**Financing Mass Transit in New York:**

# *Basic Principles / Practical Options*

**Submitted by**

**Keep NYC Free**
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**to**

**The Commission on MTA Financing**

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Chairman Ravitch, Members of the Commission:

Keep NYC Free – a coalition of business, labor and civic groups that came together in 2007 to oppose to New York City's proposed congestion pricing system, and to advocate other, more effective approaches to relieving traffic congestion in the City – appreciates having been given an opportunity to submit testimony to the Commission on MTA Financing.

The need to create a sustainable funding structure that will ensure the MTA's continued ability to provide essential transit services is probably more pressing today than at any time during the past 25 years. The challenge is particularly difficult, given the weakness of the national economy – the likely impact of turmoil in the financial services sector on the City's and the region's economy – and the uncertain effects of the capital markets crisis on the MTA's ability to finance its capital program. As New Yorkers, we greatly appreciate the Commission members' willingness to take on this challenge.

The heart of our message to the Commission can be summed up briefly and simply:

- The congestion pricing system that effectively tolled free East River crossings proposed last year by the City, and modified by the Traffic Congestion Mitigation Commission, was seriously flawed – both as a means of raising revenue for mass transit and as a means of relieving congestion;

- There are much better options available to the MTA, the State and the City for financing mass transit – options that will provide much more revenue, and do so more reliably, more efficiently and more equitably, and with fairness.

- New York City and State -- as outlined by the Independent Budget Office -- make up historic underfunding of MTA. Several revenue measures below should apply to making up these shortfalls.

Before identifying sources of financing that we think are far superior, we will first cite some basic principles that we believe should guide the evaluation of any proposals for funding mass transit.

# 1) Financing transit: Some basic principles

The following are some basic principles that the Commission might find useful in evaluating the many options that are available for financing transit infrastructure and services in the New York metropolitan area.

### *1) Allocate costs in proportion to benefits.*

The cost of financing mass transit should be allocated in a way that is roughly proportional to the benefits that various interests derive from the system's existence, and from the services it provides. Broadly speaking, we believe this means that responsibility for financing transit should be allocated among the following groups – and in the following order:

- The nation and state and city in that order as the NYC economy fuels so much of the economy and the transit investment to date from Washington, Albany and City Hall too often appears anything but ignorant of that imperative based on the dollars each invests in transit.
- Those who own property – especially commercial property – in areas served by mass transit;
- All other participants in the City's and the region's economy.
- Motorists, whose access to the core of the region depends on the existence of high-quality mass transit services; and
- Riders, who are the primary beneficiaries of the existence of the system

### *2) Ensure that any proposed sources of revenue for subsidizing mass transit operations or financing capital improvements meet four basic tests.*

In addition to maintaining a rough balance between the cost of supporting the transit system and the benefits it provides, any proposals for increasing (or creating new sources of) dedicated revenue should be judged by several other criteria as well:

- ***Revenue efficiency.*** Any proposals for increasing revenues dedicated to mass transit should seek to minimize both initial implementation and ongoing collection costs as a share of gross revenues – and minimize as well the "compliance costs" born by those who pay – as a share of gross revenues. For every dollar in additional revenues to be collected, the goal should be to maximize the share that actually goes to transit.

- ***Economic efficiency.*** Any increase in taxes or fees dedicated to mass transit will take money from people who live, work, do business in or visit the New York area. But in terms of the damage they can potentially inflict on the City's and the region's economy, not all tax and fee increases are created equal. If new or increased taxes or charges are needed to finance mass transit, the Commission should focus on those that will cause the least damage to the City's and the region's economy.

- ***Stability and predictability.*** Proposals for new streams of revenue (or increases in existing revenue) dedicated to mass transit should be limited to those that are stable and predictable. The existing real property transfer tax, for example, has in good times delivered truckloads of cash to the MTA, reaching a high of $894 million in 2007. But its inherent volatility and unpredictability make it at best a seriously flawed way to fund mass transit. The MTA predicted in July that in 2009 the yield from this tax would fall to $483 million. In today's environment however, no one really knows what the tax will produce in 2009.

- ***Equity***. As it develops proposals for increasing revenues dedicated to mass transit, the Commission should avoid any that would unduly burden low-income or working-class New Yorkers; or unduly favor some communities within the City or the region at the expense of others.

***3) Deal with mass transit in the context of broader transportation needs.***

Important as mass transit may be, it is only one element of the City's and the region's transportation networks. Financing for mass transit should not be addressed in isolation from the financing of other transportation systems in the region. The City and the State also need to focus on the need for investment in highways, bridges, ports, airports, ferries and other facilities as well.

