**U.S. Department of Transportation**
Office of the Secretary of Transportation

The Inspector General

Office of Inspector General
Washington, DC 20590

May 17, 2010

The Honorable Patty Murray
Chairman
Subcommittee on Transportation, Housing and Urban Development, and Related Agencies
Committee on Appropriations
United States Senate
Washington, DC 20510

The Honorable John W. Olver
Chairman
Subcommittee on Transportation, Housing and Urban Development, and Related Agencies
Committee on Appropriations
United States House of Representatives
Washington, DC 20515

The Honorable Christopher "Kit" Bond
Ranking Member
Subcommittee on Transportation, Housing and Urban Development, and Related Agencies
Committee on Appropriations
United States Senate
Washington, DC 20510

The Honorable Tom Latham
Ranking Member
Subcommittee on Transportation, Housing and Urban Development, and Related Agencies
Committee on Appropriations
United States House of Representatives
Washington, DC 20515

Dear Chairmen Murray and Olver and Ranking Members Bond and Latham:

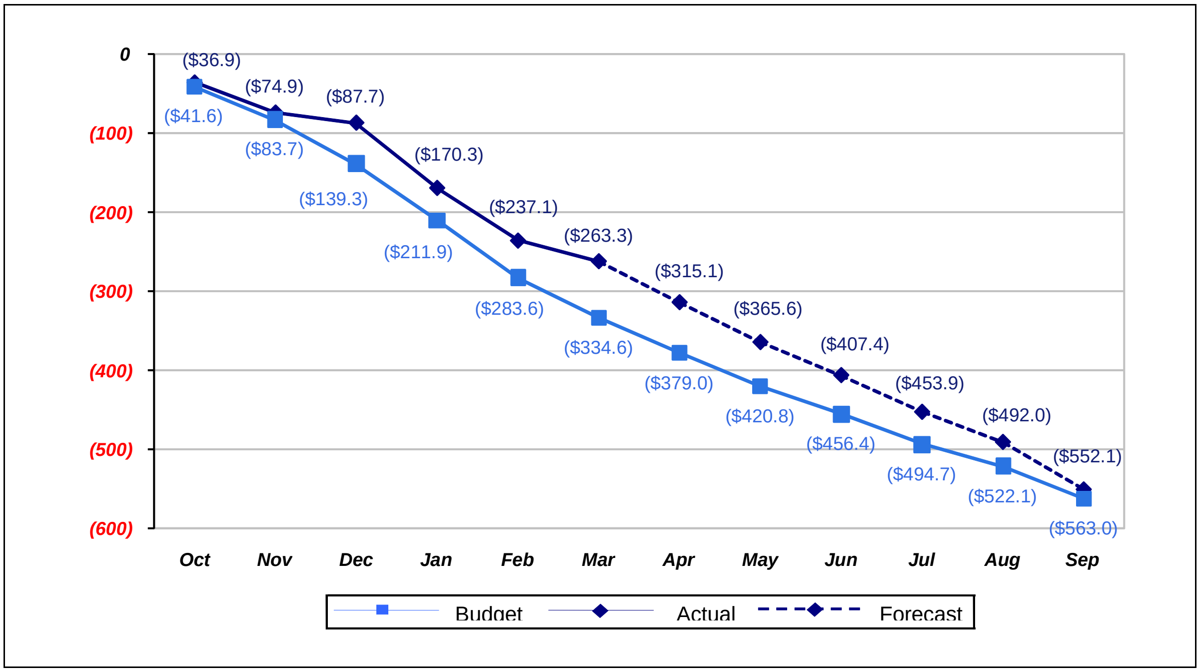
This report presents our assessment of Amtrak's financial performance for the first half of fiscal year 2010 (year-to-date) and Amtrak's forecasted end-of-year fiscal year 2010 financial performance.[1] The report also includes an update on Amtrak's use of its recently implemented Key Performance Indicators (KPI) to gauge company performance and the success of its reform initiatives.

[1] The Transportation/HUD Division of the Consolidated Appropriations Act of 2010, Pub.L. No. 111-117 changed OIG's reporting requirement on Amtrak's savings from quarterly to semiannually.

## SUMMARY

In the first 6 months of fiscal year 2010, Amtrak's operating loss of $263.3 million was $71.4 million, or 21.3 percent, better than budgeted (see figure 1).[2] However, this is $12.2 million more than its operating loss for the first 6 months of fiscal year 2009. The lower than budgeted operating loss was due to a combination of higher than expected revenues and lower than expected expenses. Much of the savings achieved in the first half of the year is expected to erode in the second half as Amtrak forecasts a year-end operating loss of $552.1 million, just $10.9 million or 1.9 percent better than budget, but $94.2 million more than fiscal year 2009. While Amtrak no longer focuses on measuring savings from reform initiatives, its new focus on KPIs appears to be an efficient approach for management to monitor operating and financial performance to budget.

