ALLEGHENY INSTITUTE FOR PUBLIC POLICY

SOLVING THE PORT AUTHORITY'S FINANCIAL PROBLEMS

Grant R. Gulibon., Research Fellow
Jake Haulk, Ph.D., President
Allegheny Institute for Public Policy

Allegheny Institute Report #07-04
June 2007

© by Allegheny Institute for Public Policy. All rights reserved. Note: Nothing written here is to be construed as an attempt to aid or to hinder the passage of any bill before the Pennsylvania General Assembly.

305 Mt. Lebanon Blvd.◆ Suite 208 ◆ Pittsburgh, PA 15234
Phone: 412-440-0079 Fax: 412-440-0085 www.alleghenyinstitute.org

Table of Contents

Key Findings and Recommendations

- In recent years, the Port Authority of Allegheny County's Port Authority Transit (PAT) has regularly faced budget shortfalls. The evidence gleaned from comparisons of PAT operating costs with those of other large United States transit systems clearly demonstrates that operating inefficiency and cost ineffectiveness, not a lack of funding, has been PAT's primary problem.
- The growth of one specific portion of PAT's budget represents a particularly dire threat to its future viability. Between 2003 and 2006, employee benefits spending at PAT rose by 59 percent, from $64 million to $101.5 million—accounting for almost 60 percent of the increase in total PAT operating costs.
- For FY 2006, the total cost of health care for the Port Authority's active employees and retirees stood at $60.6 million, with projections suggesting that by 2012, that figure will double (absent corrective action before that time).
- As 2007 began, PAT announced several tentative steps toward determining how to restructure its operations, as an estimated $25 million deficit loomed for the current fiscal year, with an $80 million shortfall projected for FY 2008. At present, this deficit is to be closed through a combination of service reductions and fare increases.
- A tried and tested solution to the Port Authority's operational inefficiency—competitive contracting of transit services—has been utilized in a number of American cities. However, a number of obstacles must be surmounted in order to even begin to construct a competitive contracting program for PAT.
- The chief federal impediment to competitive contracting is Section 13c of the Federal Transit Act. Section 13c agreements generally mean that an employee who is displaced or loses compensation as a result of a federally funded project can be eligible for a monthly dismissal or displacement allowance for a period equal to the employee's length of service, not to exceed six years.
- At the state level, the main obstacle to reform of the Port Authority is the Pennsylvania Second Class County Port Authority Act. The Act made the Port Authority the sole provider of mass transportation service in Allegheny County and anyone wishing to provide such service must obtain the Authority's permission to operate.
- There are several measures available to state and local policymakers that will produce incremental cost-saving and service-preserving changes at the Port Authority and which surmount or correct the major obstacles to reform. These include; (1) adopting a permanent hiring freeze and beginning to competitively contract routes at the rate of employee attrition; (2) accelerating attrition by offering buy outs of current employees' retirement health care obligations to increase voluntary separations;(3) amending the Second Class County Port Authority Act to end PAT's monopoly on mass transit service in Allegheny County; (4) re-opening the current PAT labor contract to get concessions on work rules and compensation; (5) and raising fares while at the same time creating a voucher program to help low-income workers who use transit and, (6) eliminating employee strikes.

Introduction

Since its creation in the mid-1960s, the Port Authority of Allegheny County's Port Authority Transit (PAT) has lurched from financial crisis to financial crisis, all the while failing to meet the goals of reducing traffic congestion, improving air quality, and inducing automobile commuters to abandon their cars and ride buses and rail cars instead. PAT's poor fiscal record and inefficient service has occurred despite generous state and local operating subsidies and massive state and federal investments in transit infrastructure projects. At the same time, the firm opposition of the labor unions representing PAT employees has consistently impeded the implementation of reforms that could have produced improved service at lower costs to taxpayers and riders.

In recent years, PAT's financial condition has steadily worsened, even as ever-more ambitious capital projects designed to increase ridership have fallen short of cost-benefit expectations—even, in one prominent case, before advancing beyond the planning stage. The Authority's primary response has been to seek higher, "dedicated" state subsidies for its operations, while attempting to placate its unions by approving labor contracts with ever more lavish wage and benefit provisions. In particular, the growth of PAT employee and retiree pension and health care costs represent a grave threat to the Authority's current and future fiscal stability. And even on the rare occasion that PAT's management has attempted to wring concessions from its unions in order to reduce costs and better design services, the interference of high-ranking political officials in those negotiations resulted in near-total acquiescence to the unions' demands. The net result has been a situation in which PAT is now planning significant fare increases and service cuts designed to close ever-widening budget deficits.

Nevertheless, there is a tested, successful alternative to the seemingly endless fiscal calamities facing PAT that has been successfully utilized in other American cities (and which is the norm, rather than the exception, in most of the rest of the Western world). Competitive contracting of transit services—under which transit policy (issues such as route design, fare levels, service standards and the like) remains under the control of the public sector, but service providers (public or private) are selected through a bidding process that determines the lowest-cost, most qualified operator—has consistently produced cost savings and improved service where it has been tried. The experiences of other cities and transit systems has, over time, led to the development of a set of successful principles that Allegheny County can utilize to reform PAT.

The following analysis examines how PAT's current precarious financial condition developed, including a brief review of the Authority's lack of operating efficiency and cost-ineffectiveness relative to its peers, and a discussion of the steadily growing problem of employee and retiree "legacy costs." It also spells out some steps that can be taken immediately to address the financial and operations efficiency problems of the Port Authority. Finally, for further reference, it contains an Appendix in which the experiences of other American cities where competitive contracting programs have been implemented over the past several decades are examined in light of their potential applicability to the situation facing the Port Authority.

PAT Operations: Expensive and Inefficient

In recent years, PAT has regularly faced budget shortfalls, with a usual response of increased fares, reduced service, and pleas for a "dedicated" source of funding that Authority officials believe would do a great deal to end its financial problems. However, the evidence gleaned from comparisons of PAT operating costs with those of other large United States transit systems clearly demonstrates that funding has not been PAT's primary problem. Indeed, relative to its peers, PAT has fared very poorly on such performance measurements as bus driver hourly wages, driver cost per passenger trip, and operating cost per trip.[1]

PAT could have reduced those costs by reducing the number of bus trips per hour of service, and this could have been accomplished by running fewer buses at non-peak hours and allowing some "niche" routes to be provided by private contractors with smaller vehicles. The latter alternative, in particular, was (and continues to be) anathema to the Port Authority's unionized workforce—in large part due to the fact that when adjusted for Pittsburgh's cost of living, Port Authority wages have consistently been higher than those of its large urban transit system counterparts.[2]

Another factor driving the increased cost of PAT operations is the fact that while bus operating hours have increased, public transit ridership has been declining in Allegheny County, both among those commuting to work and overall. For example in 1960, 24 percent of workers used transit for their work commute, but by 2000 that figure had shrunk to 10 percent. The concurrent decline of ridership and increase of operating hours translates to fewer passengers per hour, and with overall bus operating costs observed to be rising (heavily influenced by large increases in employee wages and benefits), the result is higher costs per passenger.[3]

A Legacy of Red Ink

While the Port Authority's failure to operate its services cost-effectively and efficiently has contributed heavily to its financial woes, the growth of another portion of its budget represents an even greater threat to its future viability. PAT's operating budget grew by 31 percent (from $243 million to $319 million) between 2003 and 2006—but during the same time period, employee benefits spending at PAT rose by 59 percent, from $64 million to $101.5 million—accounting for almost 60 percent of the increase in total PAT operating costs. In 2003, PAT's ratio of benefits to wages was 48 percent. By 2006, it had

---

[1] Jake Haulk and Frank Gamrat, "PAT Answers Won't Do," Allegheny Institute *Policy Brief*, Vol. 4 No. 44, November 15, 2004.
[2] Jake Haulk and Frank Gamrat, "Port Authority Costs—Round Two," Allegheny Institute *Policy Brief*, Vol. 5, No. 1, January 6, 2005.
[3] Jake Haulk and Frank Gamrat, "Funding Crisis? No, It's a Spending Crisis," Allegheny Institute *Policy Brief*, Vol. 5, No. 6, February 10, 2005.

risen to 74 percent, and benefits accounted for 33 percent of total operating costs (or $30,000 in benefit payments per employee).[4]

