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AMTRAK

Deteriorated Financial and Operating Conditions Threaten Long-Term Viability

Statement for the Record
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Development Division

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Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to testify at this hearing on Amtrak. Today, we will present the findings from our recently issued report on Amtrak's financial and operating conditions[1] and comment on its recent request for appropriations. For fiscal year 1996, Amtrak requests $1.06 billion in federal assistance, a slight increase over fiscal year 1995's $1.01 billion appropriation. In summary, we found that:

-- Amtrak's financial and operating conditions have always been precarious but have deteriorated steadily since 1990 to the point where its ability to offer service over the current nationwide system is seriously threatened. Since 1971, Amtrak has received over $13 billion in federal funding. This support has increased from $640 million in 1990 to about $1 billion in 1995, but the increase has not covered the widening gap between Amtrak's expenses and revenues. Requirements for capital investment have grown, with unmet needs for equipment and improvements in facility and track now totaling several billion dollars.

-- Over the past several years, Amtrak has taken actions to address this situation by assuming debt, deferring maintenance, and reducing staffing. These actions, while necessary for day-to-day survival, have simultaneously diminished the quality and reliability of service and contributed to the decline in ridership and revenues. Most recently, on December 14, 1994, Amtrak announced an aggressive plan to reduce annual expenses by $430 million by adjusting routes and service frequencies, retiring its oldest cars, reducing staff, and improving service and productivity. These actions are directed at closing the gap between the expected operating deficit and federal grants for 1995. However, the gap will begin growing again in 1996, totalling $1.3 billion by 2001 (assuming federal and state support remain at 1995 levels), and the announced actions do not resolve Amtrak's need for equipment and improved facilities. Finally, the success of Amtrak's plan is very dependent on increased financial support from state and local governments as well as legislative changes, such as providing Amtrak with greater flexibility to contract out its work.

-- It is unlikely that Amtrak can overcome its problems in financing, capital investments, and service quality--and

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[1]<u>Intercity Passenger Rail: Financial and Operating Conditions Threaten Amtrak's Long-Term Viability</u> (GAO/RCED-95-71, Feb. 6, 1995).

continue to operate the existing 25,000-mile nationwide system--without significant increases in either passenger revenues or subsidies. Amtrak's ability to overcome these problems is limited by an unfavorable operating environment, including intense fare competition from airlines. In addition, Amtrak estimates that it needs over $4 billion to bring its equipment and facilities systemwide, and track in the Northeast Corridor, up to a state of good repair. Also, Amtrak must soon negotiate new labor agreements and may confront additional costs for new agreements with freight railroads to use their track.

