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**Issues to watch in the next 60 days: Preliminary analysis based on SMP's agreement in principle with the Cascadia Monorail Company.**

On June 3, 2005, the Seattle Monorail Project announced that it has reached an agreement in principle with the Cascadia Monorail Project. While the full details will not be known until the SMP releases the contract on June 20, the information available to date raises some questions.

The overarching question is will the SMP have sufficient revenue to build the project approved by Seattle voters in 2002? Subsidiary questions include: How much will the Green Line cost? Is the MVET revenue stream sufficient to service the level of debt necessary to finance the project? What risk has been shifted from the fixed-price contract to the Agency? Does the contract change the project approved by the voters in the 2002 election? Will the Green Line ever be self-sustaining?

**How much will the Green Line cost?**

The 2002 initiative limited monorail debt to \$1.5 billion in 2002 dollars (inflated \$1.75 billion in year of expenditure dollars). Based on the preliminary information provided by the SMP, however, the project is already over budget and projected costs appear to exceed the voter-mandated limit on debt.

**Based on SMP statements and expert estimates, current projected Green Line costs exceed \$2 billion, making the project roughly \$625 million over budget before even breaking ground.**

Contract announced June 3, 2005	\$1,600 million
Contingencies (according to Joel Horn)	\$ 200 million
Existing Agency debt (BofA Line of Credit)	\$ 100 million
Utility relocation (estimate)	\$ 50 million
Agency costs during construction (estimate)	\$ 150 million
Start up subsidy for Green Line operations (2002 Plan)	<u>\$ 25 million</u>
	\$2,125 million

Additional costs include any further debt incurred by the Agency prior to issuing bonds, reimbursement to the City for oversight of the project, improvements around stations, litigation, mitigation, and remediation of environmental hazards discovered during construction, all of which could easily combine to add tens, if not hundreds, of millions to the total cost of the project.

In the next 60 days, it will be important to determine how the SMP plans to address the need for more than \$1.5 billion (2002 dollars) worth of debt. One possibility is that the Agency will issue the maximum allowable debt—assuming that the credit markets are willing to purchase the debt—pay off a portion of the debt over a few years, and then issue more bonds to again push indebtedness up to the legal limit. This process could be repeated multiple times. Rather than issuing all of its debt and paying it off steadily over 25 to 30 years, the Agency may issue and reissue debt over a protracted period and extend the period of repayment for total project debt to 40 years or beyond.

### **Is the MVET sufficient to finance the project?**

The SMP faces two significant challenges in financing the Green Line: a 30% shortfall in the MVET revenue stream (the sole source of revenue to pay by monorail bonds) and litigation challenging the constitutionality of the MVET.

Whatever the quantity of debt the SMP plans to issue, the shortfall in MVET revenue impedes the Agency's ability to pay for the Green Line. Projected MVET revenues will support \$500 to \$900 million in first-round bonds, but there is a very real possibility that subsequent Agency bonds will either not receive investment grade ratings or earn a junk bond rating and may be un-sellable or sellable at prohibitive rates of interest. If the MVET revenue stream cannot support all necessary bonds, then the SMP may not have sufficient funds to complete the project.

SMP staff has only recently admitted that the two lawsuits challenging the MVET prevent the Agency from selling bonds. Until the Washington Supreme Court rules on the cases, the future of the revenue source to pay the bonds is uncertain and investors are unwilling to take the risk of buying monorail bonds. The lawsuits ask that SMP's authority to levy the tax be ruled unconstitutional, or, alternatively, that the MVET be redefined and be based on the fair market value of cars rather than on MSRP as is currently the case. If the MVET were recalculated based on market value, experts project the SMP could lose roughly 20% of its revenue, making the project financially unviable.

Unable to sell long-term bonds, the SMP is contemplating selling \$500 million in short-term "commercial paper" to pay the contractor to begin construction. The sale of commercial paper faces the same problem associated with the sale of long-term bonds—if the investment community will not buy bonds backed by a revenue stream that may be declared unconstitutional, why would it buy short-term paper backed by the same revenue stream?