The increase in the Port Authority's employee benefit costs has been driven by rising health care premiums, as well as the requirement that the agency raise its pension contributions to make sure that its plans are fully funded on an actuarial basis. Port Authority employees can retire with full benefits and pensions after 25 years of continuous service, and some employees can reach age 55 and retire with full benefits if they meet "certain service requirements" even if they do not have 25 continuous years of service. When fully retired, a Port Authority employee receives 2.25 percent of his average annual compensation over the last four years of service multiplied by the years of continuous service (or an employee may choose the option of using the average of the highest four years of the last eight).[5]

The effect of these rules is that a 55 year-old with 30 years of service could receive 67.5 percent of his average pay during his last four years of service (or the average pay of the highest four years of his last eight). This creates an incentive for workers to increase their overtime usage when close to retirement. In addition, retirees receive lifetime health care benefits (including medical, hospital, prescription, dental and vision benefits, along with Medicare Part B premium reimbursement) at no or significantly reduced cost to retirees. As of FY 2006, there were 3,216 recipients, costing $25.8 million—a figure 79 percent higher than that of 2003—and these costs will only increase in future years as more current employees retire.[6]

For FY 2006, the total cost of health care for the Port Authority's active employees and retirees stood at $60.6 million, with projections suggesting that by 2012, that figure will double (absent corrective action before that time).[7] Authority officials and other state and local observers believe that PAT's health care costs—particularly those for retirees—are the single largest threat to the agency's future viability, and that dramatic cost-saving changes are needed. However, union officials have flatly stated that they will accept no changes to the current system of lifetime, taxpayer and rider-paid health benefits for PAT retirees.[8]

PAT's Current Situation: Steps to Reform Thwarted

Despite its deteriorating fiscal situation, PAT was able to temporarily escape financial "crises" in 2005 and 2006. These crises, however, were not "solved" by any reform on PAT's part, but by the intervention of Gov. Ed Rendell, who used $666 million in "unanticipated" federal money to bail out the Port Authority and its Philadelphia-area

---

[4] Jake Haulk, "Port Authority Employee Costs Gallop Higher," Allegheny Institute *Policy Brief*, Vol. 6, No. 59, November 3, 2006.
[5] *Ibid.*
[6] *Ibid.*
[7] Jim Ritchie, "Port Authority Financial Crisis Resists Fix," Pittsburgh *Tribune-Review*, May 5, 2007.
[8] *Ibid.*

counterpart, the Southeastern Pennsylvania Transportation Authority (SEPTA).[9] But while Gov. Rendell may have "saved" PAT for the short term by providing some stopgap funding, other recent actions on his part set back the implementation of sorely needed long-term reforms of PAT operations.

An Opportunity for Improvement Lost

As negotiations on a new contract with its main labor supplier, the Amalgamated Transit Union (ATU), approached in 2005, PAT management seemed to have internalized their operating cost problems and announced a proposal to begin to deal with them. The proposal outline included higher employee payments toward pensions and health care, a two-year wage freeze to open the contract, and outsourcing 20 percent of bus operations to the private sector—a policy that other transit systems in the United States and around the world have adopted with great success.

Predictably, the ATU responded by stating that competitively contracting any PAT service would be "asking the (union) to give away our work" (ignoring the fact that the work belongs not to them, but to PAT, as well as to the riders and taxpayers who pay their well-above-average salaries and benefits). And those salary and benefit levels are not just well above the standards of transit agencies across the United States, but they also far outpace those of other transit agencies in the Pittsburgh region—several of which contract out their services with private providers.[10]

Despite its tough early negotiating stance, the Port Authority was unable to win the concessions and reforms it sought at the bargaining table. The major factor contributing to its failure was the intervention in the talks of Gov. Rendell and Allegheny County Executive Dan Onorato, who helped the ATU win a contract that guaranteed wage increases for three years, limited employees' health care contributions to just one percent, contained no service cuts or layoffs, and—most importantly—forbade PAT management from contracting out any of its bus operations. As has occurred in past negotiations, the ATU's right to strike, and the leverage over the Pittsburgh area's overall transportation network it provides, tipped the final result in its favor.[11]

2007: PAT Proposes A Dramatic Downsizing

With bolder reform alternatives precluded for the time being, as 2007 began, PAT announced its intention to take several tentative steps toward determining how to restructure its operations, as an estimated $25 million deficit loomed for the current fiscal year, with an $80 million shortfall projected for FY 2008. This deficit was to be closed through a combination of cost reductions and fare increases, and the details of the original plan included a 25 percent reduction in the number of vehicle hours, 400 job

[9] Jake Haulk, "Bus Transit Costs: What's to be Done?", Allegheny Institute *Policy Brief*, Vol. 5, No. 10, March 8, 2005.
[10] Jake Haulk and Eric Montarti, "Three (Big) Cheers for the Port Authority," Allegheny Institute *Policy Brief*, Vol. 5. No. 21, May 26, 2005.
[11] Jake Haulk, "Time to End Transit Unions' Right to Strike," Allegheny Institute *Policy Brief,* Vol. 5, No. 46, November 21, 2005.

cuts, and the elimination of 124 of 213 weekday routes (a 60 percent reduction, but one that, according to PAT, would result in just an 11 percent drop in ridership).[12]

Most of the routes originally targeted for elimination by PAT had fewer than 300 daily riders, suggesting that they might be better served by smaller vehicles running less frequently.[13] However, union intransigence and political interference have largely prevented such an initiative, as PAT's labor contract specifies that the number of small transit vehicles (STV) that can be used to replace "fixed route service" cannot exceed 3 percent of the total number of large buses in use during peak hours. As a result, while PAT has 80 smaller buses, they are mainly used in low-density areas not served by existing PAT fixed routes. PAT's wage rates for STV drivers are lower than those paid to the operators of large buses, and maintenance has been outsourced for those vehicles at a savings of $7 million annually. However, despite these savings, the relatively small size of the STV fleet means that it has little effect on the Port Authority's overall costs.[14]

Other Port Authority routes originally targeted for elimination had much higher ridership figures, but were selected due to cost considerations, and many of those (as well the less traveled routes slated for elimination) were suburban routes. One alternative to eliminating these routes totally would be to cut back the number of trips, thus reducing the cost per rider. Others might include combining routes, using smaller vehicles, and decreasing non-rush hour frequency. Finally, the Port Authority could and should make fares for those routes commensurate with trip length.[15]

Opposition to the Port Authority's original plan was voiced in the usual quarters (transit advocacy groups and the unions), so in early March 2007, a revised plan was announced that called for service changes to take place in three phases, beginning on June 17. Phase 1 would reduce fixed-route service hours by 15 percent, rather than 25 percent, and would eliminate 29 of the 213 weekday routes, rather than 124. Phase 2 would begin on September 2 and would reduce service by an additional 10 percent if the PAT budget deficit was not eliminated by that date. Finally, Phase 3 would start on January 1, 2008, and would include fare increases for fixed routes. Two possible plans for the fare increases have been floated—one for a flat $2 fare, and another that would keep the "zone structure" and raise the base fare from $1.75 to $2.50. All in all, PAT anticipated a 4 percent ridership loss under the revised plan.[16]

[12] Jake Haulk and Eric Montarti, "The Long-Awaited Restructuring of the Port Authority," Allegheny Institute *Policy Brief*, Vol. 7, No. 2, January 9, 2007.
[13] *Ibid.*
[14] Jake Haulk and Eric Montarti, "Union Contract Constraints on the Use of Small Buses," Allegheny Institute *Policy Brief*, Vol. 7, No.8, February 22, 2007.
[15] Jake Haulk and Eric Montarti, "The Long-Awaited Restructuring of the Port Authority," Allegheny Institute *Policy Brief*, Vol. 7, No. 2, January 9, 2007.
[16] Rochelle Hentges, "Port Authority Revises Plan for Fare, Service Changes," Pittsburgh *Tribune-Review*, March 23, 2007.

Real Reform of the Port Authority: Opportunities and Obstacles

In the face of the Port Authority's exorbitant "legacy costs," operational inefficiency, and poorly conceived capital investment decisions, simply maintaining the status quo is an unsustainable option. What is needed is a process by which PAT's current operating and capital costs can be reduced through a "right-sizing" of the system to meet the actual mass transit needs of present-day Allegheny County, and which also limits the "legacy cost" obligations—namely pension and retiree health care expenses—it will be facing in future years.

