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Report to the Chairman, Committee on Commerce, Science, and Transportation, U.S. Senate

July 1999

INTERCITY PASSENGER RAIL

Amtrak's Progress in Improving Its Financial Condition Has Been Mixed

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General Accounting Office
Washington, D.C. 20548

Resources, Community, and
Economic Development Division

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July 9, 1999

The Honorable John McCain
Chairman, Committee on Commerce,
Science, and Transportation
United States Senate

Dear Mr. Chairman:

Since its inception in 1971, the National Railroad Passenger Corporation (Amtrak) has accumulated massive financial losses, with recent losses averaging over $800 million per year. To help Amtrak sustain operations and make needed capital investments, the federal government has provided it with nearly $23 billion in financial assistance since 1971. In 1994, in response to a request from the administration, Amtrak established a goal of eliminating its need for federal operating subsidies by fiscal year 2002 (termed being "operationally self-sufficient"). To accomplish this goal, Amtrak developed a series of strategic business plans designed to increase revenues and control costs.

In 1998, we reported that Amtrak was in a precarious financial condition.[1] This report responds to your request to provide an updated assessment of Amtrak's current financial performance as well as its prospects for improved future financial performance. In particular, this report discusses (1) Amtrak's overall financial performance in fiscal year 1998; (2) the prospects for Amtrak to meet its financial goals for operating self-sufficiency outlined in its most recent strategic business plan; and (3) the extent to which current and anticipated federal funding and recently enacted legislative reforms aimed at helping Amtrak better control its costs are likely to help improve its financial condition.

Results in Brief

Amtrak's overall losses increased in fiscal year 1998 after several years of improvement. In fiscal year 1998, Amtrak's net loss (total expenses less total operating revenues) was $930 million, the largest loss in the last 10

[1]Intercity Passenger Rail: Prospects for Amtrak's Financial Viability (GAO/RCED-98-211R, June 5, 1998); Intercity Passenger Rail: Financial Performance of Amtrak's Routes (GAO/RCED-98-151, May 14, 1998); Intercity Passenger Rail: Outlook for Improving Amtrak's Financial Health (GAO/T-RCED-98-134, Mar. 24, 1998); and Intercity Passenger Rail: Issues Associated With a Possible Amtrak Liquidation (GAO/RCED-98-60, Mar. 2, 1998).

years.[2] By comparison, Amtrak's net loss in fiscal year 1997 was $762 million.

Amtrak has made some progress in reducing its reliance on federal operating support. However, between now and 2002, it needs to achieve about 5 times as much in financial improvements (or what it terms "net impact") as it has been able to achieve over the past 4 years to reach operational self-sufficiency. Amtrak's current strategic business plan, approved by its Board of Directors in October 1998, estimates that ongoing and planned initiatives will result in a cumulative net impact of $1.6 billion from fiscal year 1999 through fiscal year 2002, primarily through increases in revenues as a result of taking business plan actions. However, uncertainty surrounds Amtrak's ability to achieve this net impact and to reach operational self-sufficiency by fiscal year 2002. For example, the plan contains over $160 million in "placeholders" for productivity increases and other reforms to be defined at a later date. Furthermore, Amtrak's expectations to increase revenues through other initiatives, such as implementing new high-speed service between Boston and Washington, D.C., and increasing its express service (the delivery of higher-value, time-sensitive goods) are based on critical assumptions—about such things as passenger ridership and the ability to obtain access to specialized equipment—that have yet to be tested in the marketplace.

Current and anticipated annual federal funding and recently enacted reforms aimed at helping Amtrak better control its costs will likely have little short-term impact on improving its overall financial condition. First, Amtrak plans to use nearly $1 billion of the $1.6 billion it expects to receive in federal capital appropriations over the next 3 fiscal years for maintenance rather than capital improvements. While maintenance is important for preserving assets and Amtrak's fiscal year 1999 capital appropriation could be used for equipment maintenance, Amtrak's plans to continue to use capital appropriations in this way means it will forgo or delay capital investment projects that could increase future revenues and reduce future costs. However, Amtrak's Board of Directors has approved plans for $1.3 billion of capital improvements from the $2.2 billion made

[2]This net loss is adjusted to exclude federal financial assistance counted as revenues. The Amtrak Reform and Accountability Act of 1997 eliminated the requirement that Amtrak issue preferred stock to the Department of Transportation in the value of the federal appropriations received. As a result, beginning with its fiscal year-end 1998 audited financial statements, Amtrak recorded a significant amount of federal financial assistance as revenues instead of preferred shareholder equity. In addition, Amtrak received federal financial assistance in fiscal years 1998 and 1999 through the Taxpayer Relief Act and recorded a portion of these funds as revenues. In this report, we present net loss amounts, excluding the amount of federal financial assistance that Amtrak's audited financial statements include as revenues in 1998. This adjustment allow us to better compare Amtrak's net loss position with those of previous years.

available to it through the Taxpayer Relief Act of 1997. In addition, as we reported in 1998, while the Amtrak Reform and Accountability Act of 1997 provided Amtrak greater flexibility in its business operations, the reforms provide few financial benefits in the short term. We found this condition continues to exist largely because Amtrak and its unions have not completed negotiations over labor protection arrangements and reforms for contracting out work.

Background

The Rail Passenger Service Act of 1970 created Amtrak as the nation's intercity passenger railroad. Prior to Amtrak's creation, intercity passenger service was provided by a number of individual railroads, which had lost money, especially after World War II. The act, as amended, gave Amtrak a number of goals, including providing modern, efficient intercity passenger rail service; giving Americans an alternative to automobiles and airplanes to meet their transportation needs; and minimizing federal operating subsidies. As of June 1999, Amtrak provided intercity passenger service along 42 routes that include most states.

Like all major national intercity rail services in the world, Amtrak receives substantial government support. From 1971 through June 1999, the federal government provided Amtrak with nearly $23 billion in financial assistance. However, in December 1994, at the direction of the administration, Amtrak established the goal of eliminating its need for federal operating subsidies, that is, achieving operational self-sufficiency, by fiscal year 2002. In addition, the Amtrak Reform and Accountability Act of 1997 authorized appropriations for Amtrak's operating and capital expenses through fiscal year 2002 but prohibited Amtrak from using federal funds for operating expenses, except for an amount equal to excess Railroad Retirement Tax Act payments after 2002.[3] In fiscal year 2002, Amtrak expects to spend only $185 million (its estimated payments to the railroad retirement system in excess of the retirement benefits for Amtrak employees) of federal funding for expenses other than capital projects.

To meet the goal of operating self-sufficiency and respond to continually growing losses and a widening gap between operating deficits and federal operating subsidies, Amtrak developed a series of strategic business plans. By following these plans, Amtrak has attempted to increase revenues and control costs through such actions as expanding mail and express service,

[3]Amtrak participates in the railroad retirement system, under which each participating railroad pays a portion of the costs for all retirements and benefits in the industry.

adjusting routes and service frequency, and reorganizing into strategic business units. Its Board of Directors approved Amtrak's most recent strategic business plan in October 1998.

