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STATEMENT OF WILLIAM T. COLEMAN, JR., SECRETARY OF TRANSPORTATION, BEFORE THE SUBCOMMITTEE ON SURFACE TRANSPORTATION, COMMITTEE ON COMMERCE OF THE UNITED STATES SENATE, REGARDING THE RAILROAD REVITALIZATION ACT, WORKING DRAFT NO. 1 OF THE RAIL SERVICES ACT OF 1975, AND THE RAIL REHABILITATION ACT OF 1975, MONDAY, OCTOBER 20, 1975.

Mr. Chairman and Members of the Subcommittee:

I appear today before this Committee to continue our dialogue to try to resolve the crisis which faces our Nation's railroad service. Unfortunately, Subcommittee Working Draft No. 1 of the Rail Services Act of 1975 is so far off the mark that the dialogue will have to be much longer than I would have thought necessary, but I have no other alternative. Mr. Chairman, I must do some plain talking on the subject for, while it is clear we share a common objective, it is equally clear that there are monumental differences between the Administration and USRA and the drafters of Working Draft No. 1 of the Rail Services Act of 1975 which must be reconciled if we are to achieve the goal of providing reliable, competitive, and profitable freight rail service and the level of passenger service justified by the public interest. Those differences are: the Administration's role in the task of revitalizing our railroads, the level of expenditure of the Federal

taxpayer's money, and whether it is to be loans or grants, and the response to the need for regulatory reform.

Let me also say at the beginning of my testimony that I make a clear distinction between freight and passenger rail service. There is no present alternative to an efficient, profitable rail freight system in this country. It is the number one transportation priority in the Nation today.

I would first like to give you my comments on the provisions of the Working Draft bill which deal with the implementation of USRA's final system plan. I will confine my comments to those points where the Working Draft differs from the amendments to the Regional Rail Reorganization Act that USRA has proposed and the Administration supports. Actually, the Working Draft differs so dramatically from the USRA amendments that I think we could all derive some benefit from reviewing the history of how the Final System Plan and the USRA implementing amendments came about.

Under the mandate of the RRRA, USRA was directed to produce a Final System Plan that would create a private, financially self-sustaining rail system in the northeast and midwest, would retain and promote transportation competition in the region, and

would establish a rail system that met the needs of the region and preserved the existing patterns of service as much as possible. These goals were to be achieved within (1) a funding limit of $1 billion in loan guarantees for ConRail, (2) up to $250 million for employee protection, and (3) up to $180 million for light density lines with 70-30% federal-state cost sharing over a 2 year period.

After extensive investigation and analysis, USRA issued its Preliminary System Plan on February 26 of this year. The Rail Services Planning Office of the ICC conducted hearings on the PSP and issued a lengthy evaluation.

Based on all these comments, hearings, new data, and further investigation and analysis, USRA returned to the task of preparing the Final System Plan. USRA determined that ConRail would require more than $1 billion in overall funding and in a form different from loan guarantees. After detailed studies USRA determined that the amount needed was $1.85 billion and there should be a cushion of $250 million. The Administration accepted USRA's determinations. The sole question was how this government money should be invested and what protection should the investor of such money have. The Administration and USRA then agreed on how such money should be invested. Indeed, the vote of the Board was

10-0 on this question. Only Governor Scranton, who was absent, did not vote. I will be happy to introduce into the record a copy of the USRA Board Minutes to attest to this fact. I think it should be equally clear that the public investment had to be protected by the kinds of provisions appropriate when huge amounts of taxpayer money is being spent. USRA and the Administration reached agreement on this issue.

What later emerged was USRA's Final System Plan and the USRA package of implementing amendments -- the product of these joint efforts. The USRA amendments cannot be called blithely "an Administration bill". We strongly support the USRA bill; it is the product of thoughtful and fair negotiations between USRA and the Administration on how to protect the public investment.

I have reviewed these events because after all these efforts by so many people, I am astounded at how quickly, and in some areas how completely, the fruit of those efforts has been discarded. USRA spent $40 million, 18 months of work, and employed 250 people. I urge this Committee to consider the process by which the USRA amendments were drafted and the substantive merits of those amendments, and then to consider again whether the USRA amendments should not receive the endorsement of this Committee.