A tried and tested solution to the Port Authority's operational inefficiency—competitive contracting of transit services—has been utilized in a number of American cities (and is the rule, rather than the exception, in much of the rest of the Western world). The Appendix to this report discusses in detail how competitive contracting works and examines the guiding principles of successful programs. However, of most immediate concern with regard to the Port Authority's situation are the obstacles that must be surmounted in order to even begin to construct a competitive contracting program for PAT. The following sections examine these obstacles in greater detail.

Barriers to Competitive Contracting

In the United States, the federal government exerts a great deal of influence over state and local transit policy, in that it not only provides a large share of transit funding, it also imposes mandates on transit operations. Most onerous among these mandates are the labor protection requirements imposed under Section 13c of the Federal Transit Act—requirements that represent far more generous provisions than those available to other private or public sector workers.[17] The following section describes Section 13c's impact on potential transit competitive contracting programs in greater detail.

What is Section 13c?

The Federal Transit Act states "the condition of existing transit workers (shall) not be diminished through transit projects initiated with federal funds." Therefore, any events resulting from federal assistance that cause a change in operations or organization are subject to this provision, including the use of funds to "acquire, improve or operate" a transit system. Section 13c of the Act generally requires that provisions addressing five specific instances be included in transit employee "protective arrangements":

- The preservation of rights, privileges and benefits under existing collective bargaining agreements.
- The continuation of collective bargaining rights.
- The protection of employees against the worsening of their positions with respect to their employment.
- Assurances of employment to employees of acquired mass transportation systems.

[17] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.

- Priority of re-employment to those workers laid off or terminated, as well as paid training or retraining programs.[18]

In grant applications to the federal government, transit agencies must estimate the impact on their employees and specify proposed protections. The Federal Transit Administration (FTA) then forwards the application to the United States Department of Labor (DOL), which is authorized to determine whether or not treatment of employees is "fair and equitable." DOL refers most applications that do not involve routine replacement of equipment or facilities to unions representing system employees. DOL encourages management and unions to negotiate acceptable employee protections, and does not mandate specific protections unless the parties are not able to agree, or if the negotiated provisions do not, in DOL's view, meet the requirements of Section 13c.[19]

While terms of Section 13c agreements vary, they generally include protections against a worsening of employee conditions—meaning that an employee who is displaced or loses compensation as a result of a federally funded project can be eligible for a monthly dismissal or displacement allowance for a period equal to the employee's length of service, not to exceed six years.[20] A displacement allowance pays an affected employee the difference between the wages in his current position and the one from which the employee was removed, while a dismissal allowance pays the employee the full wage for the position the employee lost.

To illustrate the potential magnitude of such payments for a transit authority, consider the following example drawn from an ultimately unsuccessful effort to competitively contract a portion of the Boston-based MBTA's bus service:

- MBTA research indicated that private contractors typically hired 70 to 90 percent of the employees of the former public monopoly provider.
- MBTA assumed that the contractor would hire 85 percent of the 628 employees that would have been affected by one particular contract "bundle," thus leaving 109 potentially without jobs.
- MBTA estimated that it would have been able to reassign 57 of those 109 employees to other vacancies within the agency, leaving 52 employees to be laid off (and therefore subject to Section 13c protection). This meant that a laid-off bus driver who had been earning $3,000 per month with MBTA and subsequently found a new position at $2,000 per month would have been able to claim a "displacement allowance" of $1,000 per month for as long as six years under the terms of Section 13c (or a "dismissal allowance" of $3,000 per month if he had not found a new position). The estimated cost of paying all 52 employees a displacement allowance of $1,000 per month for the full six years would have been $3.744 million, while paying all 52 a dismissal allowance of $3,000 per month for the full six years would have cost an estimated $11.232 million.

[18] United States Department of Labor, "Fact Sheet on Protections for Transit Workers," Transportation Research Board (1995), Government Accountability Office (2000).
[19] *Ibid.*
[20] *Ibid.*

- To try to minimize its potential Section 13c liability, MBTA developed a layoff process that would have first targeted low-seniority employees. MBTA estimated that by using this procedure, its Section 13c liability would have been between \$2.9 million and \$4.3 million.[21]

To illustrate the Port Authority's potential Section 13c liability if it were to contract a portion of its bus system at a rate faster than employee attrition, consider an example in which a contracting initiative would be projected to leave 100 bus operators to be laid off, and in which 50 of those 100 could be reassigned to other open positions within the Authority. In such a case, 50 operators would be laid off and subject to Section 13c protection. Assuming that each of those 50 drivers earns at the Port Authority average hourly rate of \$20.82[22], this would translate to a monthly base salary of \$3,608.80 for each operator. If each of those drivers had at least six years of service and was not able to subsequently find other employment, PAT could face a dismissal allowance liability of just under \$13 million over the six-year period immediately following such layoffs.

Now, further assume that each of those 50 former PAT bus operators was able to find new employment, but with a monthly base salary of \$2,366 (the figure for bus operators with the nearby Indiana County Transit Authority (ICTA).[23] The difference between the drivers' monthly base salary with PAT and their new monthly base salary would be \$1,242.80, meaning that over a six-year period, PAT could face a displacement allowance liability of just over \$4.47 million.

Thus, for the Port Authority to lay off all drivers and mechanics in order to create outsourcing opportunities could cost in excess of \$600 million in wages alone. Moreover the Port Authority would still face the cost of operating the transit system. In short, this strategy is not a financially viable option.

Mechanics of Section 13c Regulations

Section 13c does not protect employees from either direct or indirect adverse effects not resulting from federal funding, such as changes in the volume and character of employment arising from causes other than the specific federally supported project. If federal funds are used by a transit provider to acquire another transit provider, the employees of the acquired provider must be assured of continued employment with the new provider, and the new provider must preserve all previous rights, privileges and benefits, as well as continue to honor existing collective bargaining rights. Employees of a transit provider not acquired with federal funds who lose their jobs as a result of federal funding must only be given priority of re-employment for any vacant position with any

[21] Robert M. Melia, "Missing the Bus: The Fight to Contract Privately for MBTA Bus Service," *Government Union Review*, Vol. 18, No. 2, July 1998.
[22] Pennsylvania Transportation Funding and Reform Commission, "Transit Agency Operational Audit: Port Authority of Allegheny County," January 2007.
[23] *Ibid.*

employer under the control of the grant recipient, not assured employment (but such employees must be paid a dismissal or displacement allowance as appropriate).[24]

Section 13c also requires the continuation of any collective bargaining rights that were in place when the employer first received federal funds. It does not, however, grant collective bargaining rights to employees who did not have them before the receipt of federal funds. Regarding employees who do not have collective bargaining rights, but who can meet, confer and present grievances under state law or as an ongoing practice, Section 13c mandates that these practices continue.[25]

Subsequent grants to a transit provider are usually based on an existing Section 13c protective agreement. Such agreements can only be changed if one of the parties to the agreement has an objection that "raises material issues that may require alternative employee protections" or "concerns changes in legal or factual circumstances that may materially affect the rights or interests of employees."[26] If DOL finds the objection to be sufficient, it directs the parties to negotiate the items at issue and will certify them if they meet Section 13c standards. If not, DOL will determine appropriate arrangements after all sides have had a chance to submit written arguments. One party in a Section 13c agreement does not have to respond to objections raised by the other, but they are encouraged to discuss any such issues as soon as possible. The parties have a 15-day review period in which this may take place, and the DOL has 10 days afterward to consider any objections filed. DOL may consider comments or objections in determining their sufficiency.[27]

Section 13c requires that protections apply to *all* transit employees in the service area of the federally funded project. This further requires that protective arrangements be in place for the grantee's employees, for employees of any contractors of the grantee providing transit services, and those of other mass transit providers in the service area. Indeed, Section 13c provisions apply to grantees where neither their employees nor those of any other transit provider in the area are represented by a union, and in such a case, the DOL has a "non-union certification" that provides the employee protections. For grantees whose employees are represented by a union, "substantially equivalent" protections must be provided to all non-union employees in the service area.[28]

For the purposes of Section 13c, the "service area" is defined as "the geographic area over which the project is operated, adjacent areas, and the area whose population is served by the transportation project receiving federal funds."[29] If one transit system

