Summary of Policy

The Financial Stability Policy provides guidance for development of the Ten-Year Forecast, Long Range Transportation Plan and fiscal year budget. It provides additional safeguards and more transparency in Metro's budgetary process and supersedes the Financial Standards Policy.

The purpose of the policy is to ensure that: Metro prudently manages its financial affairs, establishes appropriate cash reserves, limits the level of debt that may be incurred, our debt assumptions are based on financial parameters similar to or more conservative than those that would be placed on Metro by the financial marketplace; there is a framework for developing the upcoming year's budget and other longer-range financial plans; and, establishes future business targets for management to achieve.

The Financial Stability Policy is divided into three sections: Goals, Strategies, and General Fiscal Policies. Additional financial guidance is found in the Business Planning Parameters and Debt Parameters.

The Financial Stability Policy adopted by the Board in January 2007, states that prior to the start of each new fiscal year, the Board shall review and approve the Financial Stability Policy that will be used by management as a framework for developing the following year's budget and will establish the Business Planning Parameters, including farebox recovery ratio, sales tax growth assumptions, and other key performance measurement goals to provide detailed guidance for development of the upcoming annual budget.

In January 2008, the Board adopted the modifications to the Financial Stability Policy including the FY09 Business Planning Parameters. Key modifications to the policy include:

- Removal of reference to a specific year in the policy statement since policy is updated each year.
- Financial Goals sections G4 and G5; Strategy sections S14, S19 and S21; and General Fiscal Policies section F11 were deleted.
- Financial Goals section G6 is now G4 as a result of sections G4 and G5 deletion. This section now identifies the specific fund source for reserves.
- Strategy section S3 now clarifies that the strategy applies to both bus and rail. It was also modified to include a statement that proposed budget presented to the Board for adoption will include a summary of actions taken or proposed to reduce expenditures.
- General Fiscal Policies section F4 was added to clarify that the Financial Stability Policy is the financial guidance policy for the agency.
- General Fiscal Policies section F9 was modified to reflect Board calendar and schedule.
- General Fiscal Policies section F9 - a language was added to clarify that budget amendments approved by the Board at the time of or prior to budget adoption shall be incorporated into the final budget document with no further Board approval required.
- General Fiscal Policies section F12 was revised to reflect the current process for Short Range Transportation Plan for Los Angeles County.
FY2008-2009 Business Planning Parameters sections B1 through B10 were added.

Debt sections D1 through D6 were added.

Detailed changes to the Financial Stability Policy are included in Attachment A. Attachment B is the revised Financial Stability Policy.

The Financial Stability Policy was adopted in January 2007 without fare policy elements. A proposed Fare Policy is presented for Board consideration in the January 2008 cycle. When approved, those elements will be incorporated in the Financial Stability Policy so that all financial policies will be contained in a single source document.

Historical Perspective

Prior to the adoption of the Financial Stability Policy in October 2006, the agency used the Financial Standards Policy, which provided parameters at the beginning of financial planning processes by which management recommendations can be measured.

The Financial Standards were divided into three sections: General, Debt, and Business Planning Parameters. The purpose of the General Standards is to ensure that the agency prudently manages its financial affairs and establishes appropriate cash reserves to meet its future financial commitments. The purpose of the Debt Standards is to limit the level of debt that we may incur and to ensure that debt assumptions are based on financial parameters similar to, or more conservative than, those that would be placed on us by the financial marketplace. These standards are consistent with the Debt Policy approved by the Board. Actual debt covenants may differ from those standards. When this occurs, the Debt Policy requires staff to disclose the covenants in the Board report that support the debt issuance. The purpose of the Business Planning Parameters is to provide management with a framework for developing the following year’s budget, other longer-range financial plans and future business targets.

Prior to the adoption of the Financial Standards, Proposition (Prop) A and C administrative funds were appropriated through the annual budget from the Special Revenue Fund to the General Fund to pay for activities not required to be accounted for in other funds. Neither voter-approved ordinance (Prop A & C) provides any definition of eligible uses for these monies. In the absence of specific Board or State approved guidelines for expenditures related to administration revenues, staff has been following generally accepted accounting principles in its General Fund.

