

**UNITED STATES SENATE
COMMITTEE ON COMMERCE, SCIENCE AND
TRANSPORTATION**

**HEARING ON THE FUTURE OF INTERCITY RAIL
PASSENGER SERVICE AND AMTRAK**

**Testimony of
HERZOG TRANSIT SERVICES, INC.
Tuesday April 29, 2003
SR Room 253
Washington, D.C.**

I am Al Landes, Senior Vice President of Herzog Transit Services (Herzog), headquartered in St. Joseph, Missouri. Herzog operates 88 passenger trains a day in the United States. We also provide a wide variety of services related to passenger and freight railroad operations, including train dispatching, maintenance and overhaul of rolling stock, station operations, and construction and maintenance of railway track and related infrastructure. We are not alone in the private-sector rail passenger business. Around the world private companies are successfully operating thousands of passenger trains daily under contract to government authorities.

As a rail passenger service operator we have closely followed the debate on reform of Amtrak and intercity passenger rail service. Currently Amtrak holds a *de facto* monopoly on American intercity rail passenger service. The results are not good. We believe one key to reform is to maximize the role of the private sector and introduce competition as quickly as possible into the national system.

Major restructuring of intercity rail passenger service along lines proposed by the Administration and others will take a long time. A program to introduce competition to selected Amtrak operations can begin now under existing law. In fact, the process has already begun. Today Amtrak operates commuter rail services as well as shorter distance intercity trains through contractual obligations with the States. These shorter distance intercity trains are commonly known as 403(b)¹ service. Recently, Amtrak requested many states to substantially increase their subsidy on these trains. The State of Missouri responded by announcing a competitive bid and issued a request for proposal to operate one of these trains, the *Missouri Mule*. Herzog prepared a bid for this service. We learned that under current conditions a private company cannot bid against Amtrak's uncooperative government-subsidized monopoly and win. In the case of Missouri, Amtrak's refusal to negotiate access to facilities and services essential to operating the route made it impossible to prepare a compliant bid. Further, once Herzog announced its interest, Amtrak dramatically and artificially lowered its subsidy requirement from \$8.9 to \$6.4 million. Amtrak succeeded in keeping competitors out of the bid process in Missouri. They did not bother to put in a bid themselves, perhaps not wanting to give the competitive process any credibility.

Herzog has learned a hard lesson. But we are not discouraged. We intend to press on and are continuing discussions with Missouri and other states on creating a mechanism to put the 403(b) bid procedure on a level playing field. We believe much can be done without a change in law. We know many states are frustrated and want to introduce the element of competition into state subsidized intercity passenger service. However, if this procedure is to be made to work, we need strong direction from both Congressional leaders and the U.S. Department of Transportation. New procedures that apply in a standardized manner across the board to 403(b) state-subsidized service are needed. We believe a "Fair Competitive Bid Procedure," to be directed by the States, but with DOT oversight, should be implemented immediately. The States would determine when, and if, they wish to solicit competitive bids for 403(b) service. DOT would establish the guidelines for competitive bidding. They would monitor (but not control) the procedure and report to Congress in conjunction with the Federal Railroad Administration/Amtrak grant process required by the Omnibus

Appropriations Act for fiscal year 2003. As soon as possible senior authorizers and appropriators from the Congress should encourage Amtrak to voluntarily cooperate in the Fair Competitive Bid Procedure. If Amtrak refuses to cooperate they should be compelled to do so through the next item of intercity passenger legislation to clear Congress.

To create a Fair Competitive Bid Procedure for intercity passenger service under current law there are four major areas that must be addressed. The first is Amtrak's control of taxpayer provided facilities, equipment and services. The second is access to track owned by private freight railroads. The third is liability. Fourth is Amtrak's ability to raise or lower its bid to any level by using its federal subsidy. The following are our proposals.

I. ACCESS TO AMTRAK EQUIPMENT, FACILITIES AND SERVICES

To create a Fair Bid Procedure for state-subsidized 403(b) service, Amtrak must make taxpayer-subsidized assets available on a fair basis. So long as Amtrak receives taxpayer subsidy Amtrak facilities, equipment and services should be made available at incremental cost² to state-qualified operators. We suggest Amtrak be required to engage in "quick fuse" negotiation so bidders can meet state deadlines at the request of the state on behalf of any qualified applicant. Disputes between Amtrak and a qualified bidder should be resolved by binding arbitration by the FRA Administrator. The following is what we learned from the Missouri experience and our proposed resolution of each issue.

Locomotives & Passenger Cars The RFP required the winning bidder to provide train sets sufficient to run the service. We scoured the private marketplace and arranged to acquire locomotives and passenger cars. However, passenger rail rolling stock is a complex and expensive capital item, typically with significant custom modifications. The market for this equipment is tight and ordering, manufacture and delivery of new or refurbished rolling stock is typically a multi-year process. Access by bidders to the rolling stock currently providing the service can best ensure continuity and quality of service.