While the Commission's principal focus may be on financing for mass transit, the Governor, the Legislature, the Mayor and will need to address a broader range of transportation needs.

***4) Fund investments needed to keep the system in a state of good repair as part of the system's year-to-year operating requirements.***

Investments needed to keep the system in a state of good repair should be treated financially as what they are in reality – part of the system's ongoing, year-to-year operating requirements. This means they should be financed from the same revenue sources as operations – and to the greatest extent possible, they should be funded on a pay-as-you-go basis.

### *5) Rigorously justify and prioritize new projects.*

Major capital projects – especially those involving addition of new capacity – should have to be justified on the basis of the most rigorous analysis of costs and benefits, and a full exploration of the available alternatives. Moreover, given the reality of severely constrained resources, New York simply cannot afford to finance every project that can be justified in cost-benefit terms. The MTA will thus have to be smart and disciplined in setting priorities among a wide range of potentially worthwhile capital projects.

Especially given the MTA's (and the State's) current financial circumstances, this might seem to be stating the obvious. But the reality is that in recent years the discipline that should have governed the MTA's capital program broke down. As a result, the agency is now struggling to finance completion of several major projects it probably should never have been started without a certain and stable source of revenue.

### *6) Separate financing of major new projects from the funding of operations and major maintenance.*

The MTA should generally segregate streams of revenue that are dedicated to operations, and to keeping the system in a state of good repair, from the financing of major new projects. The goal here is to ensure that basic operations and major maintenance are fully funded, and don't have to compete for scarce resources with higher-visibility, politically more attractive projects.

One of the implications of this principle is that, except in very limited circumstances, the MTA should not borrow against general farebox revenues to finance major projects that benefit only limited numbers of riders.

### *7) Don't start construction of projects you don't have the money to finish.*

Finally, the MTA should never start construction of a major, multi-year capital project without having reliable commitments in place for funding its completion. Again, this might seem obvious – but it is a principle that public officials, here and elsewhere, have all too often found it politically expedient to ignore.

# 2) Practical Measures that provide additional financing for Mass Transit

While Keep NYC Free does not claim to have a comprehensive solution to the problem of financing mass transit, we believe there are options available to the Commission, the City and the State that are clearly superior to the congestion pricing system proposed last year by the City.

### *1) Property tax surcharge*

Given the benefits that property-owners (especially owners of commercial property) derive from the existence of the transit system, it is more than reasonable to ask them to be part of the solution to the problem of transit financing. In fiscal year 2008, a 5% surcharge on taxes paid on Class 4 (commercial and industrial) properties in New York City would have yielded approximately $295 million, with Manhattan properties accounting for about 74% of the total. (A similar surcharge applied to Class 2 properties (multifamily housing) would have generated about $261 million

Alternatively a surcharge within 3/8 mile of a subway or rail station, on Class two and four properties valued over $5 million (with this level indexed to inflation), would raise $100 million each year.

Finally, a 5% surcharge over the first ten years of completed new construction in excess of $10 million (with this level indexed to inflation) with 3/8 of a mile of new transit projects values in excess of $200 million (with this level indexed to inflation), would raise $85 million annually and should be applied to reduce the cost of capital borrowing for the projects.

While these surcharges would add to the cost of doing business in New York City, the costs that serious deterioration in the quality and reliability of transit service would impose on commercial property owners and their tenants could prove to be far greater.

### *2) Non-resident income tax*

Residents of the suburbs (both in New York and other states) who work in New York City benefit from the existence of MTA rail and New York City transit services, even if they are not regular users of those services.

Commuters have not been subject to City income taxes since 1999, when the Legislature repealed the City’s commuter tax. In February 2008, the New York City Independent Budget Office estimated that if the tax were in place in fiscal year 2009 at the same rates that had applied before 1999 (0.45% on wage and salary income, 0.65% on income from self-employment), it would produce $713 million in revenue for the City, rising to $835 million in 2012.

While projected revenues would now be somewhat lower – in particular as a result of the upheaval in financial services – the additional revenues the City would gain from this non-resident income tax would nevertheless be substantial. Our proposal would double the tax rates and the projected revenues.