In August 2001, the Board directed staff to report their findings raised in the FY1998 - 2000 Triennial Performance Audit, accompanied with any necessary corrective policy measures regarding the use of Prop A & C funds claimed for administration. Specifically, the audit findings stated, “the use of Planning and Administration funds claimed is not clearly identified in the annual budget or financial audit documents.”

In October 2001, staff embarked on developing standards, which would incorporate existing Board adopted financial guidelines and add areas such as the General Fund that are not presently addressed. These standards would set the parameters in the development of fiscal year 2003 budget.
In April 2002, the Board adopted the Financial Standards Policy that sets the parameters by which the Board and the public can be assured that financial plans are conservative, prudent, and provide for continued financial viability. However, in May the Board found that the Financial Standards might not have been clear regarding eligible uses of Prop A & C Administrative funds.

In June 2002, the FY03 Financial Standards was revised to address clarification to standard B9 on its eligible uses of Prop A and C administrative funds. For example, funds taken off the top for the administration of Prop A & C programs should not be expended for regional programs that are operations related, Metro Operations related activities.

In September 2002, staff reported that the June 2002 revisions to the Financial Standards resulted in the $10.7 million reclassification of regional costs from the General Fund to the Enterprise Fund and the reprogramming of funding from Propositions A and C Administrative Funds to Proposition C 40%. The Municipal Operators (Muni’s) have requested that all Proposition C 40% funds used for bus operations be “fair shared” with them. At the Board’s request, the Muni’s portion ($3.854M) was programmed to the Universal Fare System Project for implementation of the Regional program.

In January 2003, the Board approved minor clarifications to the FY03 Financial Standards and updated the sales tax forecast numbers for the development of the FY04 budget as well as capital plan.

Key changes made to the FY05 Financial Standards were the additions of service planning assumptions for bus operations based on 2.1% annual ridership growth and 2.5% annual growth in rail passenger demand. Other changes include the annual sales tax forecast for development of the FY05 budget was increased from $565.8 million to $595.0 million for Prop A and from $565.7 million to $594 million for Prop C, consistent with the 10 Year Forecast dated July 2003.

In Fiscal Year 2006 the Financial Standards were amended in the following areas:

- **General - G2**: An independent certified public accounting firm shall perform an examination of the agency’s consolidated financial statements (including Single Audit requirements) and retirement plan financial statements on an annual basis. The goal is to receive an unqualified opinion on the financial statements and an opinion that the agency is in compliance with Federal Single Audit requirements in all material respects and to receive the Government Finance Officers Association (GFOA) award for excellence in financial reporting.

- **General G9**: The annual budget establishes the legal level of appropriation. The budget shall include operating, capital, regional funding, and other components necessary to implement the policy directions contained in previously Board adopted longer-term plans, i.e., Long Range Transportation Plan and Short Range Transportation Plan. Appropriations for the opening budget lapse at the end of one year. Appropriations for the capital and regional funding budgets are approved on a life of project basis. The budget shall be prepared in a fashion to clearly describe the projects and programs contained therein and to receive the
GFOA award for excellence in budgetary presentation.

- General - G12: The agency shall maintain a cost-effective system of internal control to adequately safeguard assets. In assessing the internal control system, management must weigh the cost of control against the expected benefit to be derived from its implementation. Management will develop a risk assessment and an audit plan each year simultaneously with the adoption of the annual budget and present it to the Board. Recommendations for improvements to the system of internal controls are requirements of the various regularly scheduled and specifically directed audits that are performed in accordance with generally accepted governmental auditing standards. These recommendations, management’s action plans and progress toward implementation will be reported to the Board’s Executive Management and Audit Committee on a regular basis.

- Business Planning Parameters - B1: Sales tax revenue forecasts shall be based on the 20 year historical growth in Los Angeles County taxable sales, which is currently 4.1%.

- Business Planning Parameters - B2: Passenger revenue forecasts shall be derived from historical actual revenues. During periods affected by actual or proposed fare structure changes, the impacts on ridership and average fare forecasts shall be estimated conservatively. The Board will review and update the fare policy on a regular cycle, at least each 5th year since prior review and approval. From time to time, management may propose fare modifications to achieve transit ridership improvements and subsidy per passenger targets (see B4) and to maintain financial viability.