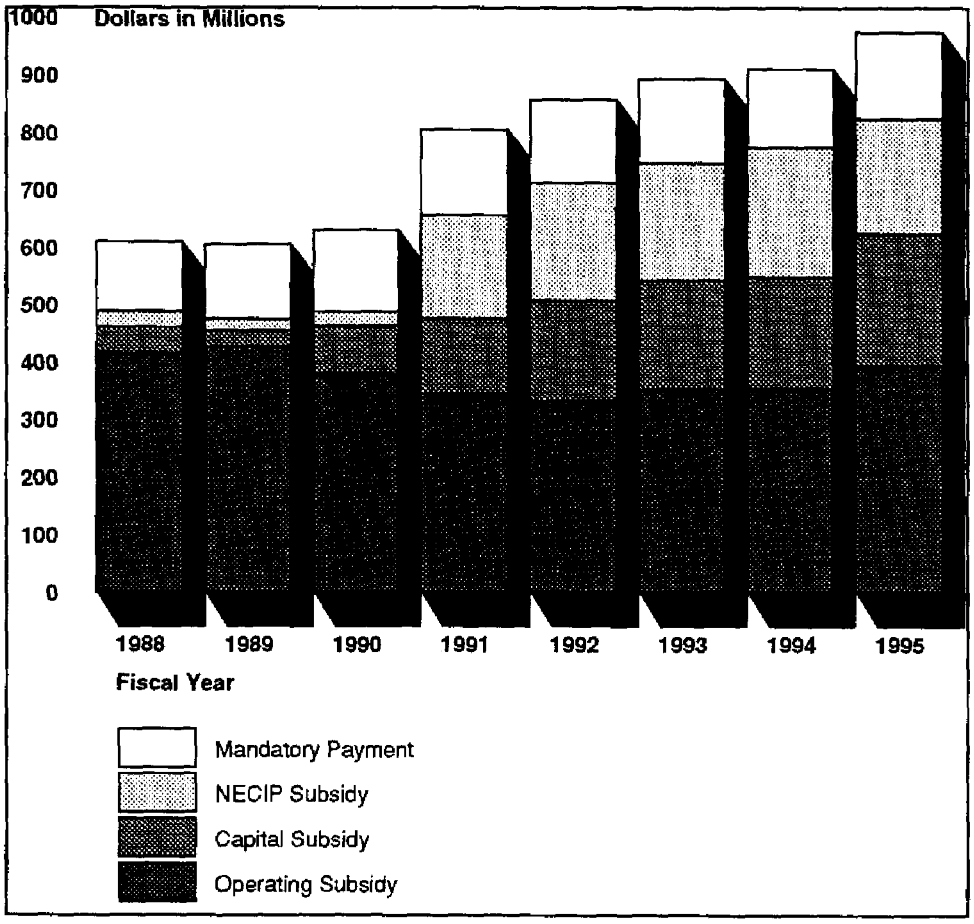
-- Determining Amtrak's requirement for federal operating and capital grants is complicated by a number of factors. While Amtrak's total grant request slightly exceeds its 1995 grant, Amtrak is requesting $260 million in operating assistance for fiscal year 1996, $132 million less than for fiscal year 1995. However, to cover total expenses Amtrak will need $311 million in additional revenues and/or state and local contributions. There is no way of telling whether this added income will materialize. Amtrak's request for $600 million in capital assistance is $170 million more than received in fiscal year 1995. However, the request is not sufficiently disaggregated for us to determine how much of the total capital grant request would be spent on the Northeast Corridor and how much would be spent elsewhere in the Amtrak system.

In light of Amtrak's serious financial and operating problems, our 1995 report offers several matters for congressional consideration relating to the scope of Amtrak's mission and its basic route network. Our report also recommends that Amtrak provide the Congress with cost and related information associated with various legislative proposals that Amtrak believes will further reduce its expenses.

GOVERNMENT SUPPORT FOR PASSENGER RAIL SERVICE

In 1995, out of a total budget of over $2 billion, Amtrak will receive $972 million from operating and capital grants, funds to improve the infrastructure that Amtrak owns in the Northeast, and a payment for retirement and unemployment benefits. (See fig. 1.)

Figure 1: Federal Appropriations for Amtrak, Fiscal Years 1988 Through 1995



Notes: Before fiscal year 1990, the Federal Railroad Administration's (FRA's) mandatory payments to the Railroad Retirement Trust Fund were included in Amtrak's operating grant; its payments to the fund for fiscal years 1988 through 1990 are estimated. The fiscal year 1993 appropriation includes $20 million in supplemental funds for operations and $25 million for capital.

Source: Amtrak.

