U.S. Senate Committee on Appropriations
PRESS RELEASE

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For immediate release: Tuesday, February 27, 2007
Contact: Tom Gavin, 202-224-3904

U.S. Senate Appropriations Transportation and Housing and Urban Development Subcommittee Testimony of Robert Serlin, RIM Services, LLC

WASHINGTON, D.Cé . The U.S. Senate Appropriations Transportation and Housing and Urban Development Subcommittee on Wednesday held a hearing to examine the proposed Fiscal 2008 budget for Amtrak. The subcommittee heard from Mr. Robert Serlin, President of RIM Services, LLC. Mr. Serlinõs prepared testimony is below.

My name is Robert Serlin. I have, for over 20 years, developed business solutions to revitalize capital-intensive transportation and basic commodity companies. I am President of RIM Services, LLC.

Thank you for inviting me to comment on Amtrakõs financial condition, efforts Amtrak has made to improve its financial condition, and Amtrak funding options. I will limit my comments toð

Å exploring a new Amtrak funding option that can revitalize Amtrakõs owned rail properties in the Northeast and Midwest;
Å eliminating much of Amtrakõs private-sector debt; and
Å giving this Subcommittee a means to reallocate limited transportation budget dollars to other priorities, including enhanced rail passenger service.

In 1997, JP Morganð currently the third largest bank in the United Statesð invited me to assemble a group of experienced rail industry professionals and companies to develop a plan to address Amtrakõs recurrent funding problem. Ultimately, using techniques from existing legislation and Federal programs, a method to inject significant non-appropriated funds into Amtrak and its owned infrastructure was identified. The solution was embodied in the Infrastructure Management Organization (ñIMOò) Plan.

The IMO Plan, developed as a direct result of numerous meetings with stakeholders interested in better intercity rail serviceð

Å preserves Amtrak as our countryõs single national passenger rail carrier;
Å keeps all of Amtrakõs assets under Federal ownership and oversight;
Å frees monies to this Subcommittee to appropriate as the Federal share under Lautenberg-Lott; and, most importantly,
Å provides a platform to grow train services and rail industry employment.

BACKGROUND

Amtrak is active in two different businesses: furnishing rail transportation services, and owning and operating rail infrastructure.

Å The rail transportation services business is a variable cost business. New train services can be added and existing train services dropped or modified on short notice with few drastic or unforeseeable financial consequences.

Å The rail infrastructure business, in contrast, is a fixed cost business. Infrastructure projects take years, sometimes decades, to implement. During the implementation period, there is very little to show other than large front-loaded outlays. Furthermore, once completed, those formerly new infrastructures must be repaired, maintained and upgradedð invisible tasks, for which the public has little appreciation, and consequently, for which it has proven not possible to appropriate funds.

Amtrakøs owned rail infrastructure is the overwhelming problem. Though it has been recognized for decades as the part of Amtrak that singularly requires the most funds, this is a truth no one dares to speak. Amtrak cannot live without using its owned infrastructure, but it also cannot afford to keep it.

While Amtrak operates passenger trains over roughly 23,000 route-miles, it owns and is responsible for only about 2% or 600 route-miles (about 500 route-miles in the Northeast and about 100 route-miles primarily in Michigan).

Former Amtrak President David Gunn stated in a Railway Age article that it is a myth that Amtrakøs long-distance trains are the primary source of Amtrakøs losses. ñOut of our current year federal subsidy of $1.05 billion, only $300 million will go to covering the operating loss of long-distance trains.ò Kenneth Mead, former Inspector General, U.S. Department of Transportation, found that eliminating long distance trains would only reduce operating losses by $300 million. In 2003, Amtrak lost approximately $1.3 billion. Consequently, losses of about $1 billion must be attributable primarily to Amtrakøs owned infrastructure.

A previous Amtrak President, W. Graham Claytor, Jr., once said Amtrak would be unfundable were the country to recognize that the great majority of Amtrakøs annual appropriations went into Amtrak-owned rail infrastructure in just a few Northeastern states. On a route-mile basis, two states alone account for over 50% of Amtrakøs owned Northeast Corridor infrastructure.

Even without political considerations, it is inherently harder to secure public support for infrastructure projects than for transportation services. Infrastructure investment benefits are not immediately, publicly apparent and can easily be delayed with few immediately visible consequences. Yet, infrastructures must be funded. Without continuous funding, infrastructure will deteriorate to the point of being unusable.

Since 1997, the Department of Transportationøs Inspector General, the Government Accountability Office and, most recently, numerous members of Congress have reached the conclusion: the status quo is not sustainable and change is necessary.