Historically, Amtrak received separate federal appropriations for operating expenses and capital improvements. For fiscal year 1999, Amtrak received a single capital appropriation of $609 million instead of separate appropriations for operating and capital assistance. However, the conference report accompanying the appropriation provided that Amtrak could use appropriated funds for the maintenance of equipment (an operating expense) in addition to traditional capital investments.

The Congress also provided Amtrak with financial assistance through the Taxpayer Relief Act of 1997. This act made a total of about $2.2 billion available to Amtrak in fiscal years 1998 and 1999 to acquire capital improvements and pay for the maintenance of existing equipment, among other things.

The Amtrak Reform and Accountability Act of 1997 made certain reforms to Amtrak's operations. Among other things, the act (1) eliminated existing statutory and contractual labor protection arrangements as of May 31, 1998, and required negotiations over new arrangements; (2) repealed the statutory ban on contracting out work when it would result in employee layoffs and made contracting out part of the collective bargaining process (except for food and beverage service, for which contracting out was already allowed); and (3) placed a $200 million cap on the aggregate amount that Amtrak and others must pay rail passengers for all claims (including claims for punitive damages) arising from a single accident or incident.[4]

The act also established an independent council—the Amtrak Reform Council—to evaluate Amtrak's performance and make recommendations for cost containment, productivity improvements, and financial reforms. If at any time more than 2 years after the enactment of the act and the implementation of a financial plan for operating within authorized funding levels, the Council finds that Amtrak is not meeting its financial goals or that Amtrak will require federal operating funds after December 2002, then the Council is to submit to the Congress, within 90 days, an action plan for a restructured national intercity passenger rail system. In addition, if the

[4]These include claims made against Amtrak, any high-speed railroad authority or operator, any commuter authority or operator, any rail carrier, or any state.

above events occur, Amtrak is required to develop and submit an action plan for its liquidation.

The act also eliminated the requirement that Amtrak issue preferred stock to the Department of Transportation in the value of federal appropriations received. As a result, beginning with its fiscal year-end 1998 audited financial statements, Amtrak, following guidance from its external auditors, recorded a significant amount of federal financial assistance as revenues instead of preferred shareholder equity. In addition, a significant amount of the federal funds made available by the Taxpayer Relief Act was also recorded as revenues. One effect of this situation is that Amtrak's fiscal year 1998 financial statements are not comparable to previous financial reports unless certain adjustments are made. In this report, we present net loss and working capital amounts that exclude the amount of federal assistance that Amtrak's audited financial statements include as revenues or current assets in 1998. These adjustments allow us to better compare Amtrak's net loss and working capital positions over time.

Amtrak's Overall Losses Increased in Fiscal Year 1998

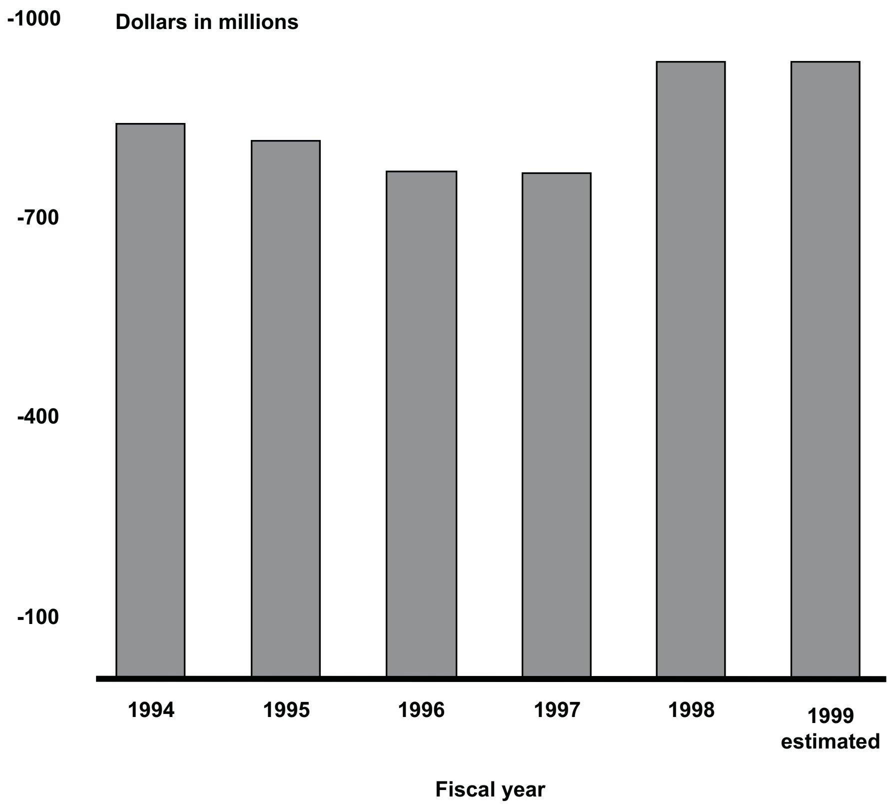
Amtrak had made some progress in reducing its net losses in recent years—from about $833 million in fiscal year 1994[5] to $762 million in fiscal year 1997. However, Amtrak's net loss (adjusted to exclude $577 million of federal funds that its audited financial statements count as revenues)[6] increased to $930 million in fiscal year 1998. (See fig. 1.) This amount is the largest net loss in the last 10 years. One of the reasons for the increase is that the 1998 figure includes retroactive payments attributable to labor negotiations concluded by the end of 1998.[7] But, even when the roughly $106 million of such labor payments are not included in the net loss, the net loss is still $824 million, $62 million more than in fiscal year 1997.

[5]The net loss for fiscal year 1994 excludes a one-time charge of $244 million for restructuring costs and other items.

[6]See the "Background" section for why we made adjustments to the net loss and working capital amounts we present for fiscal year 1998.

[7]Although these retroactive payments are attributable to the period 1995 through 1998, Amtrak's fiscal year 1998 financial statements reflect the liability for the retroactive portion of all labor agreements made in fiscal year 1998 and expected to be made in fiscal year 1999. Amtrak will make these retroactive payments in fiscal years 1999 and 2000.

Figure 1: Amtrak's Net Losses, Fiscal Years 1994 Through 1999



Note: The amount shown for fiscal year 1998 has been adjusted to exclude federal financial assistance from revenues.

