BUDGET AND RESERVE POLICY
BOARD OF DIRECTORS
APRIL 15, 2020

OVERVIEW

- Budget impacts of the failure of Measure I
- Setting a minimum reserve policy
- The financial impact of the COVID-19 shut-downs
- Budget timetable and process

BUDGET OUTLOOK FOLLOWING ELECTION

- Measure I would have allowed refinancing of debt for construction of the SMART system
- Average reduction of $12 million per year in debt service cannot be achieved
- Long-term stability will require expenditure reductions of $9 million as shown during the strategic planning process in 2019

BUDGET OUTLOOK FOLLOWING ELECTION

- Budget problem identified in 2019, IF NOTHING CHANGES:

	CURRENT YR	PROJECTIONS		
	2019-20	**2020-21**	**2021-22**	**2022-23**
Operations Revenue	$51.0	$56.5	$54.1	$55.5
Operations Expense	-$41.3	-$43.2	-$44.5	-$45.8
Debt Service	-$16.7	-$17.4	-$18.1	-$18.7
Capital Expenses Not Covered by Grants	-$12.2	-$0.3	$0.0	$0.0
Subtotal (Needs Reserves/Annual Deficit)	-$19.2	-$4.4	-$8.5	-$9.0
Starting Unrestricted Reserves	$26.5	$7.3	$2.9	$0.0
Ending Unrestricted Reserves/Cumulative Deficit	**$7.3**	**$2.9**	**-$5.5**	**-$9.0**
Agency Reserve	**$17.0**	**$17.0**	**$11.5**	**$2.5**
			Dimishing Reserves	

- Original budget challenge to reduce expenditures, original estimates to address would have meant $3 million in reductions in EACH of the next three Fiscal Years
- Total of $9 million in reductions would have solved for future imbalance that would have eliminated reserves if nothing were done.

REFINANCING AS COST SAVING STRATEGY

- Without Measure I and additional years to spread the construction debt, the significant $12 million per year reduction in debt service we had hoped to achieve **cannot** be realized.
- Prior to 2020 we did not project significant benefits to refinancing within the existing bond term because rates were much higher.
- Decline in interest rates in recent weeks, potential for opportunities to refinance the outstanding Measure Q Sales Tax Revenue Bonds to generate some debt service savings does exist
- In conjunction with SMART's expert Municipal Advisor, PFM Financial Advisors LLC, we are monitoring the municipal bond market for an opportunity to lower our payments.

REFINANCING AS COST SAVING STRATEGY

- Using rates that existed on April 3, a taxable advance refunding could generate between **$1.1 and $2.5 million** of annual cashflow savings through FY2029 depending on the structure, terms and other factors.   This is far below the $12 million Measure I sought to achieve.
- A number of things could affect that pricing, including the willingness of investors to participate, a change in rates or credit ratings, and continued economic uncertainty, along with the ability to call the bonds earlier than 2029.
- We are evaluating two structures:
  - A negotiated public offering
  - A "private" or direct placement of debt
- Public Offering
  - Longer process that might result in no savings to SMART due to the time involved, volatility in the market, credit process and other factor.
- A Direct Placement
  - Approved by the Board
  - Places debt directly with a financing entity
  - Saves time, allowing us to capture potential savings before they disappear

MINIMUM RESERVES

- Currently benefitting from our reserves which allow us time to address the fiscal crises
- Reserve policies adopted by other entities are as follows:

Agency	Published Reserve Policy
City of Santa Rosa	15-17% of Annual Expenditures
City of San Rafael	10% of Annual Expense
City of Novato	15% of Annual Expense
County of Sonoma	8.3% of Annual Revenues (One Month)
County of Marin	5% of Annual Expense
Golden Gate BH&TD	7.5% Annual Operations, 3.5% Emergency
SF MTA (Muni)	10% Annual Operating Expenses
Utah Transit	9.33% of Annual Expense
Trimet, Portland	2.5 Months Operating Expense (21%)
VTA (Santa Clara)	15% of Expense, Sales Tax stabilization fund $35 M (10%)

- Minimum reserves should be large enough to weather a TYPICAL financial challenge, without putting too much capital aside that is needed for other operating challenges

MINIMUM RESERVES

- SMART's challenge is to recognize the significant role that sales tax plays in funding our budget.

