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ISSUE BRIEF

SEVEN WAYS THE MTA CAN SAVE $10 BILLION

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Contents

Executive Summary

In mid-July, the state-subsidized Metropolitan Transportation Authority, under fire for the past two years for poor performance, released a preliminary "transformation plan," required as part of this year's state budget, enacted in April 2019. The plan directs the MTA to rethink many aspects of its business practices, from consolidating three separate bus divisions to reforming civil-ser-vice rules.[1] A recently enacted state law directs the MTA board to vote on the final plan this week.[2] Though the initial report offers constructive suggestions on consolidating back-office functions and separate bus companies to save up to $500 million a year, it ignores or glosses over some of the key factors that are driving up MTA costs, culminating in a potential $1 billion deficit in three years.

The review comes at a time when it is increasingly important that the MTA spend its money more wisely. Beginning in 2021, the authority will receive $2 billion in annual new revenues, approved in the state budget, to be generated from three sources: congestion pricing in Manhattan below 60th St.; an increased tax on "mansions" sold in New York City; and a change in the Internet sales tax. The new revenues will support $25 billion in bonded debt for the MTA. This debt will fund infrastructure upgrades that likely include subway-signal modernization and step-free transit accessibility for the elderly and disabled and riders with small children. It is also to be spent on repairs to and replacements of tracks, cars, buses, and other infrastructure to the subway, bus, and commuter rail lines and the potential expansion of these lines.[3]

Nevertheless, the projected new revenues will not cover the MTA's projected capital needs. If the MTA continues its capital expenditures at the pace of the past half-decade, the authority will spend an additional $66 billion on major projects by 2030.[4] Moreover, the MTA has a long history of completing capital projects late and over budget, and its construction costs are far above global standards.[5] As the MTA undertakes its internal reviews, the authority, as well as the state legislature, comptroller, and governor should focus on a few key additional areas where the potential for savings is large. This issue brief suggests seven areas where the MTA can realize $10 billion of savings over a decade in direct capital savings, in new non-taxpayer revenues, or in savings to the day-to-day operating budget that could go toward capital spending (see the summary table below). Several of New York's nonprofit good-government groups—including Reinvent Albany, the Regional Plan Association, the Empire Center for Public Policy, the Citizens Budget Commission, and the Partnership for New York City—have recently offered discrete ideas for achieving MTA efficiencies that this paper takes up.

How the MTA Can Save $10 Billion over 10 Years *

Prevailing Wages and **Work Rules**	2,000,000,000
Procurement	1,400,000,000
Materials Costs	3,700,000,000
Productivity Gains	1,300,000,000
Health Care	1,300,000,000
Commercial Revenue Generation	300,000,000
Total	**10,000,000,000**

*Savings are based on author's calculations drawn from sources named in the text.

Where to Find the Money

1. Prevailing Wages.

New York State law orders construction firms on public works projects, including MTA projects, to pay "prevailing wages" set by the state's department of labor. The mandate covers pension and health-benefits contributions as well as cash wages. For example, the current wage for tunnel workers on a government project in New York City's five counties is $58–$65 an hour, plus an additional $39–$42 in hourly benefits.[6]

A comparison between the public-paid (including MTA) projects and the private sector is instructive. The current rate for an electrician working on a government project is $56 per hour, plus an additional $56.54 in hourly benefits.[7] By contrast, an electrician working in the general (non-prevailing-wage) market in the New York region is paid $36 in wages an hour, a 56% difference, not including benefits, which are generally lower in the private sector.[8]

Statewide, prevailing wages have a large impact. A 2017 Empire Center study found that prevailing-wage requirements push up overall project costs by 13%–25%.[9]

2. Work Rules.

The impact of prevailing wages is inextricably linked to work rules, the MTA's second-largest source of capital-cost savings. The labor contracts between contractors and construction unions include inefficient work rules that drive down productivity—that is, the amount of work done per hour. For example, an "operating engineer" must be on hand to control even a fully automated elevator at a construction site. Plumbers, electricians, and painters cannot perform even modest tasks outside their respective classifications.