Obtaining legislative approval would, of course, be no easy task. Dedicating all or part of the proceeds to operations, maintenance and improvement of New York City transit, commuter rail and other regional transportation infrastructure might help overcome resistance to the tax. As a further step, the Legislature could consider dedicating taxes paid by residents of other counties (Nassau, Suffolk and Westchester, for example) to finance transportation projects in those counties, while taxes paid by non-New York State residents would be dedicated to financing the New York City transit system,

### *3) An increase in the state motor fuel tax to fund highway, bridge and transit needs*

New York imposes several different taxes on the sale of gasoline and other motor vehicle fuels, including state sales and excise taxes, the petroleum business tax, and several other levies, which together averaged about 44 cents per gallon. One of these taxes – the 8 cents per-gallon motor vehicle fuel excise tax – generated about $511 million in State revenues in fiscal year 2008.

Even after taking into account recent declines in fuel consumption, increasing the motor vehicle fuel excise tax by 4 cents – less than a 10% increase in total state taxes on gasoline and other fuels – could generate approximately $250 million in additional revenues. All of this additional revenue could be dedicated to maintaining and improving the state's transportation infrastructure.

### *4) Increase existing bridge and tunnel tolls*

The MTA could also increase motorists' contribution to financing mass transit and other transportation infrastructure in the New York metropolitan area through a further increase in bridge and tunnel tolls. We estimate that increasing one-way tolls on the Queens-Midtown and Brooklyn-Battery Tunnels, and on the Triborough, Henry Hudson, Whitestone, Throgs Neck, and Verrazano bridges by an average of 50 cents, and the tolls on the Marine Parkway and Cross Bay bridges by 25 cents, would yield about $147 million in additional revenue for the MTA, which could be dedicated both to sustaining the region's transit and commuter rail networks, and to maintaining highway and bridge infrastructure.

### *5) Revenue from higher fines, parking fees and street closing fees*

Last year, Keep NYC Free proposed several measures the City could adopt that we believe would be much more effective than the City's proposed congestion pricing system in addressing the real causes of traffic congestion in the Manhattan central business district.

While the principal focus of these alternatives was on reducing congestion rather than financing mass transit, several of them would also generate significant new revenues for the City. We estimate, for example, that:

- Substantially increasing the price of on-street parking in the CBD, and expanding the City's muni-meter system to cover several thousand on-street parking spaces that are not currently metered, could yield $50 million or more in additional parking revenues.

- Sharply increasing fines for the types of parking violations that contribute most to traffic congestion in the CBD – for example, increasing the fine for parking in a bus lane from $115 to $250 – could yield $75 million or more in additional revenue.

- Stricter regulation, including appropriate fees and penalties, for the use of street space by construction contractors and utilities – currently as little as $50 for three months. The fee should be monthly and range from $100 to $1,000 and could raise in excess of $500 million.

The City could consider dedicating these revenues to measures that would help alleviate congestion, such as upgrading traffic signals at key intersections or expanding the number of taxi stands in the CBD; or that would expand the range of transit options available to New Yorkers, such as new ferry and bus rapid transit services, or to finance an increase in its funding for mass transit to address the shortfalls identified by the Independent Budget Office.

### 6) *Increase vehicle registration fees.*

A $50 registration fee increase would raise $250 million according to the RPA and would enable the state to finance an increase in its funding for mass transit to address the shortfalls identified by the Independent Budget Office.

### 7) *Increased use of "project-based financing" to fund mass transit capital improvements that increase the value of real estate in proximity to the project.*

*Project-based financing* involves capturing the added property values that result from the construction of a major transit improvement. The planned extension of the 7 train through the Hudson Yards area is unique among the MTA's major capital projects in terms of its reliance on project-related financing – in this case, using payments in lieu of taxes from the Hudson Yards district to support bonds issued to finance the extension.

While the project currently faces an uncertain future, due to increases in costs and continuing uncertainties in the real estate market, the original concept of having the property-owners and developers who would benefit most from extension of the 7 line participate in its financing was sound.

The City, the State and the MTA should explore how that concept might usefully be applied to other projects. It will be important to ensure, however, that property-owners' and developers' contributions reflect the value that transit improvements add to their projects, rather than simply a diversion of funds that would otherwise have been owed the City in real property taxes.

### *8) Institute a modest broadbased regional payroll tax.*

A regional payroll fee – 0.25% rate in MTA counties would raise $600 million.0.5% excluding incomes below $50k would realize $400 million; and 1% excluding incomes below $50k, generates $800 million (RPA). 0.333% across the board would realize $1 billion (CM Fidler).

### *9) Institute a Regional Sales Tax*

An additional sales charge 1 /4% increase would raise $200 annually (RPA)

### *10) Enlisting the Private Sector*

Look at using the private sector to finance, design, build and operate major transportation projects (consistent with prevailing wages) and free any tax levy and federal assistance funding for transit needs better suited for tax levy and federal aid.