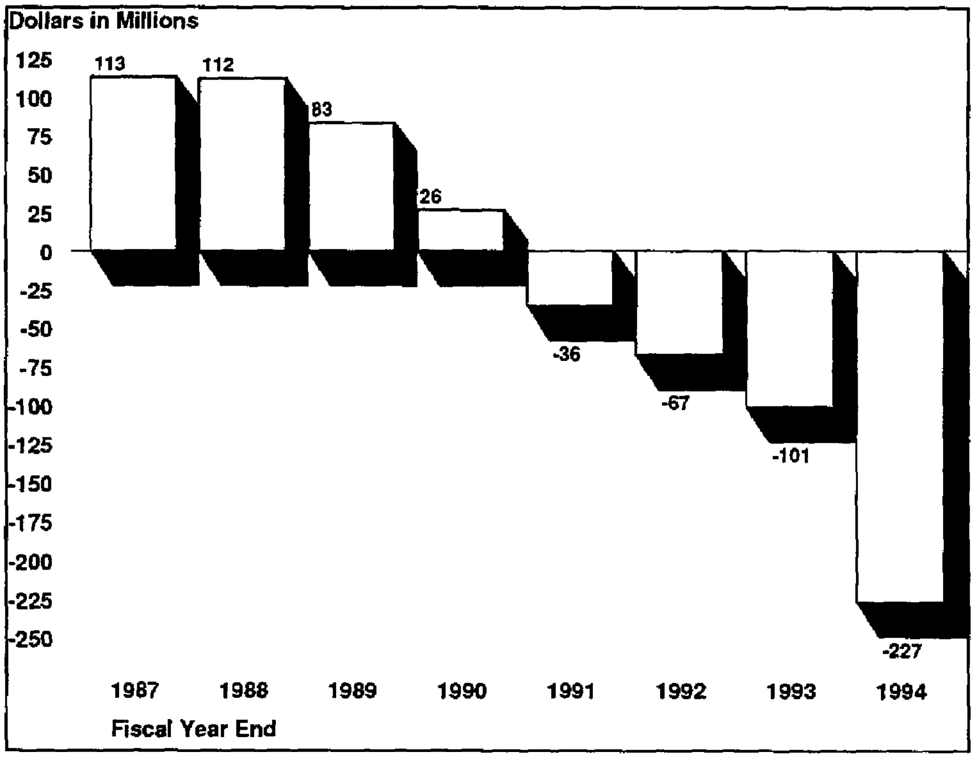
Among the world's passenger railroad systems, Amtrak is not unique in its need for government assistance. In Europe and Japan, where conditions are more conducive to rail travel, intercity passenger service requires substantial public support, including significant investments in the infrastructure. For example, France plans to invest nearly $25 billion in its railroad during the 1990s. This amount includes $6.8 billion for rolling stock, $5.3 billion for investments in infrastructure on high-speed lines, and $1.1 billion for other investments in infrastructure. Germany plans to invest over $70 billion in its main railway lines in the 1990s, including $28.8 billion for improvements in infrastructure, $18.5 billion in other upgrades, and $8.2 billion in equipment.

In the United States, other modes of transportation also have benefited to varying degrees from public investment and operating assistance. Some forms of travel, such as general aviation and mass transit, continue to receive substantial public support either in total or on a per-trip basis. In addition, unlike other transport modes, intercity rail does not have access to a trust fund to meet its capital investment needs.

AMTRAK'S FINANCIAL CONDITION HAS REACHED A CRITICAL STAGE

Over the years, Amtrak has made numerous attempts to reduce expenses and improve the efficiency of its operations. While these actions have served to hold down the corporation's operating deficit, they have not arrested Amtrak's financial decline. Since 1990, Amtrak's problems have accelerated. From 1991 to 1994, revenues were lower than projected, while expenses were higher than planned. Projected revenues did not materialize for a number of reasons, including declining service quality and competition from airlines. Amtrak overestimated passenger revenues by $600 million from 1991 through 1994. As a result, Amtrak's revenues and federal operating subsidies have not covered the operating deficit. To help cover the gap, Amtrak drew down its cash resources. At the end of 1994, it had a negative working capital balance of $227 million. (See fig. 2.) Amtrak also deferred maintenance on train equipment and reduced staffing levels and some services. Despite these efforts, the 1994 deficit exceeded the federal operating grant by $76 million. Amtrak projected that this gap would increase to almost $200 million in 1995.

Figure 2: Amtrak's Working Capital Surplus/Deficit, Fiscal Years 1987 Through 1994



Notes: Working capital is the difference between current assets and current liabilities.

Amounts are in current-year dollars. In 1994 dollars, working capital declined from $144 million in 1987 to a deficit of $227 million in 1994.

Source: GAO's analysis of Amtrak's data.

