



EXECUTIVE OFFICE OF THE PRESIDENT

OFFICE OF MANAGEMENT AND BUDGET

WASHINGTON, D.C. 20503

APR 16 1975

ACTION

Eno

Center for
Transportation

MEMORANDUM FOR THE PRESIDENT

FROM: JAMES T. LYNN

SUBJECT: METRO Construction and Financing

Statement of Issue

What should the Administration's position be with respect to further financing of the Washington area METRO rail system?

Background

Current METRO construction stems from a substantial history of executive and congressional legislative support for a regional rapid-rail system. Based on earlier studies, Congress authorized a system of 25 miles in 1965. The Washington Metropolitan Area Transit Authority (WMATA) had been created as an interstate compact agency to plan and carry out the transit program. To obtain greater participation from local jurisdictions and improve area-wide transportation, a 98-mile system was proposed late in the Johnson Administration. The legislation was resubmitted, with some technical changes, as a Presidential program proposal early in the Nixon Administration. The Congress enacted the National Capital Transportation Act of 1969 authorizing the 98-mile system on December 9, 1969, at a system cost of \$2.5B.

Events in 1970 and 1971 such as greater than anticipated inflation in construction costs, congressional funding delays, and the weak state of the market for the Authority's bonds led to a gap in the 1969 financial plan. The Administration strongly supported legislation to provide a Federal guarantee for taxable bonds with a 25% interest subsidy to generate the additional necessary financing, enacted July 13, 1972.

The 1969 Act, as amended, endorsed a 98-mile system and authorized \$3.0B of financing through three sources: revenue bond proceeds, local contributions, and Federal contributions.

Total project costs	<u>\$2.980M</u>
Revenue bonds	1.110M
Net project cost:	1.870M
Federal share (2/3)	(1.147M)
Local share (1/3)	(.723M)

Additional Federal financing was provided on an 80%-20% basis to construct facilities for the handicapped (\$52M Federal share, \$13M local share). \$11.3M was added for construction of "Federal interest" stations to serve the Smithsonian and Arlington Cemetery.

Two recent analyses performed for WMATA materially alter this financial scheme:

Bond Repayment Problem

Debt service on the \$1.2B of bonds was to be liquidated by farebox revenues from the rail system. To date, \$997M of the bonds have been issued with a Federal guarantee, with a pledge from the local governments that they would take "whatever action is necessary" to pay any principal and interest costs not met through the farebox.

Recent analysis indicates that because of higher than anticipated costs of rail system operations, unanticipated bus deficits, and the current level fare policy, the bond obligations cannot be fully covered by the farebox revenues. Localities are now faced with the need to make substantial unanticipated annual contributions toward the \$2.9B required through the year 2015 to repay the bonds. This prospect, combined with doubt whether 98 miles will be built, makes issuance of the remaining bonds (\$200M) open to question.

Construction Cost Escalation

The existing financial plan was based on a cost estimate of about \$3.0B. Construction has been delayed by factors such as Hurricane Agnes, congressional funding delays, strikes of various construction crafts, and environmental impact suits.

In addition, cost estimates have grown due to design changes, unforeseen construction conditions and unprecedented inflation. An analysis of the 98-mile system, made in late 1974, now projects a cost of \$4.5B or \$1.5B more than currently authorized. Even this total is subject to upward revision if further unscheduled delays occur and the inflation rate continues.

Construction Status and Local Concerns

Construction of METRO began in the core area of the District and has radiated outward. Forty miles are now under construction and an additional 30 miles are under final design. If all existing commitments--Federal and local--toward the \$3.0B plan were met, 76 miles of the system could be built. However, WMATA believes a Federal decision not to provide additional funding toward the \$4.5B cost estimate would collapse existing financing arrangements to the point that only 47 miles could be built (at a cost of about \$2.4B).

The financial contribution of the local governments is based upon their proportionate share of a 98-mile system, even though actual construction to date in Maryland and Virginia is relatively small. This has caused great concern on the part of local suburban officials who fear that their areas will not receive the transit service for which payment has already been made. They also fear that a truncated system will have operational problems and not provide adequate revenues to meet operating costs.