- Business Planning Parameters – B3: It is our long-term strategy to maintain a reasonable subsidy per passenger ratio (operating expenses, excluding depreciation, minus operating revenues divided by passenger boardings). However, with the additional consent decree costs with no corresponding increase in passengers, subsidy per passenger has grown as follows:

<table>
<thead>
<tr>
<th>Subsidy Per Passenger</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>FY02 Actual</td>
<td>$1.43</td>
</tr>
<tr>
<td>FY03 Actual</td>
<td>$1.55</td>
</tr>
<tr>
<td>FY04 Actual</td>
<td>$1.75</td>
</tr>
<tr>
<td>FY05 Budget</td>
<td>$1.56</td>
</tr>
<tr>
<td>FY05 Projected</td>
<td>$1.64</td>
</tr>
<tr>
<td>FY06 Projected</td>
<td>$1.69</td>
</tr>
</tbody>
</table>

- Business Planning Parameters - B4: The Board desires to steadily improve efficiency over time. For agency operated bus and rail service, cost per revenue vehicle service hour (measured separately for bus and rail) may not increase more than the projected rate of inflation for the Los Angeles area plus the incremental costs associated with the addition of new services, programs, and/or facilities as approved by the Board.

- Business Planning Parameters - B5: Service planning assumptions for bus operations will be based upon
demonstrated needs as defined through the 5 Year Short Range Plan.

➢ Business Planning Parameters - B6: Staffing for FY 2006, measured in Full Time Equivalents (FTE), will be held to or below the FY 2005 level adjusted for service expansion or other new scope that has been approved by the Board.

➢ Business Planning Parameters - B8: The capital plan covers the agency’s assets including major transportation infrastructure projects, i.e., Bus Rapid Transit, Light Rail Transit, bus maintenance facilities and is included in each annual budget. The capital plan shall include funding for asset replacement and expansion projects. Capital projects in excess of $5 million shall be presented separately for life-of-project approval by the Board. Capital projects with life-of-project budget changes that cause the project to exceed $1 million or if the change exceeds $1 million shall be presented to the Board for approval.

In June 2006, the Board noted that serious challenges remain for Metro to both address the bus operating and capital structural deficit and to develop a fiscally responsible FY07-08 budget. To better meet these challenges, the Board passed a motion directing the CEO to report back with an analysis of and recommendations for a number of proposed changes in fiscal policy.

In October 2006, staff presented to the Board, its analysis of the Board motion on fiscal policy improvements and discussed its proposal for Financial Stability Policy which incorporates revisions and additions to the existing Financial Standards Policy adopted in February 2002, including various changes consistent with the Board motion. Board members provided feedback and the proposed policy have been revised to include those requests and recommendations.

In January 2007, the Board approved the Financial Stability Policy which superseded the previously Board approved Financial Standards.

Last Board Action

January 24, 2008 – Financial Stability Policy

The Board approved on consent calendar

A. Adoption of the Modifications to the Financial Stability Policy.

Attachments

A. Summary of Changes to the Financial Stability Policy

B. Revised Financial Stability Policy

See Related

Annual Budget
Audit Plan
Debt Policy
Investment Policy
Interest Rate Swap Policy
## Attachment A: Summary of Changes

