STATEMENT OF
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Chairman Hutchison and Members of the Subcommittee, I appreciate this opportunity to appear before you today to discuss rail finance, focusing on equipment and infrastructure investments for intercity passenger rail service. I will be brief.

In order to discuss rail finance, the Administration has focused on two questions that first must be answered: what intercity rail passenger service should America have and who decides this type of service? The answers to these questions strongly affect the answer to the question of how to finance intercity passenger rail service in this country.

The present Amtrak route system has changed little over Amtrak's thirty years of existence, seemingly locked in place by history and politics. That is starkly anomalous in America's transportation system. What other transportation company or mode of travel has changed its routes and service so little in the last thirty years? Most transportation providers have changed their systems dramatically over that time span in response to changes in travel patterns driven by economics and demographics. If Amtrak's system were not so ossified, perhaps Amtrak would serve more passengers today than it did thirty years ago. It appears that moving decision-making on routes and service closer to the customers would be a very good thing.

This observation appears to be borne out wherever States have taken a strong role in determining what routes will be operated to serve their citizens, what kind of equipment should be used, what kind of service should be provided, and on what schedule. The states of California, North Carolina, and Washington are all excellent examples of states stepping up to the plate and meeting this challenge, paying for what they want above and beyond what Amtrak would otherwise provide, and getting noticeably better rail service for their citizens as a result. Citizens have responded to those investments: three California state-supported routes have attracted 2.35 million riders in the first seven months of this fiscal year, almost 44% of the total ridership for the same period on the Northeast Corridor Acela, Metroliner and Regional services.

The Administration proposes to build on the examples set by these states to reform and strengthen the Federal role in passenger rail to mirror much more closely the current Federal program supporting mass transit. The Federal government would continue to define rail safety standards and enforce them. The Department of Transportation would provide capital grants directly to states and interstate consortia of states that want

passenger rail. State government agencies would determine the level of passenger services needed and the price for such service, and contract with third-party operators to provide long-distance and corridor trains. The same program would apply to legacy long distance routes, current and new corridor services -- at higher speeds or not. To the extent that states' service choices require operating subsidies, state governments would be required to provide that subsidy.

It is possible that in the early part of the authorization cycle, the Federal Government would provide limited subsidies for corridor and long distance trains, and fund the capital backlog for certain passenger rail projects. By the end of the authorization cycle, however, state governments would be responsible for at least 50 percent of needed capital investment for all intercity passenger rail service– similar to Federal capital investments in the Federal Transit Administration's "New Starts" program. Similarly, by the end of the authorization period all rail operational costs will be borne by riders or States or State rail consortiums.

We believe this an appropriate division of State and Federal transportation responsibilities. It reflects the way the Federal government handles other transportation programs. After an appropriate transition period, only services States are willing to pay for would be continued.

Like other Federal programs that invest in transportation, intercity passenger rail service would require careful thought and planning up front before either the states or the Federal government make significant investments. Intercity passenger rail service should be part of state transportation plans already required by Federal surface transportation legislation. Careful passenger rail planning should go a long way toward overcoming the long-term problem that our modes of intercity passenger transportation, which were conceived independently for the most part, do not interrelate well. States, however, have a powerful interest in enabling their citizens to navigate our transportation system seamlessly. The states that do so stand to reap considerable economic advantages, such as being more attractive as a location for businesses. A sound planning process should also help make sure that intercity passenger rail service goes where people want to travel, when they want to go, and at an appropriate price.

This may result, for example, in a lot more attention being paid to some of the submarkets along long distance routes, instead of the points of origin and of final destination for these routes. As I understand it, on many long-distance routes few passengers travel the entire length of the route. Instead, most passengers start and stop at intermediate points along the way. It would make sense for a state or two neighboring states having a submarket that attracts a lot of passengers to want more service on that part of the longer route and to invest accordingly. North Carolina is doing that between Charlotte and Raleigh. Oregon and Washington are doing that between Eugene, Portland, Seattle and Vancouver, British Columbia. Those states are reaping significant benefits from doing that and we should help them.

In many places, states may decide that it is more important to have fast, frequent, timely, and reliable service in relatively short corridors that have a lot of business travel. In such corridors, rail can compete effectively with air and highway for business travelers. The Northeast Corridor, where Amtrak is the dominant carrier, is the best illustration of that prospect. Especially where airports and highways are already overcrowded and land is so scarce that it will be hard to build more airports or highways, it is especially important to make full use of existing rail capacity. Since states will be making the key decisions about whether to build additional airports or highways, it makes sense to have them make key decisions about passenger rail service and if it should be expanded, reduced, or eliminated altogether. Then the states can comprehensively plan the best ways to get their citizens from one place to another without needless constraints on modal choice.

