

THE CITY OF NEW YORK  
INDEPENDENT BUDGET OFFICE

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July 28, 2003

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Dear Mr. Russianoff and Ms Leon:

In a letter dated June 3, 2003, the Straphanger's Campaign and Common Cause asked the Independent Budget Office to publish "model principles for budgeting and financial reporting" for the Metropolitan Transportation Authority (MTA) and MTA New York City Transit. This letter and the attachment are in response to your request.

As a public authority governed by a board appointed by the Governor and funded both by user charges and by general tax revenues, the budgeting and financial reporting of the Metropolitan Transportation Authority should be characterized by *openness*, *accountability*, and informed *participation*. There are numerous models for and examples of budgeting and financial reporting that facilitate those objectives. We have drawn on recommended best practices in formulating a set of principles for the MTA.

Recognizing the need for change, the MTA included a new budget process in its proposed reorganization legislation, introduced on June 10<sup>th</sup> 2003 as Assembly Bill no. 8904. Although the reforms contained in the MTA proposal would go some ways toward greater openness, accountability, and participation, in other respects the proposal could be strengthened. Specifically:

- The time for review and comment on the final proposed agency budgets should be at least as great as that for the preliminary budget proposals. To that end, the date for submitting final proposed budgets should be moved up in time.
- The proposed budget message risks falling short of providing a comprehensive and accessible operating and financial plan. Instead, the authority should adopt a program budget approach that presents agency budgets in terms of the services the authority provides, and not just in terms of organizational units and objects of expenditure.
- The budget documents should include narrative description of budget and policy proposals as an integral part of the budget presentation, not as a separate document.

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- Performance measures should be integrated into the budget documents' program categories.
- Operating and capital budgets and programs cannot be considered separately. The individual agencies should include a presentation of the MTA capital construction budget and program as it relates to each agency as part of the preliminary and final budget proposals.
- The authority should consider an independent review, certification, or even production of revenue and ridership forecasts.

If further oversight mechanisms are desired, they should be designed to assure their independence and to have full access to needed information from the authority.

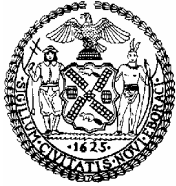
The attachment spells out in greater detail general principles and best practices for public sector budgeting, and evaluates the MTA's proposal based on those principles.

Please do not hesitate to call on us if we can provide any further assistance in this or other matters.

Sincerely,

Ronnie Lowenstein  
Director

- c. Hon. Peter S. Kalikow  
Edward B. Dunn  
Katherine Lapp  
Stanley Brezenoff  
Paul Crotty  
Diana Fortuna  
Michael Jacobson  
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## **Principles for MTA Budget and Financial Reporting**

During the fall and winter of 2002-2003, the Metropolitan Transportation Authority (the MTA) was widely criticized for having failed to make public adequate information on its financial condition to allow independent evaluation of the need for a fare hike. The authority has asserted that it has made all relevant information available, and that it publishes a voluminous amount of information about its operations and finances.

In response to the storm of criticism, including subpoenas and highly critical audits from the State and City Comptrollers, the MTA announced on May 13<sup>th</sup> a plan to reform its budget reporting practices. The authority has prepared legislation to enable its proposed reorganization and codify the proposals it announced.

In a letter dated June 3, 2003, the Straphanger's Campaign and Common Cause asked the Independent Budget Office to publish "model principles for budgeting and financial reporting" for the MTA. We begin with some general goals for budget and financial reporting, review the current requirements for MTA reporting and the authority's current practice, and then present a series of principles to guide evaluation of the MTA's proposals and their implementation. We then apply these principles to evaluate the MTA's proposals.

### **Background**

The MTA is chartered under the New York State public authorities law. The authority is governed by a 16-member board, the chairman of which is appointed by the Governor. The MTA is composed of several component agencies, including New York City Transit, which operates subways and buses within the city; two commuter railroad lines, Metro-North, which serves several upstate counties, and the Long Island Railroad, which serves suburban communities of Nassau and Suffolk counties. There is also Long Island Bus which operates bus service on Long Island. The MTA, through MTA Bridges and Tunnels, owns several river crossings, including the Triborough Bridge, the Queens Midtown Tunnel, and others.