<table>
<thead>
<tr>
<th>Location in Policy Doc</th>
<th>Reason for Change</th>
<th>Proposed Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Policy Statement</td>
<td>Remove reference to a specific year since policy is updated each year.</td>
<td>Additional financial guidance is found in the Business Planning Parameters and Debt Parameters adopted in FY2006-07 and included with the Financial Stability Policy.</td>
</tr>
<tr>
<td>Paragraph 2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial Goals</td>
<td>No longer required.</td>
<td>Delete Reserved designation and renumber remaining goals.</td>
</tr>
<tr>
<td>G4, G5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial Goals</td>
<td>Identify specific fund source for reserves.</td>
<td>Establish and maintain reserves—General Fund balances equal to 5% of the operating budget to ensure that Metro can adjust to economic downturns, extraordinary cost increases and other financial emergencies.</td>
</tr>
<tr>
<td>G4</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategy</td>
<td>Clarify that the strategy applies to both bus and rail. Clarify the performance measure.</td>
<td>Endeavor to keep growth in regional bus and rail operating expenses (as measured by a rolling average of growth in bus and rail operating cost per vehicle service hour) at or below the rate of inflation.</td>
</tr>
<tr>
<td>S3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategy</td>
<td>Advise the Board of the actions taken to reduce expenditures to achieve a balanced budget.</td>
<td>A proposed strategy for mitigating expenditures will be presented to the Board at the time of adoption. The proposed budget presented to the Board for adoption will include a summary of actions taken or proposed to reduce expenditures.</td>
</tr>
<tr>
<td>S3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategy</td>
<td>No longer required.</td>
<td>Delete Reserved designation and renumber remaining strategies.</td>
</tr>
<tr>
<td>S14-S19</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategy</td>
<td>Delete S21 as it duplicates G4.</td>
<td>Maintain a 5% operating reserve to be used in times of significant revenue decline to preserve the region’s ongoing ability to deliver safe and reliable service to the customer and to reinvest in capital.</td>
</tr>
<tr>
<td>S21</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Location in Policy Doc</td>
<td>Reason for Change</td>
<td>Proposed Change</td>
</tr>
<tr>
<td>------------------------</td>
<td>------------------</td>
<td>-----------------</td>
</tr>
<tr>
<td>General Fiscal Policies F4</td>
<td>Add this new General Fiscal Policy statement to clarify that the Financial Stability Policy is Metro's financial guidance policy.</td>
<td>The policies and procedures described herein shall be known as the Financial Stability Policy and shall supersede all other financial policies previously adopted by the Board.</td>
</tr>
<tr>
<td>General Fiscal Policies F5</td>
<td>Grammar change.</td>
<td>...The Metro shall make annual contributions that when combined with employee contributions, fund actuarially computed costs as they accrue.</td>
</tr>
<tr>
<td>General Fiscal Policies F8</td>
<td>Grammar change.</td>
<td>...Such funds are generally available for appropriation in the a subsequent budget cycle in accordance with their ordinance designations.</td>
</tr>
<tr>
<td>General Fiscal Policies F9</td>
<td>Modify to reflect Board calendar and schedule.</td>
<td>...By December January of each fiscal year, the board shall review and approve the Financial Stability policy that will be used by management as a framework for developing the following year's budget. By February, the Board and will establish the Business Planning Parameters including farebox recovery ratio...</td>
</tr>
<tr>
<td>General Fiscal Policies F9</td>
<td>Add language to clarify that differences between the proposed budget book and adopted budget do not require separate Board approval.</td>
<td>Budget amendments approved by the Board at the time of or prior to budget adoption shall be incorporated into the final budget document with no further Board approval required.</td>
</tr>
<tr>
<td>General Fiscal Policies F10</td>
<td>Correct language.</td>
<td>Appropriations for the capital and regional-funding budgets are approved on a life-of-project basis...</td>
</tr>
<tr>
<td>General Fiscal Policies F11</td>
<td>No longer required.</td>
<td>Delete Reserved designation and renumber remaining policies.</td>
</tr>
</tbody>
</table>

Financial Stability Policy and FY09 Business Planning Parameters
<table>
<thead>
<tr>
<th>Location in Policy Doc</th>
<th>Reason for Change</th>
<th>Proposed Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>General Fiscal Policies F12</td>
<td>Revised to reflect current process.</td>
<td>Annually, Metro shall adopt a five-year (short-range) transit plan for Los Angeles County. The plan will include service levels and ridership by mode for each of the years. The five-year plan will also identify the capital investment needs to support the existing regional system and regional service expansion. The SRTP will incorporate the first five years of Metro's ten-year forecast which includes a hierarchy of strategies that are to be implemented when Metro's financial stability is threatened and strategies required to eliminate any potential deficit. Metro shall periodically develop and adopt a Short Range Transportation Plan (SRTP) for Los Angeles County. The SRTP identifies Metro's priorities for implementing major capital projects in the near term (usually over a five or six year period), and identifies project implementation schedules and available funding.</td>
</tr>
</tbody>
</table>

