Case Study—New York Metropolitan Transportation Authority Transit Facility Revenue Bonds, Series 1998C

In December 1998, the Metropolitan Transportation Authority issued $317.245 million in principal amount of its Transit Facilities Revenue Bonds, Series 1998C. There are $2.282 billion aggregate principal amount of transit facility bonds of the Authority outstanding including the series 1998C Bonds.

The Parties

The Metropolitan Transportation Authority, a public benefit corporation of the State of New York, has responsibility for developing and implementing a unified mass transportation policy for The City of New York and Dutchess, Nassau, Orange, Putnam, Rockland, Suffolk, and Westchester counties (collectively with the city, the “Transportation District”). The Authority carries out these responsibilities directly and through its subsidiaries and affiliates, including the New York City Transit Authority, an affiliate of the Authority, and the Manhattan and Bronx Surface Transit Operating Authority (MaBSTOA), a subsidiary of the Transit Authority.

The Project

The city’s rapid transit system is by far the largest in the nation. Only a few cities in the world have a subway system comparable in physical size and ridership. The subway system has over 656 miles of mainline track extending 230 route miles. It operates 24 hours a day, 365 days a year. In calendar year 1998, approximately 1.2 billion revenue passengers used the subway. The Transit Authority employs approximately 25,000 workers in rapid transit. It currently has a fleet of approximately 5,800 subway cars, two major subway car repair shops, 14 maintenance shops, 23 subway car storage yards, and 468 passenger stations.

The Transit Authority and MaBSTOA presently operate bus service on approximately 230 local and express routes throughout the city. The majority of bus routes are designed to serve passengers traveling within a particular borough or to serve as feeders to the subway system. In calendar year 1998, approximately 625.5 million revenue passengers used the bus system. Together, this bus system employs approximately 13,000 persons and operates approximately 4,100 buses.

To assist the Transit Authority and MaBSTOA in carrying out its role, the Authority has been authorized to issue bonds, payable from certain revenues and operating subsidies of the Transit Authority and MaBSTOA, to fund a portion of the capital needs of the Transit Authority and MaBSTOA. The Series 1998C Bonds were issued by the Authority to refund other bonds issued for such purpose.
The Financing

The Series 1998C Bonds are special obligations of the Authority payable solely from and secured by a pledge of the items pledged under the Transit Facilities Special Obligation Resolution of the Authority, adopted October 14, 1982, as supplemented. These include the Revenue Fund into which there is to be deposited, pursuant to an agreement among the Authority, the Transit Authority, and MaBSTOA, dated July 1, 1982, as authorized by Title 9 of Article 5 of the Public Authorities Law, as amended (the Transit Authority Act), fares collected for use of the subway and bus systems operated by the Transit Authority and MaBSTOA, payments from concessionaires, and operating subsidies (not including federal operating subsidies). The operating subsidies include expense reimbursement payments from the State of New York, the city, and the Triborough Bridge and Tunnel Authority (TBTA), an affiliate of the Authority. The operating revenues and subsidies pledged under the Resolution are collectively referred to as the “pledged revenues” or “revenues.”

The Series 1998C Bonds are on a parity as to the lien on pledged revenues with all bonds that are, and with all bonds and parity obligations that from time to time may be, issued and outstanding under the Resolution.

The financing agreement obligates the Transit Authority and MaBSTOA to fix or adjust the rates of fares, fees, rentals, and other charges for the use of the system at the level required by the Resolution, which obligates the Authority to cause the Transit Authority and MaBSTOA to adjust such rates as necessary to produce revenues, together with other lawfully available moneys, sufficient to pay debt service on bonds and parity obligations, maintain all debt service reserve funds at their required levels, and pay all operating and maintenance expenses and other obligations of the Transit Authority and MaBSTOA as they become due. This covenant is similar to a traditional revenue bond rate covenant with the added feature of including subsidy payments and other available revenues. Due to the lack of control the Authority has over the amounts of subsidies and other revenues, such amounts would not have been included in a traditional revenue debt analysis.

The Transit Authority and MaBSTOA have covenanted in the financing agreement that prior to the commencement of each fiscal year the Transit Authority and MaBSTOA will prepare inspection, maintenance, and repair programs and revise such programs, if necessary, in order to procure an Independent Engineer’s Certificate stating that such programs are reasonable and appropriate. Such a certificate has been furnished for each fiscal year required. The Transit Authority and MaBSTOA have also covenanted to include the cost of such programs in their annual operating budgets and, on or before the commencement of each fiscal year or 60 days following the receipt of the Independent Engineer’s
Certificate, whichever comes later, to fix or adjust fares or other charges required to generate revenues during the fiscal year sufficient, together with all other lawfully available moneys, to pay the debt service on bonds and parity obligations, operating and maintenance expenses included in such budgets, and all other obligations to become payable during the fiscal year.

The financing agreement further provides that if the actions by the Transit Authority and MaBSTOA to meet their obligations under the financing agreement are not sufficient to allow the Authority to meet its obligations to make payments to holders of bonds and parity obligations and to make all required deposits under the Resolution, the Transit Authority and MaBSTOA shall, and the Authority and the Trustee may, take such actions to require the Transit Authority and MaBSTOA to fix or adjust the rate or rates of fares, fees, rentals or other charges for the use of the system as shall be necessary to produce revenues that, together with all other lawfully available moneys, shall enable the Transit Authority and MaBSTOA to make the payments required under the financing agreement.