Ken Mead, the former Department of Transportation Inspector General put it most succinctly on September 21, 2005 when, before the House Committee on Transportation and Infrastructure, Railroads Subcommittee he stated: ñWe have testified numerous times since Amtrakøs authorization expired in 2002 that the current model is broken. Amtrak continues to incur unsustainably large operating losses, provide poor on-time performance, and bear increasing levels of deferred infrastructure and fleet investment on its system.ò Infrastructure degradation reduces service reliability, and jeopardizes all of Amtrak and its national rail system.

The IMO Plan offers a solution both to Amtrakôs short-term funding requirements and the two-pronged challenge of Amtrakôs infrastructure needsð injecting new current maintenance funds annually into Amtrakôs owned Midwest and Northeast infrastructures, and addressing Amtrakôs looming $9 billion deferred maintenance liability.

Under the IMO Plan, the IMOð

Å makes a one-time payment of about $2.0 billion to Amtrak;

Å assumes from Amtrak almost $750 million in infrastructure-secured debt;

Å funds the backpay for Amtrak employees (estimated by Amtrak to be about $200 million); and

Å invests not less than $600 million annually in Amtrakôs owned Midwest and Northeast infrastructures.

THE IMO PLAN

The IMO Plan separates Amtrak into two Federally owned entities.

The first Federal entity, Amtrak, continues its primary responsibility as a transportation service provider. It retains the reservations system, locomotives, passenger cars, maintenance of equipment workshops, and operating rights on the nationôs rail network. It continues to operate all of its current intercity, Northeast Corridor and contract commuter trains.

By separating Amtrakôs train operating functions from its owned infrastructure, William Crosbie, Amtrakôs Senior Vice President of Operations estimated that the current forty-six state network can be sustained on an annual appropriation of under $500 million ð significantly less than the $1.5 billion that Amtrak is requesting for FYô08.

The second Federal entity owns the 600 route-miles of Amtrak infrastructure, passenger stations on that infrastructure, and overhead wires that power the trains. The Surface Transportation Board (STB), in a process similar to its existing ñdirected serviceò authority, would conduct a public solicitation and select a private sector IMO from among the qualified applicants.

The IMO, for a period of fifty years, is responsible for managing and funding all rail infrastructure operations and improvements. This time period is necessary due to the very high level of front-end loaded investmentsð it is projected that the IMO will require about fifteen years to generate enough revenue to break even. Each improvement becomes the property of the Federal government as it is made. At the end of the fifty years, the Federal government can either re-bid the management concession or operate the infrastructure itself. At any time during the concession, the designation of the IMO is revocable for cause.

FUNDING STRUCTURE

The IMO is financed using the existing Railroad Rehabilitation Infrastructure Financing (ñRRIFò) loan program. Under the Safe, Accountable, Flexible, and Efficient Transportation Equity Act of 2005 (SAFETEA-LU), RRIF program authorization was increased to $35 billion.

The IMO would be allowed to borrow up to $17.5 billion under the RRIF program, after having given the United States Treasury a repayment guarantee issued by an investment-grade third party in the amount of the full $17.5 billion.

As interest on the loan, the IMO is required to invest a minimum average of $600 million annually in the Federal Governmentõs owned infrastructure. This ñpayment-in-kind" has been successfully used in other Federal government initiatives in defense and power generation. On average, this statutory minimum investment exceeds by more than 200% the amount Amtrak currently spends annually on its owned infrastructure . If my companyð RIMð is designated the IMO by the STB, we foresee laying out in excess of $1 billion annually.

The IMO Plan does more than just shift the financial burden of Amtrakõs owned infrastructure from Congress to the private sector; it provides natural incentives to increase capacity, services, reliability and safety. It is the IMOõs responding to these incentives that translate into an increase in the number of passengers carried by all transportation service providers and, in turn, into new revenues for the IMO. Revenue increases come from new train services that pay track-mileage fees to the IMO and from which the IMO pays for infrastructure improvements.

STAKEHOLDER BENEFITS

The IMO Plan creates a platform upon which new and exciting rail services can be launched by Amtrak, existing commuter operators, or new transportation service providers, while the IMO, which is prohibited from operating trains, focuses on infrastructure management and improvements. The result will be more service options with greater access to both the Northeastern and Midwestern rail networks, allowing more passengers to enjoy the efficiencies and benefits of rail travel.

The Plan forces the IMO to innovate by developing new opportunities for transportation service providers. To meet these goals, the IMO must be a truly neutral party. This is achieved by not permitting the IMO to operate its own trains. The IMO may not compete with its customersð the users of the infrastructure it manages. The only way the IMO should succeed is if its customers succeed.

This vision of rail passenger service can be reached. The IMO Plan is the route:

Å High-speed train trip-times between New York and Washington will be reduced from close to three hours to roughly two hours through capital expenditures that eliminate choke points and provide infrastructure redundancy.

