WHITE PAPER

Should Amtrak Services and Infrastructure be "Privatized"?

SHOULD AMTRAK SERVICES AND INFRASTRUCTURE BE "PRIVATIZED"?

"[E]fforts to foster competition have not resulted in improvements to intercity passenger rail."[1]
- Congressional Research Service (2019)

From time to time, proposals have been made to "privatize" some or all of the activities and services required for operation of Amtrak trains or Amtrak's Northeast Corridor (NEC) rail infrastructure. Proponents have suggested this would produce better service at a lower cost, attract private investment, and reduce or eliminate the need for public funding. The issues associated with Amtrak privatization, and experience with intercity passenger rail privatization in the United States and other countries, are discussed below.

Why has privatization been proposed?

It is not clear what problem Amtrak privatization proposals are intended to solve. Most of them originated two decades ago, when Amtrak was in decline and facing a seemingly insurmountable financial crisis. They are modeled on the mid-1990s privatization of rail infrastructure and train operations in Great Britain and several other countries, which some initially viewed as a success.[2]

The situation is very different today. British rail privatization is almost universally regarded as a failure, as discussed below, while Amtrak has experienced sustained improvement.

Despite limited funding, Amtrak's ridership is growing and its annual revenues are at an all-time high. Amtrak recovers 95% of its operating costs from revenues, and is on track to eliminate its operating loss entirely by 2021. Amtrak is already operated as a for-profit company, as required by federal law. It has business-focused leadership with experience in successfully operating for-profit companies in the transportation and other industries.

Amtrak is beginning to attract the public and private investment it needs to advance vital capital projects, including the Gateway Program to improve, replace and double the capacity of the nation's most vital rail infrastructure between New Jersey and New York; new high-speed trainsets for its premium *Acela Express* service; and the new Moynihan Train Hall in New York City and station redevelopment in Chicago, Philadelphia and Baltimore.

How has privatization worked in other countries?

In 1994, Britain did what proponents of Amtrak privatization advocate: it conveyed its rail infrastructure to a newly-formed private entity and franchised its train operations to for-profit companies. Twenty-five years later, Britain's privatization experiment has produced a series of fatal train wrecks and national rail crises, renationalization of infrastructure, and a recent declaration by the head of a government review panel that the current system of franchising train operations "cannot continue."[3]

- Britain renationalized its rail infrastructure in 2002 after its private infrastructure owner, Railtrack, became insolvent and 42 people died in three fatal accidents attributed to its negligence and

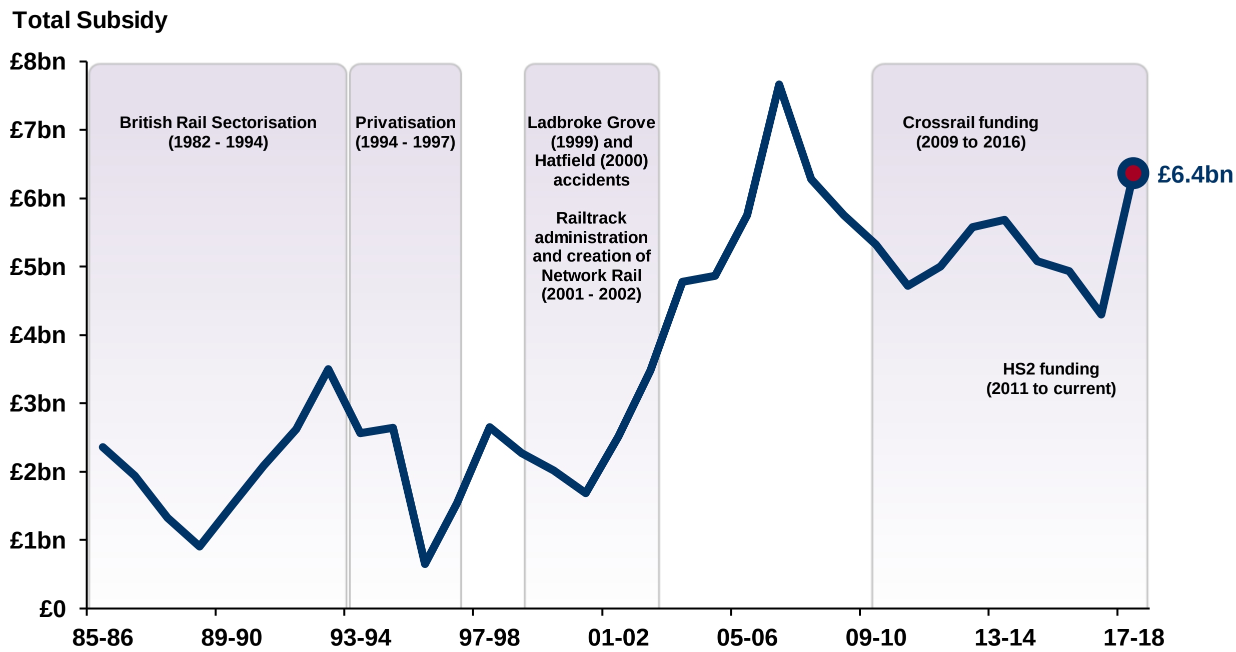
[1] Congressional Research Service, *Improving Intercity Passenger Rail Service in the United States,* June 25, 2019 (https://fas.org/sgp/crs/misc/R45783.pdf)(CRS 2019 Report), p. 19.
[2] See Vranich, Joseph, *Derailed: What Went Wrong and What To Do About America's Passenger Trains* (St. Martin's Press – 1997), which cited the privatization of passenger rail services in Great Britain, New Zealand and Argentina as models for the partial privatization of Amtrak.
[3] BBC News, "Rail franchise model cannot continue, says review chief," Feb. 26, 2019 (https://www.bbc.com/news/business-47378448).

