

III. PRINCIPLES AND KEY CHANGES UNDERLYING THE COUNCIL'S RECOMMENDATIONS

A. PRINCIPLES

In developing its restructuring plan for Amtrak, the Council has been guided by a number of principles the Council believes important to improving the rail passenger service program.

- There should be transparency and accountability in management structures, accounting systems, and financial reporting for both train operations and infrastructure.
- There should not be any unfunded mandates to provide train services nor any cross-subsidization of rail passenger service by offsetting losses from one region or class of services or with profits from others. Train operating companies, including Amtrak, should have incentives to maximize profits from specific corridor services and to reinvest operating profits into such services to improve operations and profitability.
- Rail passenger service decisions should be made on a regional basis to the maximum extent possible, particularly if regional entities and states provide operating and capital funding grants for the rail passenger service.
- State and local governments should have more flexibility in how they use federal transportation funds.
- All users of the Northeast Corridor should bear fair and reasonable portions of the operating and capital costs of maintaining and improving the Northeast Corridor.
- Train operators should be shielded from political influences so that they are free to make operational and marketing decisions as commercial companies based on customer demand.
- Any federal subsidy to intercity passenger rail service should be offered on a performance basis. Such performance-based formulas could include a percentage of revenue performance measure or a farebox recovery ratio.
- Congress should take steps to improve intermodal connectivity between rail and other modes of passenger transportation, including direct connections at airports, possibly with incentives for airport operators to encourage travelers to take trains for shorter trips.
- Inasmuch as transportation policy generally accepts the policy that the Federal government assumes responsibility for funding infrastructure while the private sector assumes responsibility for operations, Amtrak is an anomaly. The Council recommends that Congress recognize the Federal responsibility for rail infrastructure through the creation of a Rail Infrastructure Trust Fund, (which should not be funded by the current 4.3 percent deficit reduction tax on rail diesel fuel).

- For any franchising to be successful, there must be a level playing field for potential competitors to Amtrak. Franchisees must be able to access the rights-of-way of the freight railroads on an incremental cost basis and with operating priority, must be afforded the same statutory limitation on liability as Amtrak, and must be able to purchase insurance on the same terms as Amtrak.
- If franchising is invoked, franchises should provide exclusive – not open access – to franchise operators to provide rail passenger service where the franchisee will operate over privately-owned rights-of-way. Franchises should be designed to avoid cherrypicking of Amtrak routes.
- The national network should reflect current and prospective travel demand (with an emphasis on current travel patterns). A process should be put in place to evaluate routes based on objective criteria so that service can be added where justified and terminated where warranted.

B. BASIC DESIGN—A NEW BUSINESS MODEL

To solve Amtrak’s basic problems, a new set of models is needed for organizing, funding, and implementing train operations, infrastructure management, and government program administration, policy development, and oversight.

1. The Role of Government – Administering the Program

Extensive program administration, oversight, and policy development authority resides under current law in the existing Amtrak organization. The Council recommends that the Congress vest this authority in a restructured National Railroad Passenger Corporation, which would be a small government program administration agency directed by a board representing all regions of the US. The NRPC would perform much as did the United States Railway Association (USRA), which Congress established in 1973 to carry out the successful planning and oversight of Conrail. USRA reviewed Conrail’s business plans and monitored their execution, disbursed federal funds, and could withhold funds if Conrail did not take actions to improve its performance. USRA also shielded Conrail from political interference, and worked closely with Conrail’s management, contributing its success. The Council believes that government administration and oversight cannot be exercised effectively under the current statutory structure and that the national passenger rail program would benefit from an effective oversight organization.

2. Train Operations – Accountable and Efficient

The vision for train operations is a customer-focused commercial enterprise shielded from political interference, and directed by a board with extensive transportation operating experience. The organization would have the ability to modify routes, schedules, and prices to improve financial performance, a culture that puts the customer first, the tools to effectively manage the business, and appropriate compensation incentives. The operating company would also be held to new performance standards set by a government oversight entity for measures such as operating income, operating ratio, ridership, and on-time performance. The operating entity would not be expected to operate unprofitable service unless compensated for losses under a service contract with the federal government or the affected states.