---

[24] United States Department of Labor, Employment Standards Administration, Office of Labor-Management Standards, "Compliance Assistance—Employee Protections Under the Federal Transit Law," 49 USC, 5333(b) (formerly identified as Section 13c of the Federal Transit Act).
[25] United States Department of Labor, Employment Standards Administration, Office of Labor-Management Standards, "Compliance Assistance—Employee Protections Under the Federal Transit Law," 49 USC, 5333(b) (formerly identified as Section 13c of the Federal Transit Act).
[26] *Ibid.*
[27] *Ibid.*
[28] *Ibid.*
[29] *Ibid.*

connects to or competes with another, employees of the second system are considered to be in the service area of the project. If a transit system feeds into a facility that serves rail and bus, then the rail and bus employees would be considered service area employees and would be entitled to Section 13c protections. The result in such a case would be that a transit company or authority would end up providing protective arrangements for employees other than its own, and negotiating such agreements with unions even if it does not bargain collectively with its own employees.[30]

Unionized transit employees wishing to file a claim under Section 13c would contact their union representative for a copy of the Section 13c arrangements and for guidance on how to file a claim. Non-union employees can obtain the necessary information from the grant recipient. There are procedures in place in the event that a transit provider disputes a claim. However, unions cannot block the certification of a pending grant because of an impasse in collective bargaining negotiations or a number of outstanding grievances. At the same time, the re-negotiation of a Section 13c agreement cannot be justified on this basis.[31]

Section 13c protections must be in place even if a federally funded project will not harm transit employees, as such protections must be in place and certified by DOL before federal funds can be released. To reduce the likelihood that they will be liable for Section 13c claims, transit agencies can reduce personnel through attrition or offer employees work in other jobs with equal or better pay and working conditions, retraining them if needed. Simply put, changes that minimize the adverse impact on employees mean that the transit provider can minimize the likelihood of claims.[32]

Because Section 13c requires that a grant recipient "protect the interests of all mass transit employees in the service area of the federally funded project" (including those of its contractors and employees of other transit providers in the service area), if none of these employees are unionized, DOL will certify grants according to the terms of the "non-union certification." But if any employees in the service area are unionized, a "non-union certification" cannot be used, and the union must be allowed to help develop the Section 13c arrangements. This process, however, does not create a collective bargaining relationship between a union and a grant recipient if one does not already exist.[33]

Impact of Section 13c on Competitive Contracting

Overall, Section 13c discourages innovations that could reduce transit costs, such as competitive contracting. It is estimated to add as much as $2.5 billion to the annual cost of United States transit services, and in so doing it effectively serves as an unfunded federal mandate. Because of Section 13c, agencies that have implemented competitive

[30] United States Department of Labor, Employment Standards Administration, Office of Labor-Management Standards, "Compliance Assistance—Employee Protections Under the Federal Transit Law," 49 USC, 5333(b) (formerly identified as Section 13c of the Federal Transit Act).
[31] *Ibid.*
[32] *Ibid.*
[33] *Ibid.*

contracting have largely done so by limiting the rate of that implementation to the natural rate of employee attrition (although Denver was able to competitively contract at a faster pace by continuing to pay redundant workers until attrition opened up new positions). However, the effect of past United States Department of Labor interpretations of Section 13c favoring labor unions has been to discourage many transit agencies from even attempting competitive contracting,[34] in that Section 13c requires that "for any public agency to receive federal transit grants, the labor rights, privileges and benefits have to be preserved and continued."[35]

If Section 13c is interpreted in such a way as to prevent transit agencies from utilizing competitive contracting as a tool to rein in labor costs, there is little incentive for politicians and taxpayer advocates to fight the necessary battles to implement and sustain such programs. However, it is important to note that in the cases of Denver, Houston, Los Angeles and San Diego, Section 13c was not invoked by the unions, largely due to the fact that the competitive contracting programs for those cities were carefully designed to avoid layoffs or other actions that could be construed as a "worsening" of working conditions. Contracts were bid out for new bus lines, and existing routes were competed out at a rate that would accommodate the normal rate of attrition for drivers in each system.[36]

Political and Other Impediments to Competitive Contracting of Transit Services

At the same time that Section 13c impedes competitive contracting on the labor front, other aspects of the United States' political system present additional obstacles to competition. The separation of powers between the federal and state governments leads to the capture of the system by special interest groups who benefit from increased public transit spending. For instance, legislators of both major political parties, regardless of their overall views on fiscal policy, are constantly scrambling to bring larger and larger shares of federal money back to their home state or district, and they are highly susceptible to pleas from local interests—such as transit agencies—that have the potential to showcase their ability to "bring home the bacon."[37]

Local and state party influence in candidate selection for Congress also tends to make candidates, whatever their positions on federal issues, more likely to support spending projects favored by local interests that may be politically influential. This has been very much evidenced in the saga of the Port Authority's North Shore Connector project, as seen in the "use them or lose them" attitude shown in regard to the federal funds promised to it. Also, Congressional opposition to competitive contracting has been solid, due to the Democrats' near-unanimous loyalty to (and heavy dependence upon) labor

---

[34] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[35] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.
[36] *Ibid.*
[37] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.

unions, some Republican support for the positions of organized labor, and the lack of a consistent voice on labor issues from business interests. And when considering the actions of the President or state governors to push for policy reforms such as competitive contracting, most often, the attention that must be paid to local concerns often blunts action for dramatic reforms.[38]

Finally, the influence exerted by those who directly benefit from expanding the size and cost of the public transit industry (labor unions, providers of large capital projects, and other advocacy groups) is much more concentrated than the relatively diffuse influence of those taxpayers who want greater cost savings and better efficiency. As detailed in the Appendix, the failure of many initially successful efforts to facilitate competitive contracting by separating transit policy from operations to withstand persistent union and other attacks is testimony to that fact.

Potential State Barriers to Competitive Contracting at the Port Authority

In addition to the federally related barriers to competitive contracting, any effort to competitively outsource any Port Authority operations would currently be hindered by the Pennsylvania Second Class County Port Authority Act. The Act made the Port Authority the sole provider of mass transportation service in Allegheny County and anyone wishing to provide such service must obtain the Authority's permission to operate. In effect, there is no separation of mass transit policy from operations in Allegheny County.

According to the terms of the Act, the Port Authority has the exclusive right to operate a transit system in Allegheny County, except for those transportation systems which operate into the county in order to pick up and drop off passengers there. Outside transportation systems cannot pick up and drop off passengers entirely within Allegheny County unless the Port Authority agrees to it. In such a case, the Port Authority must be of the opinion that allowing an outside system to operate fully within Allegheny County would be serving the purpose for which the Authority was created. The Authority was also given the power to, by agreement with an existing transportation system now serving the said service area, permit a continuation of such services where, in the opinion of the Authority, the continuation would serve the Authority's purposes.[39]

The Act also notes that the Authority shall not be required to bargain over matters of "inherent managerial policy"—which includes, but is not limited to, such "areas of discretion or policy" as the functions and programs of the Authority, standards of services, its overall budget, utilization of technology, the organizational structure, and selection and direction of personnel. The Authority is required to meet and discuss policy matters affecting wages, hours and terms and conditions of employment, as well as the impact thereon, at the request of the authorized representative.[40] This raises the question

---

[38] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[39] Second Class County Port Authority Act, 1956, April 6, P.L. (1955) 1414, & 13.5.
[40] *Ibid.*

of whether the Act could be interpreted as meaning that the Authority is not required to bargain with its unions over a management initiative to begin a competitive contracting program.

One additional Pennsylvania law that may present some concerns regarding competitive contracting of PAT bus services is Act 195 of 1970—the so-called Public Employee Relations Act (PERA), which governs collective bargaining between public employers (the Commonwealth of Pennsylvania, its political subdivisions, and non-profits and certain other organizations that receive state, federal or local grants or appropriations) and employees. Employees covered under PERA include all of those employed by a public employer except elected officials, gubernatorial appointees, management-level employees, confidential employees, clergy and other religious professions, church office or facility employees, and police and firefighters.[41] In particular, Section 20 of PERA may have implications for the Port Authority.

Section 20 notes that the rights granted to "certain public employees" by three other Pennsylvania laws (or parts thereof) shall not be "repealed or diminished" by PERA. One of those three laws is the Second Class County Port Authority Act, specifically Section 13.2, which not only grants PAT's first-level supervisors collective bargaining rights, but also states that employees of any transit system acquired by the Port Authority cannot be placed in a worse position relative to wages, benefits and working conditions, and that the Authority must make "every reasonable effort" to settle disputes by collective bargaining. While the Port Authority would not be acquiring a new transit system if it were to competitively contract some of its bus routes, it is possible that opponents of contracting might seize upon this provision in an attempt to impede a contracting program.