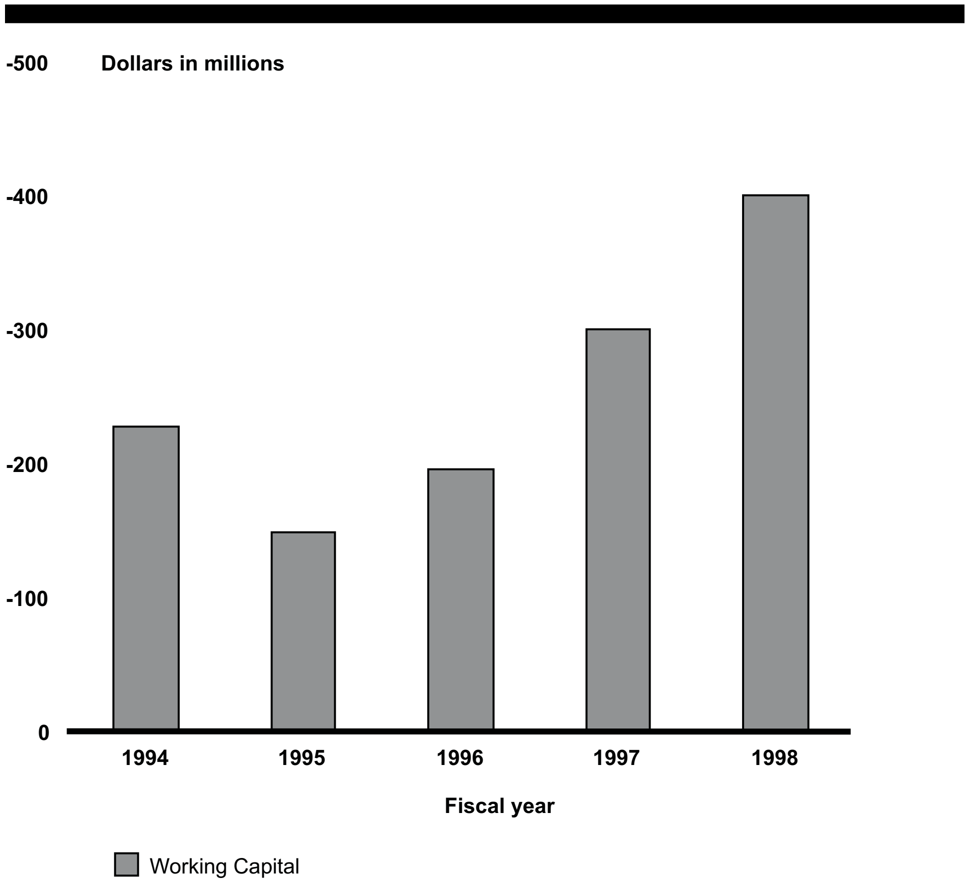
Source: GAO's analysis of Amtrak's data.

Amtrak officials stated that the increase in net loss is also due to an increase in capital investment that resulted in increased depreciation expenses. Specifically, depreciation expenses, a noncash item, increased by $52 million in 1998—from $242 million in fiscal year 1997 to $294 million in fiscal year 1998. Amtrak expects that depreciation expenses will grow by another $66 million in fiscal year 1999 and by additional amounts in subsequent years as it makes additional capital investments. While an increase in depreciation—which reflects the amount of capital equipment that is consumed and must be replaced in future years—increases net loss, Amtrak points out that investments resulting in increased depreciation expenses are expected to have positive effects in the future, such as increasing revenues, reducing costs, and eliminating the need for federal operating support.

In October 1998, Amtrak estimated that the net loss for fiscal year 1999 will be $930 million. However, through April 1999, Amtrak's net loss for the current fiscal year is $11.4 million less than expected.

Another measure of Amtrak's overall financial condition is its working capital (current assets less current liabilities). Working capital measures a corporation's ability to pay its bills when due. Amtrak's working capital deficit (adjusted to exclude $647 million in short-term investments and related interest resulting from unspent Taxpayer Relief Act funds) at the end of fiscal year 1998 was about $400 million. This amount is $100 million worse than the $300 million working capital deficit Amtrak recorded at the end of fiscal year 1997 and is the worst such deficit in at least the last 10 years. Figure 2 shows the degree to which working capital balances have fallen over the past 4 years.

Figure 2: Amtrak's Working Capital, Fiscal Years 1994 Through 1998



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

Amtrak continues to need to borrow money to pay its current-year operating expenses, including those for payroll, fuel, ticket stock, and food. At the end of fiscal year 1997, Amtrak had outstanding borrowing of $75 million to meet its operating expenses. At the end of fiscal year 1998, the amount of outstanding borrowing needed to meet operating expenses had fallen to $50 million. This $50 million in year-end borrowing was half of what Amtrak had estimated at the beginning of the fiscal year. However, at the end of fiscal year 1999, Amtrak estimates, it will need to have $100 million in borrowing to meet its operating expenses. Additionally, Amtrak plans to have short-term borrowing of $100 million outstanding at the end of fiscal year 2000.

To help its cash flow, Amtrak is seeking legislation specifically authorizing it to use its fiscal year 2000 capital appropriation to pay for a wider variety of maintenance expenses than in fiscal year 1999. This would be similar to the flexibility allowed recipients of federal transit financial assistance. For fiscal year 2000, Amtrak is requesting the authority to use its capital appropriation for maintenance-of-way expenses (e.g., costs for maintaining tracks) in addition to maintenance-of-equipment expenses, as permitted in fiscal year 1999. Without this authority, Amtrak has stated that it will not be able to use existing cash to cover $50 million of its operating expenses in fiscal year 2000. As of June 1999, Amtrak had not developed a way to meet its financial obligations if the Congress does not allow this flexibility.

Amtrak's Prospects for Achieving Operating Self-Sufficency Are Clouded by Uncertainties in Its Business Plan and by Past Performance

Amtrak's October 1998 strategic business plan does not anticipate that the corporation will use any federal subsidies for operating expenses (other than for excess railroad retirement expenses) in fiscal year 2002—1 year earlier than requested by the administration and specified in the Amtrak Reform and Accountability Act of 1997. However, considerable uncertainty exists about whether Amtrak will be able to achieve its targets for revenues and expenses for several key business plan actions, and Amtrak historically has not met its financial goals for increasing revenues and reducing expenses.

