



UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

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ACCOUNTING AND FINANCIAL
MANAGEMENT DIVISION

April 13, 1982

B-207054

To the Board of Directors
United States Railway Association

The accompanying statement of financial position of United States Railway Association (Association) as of September 30, 1981, and the related statements of operations and changes in financial position for the year then ended have been compiled by us.

A compilation is limited to presenting in the form of financial statements information that is the representation of management. We have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

As discussed in the Association's financial statements under note 2 to the statements, Consolidated Rail Corporation (Conrail) securities are valued at cost, which equals their redemption value. As described in notes 4, 5, and 6 to the statements, current conditions arising from the provisions of the Northeast Rail Service Act of 1981 created uncertainties regarding the Association's interest in Conrail. Pursuant to these provisions, the Association's interest in the investments in Conrail as well as the loans receivable from the Delaware and Hudson Railway Company is limited to an interest which attaches to such debt in the event of bankruptcy, substantial sale, or liquidation of the assets of these railroads. In addition, notes and loans receivable from Conrail and the bankrupt estates plus the accrued interest receivable on these notes and loans, as shown in notes to the statement, are subject to legal settlements of reorganization plans of the bankrupt estates.

We are not independent with respect to the Association since the Comptroller General is an active member of its Board of Directors.

W D Campbell
W. D. Campbell
Acting Director



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(See Accountant's Compilation Report)

UNITED STATES RAILWAY ASSOCIATION

STATEMENT OF FINANCIAL POSITION

AS OF SEPTEMBER 30, 1981

	----- (thousands) -----	
ASSETS:		
Cash	\$	22
Letters of credit (note 3)		340,750
Short term investments		112
Advances and prepaid expenses		18
Interest receivable (notes 4)	\$	84,373
Loans receivable (note 5)		<u>164,476</u>
		248,849
Less allowance for loan losses		<u>66,515</u>
Notes receivable (note 6)		182,334
Furniture and equipment		60,863
Investments: (note 6)		1,178
Conrail 7.5 percent debentures, due January 1, 2011		1,000,000
Conrail Series A preferred stock		<u>2,548,784</u>
		<u>3,548,784</u>
Total assets		<u>\$4,134,061</u>
LIABILITIES AND EQUITY:		
Liabilities:		
Accounts payable and accrued liabilities	\$	3,286
Interest payable		13,793
Loans payable (note 7)		214,953
Commitments (note 8)		
Total liabilities		<u>232,032</u>
Equity:		
Appropriations (note 9)		337,503
Contributed capital		3,281,178
Retained earnings		<u>283,348</u>
Total equity		<u>3,902,029</u>
Total liabilities and equity		<u>\$4,134,061</u>

The accompanying notes are an integral part of this statement.

(See Accountant's Compilation Report)

UNITED STATES RAILWAY ASSOCIATION

STATEMENT OF OPERATIONS

FOR THE YEAR ENDED SEPTEMBER 30, 1981

(thousands)

REVENUES:	
Interest income--Conrail securities	\$ 77,041
Financing income--section 211 loans	<u>34,933</u>
Total revenues	<u>111,974</u>
OPERATING EXPENSES:	
Personnel compensation and related benefits (note 10)	11,572
Travel, relocation, and representation	428
Printing and expendable items	337
Rent, utilities, and communications	1,944
Contractual administrative services	467
Contractual professional services	11,216
Financing expenses--section 211 loans	43,252
Allowance for loan losses	<u>66,515</u>
Total expenses	<u>135,731</u>
OPERATING LOSS BEFORE APPROPRIATIONS	(23,757)
APPROPRIATIONS	<u>25,964</u>
NET INCOME	<u>2,207</u>
RETAINED EARNINGS, BEGINNING OF YEAR (restated)	281,158
RETAINED EARNINGS END OF YEAR	<u>\$283,365</u>

The accompanying notes are an integral part of this statement.