Action Steps to Take Now For Lasting Port Authority Reform

In light of the aforementioned limitations placed on transit agencies that largely impede significant immediate labor-related cost saving through competitive outsourcing it's obvious improving the financial situation at the Port Authority will require finesse and an incremental approach. That is to say, other than the painful service cuts and employment reductions already planned, there is no statutory prescription for quickly saving money by downsizing operations.

But at some point, continuing to slash service to lower PAT spending because limited funds are increasingly being used to cover retiree medical costs and to pay current union employees overly generous wages and benefits will begin to have a serious, deleterious effect on the region's economy. The retiree health care expenses are constitutionally unavoidable, having been promised to retirees in labor contracts over the years. At the same time, the compensation rates for current employees cannot be lowered unless there are contract concessions by the unions. Based on the previous behavior and recent rhetoric of union leaders, there is little or no possibility of concessions in the near

[41] Pennsylvania Department of Labor and Industry, "Pennsylvania Public Employee Relations Act," http://www.dli.state.pa.us/landi/CWP/view.asp?a=185&Q=182080.

future—even if the Port Authority management asks for a contract re-open, which it seems disinclined to do.

Thus, it is incumbent on County and state officials to pressure the Port Authority to institute doable, incremental cost-saving and service-preserving reform measures. The following are five concrete steps designed to achieve the twin goals of reducing PAT's costs and improving its service efficiency.

Step One: Adopt a Permanent Hiring Freeze and Move to Competitive Contracting

First of all, the Port Authority should announce a permanent hiring freeze. As positions open up due to attrition and retirements, PAT-provided service can be reduced. Routes and runs thus made available should be outsourced to the private sector using a method along the lines of the Denver competitive contracting model discussed in the Appendix. Over time, more and more service can be outsourced to private contractors at significant savings as drivers leave the system. This accomplishes two goals: 1) It improves the cost efficiency of the system overall; and 2) it slows the growth in the number of future retirees who will be owed medical benefits.

Step Two: Offer to Buy Out Current Employees' Retirement Health Care Obligations

The second step should be to determine the discounted present value of future retiree medical expenditures for each active Port Authority employee, based upon age and years of service, and then make buyout offers to employees at a level below that amount but adequate to get some to accept. To the degree this is successful, two things are accomplished: 1) It reduces the future pool of retirees, a key ingredient in solving the Port Authority's financial woes; and 2) it creates more opportunities to outsource still more service with the cost savings that can bring.

It is also important to note that under GASB regulations, beginning in 2008, PAT will have to show unfunded retiree medical obligations on its balance sheet. This liability will undoubtedly be in the hundreds of millions of dollars. So, there is every imperative for PAT to do something now to lower this liability, in that its bond ratings will be negatively affected by the new liability (and its impact on net worth). Therefore, a buyout plan should be evaluated and, if found to be cost-effective, implemented.

A brief look at three examples demonstrates the possible costs of a buyout. First, assume that a 45 year-old driver plans to retire at age 60. For this individual, the present value of the cost of retiree medical benefits is $76,800. This calculation assumes the driver and his/her spouse each live 20 years after his/her retirement at an average cost of $20,000 per year during that period. The discounted value of those premiums from the date of retirement is $211,880. Today's value of $211,880 to be paid 15 years hence is $76,800. All calculations assume a 7 percent discount rate. With a lower discount rate, the present value will be greater, and with a higher discount rate, the present value will be lower.

In the second example, a 50 year-old driver plans to retire at 55. The present value of his/her retiree medical benefits, assuming he/she lives 25 years after retirement, is calculated at $141,000. Finally, in a third example of a 35-year old driver, the present value of retiree medical benefits is $39,000.

Clearly, the "buyout" cost for employees is much lower for the younger workers. Nevertheless, to the extent that 50 year-olds would be willing to accept, for example, $100,000 to walk away from their retiree medical benefits, a buyout would still improve the balance sheet of the Port Authority. In the case described above, this would remove a net of approximately $40,000 in liabilities per driver, assuming the Authority has to borrow the money to pay for the buyout. If the buyout funds could be raised without having to borrow all of the money needed, the liability reduction would be higher.

This plan would require designing an individual offer for each employee. The guideline would be to make buyout offers based on no more than, say, 80 percent of the present value of the medical obligations. As buyouts are successful and employees leave voluntarily with whatever pension benefits they had accumulated intact, the open positions can be used make more routes available for competitive contracting.

It is impossible to estimate how many employees might opt for a buyout. However, as long as the Port Authority continues to grapple with the rising costs of medical care for retirees, it is probable that further cuts in service and workforce will be necessary to make room in the budget for those skyrocketing, unavoidable expenditures. In such an environment (i.e., with the threat of layoffs looming each year), it should be easier to get a higher percentage of workers to accept a buyout.

Of course, the downside is that as employees take buyouts, there will be fewer layoffs needed, but on the other hand, if workers leave voluntarily, their jobs can be replaced with outsourced drivers or mechanics. In the long run, that has the double advantage of helping lower current costs as well as reducing future spending on medical benefits. There is no good reason not to at least offer a buyout program.

Step Three: End PAT's Monopoly on Mass Transit in Allegheny County

The General Assembly should quickly amend the Pennsylvania Second Class County Port Authority Act to strip PAT of its exclusive authority to provide mass transit services in Allegheny County. There is no justification for allowing PAT to be the sole provider in view of the restraints imposed by collective bargaining agreements and the legacy costs and work rules they contain, as well as the limitations on outsourcing imposed by Section 13c of the Federal Transit Act and the potential implications of Pennsylvania's Act 195.

By removing PAT's status as sole provider, other regional transit systems or private vendors could offer transportation service in areas not served by the Port Authority. Private service providers would be required to meet Utility Commission criteria for financial stability and wherewithal, insured, bonded and properly certified drivers and vehicle maintenance. There is no valid reason to prevent people who want bus service and who are willing to pay for it to be deprived of service simply because PAT cannot afford to offer it (owing to cutbacks due to its outlandish cost structure and inefficient operations).

Step Four: Re-Open the Current PAT Labor Contract

PAT management should work to re-open the current union contract and ask for a number of concessions to help reduce Port Authority costs now and in the future. These concessions would include:

1) Wage givebacks and a greater employee contribution to their health care costs.
2) A shift to a defined contribution pension plan for new employees.
3) Relaxation of the contract constraint on the use of smaller buses, a restraint PAT management could have, under Pennsylvania law, refused to accept in the first place. Smaller buses can be used to run circulating collection routes at lower cost, while alleviating traffic on downtown streets.
4) Request union permission to outsource routes that have been eliminated due to PAT's cost-cutting efforts, especially long commuter routes.
5) Relaxation of any other work rules that reduce management flexibility to make optimal and responsive resource reallocation.

Any of these changes would be beneficial in PAT's efforts to improve efficiency and lower its cost per passenger carried.

Step Five: Raise PAT Fares and Create a Voucher Program For Low-Income Workers

Finally, the Port Authority should raise fares significantly and ask the state to help create and fund a voucher plan for low-income workers. Passengers should cover at least 40 percent of the cost of providing service through the fare box. Currently, the fare box contributes about 30 percent of operating expenses. That could mean as much as a dollar more per ride.

To avoid creating an excessive hardship for low-income workers who need public transportation to get to their jobs, the state should divert some of the economic development grant funds that it currently spends on ineffective "job creation" projects to create a fund to underwrite the voucher program. For example, the state could cover up to half the price of a monthly PAT pass. These passes would be means tested and controlled by PAT as the pass issuer.

On the grounds that is better to keep people working if possible, a transit voucher program makes good economic sense. Of course, it would have to be designed to minimize fraud and abuse. But it is time to rationalize the whole fare structure to better reflect the costs of providing and the benefits of using PAT bus service. As cost savings are implemented and take effect, the need for further fare hikes will go down.