The Working Draft prepared by the staff differs critically

from USRA's proposal and the Department's recommendation in its failure to include creation of the Government Investment Committee of the USRA Board. Composed simply of three persons already members of the USRA Board, the GIC is a body designed to place public officials who are accountable to the people and to the people's representatives in a position to decide what should be done by way of further government investment, if and only if ConRail fails to meet the financial schedule, even after providing more than adequate latitude for changes from the financial projections. No one should fear that the GIC will become excessively entangled in ConRail's daily affairs; its authority to intervene in investment decisions of USRA is subject both to specific conditions in the proposed USRA amendments and to further conditions agreed upon by ConRail and USRA. The GIC's power is limited to extreme situations in which it appears that, despite government investment, ConRail has failed substantially to live up to agreements with USRA under which the government investment was made, or is clearly on the road to financial disaster.

The Working Draft bill prepared by your Committee's staff reduces the ConRail Board from fifteen to nine members,

reducing from six to two the number of Presidential appointees and from two to one the number of representatives of the debenture and series A preferred stockholders. Finally, the President of USRA and the President and Chairman of ConRail are not made ex officio Board members, and the USRA plan for periodic resignation by the Presidential appointees is abandoned in the draft bill in light of the other changes.

Meaningful membership on the ConRail Board of people nominated by the government is essential if the taxpayers of this country are to be given assurance that their investment will be watched by people responsible to them. In any other investment decision of this magnitude, the group making the only significant outside investment in an enterprise would ask for Board membership as a prudent check on the uses to which their money was being put. The public is entitled to at least this minimum typical protection when a private corporation such as ConRail is to be the beneficiary of a huge infusion of federal money. At the same time this government participation will not hamstring the private enterprise incentives or freedom of ConRail management. Since the government wishes to be repaid, it would seem clear that the government-nominated directors will be as interested as any other director in the financial success and long-run health of ConRail.

Indeed the Supreme Court, in its opinion on the constitutionality of the Rail Act, recognized the broader responsibility of such directors to all financial interests in ConRail. See Regional Rail Reorganization Act Cases 419 U.S. 102, 152 (1974).

Legislating membership on the ConRail Board of the Corporation's chief operating officers is an important means of bringing to the Board accurate information about operations and finance. More importantly, it puts influential voices for management flexibility and freedom on the Board. Simply leaving this choice up to the other directors, as the staff's draft bill presently does, does not provide enough assurance that management will have a spokesman on the Board.

In three critical places the Working Draft commits the federal government to potential expenditures vastly larger than those held to be required to make ConRail successful as set forth in the Final System Plan. First, under the Working Draft the certificates of value will have a total value equal to whatever the special court decides is the constitutional minimum value to which the transferor railroad is entitled if the transferor elects this remedy. Second, all profitable railroads which accept transfers of property designated under the Final System Plan will be indemnified and held harmless by the federal government from any subsequent deficiency

judgment, not just those roads accepting transfers found by USRA to be essential to the Final System Plan's basic industry structure. Finally, the Working Draft authorizes a total federal investment in ConRail of $4 billion which is $1.9 billion more than the Final System Plan states is needed. The Department of Transportation opposes each of these unnecessary and foolish extra expenditures and fails to see how any government officials could authorize investment in a private company which is beyond what USRA said is needed. Providing more money would simply be an incentive for inefficiency.

I would like at this point to address two related attempts, reflected in a new section in the staff's Working Draft bill, to persuade Congress to inflate the certificates of value to be distributed to the railroad estates. The first attempt is the estates' more audacious gamble--to give the certificates a ceiling not of $422 million, the value which USRA has placed on the estates' assets, but rather of whatever the special court says the creditors are constitutionally due. In their second, more mitigated attempt, the estates suggest that the certificates be given a value equal to whatever the special court decides is the net liquidation value of the rail assets rather than the fixed $422 million figure which USRA's exhaustive study indicated was the net liquidation

value of the bankrupts' properties.