(See Accountant's Compilation Report)

UNITED STATES RAILWAY ASSOCIATION
STATEMENT OF CHANGES IN FINANCIAL POSITION
FOR THE YEAR ENDED SEPTEMBER 30, 1981

(thousands)

SOURCES OF FUNDS:	
From operations:	
Operating loss before appropriations	\$ (23,757)
Add item not requiring funds:	
Allowance for loan losses	<u>66,515</u>
Total funds from operations before appropriations	42,758
1981 appropriation for operations	29,000
1981 appropriation for Conrail securities	485,000
Transfer from Federal Railroad Administration	15,000
Increase in accounts payable and accrued liabilities	299
Decrease in:	
Accounts receivable, advances, and prepaid expenses	102
Interest receivable	63,527
Loans receivable	<u>219,689</u>
Total sources of funds	<u>855,375</u>
USES OF FUNDS:	
Purchase of:	
Conrail Series A preferred stock	165,000
Furniture and equipment	687
Increases in notes receivable	60,863
Decrease in:	
Interest payable	10,143
Loans payable	266,828
Conrail Series A preferred stock received as payment of interest	<u>14,137</u>
Total use of funds	<u>517,658</u>
Increase in cash, letters of credit, and short term investments	337,717
Cash, letters of credit, and short term investments- beginning of year	<u>3,167</u>
Cash, letters of credit, and short term investments- end of year	<u>\$340,884</u>

The accompanying notes are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

SEPTEMBER 30, 1981

1. THE ASSOCIATION. The United Railway Association (Association) is a Government corporation under section 201 of the Government Corporation Control Act. The Association was established by Congress under the Regional Railway Reorganization Act of 1973 (3R Act) to plan and finance the restructuring of the Nation's largest railroad, the Penn Central, and seven smaller bankrupt rail carriers in the Northeast and Midwest. The purpose of the 3R Act is to preserve essential rail services in the region at the least possible cost to the taxpayer.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES. The following is a summary of significant accounting policies of the United States Railway Association:
 - Assets, liabilities, revenues, and expenses are recognized on an accrual basis of accounting.
 - Federal Government appropriations used for the purchase of capital assets are recognized as contributed capital in the year that liabilities related to these purchases are incurred. Federal Government appropriations used for operating expenses are recognized as income in the year that liabilities for these expenses are incurred. (See note 9.)
 - Loans receivable are stated at face value of loan agreements. Allowance for loan losses is adjusted at the end of the fiscal year to an amount equal to 100 percent of the section 211(a) receivables including interest plus an amount equal to the historical loss percentage on contested amounts of section 211(h) receivables including interest.
 - Notes receivable are stated at face value. They are "contingent interest notes" received by the Association in payment of interest on Conrail 7.5 percent debentures.
 - Furniture and equipment items costing \$200 or more are capitalized and stated at cost without allowance for depreciation. Depreciation expense is not recognized due to the temporary nature of the Association's existence and the relative immateriality of the depreciation expense amounts involved.
 - Holdings in Conrail Series A preferred stock resulting from purchases are stated at cost (\$100 per share). Shares received in payment of interest due on Conrail debentures are stated at redemption value (\$100 per share).

3. LETTERS OF CREDIT. The letters of credit represent funds available at the U.S. Treasury which may be drawn on as needed by the Association to meet operating expenses and to purchase capital assets as authorized by the Congress.

4. INTEREST RECEIVABLE. Interest receivable as of September 30, 1981, consisted of accrued interest on the following investments and loans:

Conrail 7.5 percent debentures	\$31,438,356
Notes receivable	2,041,002
Section 211(a) loans	12,725,849
Section 211(h) loans	<u>38,168,046</u>
Total	<u>\$84,373,253</u>

Interest payments on Conrail 7.5 percent debentures are due on April 30 each year. As provided in the financing agreement between the Association and Conrail, interest on these debentures may be paid in Conrail Series A preferred stock or notes receivable, which are "contingent interest notes," if cash is not available. To date, all interest payments have been in the form of stock and notes.

Interest receivable on section 211(a) loans consisted of \$1,340,957 accrued but not due until December 20, 1981, and \$11,384,892 due but deferred by the Association's Board of Directors.

Interest receivable on section 211(h) loans consisted of \$9,980,010 accrued but not due until October 31, 1981, and \$28,188,036 resulting from the compounding of interest in accordance with financing agreements.

5. LOANS RECEIVABLE. Loans receivable as of September 30, 1981, consisted of loans made under section 211(a) and section 211(h) of the 3R Act, as follows:

Section 211(a) loans:	
Delaware and Hudson Railway Company (D&H)	\$ 37,250,000
Section 211(h) loans:	
Conrail	\$48,519,890
Reading Railway Company	25,945,700
Erie Lackawanna Railway Company	24,263,393
Central Railroad of New Jersey	20,267,693
Other estates	<u>8,228,853</u>
Total	<u>\$164,475,529</u>

DELAWARE AND HUDSON RAILWAY

The Delaware and Hudson Railway Company's indebtedness to the Association represents loans made pursuant to section 211(a) of the Regional Rail Reorganization Act of 1973 (3R Act) and interest accrued thereon.