contracting out of infrastructure maintenance.[4]

- While franchising of Britain's train operations has produced profits for some private franchisees, others who submitted low bids to secure contracts have later walked away from their obligations, necessitating government takeovers. Fares have risen while service has deteriorated. On-time performance is at a 13-year low, and trains are frequently cancelled because franchisees do not have enough employees to operate them.[5]

- Instead of declining, government subsidies for rail have increased significantly since the 1994 privatization, even with adjustment for inflation, as shown in the table below.

Government Subsidies for Rail in Great Britain[6]



Other countries that privatized their rail service during the mid-1990s have been compelled to return it to public stewardship due to private operators' safety, financial and infrastructure maintenance deficiencies. Argentina began renationalization in 2012 following an accident that killed 51 passengers and private investors' failure to fulfill contractual obligations.[7] New Zealand had to renationalize its privatized rail infrastructure and operations in 2004 due to the private operator's inadequate infrastructure maintenance and financial distress.[8]

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[4] Butcher, Louise, "Railways: Railtrack, 1994-2002," House of Commons Library, March 24, 2010 (https://researchbriefings.parliament.uk/ResearchBriefing/Summary/SN01224) and "Potters Bar crash: how the events unfolded," The Telegraph, May 13, 2011 (https://www.telegraph.co.uk/news/uknews/road-and-rail-transport/7918778/Potters-Bar-crash-how-the-events-unfolded.html).

[5] "Is Britain's rail franchising system fit for purpose?," Financial Times, Jan. 4, 2018. https://www.ft.com/content/db6a433c-f15f-11e7-b220-857e26d1aca4.

[6] Office of Rail and Road (Great Britain), *Rail Finance: 2017-18 Annual Statistical Release,* Oct. 11, 2018, p. 2 (figures shown are in pounds adjusted to 2018 levels).

[7] "The decadence of Argentina's rail system," Buenos Aires Herald, June 5, 2013.

[8] "Back to the future with Jim's KiwiRail," Stuff, Jan. 7, 2008 (http://www.stuff.co.nz/the-press/513331/Back-to-the-future-with-Jims-KiwiRail).

Other than Great Britain, Japan is the only major European or Asian country that has privatized most or all of its rail network. Japan's 1987 privatization followed decades of publicly-funded construction of high-speed rail lines, and required a public expenditure equivalent to $186 billion in then-current dollars for assumption of debt and creation of what was essentially an endowment to subsidize unprofitable operations.[9]

How has privatization of Amtrak services worked?

A few states that fund state-supported Amtrak services have contracted with third parties to provide on-board food service, passenger information, local marketing or maintenance of state-owned equipment. While some of these arrangements have been satisfactory, privatization efforts motivated by unrealistic expectations of cost savings or ridership increases have not been successful. In at least two cases, states have asked Amtrak to take over providing services they had unsuccessfully contracted out to private companies.

A Midwestern state that recently privatized some services for an Amtrak state-supported route encountered the same problems that Great Britain has experienced with its route franchising. The first company selected advised the state after its selection that it would require a large up-front payment, not disclosed in its bid, for equipment.[10] The state then contracted with a second company to provide equipment, food service and marketing. During the first year of this arrangement, ridership fell 10.5% and mechanical delays, due to problems with the contractor's equipment, increased 35%. After just 17 months, the contractor asked to be relieved of its contractual obligations after the state declined its request for a large increase in state subsidies.[11]

What private companies have shown interest in replacing Amtrak?