One major purpose of the proposed legislation is to reorganize the authority, eliminating the current subsidiaries and replacing them with five agencies: bridges and tunnels, bus, subway, rail, and capital construction.

### **General Goals for Budget And Financial Reporting.**

The MTA is neither a general-purpose local government, nor is it quite like an “ordinary” New York State public authority. Unlike a local government, there is no legislative body to review the executive’s budget proposal. But the budget and financial condition of the MTA is of intense interest to its users and to the state and city governments that help finance its operations. A few general principles are applicable to its budget and financial reporting as they are to that of all other general- or special-purpose governments:

- *Openness*: As a public authority, the authority’s budget and financial condition should be fully disclosed and available to the public and its elected officials on a timely basis.
- *Accountability*: The authority, like any public agency or government, is ultimately accountable to the public who pays for its services, either through fares and tolls or through taxes and subsidies. Without adequate and timely information, full accountability is not possible.
- *Participation*: As a public agency, the MTA is required to give the public the opportunity to be heard. Current law requires public hearings on proposed fare increases or major service changes. Participation is facilitated and enhanced when the public has more and better information.

### **Current MTA Requirements and Practice**

The New York State Public Authorities law requires all public authorities to provide annual financial and budget reports to the Governor, the chair and ranking minority members of the Senate Finance Committee and Assembly Ways and Means Committees, and the State Comptroller (§2801 and 2802). In addition, the Comptroller is required to examine the books of public authorities—generally, at least once every five years; but in the case of the MTA the requirement is for an annual examination.

Annual budget reports of public authorities must be submitted no later than 60 days prior to the beginning of the fiscal year (i.e., November 1<sup>st</sup> for the MTA). No hearings are required, nor is there any provision in the law requiring any of the recipient elected officials to comment on the budget report. It is, in fact, a report, and not a proposal or a submission requiring review or approval, except by the MTA board.

Sec. 1269-d of the MTA statute requires it to submit an updated five-year “strategic operation” plan each July 1<sup>st</sup>. (In his April audit, the State Comptroller asserted that the MTA had not fulfilled this requirement.) The plan is to include, *inter alia*:

- “long-range” operational goals and objectives;
- service and performance standards;
- projected fares;
- estimated operating and capital sources of funding;
- estimated operating and capital costs adequate to meet the planned service and performance standards;
- “an analysis of the relationship between” the capital program and the planned service and performance standards.

The update is also required to report on the achievement of planned service and performance standards in the previous year.

Again, no hearings or other formal review of the plan is required, but the authority is required to consult with local officials in the preparation of the plan and to “take into consideration” any requests from them for service improvements.

### **Principles and Best Practices**

In this section we present some general principles and best practices for budget and financial reporting so as to realize the three broad goals of openness, accountability, and participation.<sup>1</sup> We subsequently discuss the MTA’s legislative proposal and how it measures up against them.

***Appropriate time horizon.*** The appropriate time horizon for presentation of a fiscal plan should be dictated by the timing of the consequences of decisions made today on an entity’s future fiscal condition. Two factors in particular dictate a multi-year time horizon for the MTA’s financial planning. First, fare policy has typically been changed with less than annual frequency, so that fare changes must be evaluated for their longer-term impact. Second, significant aspects of the authority’s operating budget also span a multi-year horizon, including labor agreements and capital projects.

At the same time, planning for the future inevitably entails greater uncertainty the further out one projects. Although some transit agencies plan for only two outyears, a four- to five-year horizon seems appropriate in most cases. A five-year plan would be consistent with the MTA’s capital planning cycle.

***Presentation.*** The presentation of budget and financial information is key to facilitating openness, accountability, and participation.<sup>2</sup>

***Timeliness.*** Budgets of large agencies are inherently complex, which dictates that adequate time for review and comment must be provided if any meaningful measure of participation is to be possible. The National Advisory Council on State and Local Budgeting (NACSLB) recommends that

*in order for the budget to be adopted in a timely manner, processes should be developed to assist stakeholders in understanding tradeoffs and to help decision-makers make choices among available options. The processes*

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<sup>1</sup> Although the MTA in its May 13<sup>th</sup> press release cited New York City’s budgeting as a model for its own proposed reforms, we have drawn on “best practices” literature on budgeting and financial reporting. While the enormous size and complexity of the city’s budget poses unique challenges, it would fall short on several of the principles and practices outlined here. See National Advisory Council on State and Local Budgeting: *Recommended Budget Practices: A Framework for Improving State and Local Budgeting* (Government Finance Officers Association, 1998; available at [www.gfoa.org/services/nacslb/](http://www.gfoa.org/services/nacslb/)). See also Ed Lazere, *Improving the Transparency of the DC Budget* (Washington, D.C., D.C. Fiscal Policy Institute; July 29, 2002; available at [www.dcfpi.org/7-29-02bud.pdf](http://www.dcfpi.org/7-29-02bud.pdf)).