- We recommend a **minimum** reserve policy that preserves $10 million as your minimum for Fiscal Year 2021 and beyond.

- This calculation is 25% of our Fiscal Year 2020 ongoing operations expenditures (excluding capital project and debt costs). This is **higher** than most entities carry but necessary given the uncertainty we continue to face

- $10 million should be a **minimum** dollar amount despite our plans to reduce expenditures in the coming months

- Further, we recommend that your Board adopt a policy that states the use of SMART's reserve should require a 2/3 vote so that the use of the funds is preserved

NEW BUDGET CHALLENGE: COVID-19

- The COVID-19 shelter-in-place order presents a giant new challenge
  - Loss of Fare revenue immediate $90,000
  - Staff vacancies, new leave mandates (unfunded)
  - Unknown but significant sales tax revenue impacts

- Challenge of anticipating sales tax impact when receipts lag 2-4 months behind transactions

- Further challenge of anticipating impacts of Governor's order allowing businesses 90-day extensions, and, in some cases, up to 1 year to submit their tax receipts
  - Small businesses (with taxable sales of $5 million or less) can defer remittance of their sales and use taxes for up to one year to July 2021.
  - Approximately 360,000 filers will be eligible for deferral of up to $50,000 in what is essentially an interest-free loan from state and local agencies.

NEW BUDGET CHALLENGE

- Our initial projection:
  - Loss of 20% sales tax related revenue in Fiscal Year 2019-20 which ends in June.
  - Loss of 30% in budgeted fare revenue for Fiscal Year 2019-20.
- Total losses of $11 million in Fiscal Year 2019-20 as shown in red

FISCAL YEAR 2019-20 IMPACTS OF SHELTER-IN-PLACE			
Measure Q - Sales Tax			
	Original	$	39,312,541.0
	Revised		31,450,033
	(loss)		(7,862,508)
State Rail/Transit Funding			
	Original State		7,786,239
	Revised State		6,228,991
	(loss)		(1,557,248)
Fare Revenue			
	Original		4,137,000
	Revised		2,482,200
	(loss)		(1,654,800)
Total Loss (Projection)		$	(11,074,556)

“CARES” ACT RELIEF

Coronavirus Aid, Relief, and Economic Security (CARES) Act

- CARES Act provided $25 billion to public transportation systems
- $1.3 Billion to the Bay Area
- Funds have been allocated for the **specific use of maintaining transit staff and a reasonable level of service** by backfilling for both the loss of revenues and the reimbursement for expenses as a direct result of COVID-19.
- 27 Bay Area General Managers and Metropolitan Transportation Commission (MTC) Executive staff have been negotiating since Congress settled on an amount
- Subject to MTC approval on April 22 and then Federal Transit Agency (FTA) grant approval
- SMART’s initial allocation is estimated to be $10 million
- May be additional funds forthcoming in the coming months as only 60% of the funds are being proposed to be allocated at this time.

“CARES” ACT RELIEF

Initial $10 million grant will partially address our estimated **Fiscal Year 2019-20** loss.

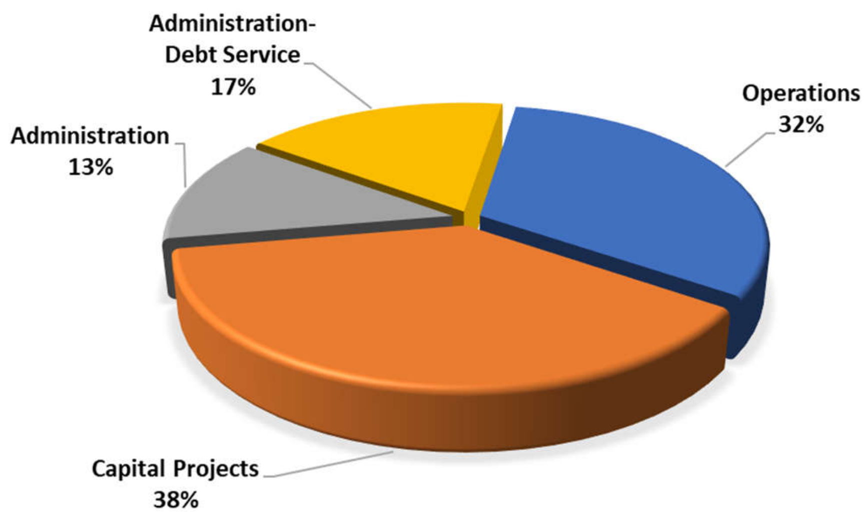
However, impacts to SMART likely to continue--