Both versions subtly seek to prey upon the uncertainties and imprecisions necessarily found in even so thorough and authoritative a report as the Final System Plan. In the name of relieving some of the resultant anxieties, the estates suggest this slight-of-hand trick with the certificates of value. The estates' efforts reflect their repeated claims that the process in which we are all engaged is a condemnation rather than a reorganization. It is true that the certificates of value as suggested by USRA are instruments not typical in an ordinary reorganization, and are in no sense compelled by reorganization law or constitutional law. They were originally suggested by USRA simply to give the estates some additional insurance from the uncertainties necessarily involved in this reorganization. The estates are now attempting to turn this gratuitous USRA effort on its head in the hope that inflating the certificates will misleadingly signal to the courts some admission by Congress that it thinks it may be working a condemnation. But all our energy has been bent to the task of making sure this process is <u>not</u> a condemnation but rather an income-based reorganization. It would be ironic, and tragic, if the estates succeeded in making the certificates of value,

which are a legally superfluous sweetener for the creditors, the vehicle by which this reorganization is transformed into a condemnation. To open up the value of the certificates as the estates suggest is not only unnecessary to an income-based reorganization, it is, and of course here the true motives of the estates are exposed, a dangerous raid on the U.S. Treasury and the American taxpayer.

The draft bill's expansion of the indemnification protection is wholly at odds with the purpose of the indemnification proposal in the Final System Plan and an unnecessary potential expenditure. The proposal to indemnify profitable railroads only for those transfers deemed essential to the Final System Plan, a proposal which means indemnification for the Chessie alone, was purposefully made to be very narrow. USRA and DOT do not suggest that the American taxpayer underwrite the investment schemes of all the profitable railroads in the northeast and midwest. The exception for the Chessie was made because that transfer is essential to the fulfillment of one of the statutory goals of the Final System Plan - the promotion of competition. The other transfers are not essential to the FSP's goals. The blanket indemnification plan in the draft bill places the federal

government in the position of partially bankrolling the expansion dreams of a number of private railroads when no public purpose is served. I do not think the federal government should be an investment banker for these railroads, and I hope this Committee does not think so either.

Let me say, unequivocally, that increasing the federal investment at this time in ConRail to $4 billion is irresponsible. Let me also point out that if the federal government invests more than the minimum necessary to make ConRail a viable, profit-making, private company, the beneficiaries of the excess will not be the general public but rather tha bankrupt estates who will have transferred to ConRail the rail assets which now are little more than monuments to their mismanagement, and who will receive back owner ship interest in a gold-plated ConRail. I suggest that before we make this gift of taxpayer money to the Penn Central creditors we place some faith in the planning efforts of USRA and the recommendations it has made. USRA has told us that $2.1 billion is sufficient, and it seems appropriate to see what that huge sum can accomplish before we commit even more federal money.

While there are further points at which the draft bill differs from the USRA proposal which we support, let me close this discussion with mention of the draft bill's section on supplementary transfers.

This section would place authority for proposing supplementary transfers solely in USRA, limit the time during which such transfers can be made to the four year period following the effective date of the Final System Plan, and give the ICC review powers over these transfers.

The ICC's new role is inconsistent with the purely advisory power accorded it in the Regional Rail Reorganization Act. Moreover, the reintroduction of review under section 5 of the Interstate Commerce Act is incompatible with the spirit of section 601(b) of the RRRA which exempts this reorganization process from the ICC review that so often slowed earlier reorganizations. It might well be asked if the ICC could conduct a meaningful section 5 review of a supplementary transfer in a vacuum, that is, review the supplementary transfer under section 5 standards yet not review the Final System Plan transfers which provide the context in which supplementary transfers will be made. The ICC's role seems particularly superfluous given the hearings conducted by USRA and the plenary review of the special court. The ICC will almost necessarily duplicate the work of one or the other.

The draft bill would permit anyone to petition USRA to consider supplementary transfers rather than limiting this group to USRA, the ICC, and the Secretary of Transportation, a situation which could produce intolerable confusion and duplication. At the same time, if USRA rejects a proposed supplementary transfer, it is never presented

to the special court even if it has merit and would be approved by the court. In contrast, the procedure under the USRA amendments would permit the Secretary of Transportation to "appeal" a rejection by USRA to the special court when USRA rejects a supplementary transfer suggested by the Secretary, and thus provide at least some check on USRA's decisions. When such an "appeal" is taken, the special court still has the benefit of USRA's evaluation, and the Secretary thus is not usurping USRA's planning role. Rather the Secretary becomes the mechanism by which the special court's independent evaluation of the USRA decision can be obtained. Supplementary transfers could prove to be the critical element in the ultimate fate of the bankrupt Northeast and Midwest railroads. Blocking a needed transfer could be as damaging as permitting an unwise one. I therefore urge that the Committee carefully consider whether it is prudent to permit USRA to make the unreviewable decision that a transfer will not be permitted, and urge the Committee to recommend to the Senate instead the adoption of the procedure for supplementary

In reviewing the draft Senate bill, I noted that there was no reference to the Department's proposed amendments to Title IV of the Regional Rail Reorganization Act respecting the program of operating and capital assistance to light density lines. My Department has labored diligently

to devise much-needed improvements in the Title IV process, and I would strongly urge that the Subcommittee give our proposed amendments due consideration prior to reporting out a comprehensive bill.