**FY2008-2009 Business Planning Parameters**

<table>
<thead>
<tr>
<th>BPP B3</th>
<th>Reserved.</th>
<th>The farebox recovery ratio assumed for the FY09 budget is 27.7% with a fare revenue per boarding of $.67.</th>
</tr>
</thead>
<tbody>
<tr>
<td>BPP B4</td>
<td>Revised to reflect current process.</td>
<td>...The projected incremental cost impact on cost per revenue vehicle hour of new services, programs, and/or facilities shall be presented to the board for approval as part of the annual update of the SRTP each year during the annual budget process.</td>
</tr>
</tbody>
</table>

Financial Stability Policy and FY09 Business Planning Parameters
<table>
<thead>
<tr>
<th>Location in Policy Doc</th>
<th>Reason for Change</th>
<th>Proposed Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>BPP B5</td>
<td>Revised to reflect FY09 goal.</td>
<td>Service planning assumptions for bus operations will be based upon demonstrated needs as defined through the five-year Short Range Plan and approved by the Board. Ridership is expected to grow by 2.5% in FY09.</td>
</tr>
<tr>
<td>BPP B6</td>
<td>Revised to reflect FY09 goal.</td>
<td>Staffing for FY08 FY09, measured in FTE's, will be held to at, or below, the FY07 FY08 level, adjusted for service expansion or other new scope that has been approved by the Board.</td>
</tr>
<tr>
<td>BPP B8</td>
<td>Revised to clarify original Board intent in Financial Standards.</td>
<td>...Capital projects in excess of $5 million shall be presented separately for life-of-project budget approval by the Board prior to inclusion in the annual budget.</td>
</tr>
<tr>
<td>Debt D3</td>
<td>No longer required.</td>
<td>Delete Reserved designation and renumber remaining policies.</td>
</tr>
</tbody>
</table>

Financial Stability Policy and FY09 Business Planning Parameters
Financial Stability Policy

Policy Statement

We have an important responsibility to the taxpayers of Los Angeles County to prudently manage our long and short-term finances. In time of economic change and uncertainty, it is especially important for us to ensure our ability to deliver safe, quality and reliable transportation services that are based upon a strong and stable financial foundation.

The Financial Stability Policy is divided into three sections: Goals, Strategies, and General Fiscal Policies. Additional financial guidance is found in the Business Planning Parameters and Debt Parameters. The purpose of the policy is to ensure that we prudently manage our financial affairs, establish appropriate cash reserves, limit the level of debt that may be incurred, ensure that the debt assumptions are based on financial parameters similar to or more conservative than those that would be placed on us by the financial marketplace and to provide management with a framework for developing the upcoming year’s budget and other longer range financial plans and establishing future business targets for management to achieve.

Financial Goals

G1. Maintain public safety on our bus and rail system as the top priority.

G2. Maintain an operating and capital financial base that is sufficient to deliver safe, quality transportation improvements and transit service efficiently and cost-effectively to meet the levels of demand.

G3. Continuously improve productivity.

G4. Establish and maintain General Fund balances equal to 5% of the operating budget to ensure that we can adjust to economic downturns, extraordinary cost increases and other financial emergencies.

G5. Maintain the highest possible credit rating and reputation for prudent financial management.

FY2008-2009 Financial Strategies

S1. We give top priority to funding of public safety on our bus and rail system. Present the details of the safety and security budget to the Board of Directors for separate approval at the time of annual budget adoption.

S2. Adjust transit operating expenses as needed to reflect changes in service demand, technology, productivity and revenue availability.
S3. Endeavor to keep growth in regional bus and rail operating expenses (as measured by growth in bus and rail operating cost per vehicle service hour) at or below the rate of inflation. The proposed budget presented to the Board for adoption will include a summary of actions taken or proposed to reduce expenditures.

S4. New programs proposed for Board adoption will include a cost recovery analysis to determine the cost of implementing the program in measurable terms.

S5. Departments who provide services to the public or outside entities will perform a cost recovery analysis during the fiscal year budget process and make the information available as part of budget adoption.

S6. Any capital project savings above $200,000 must return to the Board for approval prior to the reprogramming or transfer of funds to other projects or programs.