AMTRAK ANNOUNCES A PLAN TO ADDRESS FINANCIAL DIFFICULTIES

To address this situation, Amtrak is taking action to reduce its workforce by 5,600 positions (out of 25,000), eliminate 21 percent of the train miles of service it offers, and retire nearly all of its oldest passenger cars. On February 1, 1995, Amtrak implemented frequency reductions on three routes--between Atlanta and New Orleans; between New York and Tampa; and between St. Paul/Minneapolis and Portland Oregon. Amtrak has also announced plans to eliminate 3 routes and segments of 10 others, effective

April 1, 1995.[2] Also, Amtrak plans to achieve significant cost savings by contracting out maintenance work, consolidating crafts, reducing train and engine crews, and taking other actions to reduce costs and improve service.

The service cuts are part of Amtrak's Strategic and Business Plan first issued in January 1995. This plan proposes a number of actions to eliminate the gap between losses and federal support for fiscal year 1995 and to eventually reduce annual expenditures by $430 million. If nothing is done, Amtrak expects to lose more than $7.3 billion from 1995 to 2000. If federal subsidies stay constant at 1995 levels, the cumulative net losses after subsidy would be about $3.8 billion, again assuming that no actions are taken. Amtrak clearly had to take some action, and its new plan is an aggressive first step. Yet even if Amtrak could accomplish its entire plan, it still expects its losses to exceed the federal and state subsidies by $1.3 billion from 1996 through 2000, assuming that federal and state support remain constant at their 1995 levels. In February, 1995, Amtrak published a revised Strategic and Business Plan that included a scenario of declining, rather than level, federal support over the next five years. Under this scenario, Amtrak will need $311 million from revenue increases and state and local contributions in 1996, escalating to $750 million in 2000, to compensate for the decline in federal operating assistance.

Amtrak also has proposed a number of legislative initiatives that it believes will improve the railroad's long-term financial viability. For example, Amtrak proposes that states be given increased flexibility to use their federal transportation allocation to support intercity rail passenger service. Amtrak would also like relief from Railroad Retirement Act requirements. Other proposals include, but are not limited to being provided more freedom from legislation to collectively bargain for more efficient work practices, receiving increased track maintenance payments from commuters and freight railroads that use the Northeast Corridor, being provided the ability to issue tax-exempt debt, placing limitations on liability for punitive damages in personal injury cases, and receiving an exemption from federal fuel taxes.

Amtrak believes that its plan will help put the railroad on the road to financial recovery and that by the year 2002 Amtrak might be in a position to eliminate the need for federal operating subsidies while continuing to operate most of its existing service. However, an important underpinning of Amtrak's goal to eliminate

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[2]Amtrak has reached interim agreements with the states that would preserve at least some level of service on the Chicago to Milwaukee, St. Louis to Kansas City, and San Jose to Roseville routes. Discussions are ongoing with other states affected by route eliminations.

the need for operating subsidies are assumptions about changes in the current environment, including: (1) substantially more financial assistance from state and local governments, (2) greater flexibility in dealing with railroad labor, and (3) increased capital assistance to rectify the deteriorated condition of its infrastructure. Without these changes, the recently announced cuts will be just the beginning of route abandonments and service cutbacks.

Table 1 shows Amtrak's federal assistance for fiscal year 1995, its requested funding, and the administration's request for fiscal year 1996.

Table 1: Amtrak's Actual Appropriations for Fiscal Year 1995 and Amtrak's and the Administration's Fiscal Year 1996 Requests

Dollars in Millions

Category	Amtrak's actual appropriations, fiscal year 1995	Amtrak's request, fiscal year 1996	Administration's request, fiscal year 1996
Operating assistance	$392	$260	$300
Mandatory retirement payment	150	0	120
Transition costs	0	150	100
General capital	230	365	230
Northeast Corridor improvement	200	235	235
Farley Building	40	50	50
Total	$1,012	$1,060	$1,035

Source: Amtrak.

