To: Chairman Smedberg and the VRE Operations Board

From: Doug Allen

Date: June 16, 2017

Re: FY 2019 Key Budget Issues

Recommendation:

The VRE Operations Board is being asked to provide feedback and direction for the development of the FY 2019 Budget and Capital Improvement Program (CIP).

Background:

VRE has adopted a financial planning process that provides for early consideration of key budget issues and assumptions. During the budget cycle, VRE staff meets monthly with the member jurisdictions’ Chief Administrative Officers (CAO) Budget Taskforce to develop the annual proposed budget and an independent CAO recommendation is provided to the Operations Board and Commissions in conjunction with the final budget submission at the December Operations Board meeting. In addition, the Capital Committee reviews major capital needs and issues for referral to the full Operations Board as required. The Committee met in May to review the Key Issues related to the capital program.

In accordance with the VRE Master Agreement, a consolidated financial projection over a six-year time frame is provided each year as a component of the annual budget. In 2016, a Financial Plan was developed to forecast the cost of current operations and various growth scenarios through FY 2040, the period covered by the VRE System Plan. The Financial Plan established that even to maintain the current level of service, VRE requires substantial operating and capital funding that cannot be met with currently identified funding sources, ranging from a gap of $40M to $65M depending on if VRE were to maintain service, enhance the system capacity to meet the future growth in the region, or implement the full System Plan. (The Financial Plan projections are currently being updated to include revised ridership and funding projections and to incorporate a modified System Plan service profile, which may alter the estimated unfunded need.)

These funding gaps over a long-term horizon will also be apparent in the FY 2019 operating and capital budget and the FY 2019 – FY 2024 six-year forecast and CIP.
VRE’s *Financial and Debt Principles* addresses the prioritization of projects within the Capital Improvement Program and states:

*Projects included in VRE’s Capital Improvement Program will be prioritized with emphasis on regulatory requirements, the maintenance of equipment and facilities to support current service levels, and provisions for passenger safety.*

Included in these priorities is the required replacement of the Ivy City midday storage facility, a prerequisite for continuing to provide the current level of service, as further described below. In addition to these first level priorities, the CIP decision-making emphasizes the commitment to ensure the development of the railroad infrastructure in the CSXT territory; project readiness; funding availability; and the identification of funding to complete projects with some but not total funding.

**Proposed FY 2019 Key Issues**

**Key Issue #1: State funding beyond FY 2018:** Changes to the level of and allocation method for state transit funds will exacerbate VRE’s capital and operating funding challenges.

The FY 2018 to FY 2023 CIP and Six-Year Financial Forecast illustrated the funding challenges VRE faces, since currently identified funding falls short of the system’s operating and capital needs. One major factor is the uncertainty of available levels of future state funding for capital needs, which is expected to drop off sharply in FY 2019 and FY 2020 when bond funding supporting the state contribution to capital projects is no longer available. VRE’s FY 2018 Budget was based on $10.6M of state transit capital funds used as match for federal formula funds and an additional $5.7M to support track access fees, based on a “tiered” percentage funding system that has been in place since FY 2014.

The Transit Capital Revenue Advisory Board (RAB) was created to identify possible sources of replacement revenue and to develop a methodology for project prioritization, with technical support provided by the Transit Service Delivery Advisory Committee (TSDAC). *The current proposals to develop a statewide prioritization process for the allocation of state capital funds for state of good repair projects will mean VRE cannot depend on consistent state support for our highest priority projects and could well have significant difficulties in meeting federal grant match requirements.*

In the draft Rail and Public Transportation Improvement Program to be presented to the Commonwealth Transportation Board (CTB) in June 2017, the total level of operating assistance is projected to hold steady through FY 2021 and increase slightly beginning in FY 2022. However, the expansion of WMATA’s Silver Line (Phase II scheduled to open in 2020) will materially impact the amount received by VRE and other transit providers in future years.

**Key Issue #2: Jurisdictional subsidy and fare increases:** The VRE service currently must be supported within the confines of jurisdictional budget constraints and a competitive and equitable fare structure. Although additional ongoing dedicated funding sources to support
both the operating and capital needs of the commuter rail service are needed, fare and subsidy levels must also be routinely increased to at least partially accommodate ongoing contractual increases.