The Council believes that the most effective means for ensuring that the operating company operates as an efficient commercial enterprise would be to place the operating company in a competitive commercial environment. Thus, after an appropriate transition period, the new government oversight entity would have the option of contracting out specific operating company services to private, regional, or state operating entities, pursuant to competitively bid franchise arrangements (in which the operating company would be a participant). To make a clear break with the current de facto operating monopoly held by the existing Amtrak organization and to fine-tune the effectiveness of the franchise approach, pilot projects could be immediately introduced for selected services or operations. Appropriate labor protective conditions (ultimately to be determined by Congress) would protect the rights of current Amtrak employees for any franchised operations.

3. Infrastructure Management – Accountability to Regional and Local Needs in the Context of a Federal-State Partnership

The model for infrastructure management is a U.S. government-owned corporation responsible for ownership and maintenance of the Northeast Corridor and (initially) other Amtrak-owned infrastructure. It would be authorized to buy or sell assets and, to the extent possible, transfer all non-NEC Amtrak properties to state and local governments. Funding would come (inter alia) from federal and state capital subsidies, trackage fees on intercity, commuter, and freight carriers for use of the Northeast Corridor, and real estate development revenues from such things as utility and communications easements. In addition to current sources of funding for the NEC infrastructure, which have proven inadequate under the current Amtrak program structure, funding from a variety of sources will be needed to return the NEC to a state of good repair and to fund improvements. The reauthorization of Amtrak this year, current proposals to provide infrastructure funding for corridor development, and reauthorization of TEA-21 and AIR-21 in 2003, may well provide appropriate opportunities for increasing rail development funding. To ensure accountability to regional and local needs, the infrastructure corporation would be controlled by a board of directors consisting of current users of the NEC. The board would also coordinate operations on the NEC by the various users to ensure equitable access arrangements. To provide incentives for efficient infrastructure management, the new government oversight entity would, after an appropriate transition period, have the option to contract out management of the NEC infrastructure or to transfer ownership and management to the NEC states. Appropriate labor protective conditions would protect the rights of current Amtrak employees for any franchised operations.

C. KEY CHANGES TO IMPROVE THE INTERCITY RAIL PROGRAM

The Amtrak Reform Council's recommendations for restructuring Amtrak suggest four major changes to the intercity passenger rail program. The suggested changes address root causes of Amtrak's failure: an unworkable institutional structure, the lack of a government commitment to intercity passenger rail service – both in terms of policy program management and funding – and the absence of competition for the provision of services. Options for reform were judged according to the option's potential for getting more value out of the federal and state investments in intercity rail service; managing an effective program instead of a train operating company; and providing a foundation for the development of high-speed rail corridors.

1. Separation of All of Amtrak's Passenger Train Operations from the Northeast Corridor Infrastructure (NEC)

The Amtrak Reform Council recommends that Amtrak's responsibilities for owning and maintaining the NEC and other track and related infrastructure should be separated from its responsibilities for train operations. The Council reached this conclusion based on the following:

- *Amtrak's responsibilities for maintaining the Northeast Corridor make it more difficult for Amtrak to achieve and sustain operating self-sufficiency.* Operating expenses (even without considering capital costs) associated with maintaining the corridor add significantly to Amtrak's operating deficit. And since trackage use fees paid by the commuter authorities are based on incremental rather than full costs, Amtrak must fund a disproportionate share of NEC maintenance costs.
- *Amtrak should focus on its core mission as a service provider.* Amtrak's primary mission is to provide intercity passenger and mail and express service. Amtrak should focus exclusively on this mission and be freed from the financial and managerial distractions associated with track ownership and maintenance.
- *Separating the NEC infrastructure from Amtrak's operations will provide a true picture of the costs of the infrastructure and how funds are being used to maintain it.* There is currently no separate accounting for the NEC infrastructure. Capital and operating subsidies appropriated to Amtrak and are used to meet Amtrak's immediate needs. Critical maintenance needs are being ignored. For example, the Office of Inspector General of the U.S. Department of Transportation found that while Amtrak needs to spend at least \$135 million annually on minimum operational reliability investments, in fiscal years 1998, 1999 and 2000, Amtrak on average invested only \$71 million.
- In November 1999 the Amtrak Reform Council recommended to Amtrak's Board of Directors that Amtrak keep separate financial records for the NEC infrastructure. While Amtrak agreed to do so, Amtrak has never produced this information.
- *The Northeast Corridor will require significant capital in the coming years; Amtrak is looking to 'non-federal' sources to provide a significant amount of the needed funding.* Amtrak's long-term capital plan for FY2001-FY2020 identifies the capital needs on the Northeast Corridor as \$27.9 billion, of which \$10 billion is needed to meet current service needs and \$17.9 billion is needed for growth. Amtrak's plan assumes that \$4 billion of the \$10 billion needed to meet current service needs will come from non-federal sources and that non-federal sources will contribute \$15.7 billion of the \$17.9 billion needed for growth.
- *The Northeast Corridor is a regional asset and Amtrak is not the dominant user.* The NEC is a critical transportation asset for the northeastern states. The Corridor contributes to the economic health and growth of the region; its true value greatly exceeds the value to Amtrak alone. While Amtrak owns the majority of the right-of-way, it is the minority user of the