***Figure 1. Amtrak Actual vs. Budget Fiscal Year 2010 Operating Loss (Dollars in Millions)***




Source: OIG analysis of Amtrak data

2 Operating loss is reported on an earnings before interest, taxes, depreciation, and other post-employment benefits (EBITDO) basis, unless otherwise noted. EBITDO operating loss is a measure of Amtrak's ability to operate within its available resources and serves as a reasonable proxy for Amtrak's Federal operating support requirements.

## AMTRAK'S FISCAL YEAR 2010 OPERATING LOSS THROUGH MARCH WAS BETTER THAN BUDGETED

Amtrak's operating loss for the first 6 months of fiscal year 2010 was better than budget by $71.4 million. This was due to a combination of higher than expected revenues and lower than expected expenses. Table 1 details Amtrak's year-to-date and forecasted year-end financial performance. While the Operating Loss is significantly better than budget for the first 6 months of fiscal year 2010, it is $12.2 million worse than the company's net loss for the same period in fiscal year 2009. Year-to-date ridership has increased from last year's levels and is higher than budgeted, driven primarily by higher gasoline prices (which causes travelers to seek transportation alternatives to driving), improved on-time performance, and an improved economy. Lower expenses were driven primarily by lower benefit expenses and a successful hedge against fuel prices. These factors are discussed in more detail below.

***Table 1: Amtrak's Fiscal Year 2010 Financial Performance through March (Dollars in Millions)***

| | Fiscal Year 2010 | | Fiscal Year 2009 | Variance Favorable/(Unfavorable) | |
|---|---|---|---|---|---|
| | Actual | Budget | Actual | Budget | Fiscal Year 2009 |
| **Total Operating Revenues** | **$1,187.5** | **$1,147.6** | **$1,156.5** | **$39.9** | **$31.0** |
| **Total Operating Expenses** | **$1,450.8** | **$1,482.2** | **$1,407.6** | **$31.4** | **($43.2)** |
| **Operating Profit / (Loss)** | **($263.3)** | **($334.6)** | **($251.1)** | **$71.4** | **($12.2)** |

Source: OIG analysis of Amtrak data

Amtrak is projecting a significant deterioration in its second-half operating results. Specifically, Amtrak projects an unfavorable variance to its second half of fiscal year 2010 budgeted operating loss of $60.4 million. This is primarily due to an expected significant increase in wages and employee benefits compared to budget. For the year-end, Amtrak forecasts an operating loss of $552.1 million, only $10.9 million better than budget and $94.2 million more than last year's actual operating loss. The difference in operating loss over fiscal year 2009 is due to an increase of $88 million in the fiscal year 2010 Federal operating subsidy for an expected increase in wages with no associated ridership growth. Operating revenue is forecast to be $52.9 million more than budget and $124.6 million more than fiscal year 2009. Increased revenues, however, are forecast to be more than offset by operating expenses. Amtrak projects operating expenses to be $42.0 million more than budget and $218.8 million more than fiscal year 2009. Table 2 details Amtrak's forecasted year-end financial performance.

***Table 2: Amtrak's Fiscal Year 2010 Forecasted Year-End Financial Performance (Dollars in Millions)***

| | Fiscal Year 2010 | | Fiscal Year 2009 | Variance Favorable/(Unfavorable) | |
|---|---|---|---|---|---|
| | Actual | Budget | Actual | Budget | Fiscal Year 2009 |
| **Total Operating Revenues** | **$2,450.2** | **$2,397.3** | **$2,325.6** | **$52.9** | **$124.6** |
| **Total Operating Expenses** | **$3,002.3** | **$2,960.3** | **$2,783.5** | **($42.0)** | **($218.8)** |
| **Operating Profit / (Loss)** | **($552.1)** | **($563.0)** | **($457.8)** | **$10.9** | **($94.2)** |

Source: OIG analysis of Amtrak data

### *Operating Revenues*

Revenues for the first half of fiscal year 2010 totaled $1.2 billion, $39.9 million better than budget and $31 million better than the same period in fiscal year 2009. Total passenger related revenues alone totaled $937.2 million, $35.6 million (3.9 percent) better than budget and $38.6 million (4.3 percent) better than the first half of fiscal year 2009. Non-passenger related revenue was also higher than budget, primarily due to a $2.5 million settlement with a railroad tie manufacturer as well as a one-time revenue recognition related to an advertising contract.