In my opening comments, I said that I make a clear distinction between rail freight and rail passenger service. Now let me address this second aspect of rail service - passenger service, and, in particular, passenger service in the Northeast Corridor.

First, I would like to turn to the 1971 and 1973 recommendations regarding passenger service improvements in the Northeast Corridor. The 1971 recommendation was in two parts, each interdependent with the other. They were (1) that passenger service in the Corridor be upgraded to allow trip times of 2-1/2 hours between Washington and New York and 3 hours between New York and Boston, this requiring speeds of 150 mph, and (2) that a federal expenditure of $460 million for upgrading and rolling stock would accomplish this result. The 1973 Report upped the cost estimate for the upgrading and the rolling stock to $700 million. Based upon these facts, Congress provided in the Regional Rail Reorganization Act, that the Final System Plan be effectuated in such a way as to facilitate upgrading passenger service in the Corridor to standards consonant with the 1971 Report.

If the cost estimates of either of these studies were even remotely accurate today, I would have no trouble in recommending to the Congress a program to establish 150 mph service from

Washington to Boston under certain conditions. But the actual cost is almost $4 billion, including $400 million for the rolling stock. This sum is twice the Federal share of what USRA says will be needed to rehabilitate and operate the freight lines in the Northeast and Midwest United States, a system comprised of 15,000 miles of track and the properties of seven railroads. It is a particularly staggering sum when you realize that this $4 billion would be on top of the approximately $2 billion for ConRail, and all of this to be spent in one region of the country. In addition, in order to achieve speeds of 150 mph, freight traffic must be taken off the corridor. This means acquiring the B&O line from Washington to Philadelphia and upgrading it for high density traffic, and the acquisition cost is unknown. I just don't think it is realistic to spend billions of dollars for just one passenger route in the Northeast in addition to what we will necessarily spend to rehabilitate the freight lines in the Northeast, all of which offers limited benefits to the rest of the country.

I am well aware of the Congress's often expressed interest in seeing improvements to the Northeast Corridor Rail Passenger Service move off the drawing board -- I too have been frustrated by the seemingly endless process of planning and studying. The public wants tangible,

visible improvements now. They correctly perceive that time spent arguing over the end level of a multi-year improvement program (that won't be completed until at least 1980) only delays unnecessarily the project's initiation. We can and should begin now.

Unfortunately, we cannot recommend an expenditure of $4 billion for passengers in the Northeast Corridor. The budget crunch is a reality, and there are all too many competing demands for federal funds.

The program which we are proposing for the Corridor is in our view a sound one - one that will represent a significant upgrading of the capabilities of the rail passenger system in the Corridor at the same time that it provides a sound basis for further improvements as they become necessary. Specifically, our program will, on a 90-10 cost-sharing basis with States and localities:

- Eliminate entirely the deferred maintenance which has accumulated along the Corridor since 1969, thereby establishing both a smooth ride the length of the Corridor and a sound basis for an adequate annual maintenance program;
- Rehabilitate and upgrade the numerous deteriorated bridges on the Corridor, many of which have not received proper levels of maintenance for decades;

- Provide for improvement in the signalling and control system needed to improve the safety of passenger operations;
- Improve Corridor operations by converting the obsolete electrification system to normal commercial power and replace the old electric generating equipment;
- Improve the operational aspects of stations along the Corridor;
- Plan this in a way which would be most compatible with future improvements in service levels.

Finally, I believe that implementation of this project has great potential for providing jobs for unemployed workers. The Northeast Corridor construction work should therefore be undertaken in such a way so as to maximize the benefits of giving useful employment to those currently on relief.

In summary, the Administration's program for the Northeast Corridor will expeditiously upgrade the Corridor to a level which will allow consistent trip times of 3 hours between Washington and New York and 4 hours between New York and Boston.