S7. Implement technology and productivity advancements designed to reduce or avoid increasing operational costs.

S8. Explore greater efficiency, effectiveness and ways to increase ridership.

S9. Work to increase and optimize ridership on our system through partnerships that foster transit-oriented development and improve access to the system.

S10. Regularly review productivity improvement programs and results as part of the annual budget process.

S11. Adopt an annual budget that includes an allocation to capital programs adequate to meet annual baseline reinvestment needs for projects and programs which are essential to ensure system performance.

S12. Pursue grant funding for capital projects pursuant to the priorities as addressed in the Long Range Transportation Plan, Short Range Transit Plan, and Five-Year Capital Improvement Program.

S13. Use debt financing prudently to leverage local, regional, state and federal funding for major cyclical capital investments, such as, transit vehicles, facilities, fare collection equipment, and train control renovation and replacement.
S14. Increase revenue from other sources such as advertising, parking, concessions, and joint development while meeting customer needs and providing safe, reliable service.

**General Fiscal Policies**

F1. Complete and accurate accounting records shall be maintained in accordance with Generally Accepted Accounting Principles as promulgated by the Government Accounting Standards Board. The fiscal year-end for financial reporting purposes shall be June 30.

F2. An independent certified public accounting firm shall perform an examination of our consolidated financial statements (including Single Audit requirements) and retirement plan financial statements on an annual basis. The goal is to receive an unqualified opinion on the financial statements and an opinion that we are in compliance with Federal Single Audit requirements in all material respects and to receive the government Finance Officers Association (GFOA) award for excellence in financial reporting.

F3. Funds shall be invested within the guidelines of the Board’s approved Investment Policy and in compliance with applicable state law, California Government Code Section 53600 et seq.

In accordance with the Investment Policy, the Board shall approve the Financial Institutions Resolution that designates the officials empowered to open, close, or authorize changes to accounts and authorizes the officials to designate individuals as Official Signatories for financial accounts.

F4. The policies and procedures described herein shall be known as the Financial Stability Policy and shall supersede all other financial policies previously adopted by the Board.

F5. An annual actuarial analysis shall be performed on all our self-administered retirement plans. We shall make annual contributions that, when combined with employee contributions, fund actuarially computed costs as they accrue.

F6. Appropriate insurance coverage shall be maintained to mitigate the risk of material loss. For self-insured retentions, we shall record the liabilities, including losses incurred but not reported, at 100% of the net present value.

The goal is to maintain restricted cash balances in amounts equal to the present value of estimated liabilities but in no event less than the next year’s projected cash outflows. An actuarial review of self-insured liabilities will be made annually.
F7. Since sales taxes are received on a monthly basis, the allocations among the various ordinance categories shall also be recorded monthly. Expenditures against appropriations are limited to cash actually on-hand during the fiscal year.

F8. Sales tax collections received during a fiscal year that are in excess of the sales tax budget for that year shall be reported as unreserved, designated fund balances in the Special Revenue Fund. Excess Local Return monies are disbursed when received. Any other excess balances may only be expended pursuant to Board authorization. Such funds are generally available for appropriation in a subsequent budget cycle in accordance with their ordinance designations.

F9. The fiscal year shall end on June 30 of each year. By January of each fiscal year, the Board shall review and approve the Financial Stability Policy that will be used by management as a framework for developing the following year’s budget and will establish the Business Planning Parameters including farebox recovery ratio, sales tax growth assumptions, and other key performance measurement goals to provide detailed guidance for development of the upcoming annual budget. The Board shall approve the budget by June 30 of each fiscal year. Budget amendments approved by the Board at the time of or prior to budget adoption shall be incorporated into the final budget document with no further Board approval required.

F10. The annual budget establishes the legal level of appropriation. The budget shall include operating, capital, regional funding and other components necessary to implement the policy directions contained in the Financial Strategies Section of the Financial Stability Policy, previously Board adopted longer-term plans such as the Long Range Transportation Plan and the Short Range Transit Plan. Appropriations for the operating budget lapse at the end of one year. Appropriations for the capital budgets are approved on a life-of-project basis. Any allocations of one-time revenues to any program or project will be identified for the Board at the time of budget adoption or budget change and will only be recommended after considering the alternatives of reducing the level of service, reducing the cost per unit of service, reducing the scope of capital projects, deferring capital projects and/or raising fares. Any requests for project or program funding after annual budget adoption will be referred to the appropriate Board committee for Board review and recommendation. The budget shall be prepared in a fashion to clearly describe the projects and programs contained therein and to receive the GFOA award for excellence in budgetary presentation.