- **Proposed Resolution:** Because Amtrak locomotives and passenger cars in 403(b) service have been acquired with significant public subsidy they should be made available to alternative bidders by Amtrak at a fair market lease or sale value. The FRA Administrator should arbitrate the negotiation upon request by the State or state-qualified bidders.

Access to Stations The RFP required access to passenger stations along the route. Herzog readily negotiated access to city-owned stations. Amtrak owns the critical St. Louis Station. When Herzog tried to negotiate access to that station Amtrak informed us they could not negotiate access in a timely fashion to meet the bid deadline³ therefore Herzog was unable to submit a compliant bid.

- **Proposed Resolution:** At state request, Amtrak should make stations and facilities available at incremental cost in a "quick fuse" negotiation conducted in a timely enough manner to not impede the bid process. Negotiations would be arbitrated if necessary by the FRA Administrator at request of the state or one of the bidding parties.

Establishment of Maintenance Facilities The RFP required the operator to provide a maintenance facility for rolling stock. Herzog identified an excellent vacant Amtrak property that included an abandoned building adjacent to the St. Louis station. Amtrak responded that the site had been identified as a possible future maintenance facility “and must be reserved for that use.”⁴ Herzog was able to identify alternative, although less desirable property.

- **Proposed Resolution:** At state request Amtrak should either provide access to maintenance facilities and property at incremental cost or make the property available by lease or sale at fair market value. The only exception to this would be if Amtrak had a legitimate current alternative use for the property in question for intercity passenger service as determined by the FRA Administrator.

Cooperative Through Ticketing Arrangements A condition of the RFP was cooperation with Amtrak to implement a through ticketing system. The need was to make the transition between service providers seamless for the riding public for whom the *Missouri Mule* service would only be a part of their rail journey. Amtrak would not cooperate on this issue, stating, “We do not make this system available to any third parties.”⁵ This made it impossible to submit a compliant bid as it would have kept the Missouri Mule out of the national network. This alone could doom the operation.

- **Proposed Resolution:** Amtrak must cooperate with any state-designated intercity passenger rail operations bidder on through ticketing arrangements. Disputes should be subject to binding arbitration by the Administrator of the FRA.

II. TRACK ACCESS

Herzog recommends that a 403(b) Fair Competitive Bid Procedures mechanism be established with no change in Amtrak’s current incremental cost access to privately owned infrastructure. Privately owned railroads must retain the right to approve private sector bidders who would conduct train operations over their property. We recognize that this will provide Amtrak with an enormous advantage. However, as long as Amtrak holds the right of mandatory access at incremental cost over private property, their fee for that privilege should be transparent and public. This will establish a benchmark for private sector competitors to negotiate from.

We believe this would be a successful formula. It grants the freight railroads great leverage in the process. It assures owner railroads need only negotiate with responsible and safe bidders while improving their rate of return from passenger service.⁶ 403(b) Fair Competitive Bid Procedures will give the track owners an opportunity to prove once and for all that they will cooperate in a process that will permit world-class passenger service over privately-owned lines without forced government access.

III. LIABILITY

To create a 403(b) Fair Competitive Bid Procedure an additional issue of insurance needs to be addressed. The Amtrak Reform Act established liability at \$200 million per accident. Amtrak has negotiated a nationwide policy of insurance coverage, supported with taxpayer dollars. It is difficult but not impossible for a smaller private-sector operator to obtain specific coverage for a limited operation.

- *Proposed Solution:* Intercity passenger rail insurance coverage could be combined into a common pool policy. This pool could be managed by the FRA or a qualified non-profit industry association. Each operator qualified by a state would pay a premium into the common insurance pool.

IV. AMTRAK BID PROCEDURES

In the Missouri case, as soon as Herzog made its interest in bidding for the service known, Amtrak suddenly lowered its request for state subsidy. This proves competition works! However, if its original request was based on justifiable real numbers, its suddenly lowered request merely shifts the subsidy from state to federal taxpayers. The ability to do this alone gives Amtrak complete control of a bid process. It is impossible to know Amtrak's real cost or to separate out the subsidy in a bid environment. Given this, it is impossible to compete fairly against a taxpayer-subsidized company. Amtrak has in fact candidly admitted that they cannot bid against private companies without federal money.⁷

- *Proposed Solution* In connection with its grant-making authority, the FRA should instruct Amtrak to reorganize its accounting in a transparent fashion that separates the subsidy and requires Amtrak to account exactly like a private company. The FRA and Congress should monitor this process carefully and make public reports. This solution may require future legislation.