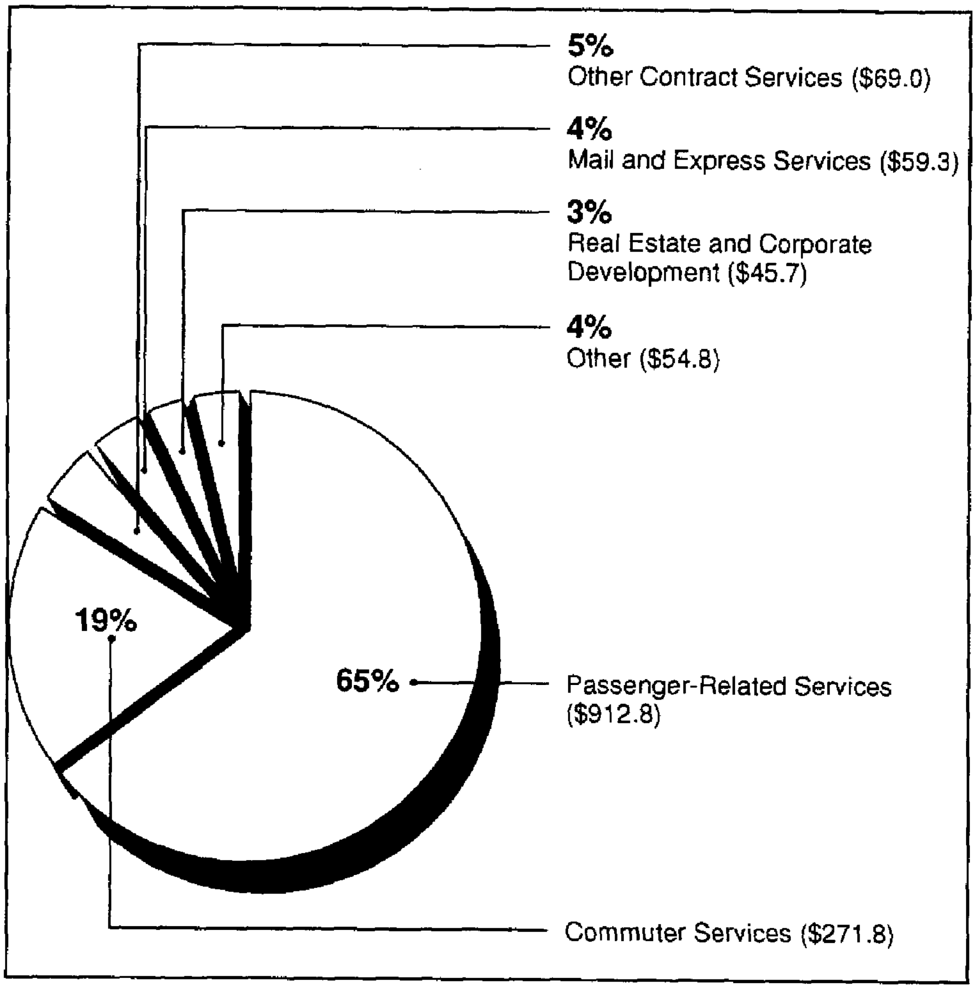
INCREASED REVENUES ARE NOT A LIKELY SOLUTION TO AMTRAK'S PROBLEMS

Increased contributions from state and local governments will be critical to closing Amtrak's projected budget gap because, as we stated in our 1995 report, passenger revenues are not likely to increase enough over the next few years to reverse Amtrak's deteriorating condition. None of Amtrak's routes--including those in the Northeast Corridor--are profitable when capital costs are taken into account. Revenues in the corridor cover about 65 percent of the routes' costs, compared with about 50 percent for routes elsewhere. Furthermore, passenger ticket revenues have declined about 14 percent in real terms--from over $1 billion in 1990 to about $880 million in 1994. The decline resulted from, among other things, a weak economy; intense price competition from airlines in certain markets; Amtrak's old and poorly maintained facilities and equipment; and accidents involving Amtrak trains. While the economy has recovered and the impact of train accidents has begun to abate, the other factors continue to inhibit ridership growth.