In addition, they are concerned that local transit and air pollution goals will not be met if less than 98-miles are built. They further assert that local fiscal resources cannot bear additional burdens, particularly in the face of continuing bus operation deficits and the bond problem. (Their position is set forth in more detail in Attachment A.) As a result, the WMATA Board--representing the local jurisdictions concerned--is seeking Administration support for authorizing legislation which would provide Federal financing of 80% of the funds needed to meet the new \$4.5B cost estimate, with the 80% retroactive to fiscal 1974.

Current Congressional Situation

Existing WMATA legislation was developed cooperatively between the previous Administration and WMATA and transmitted jointly by the Secretary of DOT, the District, and WMATA.

Due to the dramatically higher cost estimates, mutually acceptable legislation will now be much more difficult to achieve.

Unless the Administration and WMATA jointly agree on a policy, WMATA would probably develop its own proposal. Such a bill would seek to maximize Federal underwriting of the project. As an interstate compact agency with no Federal Board member, there is no direct means of preventing WMATA from pursuing an independent course--if they choose to forfeit Administration support. Such a WMATA bill could be expected to receive a sympathetic hearing from the Senate and House District Committees which have strong local representation, particularly since the election to Congress this fall of two former WMATA Board members.

Since no legislation has yet been introduced, congressional views are so far relatively unfocused. The House Budget Committee, however, has included an initial increment of \$211M for METRO construction in its proposed expenditure plan. District Committee Chairman Diggs had asked the Budget Committee for the entire \$1.2B. This indicates that the D.C. Committees would tend to favor the WMATA proposal or at least a substantial Federal contribution.

The fate of such a bill on the floor would be much less certain. There may be a congressional feeling that too much has been invested to turn back now. This is the view purported to be expressed to WMATA congressional liaison staff. On the other hand, it is likely that there will be little enthusiasm in the Congress as a whole for spending such a large amount on transit in the National Capital area compared to the resources available for the rest of the nation. There also may be opposition by the House Public Works Committee to the shift of D.C. highway funds to mass transit, in the alternative discussed below.

Interstate Highway Transfer

A resource that could be used to provide additional funding is the "Interstate Transfer" provision of the 1973 Highway Act. Under this act, localities can substitute transit projects--on an 80%-20% basis--for segments of the Interstate Highway System which they decide not to build. Maryland, Virginia and the District all have controversial interstate segments which may not be built. Current estimates of the costs to complete such segments are:

D.C. - \$1,418M

Maryland - \$306M

Virginia - \$157M

In the District, both the Mayor and the City Council have expressed the view that much of their interstate construction will not be approved. Maryland has already announced that it does not plan to complete several interstate segments in the Washington area and plans to use these funds to extend the Rockville METRO line and upgrade highways elsewhere in the State. It is doubtful that Virginia would be very receptive to use of interstate funds for METRO construction.

Although the total cost of completion of these interstate segments may be reasonably close to the shortfall in METRO's present financial plan, the routine timing of the availability of interstate substitution funds falls substantially short of the rate at which METRO plans to obligate funds. Under either the current interstate allocation system or the Administration's new proposal, METRO would have a substantial cash shortfall in FY 1976-78. One approach to eliminate this problem would be to have all interstate transfer funds immediately available for obligation (i.e. funds for the cost of the completion would be immediately available for obligation rather than on a pro rata basis over a period of years as with other interstate funds). OMB has rejected this proposal because it would substantially reduce Executive control over all future transfers and represents a significant uncontrolled add-on to future Federal transportation expenditures.^{1/}

Special legislation for METRO could be proposed to accelerate Federal payments to the District to augment their interstate funds. This, in effect, would be borrowed from their future year interstate allocations. Thus, the local jurisdictions could increase their obligations in FY 1977-79 at the expense of anticipated FY 1980-85 allocations. Such increases would have to represent an addition to the Federal budget as it is not politically feasible to have these increases absorbed within proposed interstate program levels. In the long run, these would be offset by the non-use of interstate highway construction funds through the 1980's.

The additional costs of METRO construction above amounts assumed in the budget and their relationship to anticipated Federal interstate payments are displayed below.

^{1/} The appropriate treatment of interstate transfer financing nationally will be further addressed in the final Administration decisions regarding a 1975 Federal Highway legislative proposal.

