TESTIMONY OF DONALD M. ITZKOFF
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ON THE CURRENT STATE OF AMTRAK
BEFORE THE
SUBCOMMITTEE ON SURFACE TRANSPORTATION ANDMERCHANT MARINE
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION
UNITED STATES SENATE

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Chairman Hutchison and members of the Subcommittee, I am pleased to appear before you today to discuss Amtrak's progress in overcoming the extraordinary hurdles of recent years and to outline the challenges that remain. Administrator Jolene Molitoris is unable to be here this afternoon because of a previous commitment that could not be rescheduled but she looks forward to a future opportunity to discuss with you the Administration's reauthorization recommendations in detail.

Two years ago, in FRA's first appearance before this Subcommittee, we shared with you the Clinton Administration's vision for Amtrak. We expressed our view that intercity rail passenger service is a safe, energy efficient and environmentally sound means of transportation that can and should be an integral part of this Nation's transportation system. In 1995, we underscored the Administration's commitment to Amtrak's partnership with its stakeholders and customers to transform the Corporation into a cost-effective provider of high-quality intercity passenger service for the 21st century. I am here today to reaffirm that commitment.

Amtrak has progressed substantially since the last time we met here to discuss its future, but much remains to be done.

Significant Accomplishments

When then Transportation Secretary Peña joined Amtrak's Board in 1993, Amtrak faced difficult circumstances. The condition of Amtrak's capital assets, in particular its equipment, reflected the disinvestment that had occurred over the previous decade. The quality and performance of Amtrak service continued to decline even as its projected requirements for Federal operating subsidies escalated. Beyond these obvious signs of distress, we found a company with little entrepreneurial spirit -- a company with a flagging culture mirroring a dependence on Federal operating subsidies. Amtrak could not even identify the net bottom line impact of any particular train or service. We were faced with system wide averages and guesses when we needed hard data as a foundation for a strategy for improving Amtrak's financial performance. In 1994, the Department of Transportation and Amtrak's Board of Directors adopted as a goal the elimination of Amtrak's dependence on Federal operating subsidies, while improving service and preserving a National system. Our strategy was to restructure Amtrak into a bottom line-oriented corporation with a customer focus, to provide adequate capital investment to modernize equipment and facilities, and to provide sufficient operating assistance to carry Amtrak through the transition period, to the year 2002 when Federal operating subsidy would no longer be required.

Thus far, it would appear that the strategy is working. The new management team has restructured Amtrak into a customer oriented company with a focus on the bottom line.

As a first step, the Corporation has made significant progress in "unbundling" Amtrak's finances and now more clearly can assess the revenues and expenses associated with a particular service, how that service affects other services, and how common costs should be allocated. Such information is necessary both for the Board's consideration of strategic actions and as a tool for management. Product line managers now focus on specific aspects of individual trains to identify opportunities for increasing revenues and controlling expenses.

Tom Downs also recognized early the need for a management structure to target specific parts of Amtrak's business. He created three strategic business units (SBUs) covering different parts of the United States, and addressing different customer segments of Amtrak's business. These SBUs are the Northeast Corridor, headed by George Warrington; Amtrak Intercity, headed by Mark Cane; and Amtrak West, headed by Gil Mallery. Each of these executives, while maintaining Amtrak's long standing commitment to safety, now also tailors service and marketing strategies to their specific requirements, with evaluation based on bottom-line business performance.

<u>Customer Service</u>

Amtrak's SBU strategy has facilitated new ways of approaching passenger rail with innovative customer service initiatives and results. Highlights include:

- <u>Intermodal marketing partnerships</u>, notably the partnership between Amtrak and United Airlines designed to provide travel by air in one direction and rail in the other, as well as the new business relationship Amtrak has forged with Greyhound Bus Lines.

- Partnerships with manufacturers such as the successful demonstration of the Talgo Pendular 200 now operating between Seattle and Vancouver, BC, the demonstration of ABB's Flexliner IR4E, which is a diesel-fueled, lightweight train set for possible operation in the San Diegan corridor, and the recent Turboliner demonstration in New York State.
- Partnership with States for new services such as the Piedmont Service sponsored by North Carolina, between Raleigh and Charlotte, in which the state purchased its own equipment as well as its own maintenance facility to guarantee high-quality service; the Mount Baker International service sponsored by Washington State between Seattle and Vancouver, BC, and the Vermonter, sponsored by Vermont, between New York City and St. Albans, near the Canadian border, which has proved so successful that the State is planning to add a second train.
- The Great American Station Foundation designed to leverage private and public sector funds to rebuild and revive the Nation's railway stations.
- Special newsletters targeted at passengers on specific services such as the Northeast Corridor giving them the latest information on news and events.
- Pricing innovations including bargain fares on underutilized trains.