Another part of effective planning for transportation systems is compliance with environmental laws. Before major Federal funding decisions can be made, without regard to the type of funding used, assessments of environmental impacts must be completed, environmental impact statements or findings of no significant impact prepared, and all necessary permits obtained. State governments are very familiar with these processes and have learned to negotiate them successfully. They can be expected to handle compliance with the environmental laws as quickly and efficiently as it can be done. California, North Carolina and Virginia, and Florida are doing that very effectively right now for the additional rail service they are seeking with higher speed rail projects.

Thorough planning also involves thorough discussions and negotiations with the freight railroads which own the rights-of-way and tracks over which most of the Nation's current and future passenger rail services operate outside the Northeast Corridor. Passenger rail services pose significant operational challenges for freight railroads, and expansions of current services or new service on intercity corridors should not impair the current capacity for carrying freight, lest such investments will lead to increased congestion of our highways by more trucks. Better yet, states considering passenger rail investments should make capacity improvements that benefit both passenger and freight users to maximize the congestion relief afforded by the projects. Policymakers may need to decide whether the current pricing mechanisms of passenger rail access at incremental costs will lead to the most efficient use of public and private infrastructure assets.

Of course, it is also important to provide funding for intercity passenger rail service in a way that best assures that the taxpayers get their money's worth. The standard grant agreement relationship used by the Federal government to provide most financial assistance affords reasonable controls on and accountability by recipients. Properly used, grant agreements make clear what the public will get, when the public will get it, and what it will cost. Reasonable and workable financial controls are used. All aspects of the program are "in the sunshine" and audited. This is a prudent means of seeing that Federal funds are well spent and produce the benefits intended by the Administration and Congress. This kind of thorough financial planning is also mirrored in proposals in the Administration's surface transportation reauthorization ("SAFETEA," mentioned below), in which states are required to develop financial plans for Title 23 projects over $100 million.

This Administration has a strong record of support for innovative financing for surface transportation projects, as the recently introduced Safe, Accountable, Flexible, and Efficient Transportation Equity Act ("SAFETEA") reauthorization proposal demonstrates. The Transportation Infrastructure Finance and Innovation Act (TIFIA) established a Federal credit assistance program that is already available for intercity rail projects. SAFETEA proposes to expand the use of TIFIA credit assistance by broadening eligibilities to include private freight rail facilities and reducing the project size threshold for TIFIA projects to $50 million from $100 million. States would be allowed to impose user charges on federal-aid highways, including the Interstate System, provided that such charges were part of a program to relieve congestion and/or improve air quality. Transportation projects (highway facilities and surface freight transfer facilities) will be eligible for tax-exempt private activity bonds, exempted from a state's private activity ceilings, encouraging private operation of transportation projects. States will be given more freedom to use innovative project delivery methods such as design/build, which are often a key in setting fixed prices for projects to attract private investment.

One of the common threads in most innovative financing mechanisms for surface modes—state revenue bonds, toll roads, TIFIA, Grant Anticipation Revenue Vehicles—is that most of these financial instruments require repayment. Debt instruments used for transit and road construction either pledge dedicated tax revenues, dependable funding streams from Federal or state programs, or reasonably expected revenues from transportation facility users.

Various kinds of debt instruments are proposed from time to time to fund intercity passenger rail service. The Administration does not think dedicated debt instruments are suitable for this purpose. Unlike most other transportation debt financing mentioned above, intercity passenger rail does not generate adequate cash flows to service significant additional debt, nor is it supported by reasonably anticipated, long-term dedicated funding streams from the Federal government. We believe that there may be corridors in which passenger rail services can cover costs of operations and maintenance, but few corridors will generate revenues sufficient to provide adequate coverage beyond operating and maintenance expenses to repay interest and principal of debt raised for project capital costs.