The Administration, I believe, correctly questions the wisdom of spending billions of dollars in order to save 30 minutes of travel time for those desiring to move between New York and Washington. Today this truly cannot be said to be the Nation's highest priority. In spite of this, however, I am just as insistent that my term in office be characterized by more than an additional pile of unimplemented studies. There are significant improvements that can and will be made along the Corridor.

I would like to make one final comment about the Northeast Corridor project. The proposed legislation is unclear regarding the role of the Department and unclear regarding the role of USRA in financing. The Department should provide and approve the plans and specifications with respect to the program, and all funding of the program should be provided through the Department. There should be an agrement negotiated between the Department and Amtrak defining roles, the construction engineering, planning, management and implementation responsibilities, financing and repayment.

I would now like to discuss the regulatory reform aspects of the Rail Services Act. If there is to be a revitalized freight rail system in this country, there must be fundamental reform of the economic regulation of the railroads. Title I of the Draft Bill of the Rail Services Act would remove the ICC's authority with respect to maximum ratemaking except in areas where there is market dominance, and this term is defined in the draft to mean the lack of effective competition. This bill also provides that where there is no market dominance, the Commission may not suspend a rate increase. We continue to believe that even where market power is shown, a no-suspend zone is still needed pending a decision on the ultimate lawfulness of rates. I think that this approach with respect to maximum rates is very useful although I continue to believe strongly that the Secretary should be involved in the process of defining "market dominance" to counterbalance the Commission's proclivity to see monopoly where there is none.

In contrast to the provision for maximum rates, I am quite disturbed with the approach taken with respect to downward flexibility and minimum rates. Under the draft bill of the Rail Services Act, the Commission may not determine that a rate is unlawful on the basis that it is too low if the rate is above the "long-term variable costs" of the transportation involved. There are at least two problems with this provision. First, the definition of "long-term variable costs"

should be clarified. I do not think that there should be a reference to "long-term". In addition, it is important that the costs of capital should be included in variable costs only to the extent that new capital will be required to maintain a service that is economically viable. It is important that no provision be made which requires railroads to earn a return from capital equipment that will not and should not be replaced. Such a requirement would aggravate the present problem of under-utilized and excess facilities and cause rates to be too high.

Second, the minimum rates provision of this draft of the Rail Services Act and the prohibition on Commission interference does not apply to cases where there is intermodal competition - exactly where you need rate flexibility. In such cases the Commission can determine that a compensatory rate -- and I emphasize the word "compensatory" -- is unlawful if it is below the rate of the competing carrier and the rail carrier is charging a higher rate for "equivalent service" -- an undefined term -- in another part of the country.

The provision in the present draft is highly anti-competitive, unfair and anti-consumer. It is anti-competitive because it creates a very serious obstacle to railroads' reducing their rates below the rate of the competing water carriers even though that railroad rate

covers variable or fully allocated costs. It is unfair because this prohibition applies only to regulated carriers, and thus will apply essentially only to the railroads and not to the competitors of the railroads who are in large part not regulated. It is anti-consumer because it means the consumers will pay more for the service than its economic worth.

We have discussed before the myths that are used to support this straight-jacket approach to minimum ratemaking. The water carriers say that if the railroads are allowed to charge lower rates than the water carriers the water carriers will be put out of business. They create an image of the big and prosperous railroads using tremendous financial strength to absorb temporary losses to under-cut the prices of the water carriers and destroy the small and weak water carrier industry. This is not true. We all know that the railroads do not have monopoly power where they face water carriers. They do not have the financial strength to absorb losses. They have difficulty attracting capital for their ordinary needs. Further, there can be no incentive for the railroads to drive water carriers out if those carriers can just turn around and re-enter the market the next day. The water carriers are prosperous, they are essentially unregulated, and they have sufficient resources to resist the railroads if that ever should be necessary. It should also be

noted that virtually every regulated water carrier is part of a large conglomerate. You are not protecting the water carriers from unfair competition with this provision; you are insolating them from fair competition. And at the same time you are denying the American consumer a lower transportation bill and a healthy railroad industry. I continue to believe that the Administration proposal prohibiting rates below variable cost, the modest limits of our non-suspend zone, and the retention of sections 2, 3 and 4 of the Interstate Commerce Act offer more than adequate protection to the water carriers.