- Rosy scenario:
  - Short-lived impact with quick revenue recovery
  - Unlikely given the broad economic shock we are experiencing
- More likely scenario:
  - Could take a year or more for sales tax to return to pre-COVID-19 levels.

- In the likely scenario: Preparing for second impact of an $11-14 million loss in Fiscal Year 2020-21 beginning July 1.
- A second negotiation with the Bay Area transit operators over remaining CARES Act allocations would assist with this impact
- Recovery likely to take much longer and impacts could be much higher.

BUDGET COMPOSITION

Budget Composed of Three Different Parts: Capital+Administration+Operations

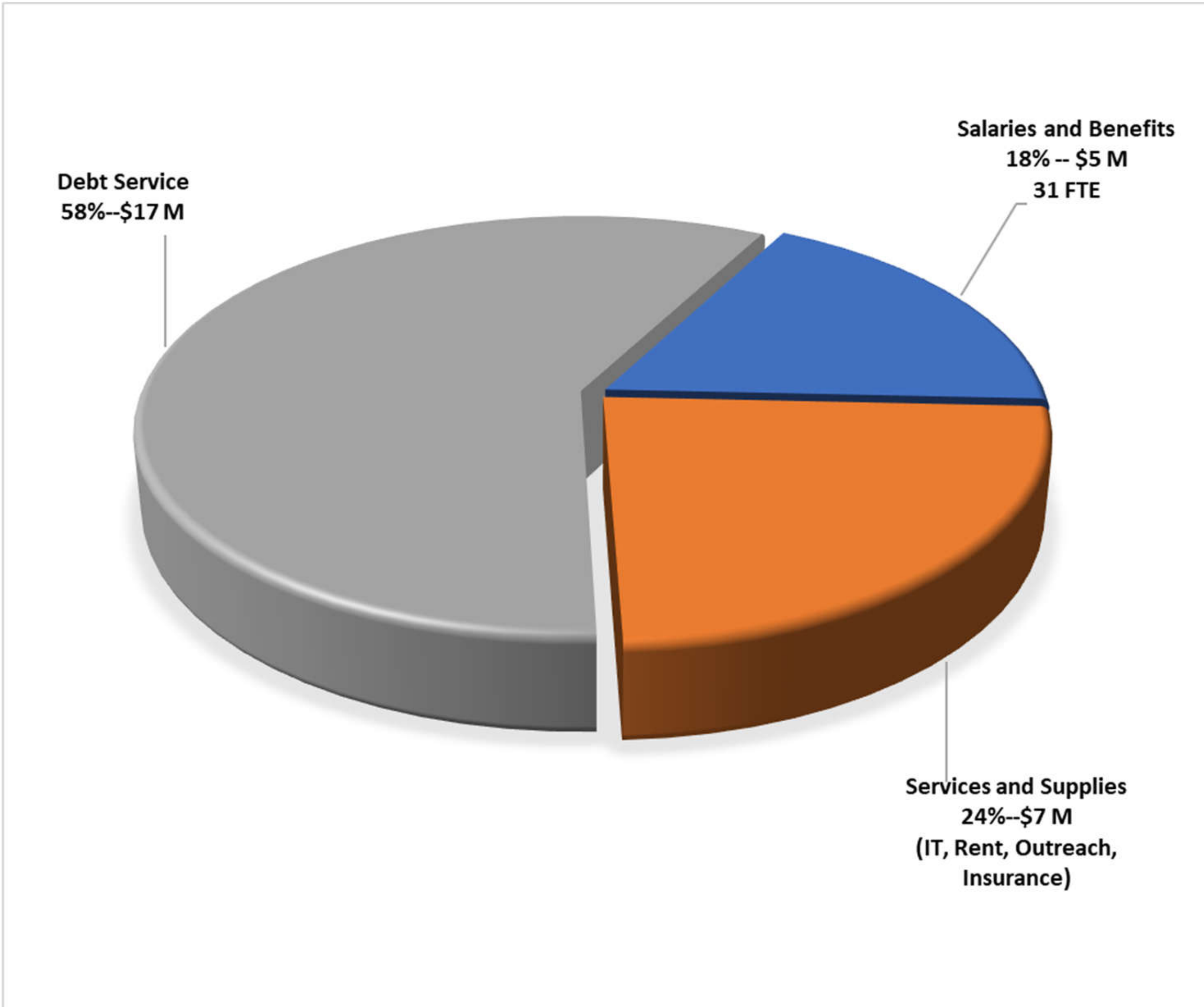


CAPITAL BUDGET

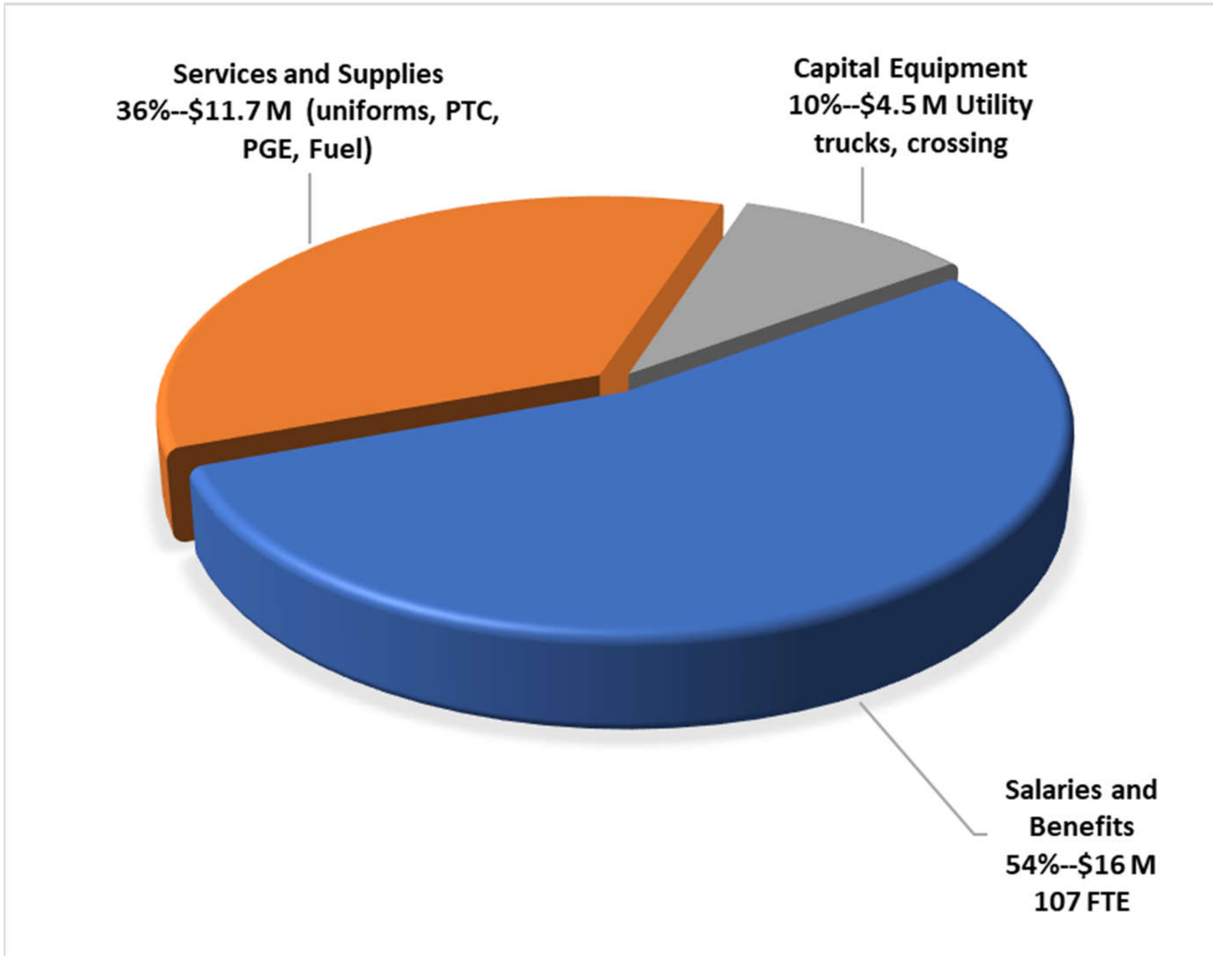
- FY 2019-20 current budget of $51 million
- Almost entirely grant funded, one time in nature
- Reductions will not significantly impact operating imbalance

