

**Before the Subcommittee on Transportation,  
Committee on Appropriations,  
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# **Assessing Amtrak's Future**

**Statement of  
The Honorable Kenneth M. Mead  
Inspector General  
U.S. Department of Transportation**



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Mr. Chairman and Members of the Subcommittee:

We appreciate the opportunity to testify on Amtrak's financial future.

Our testimony today will focus on (1) the independent assessment of Amtrak and its oversight by the Office of Inspector General, (2) the meaning of financial self-sufficiency as it relates to Amtrak, and (3) our work on the Northeast Corridor.

### Assessing Amtrak's Financial Status

In the Amtrak Reform and Accountability Act of 1997, Congress directed the Secretary of Transportation to contract for an independent assessment of Amtrak's financial requirements through Fiscal Year (FY) 2002. The assessment will examine Amtrak's operations, accounting and bidding practices, and Strategic Business Plan. It will also determine whether Amtrak's plans and projections for reaching self-sufficiency are reasonable, realistic, and based on sound business practices. The Office of Inspector General is directed to, and will, oversee this assessment, which will begin in April and be completed before the end of this fiscal year.

Amtrak's revised Strategic Business Plan, which was adopted by its Board of Directors on March 10, 1998, contains a number of core assumptions that Amtrak believes must materialize in order to achieve self-sufficiency. These assumptions, which specify revenue targets, expense goals, and funding levels, comprise what Amtrak terms its "glidepath" to self-sufficiency. An essential part of the independent assessment involves a close scrutiny of these assumptions.

- First, Amtrak projects annual revenues will increase from \$1.7 billion in FY 1997 to \$2.3 billion by the end of FY 2002. Most of this revenue increase is expected in FYs 2000 and 2001 and will primarily reflect revenues realized from the introduction of high-speed rail service. Total *passenger revenue* is projected to grow by 18 percent in FY 2000 and 10 percent in FY 2001; this compares to about 7 percent and 5 percent growth projected for FY 1998 and FY 1999, respectively, and actual growth in FY 1997 of 7 percent. Initiating, marketing, and operating high-speed rail service entails considerable uncertainty over its operating costs and the net revenue it will generate. Amtrak believes that its revenue projections for this new service are conservative and realistic. Validating Amtrak's forecasting methodology and the assumptions behind it are key elements of the independent assessment.

- Second, Amtrak plans to limit operating cost growth. Amtrak projects an average annual increase in operating costs of 3.75 percent through FY 2002, which is only slightly more than the annual average cost growth of 3.6 percent for the last 5 years. Limiting cost growth through FY 2002 will be particularly challenging as Amtrak incurs significant costs related to starting and operating high-speed rail service. Amtrak's cost growth projections, however, depend on instituting an array of productivity enhancements and cost saving measures. The independent assessment will validate the assumptions and methods used to project costs for Amtrak's various markets and services to determine whether these projections are reasonable.
- Third, the Amtrak Reform and Accountability Act of 1997 authorized \$5.2 billion for Amtrak, of which the Administration proposes to spend \$2.2 billion for capital assistance between FY 1999 and FY 2002. Amtrak also received an additional \$2.2 billion in capital assistance under the Taxpayer Relief Act of 1997.<sup>1</sup> In light of Amtrak's capital requirements, and its plans to use the assistance provided by these two Acts, this level of capital assistance will not be sufficient to address all of Amtrak's capital requirements. Many of Amtrak's plans for operating cost savings hinge on the successful completion of capital projects. For example, Amtrak recently completed construction of a new Consolidated National Operations Center in Wilmington, Delaware. This project will centralize work formerly conducted at four sites and save Amtrak a projected \$6.1 million between FY 1998 and FY 2003. If funds are not available for capital projects such as this, the associated cost savings reflected in Amtrak's Strategic Business Plan will not be realized. One of the major tasks of the independent assessment is to conduct an analysis of Amtrak's existing and projected capital requirements and investments throughout its system.
- Finally, the current plan is predicated on Amtrak's ability to use Federal capital funding for the maintenance of equipment, infrastructure, and facilities. Amtrak's maintenance costs, such as repairing track and switches, and reconditioning rail car components, have generally been considered operating expenses, and generally have not been paid with Federal capital assistance. Complete rebuilding of track, purchase of new locomotives and rail cars, and construction of new facilities are generally considered capital expenses, and have been paid with capital assistance. We are discussing with the Surface Transportation Board the definitions of capital and operating expenses as they are applied to the freight railroads; we will be sharing our findings with you shortly. Amtrak's revised Strategic Business Plan assumes that it will be able