Amtrak Cites a Narrowing Budget Gap

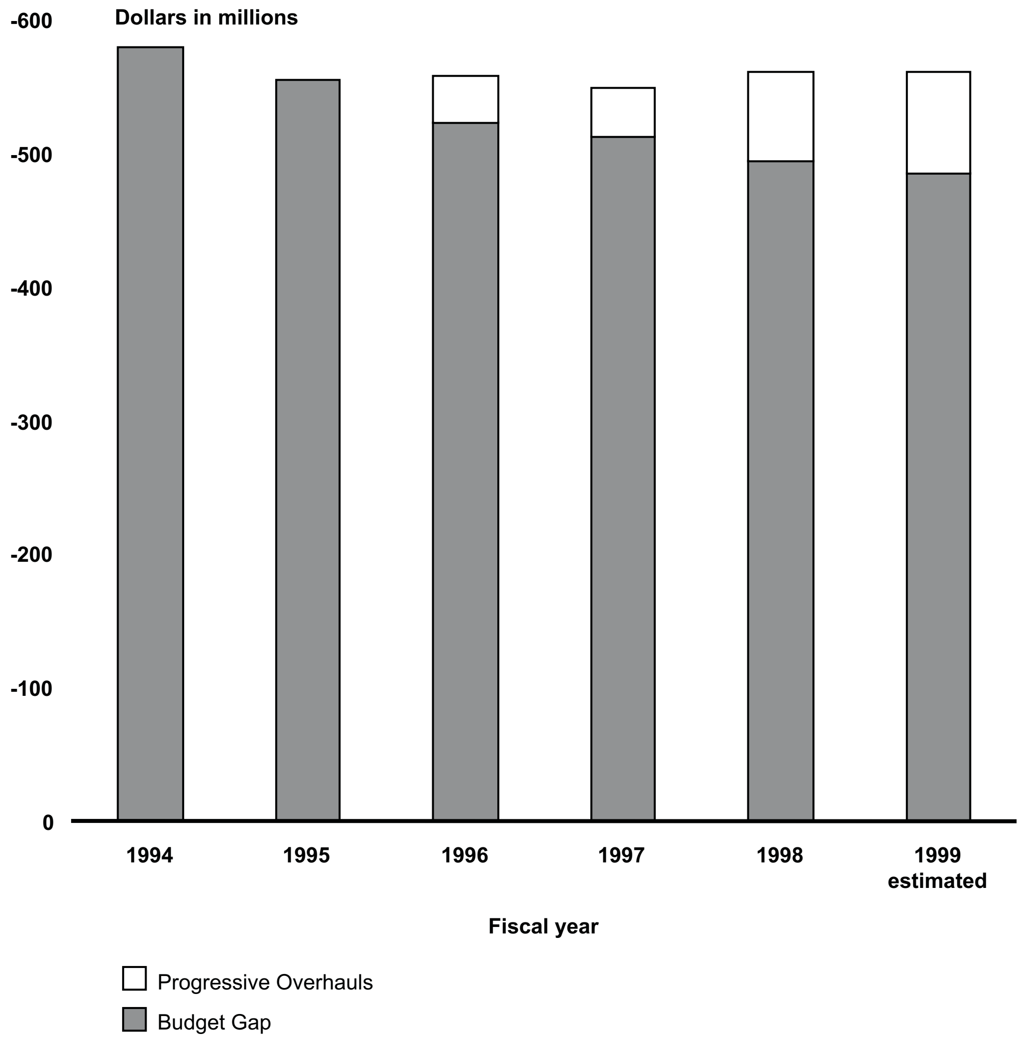
Amtrak's efforts are pointed toward achieving operating self-sufficiency by fiscal year 2002. To do this, Amtrak's strategic business plan focuses on reducing what it calls its "budget gap,"[8] which Amtrak defines as the corporation's net loss less capital-related expenses, including depreciation of its physical plant (such as locomotives, cars, and stations), other noncash expenses, and expenses from its program to progressively overhaul railcars (i.e., to conduct a limited overhaul of cars each year rather than a single comprehensive overhaul every several years). In essence, the budget gap represents expenses not funded by its revenues or its capital program.

According to Amtrak, its budget gap fell by $18 million in fiscal year 1998—from $512 million in fiscal year 1997 to $494 million in fiscal year 1998 after an adjustment for the cost of retroactive labor payments is made. (See fig. 3.) Even though Amtrak's audited financial statements

[8] Amtrak also calls this its "budget result."

allocated the full $106 million amount of the retroactive payments for recently negotiated labor agreements to fiscal year 1998 expenses, Amtrak officials, in calculating the budget gap, allocated the amounts over the years for which those payments actually accrued ($35 million in fiscal year 1996 and in fiscal year 1997 and $36 million in fiscal year 1998). Amtrak officials told us that they believe that such an allocation is a more appropriate methodology for presenting its financial situation. The result of this allocation improves Amtrak's fiscal year 1998 budget gap by $70 million. Amtrak's October 1998 strategic business plan estimates that the budget gap will be reduced by another $10 million in fiscal year 1999.

Figure 3: Amtrak's Budget Gap and Progressive Overhaul Expenses, Fiscal Years 1994 Through 1999



Note: Amtrak's progressive overhaul program started in fiscal year 1995 (and affected its expenses starting in fiscal year 1996). For fiscal year 1998, amounts for progressive overhauls include $4 million to prepare for the Year 2000 date change.

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

However, even with these improvements in Amtrak's budget gap, Amtrak must still reduce its losses substantially if it is to become operationally self-sufficient by the end of fiscal year 2002. In the next 4 fiscal years, Amtrak must reduce its budget gap by $309 million, from $494 million to an amount equivalent to excess railroad retirement payments[9] (estimated at $185 million in fiscal year 2002). This needed improvement by 2002 is about 5 times the $60 million improvement Amtrak was able to achieve in the previous 4 fiscal years, 1995 through 1998.

Another issue in Amtrak's calculation of the budget gap is the treatment of progressive overhaul expenses. Amtrak does not include these expenses in its calculation of the budget gap even though they are considered to be operating expenses under generally accepted accounting principles. As described, the Amtrak Reform and Accountability Act of 1997 prohibits Amtrak from using federal funds for operating expenses, except for an amount equal to excess Railroad Retirement Tax Act payments after 2002. According to Amtrak officials, while generally accepted accounting principles require the recording of such spending as operating expenses, Amtrak funds progressive overhauls through its capital program and therefore believes that the costs for them should be counted as capital costs.[10] If progressive overhauls are included in the calculation of the budget gap, the gap increases by $12 million in fiscal year 1998—from $549 million in fiscal year 1997 to $561 million in fiscal year 1998—and in fiscal year 1999 will be $560 million.

Amtrak's Strategic Business Plan Emphasizes Revenue Growth to Achieve Operational Self-Sufficiency

Under its October 1998 strategic business plan, Amtrak plans to reach financial health by emphasizing business growth, that is, primarily by increasing revenues. Amtrak expects significant revenue increases from implementing new high-speed rail service between Boston and Washington, D.C., and expanding its express service (delivery of higher-value, time-sensitive goods). Amtrak also plans to increase its revenues and control costs by developing a market-based intercity route network that aligns its passenger service more closely with customer demand (adding trains to certain routes or starting new service where appropriate, for instance). Amtrak does not plan to eliminate any routes or services in fiscal year 1999 but has not made any long-term decisions about routes. (In 1997, 39 of Amtrak's 40 routes were unprofitable when

[9]See the “Background” section.

[10]According to Amtrak, if it is unable to fund its progressive overhaul program from federal funds after 2002, it may be forced to move to a heavy overhaul program. Amtrak officials believe that the progressive approach keeps its equipment in a higher average state of good repair and is less expensive.

train, route, and system costs are included.)[11] In addition, by developing and implementing service standards (such as improving service to passengers), Amtrak expects to increase ridership (and revenues) through higher-quality and more consistent service. Finally, Amtrak plans to contain costs primarily by reducing the costs of electric power in the Northeast Corridor and enhancing productivity in a number of ways throughout its system.