(\$ in millions)

	<u>1976</u>	<u>1977</u>	<u>1978</u>	<u>1979</u>	<u>1980</u>	<u>Total</u>
METRO overrun	237	461	532	206	41	1477
Federal share (80%)	190	369	425	165	33	1182
D.C. Interstate	200 ^{1/}	85	85	90	90	550
Net Accelerated Payments	(-10)	284	340	75	(-57)	632

1/ FY 1976 availability depends upon how quickly the District can implement interstate transfers and the size of overall Federal highway funding. Some acceleration may be needed in FY 1976.

Financing Alternatives

Alt. #1. The Federal Government to pay 80% of the increased costs plus 80% of the costs since July 1, 1973. (The date on which the national mass transit program went to 80-20.) Local officials on November 21 voted unanimously to seek this arrangement. It would entail additional Federal contributions of \$1,257M and additional local contributions of \$135M.

Alt. #1A. To ease the near-term Federal outlay impact, WMATA has proposed that the Federal Government authorize the sale of \$1.257M in taxable bonds for which the Government would pay the principal and interest over a 40-year period. Annual liquidating appropriations would be \$88M, with a \$14M tax recapture for a net annual Federal cost of \$74M.

Alt. #2. No further special Federal financing. Any additional funds would come from a combination of local funds, interstate substitution funds, and perhaps, the UMTA nationwide mass transit program late in the decade. The current UMTA funding assumptions do not include any planned coverage for METRO. This alternative assumes the localities would repay existing bond obligations, but some contingent Federal liability of up to \$997M already exists due to the Federal guarantee.

Alt. #3. Reliance on Interstate Funds with accelerated payments. Funding would come from money available through interstate transfer. Legislation, in the form of an amendment to the National Capital Transportation Act, would be submitted soon to provide for such a mechanism.

This mechanism would allow local officials to choose between highway mileage and mass transit. Until final local decisions on highway substitutions are made, it will not be known if such funds will be adequate to complete the system. If these funds are not adequate, or if fiscal uncertainties cause a failure to issue the remaining bonds, a decision on possible additional Federal assistance will be needed. However, any consideration of this question should not be required until all highway substitution decisions are made and resultant funding substantially committed, in two to three years.

(A table showing costs of the alternatives is Attachment B.)

Pros and Cons

Alt. #1. (80% Federal share of new total cost, retroactive to FY 1974)

Pro

- Provides relief for overburdened local fiscal resources. Local funds already committed would match additional Federal contributions. Also requires added local resources.
- Carries out existing Federal commitment. "Keeps faith with citizens of the region."
- Makes formula consistent with national transit formula.
- Insures maximum transit and environmental objectives.

Con

- Requires highest level of added Federal resources-- \$1.2B over next 3-4 years. Difficult burden for Federal budget to sustain.
- No logical reason for retroactive shift, particularly in light of other benefits (e.g., bond guarantee) given to METRO not in national program.
- Disproportionate amount of Federal spending on single transit project compared with new Federal transit capital program for entire nation of \$11.8B over 6 years.

- Endorses primarily at new Federal expense, construction of marginal segments of transit system.

Alt. #1A. (40-year bond financing)

Pro

- All advantages of Alt. #1.
- Lessens severe outlay impact on Federal budget in near term.

Con

- Adds interest costs to principal used for construction, raising total additional costs over 40 years to \$2.9B.
- Sets bad precedent for Federal bonds for individual projects.

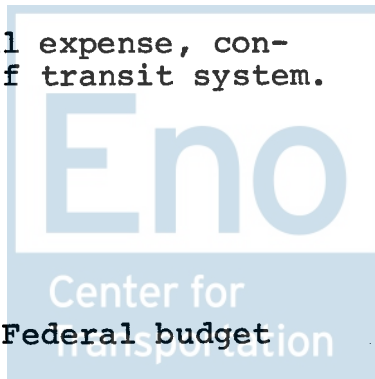
Alt. #2. (No additional special Federal funding)

Pro

- Keeps special Federal funding at lowest level.
- Provides incentive for localities to use Interstate highway transfer provisions of 1973 Highway Act to pay for transit to the extent possible.
- Allows completion of significant portion of system if existing local commitments are kept, depending on local highway substitution decisions.

Con

- Would be perceived as renegeing by Federal Government, which local officials regard as committed legally and morally to complete a 98-mile system.
- Local governments committed to share capital costs and guarantee bond repayment based on 98-mile system. Voters in Virginia, where bond referendum was required, heavily favored issuing bonds on premise of full system.



