

Sound Transit Expert Review Panel

April 12, 2007

<p>The Honorable Christine Gregoire Governor of the State of Washington Office of the Governor 416 – 14th Avenue S.W. P.O. Box 40002 Olympia, WA 98504-0002</p>	<p>Representative Judy Clibborn, Chair House Committee on Transportation 41st Legislative District House of Representatives 435 John L. O'Brien Building P.O. Box 40600 Olympia, WA 98504-0600</p>
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Dear Madams and Sirs:

This is the seventh letter from the Sound Transit Expert Review Panel (Panel) providing you with comments on key assumptions and methodologies being used by Sound Transit to prepare recommendations for a Sound Transit 2 (ST2) ballot proposition that will be submitted to voters in the fall of 2007.

The Panel's most recent meeting occurred last week, on April 5th and 6th. The meeting included an extensive tour of the construction progress on the Central Link Light Rail project, including the downtown Seattle bus tunnel retrofit, the Beacon Hill tunnel, the newly completed light rail maintenance facility at Forest Street in Seattle, and the at-grade construction in the Rainier Valley. In addition, the Panel was briefed on the most recent ST2 plan under review by the

Sound Transit Board, the status of ST2 financial planning, Sound Transit's recent experience with construction bids, and planning for ST2 maintenance facilities.

The following provides a summary of the Panel's comments they wish to pass along to you from last week's meeting. We are preparing this letter in time to be presented to the Sound Transit Board at its workshop later this week.

Maintenance Base Cost Estimates

In our letter of January 8, 2007, we raised several questions regarding Sound Transit's current and proposed maintenance facilities for the light rail program. At last week's meeting we continued those discussions, with Sound Transit staff presenting the plans for ST2 light rail maintenance facilities. Sound Transit staff recommends adding a full service facility in south King County and a light maintenance and yard (storage) facility in east King County. In addition, during our tour on April 5th we visited the Forest Street Maintenance Facility currently being completed.

After our January meeting Panel members asked for a comparison of the construction and right-of-way costs for the Forest Street maintenance base, with the anticipated costs for the proposed South King County facility and the East King County facility. The following table was presented by staff:

	East	South	Forest St. (at full build out)
ROW Acquisition	\$92.7	\$46.9	\$42.0
Construction	<u>\$102.4</u>	<u>\$150.0</u>	<u>\$74.0</u>
Total	\$195.1	\$196.9	\$116.0

* Note: Sound Transit staff is reviewing the Forest St. numbers for accuracy, but these are the numbers reviewed by the Panel.

The actual construction cost to date of the Forest St. facility is \$64.0M. However, at full build out of the yard the cost is expected to be approximately \$74.0M. This facility, at its full capacity, will store and maintain 105 light rail vehicles (LRV's), and include multiple bays, lifts, turntables and cranes for conducting heavy maintenance. The facility also includes an LRV washer system, a car painting room, wheel truing capability, and other equipment necessary to meet all of the "heavy" maintenance needs of light rail vehicles.

The estimated construction cost of the South facility is projected to be \$150.0M. This facility would also store and maintain 105 LRV's, and have the same "heavy" maintenance capabilities as the Forest St. facility. Using 2006 (\$) dollars for all of the above estimates, the Panel believes that the construction cost for the South facility should be very similar to the construction cost of the nearly completed Forest St. facility.

With regard to the East facility, Sound Transit Staff is proposing that it will be used for light maintenance and a storage yard for 40 LRV's. The heavy maintenance would be performed at the Forest St. and South facilities. However, the construction cost estimate for the East facility is \$102.4M in 2006 dollars, well in excess of the Forest St. Facility (\$74.0). It is logical to assume that the cost to construct a light maintenance facility and yard for 40 LRV's should be substantially less than the cost of a full maintenance facility and yard for 105 LRV's.

The Panel recommends that Sound Transit review and revise the construction cost estimates for the South and East Light Rail Maintenance facilities included in the ST2 proposal.

In our January 2007 letter the Panel expressed caution about the number of planned maintenance bases for the entire light rail system. The letter stated, "... *that maintenance facilities are costly to construct, staff and equip. In general, regional transit systems typically try to minimize the number of maintenance facilities.*" Panel members continue to express this caution and suggest that minimizing the number of maintenance bases should be considered as a principle for decision making about future maintenance facilities. In this regard, care should be taken to size and provide flexibility for expanding the South maintenance facility to accommodate potential future expansion needs. This is particularly important in light of the limitations on the size of the Forest St. facility. In addition, the Panel also suggests that Sound Transit staff review the scope of the East King County maintenance facility to insure that its construction will not duplicate the heavy maintenance functions provided at the Forest Street and South bases.

Financial Planning

At the April meeting, Sound Transit staff presented three items: 1) proposed updated financial policies; 2) response to concerns raised in this Expert Review Panel's March 23, 2007 letter; and 3) preliminary numbers for the ST2 finance plan.