These and other customer service improvements have earned Amtrak the award for the Most Improved Transportation Company in Customer Service by Knowledge Exchange, an independent financial analysis and publishing firm. At the same time, this close relationship of the SBUs to Amtrak's State, local and private sector partners has brought additional funding to the Corporation. In FY 1996, operating support payments provided by the States were up 75 percent over FY 1995. Amtrak also attracted $50 million in additional capital investment, and States such as California and Washington acquired new equipment to support Amtrak service.

<u>Bottom Line Focus</u>

Amtrak's emphasis on the bottom line has already paid dividends. In December 1994, Amtrak's management projected a cumulative eight year (FY 1995 to FY 2002) shortfall of $5 billion. Through measures taken in FY 1995 and FY 1996 Amtrak reduced that projected deficit by two-thirds. Amtrak has increased its revenues over the last two years despite reducing the annual train-miles operated by 16 percent and employment by 8 percent. The number of passenger-miles traveled per dollar of Federal operating subsidy, a measure of cost effectiveness, increased by almost 25 percent in FY 1996 over the prior year and is projected to increase again in FY 1997. In addition, the cash operating deficit declined by 16 percent between FY 1995 and FY 1996 and is projected to decline again between FY 1996 and FY 1997.

These positive results demonstrate Amtrak's commitment to transforming its business approach. The magnitude of the challenges ahead will require sustained and continuing innovation.

Importance of Capital

Adequate capital is essential in an environment such as the railroad business, with its extensive plant and equipment. The Clinton Administration has demonstrated its commitment to the future of intercity rail passenger service through a pattern of long-term capital investment. In each year since FY 1993, the President has requested significant levels of funding for both Amtrak general capital and for the Northeast Corridor Improvement Project. Cumulatively, the Federal capital investment over the last four years has exceeded the total Federal capital investment in Amtrak over the preceding 10 years.

Capital investment has significantly enhanced Amtrak's financial performance and has even greater implications for the long-term future of intercity rail passenger service. When we last testified on Amtrak before this Subcommittee, we identified the so-called "heritage cars" as a major problem blocking a successful future for Amtrak. These heritage cars -- the equipment Amtrak inherited upon its creation in 1971 -- accounted for nearly one third of Amtrak's fleet as late as 1995. Cars 40 years old and older were not uncommon. The low capacity and high cost of maintenance of this equipment badly hurt Amtrak's bottom line. (By way of comparison, a modern Superliner sleeping car provides Amtrak with 50 percent more passengers per car and costs less to maintain than the heritage sleeping car it replaces.)

Recognizing these problems, and building on the Administration's commitment of adequate capital, Amtrak's Board moved aggressively to renew Amtrak's passenger fleet. During FY 1997, Amtrak will take the last delivery on its Superliner and Viewliner orders and, except for some specialty and mail cars, the "heritage" equipment will be gone from everyday service.

Amtrak's aging cadre of locomotives also proved expensive to maintain and prone to break down. Since our last hearing, Amtrak has made significant progress in renewing its locomotive fleet. Just last year, Amtrak ordered 148 new diesel locomotives that will provide reliable, modern power for its long distance trains and 15 new electric locomotives for the conventional service on the Northeast Corridor.

The order of the new high-speed trainsets for Northeast Corridor service represents the most exciting, and potentially the most profitable, development in the use of capital. Just less than one year ago, Vice President Gore announced this acquisition at Union Station, which heralds the future for high-speed rail in the United States. The 150 mph "American Flyer" equipment will have all the modern amenities of the French *TGV* or other foreign high-speed trains. They will also be the safest high-speed trains ever constructed, as a result of FRA's partnership with Amtrak in requiring the most rigorous passenger equipment standards for high-speed trains anywhere in the world. The new trains will enter revenue service in 1999 at about the same time as Amtrak completes the extension of electric operation from New Haven to Boston. Construction began last July on the electrification project, the major remaining infrastructure project needed before Amtrak can operate high-speed over the entire length of the Northeast Corridor. High-speed service between Washington and Boston will have a major positive impact on Amtrak's financial condition. Amtrak's Metroliner service on the Northeast Corridor already has shown an operating profit in FY 1996, and the new high speed service will develop an expected Northeast Corridor operating profit of $150 million per year by the year 2000. This new revenue will reduce Amtrak's reliance on operating subsidies and ultimately benefit other routes elsewhere on Amtrak's system.

Significantly, on all of these equipment orders Amtrak has attracted substantial non-Federal financing. Indeed, Amtrak has financed almost 75 percent of the purchase price of the high-speed equipment — a leveraging of Federal capital investment not often seen in public transportation circles and an accomplishment of Amtrak's management that deserves substantial recognition. The constructive use of non-Federal financing highlights the commitment of Amtrak's Board of Directors and management to pursue every reasonable means to improve the quality and economics of intercity rail passenger service. It has also demonstrated that the financial markets believe in the long-term future of Amtrak.