The FY 2018 six-year financial forecast projected a subsidy increase of 3% for FY 2019. The jurisdictional subsidy amount was last increased by 5% in FY 2017 to approximately the total subsidy amount paid in FY 2009. With the decreased gasoline costs over the last two years, several of the jurisdictions who were exclusively relying on the fuel tax to pay the VRE subsidy are no longer able to do so.

VRE has had four fare increases in the last six fiscal years (FY 2013, FY 2014, FY 2016 and FY 2018) in order to maintain the current level of service at a reasonable cost to the rider. The FY 2018 six-year financial forecast projected no fare increase in FY 2019.

**Key Issue #3: Level of service**: Some trains are currently at or over 100% capacity. Planned service improvements include the lengthening of peak trains as additional rail cars are received.

Five rail cars were ordered in FY 2015 and placed in service in FY 2017. An additional nine rail cars ordered in FY 2016 are expected to be received in FY 2018. These additional rail cars along with infrastructure improvements to stations and storage yards will allow for the lengthening of existing peak trains. The Smart Scale grant provided funding for additional rail cars in the latter year of the FY 2019 to FY 2024 CIP to further lengthen existing peak trains.

**Key Issue #4: Capital costs at Washington Union Terminal (WUT)**: VRE’s future required contribution to capital investments at WUT is dependent on the cost sharing mechanism being developed by the Northeast Corridor Commission.

The FY 2018 to FY 2023 CIP included $45M to fund track, signal, platform and passenger facility upgrades and re-alignments at Washington Union Terminal (WUT). Some of these funds will be used for interim improvements at the terminal, as agreed to between Amtrak and VRE. The more significant costs will be the result of the allocation of infrastructure improvements to all users of the terminal based on a formula that is currently being developed by the Northeast Corridor (NEC) Commission. At this time, we do not know whether the amount programmed is higher or lower than the amount that will be required. More specific information should be available over the next several months so this potential cost can be better quantified.

The NEC Commission was created under a provision of the Passenger Rail Investment and Improvement Act of 2008 (PRIIA) in order to develop consistent methodologies for the equitable sharing of operating costs and infrastructure investments within the Northeast Corridor for commuter and intercity rail services. The Commission is comprised of members from each of the NEC states, Amtrak and the U.S. DOT with non-voting representatives from freight railroads and states, such as Virginia, which connect to the
NEC. The Commission approved a cost allocation policy for operating costs in September 2015; for VRE this policy now determines the cost of our access to WUT. The Northeast Corridor Capital Investment Plan for Fiscal Years to 2018 to 2022 outlines $38B of backlog or improvement projects needed to support the Corridor. The Commission is currently working on a method for allocating these capital costs to the users of NEC assets.

**Key Issue #5: Maintenance and Replacement of VRE Assets:** The maintenance of rolling stock equipment and facilities to support current service levels is a priority in the VRE capital program. Federal formula funds devoted to maintaining transit assets in a “State of Good Repair” are expected to provide for these costs over the life-cycle of VRE’s assets. However, replacement of the fleet at the end of the expected useful life of the equipment will require additional funding mechanisms.

The federal priority of maintaining transit systems in a “State of Good Repair” has been continued in the Fixing America’s Surface Transportation (or FAST) Act, the current federal transportation authorization, and the funds to adequately maintain equipment and facilities will be available from this source. VRE’s ongoing transit asset management initiatives will be used to refine the costs that were included in the prior year budget and CIP for related projects.

VRE’s current fleet of railcars and locomotives were purchased during a compressed time period. As a result, the replacement of the fleet at the end of its useful life is projected to be needed during a five-year period beginning in FY 2030, at an estimated cost of approximately $450M. Although this need falls well beyond the projection period in the annual budget and CIP, this issue was highlighted in the longer-term Financial Plan forecast.

**Key Issue #6: Midday Storage:** The construction of alternate midday storage facilities will require a significant funding commitment over the next several years.

The current agreement with Amtrak includes provisions for Amtrak to reclaim VRE’s midday storage space at the Ivy City yard for their own use during the next several years. As a result, VRE must proceed expeditiously to replace the storage yard now used at Ivy City. Work done on the project thus far indicates it will require a substantial portion of available federal formula funds over the term of the FY 2019 to FY 2024 CIP and may require the identification of other funding sources or short-term bridge financing until additional federal funds are available.