The Nation and the consumer is also not going to benefit from the provision in Section 103 of the draft bill of the Rail Services Act which would permit the Commission to raise rates on its own initiative to cover "constant costs" -- again to benefit the water carriers -- and to "equalize" the rates to various ports. If it is cheaper to ship from one port than another then the rates should reflect that cost saving and thus make our goods more competitive in world markets. I should also note that constant or fully allocated cost pricing is inconsistent with the right to price on the basis of variable costs as endorsed elsewhere in the bill.

We talked about rate bureaus before, but I think this is a very important topic that needs to be emphasized. In the Administration

bill we provided a great deal of pricing flexibility, but to protect against the abuse of this pricing flexibility and to guarantee the users of rail services a fair break, we severely restricted the ability of the railroads to come together collusively to discuss, agree or vote on most rate matters. We did not propose to prohibit the rate bureaus from performing certain valuable administrative functions. The draft bill of the Rail Services Act would prohibit voting and formal agreements, but would allow discussions. Thus, the carriers could still discuss rates and this creates a real opportunity for tacit agreement. This draft of the bill adds to such opportunities by allowing carriers to pre-notify other carriers of proposed rate changes without any time limits or requirement that the actual rate mentioned in the notice be ultimately filed. I strongly believe that we need reform of the rate bureaus, and I also believe the Sub-committee draft does not accomplish this reform in a meaningful way.

If I might summarize the regulatory reform approach of the draft bill of the Rail Services Act: the bill provides a great deal of upward pricing flexibility, little downward pricing flexibility, and allows the railroads to continue to set rates collusively. Unfortunately, I am unable to characterize the bill in any other way and I would hope, after review, you will make the changes we indicated in the Administration Bill. The degree of regulatory reform in this bill is unacceptable. We have made it clear many times that we will only

accept federal financial assistance based on fundamental regulatory reform.

The next area I would like to discuss is mergers and consolidations. We are all aware of the critical need to restructure our railroads and the problems with restructuring proposals at the ICC. We are pleased that the draft bill includes a restructuring provision, but we strongly oppose the use of USRA. USRA is not the appropriate body to make such decisions. It is an organization established for an important but limited purpose and with a single focus. It does not have the broad, national perspective needed for such decisions. In addition, it is highly uncertain as to whether USRA will be able to retain the high level of expertise presently represented by its Board of Directors and staff once the crisis of the bankrupt railroads in the Northeast-Midwest is past. Even more importantly, I strongly object to placing such a decision-making authority in an agency that is isolated from the Administration and from the day-to-day processes which are so necessary to produce the compromise and perspective needed for effective public decision-making. The Department has, by law, the mandate to solve national transportation problems and is responsible to the people -- through the Congress -- for its actions. The whole theme of this title and many other parts of the draft bill is to take away from the Department

the whole railroad revitalization program. It also places in the hands of an agency not subject to the budget process the discretion to spend government money in huge amounts, and I totally object to such an irresponsible approach.

Title V of the Rail Services Act would establish a so-called Railroad Trust Fund which is simply a device to raid the public treasury. This fund would be under the direction of USRA. The trust would be funded at first by the sale of notes to the Treasury, and later by direct appropriations and the sale of bonds to the public. The initial funding level would be $4.0 billion for implementation of the Regional Rail Reorganization Act, which is discussed above, and $1.4 billion for other rail assistance. This $1.4 billion would be the level through December 31, 1977. After that time, Congress would determine a new level.

There would be two decision makers in this process. USRA would approve applications for "working capital and for such other financial needs as may be approved", and the Secretary would approve applications for "fixed plant" rehabilitation. The assistance would be provided via the purchase of so-called Redeemable Purchase Shares from the applicants. The shares would provide that dividends would not be paid in the first ten years and there would be a redemption feature. In essence, this financial assistance is a way to give very

low-cost, 30-year loans.

I find many of its features disturbing. First, I strongly object to the involvement of USRA in this provision. This is Federal money that is being spent, and the Executive Branch must be involved to ensure that taxpayers' interest are properly represented. This objection is so fundamental that I do not think it is necessary to dwell on the confusion that would exist in having two agencies disperse the funds for purposes which, from the language of the bill, are indistinguishable.

The second major objection goes to the type of financial assistance provided in this bill. The Administration proposed $2 billion in loan guarantees. This is in addition to the money proposed for implementation of the Regional Rail Reorganization Act and other possible assistance for the Northeast Corridor. These loan guarantees could be processed through the Federal Financing Bank, and this would result in an interest reduction of at least 2 percent below the market rate for ordinary loans.