F11. A regional long-range (covering at least 20 years) transportation plan for Los Angeles County shall be adopted at least once every five years. For interim years, staff will report on changes affecting the major financial assumptions of the plan and progress toward the implementation of new projects and
programs. The plan update report shall also highlight Board approved actions taken during the interim period that affect the plan outcomes or schedules.

F12. Periodically, a Short Range Transportation Plan (SRTP) for Los Angeles County may be developed and adopted. The SRTP identifies priorities for implementing major capital projects in the near term (usually over a five or six year period), and identifies project implementation schedules and available funding.

F13. A cost-effective system of internal control to adequately safeguard assets shall be maintained. In assessing the internal control system, management must weigh the cost of control against the expected benefit to be derived from its implementation.

Management will develop a risk assessment and an audit plan each year prior to the adoption of the annual budget. The Board's Executive Management and Audit Committee (EMAC), as the audit committee will provide input and approve the audit plan. Furthermore, completed internal audits will be submitted to the Board under separate cover as they are distributed to the Chief Executive Officer.

Recommendations for improvements to the system of internal controls are requirements of the various regularly scheduled and specifically directed audits that are performed in accordance with Generally Accepted Governmental Auditing Standards, the Institute of Internal Auditors Standards for the Professional Practice of Internal Auditing and Information Systems Audit and control Association Information Systems Auditing Standards, where appropriate. These recommendations, management's action plans and progress toward implementation will be periodically reported to the Board under separate cover.

F14. The Board will review and update the Debt Policy annually to ensure that debt assumptions used in financial planning are based on financial parameters similar to, or more conservative than, those that would be placed on us by the financial marketplace.

F15. Retiree Medical Liabilities – The Government Accounting Standards Board has adopted Statement #45 (GASB 45) that is effective for our fiscal year ending June 30, 2008. As defined in the standard, a significant liability recognizing the past and future costs of providing medical and related benefits, other than pensions, to its retirees is required to be recorded. Annually, the actuarially required contribution (ARC) is required to be recorded as an expense. The ARC recognizes the cost of the retiree benefits earned by current employees during the period and amortization of the unfunded past liabilities. GASB 45 does not mandate an entity's approach to setting aside cash to provide the future benefits.
It is our policy to fully fund the ARC, i.e., set aside and restrict the cash. However, since this amount is significantly greater than the current amount needed for these expenditures on the "pay as you go" basis, a separate discussion of this issue will be brought to the Board in setting the upcoming parameters for each upcoming budget year. A greater accounting liability will result when setting aside less cash than the ARC amount. The ARC will be recognized as an expense in the financial accounting system as required by GASB 45.

FY2008-2009 Business Planning Parameters

B1. Sales tax revenue forecasts shall be based on the 20 year historical growth in Los Angeles County taxable sales, which is currently 4.0%.

B2. Passenger revenue forecasts shall be derived from historical actual revenues. During periods affected by actual or proposed fare structure changes, the impacts on ridership and average fare forecasts shall be estimated conservatively.

The Board will review and update the fare policy on a regular cycle, at least each 5th year since prior review and approval. From time to time, management may propose fare modifications to achieve transit ridership improvements and to maintain financial viability.

B3. The farebox recovery ratio assumed for the FY09 budget is 27.7% with a fare revenue per boarding of $.67.

B4. The Board desires to steadily improve service efficiency over time. For our directly operated bus and rail service, cost per revenue vehicle service hour (measured separately for bus and rail) may not increase by more than the projected rate of inflation for the Los Angeles area plus the incremental costs associated with the addition of new services, programs, and/or facilities as approved by the Board.

The projected incremental cost impact on cost per revenue vehicle service hour of new services, programs, and/or facilities shall be presented to the Board during the annual budget process.