Few established private rail operators – and none of the major U.S. railroads – have expressed any interest in operating privatized Amtrak services or infrastructure, even with government subsidies. Rather, nearly all responses to solicitations of interest and unsolicited proposals have come from very small companies, most of which have never operated a passenger train, or from foreign railroads controlled by the governments of China, Japan and European countries.

A Congressionally-mandated Federal Railroad Administration (FRA) solicitation for development of high-speed services on the NEC and other corridors in 2008 did not attract a single proposal for the NEC, or any proposals for other corridors that included guarantees of private funding.[12] A similar 2016 solicitation did not produce any potentially viable proposals for privatization of Amtrak corridor routes. The only NEC proposals came from Amtrak and a consortium led by China's government-owned railway, which indicated that the consortium would be interested in constructing and operating a dedicated high-speed rail line along the NEC if federal and state governments provided most of the funding for it.[13] A 2017

[9] Peterman, David R., *Intercity Passenger Rail Restructuring in Other Countries,* Congressional Research Service, April 15, 2003, p. CRS-5; Government Accountability Office, *Intercity Passenger Rail: National Policy and Strategies Needed to Maximize Public Benefits from Federal Expenditures*, GAO-07-15, November 2006 (https://www.gao.gov/assets/260/253370.pdf), pp. 135-137.

[10] Morisse Vizza, Chris, "Whistle-blower: INDOT wasted time on alternative," Lafayette Journal & Courier, Nov. 18, 2014 (https://www.jconline.com/story/news/2014/11/18/indot-amtrak-whistle-blower/19248481/).

[11] "Amtrak takes over Hoosier State train, Lafayette Journal & Courier, Jan. 30, 2017 (https://www.jconline.com/story/money/2017/01/30/indot-yanks-hoosier-state-train-contract/97257928/).

[12] DOT Office of Inspector General, *FRA Continues to Make Progress Implementing PRIIA Responsibilities But Faces Challenges with Rail Planning,* Report No. CR-2014-030, Feb. 25, 2014. (https://www.oig.dot.gov/sites/default/files/FRA%20Progress%20Implementating%20PRIIA%5E2-25-14.pdf), p. 21.

[13] FRA-2016-0014, Proposals for High Speed Rail Corridors (https://www.regulations.gov/searchResults?rpp=25&po=0&s=fra-2016-0014&fp=true&ns=true), Zhongmin Yang - Response.

FAST Act-required solicitation that offered large federal subsidies to entities willing to take over Amtrak long-distance routes did not attract a single bid.[14]

Would privatization make Amtrak services profitable?

Amtrak was created because the private railroads were losing large amounts of money – over $1.4 billion in current dollars - from operating intercity passenger rail service. It acquired the NEC after the previous owner went bankrupt. While Amtrak's NEC operations cover their operating costs, they do not generate enough revenues to cover all of their capital costs, as business enterprises must do to earn profits and attract private investment. No other Amtrak route – or regularly scheduled intercity or commuter passenger train service anywhere in North America – generates enough revenues to cover its operating costs.

Most privatization proposals assume that financial performance could be improved by operating more trains to attract additional passengers, reducing costs, and on the NEC by generating new revenues from other users or from real estate development. These assumptions ignore important realities:

- 90% of the trains on the NEC are commuter and freight trains entitled by law to operate in return for cost-based payments that do not include any profit.

- The NEC does not have excess capacity to accommodate any significant increase in train operations. Major chokepoints – such as the two single-track Hudson River Tunnels between New Jersey and New York and stations in Washington, New York City and Boston – are already at capacity during peak periods, and trains are often canceled or delayed at other times due to major infrastructure maintenance projects. Many of the investments required to address these infrastructure deficiencies are unfunded and will require a decade or more to construct once funding is made available, during which capacity will be further constrained.

- A private entity could not avoid most of the drivers of Amtrak's costs.

  - Labor costs – wages, salaries and benefits – account for over 60% of Amtrak's operating costs. Wages, benefits, work rules and staffing requirements governing Amtrak's operating employees are negotiated between Amtrak and railway labor unions pursuant to the unique provisions of the Railway Labor Act (RLA). A private company that operated Amtrak trains or maintained NEC infrastructure would, like Amtrak, be subject to the RLA and other "railroad" laws, including the Railroad Retirement Act that imposes taxes used to fund the pensions of railroad retirees and their survivors.