### *11) Increasing transit fares*

Finally, the MTA, the City, the State and the riding public all need to start acknowledging the reality that transit and commuter rail fares will have to rise with regularity based on normal system cost increases, in order to meet the cost of operating and maintaining these systems. There should be agreement that the fare cover a set proportion of system operations and annual reviews should indicate whether cost increases occur and thus automatically trigger an increase.

Despite the political sensitivity of this topic, the case for increasing fares is compelling. Because of the impact of various MetroCard pricing plans, and discounts provided to various groups of riders, MTA NYC Transit's actual fare revenue per bus and subway rider in 2008 averages only about $1.25. Since 2003, average fare revenue per rider has declined in real terms (that is, after adjusting for inflation) by 6%.

An increase – one time – of subway, bus and commuter rail fares by an average of 12.5% – an average of about 16 cents per ride for subway and bus passengers – would, even after taking into account a modest decline in ridership in response to higher fares, realize additional 2009 farebox revenues of approximately $500 million. Thereafter regular increase would follow the formula outlined above.

The table below summarizes the revenues that could potentially be generated from the sources described above.

## Potential new revenues for mass transit: selected examples

| Annual Revenue Options to fund Mass Transit | Potential annual revenue ($ millions) |
|---|---:|
| 5% surcharge on Class 4 real property tax in NYC | $295 |
| 5% surcharge on Class 2 real property tax in NYC | $261 |
| 5% surcharge on Class 2 and 4 property valued over $5 million within 3/8 mile of transit improvement | $100 |
| 5% surcharge on new construction over $10 million within 3/8 mile of transit improvements | $85 |
| Non-resident income tax at double pre-1998 rates | $1,800 |
| Increase state motor fuel tax by 4 cents/gallon | $250 |
| Increase MTA bridge and tunnel tolls by 50 cents each way | $147 |
| Increase on-street parking fees, fines for parking illegally in the Manhattan central business district | $125 |
| Increase Street Closing | $500 |
| Increased Registration Fees | $250 |
| Project-based financing of major new MTA capital projects | $200 |
| Regional Payroll Tax (various options) | $400 to $1,000 |
| Regional Sales Tax | $100 |
| Enlisting the Private Sector | $75 |
| Increase transit and commuter rail fares in 2009 by an average of 12.5% | $500 |
| TOTAL | $5,088 to $5,688 |

As the preceding examples illustrate, there are many ways to increase revenues dedicated to meeting New York's mass transit that from the perspective of revenue efficiency are far superior to the congestion pricing scheme proposed by the City and modified by the Traffic Congestion Mitigation Commission.

Through some combination of these (and perhaps other) options, the City and the State can create a financing structure that meets the operating, maintenance and capital needs of the City's and the region's transit systems – and that broadly and equitably spreads responsibility for supporting these systems among riders, motorists, property owners and others who benefit from their existence. And we can do so without resorting to an inefficient, inequitable and economically counterproductive congestion pricing scheme.

# 3) Congestion Pricing Doesn't Work As A Viable Funding Resource for Mass Transit

Viewed against the background of the principles and criteria outlined above, it is clear that as a means of raising new revenue for mass transit, the congestion pricing system proposed last year by the City, and modified by the Traffic Congestion Mitigation, is deeply – and probably irreparably – flawed.

- ***Revenue inefficiency***

In terms of revenue efficiency, the proposed congestion pricing system is clearly the least efficient of the major options under discussion. It would be costly to implement and to operate. And by causing a shift of 83,000 riders per day from private automobiles to mass transit, it would impose \$767 million in otherwise unnecessary capital costs on the MTA, and increase its annual deficit by \$103 million.

After taking into account its capital and operating costs and the additional costs imposed on the MTA, we estimate that of the \$462 million in gross revenues that the congestion pricing scheme proposed by the Traffic Commission Mitigation Commission would generate, only about \$228 million – only 49 cents of every dollar collected – would actually be available to fund transit operations or capital improvements.

In terms of revenue efficiency, the performance of the proposed congestion pricing system is in fact so poor that this criterion alone should be sufficient to disqualify it from serious consideration by the Commission on MTA Financing. This is not, however, the congestion pricing scheme's only weakness.

- ***Risking damage to the City's economy***

As we noted previously, any new or increased taxes or fees charged to those who live, work, do business in or visit New York City impose real costs on the City's economy. If increased taxes or fees are ultimately needed to support mass transit, it is thus essential – especially when the risks to the City's and the region's economy are as great as they are today – that the City and the State focus on those that will inflict the least damage on the City's economy.