Amtrak's fastest growing source of revenues is its contracts to operate local commuter rail systems, which together carry about 7 million more passengers per year than the 22 million intercity passengers carried on Amtrak's intercity trains. These contracts generated over $270 million in 1994 and accounted for 19 percent of Amtrak's operating revenues. (See fig. 3.) Amtrak also believes that new high-speed rail service in selected corridors could increase its ridership and revenues. While high-speed service is now limited to the electrified portion of track between Washington, D.C., and New York City, Amtrak is extending electrification to Boston, improving the tracks, and hopes to purchase new trains that will allow high-speed service from Washington, D.C., to Boston beginning around the year 2000. Between 2000 and 2010, Amtrak expects its market share between New York City and Boston to grow to a level similar to its current 45-percent share between New York City and Washington, D.C.

Figure 3: Amtrak's Operating Revenues for Fiscal Year 1994

Dollars in Millions



Note: Total operating revenues were about $1.4 billion in fiscal year 1994.

Source: GAO's analysis of Amtrak's data.

AMTRAK MUST ADDRESS SIGNIFICANT CAPITAL INVESTMENT NEEDS AND POTENTIAL COST INCREASES

Replacing and modernizing Amtrak's physical assets--maintenance facilities, train equipment, and track--is more critical to the corporation's long-term financial well-being than resolving the current shortfall in operating funds. Disinvestment over the past decade has led to critical investment needs to bring infrastructure and rolling stock to a state of good repair. By the year 2010, Amtrak also will need substantial funding for Northeast Corridor infrastructure maintenance and to support high-speed rail.

Finally, Amtrak must address labor's wage demands and renegotiate freight railroad compensation agreements that expire in 1996.

Over a 10-year period, Amtrak's equipment and facilities depreciated at the rate of $200 million per year, while investment has averaged only $140 million. However, most of Amtrak's annual capital grant is already committed to paying off prior purchases and meeting legal mandates such as environmental cleanup. Also, because capital grants are subject to the annual appropriations process, it is difficult for Amtrak to formulate and implement long-term investment projects.

Investment Needed in Equipment and Facilities

The condition of Amtrak's physical plant---its cars, locomotives, maintenance facilities, stations, and track right-of-way---has deteriorated with heavy use and little capital invested to replace or rehabilitate these assets. Bringing these assets up to a state of good repair--the condition that should have been maintained over the years--will cost close to $4 billion, according to Amtrak's current estimates. (See table 2.)

Table 2: Capital Required to Achieve a State of Good Repair

Element	Estimated cost ($ millions)
Rolling stock replacement	$1,100
Rehabilitate maintenance facilities	200
Rehabilitate right-of-way between New York and Washington, D.C.	2,500
Total	$3,800

Much of Amtrak's rolling stock is old and worn out---31 percent of the cars and 54 percent of the locomotives are beyond their useful lives. Amtrak's recent retirement of much of its "Heritage Equipment", which was inherited from freight railroads when Amtrak was created, will improve the age profile for the passenger car fleet and reduce maintenance requirements. Purchasing new equipment, (mostly locomotives) at a cost of about $1.1 billion will allow Amtrak to retire rather than overhaul old equipment. Assuming Amtrak can purchase the needed equipment, overhaul costs would be $427 million between 1995 and 2002, according to an Amtrak financial management official. If Amtrak cannot replace the equipment, the amount needed for capital overhauls will be substantially higher during those years.

In addition, several of Amtrak's 18 maintenance facilities need substantial renovation and/or modernization, which Amtrak estimates will cost about $200 million. The Beech Grove, Indiana, facility is one of Amtrak's largest facilities and most in need of repair. Beech Grove, responsible for overhauls of and repairs to 61 percent of Amtrak's total fleet, is nearly 100 years old. At the facility, deteriorated track causes frequent derailments, buildings are run down, and some buildings cannot accommodate the work for which they are used. Amtrak estimates that renovating and modernizing this facility will cost over $38 million, including $9.8 million budgeted for fiscal year 1995.