Amtrak estimates that its business plan initiatives will result in net financial improvements of $1.6 billion for fiscal years 1999-2002. (See table 1.) In particular, it expects to begin obtaining most revenue increases and cost savings beginning in fiscal year 2000. For example, over the period covered by the plan, Amtrak expects that its initiative for express service will generate a cumulative net impact of about $60 million. Of this $60 million, Amtrak expects to obtain about $56 million between fiscal years 2000 and 2002. Amtrak also estimates that its new high-speed rail service, which will begin in fiscal year 2000, will have a $408 million net impact during the period. Over one-third ($631 million) of the total net impact of $1.6 billion is expected to occur in fiscal year 2002, the last year of the plan.

[11]Intercity Passenger Rail: Financial Performance of Amtrak's Routes (GAO/RCED-98-151, May 14, 1998.)

Table 1: Estimated Financial Results of Amtrak's Initiatives From Fiscal Year 1999 Through Fiscal Year 2002

Dollars in millions

Initiative	Change in revenues	Change in expenses	Net impact	Basis for estimate
Align network to meet customer demand	$60	($45)	$105	Officials' professional judgment
Implement service standards to improve quality	85	(20)	105	Officials' professional judgment
Undertake actions to be defined later	56	(154)	210	Placeholders to balance annual budgets
Begin high-speed service	822	414[a]	408	Ridership forecast
Expand express service	248	188[a]	60	Analyses of market potential
Purchase electricity at wholesale rates	(5)	(34)	29	Contract with a utility company
Subtotal	**$1,266**	**$349**	**$917**	
Implement hundreds of other initiatives[b]	840	148	692	Strategic business units' forecasts
Total	**$2,106**	**$497**	**$1,609**	

[a]The expenses for high-speed rail service and express service exclude $179 million and $8 million for depreciation, respectively.

[b]These hundreds of individual initiatives have been developed by Amtrak's three strategic business units—the Intercity, Northeast Corridor, and West business units, as well as Corporate/Service centers. We did not review the bases for these estimates.

Source: GAO's analysis of Amtrak's October 1998 strategic business plan.

Table 1 also shows that the expected financial impact from six key initiatives will account for nearly 60 percent of the expected net impact—$917 million. The remaining benefits come from hundreds of individual actions outlined in Amtrak's business plan. Overall, Amtrak projects that if it achieves the financial benefits associated with these initiatives, including 100 percent of the $631 million in financial improvements it projects for fiscal year 2002, it will gradually reduce its reliance on federal operating assistance, and achieve operating self-sufficiency in 2002.

To Achieve Estimated Net Impacts for Six Key Initiatives, Amtrak Must Address Uncertainties in Its Strategic Business Plan

All plans are subject to uncertainty and Amtrak's estimates for six key initiatives reflect this uncertainty. First, Amtrak plans to align its service to better meet customer demand, referred to as implementing a market-based network. Amtrak expects to generate $105 million in net impact over the period by such actions as serving currently unserved markets that have good demand potential. According to Amtrak officials, for the most part this estimate was based on senior officials' judgment of changes in revenues and expenses resulting from analysis of the potential for partnerships with states and local governments in certain transportation corridors. However, Amtrak did not supply us with any information on how it derived the $105 million amount.

Second, Amtrak expects to generate another $105 million in net impact by implementing a variety of service standards designed to ensure a consistent, high-quality product. These service standards will be focused on encouraging employees to provide consistent, high-quality service; improving customer-to-staff ratios; addressing customers' complaints and resolving them as quickly as possible; and instituting a service guarantee program (such as providing a transportation credit) if service does not meet established standards. Overall, Amtrak expects that these efforts will increase revenues by generating additional ridership and reduce operating costs by lowering employees' absenteeism. However, the service standards had not been defined at the time the $105 million estimate was made. Instead, Amtrak officials told us that the $105 million estimate was based on extensive analysis completed by senior management, including benchmarking against corporations that had implemented similar types of programs, such as the United States Postal Service, Ritz Carlton, Sears, and Continental Airlines. Amtrak then estimated that it could have a net impact of $59 million per year from (1) a reduction in occasions in which customers will not ride Amtrak again as the result of poor, inconsistent service ($10 million per year); (2) fare increases justified by higher-quality, more consistent service ($20 million per year); (3) increases in employees' productivity ($23 million per year); and (4) reductions in absenteeism ($6 million per year). An Amtrak official told us that Amtrak chose to be conservative in estimating a $105 million in savings over the life of the 4-year plan, rather than utilizing the full $59 million per year in its estimate of savings.

Third, Amtrak's plan contains a broad category of undefined actions referred to as "undefined initiatives" and "planned management actions to be developed." These categories represent $210 million in net impact for which Amtrak had not identified specific initiatives or developed any plan of action at the time the plan was approved. The amounts were placeholders to balance the yearly budgets. According to Amtrak officials, these initiatives represent the gap that Amtrak must fill even if it successfully implements all of its other business plan actions. Amtrak intends to achieve this net impact primarily through cost savings that it will identify on an ongoing basis. By June 1999, Amtrak officials had identified actions representing a net impact of about $49 million, reducing the dollar amount of actions yet to be defined to about $161 million.

Fourth, Amtrak's plan estimates $408 million in net impact from implementing high-speed rail service in the Northeast Corridor. This estimate was based on an extensive ridership forecast. However, in November 1998 the Department of Transportation's Office of Inspector General questioned $192 million of the gross revenue projections for fiscal years 1999 through 2002. In particular, the Inspector General's review indicated that Amtrak was too optimistic regarding the system's ability to generate ridership in the early years of the forecast.[12] While Amtrak disagreed with the Inspector General's assessment of the expected gains in ridership in the early years, this type of disagreement highlights the inherent uncertainty in estimating revenues from high-speed rail service.

Fifth, Amtrak estimates that its express service will result in a net impact of $60 million, which Amtrak officials stated was based on their assessment of the market potential for this service. Amtrak has made some initial steps in this area. For example, it has entered into a partnership with the United Parcel Service and four other carriers to provide time-sensitive express service generating an estimated $2.9 million in annual revenues (less than 1 percent of Amtrak's estimate of revenues from express service over the period covered by the business plan). However, Amtrak is new to this area and does not yet have a track record on which to base its projections. In addition, Amtrak does not yet have long-term contracts to support much of the projected financial benefit. Furthermore, much of the expected benefit depends on Amtrak's expanding its fleet of express equipment through acquisition, leasing, or other arrangements, most of which still need the approval of Amtrak's Board of Directors. Thus, while it is possible that Amtrak may achieve its net revenue goal, many important actions remain to be taken.

Finally, Amtrak plans to have net savings of $29 million from buying electric power in the Northeast Corridor at wholesale rates. Currently, Amtrak buys electricity at retail rates for its own use and for resale to commuter railroads owned by state and local governments. Its estimated cost savings were based on negotiations with a utility under which Amtrak would purchase power at a wholesale price. However, the Federal Energy Regulatory Commission denied a request to treat Amtrak as a government entity that would be exempt from the Federal Power Act's restrictions on wholesale power purchases. Consequently, Amtrak now plans to seek enactment of legislation that would designate the railroad as a power wholesaler. Amtrak's estimate of savings is contingent upon obtaining this

[12]Amtrak officials pointed out that the Inspector General's report included greater estimated revenues than Amtrak did after 2003, resulting in a convergence of the estimates by 2006.

legislation by September 30, 2000. In the meantime, Amtrak officials stated that Amtrak will help cut its electricity costs by using a competitive bid process allowed under deregulation, including “retail choice” programs in Pennsylvania, New York, Massachusetts, Rhode Island, and Connecticut for electric power purchases. However, this approach will not achieve Amtrak’s estimated $29 million in savings.