Step six: Eliminate the right to strike of drivers and mechanics

There is no meaningful way to address the Port Authority's long term financial outlook without taking away the employees' right to strike. Work stoppages that deny the population a vital public service create tremendous pressure on management and the board to agree to collective bargaining agreements that are financially imprudent. The current crisis is traceable in large part to the strikes and threats of strikes in the past. Pennsylvania's legislature simply must correct this problem if they truly want Philadelphia and Pittsburgh to ever have stable, fiscally sound operations.

Conclusion

None of the steps described above will be easy to implement. Their success depends on a firm commitment on the part of county, state and Port Authority officials to make sure that each reform measure is implemented correctly and enforced vigorously. Yet, if the responsible officials make the commitment to change the way the Port Authority operates its bus system, PAT can replicate the success of other American and international cities that have improved efficiency, cost-effectiveness and service quality of their public transit systems—and state and local taxpayers will finally see an end to the "crisis mentality" that has dominated public transit policy in Allegheny County for far too long.

Appendix: Competitive Contracting of United States Transit Systems

According to a 2004 study, approximately 10 percent of all United States bus service was competitively contracted as of 2001, as is 15 percent of regional suburban rail service. United States competitive contracting of transit services began in the 1970s with demand-responsive systems for elderly and disabled citizens. The Port Authority's ACCESS service is provided in such a manner. In most cases, this work was so small in comparison to other transit services that unions did not oppose these contracting programs. Also, a great deal of school bus service under the control of government entities is competitively contracted.[42]

Most of this contracting of transit services in the United States is occurring in smaller systems, such as the southwestern Pennsylvania-based Mid-Mon Valley Transit Authority and Westmoreland County Transit Authority. One of the main reasons for the relative lack of competitive contracting in the United States relative to the rest of the world is restrictive government regulation, which will be addressed in greater depth in the analysis that follows. In fact, government consolidation of private transit companies into public agency monopolies in the years preceding the decade of the 1970s contributed heavily to the cost problems that would follow, as unions were able to win progressively costlier labor contracts from these newly created government entities.[43]

Since 1970, the United States has more than tripled its expenditures on public transit, and by the 1980s, it was clear that these growing costs had not translated into greater ridership. To bring costs down, some United States public authorities turned to competitive contracting of transit operations, under which the authorities would decide what service would be provided, along with the terms of service and the fares to be charged, but the service operator would have to win the job in competition with other private (and public) transit providers.[44]

A successful competitive contracting program can provide not only cost savings, but also management flexibility to offer new services. A 2001 survey of transit managers conducted by the Transportation Research Board of the National Research Council found that 93 percent of those surveyed stated that their expectations for competitive contracting had been "at least partially met," with a "solid majority" of those saying that contracting "fully met" their expectations. More than half of the managers surveyed reported that "reduced operating costs were among the positive effects of contracting."[45]

A 1989 study found 22 to 39 percent documented savings for situations in which previously publicly provided bus service was subjected to competitive contracting, and as of 1995, a study comparing the cost of competitively provided bus services found a 30

[42] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[43] *Ibid.*
[44] *Ibid.*
[45] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.

percent advantage for competitive contracting.[46] Through the limited contracting programs undertaken for United States fixed-rate bus service, several basic principles have been developed as components of successful contracting programs:

- Bid contracts on a fixed-price basis (such as on a price per revenue hour). If a company can drive its costs under the bid price, it can increase its profit.
- Promote competition by having several contracts for a relatively small group of routes and for a relatively short time period (no more than three years with two one-year options). Making the interval this length would be long enough to avoid repeat transaction costs common to repeated re-bidding, but short enough to maintain competitor interest and discourage contractor complacency.
- Monitor the contractor's performance continuously throughout the contract and enforce contract penalties for substandard performance. Contracts can and do mandate penalties for violations, such as late starts, cancelled runs, unclean buses, and "excessive breakdowns."[47]
- Provide bus contractors with vehicles (and perhaps service facilities). This action can foster competition by reducing capital costs, which are often a substantial barrier to entry for smaller firms, and by making it easier for the public agency to re-take the service in the event of poor contractor performance.[48]
- Above all, a successful contracting program requires that transit policy and transit operations be separated, meaning that the agency overseeing the contracting program should not be bidding on contracts as well. In many cases, a separate policy agency has been set up to administer the contract and enforce service requirements.[49] (This would currently be problematic in the case of the Port Authority, as was discussed in the main body of this report.)

Successful United States Competitive Contracting Programs

The following section outlines the experiences of a number of United States transit systems that have implemented competitive contracting programs. All of them have achieved various levels of success, but many of them have become "victims of their own success," as transit unions and political officials opposed to competitive contracting worked to undermine the program features responsible for that success. These experiences illustrate both the path that the Port Authority can follow to reform and the obstacles that must be surmounted as that path is navigated.

<u>San Diego</u>

In 1979, a relatively lopsided contract settlement in favor of the local public transit union (which contained a driver wage rate of $10 per hour—the highest such wage in the

---

[46] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.
[47] *Ibid.*
[48] *Ibid.*
[49] *Ibid.*

United States at that point) led to rapidly escalating San Diego transit costs. As a response, beginning in 1980 competitive contracting was instituted, and by 2001, competitively contracted costs per kilometer were 40 percent lower than the non-competitive service.[50]

The conversion to competitive contracting in San Diego was aided greatly by an act of the California legislature which placed authority for transit policy with the Metropolitan Transit Development Board (MTDB), rather than the former public monopoly operator, San Diego Transit (SDT). SDT became a subsidiary of MTDB, which coordinated the actions of agencies administering competitively contracted services (including itself). Union employees were not fired as a result of competitive contracting, but were instead "re-allocated to other non-contract routes at the time of contract changes."[51] Upon the first existing San Diego Transit route conversion in 1989, the union did sue, claiming that "the route belonged to San Diego Transit and could not be given away"—a sentiment echoed by the ATU during its most recent contract negotiation with the Port Authority.[52]

Union employees providing transit services under MTDB were contracted with San Diego Transit, not MTDB, and because it was not a transit service provider, MTDB kept substantial authority to implement competitive contracting. However, union-backed 2002 legislation combined SDT into MTDB, thereby recombining policy and operations—and this hindered the conversion to competitive contracting. Still, by 2001, 40 percent of San Diego bus services were competitively contracted, and the operating costs per mile of the competitively provided service were 33 percent below that of San Diego Transit. Overall real bus costs per mile (both competitive and non-competitive) had declined by 30 percent, showing just the threat of competition had exerted some downward pressure on the public monopoly's costs.[53] In sum, San Diego Transit's costs fell by an inflation-adjusted 16 percent from 1979 to 2001, and while overall San Diego operating expenditures increased by 20 percent from 1979 to 2001, service went up by 72 percent, productivity rose 43 percent, and bus ridership increased by 50 percent.[54]

Houston

The Metropolitan Transit Authority of Harris County (Metro) was one of the first public transit agencies in the United States to subject a substantial amount of service to competitive contracting. The contracting program began with the competitive bidding of park-and-ride services in the 1970s, and it was expanded in 1997 with a contract for private operation of an entire bus garage and all services therein. All union jobs were protected in the transition, as Metro became the first public agency to convert an entire

[50] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[51] *Ibid.*
[52] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.
[53] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[54] *Ibid.*

facility (rather than certain routes) to competitive contracting. In 2000, the contractor ran 130 buses providing 12 percent of Houston's service, and reported operating costs 26 percent below those of the public agency.[55]

Los Angeles

In 1977, the Los Angeles County Transportation Commission (LACTC) was created to oversee public transportation policy and control all subsidies, but not to operate transit service itself. Service was provided by the Southern California Rapid Transit District (SCRTD) and eight individual municipal operators, and the collective agreements with their union workforces were with the operators, not LACTC, thus keeping policy and operations separate.[56]

Two years later, the California legislature allowed the creation of "local transportation zones," which gave local and regional communities the power to establish new public transportation districts to competitively contract previous public monopoly services.[57] This led to the 1988 creation of the Foothills Transit Zone, which, as of 2000, had 231 contracted buses running more than a dozen routes in the San Gabriel Valley and were operating at a unit cost 42 percent lower than the publicly operated lines of the Los Angeles County Metropolitan Transportation Authority (LA Metro). In addition, the Los Angeles City Department of Transportation also contracted out several former SCRTD routes, and as of 2000, those routes had 131 buses running at a per-hour cost 39 percent below that of the public agency. Finally, when LA Metro contracted out some of its "high-subsidy" routes to private carriers, 129 buses were operated in peak service at a 40 percent cost savings over the LA Metro fully public lines.[58]

However, in the early 1990s, local political officials prevailed upon the California legislature to combine LACTC and SCRTD into LA Metro, claiming that the two agencies were wasteful and duplicative. The merger ended the "separation of policy and operations" that had made the contracting initiative so successful, and it led to significant cost escalation (both in terms of operating and capital costs).[59]

San Francisco

As of 2003, 15 percent of the transit service in the San Francisco Bay area was competitively contracted among several transit agencies. The largest contract was with

[55] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.
[56] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[57] *Ibid.*
[58] E.S. Savas and E.J. McMahon, "Competitive Contracting of Transit Services: A Better Deal for Riders and Taxpayers," Center for Civic Innovation at the Manhattan Institute, Civic Report No. 30, November 2002.
[59] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.

