

AGENDA ITEM 9-E
ACTION ITEM

TO: CHAIRMAN ZIMMERMAN AND THE VRE OPERATIONS BOARD

FROM: DALE ZEHNER

DATE: AUGUST 21, 2009

**RE: REFERRAL OF PRELIMINARY FY 2011 VRE OPERATING AND
CAPITAL BUDGET TO THE COMMISSIONS**

RECOMMENDATION:

The VRE Operations Board is being asked to authorize the Chief Executive Officer to refer the Preliminary FY 2011 VRE Operating and Capital Budget to the Commissions for their consideration, and that the Commissions, in turn, refer these recommendations to the jurisdictions for their review and comment.

BACKGROUND

FISCAL YEAR 2010 BUDGET

A discussion of FY 2009 revenue and expenses and the use of the estimated surplus will be presented at the meeting, once the year-end close process is substantially complete.

The FY 2010 budget projections have changed since the budget was adopted, as indicated in previous reports to the Operations Board. Some of the major items that have changed since the budget was approved in December 2008 are as follows:

- **Higher than anticipated Commonwealth revenue:** In December 2008, the Commonwealth estimated that they would fund their portion of the match to the federal capital program at **17%** in FY 2010 and VRE's budget was adjusted accordingly. In May, the Commonwealth published their draft Six-Year Improvement Program, with FY 2010 average funding of **78%**, which is expected to result in additional funding to VRE of nearly **\$3.3 million**, net of a \$400,000 decrease to operating funds. **However, the Commonwealth is continuing to experience less than anticipated revenue, which could impact the amount that they are actually able to fund.**
- **Diesel fuel costs:** The adopted budget was based on diesel fuel costs of \$2.65 per gallon for 1.76 million gallons. Because of fuel hedging activities we have locked into pricing for about 42% of our usage and are now projecting an average price of \$2.30, including an estimate of costs for the unhedged fuel purchases. This results in fuel costs of approximately \$350,000 less than the amount budgeted. The situation will be monitored as market prices continue to be volatile.
- **Insurance premium costs:** Insurance premium costs for FY 2009 are slightly lower than budgeted, although this will be balanced by less than anticipated earnings in the Trust Fund for FY 2009 and FY 2010.
- **Fare revenue:** Budgeted fare revenue of \$26.9 million appears to be reasonable based on current ridership, but will continue to be evaluated. Average Daily Ridership (ADR) for FY 2010 is estimated at 15,600 and the cumulative ADR for FY 2009 was 15,754.
- **Amtrak retroactive payments:** In January 2008, Amtrak agreed to a settlement with their employee groups that included retroactive payments for the period 2002 to April 2008. VRE is responsible for payments made to Amtrak employees assigned to VRE service during that period. VRE has been given estimates of this cost and, based on those estimates, have set aside \$2 million for this purpose. However, the final invoice may differ from the estimate.
- **Local match for federal grants:** The federal formula allocation for VRE for FY 2010 is \$600,000 higher than the amount budgeted and the local match will need to be reflected in the revised budget.

VRE staff is reviewing options for how this one-time fund surplus should best be used and will incorporate the use of these funds in the mid-year budget amendment. Recommendations under consideration are as follows:

- Removal of \$400,000 transfer from sale of Mafersa cars; this was added in order to balance the budget when it appeared that Commonwealth funds would be much lower than initially anticipated.

- Restoration of the VRE working capital level, in accordance with the budget guideline adopted for FY 2011.
- An increase to the insurance trust fund balance to restore the balance to the \$10 million required by the Commonwealth; this will reduce the needs in FY 2011 for this purpose.
- Additional funding for locomotives, particularly to match or augment other funds.

At this time, VRE staff is not recommending using the FY 2010 surplus for operating needs in FY 2011.

FISCAL YEAR 2011 PRELIMINARY BUDGET

BACKGROUND:

In accordance with the VRE Master Agreement, which outlines the process for annual budget approval, the preliminary FY 2011 VRE Operating and Capital Budget is attached for review.

VRE staff met with the CAO Taskforce in June and again in August to discuss jurisdictional budget issues and concerns and to review current VRE projections. From these meetings, VRE staff gained an understanding of the significant budget difficulties that the jurisdictions are facing and their need to reduce expenditures wherever possible. As described below, VRE is projecting several large nondiscretionary expense increases in FY 2011. Nearly 80% of VRE's operating costs are fixed (such as insurance and debt service), or contractually determined (such as track access and operating and maintenance service costs), or items such as fuel over which VRE has limited control. As a result, the only options available for substantial cost reductions or additional revenue are fare increases, subsidy increases or major service reductions.

Projections for the cost of operating and maintaining the trains are based on the contracts in place for FY 2010 with escalators similar to those used in years past. Once the new contract has been negotiated in the fall, these amounts will be adjusted as needed. In addition, the cost of Union Station access and mid-day storage is also based on the contract currently in place, although the amounts for future years may differ; negotiations are currently underway.

No fare increase has been included in the preliminary budget. The fare indexing policy is not applicable as a result of the budget guidelines, which direct VRE staff to maintain or reduce jurisdictional subsidy.

VRE staff is committed to maintaining or reducing jurisdictional subsidies for FY 2011.

DISCUSSION:

The FY 2011 preliminary budget totals \$86.7 million, of which \$2.4 million is currently unfunded (assuming level local subsidy and no fare increases in FY 2011). As in the past, VRE will submit a balanced budget to the jurisdictions in November so that it can be evaluated prior to its submission to the Operations Board in December.