Amtrak Has Not Achieved Its Plans for the Budget Gap, Although Performance Is Improving

Amtrak has been unable to achieve its planned budget gap in any of the last 4 years. Specifically, from fiscal year 1995 through fiscal year 1998, Amtrak’s budget gap was, in total, $285 million more than planned, as shown in table 2.[13] This result occurred primarily because Amtrak’s expenses were significantly higher than planned. During the 4-year period, Amtrak’s revenues were $34 million less than planned, and expenses were $251 million more than planned. As a result, Amtrak’s actual budget gap was higher than it expected. However, the table also shows that the difference between the planned budget gap and the actual budget gap has been decreasing since fiscal year 1996. Moreover, through April of the current fiscal year, the budget gap is about $10 million less than what Amtrak had estimated for the first 7 months of fiscal year 1999.[14]

Table 2: Degree to Which Amtrak’s Budget Gap Exceeded Its Goals for Fiscal Years 1995 Through 1998

Dollars in millions

	Difference between planned and actual performance—Better/(Worse)				
	1995	1996	1997	1998[a]	Total
Revenues	$152	($48)	$48	($186)	($34)
Expenses	(163)	(77)	(155)	144	(251)
Budget gap	($11)	($125)	($107)	($42)	($285)

Note: Expenses of about $106 million in fiscal year 1998 retroactive labor payments were not included in this analysis because they were not in Amtrak’s strategic business plans.

[a]Compares differences based on Amtrak’s September 1997 strategic business plan rather than the revised March 1998 plan. See the “Agency Comments and Our Evaluation” section for a pertinent discussion.

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

[13]This table focuses on the difference between actual and planned performance. See fig. 3 for total losses reflected by the budget gap.

[14]Amtrak’s budget result was a loss of about $35 million for the first 7 months of fiscal year 1999, as opposed to the estimated $45 million loss.

The table shows that Amtrak's revenues exceeded planned amounts for 2 of the 4 years. Fiscal year 1998 revenues were significantly lower than planned (by $186 million), primarily because of lower than expected express service business. In contrast, expenses were greater than planned in fiscal years 1995 through 1997 but much lower than planned (by $144 million) in fiscal year 1998. The better than planned results were primarily due to lower than expected train operation costs, such as lower than expected fuel costs. If Amtrak experiences difficulties in controlling expenses over the next 4 years, it will have to generate significantly more revenues than planned in order to achieve operating self-sufficiency.

Federal Funding and Reform Legislation Will Likely Have Little Short-Term Impact on Improving Amtrak's Overall Financial Condition

Current and planned annual federal funding and reforms contained in the Amtrak Reform and Accountability Act of 1997 are likely to have little short-term impact on improving Amtrak's overall financial condition. In the short term, continued annual federal funding will help Amtrak cover a significant portion of its operating expenses for maintenance and help meet its cash flow needs. However, in the long term, using these funds for maintenance expenses will limit the use of funding for capital investments that would help Amtrak reduce its costs and increase its revenues in the future. Finally, although the act allowed Amtrak greater flexibility in its business operations, these reforms are not likely to provide immediate financial benefits.

Use of Federal Funds for Maintenance Expenses Limits Needed Capital Investments

According to its October 1998 strategic business plan, Amtrak ultimately plans to use $559 million (about 92 percent) of its $609 million fiscal year 1999 capital appropriation to pay for the maintenance of equipment—a use specifically referred to in the conference report accompanying the appropriation. Most of the remaining $50 million will be used to pay principal on its capital debt. Amtrak plans to continue using a large portion of the appropriations that it expects to receive from fiscal year 2000 through fiscal year 2002 for maintenance expenses (including progressive overhauls)—in total, about $1 billion. This $1 billion represents nearly two-thirds of the $1.6 billion Amtrak expects to receive through annual federal capital appropriations.[15]

The short-term benefits of using substantial portions of its capital appropriations for maintenance carry long-term consequences. Capital investments play a critical role in supporting Amtrak's business plan and

[15]According to Amtrak's October 1998 strategic business plan, the Office of Management and Budget's 5-year funding plan incorporated anticipated capital support of $571 million for fiscal year 2000 and $521 million each year for fiscal 2001 and 2002, for a total of about $1.6 billion for the 3 fiscal years.

ultimately in building and maintaining Amtrak's viability.[16] However, as we reported last year, Amtrak had a $500 million shortfall between its estimated capital needs and available funding.[17] Using federal funds for maintenance will limit the funds available for needed capital investments that would help Amtrak reduce its costs and increase its revenues in the future. By using its federal appropriations to cover maintenance expenses, Amtrak may widen this gap between its stated capital needs and expected available funds.

However, in fiscal year 1999, Amtrak has plans to use $758 million of the $2.2 billion it received through the Taxpayer Relief Act of 1997 for capital improvements in addition to the $558 million its Board of Directors approved for capital investments in fiscal year 1998. Amtrak does not yet have a capital plan detailing its capital investments for the remainder of these funds. Amtrak has pledged to ultimately use all of the $2.2 billion for high-return capital initiatives and for certain mandatory and tactical projects. In the short term, Amtrak plans to temporarily use a significant portion of these funds for certain authorized expenses for equipment maintenance because (under an agreement with the administration) the railroad will not draw down all of its fiscal year 1999 federal capital appropriation in the year in which the funds are appropriated.[18] Amtrak expects that as its revenues increase as a result of its strategic business plan initiatives, it will repay the borrowed Taxpayer Relief Act funds.

Finally, after 2002, questions about whether Amtrak is truly operationally self-sufficient would arise if Amtrak's capital appropriations are made available and used for maintenance expenses, which are operating expenses. On the other hand, if Amtrak is not permitted to continue to use appropriated funds for maintenance, then it would have to look for additional ways to increase revenues and reduce expenses.

Short-Term Financial Effects of Amtrak Reform Legislation May Be Limited

The Amtrak Reform and Accountability Act of 1997 was intended to help improve Amtrak's financial condition by making reforms to Amtrak's operations to help the railroad better control and manage its costs. Among the act's reforms aimed at improving Amtrak's financial condition were provisions that

[16]See GAO/T-RCED-98-134.

[17]See GAO/T-RCED-98-134. As of early June 1999, Amtrak's Board of Directors had not approved a revised capital plan showing capital needs and the funds expected to be available to meet those needs.

[18]Amtrak's October 1998 strategic business plan assumes that it may draw down only 40 percent of each year's general capital appropriation on the first day of the fiscal year and the remaining 60 percent on the first day of the following fiscal year.