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<sup>1</sup> The Taxpayer Relief Act of 1997 provides \$2.32 billion in capital funds, of which \$139 million must be set aside for the six non-Amtrak states. These are: Alaska, Hawaii, Maine, Oklahoma, South Dakota, and Wyoming.

to apply a more flexible definition of capital, one that will allow it to use its capital grants to pay for some of its maintenance expenses. This proposed change has clouded the issue of Amtrak's self-sufficiency from Federal operating support.

### Concept of Self-Sufficiency

Legislation contemplates that Amtrak will achieve operating self-sufficiency by FY 2002. *Clarity is needed on what this means.* From Amtrak's perspective, self-sufficiency has meant no operating subsidy, but has never meant operating without Federal capital assistance.

If Amtrak is correct, the definition of what constitutes an "operating" expense and what constitutes a "capital" expense becomes quite significant. This is because the Administration's FY 1999 budget does not request operating assistance for Amtrak. Instead, the request is for a \$621 million capital grant. This is over and above the \$2.2 billion in capital funds provided by the Taxpayer Relief Act. If the change in the definition of capital is approved, Amtrak has indicated that as much as \$542 million of the requested \$621 million grant may be used to pay for maintenance of equipment, infrastructure, and facilities -- expenditures formerly considered to be in the operating expense category. In FY 1997, Amtrak spent \$500 million for these maintenance categories.

We doubt that this change in nomenclature means that Amtrak has already achieved "operating" self-sufficiency. However, for planning purposes, and to avoid controversy as Amtrak proceeds on its glidepath to FY 2002, it is important for all parties to have an understanding of whether this expanded definition of capital can be relied upon in determining: (1) when Amtrak has achieved self-sufficiency, and (2) what type of expenses Amtrak's passenger and other revenues are expected to cover.

### Northeast Corridor

Finally, one of Amtrak's long-standing goals has been to significantly increase revenues by the introduction of high-speed rail service in the Northeast Corridor. In FY 2001, Amtrak projects a net contribution of \$150 million from the Northeast Corridor after introduction of this service. This contrasts markedly with Amtrak's net cash loss of \$94 million for the Northeast Corridor in FY 1997.<sup>2</sup>

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<sup>2</sup> These figures are for Core operations and consist principally of passenger revenue.

High speed rail service is scheduled to start in October 1999. The electrification project north of New Haven, Connecticut has fallen behind schedule several times, but Amtrak believes that with the current aggressive recovery schedule now in place, the project will finish on time for an October start-up. However, performance testing on the system that was originally scheduled to be completed in July 1999, is now not scheduled to be finished until October 10, 1999. While Amtrak plans to test and finish construction of the system *concurrently*, this is still a tight schedule, and Amtrak will have little time to correct problems found during testing. If the October 1999 start-up date slips, Amtrak could miss out on the significant revenues generated by high-volume, year-end holiday traffic.

Even though Amtrak has invested significantly in the infrastructure between New York City and Boston, Massachusetts in preparation for high-speed rail service, there are still needs that must be addressed. Last fall, a Metro North commuter train pulled down a mile-long section of overhead wire from the 90-year old catenary system, stranding 40,000 travelers for over four hours. In 1997, catenary-related delays occurred no fewer than 39 times. Neither Amtrak nor Metro North Railroad, which operate along this section of track; nor the Connecticut Department of Transportation, which owns the track, have any short-term plans to replace this catenary -- a project estimated to cost \$200 million.

In addition, on the south end, between Washington, D.C. and New York City, Amtrak has preliminary estimates that, over the next 20 years, it will cost between \$7 and \$9 billion to repair and upgrade the infrastructure. Unless Amtrak addresses the infrastructure problems along the entire Corridor, and improves reliability -- ridership and revenue are likely to fall short of projections, even with the introduction of high-speed rail service, as passengers turn to other modes of transportation. A key requirement in the independent assessment will be to determine whether Amtrak's funding, plans, and schedules are adequate to address capital needs in the Northeast Corridor and systemwide.