Å Commuter carriers will be able to integrate their services by operating new run-through trains, as the IMO adds infrastructure capacity, instead of being confined to historic geographic areas. For example, New Jersey Transit and SEPTA will each be able to save millions of dollars and be able to offer faster and more attractive travel options by instituting a pooled New Yorkð Philadelphia service, instead of forcing all passengers to change trains at Trenton, NJ.

Å New city pair combinations will be encouraged to permit rail passenger traffic to expand meaningfully. For example, Princeton Junction, NJ has sufficient population and business activity to support multiple direct trains daily to Baltimore and Washington. New riders will be attracted by convenient and faster direct trains offering expanded travel options.

Å Building fourteen new stations in the first twenty years at rail / highway intersections will attract more travelers though more convenient access.
Å Dedicated airport express train services will help speed travelers to airline check-in while reducing airport overcrowding.
Å Redundancy of infrastructure will provide more security and reliability.
Å More employment will be created to build and maintain the enhanced infrastructure.
Å Further employment will be created to staff and operate added train services.
Å Carbon emissions will be reduced by seamlessly shifting travelers from automobiles to electrically powered trains.

STAKEHOLDER PROTECTIONS

Addressing the needs of principal stakeholders is a key element of the IMO Planõs win-win solution.

Federal Government

The RRIF loan principal is never at risk because it is fully secured by an investment-grade third party guarantee in the full amount of the RRIF loan.

The Inspector General of the Department of Transportation is vested with the authority to certify compliance with the terms of the legislation. The IMO is also required to file with the Secretary of Transportation and Congress annual reports both of its audited financial results and its operations, thus ensuring accountability to the public and to Congress.

To align the long-term interests of the owners of the IMO to those of the Federal government, ownership of the IMO is non-transferable for the full fifty-year management concession term.

Under the IMO Plan, Congress continues to maintain oversight over both Amtrak and Amtrakõs owned infrastructure, yet is relieved of the burden of funding Amtrakõs owned infrastructure since the IMO, using non-appropriate funds, is now responsible. It frees Congress to focus more on transportation services that constituents demand, and that states and other governmental entities desire.

States

The states will gain a stronger voice and role in infrastructure investment through the reconstituted Northeast Corridor Coordination Board and the Northeast Corridor Safety Committee.

Multi-state compacts are not required and states are not obligated to fund the maintenance of or capital expenditures in the governmentõs owned infrastructure. Under the IMO Plan, state-requested projects may be expedited either by the IMO advancing funds to a state or the Department of Transportation providing funds to a state under a grant program.

Amtrak

The IMO Plan improves Amtrakõs financial statements byð
Å transferring $2 billion to Amtrak;

Å assuming from Amtrak up to $750 million in infrastructure-secured debt; and
Å relieving Amtrak of its responsible for the roughly $1 billion in annual losses attributable to Amtrakõs owned infrastructure, most of which are incurred in just five Northeastern states.

Commuter Carriers and Freight Railroads

Vested commuter carriers and freight railroads with operating rights must also be protected. All pre-existing contracts and agreements are transferred to and honored by the IMO, including the commuter carriersõ ñavoidable cost" access fee structure codified in Title 49, United States Code .

This furnishes Amtrak the means and allows it the time to address the needs of its entire forty-six state system, including the need to acquire new passenger cars and locomotives.

Labor

The existing Amtrak employees are a great and irreplaceable resource. Labor must be treated fairly and equitably in order to assure the success of the IMO. Wages must be increased to be competitive in the region.

Under the IMO Plan, the IMO is required to offer employment in seniority order to all Amtrak employees performing infrastructure work to be performed by the IMO. The IMO is also required to honor existing collective bargaining agreements. If RIM is awarded the right to be the IMO, it intends to negotiate Northeast-competitive rates of pay and working conditions for those employees to whom it offers employment.

Many of Amtrak's employees have been working for over seven years without contract base rate increases. As a result, there is pressure on many of these highly qualified workers to join commuter carriers or retire early. This potential loss of experience would be highly detrimental to the development of improved passenger services.

To assure the future integrity of both Amtrak and its owned infrastructure, I personally believe that a fair wage settlement, including full backpay for the IMO's employees must be implemented quickly. To encourage Amtrak employees to accept employment with RIM, RIM will also offer signing bonuses. This translates into payments (signing bonuses and backpay) in amounts ranging from $10,000 to $25,000 per employee. In addition, RIM is prepared to contribute sufficient monies to a trust fund to settle Amtrakõs full backpay obligation to those employees remaining with Amtrak.

If RIM is awarded the right to be the IMO, with regard to the IMOõs employees, it intends toð
Å resolve outstanding proposed contract changes by offering rate increases to make wages competitive with the commuter carriers in the area and by paying full back wages from January 1, 2000;
Å withdraw Amtrak's proposed concessionary contract changes, including Amtrak's proposal that employees pay a portion of their health and welfare premiums; and
Å negotiate for working conditions that provide quality of life improvements without adversely effecting productivity.