- eliminated, as of May 31, 1998, existing statutory and contractual labor protection arrangements that provided up to 6 years of compensation for employees who lost their jobs because of the discontinuance of service on a route or such other covered actions and required negotiation over new arrangements;
- repealed the statutory ban on contracting out work that would result in employee layoffs (except for food and beverage service, which could already be contracted out), incorporated the ban into existing collective bargaining agreements, and made contracting out subject to negotiation by November 1999; and
- placed a $200 million cap on the aggregate amount that Amtrak and others must pay rail passengers for all claims (including claims for punitive damages) arising from a single accident or incident.

As we reported in 1998, the reforms contained in the act may have little, if any, immediate effect on Amtrak's financial performance for several reasons. First, regarding labor protection arrangements, after 10 negotiating sessions, Amtrak and its unions agreed to submit the matter to binding arbitration. As of early June 1999, the panel of arbitrators had not reached a decision.

Second, Amtrak officials do not expect to address contracting out work unrelated to food and beverage service before November 1, 1999. The officials believe the repeal of the ban may provide long-term flexibility, including flexibility in union negotiations and in controlling costs, but at this time cannot predict what changes may result from these negotiations and what the effect on costs may be.

Finally, Amtrak believes the limit of $200 million per accident for rail passenger liability claims may have a limited financial effect because this cap is significantly higher than amounts Amtrak has historically paid on such claims. This reform may not result in measurable financial savings as much as in additional flexibility in negotiating with labor unions and in addressing the freight railroads' concerns over such issues as liability payments.[19]

The act also made other changes that have the potential for a significant impact on Amtrak's future. For example, it established an independent council—the Amtrak Reform Council—to evaluate Amtrak's performance and make recommendations for cost containment, productivity

[19]The financial effects—if any—of the March 15, 1999, crash of Amtrak's City of New Orleans train operating on Illinois Central Railroad Company tracks in Bourbonnais, Illinois, are not yet known.

improvements, and financial reforms. If, at any time more than 2 years after the enactment of the act and implementation of a financial plan for operating within authorized funding levels, the Council finds that Amtrak is not meeting its financial goals or that it will require operating funds after December 2002, then the Council is to submit to the Congress, within 90 days, an action plan for a restructured national intercity passenger rail system. In addition, if the above events occur, Amtrak is required to develop and submit an action plan for its liquidation.

Conclusions

Amtrak has focused its strategic business plan on the near-term goal of becoming operationally self-sufficient by 2002—a goal established by the administration and the Congress. Amtrak's plan is ambitious; and, to its credit, it is currently somewhat ahead of the plan's financial goals. Yet the overwhelming bulk of the expected financial benefits of the plan are still to come—with most to be achieved in the final year of the plan. Our concerns are two-fold. First, several aspects of the plan are subject to considerable uncertainty, including, but not limited to, identifying over $160 million in productivity and other improvements during the remaining 3 years of the plan. Second, Amtrak has a history of not meeting its financial goals, and the current 4-year plan anticipates achieving about 5 times as much in financial improvements as Amtrak was able to achieve through its business plans over the previous 4 years. We recognize that all plans by their very nature are subject to uncertainty. However, given the uncertainties in the current plan, Amtrak's history of missing financial goals, and the magnitude of the savings still to be achieved, it is difficult to be confident that Amtrak will become operationally self-sufficient within the next 3 years. The stakes are high: The Congress gave Amtrak until the end of fiscal year 2002 to reach operational self-sufficiency and required that plans for restructuring and liquidating Amtrak be prepared if the railroad does not meet this goal.

Agency Comments and Our Evaluation

We provided Amtrak and the Federal Railroad Administration within the Department of Transportation copies of a draft of this report for their review and comment. We met with Amtrak officials, including the Vice-President for Government and Public Affairs and the Controller. In general, Amtrak believed that the draft report contained inappropriate analyses and mischaracterized how Amtrak derived selected expected financial benefits in its strategic business plan.

Amtrak believes that the preferred measure of progress toward achieving operating self-sufficiency is not net loss but rather its “budget gap,” an Amtrak financial measure that excludes expenses funded from its capital program. Amtrak apparently misunderstood the purpose of our work. As stated in the draft report, the objective of this portion of our work was to assess Amtrak’s financial performance in 1998. The work was not limited to assessing progress in meeting its goal of operational self-sufficiency. Consequently, a discussion of financial performance that is limited to Amtrak’s budget gap would be inappropriate and incomplete. We have clarified the objective and the discussion of this topic in the report.

Amtrak also disagreed with our inclusion of expenses for progressive overhauls in our discussion of Amtrak’s progress in achieving operational self-sufficiency. Amtrak stated that while generally accepted accounting principles require Amtrak to record such spending as operating expenses, it funds progressive overhauls through its capital program and therefore believes that they should be counted as capital costs. As a result, in Amtrak’s view, the costs of progressive overhauls would be excluded from the calculation of Amtrak’s progress toward achieving operational self-sufficiency by 2002. As discussed in our report, generally accepted accounting principles consider progressive overhaul expenses to be operating expenses. As a result, we have not revised how these costs are categorized. We have added to this report Amtrak’s rationale for excluding progressive overhaul expenses from its budget gap and show the impact of both including and excluding it.

Amtrak stated that we did not recognize that the higher net loss in fiscal year 1998 was partially the result of higher depreciation expenses resulting from investments and that these investments will have positive impacts for ridership and revenues in the future. We agree and have included information regarding the impact that Amtrak’s capital investments have had on its operating expenses and net loss. We have also added a discussion of the important role that these investments will have on Amtrak’s ability to increase revenues in the future.

Amtrak officials stated that our analysis of actual versus planned financial results for fiscal year 1998 was inappropriate because we used Amtrak’s original strategic business plan issued in September 1997 rather than its revised plan issued in March 1998. They stated that the revised March plan is a better benchmark to judge its fiscal year performance because it reflects business changes resulting from the enactment of the Amtrak Reform and Accountability Act and the Taxpayer Relief Act in 1997, as well as other factors, such as significant management changes. We disagree. We believe that the most appropriate benchmark for evaluating yearly performance is the plan approved at the beginning of the fiscal year. Revising a plan 6 months into a fiscal year significantly reduces the uncertainty inherent in preparing an initial estimate of performance. In addition, the March 1998 plan was an exception—Amtrak typically produces a plan in September or October of each year. Finally, while we agree that the enactment of the two laws and Amtrak's change in leadership were significant events for Amtrak, the primary financial revisions contained in the March 1998 plan were reductions in revenues associated with Amtrak's mail and express service initiatives. These reductions were primarily due to revised assumptions about the market for express service, rather than a direct result of the above mentioned events.