<sup>2</sup> Many of the principles described here are put into practice in the Chicago Transit Authority’s 2003 budget proposal, available at [www.transitchicago.com/business/finance.html](http://www.transitchicago.com/business/finance.html).

*should include reporting to, communicating with, involving, and obtaining the support of stakeholders.*<sup>3</sup>

*Content.* The presentation of the budget should be made in such a way as to present all relevant information in a manner that makes it accessible to a broad audience. The budget document should articulate broad agency goals in measurable terms; present policies and plans that will guide service provision and programs; and relate spending plans to these goals and policies. The content, from broad goals down to budgetary detail, should be presented in a clear and accessible manner. In essence, this argues for a narrative that links agency goals, policies, and plans to the budget. To again cite the NACSLB's recommended best practices:

*The budget document should communicate key fiscal and policy decisions, issues, and tradeoffs. In order to facilitate stakeholder understanding of the choices that have been made, it is essential that materials be prepared in a format that is clear and comprehensible.*<sup>4</sup>

*Program orientation.* The budget is most usefully presented in terms of outputs and outcomes that are meaningful to users: that is, the agency's functions, programs, services, or activities, rather than purely in terms of standard "object classes" of expenditure, such as labor (personal services) and other-than-personal services, or OTPS (non-labor) inputs like fuel, contractual services, debt service, and the like. Program categories should be recognizable to users. Within these programmatic categories, the budget should present standard object classes of expenditure.

*Performance measures.* Accountability is enhanced when the provision of services is measured against performance benchmarks that state the agency's objectives and allow the agency and the public to evaluate how well the agency is doing. Integration of service performance indicators into the budget document enhances accountability. Performance measures should be explicitly tied to programs and spending.

*Comprehensive.* A budget should be a comprehensive operating and financial plan that covers all aspects of agency operations, with no materially relevant information omitted. Sufficient detail should be available to allow for evaluation and review of all the agency's programs and functions. Supporting detail need not be part of the main budget presentation, but should be publicly available.

*Integration of operating and capital budgets and plans.* Although the operating and capital budgets may be financed separately and even treated differently for accounting and financial reporting purposes, they should be presented—and reviewed—together. Both are integral to the provision of the agency's programs and services, and separate presentation and review impedes a comprehensive understanding.

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<sup>3</sup> *Recommended Best Practices*, op. cit.

<sup>4</sup> *Recommended Best Practices*, ibid.

### ***Transparency***

*Verifiability.* Preparing a budget inevitably requires forecasting values of key variables, including general economic performance, legal and regulatory issues, technology, demographic changes, and the like, that will impact agency revenues, demand for services, and general operating context. Forecast detail, including assumptions about key variables, should be available as part of the budget documentation.

With respect to revenue forecasting, the NACSLB recommends a consensus forecast, and suggests various routes to achieving one. An independent review, certification, or even production of a revenue forecast (and in the MTA's case, perhaps also a ridership forecast) can help ensure that participants in the budget process at least start with an agreed-upon resource baseline.

*Comparability.* For meaningful accountability, it must be possible to measure changes within the budget year, especially when the budget and financial plan are periodically updated, and to see the effects of changes on future years. It is also important to be able to compare one year's performance to another's. Typically budget proposals are presented in terms of changes from current year levels, with explanations of major increases and decreases (The City of New York's budget presentation is in this regard atypical). Ideally the proposed budget should be presented in the context of the previous year's results and the current year budget. Consistency in presentation and in the definitions of terms also enhances transparency.

### **Evaluating the MTA Proposal**

The legislation proposed by the MTA to reform its budget processes would establish a number of practices that should take it some ways toward implementing these principles, although in other respects the proposal could be strengthened.