Ticket revenue performance was driven by higher than expected ridership (see table 3). Amtrak's total ridership was 5.4 percent over budget, due to higher than expected ridership along all of its major business lines (NEC spine 7.8 percent, short distance corridors 3.8 percent, and long distance routes 4.6 percent). Within the NEC, Northeast Regional ridership was 8.8 percent better than budget, primarily due to higher gasoline prices, especially in the corridor north of New York. In addition, *Acela* ridership was 5.7 percent better than budget. Short-distance service also benefited from higher gasoline prices as well as from improved on-time performance for most routes.

Year-end forecasted operating revenues total $2.5 billion, $52.9 million better than budget and $124.6 million more than fiscal year 2009. Net ticket revenues are forecasted to be $1.7 billion at year-end, $43.7 million more than budget and $99.3 million more than fiscal year 2009.

***Table 3. Amtrak Ridership and Passenger Ticket Revenues, Actual vs. Budget – Fiscal Year 2010 through March***

| | Ridership (in millions) | | | Ticket Revenue ($ in millions) | | |
|---|---|---|---|---|---|---|
| | Actual | Budget | % Diff. | Actual | Budget | % Diff. |
| NEC:† | 5.1 | 4.7 | 7.8% | $436.6 | $415.3 | 5.1% |
| • *Acela* | *1.6* | *1.5* | *5.7%* | *$213.2* | *$205.8* | *3.6%* |
| • *Northeast Regional* | *3.5* | *3.2* | *8.8%* | *$222.9* | *$208.9* | *6.7%* |
| State-Supported and Other Corridors | 6.5 | 6.2 | 3.8% | $180.3 | $170.2 | 6.0% |
| Long Distance | 2.1 | 2.0 | 4.6% | $195.4 | $193.5 | 1.0% |
| **Amtrak Total** | **13.6** | **12.9** | **5.4%** | **$812.3** | **$779.0** | **4.3%** |

Source: Amtrak
†: Total includes NEC special trains, not shown.

## *Operating Expenses*

Operating expenses for the first 6 months of fiscal year 2010 were $1.5 billion, $31.4 million better than budget and $43.2 million worse than the same period in fiscal year 2009. Lower than expected expenses were primarily due to Employee Benefits and Fuel and Power and Utilities, which were $20 million and $8.9 million better than budget, respectively. Fuel cost savings were driven primarily by a diesel fuel hedge strategy for about half of the diesel fuel consumption, which consisted of contracts acting as an insurance policy against spikes in diesel fuel costs with flexibility to be opportunistic should prices drop. At the same time, these savings were offset by higher than expected expenses in train operations for schedule adherence payments due to higher on-time performance ($9.4 million), as well as an overage in Casualty and Other Claims total ($6.9 million) due to a one-time adjustment to the liability accounts for insurance claims.

Forecasted year-end expenses are $3 billion, $42.0 million more than budget and $218.8 million more than fiscal year 2009 total expenses, a $73.5 million decline from results through March. Higher than expected expenses forecasted for the year-end are primarily due to employee benefits, which are forecast to be $11.7 million more than budget, representing a reversal of $31.7 million over results through March; train operations, which are forecast to be $15.8 million more than budget, a continued decline of $7.6 million after March; and materials costs forecast to be $14.2 million more than budget, an additional decline of $5.0 million due to an accounting reclassification of in-house overhaul component work. With regards to the fuel line, Amtrak is expecting significantly higher than budgeted train fuel costs, while increased benefit plan usage is projected due to anticipated hiring and deferred usage from the first half for employee benefits.

## KEY PERFORMANCE INDICATORS APPEAR TO BE AN EFFICIENT WAY TO EVALUATE OPERATING PERFORMANCE TO BUDGET

Since fiscal year 2006, we have reported on savings Amtrak has achieved through operational strategic reform initiatives (SRI) at the corporate level, by business line, and at the route level. The SRIs were intended to improve Amtrak's operating efficiencies and lower its dependence on Federal operating subsidies. However, according to Amtrak officials, management was focusing too much attention on measuring the incremental impact of a given initiative or project on savings and not placing enough focus on total results. Given the variety of factors impacting the company’s operating performance, officials stated that the practice of determining the incremental impact of any given initiative on the bottom line is inefficient and time-consuming. For example, if Amtrak’s marketing department invests additional funds to promote *Acela* and revenues increase for that route, there is no clear way to determine if or what portion of the increase is due to higher gasoline prices, deteriorating airline service, or the marketing campaign. As a result, Amtrak shifted from using SRIs to establishing KPIs—criteria intended to measure both the efficiency and effectiveness of Amtrak's operational and financial performance.

While Amtrak established nine KPIs to measure efficiency and effectiveness, we are tracking three of the efficiency measures. Amtrak's cost recovery ratio measures the proportion of Amtrak expenses covered by revenues. Amtrak also established revenue per available seat mile (RASM) and cost per available seat mile (CASM) KPIs.[3] Amtrak has exceeded its cost recovery ratio, RASM, and CASM targets, which is consistent with our review of results for Amtrak's operating loss, revenue, and expenses year-to-date (see table 4).