The first step to reforming the prevailing-wage system as well as the work rules that prevailing wages fund is *transparency*. The legislature should change the state's labor law so that the terms of all construction contracts governed by prevailing wage are publicly available.

The second step is to acknowledge *motivation*. Construction contractors and unions are both under pressure to maintain the existing system in order to preserve retirement benefits for near-term and current construction-industry retirees. Many construction-union retirement-benefit funds, for example, are insolvent and depend on current payments by contractors, which, in turn, depend on the MTA to reimburse them for their current high staffing levels and low productivity.[10] Construction contractors and construction unions currently negotiate work rules without input from the MTA. The MTA should have a role in establishing work rules and could agree to share a portion of the clear, measurable savings provided by higher worksite productivity in future union contracts. The unions would deposit their portion of this savings-sharing in the insolvent retirement funds.

The third step is for the MTA and state lawmakers to *lobby* Washington to ensure that any national infrastructure-investment bill nods to the reality that private-sector construction-industry retirement burdens are constricting state and local government ability to cut infrastructure-labor costs. One-time-only federal aid to distressed construction-industry retirement funds could come with conditions attached, such as a requirement that private-sector construction workers doing business on government projects partially release their future claims on these insolvent pension funds.

Result: With labor costs constituting approximately 40% of a large project's cost,[11] even 15% savings on prevailing wages and work-rule productivity (shared equally between the MTA and construction unions) could save $2 billion over 10 years.[12]

3. Procurement.

The MTA's procurement process is plagued with several long-standing problems, as both the Regional Plan Association and Reinvent Albany have found in separate studies over the past year.[13] On major projects, the MTA generally awards a contract to a low or sole bidder and the bidder that promises to achieve the lowest responsible price (expected profit included) for delivering the project.[14] The MTA suffers, though, from a shallow bidding pool; many experienced global companies are deterred by the complexity of each agency's procurement process. The MTA is not good at determining when a low bid is not responsible; one major contractor defaulted on the East Side Access project, for example, after its bid was inadequate to complete the work.[15]

Finally, once an MTA agency awards a contract, it either requests or agrees to multiple "change orders," or amendments to the contract to change the scope and specification of work, over the life of the contract. The MTA often asks for change orders because a new technology has superseded the one specified in a contract, because poor coordination among different contracts has resulted in gaps in work, or because the initial design or engineering was insufficient. The MTA has no leverage in negotiating these change orders; once it has awarded a contract, the winning bidder effectively holds the authority hostage.

Change orders are significant. The MTA reported $731 million in change orders in 2018, according to a Reinvent Albany report. Overall, Reinvent Albany notes, in $26.5 billion worth of original contracts still active in 2018, $6 billion were changed, a 23% difference.[16]

Procurement is difficult but not impossible to reform. One of the problem's roots is lack of competition on major contracts, many of which attract a single bidder. The MTA should create a dedicated staff to travel and talk to potential global bidders, large and small, about why they hesitate to bid on MTA contracts and make the anonymized findings public. The MTA is already embarking on a long procurement-reform process. It should experiment with more flexible contract terms, including awarding contracts based on "best value" rather than low bid, and incorporating a reserve for modest changes, with both the MTA and contractors sharing the portion of the reserve that goes unused during the life of the contract. The authority should also pursue more contracts under which the private-sector contractor bears responsibility for achieving a broad result on time and on budget—and is allowed more discretion in how to achieve that result—rather than contracts that depend on thousands of individual specifications. The MTA board, which must approve large change orders, should require a consistent, detailed explanation from its staff on the reasons for individual changes so that outside observers could better assess patterns.

Result: Even modest progress on procurement to reduce change orders over a decade, paring the 2018 level by 20%, could save $1.4 billion over 10 years.

4. Materials Costs.

On a large project, approximately 40% of the expense can consist of materials such as concrete and steel. Yet the public has no way of assessing whether the MTA is paying a fair market price for materials whose prices should be based on global commodity indexes. For example, in May 2019, the MTA received three bids for concrete, ranging from $384 million to $603 million.[17] Outside observers have no way of knowing how much each bidder deviated from the underlying global index prices for wholesale base materials.