Proposed Updated Financial Policies

Staff indicated that the primary objective of the proposed financial policy changes is to give the Board more flexibility in managing the program. In so doing, several policies are proposed that would give the Board more policy latitude. As an example, the new policies permit the Board to reallocate grants awarded for projects in one subarea to any other system projects or subareas. It is our understanding that concerns have been raised that the changes may dilute the core subarea principles and that at least one Board member has proposed an amendment addressing this. The Panel notes that providing greater flexibility to the Board has the potential to improve the overall Agency's financial condition as well as its financial flexibility.

Among the recommended financial policy changes is a change related to debt service coverage. Previous policy required that Sound Transit retain 5% of its debt capacity, effectively creating a "reserve" of sorts which could be tapped in an emergency. Staff has recommended that the set-aside of debt capacity, and the subarea debt service coverage ratios, be eliminated and replaced with a higher debt service coverage ratio of 1.50 times for the agency as a whole. Staff indicates this coverage ratio would result in an approximate "reserve" of \$1.2 billion. This change improves the financial position of Sound Transit. Higher annual coverage is a more conservative approach to financial planning than a set-aside of debt capacity. The Panel does note that in some other public agencies the funds set aside to maintain the debt service coverage ratios (particularly ones as sizeable as Sound Transit's will be) are difficult to maintain as a "reserve". "Reserves" are often spent to fund needs that arise, thereby reducing the overall debt that can be issued. Typically agencies perform an economic analysis to determine the best, most efficient use of the annual coverage "reserve" fund. We hope to see further analyses relating to this topic.

Sound Transit staff has recommended additional policies, including debt and investment management, risk management, capital replacement and farebox revenues. The updated policies propose that the Board require the maintenance of the policies but not require Board adoption of them. Panel members noted that many public agencies require Board approval of changes to financial policies. It was suggested that this may be best managed by having the Board approve the major principles underlying each of the policies, with staff creating internal implementation guidelines, which are not subject to approval.

Staff Response to the March Panel Letter

In the March 23rd letter the Panel noted that the Sound Transit Board has the authority to increase the sales tax on car rentals without additional voter approval. Staff has acknowledged that Sound Transit can raise this tax, but reported that the Board has indicated no interest in so doing. The Panel suggested that this additional revenue stream could add some minor financial flexibility to the program (\$60 million over 30 years). In future public communications, it was suggested that Sound Transit should make it clear that this potential revenue source does exist, but that the Board has chosen to reserve this revenue stream.

Sound Transit staff prepared additional analyses on the risk associated with ST2 right-of-way (ROW) costs. Staff notes that ROW costs are an estimated 12% of the total capital program for ST2. If the assumed growth rate for planning purposes were to double (from 4.5% per year to 9.0% per year) the total capital costs would increase by \$1 billion in YOY dollars. This is not considered material by the agency, because the agency would still be able to meet its 1.5 debt service coverage ratio. However, given the volatility of real estate values over the past two decades, the panel notes that higher than anticipated ROW costs represents a risk to the ST2 program that will need to be carefully managed.

Staff also discussed the sensitivity analyses. The Panel's letter recommended that staff work to understand which of the underlying assumptions expose the capital program to the greatest risk. Staff orally indicated that rising construction costs and lower revenue growth rates are the most critical. The agency intends to monitor these factors on an ongoing basis and make program management changes as needed.

Finally, staff presented additional work regarding the debt equity ratio. Ratios of peer agencies were presented. The Panel appreciates the work conducted by staff to collect this information. However, the data demonstrates that it is very difficult to calculate peer agency debt to equity ratios. Therefore, the Panel found the comparisons to be not particularly useful. The Panel did not ask for any additional peer agency analysis to be conducted. At the Panel meeting last week members asked questions about the recent assertion from some members of the public that historic documentation may impose a 17% maximum debt equity ratio on the agency. During the meeting, Joni Earl committed to provide the Panel with additional information prepared by internal counsel on this matter.

Preliminary Finance Plan

Staff presented summary level information on the preliminary finance plan. Staff has not yet prepared a finance plan document, so all the data was presented in Power Point form. Until a more formal finance plan document is presented to the Panel, with the detailed schedules and model outputs, we cannot finalize our review.

However, based on the summary level materials, the Panel provides the following comments:

1. In the materials presented to the Panel, the total ST2 plan is estimated to be \$13.3 billion in 2006 dollars. The Panel notes that the RTID 2007 Draft Financial Plan presents its program in both 2006 and Year of Expenditure (YOE) dollars. Since the programs are being presented to voters together, we suggest it would be helpful for Sound Transit to use materials showing the total program cost in both 2006 and YOE dollars as well. That would permit residents of the region to review comparable data between the two programs.
2. Of the total capital program, only 25% will come from bonding. We also encourage Sound Transit to show the overall cost of bonding, including the interest component over time.
3. Sound Transit currently assumes 4% of the total funding from federal grants. Panel members have raised a caution that federal funding may expose the agency to a requirement to perform additional environmental analysis (see the March 23, 2007 letter and the paragraph below). This represents not only a schedule risk but also a funding risk.
4. No funding is assumed to come from private sources. Although Panel members have repeatedly encouraged Sound Transit to pursue public-private opportunities, the Panel believes that it is more conservative, and appropriate, to assume no revenues from this source, until and unless funding commitments are obtained.