Corridor. A 1996 study by the U.S. General Accounting Office²⁹ found that in 1993, Amtrak operated only 100 of the 1,200 daily trains on the Corridor. Most of the other trains are operated by commuter agencies. Of the 100 million passengers estimated to use the Northeast Corridor in 1993, about 89 million were commuter rail passengers and 11 million were Amtrak passengers.

- *A separate infrastructure company might have a greater opportunity than Amtrak to attract private capital.* Many believe that private capital would influence how the organization functions financially and would help ensure that funds intended for rail capital programs are used for that purpose. With an objective of protecting their investment, providers of private capital can influence the organization to take steps necessary to cut expenses (especially overhead) and achieve revenue growth to maximize the return on investment. In other words, private capital could help make a government-owned entity behave more like a business.

The Council is not proposing – in recommending that the NEC infrastructure be separated from Amtrak's train operations – to do what was done in Britain with the formation of Railtrack. In Britain, the track network in all of Great Britain was privatized immediately. Railtrack's directors do not have any relationship to the train operating companies that operate the 26 passenger franchises or to the companies operating the two freight franchises. The Council's proposal does not involve privatization; the Corridor would remain under government ownership. Unlike Railtrack, the Council proposes that the board of the NEC infrastructure organization would principally represent the users, not some random group of private shareholders. And the board would be required to produce an annual five-year business plan for the NEC infrastructure detailing the required maintenance and improvements and the associated funding requirements. In its 25 years of owning the Corridor, Amtrak has never produced such a plan. In short, the situation in the Northeast Corridor is not anything like the situation in Britain, and the Council is not doing proposing – unless the proposal is viewed in the most superficial terms – anything resembling what was done in Britain.

2. Establishing an Effective Federal Program Administration and Oversight Function

Amtrak is unlike other federally funded transportation programs in that public policy and program administration is performed essentially by Amtrak itself rather than by a government body. Amtrak decides what routes will be operated, how corridor development will proceed, and determines the funding priorities for passenger service throughout the nation. Amtrak even provides federal planning money to the states to support these planning efforts. These are all public policy roles that more properly belong with federal and state governments. Neither the Federal Railroad Administration nor any other executive branch agency has a direct role in overseeing or approving Amtrak's operations and expenditures. Amtrak may dispense federal funds as it sees fit and may retain or initiate money-losing services without objective criteria and based solely on political considerations. Government oversight is largely restricted to safety matters under the jurisdiction of the Federal Railroad Administration and audits of Amtrak's performance by the U.S. General Accounting Office, the Inspector General's office in the Department of Transportation and by the

²⁹ U.S. General Accounting Office, Northeast Rail Corridor: Information on Users, Funding Sources, and Expenditures, June, 1996.

Amtrak Reform Council. Analysis and reporting functions are not a substitute for hands-on guidance and oversight.

Amtrak's performance under the ARAA demonstrates an emphatic need for more pro-active involvement. Amtrak has consistently issued its Strategic Business Plans well after the start of the fiscal year. When it became clear that the introduction of Acela would be delayed, Amtrak took no steps to develop a contingency plan to stay on track. Amtrak has projected significant overall cost reductions in its strategic business plans since 1999. Amtrak, however, did not define specific cost reduction initiatives until FY2001, and those proposals total only \$75 million annually, clearly inadequate to meet Amtrak's strategic business plan projections. Had a federal oversight group had the authority to require Amtrak to submit realistic business plans and follow through on them as a prerequisite to receiving federal appropriations, we believe Amtrak would not be in its current financial crisis. Business plan shortcomings would have become apparent sooner and corrective actions taken to move Amtrak towards operational self-sufficiency.