The legislature should amend the state labor law so that on all projects involving contracts subject to prevailing wage, contractors and subcontractors must publicly disclose the price they paid for materials and resolve any discrepancies for costs that don't conform to those reported by global indexes, such as the Portland cement cost index.[18]

Result: A 15% reduction in costs on potentially more than $25 billion in materials purchases could save $3.7 billion over a decade.

5. Productivity Gains (shared with workers).

Over a four-year financial plan, according to a Citizens Budget Commission estimate, the MTA could save $950 million by forgoing raises for its unionized employees.[19] The MTA does not project its spending on employee wages past four years, but it is reasonable to think that zero wage increases over a decade would result in $2.5 billion in savings.

Rather than ask employees to forgo inflation-indexed raises, the MTA board should direct its staff to ask each union bargaining unit to come up with clear, measurable cost savings via enhanced productivity. Such costs savings, for example, could include carefully structured pilot experiments on automated subway trains, such as the 7 and the L, to deploy the now-redundant conductor on the train to another task. Cost savings could also include gated fare entry on commuter-rail lines to save conductor time. In turn, the MTA and the unions could share these measured savings.

Result: Shared productivity enhancements could save the MTA $1.3 billion over a decade.

6. Health Care.

The MTA will spend nearly $700 million this year on "other post-employment benefits" (OPEB), largely retiree health care. By 2022, this expense will rise to nearly $900 million.[20] To defray these costs, the MTA should start taking better advantage of the national government's existing social safety net for retirees, including the individual Medicare market, as well as (for younger retirees) the Affordable Care Act market. For example, the MTA board should direct its staff to explore moving older retirees to Medicare Advantage (with the MTA partially subsidizing individual premiums) rather than traditional Medicare (paid for in bulk by MTA's riders and New York taxpayers). This alone could save the MTA one-half or one-third of its current Medicare costs.[21] In New Jersey, for example, Governor Phil Murphy has agreed with educational-employee public-sector unions to adopt a Medicare Advantage plan, saving a projected 16% in real terms between 2019 and 2020.[22] Connecticut has recently adopted a similar plan for retired public workers.[23]

The MTA also faces unsustainably growing costs in its active-employee market: health-care costs for current employees and spouses will consume $1.4 billion in MTA revenues this year, rising to $1.7 billion by 2023. The MTA should work with unions to explore ways of cutting these costs, including narrower doctor, hospital, and prescription networks as well as in-house clinics for routine health needs. In turn, the MTA and its unions could equally share in health-care savings.

Result: Curtailing even 10% of current and retiree health-care costs could save the MTA $1.3 billion over a decade.

7. Commercial-Revenue Generation.

The Partnership for New York City and the Boston Consulting Group found that only 4% of the MTA's annual operating budget, or $700 million, is derived from non-farepayer and non-taxpayer revenues: that is, commercial revenues generated by entrepreneurial efforts such as property leases, e-commerce pickup locations, loyalty partnerships, and advertising. This is significantly below the rate achieved by the San Francisco BART system, which generates 8.6% of its operating budget from commercial sources. The MTA is already taking steps to expand this revenue, including making plans to sign new master leases for well-trafficked commercial underground spaces.[24] The Partnership suggests that the MTA board create a separate unit whose staffers have financial incentives to achieve a $1 billion annual target.

Result: If the MTA were to use most of these new revenues to defray looming operating-budget deficits and devote 10% to capital needs, it could raise $300 million for capital expenditures over 10 years.[25]

Conclusion

As it embarks on a new era of capital spending, the MTA has many ways to save and raise money, from construction labor to construction materials to shared worker productivity and health-care savings. To achieve and surpass the modest savings ideas outlined here, the MTA, its board, and the elected officials who fund and oversee this critical infrastructure provider should make labor contracts and contractor purchases more transparent, work with organized labor to achieve shared savings, and be more creative in raising non-taxpayer and non-rider revenue.

Endnotes

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