- Failure to complete because of fund shortfall will compound traffic problems by not encouraging shift of potential riders from buses and cars. Adds to pollution and demand for additional highways.
- Subsequent to inception of METRO planning, Federal clean air and energy conservation requirements have increased the need to shift riders from private auto to transit.

Alt. #3. (Use of Interstate Transfer with accelerated payments)

Pro

- Provides significant Federal support consistent with overall budget constraints. Requires additional local funding above that already planned.
- Federal support provides strong incentive to local officials to meet existing commitments for coverage of revenue bonds.
- Allows existing statutory arrangement to run its course as contemplated at outset of program. (2/3 - 1/3 basis)
- Presents a creditable posture to the Congress.
- Allows National Capital Region to choose to complete system which would significantly meet transit objectives of area with appropriate mix of highways and transit.

Con

- Fails to meet local objectives of full Federal commitment by direct appropriation with retroactive formula change.
- Sufficient funding for completion of 98-mile system requires local agreement on highway decisions which may be difficult to achieve.
- Represents "new Federal spending" in 77-79.
- Requires special legislation.

OMB Evaluation and Recommendation

Support of the full WMATA request for expansion of separate Federal financing is not justified in our view because of the high marginal cost of the transportation benefits received. Rough analysis by WMATA indicates that the additional \$1.5B will only increase ridership about 15-20 percent over a \$3B, 76-mile system. It is probable that if WMATA were applying for Federal assistance for the un-built lines for the first time through the regular UMTA program, some of their proposals might not withstand the test of cost-effectiveness and would not be funded by UMTA.

In contrast, however, the Federal involvement during the inception and development of METRO, the Federal stake in some kind of successful outcome, plus the good faith efforts of the local jurisdictions make it undesirable to take a position that no further Federal assistance should be forthcoming. Such a position would probably not be agreeable to the Congress.

Taking all factors into account, a constructive response to the WMATA proposal is recommended--Alt. #3. Full local use of interstate transfer funds and their accelerated availability should make possible completion of the system. It would provide the maximum incentive to local officials to make good their bond guarantees, reducing possible Federal liability for almost \$1B in already issued bonds. This proposal would offer a solid alternative to area officials and, if agreed to, prevent a separate appeal to the Congress.

Secretary Coleman has been briefed on the details of this memorandum. He strongly supports the effort to meet the METRO construction schedule and agrees that among the financing alternatives available, the use of the interstate transfer provision is the best means of meeting increased METRO construction costs while minimizing the total impact on Federal expenditures. His other views with respect to METRO issues are set forth in attachment C.

In summary, Alt. #3--while subject to some uncertainties--appears to be the most desirable course at this time.

Decision

Alt. #1 Alt. #1A Alt. #2
 Alt. #3 Other (See me)

Attachments

Position of Local Officials

The posture of the local officials with respect to further financing is quite clear. They are seeking to insure maximum Federal funding to carry out what they consider the Federal commitment to a full system to meet the transportation and environmental needs of the area. It is politically very difficult for them to consider alternatives to completion of the 98-mile plan.

WMATA staff has done some preliminary analysis of the transportation effects of building only 76 miles with the authorized \$3.0B because of a shortfall in funding. This analysis indicates that 270 more buses (\$20M capital cost, \$18M annual operating cost) would be required. In addition, WMATA argues that further extensive but undetermined road construction would be required to meet 1990 traffic demands. Also, the failure to divert auto passengers to mass transit would have a negative effect on air quality and environmental goals, a national priority. The most troublesome effect would be that if system construction shrinks below 76 miles, it becomes more of a District of Columbia system with lesser rail mileage for the suburbs which have financially committed themselves to the system. It also eliminates the important Mid-City Line, which in D.C. official's eyes is vital to serving low income District residents.

In the view of local officials, much of the cost overrun has been caused by national inflation which is beyond their control. They view it as unthinkable that the Federal Government would back away because of the added cost, given the fact that numerous Federal projects are initially underestimated in cost but subsequently completed. They note that the Interstate system was originally estimated in 1956 to cost less than \$30B while the Federal Government has bi-annually increased the estimated cost to \$76.3B, (as of 1972) rather than eliminate mileage in the system.