During fiscal 1978, the Association's Board of Directors informed the Congress that it could no longer make the required legal findings as to D&H's ability to repay its loans. Congress responded by enacting Public Law 95-611 which liberalized the loan conditions governing D&H. In November 1979, Congress enacted legislation permitting an increase in the D&H loan authorization from \$30 million to \$34 million. D&H's loan eligibility was increased to \$37.5 million in October 1980.

Section 1164(c)(1) of the Northeast Rail Service Act of 1981 (NRS Act) provides that in the event of an agreement between a railroad which received a loan under section 211(a) of the 3R Act and the prospective purchaser of such railroad, the Secretary of Transportation shall limit the interest of the United States in any debt of such a railroad to an interest which attaches to such debt in the event of bankruptcy, substantial sale, or liquidation of the assets of the railroad.

Section 1164(c)(2) of the NRS Act provides that any new debt issued by such a railroad subsequent to the issuance of the debt described in section 1164(c)(1) shall have higher priority in the event of bankruptcy, liquidation, or abandonment of the assets of such a railroad than a debt described in 1164(c)(1).

The Section 211(a) indebtedness of D&H to the Association falls within the purview of the legislation referred to above. Therefore, the amount of repayments which the Association may ultimately receive cannot be determined at this time.

CONRAIL

The Conrail section 211(h) indebtedness to the Association represents advances made to Conrail in its capacity as agent for bankrupt estates pursuant to section 211(h) of the 3R Act and interest accrued thereon. Advances of \$23.6 million were disbursed, as directed by Public Law 95-597, to pay health and life insurance premiums for retired employees of the bankrupt estates. The bankrupt estates' legal liability in regard to these payments has been challenged in court by the Penn Central Corporation.

Section 211(h)(6)(A) of the 3R Act provides that the Association shall, except in certain limited circumstances, forgive any 211(h) loan made to Conrail, and any interest thereon, on the third anniversary date of any such loan. Upon any such forgiveness, the Association, pursuant to section 211(h)(6)(B) of the 3R Act, has a direct claim against the estate of the railroad in reorganization whose obligations were paid with the proceeds of any 211(h) loan to Conrail.

The following schedule presents the forgiveness anniversary year of outstanding advances made to Conrail under section 211(h):

<u>FY</u>	<u>Amount</u>
82	\$33,062,095
83	5,512,449
84	<u>9,945,346</u>
	<u>\$48,519,890</u>

The amount of repayment which the Association may ultimately receive on advances made to Conrail under section 211(h) will be subject to reorganization plans approved for the bankrupt railroads.

READING RAILWAY COMPANY, CENTRAL RAILROAD OF NEW JERSEY,
ERIE LACKAWANNA RAILWAY COMPANY, AND OTHER ESTATES

The amounts due from the Central Railroad of New Jersey are evidenced by secured notes. The amounts due from the Reading Railway Company were paid in full during October 1981. The section 211(h) loans to the Erie Lackawanna and other estates are unsecured and are subject to legal settlements of reorganization plans of the bankrupt estates.

6. INVESTMENTS AND NOTES RECEIVABLE. The Association's investments in Conrail securities consist of:

- Conrail Series A preferred stock (22,800,000 shares purchased at \$100 per share and 2,687,840 shares received in payment of interest due on Conrail debentures carried at redemption value of \$100 per share).
- Conrail 7.5-percent debentures due January 1, 2011 (\$1,000,000,000).

The Association's \$60,863,000 notes receivable are "contingent interest notes" accepted from Conrail in lieu of cash payments of interest on the 7.5 percent debentures. These notes receivable have an 8-percent interest rate and mature January 1, 2011.

Section 401 of the 3R Act authorized the Secretary of Transportation to, under certain conditions, sell the interest of the United States in Conrail common stock which is held by the Secretary of Transportation. Section 402(a) of the 3R Act provides that prior to such a sale, the Secretary of Transportation shall substitute a receivable--"contingency notes" for the Conrail debt and preferred stock held by the Association.

The Association's interest in any "contingency notes" substituted for Conrail securities held by the Association would be limited

under section 402(a) of the 3R Act to the interest that the Association had in the underlying Conrail debt instruments and preferred stock in the event of bankruptcy of Conrail or a liquidation or substantial sale of Conrail's assets.

