Capital Projects Data
MUNI – Replacement and Rehabilitation Plan – Motor & Trolley Coach Fleet (September 2000)	MUNI Light Rail Vehicle 2 Retrofit Program Clarification Correspondence (November 2003)
MUNI Project Management Plan Final Draft (June 1999)	Assessment of Project Readiness and Requirements FY2005 Annual New Starts Report (Nov/Dec 2003) CS Project
MUNI Project Cost Fund Summary Report	MUNI Contracts Greater than $100,000 Report
FY2005 Operating Budget	Proposed FY2006 MTA Budget, dated 2/1/05
MUNI NTD Report - 2003	FY2005 & 2006 Operating Budget Deficit Cut Measures – MUNI
Statement of Net Assets (FY2003) MUNI, Parking, Traffic, Parking Garages	Department of Parking & Traffic – Biannual Report (FY2003 – FY2004)
MME Budget and Allocated Contingency	Project Cost/Fund Summary Report
MUNI Press Releases	
Third Street LRT Project	
Background Information on Third Street Light Railway	New Central Subway Project – Environmental Issues
Background Information on New Central Subway Project	Third Street Corridor – Project Fund Summary (March 2003)
Thirds Street Light Rail Project – Project Fund Summary – Phase 1 – Initial Operating Segment (April 2005)	Thirds Street Light Rail Project – Project Fund Summary – Phase 2 – Central Subway (April 2005)
Third Street – Final Environmental Impact Statement November 1998, Volume 1	Third Street – Final Environmental Impact Statement November 1998, Volume 2
Third Street – Monthly Progress Report (January 2004)	Quarterly Project Status Report (as of 3/31/03)
Third Street LRT Project Update (Feb. 2005)	PMOC Spot Report No. 33 (August 2002)
PMOC Draft Spot Report (March 2005)	PMOC Spot Report #2 (May 2005)
New Central Subway/Third Street Phase 2 Administrative Draft – Project Management Plan	Third Street LRT Phase 1 – Budget Status Report
MUNI Metro East Light Rail Maintenance Facility Budget	Third Street Project – Cost Reports

Inventory of Documents Reviewed

City and County of San Francisco	
SF City & County Budget Preparation Instructions FY2002 – 2003	SF City & County Budget (MUNI included) June 30, 2002
SF City & County FY2003 CAFR	SF City & County FY2004 CAFR
Demographic Data for the Bay Area (2003-2005)	SF City & County Population Estimate (U.S. Census Bureau)
SFCTA	
SFCTA – New Transportation Expenditure Plan	SFCTA – Commercial Paper ($200 million) Offering "Draft"
SFCTA – Commercial Paper Authorization	SFCTA – FY2003 Strategic Plan Update (Summary)
SFCTA – Prop "B" Resolution Balances	
FTA	
MUNI NTD Report – 2001	MUNI NTD Report – 2002
MUNI NTD Report – 2003	FTA Grant Agreements for Third Street LRT Project
FTA Notification Letter to MTA Re: FCA	
Metropolitan Transportation Commission	
Draft 2030 Transportation Plan (Oct. 2004)	
State of California	
TCRP Project Information	