Amtrak also estimates that it needs to invest about $2.5 billion to bring the Northeast Corridor right-of-way--track, signals, structures (e.g. bridges). electric traction (catenary[3] and related power structures), maintenance-of-way equipment, and tunnels--to a state of good repair. Much of this investment is needed on the south end of the corridor, between Washington, D.C., and New York, where Amtrak operates high-speed trains and has captured a large share of the transportation market. While Amtrak invested over $3 billion in this infrastructure in the past to make high-speed service possible, many elements are now heavily worn and in need of replacement. Amtrak will use $115 million of its 1995 Northeast Corridor Improvement Project appropriation to address its needs in this part of the corridor. However, this appropriation has traditionally been set aside for improvements to achieve high-speed service, as set out in the Railroad Revitalization and Regulatory Reform Act of 1976.

Additional $2.5 Billion Needed by 2010 to Achieve Reliable and Frequent High-Speed Service Between New York and Boston

In addition to achieving a state of good repair, Amtrak will need funds to continue improving the right-of-way between New York and Boston to support high-speed rail. To make these improvements, Amtrak will require about $2.5 billion--$900 million by 1999 to electrify the track and purchase high-speed trainsets and $1.6 billion between 1999 and 2010 to increase capacity and rehabilitate track. This funding will allow Amtrak to provide 16 high-speed trips per day between these cities. (See table 3.) Amtrak forecasts that its market share will increase to about 45 percent--similar to that between Washington and New York by the year 2010.

[3]Catenary is the overhead wire system that delivers electricity to the locomotive for traction, or movement.

Table 3: Estimated Cost of Northeast Corridor Maintenance and High-speed Upgrades Through the Year 2010

Dollars in Millions

Element	Estimated cost
Complete electrification, other upgrades, and purchase high-speed trainsets	$900
Capacity expansion	582
Infrastructure recapitalization and rehabilitation between New York and Boston	1,000[a]
Total	$2,482

[a]According to FRA, no clear time table exists for these repairs, but the needs will have to be addressed sometime "in the coming decades."

Source: Amtrak and FRA.

Amtrak plans to electrify the track between New York and Boston, purchase high-speed trainsets, and complete necessary infrastructure improvements (such as replacing ties, installing high-speed interlockings, and replacing some bridges) to allow 3-hour trip times. For improvements on the north end of the corridor, Congress had appropriated $712 million of this amount as of January 1995, and Amtrak estimates that it needs about $900 million more in appropriations to complete these improvements. In addition to these costs, FRA estimates that about $1 billion will be needed to rehabilitate or replace aging bridges, tunnels, or other key facilities on this part of the Corridor. FRA also estimates that $582 million will be needed around the turn of the century to expand capacity to accommodate Amtrak's 16 high-speed-trains-per-day schedule as well as anticipated growth in commuter and freight traffic on the corridor around the turn of the century. Amtrak expects that the commuter and freight railroads will contribute funds for these capacity improvements, but the exact contributions have not been determined.

Amtrak Faces Additional Costs

Labor costs are also a major factor in Amtrak's finances. Beginning in 1995, Amtrak will be negotiating changes to wages, benefits, and work rules with the 14 unions that represent 90 percent of its employees. Labor costs account for about 52 percent of Amtrak's operating costs. Amtrak has done a good job at improving labor productivity and hopes to achieve further increases in productivity if the Rail Passenger Service Act is amended to allow greater flexibility in negotiating the terms of its labor agreements. However, Amtrak already pays train and engine crews less on average than freight railroads pay for comparable jobs. Continuing to hold down labor costs will present a difficult challenge.

Amtrak could also face increased costs for track leases and liability coverage. Freight railroads own about 97 percent of the track over which Amtrak operates. In 1971, Amtrak entered into 25-year agreements with the freight railroads to compensate them for the use of their track and for related services. These agreements will expire in April 1996. Freight railroads are likely to seek increases in Amtrak's payments for incremental maintenance and liability coverage.