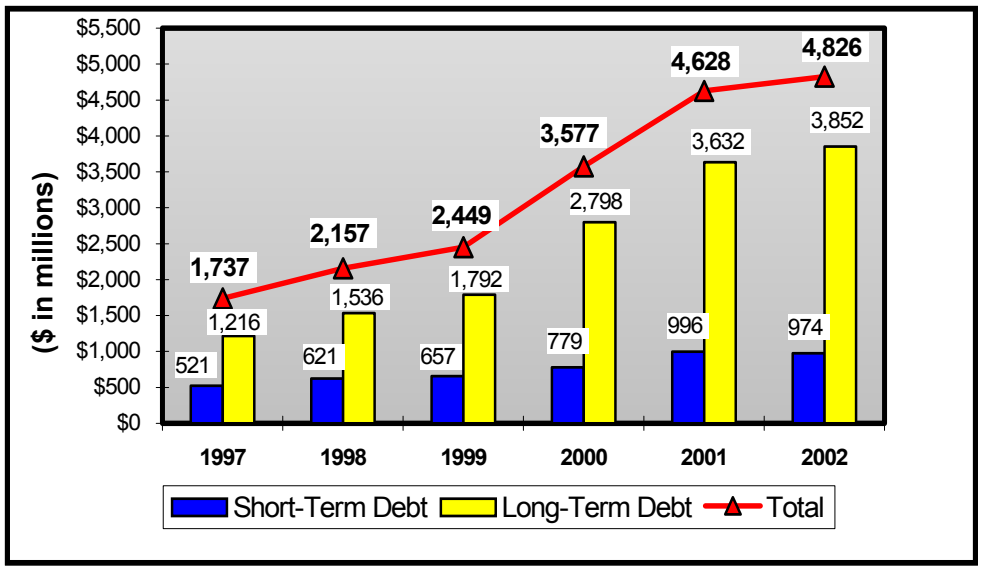
Let me also speak in general terms about tax credit bond financing, even though such matters are not our agency's primary responsibility (and such matters are considered by tax-writing committees in the Congress). As an example of the concept, you may wish to learn more about Qualified Zone Academy Bonds http://www.ed.gov/offices/OESE/SST/qzab.html), a program that offers limited amounts of tax credit bonds for equipment and rehabilitation of schools in empowerment zones and enterprise communities or schools serving a student population of which at least 35 percent are eligible for free or reduced-cost lunches. These are the only form of tax credit bond currently allowed. This program, by limiting the total term of the bonds, currently to fifteen years, roughly splits the cost of a qualifying project in half. The federal government pays the interest (through tax credits) and the local school district

repays the principal. (As you can see, this equal sharing of financial exposure is similar to the kind of financial participation we contemplate in a federal/state capital partnership for intercity passenger rail). The total size of the Qualified Zone Academy Bond program is limited to $400 million per year in new issues, and only certain qualified buyers can purchase these bonds (lending institutions such as banks and insurance companies). These provisions limit the administrative complications and costs to the Treasury of these financial instruments.

If larger amounts of tax credit bonds are issued, the permitted holders of these bonds would likely have to be expanded to include, for example, individuals and mutual funds, thus making them much more complex and increasing the administrative burdens placed on the Internal Revenue Service. If longer terms of maturity are considered for intercity passenger rail purposes, then the overall exposure of the Treasury is increased relative to any matching funds from passenger revenues or state participation. If the tax credit debt is issued in an amount that not only covers capital costs but is also used to create sinking funds from which principal is eventually repaid as interest accrues in the sinking fund then the Treasury is effectively footing the entire bill for the capital costs. Further, because there is very little liquidity in the market for these bonds the market would impose a significant premium, thereby reducing the amount of actual funding and raising the effective costs to the taxpayers of using this funding mechanism compared to more traditional means. For these reasons, the Administration would oppose such a financing mechanism for intercity passenger rail.

Before Congress considers more debt for intercity passenger rail, Congress should consider the difficulty Amtrak is having with the enormous debt it has already incurred. Amtrak's total debt grew from $1.7 billion in 1997 to $4.8 billion in 2002. Figure 1 illustrates the growth in Amtrak's total debt.

Figure 1
Amtrak Short-Term and Long-Term Debt
(Source: U.S. DOT Inspector General)



Because of this increased debt, naturally Amtrak's annual debt service has grown substantially, adding a large up-front cost to its business plan. Annual debt service requirements (principal and interest) are forecasted to be $278 million in FY 2004 (up from $111 million in 1997). This means that debt service will consume over 15 percent of Amtrak's requested FY 2004 appropriation of $1.8 billion. Amtrak's accumulated debt is a significant burden weighing down future passenger rail development. The FRA is not surprised by this massive debt and calls for its accelerated retirement. In 1983, Amtrak was unable to pay the debt service on $880 million in loans guaranteed by the Government under section 602 of the Rail Passenger Service Act. FRA paid $1.119 billion to honor its guarantee of principal and interest on Amtrak's debt, and in return the Federal government was given a lien on Amtrak's assets and given $1.119 billion of preferred plus to one share of preferred stock for each dollar of future financial assistance given to Amtrak. That preferred stock has a par value of $10 billion. So you can see that our past experiences with passenger rail debt, necessarily colors our current view that future financing for passenger rail depends on shaky promises of project revenues or future funding dependability.

That is not to say that we are opposed to the involvement of the private sector in passenger rail development, either in service delivery or financial participation. Indeed, earlier testimony before this committee demonstrated our confidence in the ability of the private sector to become involved in a number of ways in providing passenger rail services to state governments. We are convinced that the private sector may be interested in pursuing commercial applications along the Northeast Corridor, and such commercial uses may provide income streams for future corridor capital projects. Yet, we have listened to many commuter rail agencies and freight railroads that use the Northeast Corridor and the states that support such operations, and they have cautioned us against private ownership and control of the Corridor. We are taking these comments and concerns under consideration as we continue drafting reauthorization legislation for the national passenger rail system.

Thank you again for the opportunity to appear before this committee. I will be happy to answer any questions you may have.