U.S. Department
of Transportation

**Federal Transit
Administration**

Administrator

400 Seventh St., S.W.
Washington, D.C. 20590

April 29, 2005

Dear Colleague,

Many thanks to the 50 organizations and individuals who responded to my March 9 request for comments on potential changes to some of the underlying data and calculations of measures used to rate New Starts projects. Your comments were thoughtful and constructive, and the decisions we have reached regarding each of the potential changes were better informed as a result of your input. I also want to thank the more than 450 individuals who participated in the FTA Webinar on this subject. I am pleased that we were able to provide additional information and respond to your questions through this broad communication vehicle.

In the reporting instructions for the coming year, we have decided to incorporate three specific changes, as follows:

- The cost-effectiveness rating **breakpoints will be adjusted for inflation** utilizing the GDP Price Index (also known as the GDP deflator).
- Project sponsors will be permitted to **utilize either a 2025 or a 2030 planning horizon.** In communities where the MPO forecasts still utilize a 2025 planning horizon, project sponsors may extrapolate those forecasts to 2030 for the purposes of making project forecasts for this year's submission. The same planning horizon must be used for system-wide operations and maintenance cost estimates and ridership forecasts.
- All project sponsors will be required to **utilize FTA's Standardized Cost Categories and new useful life assumptions** in the development of project budgets and annualized capital costs, which will be reflected in a revised Template 8.

Although all of the comments are available for your review on the DOT Docket (http://dms.dot.gov/; Docket Number 20585), below you will find a summary of the comments received, as well as the rationale for our decision on each change.

Adjust Cost-Effectiveness Rating Breakpoints for Inflation

The current cost-effectiveness breakpoints were established in 2002. There was strong consensus among those who expressed an opinion that the cost-effectiveness breakpoints should be adjusted to reflect inflation. Nearly two-thirds of respondents did not express a preference for a specific index, but those that did express a preference generally supported the use of the Engineering News Record's (ENR) Construction Cost Index.

Although FTA considered utilizing the ENR Construction Cost Index, we ultimately rejected that index in favor of the GDP Price Index for two reasons. First, cost-effectiveness is rooted in value of project benefits (cost per hour of transportation system user benefits expressed as travel-time savings). While a construction cost index may capture the increases in project costs due to inflation, it does not reflect changes in the value of benefits as well as a more general measure of inflation. While GDP price index is not a pure income-based index it closely correlates to the consumer price index (CPI). The CPI is the traditional measure for inflating the value of time, which is integral to calculating the value of benefits, and the GDP Price Index is an acceptable surrogate. Second, unlike the ENR Construction Cost Index, the GDP Price Index is produced by a government agency and subject to verification and oversight.

Index Costs Regionally

In my previous Dear Colleague, we offered the possibility of adjusting costs based on a regional index in an effort to account for intrinsic cost differences among projects located in different parts of the country. Based upon consideration of the comments received and our own concerns about the appropriate application of the available data for this purpose, FTA has decided not to apply a regional cost index at this time.

There was no strong consensus among respondents that regional adjustments should be made. Thirteen respondents supported regional adjustments, while eight opposed the use of a regional index and another six indicated that they needed additional information in order to form an opinion on the matter. Neither the American Public Transportation Association (APTA) nor the New Starts Working Group (NSWG) expressed support for the introduction of regional cost indexing. Opposition to regional cost indexing was based on the argument that New Starts projects are more subject to national and international markets for resources like steel and concrete, rather than local or regional cost trends. In addition, many respondents argued that utilizing a regional index would introduce an unnecessary level of complexity to the calculations and reduce the transparency of the project rating process. This would make it difficult for project sponsors to determine whether they would need to make cost or scope adjustments in order to meet FTA requirements, and could call into question the comparability of FTA ratings of projects in different regions. Finally, it was noted that the ENR Construction Cost Index is currently available in a limited number of cities, and that the ENR website indicates that the index should not be used to measure cost differentials between cities.

Incorporate a 2030 Planning Horizon

In general, respondents supported the use of a 2030 planning horizon, provided that it is consistent with forecasts used by the local MPO. In areas where the MPO has not yet moved to a 2030 forecast year, respondents urged that the adoption of a 2030 forecast year be made optional, and that project sponsors in these areas be permitted to extrapolate the necessary planning data from the 2025 forecasts used in the region's long-term plan.

FTA recognizes that regions which have not already incorporated a 2030 planning horizon into their adopted long-term transportation plan could have a difficult time developing and adopting a long-term regional transportation plan in time to incorporate these forecasts into the New Starts project submissions for the upcoming year. This would be especially difficult in smaller urbanized areas that rely on a State DOT for long-range planning and travel demand forecasting.

As a result of these considerations, FTA has decided that, for the upcoming New Starts evaluation cycle, project sponsors may use either a 2025 or a 2030 planning horizon, and with endorsement from their MPO, may extrapolate from a 2025 regional long-term plan to develop 2030 forecasts for the proposed New Starts project. Regardless of whether project sponsors choose to use 2025 or 2030 as their planning horizon, they must also use that same planning year (2025 or 2030) for the estimation of operations and maintenance (O&M) costs, which reflect that year's service levels, as well as the forecast of transportation benefits. FTA will develop a policy for future planning horizon transitions (e.g., from 2030 to 2035) that will facilitate the consistent nationwide use of an appropriate planning horizon.