We continue to think that our proposal for loan guarantees is an appropriate start and is very fair in light of the fact that this money will be provided to profitable railroads. The proposal in the draft bill of Rail Services Act would provide a much greater interest subsidy. Essentially, it would provide 30-year loans at an effective interest rate of about 2 percent. I must note, however,

that under the draft, all these "loans" could be forgiven and essentially turned into grants. Again, in light of the fact that this money is being provided to private and profitable firms and in view of the financial demands of other sectors of the economy, we strongly object to such a lavish and costly subsidy program.

Also, I do not think it is fair to grant federal money to a private corporation, if such corporation makes a profit and the taxpayer does not get his money returned at the appropriate interest.

I should add as a final comment with respect to the regulatory reform portion of the Rail Services Act that the bill makes many changes in ICC structure and procedures on which I have not commented. There is not time for any detailed comments on all these provisions, but we will send a letter to you with more detailed comments.

Let me finally say a few words about the proposal advanced by the New England Regional Commission and introduced by Senator Kennedy for public ownership of railroad rights of way. As you know, such a "Consolidated Facilities Corporation" or "Confac" plan was given thorough consideration during the USRA planning process. It was rejected by the USRA Board because of its excessive cost to the taxpayer and the unreasonable and irreversible government intrusion it would entail in the affairs of the private sector. The New England plan, while somewhat different from Confac in approach,

carries the same deficiencies.

The thrust of the New England plan is to resolve the disparity in Federal investment in the various modes of surface transportation by providing an equivalent capital subsidy for the railroads. In exchange for the deed to railroad property, the Federal Government would grant a railroad operating company an exclusive 25-year lease of the property. I strongly oppose such a proposal. Such a proposal would begin a process of governmental interference in the railroads which would result in the complete nationalization of the industry. It would politicize the rehabilitation and restructuring process, and result in great waste and inefficiency. Our national interest requires that the rail system be rehabilitated, but rehabilitated in the private sector. For that reason, I most vigorously oppose the public ownership of rail rights of way under any scheme.

In addition, the cost of this proposal to the taxpayers is enormous. Property deeded under this bill to the Government would be rehabilitated in full at the expense of the taxpayer and would receive a Government contribution to its annual normalized maintenance program in the form of the purchase of all materials needed for such annual maintenance. If all railroads participated, the cost to the taxpayer for this program -- in constant dollars -- is estimated at $2 billion per year for the first ten years or $20 billion and

$1 billion per year thereafter. User fees charges to the companies would only recover in the range of $400-500 million annually. I assume that the federal government would have to reimburse the states and local governmental units for the local real estate taxes lost once the private railroad profit is transferred to the federal government and thus be no longer taxable by the state.

The proposed plan would result in a very substantial direct enrichment of private shareholders. My staff estimates that the overall effect of the maintenance grants that would be provided to ConRail under this proposal would raise the value of ConRail's common stock by at least $5 billion and potentially much more, given the remarkable growth in earnings that ConRail would demonstrate. In our view, such a program would represent an unjust and unjustifiable enrichment of ConRail's shareholders at direct taxpayer expense.

The New England plan has other marked deficiencies. It would tend to freeze the existing rail system essentially as it exists today, neglecting significant opportunities for rationalization of excess plant and the improved financial and operating efficiencies which should flow from that process. It would confer a public subsidy on what would be an asset exclusively in the hands of a private company through a lease, even though nominally owned by the public.

It would elevate to highest priority the task of rehabilitating every single mile of railroad track in the United States at great public expense when there are in many cases other investment in rail properties which would provide a higher financial return to the railroads and a higher return in service to the public which the railroads serve. And it would eliminate at a stroke the rationale for the difficult but necessary task of improving the financial performance of our rail system through the reform of outmoded and unfair economic regulatory policies which penalize the railroads and reward their competitors. I also assume that the private railroads involved would demand an absolute right to renew the leases after 25 years and perhaps at even a more unfavorable rental vis-a-vis the federal government.

Mr. Chairman and members of the Subcommittee, there is a great distance between our two positions, and I hope today we can begin to reconcile them and start on the road to railroad revitalization.

This concludes my written comments, and I would be happy to answer any of your questions.