Additional bonds (other than refunding bonds) and parity obligations may be issued only if, in addition to other requirements, the Authority meets certain tests established under the Resolution, including the delivery of a certificate of an Independent Engineer stating that it is feasible that revenues can be derived from the operations of the system so that certain coverage ratios can be maintained during the current and each of the succeeding 3 fiscal years. The Independent Engineer’s certificate must also state that certain historical revenues, adjusted on a pro forma basis as provided in the Resolution, provide four times coverage for adjusted aggregate maximum debt service.

Under the Authority's enabling legislation, the state pledges to and agrees with the holders of any notes, bonds, or lease obligations issued or incurred by the Authority, including bonds and parity obligations, that the state will not limit or alter the rights vested in the Authority to fulfill the terms of any agreements made by the Authority with the holders of its notes, bonds, and lease obligations, including bonds and parity obligations, or in any way impair the rights and remedies of such holders. The Authority’s enabling legislation also prohibits the Authority from filing a petition in bankruptcy under Chapter 9 of the Federal Bankruptcy Code or such successor chapters or sections as may from time to time be in effect. The state has pledged that so long as any notes, bonds, or lease obligations of the Authority are outstanding, it will not limit or alter the denial of authority to the Authority to so file. Similar covenants apply to the Transit Authority and MaBSTOA.

The pledged revenues of the Transit Authority and MaBSTOA are receipts derived from a number of sources that may be grouped into seven principal categories: (i) fares; (ii) income from concessions and advertising; (iii) fare and service reimbursements from the city for certain costs incurred by the Transit Authority and MaBSTOA; (iv) operating subsidies provided by the state and the city from their general
funds; (v) amounts derived from special tax-supported operating subsidies; (vi) amounts derived from TBTA’s operating surplus; and (vii) income from investments and miscellaneous other sources.

Pledged revenues amounted to approximately $3.36 billion in 1998 (representing 21 times aggregate bond service for such year). Revenues derived from fares charged to users of the system in 1995 aggregated approximately $2.0 billion, or approximately 68 percent of operating disbursements.

The rate or rates of fares charged to users of the system are determined by the Transit Authority and MaBSTOA after reviewing and adopting operating expense budgets. After assessing the availability of governmental subsidies, the Transit Authority and MaBSTOA make a determination of the level of fares needed to operate on a self-sustaining cash basis. Due to the impact of fares on users of the system and on the regional economy, it is the policy of the Transit Authority and MaBSTOA to attempt to reduce costs or obtain additional revenues from other sources prior to increasing fares. Consequently, the amount and timing of fare increases are affected by the federal, state, and city financial conditions and budgetary and legislative processes.

The Authority relies on a mixture of federal, state, and local subsidies; TBTA operating surpluses; and dedicated special taxes to make up the operating deficit and fund capital costs. There is an inherent tension between the desires of the credit markets for a secure revenue bond with customary rate covenant and coverage and the reality of transit operations, which is one of providing a public service that, while in part is user-based through fee collections, is also subsidized as part of the Transportation District’s infrastructure.

The Authority employs a rate covenant but adds to the fare box revenues other available revenue, including subsidies to determine compliance with the rate covenant. The Authority has a coverage test for the issuance of additional debt, but it is a gross coverage test of certain revenues at four times debt service. Therefore, the Authority’s fare box revenue bonds have the trappings of traditional revenue bonds, but not the substance. A traditional revenue bond would require net revenues sufficient to cover debt service. Due to the subsidy required for Transit Authority and MaBSTOA operations, there are no net revenues from operations. The inability to declare bankruptcy is very unique and of great reassurance to investors in the deficit-prone operations. Investors have the assurance that operations will continue and the Authority’s debt cannot be avoided.

There is no assurance that there is any level at which system fares would produce revenues sufficient to comply with the rate covenant of the financing agreement in the event the level of collection of dedicated taxes, operating subsidies, and expense reimbursements presently provided for the system were to be discontinued or substantially reduced. As is generally the case with publicly operated mass transit systems in the United States, the system has been dependent upon aid and assistance to meet its capital and
operating needs in the past, and it is anticipated that the system will continue to be so dependent for a substantial portion of such needs in the future.

Fare box revenue is not sufficient (and is never anticipated to be sufficient) to maintain operations and cover debt service and capital costs. The Transit Authority and MaBSTOA are dependent on governmental subsidies that can get mired in the legislative process (a delay in adopting the state budget can result in a delay in receiving certain subsidy payments and cash flow restraints), or vary depending on appropriations. In New York, where the transit system is vital to the economy and of a sufficient size to weather recession years and a downturn in ridership, a revenue based financing is deemed creditworthy. If the system was not as integrated into the Transportation District infrastructure or if it did not have the historical and institutionalized financial support that the Authority enjoys, its access to the credit markets would most likely be more limited.

The Authority as an issuer is unique in more than just the technique it uses to finance capital improvements. Having a system that generates approximately $1.9 billion a year in operating revenues and has a fare box recovery ratio of approximately 68 percent is unique. In addition to the Authority’s issuance of transit fare box bonds, the Authority has issued dedicated tax fund bonds secured by certain state subsidies. TBTA has issued general purpose revenue bonds secured by TBTA bridge and tunnel tolls, special obligation bonds secured by regional mortgage recording taxes and by TBTA net revenues on a subordinate basis, and beneficial interest certificates secured on a subordinate basis on TBTA net revenues. In 1982 and 1987 the state agreed to permit the Authority to issue service contract bonds secured by the state’s appropriation of debt service to finance Transit Authority and MaBSTOA capital needs. Being vital to a region, having a long historical existence in the infrastructure, and possessing accepted financial subsidies (such as the TBTA bridge and tunnel tolls) completes the unique nature of the Authority’s financing alternatives.