  - Collectively, labor costs, payments to host railroads (the basis for which is also specified in statute) and fuel/traction costs (driven by the level of service operated) account for approximately 75% of Amtrak's operating costs.

- Amtrak owns or dispatches/maintains only about 5% of its route network. The remaining 95% - including 94 miles of the NEC - is owned by freight railroads and state/commuter agencies. A private train operator would not have the non-transferable statutory rights that enable Amtrak to operate existing and additional trains over these railroads' lines and to pay compensation based upon incremental costs, and that give Amtrak trains dispatching preference over freight trains.

Would privatization increase investment in passenger rail?

Privatization would not change the reality that providing the United States with the passenger rail system it needs requires adequate, sustained public funding at levels much higher than Amtrak currently receives. What would change is that private operators would expect to earn and keep profits from

[14] CRS 2019 Report, p. 15.

providing services – unlike Amtrak, which is required by law to reinvest net operating revenues from the NEC ($524 million in FY 2018) in NEC capital projects. Paying profits to a private operator will be a significant additional, government-funded, expense. The California High Speed Rail Authority projects that the private operator of its planned service will require a 10% profit margin.[15]

Likewise, private investors in rail infrastructure would also expect a large return on investment (ROI). A financing expert who testified in support of NEC privatization at a 2012 Congressional hearing stated that investors in NEC infrastructure would require an ROI of 10% or more, even if the federal government bore most of the investment risks through guaranteed payments. He added that relying on private investors would make projects more costly than using federal Railroad Rehabilitation and Improvement Financing (RRIF) loans to finance investments (as Amtrak is doing for its new high-speed *Acela.*trainsets).[16]

Privatizing the NEC would require upfront or guaranteed levels of federal funding, not subject to annual appropriations, much higher levels than Amtrak receives today. One group advocating NEC privatization has proposed that the federal government provide a $40 billion "loan" – the equivalent of more than 60 years of federal appropriations to Amtrak for the NEC at current funding levels - to a newly-created private company that would take over NEC infrastructure.[17] If the federal government were prepared to provide this level of funding for NEC investments, it would be much cheaper, and a lot less risky, to give it directly to Amtrak.

What are the risks associated with privatization?

The biggest risk with privatization is that the private operator or infrastructure owner will not operate safely or will not safely maintain rail infrastructure. The second biggest risk is that the private operator will become financially insolvent and/or walk away from its contract. Past experience in Great Britain, the United States and other countries shows that these risks are very real.

The consequences of a failed effort to privatize infrastructure or operations on the NEC would be disastrous. Each weekday, 820,000 Amtrak and commuter passengers and more than 50 freight trains travel over the NEC. The estimated cost to regional and national economies for each day that NEC rail service is curtailed is $100 million.[18] Addressing the maintenance deficiencies due to privatization that led to Great Britain's fatal rail accidents disrupted Britain's rail service for years.[19]

Privatization would also create other risks. Impacted Amtrak employees, many of whom possess scarce and in some cases unique skills, would likely exercise their labor contract rights to continue Amtrak employment in other positions. This would make it difficult for a new operator or infrastructure maintainer to hire a sufficient number of employees, resulting in service interruptions. Proposals for privatization of NEC infrastructure or other Amtrak assets invariably iqnore the need to compensate Amtrak for those assets based upon fair market value. Some privatization proposals could trigger obligations for repayment of Amtrak's debt or claims by impacted Amtrak employees for labor protection benefits, which would significantly increase privatization costs.

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[15] California High-Speed Rail Authority*, Central Valley and Peninsula Corridors Operations Financial Plan Study,* May 1, 2019.
(https://www.hsr.ca.gov/docs/about/legislative_affairs/Central_Valley_and_Peninsula_Corridors_Operations_Financial_Plan_Study.pdf), p. 59.

[16] Testimony of J. Perry Offutt, Managing Director of Morgan Stanley, Before the House Transportation & Infrastructure Committee, Dec. 13, 2012 (Morgan Stanley Testimony).

[17] Railway Age, "Amtrak a 'failure'? Hardly. Here's how we see it," Dec. 19, 2018
(https://www.railwayage.com/passenger/intercity/amtrak-a-failure-hardly-heres-how-we-see-it/).

[18] NEC Commission, The Northeast Corridor and the American Economy, April 2014 (http://nec-commission.com/app/uploads/2018/04/NEC-American-Economy-Final.pdf).

[19] "How Hatfield changed the rail industry," The Guardian, Sept. 6, 2005
(https://www.theguardian.com/uk/2005/sep/06/hatfield.transport).

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