The first lawsuit challenging the MVET (Sheehan and Reynolds v. Sound Transit, Department of Licensing, and SMP) was argued before the State Supreme Court in May. The second case (Larsen v. SMP and DOL) will most probably not be heard before September. It is quite possible that the Supreme Court will refer the Larsen case back to Superior Court for additional adjudication. All of which means that the uncertainty associated with litigation could easily continue well into 2006.

## **What risks have been shifted to the SMP?**

The SMP has always maintained that the Design-Build-Operate-Maintain (DBOM) process would result in a fixed price contract and shift *all* risk of building and operating the Green Line to the contractor. This is not accurate. We know that the costs of moving public utilities (estimated at \$50 million)—an obligation to be assumed by the contractor in the RFP—have been shifted to SMP. Close examination of the contract will likely reveal more ways in which risk has shifted from the fixed-price contract to the Agency.

## **What changes have been made?**

Through the course of contract negotiations, many features of the system approved by voters in 2002 have been changed:

- The Green Line was to have 19 stations.<sup>1</sup> Now, it will have only 16 or 17. The stations at Elliott and Mercer and 35<sup>th</sup> and Avalon have been deferred indefinitely and the contract does not provide for the construction of the station at 2<sup>nd</sup> and Madison (which was to have the fourth highest ridership and provide the connection to the downtown business core and the ferries). While the SMP claims that there is money in its budget (as distinguished from the DBOM contract) to pay for the station at 2<sup>nd</sup> and Madison, it is far from clear that the property will be available in time for the opening of the Green Line.
- SMP spent \$2.3 million on preliminary station designs and promised that monorail stations would be integrated into the character of specific neighborhoods. Now, there will be one standard station throughout the line—an open air structure that provides limited opportunities for neighborhood expression.
- The 2002 Plan promised columns “as small as 36” in diameter”<sup>2</sup>—smaller than the columns for the existing Seattle Center Monorail. Now, columns will be 4 feet by 5 feet, roughly the size of the existing columns.
- Trains were supposed to come every four minutes at peak times<sup>3</sup> to maximize convenience and ridership. Now, trains will come every 8 minutes at peak, negatively affecting ridership.
- The SMP was to accrue debt amounting to no more than \$1.5 billion in 2002 dollars or \$1.75 billion in year of expenditure dollars.<sup>4</sup> Now, the project looks to exceed \$2 billion in cost.

## **Will the Green Line ever be self-sustaining?**

The 2002 initiative prohibits the use of tax revenues to support operations or maintenance after 2020, thereby requiring that the Green Line be self-supporting with operating revenue alone. The reduction in stations, increased wait-time for trains, and other as yet known changes in service (including sections of single beam guideway) will have a negative impact on ridership and fare-box revenue. As a result of insufficient revenue, the SMP will have to reduce service to cut costs (which will lead to a downward spiral)

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<sup>1</sup> August 2002 Plan, page 34.

<sup>2</sup> August 2002 Plan, page 2.

<sup>3</sup> August 2002 Plan, page 35.

<sup>4</sup> August 2002 Plan, pages 42-43.

or ask voters to raise taxes to subsidize the line. In any event, no transit agency in the nation comes close to breaking even and there is no reason to believe the Green Line will not generate an operating deficit.

## **Conclusion**

OnTrack's analysis has identified a number of issues to monitor over the next 60 days as the details of the contract are revealed and the public has an opportunity to voice its opinion of the agreement. The key issues revolve around the financial viability of the system, including whether or not the SMP has sufficient revenues to pay for the project. Additionally, the public should be concerned with the total amount of debt the Agency plans to incur and how long it will take to pay back that debt, as well as changes to the Green Line that undermine promises made to the public in 2002 and diminish the likelihood that the Green Line will ever be self-supporting.