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[3] The cost recovery ratio, RASM, and CASM formulas are derived using core revenues and expenses, and available seat miles.

***Table 4: Amtrak Key Performance Indicators, Fiscal Year 2010 through March***

| Key Performance Indicator | Actual | Budget | Variance to Budget Amount | Variance to Budget Percent | 2009 | Variance to 2009 Amount | Variance to 2009 Percent |
|---|---|---|---|---|---|---|---|
| **RASM - Core Revenue per Seat Mile** | **$0.157** | **$0.153** | **$0.005** | **3.0%** | **$0.152** | **$0.005** | **3.6%** |
| **CASM - Core Expenses per Seat Mile** | **$0.217** | **$0.221** | **$0.005** | **2.1%** | **$0.210** | **-$0.007** | **-3.3%** |
| **Cost Recovery Ratio** | **72.7%** | **69.1%** | **3.6%** | **5.2%** | **72.5%** | **0.2%** | **0.3%** |

Source: Amtrak

We analyzed other operating statistics to better understand the success that Amtrak has had in exceeding its targets. Year-to-date, Amtrak has operated 2.9 billion passenger miles, 155 million more than budgeted, while offering 6 billion seat miles, 54.7 million more than budgeted. Further, the load factor—the ratio of passenger miles to seat miles—for the first half of fiscal year 2010 was 48.6 percent, 2.2 percent more than both budget and the previous fiscal year.

According to Amtrak officials, KPIs provide a more streamlined way of evaluating performance to budget because they are derived from the annual budget and Amtrak operates to its budget targets. Amtrak officials also noted that because KPIs are linked to monthly financial statements, KPIs are tracked and updated much more frequently, allowing management to react quicker to changes in operating and financial conditions. The updates should also allow management to drill down into KPI detail in real time to determine what is driving any changes, and consequently react quicker, rather than waiting until the next month for the next round of financial statements. According to Amtrak's strategic guidance, KPIs will be used to evaluate management and to ensure that leadership's attention and effort are properly focused.

While Amtrak has abandoned the concept of SRIs, it continues to develop initiatives to improve operating performance and provide additional revenue. In its Fiscal Year 2010 Comprehensive Business Plan, Amtrak outlined six initiatives aimed at producing an additional $31.6 million in revenues, with associated costs of $14.8 million (see table 5).

***Table 5: Amtrak Fiscal Year 2010 Improvement Initiatives***

| Improvement Initiative | Impact on Revenues | Impact on Expenses |
|---|---|---|
| Increase in advertising spending to increase market share ridership | $13.2 | $7.7 |
| New state supported routes in Virginia | $8.7 | $7.1 |
| Launch of enhanced next generation e-ticketing channel | $5.7 | |
| Partnership with Rail Europe for reservations by European travelers | $1.7 | |
| Additional Cascades and Piedmont trains | $2.7 | |
| Reduction in frequency of special trains | ($0.9) | |
| Launch of Wi-Fi on *Acela* trains | $0.5 | |
| **Total Fiscal Year 2010** | **$31.6** | **$14.8** |

Source: Amtrak

In addition to providing a more efficient way of evaluating performance to budget, Amtrak officials stated that the KPIs provide for a more streamlined way to evaluate the impact of improvement initiatives. Because KPIs are derived from the budget plan and the plan is based on a number of factors that are intended to improve efficiencies, management should be able to determine whether or not improvement initiatives are effective. For example, the cost recovery ratio is considered a target that reflects the goal of reducing reliance on Federal operating support by virtue of increasing Amtrak's cost recovery ratio. If this ratio shows an increase over budget, management can assume that initiatives aimed at increasing revenue are effective. Therefore, the plan and its many assumptions are what drive the KPIs—RASM, CASM, and cost recovery ratio.

Using KPIs appear to be a more efficient way for management to monitor operating performance. However, because the KPIs have only been in place for six months, the ultimate success of this new approach has yet to be determined. As we stated in our fiscal year 2009 fourth quarter report, in addition to reporting on Amtrak's financial performance, we will continue to track and evaluate Amtrak's efficiency related KPIs.

Under separate cover, we are transmitting copies of this letter to the Secretary of Transportation and the Chairman of Amtrak's Board of Directors. If you have any questions concerning this letter, please contact me at (202) 366-1959 or Mitch Behm, Assistant Inspector General for Amtrak, High Speed Rail, and Economic Analysis at (202) 366-9682.

Sincerely,

Calvin L. Scovel III

Calvin L. Scovel III
Inspector General

cc: Secretary of Transportation
Chairman of Amtrak's Board of Directors