REASSESSMENT OF AMTRAK'S MISSION AND COMMITMENTS FOR FUNDING IS NEEDED

The Congress faces important decisions about the quality and extent of future intercity passenger rail service, including whether to maintain the current route system. Amtrak's fiscal crisis comes at a time when the federal government is not well positioned to provide the large sums of money required to bring the railroad up to a state of good repair and meet future capital needs. Passenger rail service competes for limited transportation funds, and unlike aviation, highways, and mass transit, it does not have access to a federal trust fund. State and local governments have some flexibility to allocate federal transportation funds among different modes, but their ability to assist intercity passenger rail is very limited.

Increased funding, especially capital investment, would improve service quality and encourage more riders. Doubling Amtrak's general capital grant to $500 million annually--a difficult task in today's fiscal environment--would allow Amtrak to improve maintenance facilities and its rights-of-way and purchase new equipment, primarily locomotives. But even if gains in efficiency and ridership resulted from such improvements, we estimate that Amtrak would continue to need more than $400 million in annual operating subsidies from some source through the year 2000. As described earlier, Amtrak also needs a total of $2.5 billion through the year 2010 for improvements to the north end of the Northeast Corridor.

If subsidies to Amtrak are eliminated and the railroad is privatized, it is unlikely that a nationwide passenger rail system could be preserved. Under this option, intercity service would be reduced to a few regional corridors, at most, because only a few well-traveled routes could potentially generate sufficient revenues to cover operating costs. Even in these cases, substantial federal investment in the infrastructure would likely be needed before the railroad was privatized.

If funding for Amtrak is reduced or maintained at its current level, we believe that the route network will have to be restructured and reduced beyond the recently announced changes so that quality service can be provided within the available funding. Options could be developed for routes commensurate with various levels of federal, state, and local funding. A basic network could be defined by determining where Amtrak carries the most passengers and has the greatest economic potential. Appendix I shows ridership levels throughout Amtrak's system in fiscal year 1993.

In this regard, we found that 11 of Amtrak's 44 routes earn 68 percent of Amtrak's revenues and account for 61 percent of the expenses. Also, interconnections between routes or the presence of important public benefits as defined by the Congress, such as helping alleviate congestion and pollution, would be relevant in evaluating how best to define the route network. The basic network could be augmented by regional routes supported by those states that were willing to contract with Amtrak to cover shortfalls between revenues and the full cost of operations.

CONCLUSIONS

Amtrak is at a critical juncture. A number of the issues raised by Amtrak's financial and operating condition clearly go beyond the ability of Amtrak and its board of directors to resolve and will require congressional consideration. These issues complicate this year's appropriations decisions. As our 1995 report stated, the Congress may wish to consider whether Amtrak's original mission of providing nationwide intercity passenger rail service, at the present level, is still appropriate. To facilitate the definition of the scope of Amtrak's mission, the Congress could direct Amtrak or a temporary commission, to make recommendations and offer options to the Congress defining and realigning Amtrak's basic route network so that efficient and quality service could be provided within the funding available from all sources. If the outcome of this process is a significantly scaled back Amtrak, Amtrak's capital requirements would be quite different than those needed to maintain the existing nationwide system.

Our report recommended that the President of Amtrak provide the Congress with cost and related information on proposed legislative changes that Amtrak believes could improve its long-term viability and the expected effect of these changes on Amtrak's finances and other affected parties. These include amending the Rail Passenger Service Act to allow greater flexibility in negotiating labor agreements with regard to labor protection and contracting out Amtrak work, removing from Amtrak's budget payments under the Railroad Retirement Act for non-Amtrak employees, authorizing Amtrak to issue tax-exempt debt, and exempting Amtrak from federal fuel taxes. This information will provide a vehicle for Congressional deliberation on the merits of each of Amtrak's legislative proposals.

Finally, in terms of this year's budget request, the Subcommittee may find clarification of several aspects of the request helpful. These include the specific timetable of Amtrak capital requirements over the next several years (assuming a given level of regional or nationwide service), clarification of the amount of the general capital request that will be used on the Northeast Corridor, and Amtrak's plan for obtaining additional revenues and state and local support, and the consequences of not obtaining these.

APPENDIX I

Source: Amtrak
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