San Mateo County Transit, which has services that go into downtown San Francisco. Overall, competitively provided costs were 44 percent lower than those of the public monopoly agencies.[60]

Dallas-Fort Worth

As of 2003, the largest competitively contracted transit operation in the United States was under Dallas Area Rapid Transit (DART), with 34 percent of service competitively contracted at a 42 percent savings over in-house services. However, the high cost of DART's suburban and express rail systems created pressure to cut the bus system.[61]

Minneapolis-St. Paul

In 1983, the Minnesota legislature established "separation of policy and operations" for Minneapolis-St. Paul public transit. The Regional Transit Board (RTB) was to regulate, not provide services, which were under the existing public sector monopoly agency, the Metropolitan Transit Commission (MTC), and serve as the coordinating agency for municipal governments, itself, and other agencies competitively contracting transit services. The collective bargaining agreement with the MTC unions remained with MTC, not RTB, and in this way, RTB could implement competitive contracting programs without running afoul of federal labor laws governing public transit (more detail on which will be provided later in this analysis).[62]

As RTB began to transfer services formerly provided by MTC to competitive contracting, the MTC unions lobbied to get rid of RTB, and they were ultimately successful. Transportation policy and operations were placed under the regional planning organization, the Metropolitan Council, and once again, union contracts were signed by the organization that controlled transit subsidies. The remaining contracted services constituted 17 percent of all Minneapolis-St. Paul bus service, and the cost of this service was 30 percent below that provided in-house.[63]

Las Vegas

Las Vegas is the only United States metro area in which transit service is fully competitively contracted. It had no public bus system as late as the early 1990s, although a private franchised operator served the Strip area. When Clark County decided to form a public transit system, it also decided to contract the service competitively, and it subsequently experienced tremendous growth. From 1990 to 2000, according to Census data, Las Vegas' Citizens Area Transit had the largest increase in public transit work trip market share in the United States, at 100 percent. This result was particularly impressive given that Las Vegas was also the fastest-growing metro area in the United States during that time period. Costs in Las Vegas remained low, as evidenced by the fact that in 2001,

[60] *Ibid.*
[61] *Ibid.*
[62] *Ibid.*
[63] *Ibid.*

its costs were 41 percent lower than the average for United States public transit agencies with more than 1 million operating hours (and 11 percent lower than San Antonio, the second-lowest cost system).[64]

Indianapolis

In 1972, the Indianapolis Public Transportation Corporation (then commonly known as Metro, and today known as IndyGo) was formed in response to "the growing transportation needs of the Indianapolis urban area and to promote travel to and from the Central Business District."[65] Even as suburban growth in the Indianapolis metro area increased, bus service remained oriented on downtown, and ridership declined even as subsidy increased from $1.2 million in local funds in 1982 to $6.4 million in 1992. Costs increased along with subsidy levels, and by 1992, in the face of a $1.2 million deficit, Metro implemented layoffs and service cuts. In response, senior administrators and managers were replaced, and most express routes were eliminated. The result was a $1.1 million budget surplus—achieved without a tax increase—but then-Indianapolis Mayor Stephen Goldsmith was not satisfied with merely turning a deficit into a surplus.[66]

Mayor Goldsmith—one of the pioneers in using competition to improve both the cost and quality of government services—and Metro began to re-evaluate the role of public transit in Indianapolis. Their deliberations produced the following set of principles for the future of the system:

- The city would not raise property taxes to support the transit system.
- Metro was to focus on serving the "transit-dependent" population of the Indianapolis metro area (the disabled, the elderly, and those residents without automobiles).
- Metro would, going forward be "self-sustaining" and "customer-driven."
- The preceding goals would be met by using competition to provide transit services.[67]

To this end, a panel of international experts, consultants and citizens was formed to examine private sector-oriented alternatives for Metro. The panel developed a "Strategic Plan for Public Transit" that called for the private operation of the transit system, the encouragement of innovation and experimentation, and the development of a market-driven, customer-oriented system.[68] It was expected that these changes would help to increase Metro's service quality and reduce its costs. Before the competitive contracting program began, Metro reduced its workforce through attrition, and then implemented a

---

[64] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[65] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.
[66] *Ibid.*
[67] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.
[68] *Ibid.*

small pilot contracting program of 10 routes in 1995.[69] The city expected to save $3 million by 1999 through competitive contracting, and 1995 saw a 2.7 percent ridership increase over the previous year—the first such increase in a decade.[70]

In order to avoid labor issues and increase the number of routes that could be subjected to competition, Mayor Goldsmith successfully persuaded the Indiana legislature to send its portion of Metro's subsidy to the City of Indianapolis, rather than to Metro directly. As a result, Metro had to cut part of its service, and the city became the contracting agency.[71] By establishing "separation of policy from operations" in this manner, the city was able to select a "mobility manager" to oversee the contracting program (a consulting firm).[72]

Indianapolis used the funds that had previously gone to Metro to bid out routes formerly operated by Metro, and this forced Metro's union and management to work together to create "an economically competitive contractual arrangement."[73] When Indianapolis requested bids for the reduced service (mainly weekend and less-traveled routes), Metro won the contract—and it was able to do so primarily because it had reduced its own costs through negotiations with its union that yielded lower starting salaries for its employees.[74] At the same time, the outsourcing of system oversight through the creation of the city's Office of Mobility Management also helped Metro reduce its employment, as this office was charged with system-wide planning, marketing and customer service (in addition to its oversight duties).[75]

The Indianapolis transit competitive contracting program brought about increased efficiency and service without increasing fares.[76] In fact, from 1994 to 1996, Indianapolis bus service increased by 38.4 percent, while real operating costs were up by just 8.5 percent and 70 percent of the bus system was competitively contracted.[77] As of 1997, Metro served 950,000 people with an average of 220 buses in operation, and by 1999, the operating budget for buses and paratransit services was $28 million.[78] The success of the Indianapolis transit competitive contracting program was further demonstrated by an econometric study published in 1997, in which a number of transit performance variables—labor productivity, maintenance efficiency, vehicle utilization, cost efficiency,

---

[69] Sarah E. Massey, "Privatizing MTA Services, Cost Savings or Political Buzzword?," Permanent Citizens Advisory Committee to the MTA, March 1999.

[70] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.

[71] Sarah E. Massey, "Privatizing MTA Services, Cost Savings or Political Buzzword?," Permanent Citizens Advisory Committee to the MTA, March 1999.

[72] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.

[73] "Lessons Learned in Transit Efficiencies, Revenue Generation and Cost Reduction," Center for Urban Transportation Research, College of Engineering, University of South Florida.

[74] Sarah E. Massey, "Privatizing MTA Services, Cost Savings or Political Buzzword?," Permanent Citizens Advisory Committee to the MTA, March 1999.

[75] *Ibid.*

[76] Sarah E. Massey, "Privatizing MTA Services, Cost Savings or Political Buzzword?," Permanent Citizens Advisory Committee to the MTA, March 1999.

[77] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.

[78] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.

service utilization, system revenue generation, and safety—were examined as to the effect competitive contracting had on each.[79]

The study found only variable examined not positively impacted by competition was service utilization (passengers per total vehicle miles), although both total vehicle miles operated and the number of passengers increased. In contrast, key employee performance indicators (labor productivity and maintenance efficiency) both increased by approximately 70 percent under competitive contracting, and at the same time, cost efficiency and revenue generation both improved by about 20 percent. Finally, the accident rate (per million miles) fell 41.6 percent under competitive contracting.[80]

Despite the success of the Goldsmith Administration at using competitive contracting to improve Indianapolis' transit service, lingering union resentment over the conversion to contracting remained, as well as the sentiment among some community leaders the so-called "minimalist" approach to public transit was harming the city's image and competitiveness. At present, Indianapolis public transit policy has moved largely away from the initiatives that worked so well in the 1990s—but their example provides valuable insight into how a failing public transit system can be reclaimed.