ADMINISTRATION EXPENSES FY 2019-20

$29 MILLION



OPERATIONS EXPENSES FY 2019-20
$32 MILLION



NEW BUDGET CHALLENGE

First Challenge: Measure I failure eliminating significant debt service relief

Second Challenge: Predicting and absorbing sales tax losses until the economy recovers

- Originally planned to close the Fiscal Year with significant reserves, which allow us some cushion but will be quickly depleted without significant revenue and expenditure changes.
- Prior target of $3 million for Fiscal Year 2021 now increased
- Now looking for **targeted reductions of up to $6 million**
- $6 million chosen as an aggressive but potentially achievable amount in the coming year
- The sooner we can find reductions and implement them, the quicker we will be able to address both the immediate revenue crises and long-term structural problem.

NEW BUDGET CHALLENGE

- Three major strategies for budget reduction proposals for FY 2020-21.
  - » **One-time savings**
  - » **Reduction in Ongoing Expense, Salary and Non-salary**
  - » **Reduction in Ongoing Expense Due to Reductions in Service**

1. One-time savings

Expenditure reductions for planned items that will now be deferred, such as:

- » Deferral of machinery and equipment
- » Extended replacement cycles for vehicles
- » Deferral of mitigation measures and enhancements
- » Deferral of non-safety capital projects and matching funds

NEW BUDGET CHALLENGE

2: **Reduction in Ongoing Expense, Salary and Non-salary**:

Important but could be considered for reductions without a direct impact on the SMART train schedule. Items such as:

- » Train WiFi service
- » Information Technology upgrades and servicing
- » Customer service contract with Golden Gate Bridge District
- » Debt refinancing
- » Federal and state advocacy services
- » Communications/outreach contracts and activities
- » North County bus service
- » Elimination of non-critical vacant positions
- » Discussing with our unions various means of reducing labor costs, including a possible wage reopener for the current July 1 increases.

NEW BUDGET CHALLENGE

3: Reduction in Ongoing Expense Due to Reductions in Service: Such as

» Running fewer trains

Fewer trains would mean a decrease full-time staff and related expenses

Fewer trains would mean reductions in fuel, materials, other services

» There is a potential for loss in either direct fare revenue or related revenue from State and Federal sources and the savings would be reduced by these losses.

» Could impact our ability to compete for service expansion grants depending on the severity of the cuts.

NEW BUDGET CHALLENGE

- There will be significant impacts to our riders of reductions that could reach $9 million or more over time.
- There is no way to cushion the impact of such a change from our everyday operations functions. There is no other place to look for reductions.
- Length of time of the economic downturn will impact decision making.
- A larger, more long-lasting economic downturn would mean that this initial $6 million target could be followed by a new effort to reduce expenses shortly thereafter rather than waiting for the next budget cycle.

NEXT STEPS

- **April 15:** Briefing on targets and reduction categories
- **April 21:** Citizens Oversight Committee discussion of budget and refinancing
- **May 6:** Update on budget process and any follow-up from April
- **May 20:** Preliminary Budget Presentation and Discussion
- **June 3:** First opportunity for Board Approval of FY 20-21 Budget
- **June 17:** Final opportunity for Board Approval of FY 20-21 Budget