## **BACKGROUND**

### **INDEPENDENT ASSESSMENT OF AMTRAK MANDATED BY CONGRESS**

The Amtrak Reform and Accountability Act of 1997, signed by the President on December 2, 1997, requires that the Secretary of Transportation contract for an independent assessment of the financial requirements of Amtrak through FY 2002. The Inspector General of the Department of Transportation (DOT) is directed to oversee this assessment, which must be completed within 180 days of the contract award.

#### **Independent Assessment Will Begin in April**

We are pleased to tell the Subcommittee that a competitive bidding process is almost concluded, and a contract will be awarded in April. The contractor selected will assemble a team of experts in the fields of rail operations and finance, travel and revenue forecasting, and financial modeling. The independent assessment will include a review of Amtrak's revised Strategic Business Plan and other documents to assess Amtrak's current and future financial requirements. This assessment will establish a solid set of numbers that will provide a benchmark for assessing Amtrak's financial needs. *We will provide the results of this assessment to*

*Congress before the end of this fiscal year.*

We assure you that throughout this assessment, the Office of Inspector General will be on-site and present with the contractor for all phases of the assessment. This will help us fulfill our Congressional mandate to oversee this work and to conduct our own assessments in the years ahead. We believe the results of this assessment will be invaluable to Congress, Amtrak's new Board of Directors, and the Amtrak Reform Council in making critical funding and strategic business decisions.

#### Independent Assessment of Amtrak's Financial Condition

*One of the first tasks of the independent assessment will be an evaluation of Amtrak's current financial status.* This involves reviewing Amtrak's accounting systems; its method of allocating costs and revenues; and recent trends in costs, revenues, and ridership.

The independent assessment will provide an understanding of the actual costs and revenues associated with specific routes, regional areas, and Strategic Business Units. Another task is to assess Amtrak's capital funding needs to determine whether Amtrak has planned for sufficient funds to achieve its goals. In addition, the assessment will review Amtrak's bidding procedures used in securing contracts

for services other than the provision of intercity passenger rail or mail and express service. Such contracts include providing passenger rail service or maintenance for local commuter railroads, such as Amtrak's recent bid on the overhaul of rail cars for New Jersey Transit. The assessment will review Amtrak's methods for estimating its costs of providing such service to determine whether Amtrak reflects direct and indirect costs in its bids.

To the extent possible, the assessment will determine whether fluctuations in revenue or ridership result directly from Amtrak's actions, inactions, or services provided, or whether they are caused by *forces outside of Amtrak's control*. For instance, in FY 1997, unanticipated weather-related events, such as Hurricane Fran, severe weather conditions on the West Coast, and flooding in the Midwest, resulted in \$14 million in unforeseen costs. In addition, service shutdowns precluded opportunities to earn revenue that might otherwise have been realized during these events. Learning where Amtrak stands financially, and why, will assist you and Amtrak's new leadership, in making decisions about Amtrak's future.

#### Assessment Will Review Amtrak's Revised Strategic Business Plan

On March 10, 1998, the Amtrak Board of Directors adopted a revised Strategic Business Plan. This plan details Amtrak's efforts to *reach operating*

*self-sufficiency by the end of FY 2002.* The plan was revised in response to key internal and external events that have occurred in the past year. These events include:

- Enactment of the Amtrak Reform and Accountability Act of 1997 which established an Amtrak Reform Council and mandated this independent assessment;
- A proposed FY 1999 DOT budget that changes the fundamental structure of Amtrak's traditional Federal support by providing only a capital grant;
- A change in Amtrak's leadership; and
- Internal and external events that affected forecasted revenues and expenses.

Amtrak's revised Strategic Business Plan identifies a series of steps to eliminate the need for Federal operating assistance by the end of FY 2002. The steps are based on continued Federal capital assistance and a series of revenue-enhancing initiatives.