B5. Service planning assumptions for bus operations will be based upon demonstrated needs by and approved by the Board. Ridership is expected to grow by 2.5% in FY09.

B6. Staffing for FY09, measured in FTE’s, will be held at or below the FY08 level, adjusted for service expansion or other new scope that has been approved by the Board.
B7. Regional programs such as local return, formula allocation procedure and Call for Projects shall be funded according to the terms of the laws, regulations and/or discretionary procedures approved by the Board.

B8. The capital plan covers our assets including major transportation infrastructure projects, i.e., BRT, LRT, bus maintenance facilities and is included in each annual budget. The capital plan shall include funding for asset replacement and expansion projects. Capital projects in excess of $5 million shall be presented separately for life-of-project approval by the Board prior to inclusion in the annual budget. Capital projects with life-of-project budget changes that cause the project to exceed $1 million or if the change exceeds $1 million shall be presented to the Board for approval.

B9. We apply for and receives discretionary Federal and State funding. Discretionary funding shall be requested for major system expansion projects or extraordinary transit capital needs. (e.g., Bus Rapid Transit, Light Rail Transit or new bus maintenance facilities). Discretionary funding levels shall be estimated by project based on appropriate State and Federal criteria and the likelihood of obtaining approvals.

The Board shall approve all discretionary State and Federal funding requests by project or program each year.

B10. Prop A and C administrative funds are appropriated through the annual budget to pay for activities not required to be accounted for in other funds. The following statements provide guidance for appropriation and use of Prop A and C administrative funds.

**Appropriation**

Up to 5% of Prop A may be appropriated for administrative purposes. The Prop C ordinance allows up to 1.5% to be appropriated for administrative purposes.

All sales tax funds are deposited initially into the various special revenue funds then transferred to the funds designated for expenditure. The Administrative Fund is within the Special Revenue Fund. Administrative Funds are limited to the lesser of appropriations or actual sales taxes received.

Administrative funds must be expended or encumbered within one year after the end of the year of appropriation. Lapsing is accounted for on the first-in, first-out basis. Lapsed Administrative funds, if any, are returned to the Special Revenue Fund at the end of each year for re-appropriation through the next budget process.
Eligible Uses

Administrative activities include the planning, management, execution, use and conduct of the projects and programs funded by Prop A and C funds. Administrative funds may not be used for operating or building the transit system or regional programs that are operations-related.

Following are examples, not an all-inclusive listing, of eligible uses of administrative funds:

- Indirect costs that are not allowable under federal guidelines, OMB Circular A-87, i.e., lobbying, interest expense, bad debt expense, cost of general governance.
- Indirect costs that we elect not to allocate through its annual FTA approved cost allocation plan (CAP) because to do so might burden projects or programs in an inequitable manner.
- Development of planning and programming documents required by federal and state regulations and Board policy.
- Activities that benefit our projects and programs indirectly such as internships, career development, training programs, etc.
- Transportation planning activities including bus, rail, highway and other surface transportation modes.
- Consent decree oversight.

The proposed expenditure programs for these activities will be shown in detail in the annual budget. Actual expenditures will be shown in the comprehensive annual financial report.

Debt

D1. We may not enter into a debt or financing arrangement unless the transaction is in full compliance with all applicable provisions of applicable state and federal laws and the Debt Policy.

D2. Long-term debt may be included in the budget or longer range plans; however, no such debt shall be incurred without the specific approval of the Board.

D3. The average life of debt instruments shall not exceed the average useful lives of the assets financed.

D4. Reserve funds that may be required by the financial markets for each debt issuance shall be maintained. Cash and securities, insurance or surety bonds may fund these reserves. For financial planning purposes, reserve requirements shall be included in the par amount of debt issued.

D5. We shall maintain a legal security structure of liens, agreements, pledged revenues, and other covenants which will be sufficient to secure rating of "A" or better on

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sales tax backed securities and secure A1 or P1 rating on other short-term debt, and, if necessary, to secure credit enhancement from financial institution with a rating of "AA" or better.

D6. Debt service coverage ratio minimums by sales tax ordinance categories are shown in the Debt Policy. For financial planning purposes, those ratios shall not be exceeded in the development of longer-term financial plans.