In addition to the replacement of the current storage tracks, VRE needs to increase midday train storage beyond what is currently available in order to provide for storage of all existing trains. This will be accomplished with the completion of storage tracks north and south of the L’Enfant station during FY 2018.

The new storage yard is expected to have the capacity to accommodate future growth as well as replace the current storage slots.
Key Issue #7: Resources needed to implement the capital program: Capital improvements needed to support the current level of VRE service, to increase railroad infrastructure capacity in the VRE service territory or to grow the system to meet future expected demand require the identification and commitment of funds beyond those currently available to VRE.

Each of the existing sources of capital funding VRE relies on has inherent limitations. Federal funding has increased considerably over the last several years, but the limitations on the use of our major source of federal funds, the 5337 or State of Good Repair program, will further complicate our capital funding picture. NVTA regional funding continues to be available on a discretionary basis for certain VRE capital projects, but only for those located within the NVTA jurisdictions, which has created an imbalance of funding sources within VRE. Local sources of funding are limited and must compete with other jurisdictional funding priorities. The limitations of state funding are noted above.

VRE was recently approved for Smart Scale funding for $92M in FY 2022 dollars. While this funding fills a crucial funding gap for numerous VRE projects at the construction phase, it creates a funding lag as these projects are scheduled to start earlier than when the funds will be available in FY 2022.

Key Issue #8: VRE staff level: VRE needs the staff resources necessary to operate and administer the commuter rail system safely, efficiently and in compliance with all federal and state requirements and to advance the capital program in accordance with system needs and funding commitments.

Since inception, the administration and oversight of the commuter rail system has been accomplished by a relatively small permanent staff, supplemented at times with assistance on a contract or temporary basis. For a number of years, as the system itself grew and developed, along with a continuing increase in internal and external requirements, the staff level did not keep pace. However, three new permanent positions and the replacement of three contract positions with VRE staff positions was funded in FY 2016 and an additional four new full time positions were funded in FY 2017. VRE management is currently reviewing existing staffing resources and potential needs for FY 2018, particularly in regard to resources needed to advance the capital program.

Key Issue #9: Renewal of CSX operating access agreement: The VRE five-year operating access agreement with CSX Transportation expired on June 30, 2016. In May 2016, the VRE Operations Board approved a one-year extension of this agreement through June 30, 2017 and a second one-year extension was approved in May 2017, through June 30, 2018.

Throughout this second one-year extension period, VRE, CSXT and DRPT will meet to determine capacity enhancement projects, prioritize these projects, establish methodologies to identify how the capacity enhancements will result in additional service for VRE and to identify potential funding sources. VRE staff anticipates these elements will
be integrated into the new Amended and Restated Agreement. The potential fiscal impact will be monitored throughout the FY 2019 budget process and reflected as appropriate.

**Next Steps:**

- Continuation of discussion of FY 2019 budget and CIP with the CAO Budget Task Force.
- Provision of preliminary budget and CIP to the Operations Board in September 2017 and to the Commissions in October 2017.

**Fiscal Impact:**

The fiscal impact of the FY 2019 budget and capital program will be addressed at the September Operations Board meeting.
Virginia Railway Express
Operations Board

Resolution
8A-06-2017

FY 2019 Key Budget Issues

WHEREAS, financial planning for the Virginia Railway Express is based on a set of budget issues and assumptions discussed by the VRE Operations Board prior to the development of the annual operating and capital budget; and,

WHEREAS, the VRE Operations Board has directed that the development of each annual budget involve consultation and cooperation with the Chief Administrative Officers (CAO) Budget Taskforce established by VRE’s participating and contributing jurisdictions; and,

WHEREAS, budget issues and assumptions for the development of the FY 2019 operating and capital budget were reviewed by the CAO Budget Taskforce prior to their presentation to the Operations Board; and,

WHEREAS, the Key Issues related to the CIP were reviewed by the Capital Committee prior to their presentation to the Operations Board;

NOW, THEREFORE, BE IT RESOLVED THAT, the VRE Operations Board directs VRE staff to develop the FY 2019 Budget and CIP in accordance with the Board’s direction.

Approved this 16th day of June 2017

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Paul Smedberg
Chairman

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Katie Cristol
Secretary