The Strategic Business Plan has a number of core assumptions: *(1) significantly increasing revenue; (2) limiting operating cost growth; (3) receiving the fully authorized amount of Federal capital assistance; and (4) obtaining the ability to use Federal capital assistance for maintenance of equipment, infrastructure, and facilities.*

## Revenue Projections

One of the most critical assumptions of the revised Strategic Business Plan is Amtrak's ability to increase passenger-related and other revenues. *The plan forecasts a significant growth in passenger-related revenues through FY 2002.*

Most of the \$576 million revenue increase is expected in FYs 2000 and 2001 and will primarily reflect revenues realized from the introduction of high-speed rail service in the Northeast Corridor. Other significant revenue increases are related to Amtrak's Express Cargo service (from \$3 million in FY 1997 to \$71 million in FY 2002) and Mail service (from \$66 million in FY 1997 to \$86 million in FY 2002).

## Limiting Cost Growth

Amtrak projects an average annual increase in operating costs of 3.75 percent through FY 2002. To accomplish this, Amtrak has a series of Business Plan Actions aimed at limiting cost growth. For example, productivity enhancements are projected to yield \$122 million in cost savings in FY 2002. We note that in 1996, Amtrak anticipated it could realize immediate savings of between \$22 million and \$30 million by purchasing power wholesale for its own use. Amtrak's proposed wholesale power supplier, Enron Power Marketing, has filed a petition with the Federal Energy Regulatory Commission (FERC) requesting

access to a transmission network that would allow it to supply electricity to Amtrak. This matter is currently pending at FERC.

### Amtrak's Plan is Dependent on Receiving Fully Authorized Federal Capital Assistance

A significant part of Amtrak's revenue-enhancing and operating cost reduction initiatives depends on whether Amtrak receives fully authorized amounts of Federal capital assistance. Although Federal capital grants increased in the early 1990's, *Amtrak's capital needs are still significant*. In 1995, Amtrak developed an initial plan to reach its goal of zero-operating grants. The plan was predicated on receiving an assumed level of Federal capital and operating assistance, coupled with revenue-enhancing initiatives, such as high-speed rail service in the Northeast Corridor. However, in FYs 1995 through 1997, Amtrak's funding fell short of what was assumed in its planning by \$139 million.

### Ability to Use Federal Capital Assistance for Maintenance of Equipment, Infrastructure, and Facilities

In its FY 1999 budget, Amtrak has requested permission from Congress to use a more flexible definition of the term "capital." Examples of Amtrak's traditional capital expenditures include the purchase of locomotives and passenger rail cars, complete rebuilding of track, and construction of new facilities. Maintenance costs, such as the cost of repairing track and switches, and reconditioning rail car

components, are generally considered operating expenses and therefore not generally paid with capital funds. If Congress approves Amtrak's request, Amtrak intends to use capital assistance to cover routine maintenance of equipment, infrastructure, and facilities. Using this expanded definition of capital spending, Amtrak's ability to function without Federal operating assistance will not mean what it did when Amtrak established this goal in 1995.

### **AMTRAK'S STEPS TOWARD ACHIEVING SELF-SUFFICIENCY**

Amtrak's Strategic Business Plan contemplates achieving self-sufficiency by FY 2002. Amtrak defines self-sufficiency as *eliminating the need for Federal operating assistance but a continuation of Federal capital assistance*. The Administration's FY 1999 budget requests no operating assistance, but does request \$621 million of capital assistance. Amtrak intends to use up to \$542 million of this capital assistance for maintenance of equipment, infrastructure, and facilities -- costs generally considered operating expenses. The \$621 million is over and above the \$2.2 billion in capital funds provided to Amtrak in the Taxpayer Relief Act of 1997.

## Independent Assessment to Review Amtrak's Self-Sufficiency Goal

The independent assessment will determine whether Amtrak's financial plans provide the framework for it to operate without Federal operating assistance after FY 2002, and to reach other financial goals as stated in its revised Strategic Business Plan. In addition, the assessment will determine the likelihood that Amtrak will be able to maintain its financial status beyond FY 2002. For instance, if Amtrak were to borrow heavily in order to reach its goal of self-sufficiency, *the assessment would determine whether Amtrak's revenues and Federal assistance would be sufficient to service the debt beyond FY 2002.* The assessment will also determine the likely effect of deferred maintenance and aging rolling stock on Amtrak's continued viability.