Amtrak also objected to our characterization of how it derived estimates for the expected financial benefits associated with the initiatives to (1) implement service standards and (2) align its route network to meet customer demand. Amtrak stated that the estimates were based on extensive analyses completed by senior management officials and included benchmarking with other service providers. We believe that the characterization in our draft report was wholly consistent with the information that we obtained from top financial officials and others within Amtrak. In commenting on our draft report, Amtrak officials supplied us with a rationale for how they derived the estimate for financial benefits associated with implementing service standards. We have added this material to our report. The officials did not supply any additional information on how they derived the estimate for the expected financial benefits associated with aligning Amtrak's route network to meet customer demand. Based on the additional information received, we revised our report to characterize how Amtrak developed its expected financial benefits as using "professional judgment" rather than making "best guesses."

Finally, Amtrak officials offered a number of technical and clarifying comments that we incorporated throughout the report, where appropriate.

In commenting on our draft report, the Department of Transportation stated that when the goal of achieving operational self-sufficiency was established, the administration understood that meeting the goal would not be easy. (See app. I.) It believes that Amtrak's strategic business plan provides a credible path for achieving operational self-sufficiency. The

Department also stated that it believes Amtrak is moving in the right direction and is currently ahead of its financial targets identified in the corporation's strategic business plan. It stated that our report should recognize Amtrak's increased investment in traditional capital projects. As discussed above, we have added this information to our report. The Department also commented that the Taxpayer Relief Act of 1997 authorizes Amtrak to use Taxpayer Relief Act funds for some maintenance activities. Although the draft report provided to the Department included this fact, we have added to our report a further reference to this allowed use of Taxpayer Relief Act funds.

Scope and Methodology

To determine the status of Amtrak's financial condition, we reviewed its fiscal year 1998 annual report, October 1998 strategic business plan, and fiscal year 2000 legislative report and federal grant request. We also interviewed Amtrak's Chief Financial Officer and other financial systems officials. To obtain a historical perspective on Amtrak's financial condition, we also reviewed Amtrak's annual reports for fiscal years 1994 through 1997. To provide information on Amtrak's current strategic plan for obtaining operating self-sufficiency, we reviewed its current and previous strategic business plans and the Department of Transportation's Office of Inspector General's Summary Report on the Independent Assessment of Amtrak's Financial Needs Through Fiscal Year 2002. We also discussed the current strategic business plan with a variety of Amtrak officials, including officials in its Intercity and Northeast Corridor strategic business units and Amtrak's Chief Financial Officer. We did not independently verify the accuracy of Amtrak's financial data in its current strategic business plan.

Finally, to provide information on the extent to which federal funding and recently enacted legislative reforms will help Amtrak resolve its financial problems, we first reviewed the Amtrak Reform and Accountability Act of 1997, the Taxpayer Relief Act of 1997, and Amtrak's fiscal year 1999 appropriation. We then discussed the likely impact of these acts with Amtrak officials. We also reviewed Amtrak's proposed capital plan and interviewed Amtrak officials about its contents.

We conducted our review from January 1999 through June 1999 in accordance with generally accepted government auditing standards.

As agreed with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days after the date of this letter. At that time, we will send copies of this report to interested congressional committees; George D. Warrington, the President and Chief Executive Officer of Amtrak; the Honorable Rodney E. Slater, the Secretary of Transportation; the Honorable Jolene M. Molotoris, the Administrator of the Federal Railroad Administration; the Honorable Jacob J. Lew, the Director of the Office of Management and Budget; and Gil Carmichael, the Chairman of the Amtrak Reform Council. We will also make copies available to others on request.

If you or your staff have any questions about this report, please call me at (202) 512-3650. Key contributors to this report were Ruthann Balciunas, Catherine Colwell, David Lichtenfeld, and James Ratzenberger.

Sincerely yours,

Phyllis F. Scheinberg

Phyllis F. Scheinberg
Associate Director,
Transportation Issues

Comments From the Department of Transportation

U.S. Department of Transportation

Assistant Secretary for Administration

400 Seventh St., S.W. Washington, D.C. 20590

June 14, 1999

Phyllis F. Scheinberg
Associate Director, Transportation Issues
General Accounting Office
Washington, D.C. 20548

Dear Ms. Scheinberg:

Thank you for the opportunity to review the General Accounting Office (GAO) draft report, "Intercity Passenger Rail: Amtrak's Financial Problems Persist," RCED-99-181. Amtrak will no doubt provide detailed comments on the draft report. Our comments address some of the major topics in the draft where GAO's interpretation of the facts seems unduly pessimistic.

Amtrak is moving in the right direction in preparing the foundation for a corporation that, in the early years of the next century, will provide significantly better service without requiring Federal operating subsidies. The draft report correctly notes that the Clinton Administration established for Amtrak the goal of achieving operating self-sufficiency by the end of Fiscal Year (FY) 2002. When that goal was established, the Administration understood that achieving it would not be easy. Indeed, as the draft report points out, few, if any, national passenger rail systems worldwide have achieved operating self-sufficiency. Nonetheless, the Administration remains confident that Amtrak will achieve this goal. Amtrak has shown progress each year since 1994 when considered in terms of net operating losses less depreciation and other cash expenses. Up to this point in FY 1999, Amtrak is ahead of the very difficult targets identified in its strategic plan for achieving operating self-sufficiency.

The draft report should recognize that Amtrak committed more funds to traditional capital improvements during the 5 year period between FY 1995 and FY 1999, than during any similar period in its history. This has led to a major recapitalization of Amtrak's fleet of locomotives and passenger cars, the acquisition of state-of-the-art high-speed passenger equipment for the Northeast Corridor, critical investments necessary for developing passenger markets such as the Pacific Northwest, expanding the Corporation's presence in the lucrative mail and express business, and undertaking a major infrastructure expansion by extending electric traction from New Haven, CT to Boston, MA. In addition, the draft report could recognize that

Amtrak's use of capital funds to help keep the existing fleet operating effectively is an acceptable and appropriate use of these funds. For example, the Taxpayer Relief Act of 1997 allows the use of capital funds for some maintenance activities. Furthermore, the use of capital funds for maintenance was recently authorized for the transit industry, the industry most closely resembling Amtrak, in section 3003 of the Transportation Equity Act for the 21st Century (TEA-21) (49 U.S.C. 5302(a)(1)). In the FY 2000 President's Budget, the Administration and Amtrak are seeking to bring the definition of capital that applies to Amtrak in line with the definition in TEA-21 that applies to the transit industry.

Amtrak has initiated a number of innovations to improve its financial condition. Part of the Administration's strategy for moving Amtrak to operating self-sufficiency is to make the Corporation more entrepreneurial and act more like a private business. If the Corporation is to succeed, it must consider new ideas which may not always have a track record available to serve as the basis of projections.

Amtrak has developed a strategic plan, under the auspices of the new Amtrak Reform Board of Directors, which provides a credible path for achieving the goal of an operationally self-sufficient Amtrak that provides quality service over a national system. The Department and Amtrak's Board of Directors are committed to successfully achieving that goal.

Thank you for the opportunity to offer comments on the draft report. Please contact Martin Gertel on 202-366-5145 with any questions.

Sincerely,

Melissa J. Allen

Melissa J. Allen

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