The major causes of the current gap between revenue and expenses are outlined in the table below:

Both revenue and expenses are still under review and these projections are expected to change considerably over the next several months. The assumptions used in preparing the preliminary draft are as follows:

1. Fare revenue of \$28.8 million assumes no fare increase. Ridership is estimated at 16,864 with service at the current level of 30 daily trains. The non-revenue Fredericksburg train (#312) will be converted to a revenue train. Average daily ridership in FY 2009 was 15,754.
2. Contractually set increases in access fee expenses of 4% for CSX and Norfolk Southern. The operations and maintenance contract increase (budgeted in the Amtrak line items) is projected from 5% to 6% above the FY 2010 level, until such time as a new contract is negotiated. Additional funding is budgeted for personnel and maintenance costs for mid-day storage of one train at L'Enfant.
3. Amtrak's contract expires on June 30, 2010. Should a contractor other than Amtrak be chosen in a competitive solicitation to provide train operations and maintenance service, VRE will experience transition costs from Amtrak to a new contractor. The budget assumes that VRE will use federal formula funds of \$1.6 million to offset these costs. A better estimate of any such costs will be available after the new contract is negotiated.
4. Commonwealth capital match funding is projected at a match rate of 30%. The FY 2010 match rate for the majority of the capital projects was a blended rate of 78%. No concrete projections from the Commonwealth are currently available. **This projection will continue to be reviewed over the next several months.**
5. Commonwealth formula funding for operations of \$8.7 million was received in FY 2010. At the present time, \$7.4 million is budgeted in FY 2011 as a placeholder, in light of possible cuts in the Commonwealth budget of up to

15%. **This projection will continue to be reviewed over the next several months.**

6. Fuel expenses of \$5.0 million based on a per gallon cost of \$2.70. Because the cost of fuel also results in an impact to the fuel tax revenue which many of the jurisdictions use as the source of funding for the VRE subsidy, a revised fuel tax projection for the PRTC jurisdictions will be reviewed during the VRE budget process.
7. Continued funding of the VRE capital program, which includes mid-day storage, rolling stock modifications, Broad Run maintenance facility, and \$5.1 million for locomotive procurement. Federal funds are assumed to be 1% higher than the FY 2010 award.

FY 2011 Preliminary Budget Major Revenue and Cost Change	
Revenue increases (decreases) from prior year adopted budget:	
Fare Revenue	1,882,000
Federal Operating Revenue	1,210,000
Federal Capital Revenue	2,786,000
State Revenue (excluding Operating)	914,000
State Operating	(1,707,000)
State Capital	790,000
Subsidy	-
Other	(481,000)
Total	5,394,000
Expense increases (decreases) from prior year adopted budget:	
Fuel	302,000
Amtrak (less access fees)	1,486,000
Operating Reserve/Contingency	350,000
Repairs and Maintenance - Locomotives/Railcars	450,000
Hard Capital Items	3,482,000
Access Fees	565,000
Marketing	467,000
Debt Service	330,000
Other Costs	369,000
Total	7,801,000
Net Increase in Unfunded	2,407,000

Staff continues to explore cost savings. Some of the measures previously enacted are:

- Stricter fare enforcement, which has resulted in increased fare revenue
- Enhanced vendor Metrochek submissions, which improves VRE cash flow
- Installation of wayside power at the VRE yards, which decreases the consumption of diesel fuel
- Cancellation of one round trip train in FY 2006 that provided mid-day service, in response to budgetary issues.
- Installation of a mechanized train washing facility to reduce ongoing operating costs for exterior maintenance
- Review of cell phone plans leading to a reduction in communication costs
- A line item review of all programs and contracts to determine where costs can be reduced
- Other savings to administrative line items, such as reductions in mailing, reduced copying costs and increased electronic communication

Cost savings which staff will be exploring in the future include:

- A moratorium on the use of earmarks if required local match is not available from other sources
- Installation of air compressors at train yards to further reduce locomotive idling
- Termination of parking leases that are subject to annual appropriation
- Reduction in the level of train service

FISCAL IMPACT – FY 2011 BUDGET:

The current budget shortfall is estimated at \$2.4 million. Additional draft budgets will be formulated during the fall and reviewed with the CAO Budget Task Force resulting in a balanced budget by November 2009.

Attached are the following:

- FY 2011 Sources and Use
- FY 2011 Summary Budget

TO: CHAIRMAN ZIMMERMAN AND THE VRE OPERATIONS BOARD
FROM: DALE ZEHNER
DATE: AUGUST 21, 2009
RE: REFERRAL OF PRELIMINARY FY 2011 VRE OPERATING AND CAPITAL BUDGET TO THE COMMISSIONS

**RESOLUTION
9E-08-2009
OF THE
VIRGINIA RAILWAY EXPRESS
BOARD OF DIRECTORS**

WHEREAS, the VRE Master Agreement requires that the Commissions be presented with a preliminary fiscal year budget for their consideration at their respective September meetings prior to the commencement of the subject fiscal year; and,

WHEREAS, the VRE Chief Executive Officer has provided the VRE Operations Board with the preliminary FY 2011 Operating and Capital Budget; and,

WHEREAS, staff recommends a budget built on an average daily ridership of 16,864 average daily riders; and,

WHEREAS, subject to the direction provided by the Operations Board, the budget will be updated with additional ridership and cost data and further refined through the CAO Budget Task Force review during the fall of 2009; and,

NOW, THEREFORE, BE IT RESOLVED THAT, the VRE Operations Board refers the preliminary FY 2011 VRE Operating and Capital Budget to the Commissions for their consideration; and,

BE IT FURTHER RESOLVED THAT, the VRE Operations Board recommends that the budget be forwarded to the jurisdictions for further formal review and comment; and,

BE IT FURTHER RESOLVED THAT, VRE staff is directed to consider and address comments by the jurisdictions and to forward a final recommended budget to the VRE Operations Board at the December 2009 meeting for consideration and referral to the Commissions for adoption in January 2010.