Amtrak's Current Financial Condition

While the investments we have made over the last four years will pay dividends well into the next century, Amtrak's current financial condition requires careful scrutiny. Although Tom Downs can best illuminate Amtrak's financial condition as seen through these numbers, I would like to offer some observations. In FY 1995, Amtrak had a budget shortfall of $12 million on total expenses of $2.3 billion. Currently, Amtrak faces a much larger budget gap. Both the Department and Amtrak have sought to implement the strategy of improving Amtrak's financial performance and reducing its Federal operating subsidy requirements. Over the past three years we have seen that our goal of zero operating subsidy is achievable.

FY 1996

In FY 1996, the President's budget requested $300 million for operating assistance -- a number which itself represented a reduction of almost 25 percent from the $392 million appropriated in FY 1995. We believed that this level of funding signified an aggressive, but achievable step in a downward subsidy glide path for the Corporation. Unfortunately, Congress appropriated only $185 million for operating assistance, $115 million less than the Administration requested and $107 million less than the total included in the Congressional budget resolution passed in May 1995. In addition, the unusual weather conditions that year accounted for an additional variance of more than $40 million over the Board-approved business plan.

Thus, in FY 1996, Amtrak faced over $150 million in unexpected adverse bottom line impacts beyond the aggressive target that the Administration had envisioned. Yet, Amtrak management and labor achieved the original target and almost half of the unexpected additional requirements. In most other environments, this would be considered a significant accomplishment. Instead, much critical attention has focused on the $82 million FY 1996 budget shortfall and its impact on FY 1997. It should be noted that if Congress had provided the level of funding for operations requested by the President in FY 1996, Amtrak would have finished the year with a budget surplus instead of an $82 million deficit and Amtrak would be much better positioned for FY 1997 and continued progress toward operating self-sufficiency.

FY 1997

With the $82 million shortfall from FY 1996 and additional reductions in Federal operating assistance, FY 1997 represents a further challenge. Amtrak management projected that absent supplementary measures to address expenses and revenues, the Corporation would experience a budget shortfall of $243 million for the fiscal year. After intensive discussions between the Board of Directors and management, the Board adopted a business plan for FY 1997 that would have eliminated all but $30 million of the projected shortfall. This business plan involved the discontinuance of certain routes and the restoration of daily service to others.

We recognize the impact on communities across America of the prospective loss of their intercity rail passenger service. Yet we must also acknowledge Amtrak's need to implement a business plan that would address the shortfall it faces in FY 1997. When Congress added $22.5 million to Amtrak's FY 1997 operating assistance and mandated that the routes continue in service until May, Amtrak became unable either to avoid the net losses from the routes to be discontinued or add the revenue gains from the new services anticipated. Even taking into account the additional $22.5 million appropriation to continue service, Amtrak estimates the adverse impact on Amtrak's FY 1997 budget from failing to implement the business plan in November as planned will be approximately $40 million. As a result, Amtrak now projects a FY 1997 year end shortfall of $70 million. Although significant, the $70 million budget shortfall represents an improvement of $12 million over FY 1996.

Over the last 4 months, Amtrak has worked with States, localities, and existing and potential business partners to identify measures that can make the routes targeted for discontinuance commercially viable so that they do not represent long term negative financial commitments, and instead contribute in a positive way to improving the economics of intercity rail passenger service. Presently, it is unclear whether these efforts will be successful. However, we believe that the process of Amtrak working with its partners to pursue service important to them is the best way to preserve passenger service in the long term.

Conclusion

Amtrak faces formidable hurdles. The Corporation has no cash reserves, and even with $222.5 million in Federal operating assistance this year it will run a budget shortfall of $70 million. A general economic downturn, an air fare war in the Northeast, a severe hurricane or a less than responsive appropriation could significantly worsen Amtrak's prospects in the absence of cash reserves.

The Corporation is moving in the right direction, though much more needs to be accomplished. Amtrak has made great strides under difficult circumstances in reducing its dependence on Federal operating subsidies. The Corporation has become more entrepreneurial and is aggressively seeking partnerships with States and private entities to promote and improve service and increase revenue. It has made great progress in modernizing its fleet and improving the quality of its service. At the same time, Amtrak's Board of Directors and management have shown they will make the hard decisions necessary to improve the economic viability of intercity rail passenger service. Operating assistance is now down to half of what it was two years ago.

These achievements give us confidence that the Administration's strategy of providing Amtrak sufficient time and resources to eliminate its operating deficit is working. The President's FY 1998 budget request for Amtrak supports our commitment to this approach. Our reauthorization legislation, which will be a separate title in the "National Economic Crossroads Transportation Efficiency Act" (NEXTEA), will be transmitted to the Congress in the next few days and we look forward to discussing it in detail when the Subcommittee further considers Amtrak's future. This proposed legislation:

- reinforces our commitment to a National system of high quality passenger service;
- restates our "glide path" strategy of gradual reduction of the operating subsidy to zero in year 2002;
- provides the capital resources that Amtrak will need to reach this goal; and
- creates an environment in which Amtrak management, its employees, its stakeholders at the State and local government level, and its business partners can work together for improved rail passenger service.

Administrator Molitoris and I look forward to working with this Committee and the Congress in the coming months on this important legislation.

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