The congestion pricing system proposed by the City could have a significant adverse impact on the City's economy, at a time when the City is particularly vulnerable.

- It would increase costs for a wide range of small businesses in Brooklyn, Queens and other parts of the City that serve customers in Midtown and Lower Manhattan.

- It would discourage discretionary trips into Manhattan by residents of the New York area suburbs, as well as other visitors who drive to the City. (More than 60% of all visitors to New York City arrive by car.)

- It would adversely affect a number of industries – including retail, restaurants, entertainment and automotive services – that are major employers of less-skilled, low-wage workers, and that are already anticipating a difficult 12 to 18 months.

An analysis of the potential impact of the City's proposed congestion pricing system prepared for Keep NYC Free in 2007 estimated that implementation of the proposed system would reduce overall economic activity in the City by more than $600 million, and would result in a loss of more than 7,700 full-time equivalent jobs. A revised estimate of the cost of congestion pricing in lost jobs and economic activity would today be somewhat lower – in part as a result of changes to the City's proposal recommended by the Traffic Congestion Mitigation Commission. Nevertheless, implementation of congestion pricing, even in the form proposed by the Commission, would put hundreds of millions of dollars in economic activity and thousands of jobs at risk.

- ***An uncertain revenue outlook***

With private auto travel in New York City already declining due to rising gas and toll costs, it is already clear that the revenues generated by the proposed congestion pricing scheme would be less than the City and the Traffic Congestion Mitigation Commission had forecast last year. And if the system proved to be as effective as its proponents claim in reducing the number of people driving into the Manhattan CBD on weekdays, revenues could be further reduced as well. Moreover, since the full impact of higher fuel and toll costs on auto travel can take several years to play out, the top-line revenues generated by congestion pricing could continue to decline for several years.

Even under more optimistic assumptions about future trends in oil prices, it thus seems unlikely that congestion pricing revenues would show any real growth in the foreseeable future – and they might well continue to decline.

The combination of flat or declining gross revenues and (inevitably) rising operating costs means that over time, the revenue efficiency of the proposed congestion pricing scheme would deteriorate even further.

- ***Issues of fairness***

The burden of paying for the congestion pricing scheme proposed by the City and the Traffic Congestion Mitigation Commission would have fallen disproportionately on:

- Working and middle-class residents of areas outside Midtown and Lower Manhattan who need for various reasons to drive into the Manhattan CBD; and

- Small businesses in areas such as Long Island City and Sunset Park that must make frequent trips into the Manhattan CBD to serve their customers.

Although the Traffic Congestion Mitigation Commission sought to address various concerns about the City's proposed congestion pricing scheme, it was ultimately unable to resolve them.

Proponents of congestion pricing have defended the proposed system's fairness by arguing that the median income of those who commute to work in Manhattan by car is higher than the median income of New Yorkers who uses subways and buses to get to work. While that statement may be true on its face, it is also misleading – at least to the extent that it seeks to portray New Yorkers who drive to work as a group of wealth people who aren't paying a fair share of the cost of the transit system. In reality, the majority of New Yorkers who drive to work in Manhattan are by no means affluent – in 2000, according to the Census Bureau, the median income of residents of the other four boroughs who drove to work in Manhattan was about $43,000.

Ironically, Manhattan residents who drive private cars to work are significantly more affluent – with a median income of $103,000 in 2000 – than those who drive in from the other boroughs. But under the system proposed by the Commission, the great majority of them would be exempted from paying the congestion charge.

- ***Lack of broad-based support***

The controversy over the City's proposal that arose in 2007 – and the unusually acrimonious debate over the version proposed by the Commission that followed in 2008 – showed that it will be extraordinarily difficult (if not impossible) to come up with a version of the proposed cordon pricing system that will be broadly accepted as being fair and equitable. Including it in any proposed package of transit financing initiatives could jeopardize the whole package.

- ***Failure to address the real causes of congestion***

Finally, as our analyses showed last year, the type of cordon pricing proposed by the City is not an effective way to reduce traffic congestion. It simply doesn't get at the real problems and conditions that give rise to congestion in the first place, such as:

- Inadequate enforcement of (and inadequate fines for violating) existing traffic and parking rules;

- Abuse of parking placards – a problem the City has, to its credit, taken serious steps to reduce, but that is not yet eliminated;

- Cruising by taxi drivers in search of fares;

- Under-pricing of on-street parking;

- Under-pricing of street closing permits for construction site and utility repairs; and

- Inadequate off-street space for loading and unloading

There are far more effective and far less costly approaches to reducing congestion that are already available to the City – and it has in fact already started to pursue them.

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