In a more general vein, the IMO Planð

Å furnishes incentives to resolve the outstanding Section 6 contract notices;
Å preserves collective bargaining agreements and rights, including labor representation for IMO employees;
Å makes the IMO subject to the Railway Labor Act, the Railroad Retirement and Unemployment Insurance Acts, FELA, and all rail safety legislation and FRA regulations; and
Å protects employees affected by the transfer.

The Traveling Public
For the traveling public, reliability and security redundancy will increase, while trip-times will be reduced by the IMOøs addressing deferred maintenance through aggressive engineering and construction, and major new capital investments. Train riders will also enjoy more frequent service, increased travel options, new city pairs, andð very likelyð lower prices.

The traveling public is looking for transportation options. RIM believes that rail can offer such options, but it requires a new vision. In 1974, at the high of the first energy crisis, Amtrak reported carrying approximately 10.9 million Northeast Corridor riders, compared to approximately 11 million riders in 2005. Despite the fact that the number of I-95 automobile trip more than doubled over the same period of time , Amtrakøs ridership remained flat. The following graph shows this long-term divergence.

RIM believes that Amtrak, unburdened by infrastructure ownership, can fulfill the new vision.

THE STATUS QUO HAS FAILEDð AMTRAKøS HIDDEN LIABILITY

Amtrakøs owned infrastructure, particularly its Northeast Corridor, suffers from many years of deferred maintenance and depreciated assets. Major infrastructure components, renewed in the early 1980øs, are now approaching the end of their useful and reliable lives, and will soon have to be replaced.

According to Kenneth Mead, former Inspector General, U.S. Department of Transportation, ñAmtrak [had in 2002] an estimated $5 billion backlog of state-of-good-repair investments, and underinvestment is becoming increasingly visible in its effects on service quality and reliability.ò Due to the continued inability of Amtrak to maintain its infrastructure and construction project inflation over the last five years, RIM estimates this liability today to be around $9 billion.

If Amtrakøs deferred maintenance is not addressed in a timely manner, the integrity of the Federal Governmentøs owned infrastructure will be in jeopardy. Trip-times will be increased. Service will be degraded. Safety could be compromised.

The General Accounting Office (now Government Accountability Office) defines ñstate-of-good-repairò to be a condition requiring only cyclical maintenance. The last time the Northeast Corridor was in a state of good repair, was in 1981 at the conclusion of the Northeast Corridor Improvement Project.

If all we do today is desire to bring the corridor up to a state-of-good-repair, we are aspiring to return it to its state in 1981. Is that our goal in 2007, to return the corridor to its condition in 1981?

RIM’s answer is: No! RIM believes that the Northeast Corridor should move into the 21st century and is prepared to make the investments to bring it there.

Through enactment of the IMO Plan, the repair, operations, and improvement of Amtrak’s owned infrastructure is fully funded using non-appropriated funds.

The following graph shows the positive effects of transferring the Federal Government’s infrastructure liability to the private sector and of reducingð by about two-thirdsð Amtrak’s required annual appropriations.

APPROPRIATION CHALLENGES

The Federal government is able to fund Amtrak’s annual operating budget. Amtrak’s transportation services-related commitments (whether capitalized or expensed) tend to be completed in less than one yearð a time period that corresponds to an appropriation cycle. Those outlays are expended throughout the forty-six states through which Amtrak operates.

The Federal government has been unsuccessful at funding all of Amtrak’s capital improvements and infrastructure investments. Infrastructure undertakings tend to be multi-year in nature and, to be implemented efficiently and cost-effectively, require multi-year funding commitments. They, by their very nature, do not conform to the appropriations process. This has resulted in the massive and increasing deferred maintenance liability shown above.

On January 16, 2007, Senators Lautenberg and Lott, joined by other members of this Subcommittee, introduced S. 294ð the Passenger Rail Investment and Improvement Act of 2007 (PRIIA).   The IMO Plan is highly complementary with PRIIA.

SOLUTION AT HAND

By increasing the RRIF loan authority in 2005, Congress expanded a loan program that enables the private sector to fund our nation’s rail infrastructure multi-year investments. The vehicle to achieve this is the IMO Planð a Plan that benefits labor, the Federal government, states, the commuter carriers, and Amtrak.

By passing the IMO Plan, Amtrak’s infrastructure improvements and debt repayment appropriation-requirements will be reduced by over $1 billion annually. And, that $1 billion will be available to this Subcommittee to allow federal funds to focus on providing enhanced passenger rail service to the United States.

The IMO Plan is a win-win opportunity for the nation’s rail passenger stakeholdersð labor, the States, rail passengers, transportation service providers, Amtrak.   It provides a solid base upon which to build the modern rail passenger network that government leaders and travel advocates have championed for the past thirty years.

Thank you for providing me the opportunity to testify, and I welcome questions you might have.