The Panel looks forward to a detailed review of the ST2 financial plan document. We understand that we will have an opportunity to conduct that review at our next meeting. The Panel will also conduct additional analysis regarding several outstanding issues that have been raised in previous Panel meetings. Those issues include the continued discussion between the Citizen Oversight Panel (COP) and Sound Transit staff regarding the expected rate of increase for future maintenance and operation expenses; the difference in right-of-way inflation

assumptions between Sound Transit and RTID; a review of the benefit cost methodology used by Sound Transit to meet the requirements of the Puget Sound Regional Council (PSRC) consistency review; and the issues raised in this letter.

Federal Environmental Review

As mentioned above, the Panel was told that Federal funds will be included in the ST2 finance plan. The specific projects to which Federal funds would be applied are yet to be determined. However, as they have stated previously, several Panel members said that it has been their experience that when Federal funds are used for high capacity transit projects, typically there is a requirement to comply with the National Environmental Policy Act (NEPA) on project level analyses.

In our March 2007 letter the Panel requested documentation that the federal agencies have agreed to a more limited scope of analysis for the East Link project. At last week's meeting Sound Transit staff expressed confidence that the Federal Transit Administration (FTA) concurs with detailed analysis of only No-build and LRT Build alternatives in the East Link Project FEIS, although there is no concurrence documentation. Further, staff appears to be assuming this model for other ST2 project level analyses.

We reiterate our caution that a project level NEPA document not including the full array of alternatives that meet the project purpose and need statement may expose that project to a risk of procedural challenge and delay. We strongly suggest that there be clear documentation (in some form) of FTA and/or FHWA concurrence with the scope of each project level NEPA analysis performed for ST2 projects.

Contracting Methods

In previous letters the Panel has suggested potential strategies for managing the future bidding climate in the region. In the event that the ST2 and RTID measures are approved by voters, it is certainly possible that Sound Transit will find it challenging to attract sufficient number of bidders to create a competitive bidding environment. During the Panel's tour of the Central Link Light Rail project we had considerable discussion about the lessons learned by Sound Transit regarding bidding practices. At our meeting Panel members offered several suggestions for Sound Transit consideration. Their ideas include the following:

- 1) Use of an Escalation/Adjustment clause on future contracts to reduce bid cost. If materials costs vary throughout the life of the contract the contractor needs to factor this into their bid. The owner (Sound Transit) is better off assuming this risk rather than paying for it up front.
- 2) Use stipends on large projects to encourage bidding. It was also suggested that Sound Transit consider using incentives in both quality and operations. For example by using a bidding methodology that includes A+B+incentives the contractor can bid on the time to complete the project and then accelerate further if the incentive is adequate. There are a number of innovative processes using incentives around the country that help insure timely completion, better quality and less impact on local businesses and the traveling public.

3) Use an independent review panel on large, complex or controversial projects to review more detailed designs, budgets and schedules. The panels can be made up of industry representatives not involved in the project. They can provide feedback to Sound Transit staff and the Board that otherwise would not be available.

Agreements with Local Governments

In several previous letters the Panel has commented on the advisability of working to develop term sheets with local jurisdictions even at this early stage of planning. In our March letter we again encouraged Sound Transit to continue to meet with local jurisdictions to create more formal agreements. Staff responded that it is difficult to create term sheets at this initial planning phase when so much additional design and environmental review work needs to be completed. The Panel continues to suggest that the more agreements Sound Transit can reach with local jurisdictions prior to the fall ballot measure the less risk there will be of altering scopes (and increasing budgets) after the vote. For light rail projects where a final alignment has not been selected, term sheets that describe the type and level of certain capital improvement (i.e. light standards, curbs and gutters, utility relocation, etc.) would help limit future scopes. Alternatively, if formal term sheets are not developed, Panel members have found that keeping written records that document the informal agreements, or disagreements, with local jurisdictions assist in the future negotiation of project scopes as further design work is completed.

We look forward to our next meeting. We anticipate meeting in late May or early June, assuming that the Sound Transit Board takes action on a final ST2 package later this month. Also, assuming that the proposal will go to the ballot this November, we expect that our next meeting will be our last. Our final letter will follow up on any outstanding issues raised in this, and previous letters, and report to you on our view of Sound Transit's compliance with the requirements of RCW 81.104.100 (the planning process for high capacity transportation systems) and RCW 81.104.110 (which provides the statutory authority for our panel's work).

Once again the Panel would like to thank the staffs of Sound Transit and Washington State Department of Transportation. They continue to provide information requested by the Panel and have been very helpful in our deliberations.

If you have any questions regarding this letter please let us know. You can reach the Panel members via our Administrator, John Howell, at 206-223-7660, ext. 102, or john@cedarrivergroup.com.

Sincerely


Mike Meyer, Chair

cc. Expert Review Panel Members
Senator Ed Murray
Bob Drewel, Executive Director, Puget Sound Regional Council