The proposed budget process would start with submission of preliminary budgets for the various MTA agencies by July 15<sup>th</sup> each year for the succeeding year (the MTA's fiscal year corresponds to the calendar year). The budgets would be submitted to the board and to the elected officials and posted electronically. The elected officials would have until August 15 to submit their assessment and recommendations. The authority then would have until October 26<sup>th</sup> to submit final proposed budgets, along with a separate budget message, the content of which is spelled out in some detail in the proposal. Public hearings would be held during the month of November, and the elected officials would have until the 25<sup>th</sup> of November to submit their response to the final budget proposals. The board would then adopt the budgets by December 31<sup>st</sup>. The proposal also calls for a four-year financial plan that would be updated three times a year. (An outline of the proposed budget cycle and process is attached.)

***Time Horizon.*** The quarterly-updated four-year financial plan should provide an adequate time horizon to evaluate the impact of budget and policy proposals, especially with regard to projected operating gaps that might indicate the need for fare increases or other actions. Extending the financial plan horizon to five years would correspond to the authority's capital planning horizon, but is not essential.

### ***Presentation***

*Timeliness.* The submission of preliminary budgets in July, followed by final proposed budgets in October, should provide greater opportunity for public review than has been the case in previous years. The timeline for review and comment by elected officials seems somewhat short (one month), particularly in light of the rather long time between their comments and the deadline for submitting the final proposed budgets (about 10 weeks). The proposal would be strengthened by providing an equal or greater period for review of the final proposed budgets. To that end, **the date for submission of the final proposed budgets should be moved up by about one month.**

*Content.* The MTA's proposal does not specify the form or content of the budgets except to spell out certain required elements of the accompanying budget message—which, however, “shall not be deemed a part of the budget.” The budget message is potentially a step toward providing more and more accessible information regarding the authority's programs and priorities. The requirement for “summary” explanations of “major” programs, however, could serve to limit the completeness of the presentation of the agency's budgets and falls short of a *comprehensive* and accessible operating and financial plan.

This approach also falls short of a genuine program budget. **The authority should adopt a programmatic presentation for its budget and financial reporting** that would allow users to view the budgets in terms of the services the authority provides. For example, relevant program categories for MTA Subways might include Train Operations; Station Operation; Station Maintenance and Cleaning; Train Maintenance and Repair; and Security.

The proposal also specifies that the budget message is not part of the budget itself. To make the budgets accessible to the widest range of users, **the budget document should include narrative descriptions of the budget and policy proposals as an integral part of the budget presentation.**

*Performance measures.* The MTA is currently and would continue to be required to present information on certain performance indicators, including peak and off-peak service frequency and commonly-used transit reliability indicators. **These and other performance measures should be integrated into the budget document** to provide a more comprehensive and accessible presentation of the link between resources and outcomes.

*Integration of operating and capital budgets and plans.* The MTA proposal continues to treat the capital program as distinct from the operating budget, on the grounds that the existing Capital Program Review Board provides oversight. In addition, under the proposed reorganization, a separate entity with its own budget—MTA Capital Construction—would be created to administer the authority-wide capital program.



The capital-intensive nature of MTA operations, and the increasing reliance on revenue-backed debt to fund the capital program, means that separate consideration of the capital and operating budgets will fail to provide a complete, comprehensive, and accurate picture of the agency's goals and programs, and of the implications of one for the other. **The agency budgets should include a presentation capital budget and program as it relates to each agency as part of the preliminary and final budget proposals and each financial plan update.**

The strategic operation plan required under both current law and the MTA's legislative proposal includes as one component an analysis of the relationship between capital program elements and the achievement of planned service and performance standards. This requirement could be incorporated into the capital portion of the budget presentation.

**Transparency.** The transparency of the authority's budget presentation will depend on the extent to which it makes available information on the assumptions and analysis that it relied on in its preparation. Adoption of the principles and practices outlined here would significantly enhance the transparency of the authority's budget and finances.

**Verifiability.** Another measure that would increase confidence in the authority's budget numbers would be **an independent review, certification, or even production of revenue and ridership forecasts.**

**Comparability.** The MTA proposal would require a report on actual versus budgeted revenues for the previous year, and, as part of the budget message, a statement of actual revenues for the preceding four years, as well as a forecast of recurring costs for major new or expanded programs in the four-year financial plan. This would help in constructing a baseline or "current services" program budget over time. Ideally as part of the budget document, **proposed spending and revenues should be presented at the program level, side-by-side with the previous year's results and the current year budget**, along with service level data and explanations of changes and variances.