## **HIGH-SPEED RAIL SERVICE PLANNED FOR AMTRAK'S NORTHEAST CORRIDOR**

The Northeast Corridor from Boston, Massachusetts to Washington, D.C. is 441 miles in length and serves a population of 36 million people. Amtrak owns 362 miles of the Corridor and the rest is owned by the Metropolitan Transportation Authority of New York, the Connecticut Department of Transportation, and the Massachusetts Bay Transportation Authority. More than 1,000 trains a day use the

Corridor, including those of Amtrak, eight commuter railroads,<sup>3</sup> and four freight railroads.<sup>4</sup>

In 1991, Congress and Amtrak focused on the improvements needed to implement high speed, 3-hour service between Boston and New York City, referred to as the north end. These improvements include the purchase of new, high-speed trainsets, installation of an overhead electrical system between New Haven, Connecticut, and Boston, and other infrastructure improvements between New York City and Boston. When these components are complete, trip time on the north end is expected to decrease from 4 hours, 45 minutes, to 3 hours, 10 minutes.<sup>5</sup> The high-speed rail project also includes infrastructure improvements between Washington, D.C. and New York City, referred to as the south end. When the high-speed trainsets begin operating, trip time on the south end is expected to be reduced from 3 hours to 2 hours, 45 minutes.

#### High Speed Service Begins in 1999

When all construction between New York and Boston is complete, Amtrak will offer high speed service of 3 hours, 40 minutes, using current equipment. This service is scheduled to start in October 1999, the same month operational testing is

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<sup>3</sup> Maryland Rail Commuter Service; Southeastern Pennsylvania Transportation Authority; New Jersey Transit; Port Authority Trans Hudson Corporation; Long Island Railroad; Metro-North Commuter Railroad; Shore Line East; and Massachusetts Bay Transportation Authority.

<sup>4</sup> Springfield Terminal Railway; Providence and Worcester; Connecticut Southern; and Conrail.

scheduled to be completed. *Amtrak plans to phase in 18 new, high-speed trainsets capable of achieving speeds of 150 miles per hour, further reducing the trip time to 3 hours, 10 minutes.* This is a tight schedule, and if a delay occurs, the increased revenue Amtrak expects to realize from high speed service will likely be affected, threatening Amtrak's ability to obtain self-sufficiency.

### Infrastructure Upgrades Are Needed

Aging infrastructure in all parts of the Northeast Corridor continues to affect the reliability of Amtrak's service. Preliminary estimates from Amtrak indicate that *over the next 20 years, between \$7 and \$9 billion will be required to repair and upgrade the south end infrastructure.* Capital improvements are needed to address the significant increases in congestion related to commuter and freight traffic, including major rebuilding of track, construction of new facilities, installation of additional safety equipment, and infrastructure improvements.

Commuter rail traffic along the Northeast Corridor has increased significantly since 1992. As a result, congestion has slowed service for all Corridor users -- freight, commuter, and Amtrak. Ridership projections for the major commuter operators forecast significant growth by the year 2010. For example, in 1992, the Long Island Railroad projected ridership growth of 20 percent by FY 2010. Their

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<sup>5</sup> The Congressional mandate calls for 3 hour service, which Amtrak expects to offer in later years after significant infrastructure improvements are complete.

recently revised projection for the same period of time is now a 40 percent increase. To meet the Congressional mandate of 2 hours, 30 minute service between New York and Washington, D.C., Amtrak will have to make significant, capacity-related investments along the south end.

The independent assessment of Amtrak will: (1) examine these infrastructure needs to support increased use of the Corridor; (2) compare infrastructure investments in the Northeast Corridor with investments in the rest of Amtrak's system; and (3) determine the specific relevance of these infrastructure investments, taking into consideration traffic, safety needs, infrastructure condition, and other factors that potentially could impact investment decisions.

## **CONCLUSION**

Mr. Chairman, we believe the findings of the independent assessment will play a *major role* in evaluating Amtrak's long-term financial situation. It will then be up to Congress, Amtrak's Board of Directors, and the Amtrak Reform Council to consider whether Amtrak's plans are adequate and sufficient to increase revenue and ridership, reduce costs, and invest in the capital projects needed to reach operational self-sufficiency by FY 2002. We thank you again for inviting us to discuss the Office of Inspector General's work in carrying out the Congressional directive for an independent assessment of Amtrak's future.