They also believe their fiscal resources are strained to the utmost, particularly in view of the mounting bus operating deficits--projected to reach \$52M in 1976--and the unanticipated necessity to subsidize rail system operations to pay off part of \$2.9B in bond costs.

Local officials stress that there is a strong Federal interest in completing the project. They note that in testimony on the original authorizing bill, then Deputy Director of the Bureau of the Budget, Phillip S. Hughes, stated that the legislation would (1) fulfill a mandate of Congress; (2) sustain local support and responsibility for the system; and (3) recognize the special Federal interest in the National Capital area.

With respect to the Federal interest, he noted the significant Federal impact on the area economy--employing 30% of the workforce, generating 40% of the area's total wages, and occupying about 30% of available office space. The logic was that in other localities, sectors of the local economy equivalent to the Federal Government's local role in Washington would contribute tax resources necessary to build a rapid-transit system. Hence, the proposed Federal contribution would provide compensatory recognition of the lack of comparable local tax resources. Hughes also stated that as the region's major employer, the Federal Government would benefit by improved productivity from the estimated 40% of its employees commuting to their place of employment. Finally, he noted the responsibility of the Government for the quality of life in the National Capital area for those who work, live, and visit here.

In light of these factors and firmly believing that the Federal Government has a commitment to fulfill in achieving the 98-mile system, WMATA and the local governments are pressing vigorously for the fullest Federal financial commitment.

METRO SYSTEM FUNDING PROPOSALS

(In Millions of Dollars)

	Alt. #1 80-20 Effective <u>7/1/73</u>	Alt. #1A 80-20 Effective <u>7/1/73</u>	Alt. #2 \$2.980 Million <u>System</u>	Alt. #3 80-20 of Increased <u>Cost</u>
Federal Grants ^{1/}	2,404	1,147	1,147	1,147
Local Grants	856	856	723	1,018
Bonds and Proceeds	919	919	919	919
Internally Generated Funds	275	275	191	191
Federally Supported Bonds	--	1,257 ^{2/}	--	--
Federal Interstate Transfer Funds	--	--	<u>3/</u>	<u>1,179</u>
Project Cost	4,454	4,454	2,980	4,454

1/ Does not include total 40 year outlays of \$963M in interest subsidy for bonds, recovered from Federal income tax receipts.

2/ \$74M per year average - Debt Service.

3/ Could also be supplemented by funds made available under regular Interstate Transfer procedure.

Eno

Center for
TransportationAdditional Views of Secretary Coleman

The Administration's decision on the financing issue should not force either a slowdown in the pace of METRO construction or cutbacks in the mileage of the final system. At a time when the Administration is attempting to cut back fuel consumption, when construction delays mean substantially increased costs, and when cutbacks in the METRO system would greatly reduce service to low and moderate income areas of the District, such a position would not be tenable.

While the Department concurs that the interstate transfer provision is the best available means of meeting increased METRO construction costs, the Department believes that the mechanism recommended in the proposed OMB memorandum is not the most effective way to implement the interstate transfer concept. The Department's recommended approach for managing the interstate transfer provision throughout the Nation as well as in D.C., would provide for control of the rate at which funds are obligated without the need for new legislation. Furthermore, the DOT recommendation would permit management and funding decisions on the substitute transit projects to be made in the context of the national transit program, rather than being dictated by an unrelated highway distribution formula.

THE WHITE HOUSE
WASHINGTON

May 24, 1975

MEMORANDUM FOR:

DICK CHENEY

FROM:

JERRY H. JONES

You might want to mention to the President that this is overdue and we need a decision. We should set up a meeting if he doesn't understand it.

THE WHITE HOUSE
WASHINGTON

May 15, 1975

Eno

Center for
Transportation

MEMORANDUM FOR:

DICK CHENEY

FROM:

JERRY H. IGLES

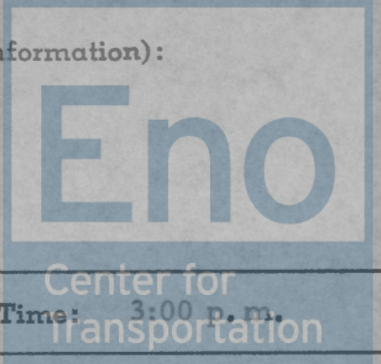
The attached Lynn memo on METRO financing was sent to the President May 2 but has not been returned. Do you know where this is hung up?