The Council believes the federal government's role should be to:

- Administer federal funds made available for intercity passenger service;
- Facilitate the development of high-speed rail corridors, including evaluating project proposals and prioritizing projects for design and construction;
- Assisting states and regional compacts of states and other transportation entities to develop, evaluate and prioritize high-speed rail passenger projects.
- Actively oversee the business plans of the operating and infrastructure companies (in a manner similar to that of the United States Railway Association (USRA) during the early years of Conrail's operations). The group should have the authority to withhold funds if the operating and infrastructure companies do not act in good faith to prepare and execute their business plans;
- Determine whether to franchise any or all Amtrak services, design franchises to be offered, administer the competitive bidding process and administer contracts with franchisees;
- Coordinate a national system of ticketing and reservations to permit seamless transfers between intercity franchises and between intercity travel and other modes of transportation; and
- In cooperation with Congress, the states, the freight railroads, the public, and other interested parties, manage public policy issues with respect to intercity passenger rail service.

3. Allowing the Introduction of Competition

One of the overriding trends in rail reform internationally has been the introduction of competition into the provision of rail passenger services through some form of franchising. While there are

many variations on the process, it generally involves competitively bidding a route or group of routes for operation under contract with a government authority for a specified period (often five to ten years). Many people have the mistaken impression that franchising can only be applied to routes or systems of routes that are profitable. This is not the case. The competition provided by franchising helps maximize returns on profitable routes (positive bids) and minimize losses on unprofitable ones (negative bids).

Competition would force Amtrak to operate more efficiently to successfully bid for franchises. Competitive forces would drive down the cost of operations, off-setting potentially higher subsidies to adequately compensate service providers for operating unprofitable routes. Amtrak or other service providers would essentially be treated like other government contractors.

Under the Council's recommendations, franchising could also apply to the Northeast Corridor infrastructure. The NRPC would have the authority to contract out maintenance of the corridor through a competitive bidding process. As for train operations, the competitive pressures of franchising could improve productivity and make federal and state dollars go further.

Franchising does not imply open access. The Council's proposal recommends that if franchising is implemented, franchisees have exclusive rights to operate services or routes. Because most rail passenger markets do not appear to be large enough to support multiple operators, exclusive franchises are most sensible. The Council envisions only a limited number of franchises and proposes that the freight railroads have input into the design of franchises and operating requirements, including ensuring that adequate capacity exists or will be provided, so that the operational effectiveness of freight service will not be adversely affected by additional rail passenger service. The Council recommends further that the NRPC design franchises in a manner that prevents bidders from cherry-picking Amtrak's network and leaving Amtrak to operate the least attractive routes.³⁰

There are several issues vital to successful franchising. The first is the ability of the franchisee to be able to access the rights-of-way of the freight railroads on the same basis as Amtrak, i.e. at incremental cost and with operating priority. Without this, service providers other than Amtrak would have to negotiate access and track use fees with the freight railroads and would be at a competitive disadvantage relative to Amtrak. It is also imperative that other service providers be able to obtain insurance and be afforded the same limitations on liability that apply to Amtrak.

The members of the Council have taken a strong position in favor of protecting the rights of rail labor. The Council recommends that all franchisees be subject to the Railway Labor Act, Federal Employer's Liability Act (FELA) and railroad retirement. Moreover, all agreement employees should have hiring preferences with new franchisees and should be transferred to franchisees with their seniority and existing contracts in place. Collective bargaining agreements would be renegotiated under the provisions of the Railway Labor Act.

³⁰ Current law also provides a forum before the Department of Transportation if a dispute develops between Amtrak and a freight railroad over an introduction of additional trains or accelerated speed that could unreasonably impair freight operations. (49 U.S.C. 21308.) Such provisions would remain in place under the Council's proposal.

4. A Secure Source of Funding

There is presently no secure source of either capital or operating funding for passenger rail service. The Council believes Congress should provide a stable and adequate source of capital funding for the Northeast Corridor, the emerging high-speed corridors and other rail-related infrastructure. The Council also believes, with respect to operating subsidies, that there should be no unfunded mandates. If Congress wishes Amtrak to continue to operate routes that lose millions of dollars annually, it should adequately fund these operations under a specific contract between the NRPC and Amtrak, and that Congress should further consider allowing franchising as a way of minimizing operating losses.