Implement New Useful Life Assumptions as Part of Standardized Cost Categories

There was general support for the Standardized Cost Categories and the proposed adjustments to useful life estimates, which clarify and lengthen these estimates for a number of assets. Some respondents expressed concern that consideration should be given to revisiting the useful life estimates for additional categories of assets.

Based on these comments, FTA will require all project sponsors to utilize the Standardized Cost Categories and new useful life assumptions in developing their budget and annualized cost estimates for the next New Starts submission. FTA will continue to work with industry experts to update the useful life assumptions for additional categories of assets for application in future years.

Assert Modal Constants in Travel Forecasts

Current FTA policy requires that forecasts for guideway modes new to an urban area be prepared with constants used for the bus mode(s) in the area, and that constants calibrated in areas that already have guideway modes be reasonable representations of the non-time/cost qualities of fixed guideway modes, rather than adjustment factors used to offset inadvertent errors introduced elsewhere in the travel models.

Respondents expressed general support for the introduction of constants for new guideway modes as a means of enabling travel models to estimate the effect of improvements to transit service quality beyond the time and cost measures already accounted for in the travel models. However, respondents also expressed a strong preference for substantial industry involvement in the development and testing of such constants prior to application. Consequently, FTA has decided to postpone any adjustments to its current policy pending the completion of additional research, analysis, industry consultation, and testing.

Exclude Soft Costs in Calculating Cost Effectiveness

Although there was strong support for removing some soft costs from the calculation of cost effectiveness, most respondents noted that the specific costs must be explicitly defined and those definitions must be consistently applied to each project. There was a considerable range of opinion about which soft costs should be excluded, from design costs to Before and After Study costs to start-up costs.

FTA has concluded that any costs that are required to design, construct or prepare the project for opening day operation should continue to be included in the cost effectiveness calculation because these costs are intrinsic to the project itself. Costs that could be considered for exclusion would be the Before and After Study and, potentially, some portion of start-up costs. Additional analysis would be required to identify other costs that would meet this criterion. Since additional work is required and since the current Standardized Cost Categories do not include this level of detail, it is not possible to implement this change for the upcoming year.

The Issue of Formal Rulemaking

A significant number of respondents, including APTA and NSWG, suggested that implementation of any potential changes be delayed until a formal rulemaking is conducted. Although FTA has considered delaying implementation of these changes until the surface transportation reauthorization has been passed and/or a formal rulemaking has been conducted, we do not believe that such a delay is either necessary or advisable. First, the changes under consideration are consistent with the existing New Starts statute and regulations and do not rise to the level of a rulemaking. And, second, the changes being adopted are important to ensuring that projects are fairly and accurately evaluated.

A Special Note on Administration Funding Recommendations

A number of you also took the opportunity to comment on our announcement that the Administration will target its recommendations for funding to projects that achieve a "medium" or higher rating for cost-effectiveness. As you know, the President and his Administration must make numerous tradeoffs and decisions as budget recommendations to Congress are developed. The framework and rationale for these decisions is not subject to rulemaking. Nevertheless, in keeping with our goal of making the New Starts decisions as transparent as possible, the Administration chose to publicly announce this internal decision-making principle.

Many of the comments regarding the funding recommendation announcement appeared to reflect a misunderstanding about its application to the project rating process. Please note that, although the Administration will not include such projects among its recommendations to Congress for funding, project *ratings* will not be affected by the change. A project that receives a "medium-low" cost-effectiveness rating may still achieve an overall rating of "recommended," provided that its land use rating is sufficiently high to offset the "medium-low" cost-effectiveness rating and that it meets all of the current financial criteria. As you know, failure to achieve a "medium" rating on any of the three financial criteria already results in an overall rating of "not recommended." Indeed, all of the "not recommended" ratings in the last two years reflected adverse ratings on one or more of the financial criteria.

There was also some apparent confusion about which projects would be subject to the Administration's new position regarding funding recommendations. In the President's FY 2006

Budget, four proposed projects identified as "Anticipated FFGAs" received specific funding recommendations; these projects will not be affected. However, the six projects listed under "Other Projects" will need to achieve a "medium" or higher cost-effectiveness rating in order to receive a funding recommendation from the Administration. None of these six projects received a specific funding recommendation in the President's Budget. In fact, as noted in the Budget and the New Starts Report, FTA did not anticipate that all six projects would ultimately receive a funding recommendation, and the President's budget set aside only $159 million of the $260 million that could be utilized if all six were ready for funding by the time Congress takes up the FY 2006 budget. Indeed, even today, only one of the six projects is in final design, which is a long-standing premise for receipt of a funding recommendation from the Administration.

Next Steps

Within the next week or so, FTA will be issuing the New Starts Reporting Instructions. These instructions will incorporate the changes noted above. As always, FTA will be pleased to assist you as you develop your project submissions, and to answer any questions you may have regarding these changes.

Again, thank you for your participation in this important decision making process. I know that the transit industry appreciates the importance of these issues, and we look forward to working with you as we continue to strengthen and improve the New Starts evaluation process and the transit projects it supports.

Sincerely,

Jenna Dorn

Jennifer L. Dorn