Date: April 17, 1975

Time:

FOR ACTION: Phil Buchen
Jim Cannon
Jack Marsh
Max Friedersdorf
Bill Seidman

cc (for information):



FROM THE STAFF SECRETARY

DUE: Date: Monday, April 21, 1975

Time: 3:00 p.m.

SUBJECT:

Lynn memo (4/16/75) re: METRO Construction and Financing

ACTION REQUESTED:

- For Necessary Action
- For Your Recommendations
- Prepare Agenda and Brief
- Draft Reply
- For Your Comments
- Draft Remarks

REMARKS:

4/22 - Called Cannon & Marsh
 4/28 - Cannon (WH) keeps saying today, today
 4/30 - Cannon (WH) says option 3.
 5/1 Jim Jones checking on Bucken comments
 5/2 - W/P

PLEASE ATTACH THIS COPY TO MATERIAL SUBMITTED.

If you have any questions or if you anticipate a delay in submitting the required material, please telephone the Staff Secretary immediately.

Jerry H. Jones
Staff Secretary

THE WHITE HOUSE

ACTION MEMORANDUM

WASHINGTON

LOG NO.:

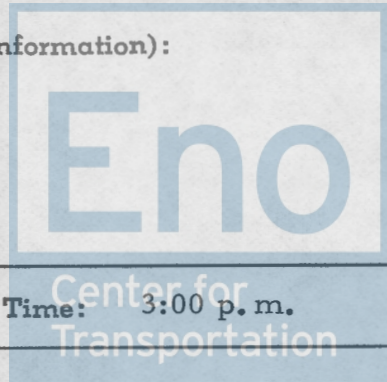
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REMARKS:

The feasibility of Alternative 3 (favored by OMB) is difficult to appraise because of our uncertainty as to whether "local agreements" required can be achieved. If as a practical matter they cannot, a new issue is raised.

Also the position of DOT (Attachment C) is somewhat vague and is not set forth with any specificity in the action memorandum.

We suggest the memorandum be altered to appraise feasibility of local agreements referred to above and to more clearly set forth DOT position as an alternative.

Rod Hills R.H.
and Ken Lazarus

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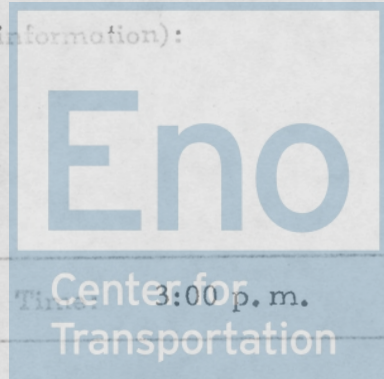
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REMARKS:

See inside

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Decision Alt. #1 Alt. #1A Alt. #2 Alt. #3 Other (See me)

with Coleman
Attachments *suggestions!*
FWJ

Date: April 17, 1975

Time:

due: 4/21

FOR ACTION: Phil Buchen
Jim Cannon
Jack Marsh
Max Friedersdorf
Bill Seidman

cc (for information):

3:00

FROM THE STAFF SECRETARY

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Center for
Transportation

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and Financing

ACTION REQUESTED:

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For Your Recommendations

Prepare Agenda and Brief

Draft Reply

For Your Comments

Draft Remarks

REMARKS:

Out #3
JM

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Jerry H. Jones
Staff Secretary

THE WHITE HOUSE

WASHINGTON

April 21, 1975

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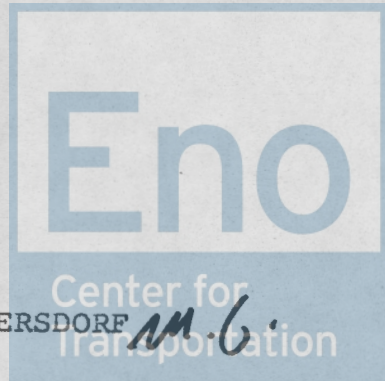
JERRY JONES

FROM:

MAX L. FRIEDERSDORF

SUBJECT:

Lynn memo (4/16/75) re: METRO
Construction and Financing



The Office of Legislative Affairs concurs with subject memo.