### **Other Considerations**

**The impact of restructuring on budget and financial reporting.** One impediment to accessible and transparent financial information in the past has been the structure of the MTA and its component agencies, which have accounting and reporting differences that make comparisons and integrated reporting difficult.

The MTA's corporate restructuring should largely eliminate this problem, and will almost certainly require the authority to realign its financial management systems in a way that will facilitate future public budget and financial reporting.

**Oversight.** There are a variety of models for fiscal oversight generally, from simple legislative oversight and budget review to formal independent oversight bodies. No particular model is necessarily best in this instance.

In the case of the MTA, a public authority, there is no legislative body, only the board. So there is no legislative review in the usual sense. Since the authority is a state-chartered entity, oversight by state elected officials is appropriate. For example, the state comptroller is required under current law (§1276-a) to audit the MTA's books annually and report on his findings and recommendations to the governor and legislature. In this respect, the provision for comment by the elected officials in the proposed MTA budget cycle provides greater scope for oversight (and participation) than previously.

If additional oversight is deemed desirable, it should possess certain attributes to be effective. Any oversight body must have as a matter of statute full access to agency financial information. (For example, the existing Capital Program Review Board may require "such supporting materials" as it needs to accompany the MTA's five-year capital program plan.)

Finally, to be effective, regular and sustained oversight is necessary. Interest in the MTA's finances waxes when fare and toll increases are on the table, and wanes when they are not. Nonetheless, decisions made today, while not necessarily requiring a fare increase this year or next, can have future consequences for fare and toll policies and for the overall fiscal health of the authority.

## **Attachment: Summary of MTA Budget Process Proposals (Proposed Sec. 1264-e)**

*Note:* Excludes capital funding and expenditures (covered under subdivisions 1261, 1261-a, 1261-b).

- May 1<sup>st</sup> Auditor General’s report to Chairman and Executive Director on actual revenues of the authority for previous fiscal year.<sup>5</sup>
- May 15<sup>th</sup> Report comparing actual revenues to budget for previous fiscal year; sent to elected officials<sup>6</sup> and electronically posted.
- July 15<sup>th</sup> Preliminary budgets and financial plan updates submitted to board and elected officials and posted electronically.
- Aug 15<sup>th</sup> Elected officials’ assessment, comments, and recommendations on preliminary budgets. May incorporate input from public hearings.
- Oct 26<sup>th</sup> Proposed final budgets and budget message submitted to board and elected officials and posted electronically. The budget message to include the following:
- Summary explanation of major programs, projects, “emphases and objectives” of budgets and of general fiscal and economic condition of the authority;
  - Supporting schedules itemizing anticipated expenses by categories;
  - Recommended changes in fares and tolls or other revenues set by the authority;
  - Statement of all actual revenues for preceding four years and for current year to date;
  - Projected revenues for current year and budget year;
  - List of non-recurring revenues in excess of \$500,000;
  - Four-year financial plan, including
    - expenditure forecast “for all existing programs”
    - revenue forecast by source
    - for “major” new or expanded programs, forecast of recurring costs when fully implemented
    - Explanation for any projected changes in existing service levels, including change in spending
  - Explanation of changes between preliminary and proposed final budgets;
  - Reconciliation with elected officials’ comments on preliminary budget.
- Nov 6-25<sup>th</sup> Public hearings on budget proposals.
- Nov 25<sup>th</sup> Elected officials’ response to final budget proposals.

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<sup>5</sup> Unless otherwise noted, all references to “the authority” or “the MTA” here include the authority and its proposed constituent agencies: MTA rail, MTA subways, MTA bus, MTA capital construction, and MTA bridges and tunnels.

<sup>6</sup> Governor, President of the Senate, Assembly Speaker, Mayor of New York City, County Execs of Nassau, Suffolk, Westchester, Putname, Dutchess, Rockland and Orange counties.

Dec 31<sup>st</sup> Adoption of the budgets by the board.

Sixty days after adoption: Update of financial plan. Updates also accompany preliminary and proposed final budget submissions.