Conrail securities held by the Association would be directly affected by action taken by the Secretary of Transportation under sections 401 and 402 of the 3R Act. In addition, the \$60,863,200 of Conrail "contingent interest notes" received by the Association in payment of interest on Conrail 7.5-percent debentures would, by the Association's terms, assume the same priority in bankruptcy or similar proceedings as the Conrail 7.5-percent debentures. The "contingent interest notes" would, however, continue to accumulate interest at a rate of 8 percent per annum. Under the Association/Conrail financing agreement, the "contingent interest notes" shall become void and unenforceable in the event of payment or redemption by Conrail of the 7.5-percent debentures and the Series A preferred stock.

In light of the possibility that the Association's interest in its investments in Conrail securities may be substantially limited as a result of actions taken by the Secretary of Transportation pursuant to sections 401 and 402 of the 3R Act, the redemption value of Conrail securities held by the Association cannot be determined at this time.

Dividends on Conrail Series A preferred stock holdings are non-cumulative. The stock (\$1 par value) is redeemable at \$100 per share. Conditions governing payment of dividends and redemption of the stock are set forth in the financing agreement between the Association and Conrail. To date, no dividends have been received on Conrail preferred stock holdings.

7. LOANS PAYABLE. Loans payable as of September 30, 1981, consisted of amounts owed to the Federal Financing Bank (FFB) as follows:

Section 211(a) advances:		
Principal advances	\$ 37,126,000	
Advances to pay interest	<u>8,985,497</u>	\$ 46,111,497
Section 211(h) advances:		
Principal advances	120,145,507	
Advances to pay interest	<u>48,696,241</u>	<u>168,841,748</u>
Total		<u>\$214,953,245</u>

Approximately 1/20 of the principal advances and the advances to pay interest under section 211(a) were due on December 26, 1981. Payment was made through refinancing with the FFB. The same terms apply to the new agreement with a maturity date of June 26, 1982. All section 211(h) advances were due January 29, 1982. Payment was made through refinancing with the FFB. The new note matures on April 30, 1982.

8. COMMITMENTS. The Association has lease agreements for space rental with L'Enfant Plaza Properties, Inc., which expire January 31, 1983. The current annual rent under these agreements totals \$827,688.
9. APPROPRIATIONS. The amount shown as appropriations represents Federal Government appropriations which remain available for new obligations in fiscal 1982 and to pay for goods and services ordered during fiscal 1981 but not yet received. The status of the unobligated funds in each of the Association's two appropriations follow:

	<u>Appropriations</u>		
	<u>Operations</u>	<u>Purchase of Conrail Securities</u>	<u>Total</u>
	----- (thousands) -----		
Unobligated funds September 30, 1981	\$90	\$335,000	\$335,090
Less: Unobligated funds in expired appropriations	74	-	74
Funds to be trans- ferred to the Fed- eral Railway Admin- istration under Public Law 97-102	-	<u>235,000</u>	<u>235,000</u>
Funds available for new obligations in FY 1982	<u>\$16</u>	<u>\$100,000</u>	<u>\$100,016</u>

10. EMPLOYEE BENEFIT PLAN. The Association has a defined contribution plan for all full-time permanent employees. Under this plan, the Association contributes an amount equal to 5 percent of the employee's eligible earnings. Also, the employee may make an optional contribution at the rate of 1, 2, 3, or 4 percent of earnings which is matched by the Association. These funds are deposited in a trust held by the Riggs National Bank, Washington, D.C. The trust is fully funded each year by the Association. The plan's expense for fiscal 1981 was \$110,899.
11. ADDITIONAL NOTE. The Association issued certificates of value for conveyed assets transferred from bankrupt railroads to Conrail. These certificates represent the contingent liability of the Federal Government and are deposited with the Special Court. (This court was established by the Regional Rail Reorganization Act of 1973 to determine the Federal Government's liability for rail assets conveyed by bankrupt railroads to Conrail. The transferors originally submitted claims totaling approximately \$16 billion. The current claims against

the Federal Government by the remaining transferors are in excess of \$100 million, plus interest at the statutory rate.) The certificates guarantee the net liquidation value, with certain adjustments, of the assets conveyed to Conrail, and are redeemable in cash by the Association on or before December 31, 1987.

During the period since the publication of the Association's last financial statements, the Government parties have concluded settlements with eight transferors wherein certificates of value were redeemed in Federal funds for approximately \$2.67 billion, including interest at the statutory rate since April 1, 1976.

Also, during this period the Government parties and two additional transferors reached agreement in principal on the terms for settlement of their claims against the Federal Government for approximately \$60 million plus interest at the statutory rate from April 1, 1976, through closing.

The Federal Government's liability in connection with the certificates of value will be decided by the Special Court.

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