Denver

In 1988, the Colorado legislature passed a bill, co-sponsored by a state representative named Bill Owens (who would go on to serve two terms as the state's governor), that became the only law in the United States mandating the competitive contracting of any public service. The law originally required Denver's public transit agency, the Regional Transportation District (RTD), to competitively contract 20 percent of its bus service within 18 months of its passage. This was accomplished at a savings, despite having to pay redundant workers to avoid federal sanctions—but it was an unusual situation in that the public operator was a competitor for the work while still overseeing the contracting program. In other words, there was no separation of policy from operations in Denver, and opponents of competitive contracting within RTD worked to undermine the effectiveness of the law.[81]

One of these efforts used a report purporting to show that RTD's in-house costs were virtually indistinguishable from those of the agency's private contractors. However, the study was found to be invalid when it was shown the in-house analysis did not account for capital costs, while the competitively bid service did. New management corrected the flaws in the study, but further attempts were made over time to show competitive contracting did not lower costs. Such efforts persisted largely due to the lack of separation of policy from operations. In any case, the contracting mandate was increased

[79] Sarah E. Massey, "Privatizing MTA Services, Cost Savings or Political Buzzword?," Permanent Citizens Advisory Committee to the MTA, March 1999.
[80] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.
[81] Matthew G. Karlaftis, Jason S. Wasson, and Erin S. Steadham, "Impacts of Privatization on the Performance of Urban Transit Systems," *Transportation Quarterly*, Vol. 51, No. 3, Summer 1997.

to 35 percent in 1999, and as of 2001, the competitively contracted RTD services cost 45 percent less than the in-house service. By 2003, the law required that 50 percent of RTD bus service be competitively contracted.[82]

By January 2005, private companies provided more than 40 percent of the total hours driven by buses in the RTD service area. Three companies provided service with 362 leased buses, and with regard to ridership, from 1988 to 1996, RTD bus boardings were up 28 percent—the largest increase among the 25 largest United States transit systems during that period. By way of comparison, the average change in boardings for those 25 systems from 1988 to 1996 was a 13 percent decrease, and PAT had a 17 percent decline. In terms of cost performance, as of the fourth quarter of 2004, RTD in-house total operating and facility costs were $82.05 per vehicle hour, while the corresponding figure for RTD's competitively contracted service was $56.68. Two major factor influencing RTD's in-house costs are its union work rules and benefit packages—a situation similar to that currently facing the Port Authority.[83]

Overall, the RTD competitive contracting program saved $30 million per year as of 2005, and it provided Denver transit users with another important benefit during the 2006 strike by RTD's unionized employees. Forty-five percent of the system's service—the routes that had been competitively contracted—continued to operate during the strike, thus weakening the union's ability to paralyze the Denver transportation network (as the ATU can do with impunity when it negotiates with the Port Authority). At the time, Gov. Owens urged striking workers to return to work immediately, and if that did not happen, he encouraged RTD to expand the competitive contracting program.[84]

In terms of driver costs, in-house RTD drivers had top wages of $18.05 per hour as of 2006, while the average hourly wage for a contracted driver was between $11 and $16. RTD's wage progression was also much steeper for drivers than for their counterparts working for private contractors. Overall contractor hourly operations costs were more than $10 less than those of RTD, and this has occurred despite the fact that contractors are subject to a variety of taxes to which RTD is not.[85]

<u>Boston: Competitive Contracting Thwarted</u>

In 1993, Massachusetts Gov. William Weld attempted to begin a competitive contracting program for Boston bus service operated by the Massachusetts Bay Transportation Authority (MBTA). The initial contract was to be for 20 percent of bus service, and it was unique at in the time in that it called for the winning bidder to assume the existing wage and benefit agreement of the public authority. Even with that provision, however, it

---

[82] *Ibid.*
[83] Jake Haulk and Eric Montarti, "Denver's Solution for Mile High Transit Costs," Allegheny Institute *Policy Brief*, Vol. 5, No. 16, April 21, 2005.
[84] Eric Montarti and Jake Haulk, "Transit Labor Negotiations in Pittsburgh and Denver: Different Planets," Allegheny Institute *Policy Brief*, Vol. 6, No. 19, April 10, 2006.
[85] Eric Montarti and Jake Haulk, "Transit Labor Negotiations in Pittsburgh and Denver: Different Planets," Allegheny Institute *Policy Brief*, Vol. 6, No. 19, April 10, 2006.

was expected to produce more than 15 percent savings over the previous monopoly service.[86]

Predictably, the affected unions opposed the proposed competitive contracting deal, and they led an ultimately successful effort to enact legislation that would severely hamstring this and any future competitive contracting initiative. The result, which came to be known as the "Pacheco Law" after its primary sponsor, requires any competitive contracting program meet a number of extremely strict standards, as determined by the State Auditor, before it can be approved. As a result, the MBTA competitive contracting effort was abandoned.[87]

Developing a Competitive Contracting Model for PAT

To facilitate competitive contracting of bus service at the Port Authority, it would be necessary for the Pennsylvania General Assembly to amend the Second Class County Port Authority Act in order to permit the creation of a county-level agency that would be solely responsible for transit policy (as other state legislatures have done). This new agency would also receive state subsidies (rather than the Port Authority, which would become only an operator of transit services). The ATU would sign contracts with the Port Authority, not the new policy agency, which should also be given a legislative mandate to begin competitively contracting bus routes in Allegheny County (and, in so doing, to "right-size" the agency).

The new Allegheny County transit policy agency would not have any employees responsible for directly operating bus transit services. This practice would avoid the taking on of a sizeable number of future employees, and therefore limit any additional legacy costs for the Port Authority (particularly in the area of retiree health care benefits). At the same time, authority over transit capital spending in Allegheny County should be vested in the new policy agency as well, and the "right-sizing" process for service would have a direct impact on future capital spending. Wasteful, low-benefit projects like the North Shore Connector would be far less likely to be built by an agency that has taken a serious look at what types of service can be best provided given the scarce resources available to it.

With regard to the implementation of a competitive contracting program, the new Allegheny County policy agency could begin by contracting Port Authority bus routes at the rate of employee attrition. The new agency would decide which routes are to be provided, the terms of service for contractors, the fares to be charged, and would also enforce provisions in contracts relating to service quality. Employees providing bus transit services in Allegheny County would be the responsibility of the contractor, including their wage and benefit costs, and contractors would be paid from fare revenues and subsidies received by the policy agency. The Port Authority would be welcome to

---

[86] Wendell Cox, "Competitive Participation in U.S. Public Transport: Special Interests Versus the Public Interest," Wendell Cox Consultancy and Conservatoire National des Arts et Metiers, September 2003.
[87] *Ibid.*

bid on all contracts, but it would likely have to get its unions to restructure their wage and benefit regimes in order to be competitive.

Finally, the goal of the competitive contracting process should not be to simply turn the Allegheny County transit system over to private operators. It is the competitive pressure generated by the bidding of multiple private and public providers that produces improved service and lower costs, not the mere substitution of a private sector monopoly for a public sector monopoly. To this end, as noted previously, contracts should be small enough and offered frequently enough in order to maintain bidder interest and contractor discipline.

By "right-sizing" the current Port Authority bus system through a competitive contracting process overseen by a new, independent policy agency, Pennsylvania and Allegheny County policymakers can create a transit system that provides the service riders need at a lower cost to taxpayers. All potential contractors—including the Port Authority—would have to adjust their operations in order to meet the expectations of the new policy agency and compete successfully for its business.

In order for this to happen, however, the Pennsylvania General Assembly and the governor will have to take on a much more active oversight role of public transit in Allegheny County. They will need to make the legislative changes necessary to separate transit policy from operations, and then maintain that separation in the face of what is sure to be unrelenting union pressure to recombine them. It also needs to give itself representation on the agency overseeing transit in Allegheny County that is commensurate with the state's funding commitment to the agency. Finally, it should mandate that the new agency begin and continue competitive contracting of bus services as a condition of further state subsidy.