CONCLUSION

Despite the fact that Amtrak's failure to cooperate made it impossible to bid in the Missouri situation, we want to make it clear that Herzog is in this game for the long run. Railroad passenger service is our business and we won't be dissuaded from competing in our market. We have asked the State of Missouri to extend the Amtrak agreement for the shortest possible time and ultimately to reopen the competitive process. We understand the great frustrations that states like Missouri, California, New York, North Carolina, and Michigan have had in trying to preserve their intercity passenger service. If a 403(b) Fair Competitive Procedure can be established, even without changes in the present law, Herzog will be a aggressive bidder in the field.

In all of the public tumult over the near bankruptcy of Amtrak, an essential fact has been lost. That is the stunning success of rail passenger service in America. Commuter authorities are running 20 times more passenger trains every day than Amtrak runs intercity passenger

trains. Transit ridership grew by nearly 20 percent between 1997 and 2001 and forty-seven of the top fifty metropolitan areas are pursuing rail investments.⁸ Further, by this time next year, nearly 40 million passengers a year will be riding on trains operated by private companies in the United States. The Herzog operations move 2.5 million passengers per year in Southern Florida, 1.4 million per year on the Trinity Railway Express in Dallas and 922,000 per year in California. The Connex operation in Boston will move 37 million passengers annually. Around the world, hundreds of thousands of passengers are carried daily on thousands of privately operated trains. This is the successful American and world-wide experience on which we have the opportunity to build. We need to draw lessons from this experience to apply to the reform of Amtrak and to realize the restoration of world-class passenger service across the United States. The next step in this reform process is implementation of the 403(b) Fair Competitive Bid Procedure we have outlined.

¹ 403(b), a term originally coined in now-repealed legislation, is still in common use to refer generally to intercity passenger rail service that is funded in some part by state government(s).

² Note that we are not asking for forced access to freight owned track at incremental cost - only access to Amtrak facilities. Since Amtrak has access to private facilities at incremental cost, there is ample justification to give private operators access to taxpayer-provided Amtrak facilities at incremental cost. This is especially true as competition will inevitably introduce efficiencies and lower the taxpayer subsidy.

³ Amtrak put on the table numerous issues that would require resolution before station or track access could be provided. These included appraisals of the property as the starting point of the long process necessary to determine an appropriate price for station and track access. In a major understatement, Amtrak concluded in a letter from Gil Mallery, Vice President of Planning and Business Development dated March 21, "...we cannot guarantee that these discussions could be completed in a time frame adequate for you to meet the RFP's timetable." The Mallery letter is attached as an exhibit.

⁴ Mallery letter of March 24.

⁵ *ibid*

⁶ Currently there are many examples of privately negotiated arrangements which permit commuter passenger trains to operate over freight railroad-owned track and permit mixed freight and passenger train operations. Making the Amtrak forced access fee transparent will help level the playing field for the bidders, for the states seeking bids and will be an advantage to the freight track owners. The difference between the Amtrak number and a privately negotiated number is a market mechanism for publicly identifying subsidy Amtrak has been receiving from freight railroads. For example Herzog operates passenger trains over Union Pacific owned line in California. This access agreement was negotiated by the commuter authority and the number is not public. Herzog would wager that the access fee is higher than comparable Amtrak incremental access fees by more than one hundred percent.

⁷ "Our existence is dependent upon federal funding and therefore our ability to be in existence and be able to bid on these contracts is because of federal aid." - Amtrak Vice President Cliff Black, Argus Urban Transport Solutions, March 24, 2003, page 4.

⁸ "Stay the Course." Surface Transportation Policy Project. Page 11, March 2003.



March 21, 2003

[REDACTED]
Vice President Corporate Development
Herzog Companies
600 South Riverside Road
St. Joseph, MO 64507

Dear Ray:

I am responding to your letter of March 11, 2003 to David J. Carol regarding Amtrak's willingness and ability to provide various services to potential providers of Missouri state-supported rail service.

We are certainly willing to begin discussions with Herzog and any other potential providers of Missouri state-supported rail service. We should begin discussions as soon as possible given the Missouri RFP's short timetable. In particular, we feel it is important to explain to you all the issues that have to be resolved in order to provide access to our station and track facilities. For example, in order to define an appropriate price for station access, it will be necessary to obtain an appraisal of the property as a starting point. Although we will endeavor to work as quickly as possible to resolve the many issues surrounding access to the facilities, we cannot guarantee that these discussions could be completed in a timeframe adequate for you to meet the RFP's timetable.

With respect to your request to use Amtrak's reservations system, please note that we do not make this system available to any third parties. With respect to your inquiry about the abandoned building and vacant property adjacent to the Amtrak station, please note that it has been identified as the site for a future maintenance facility for the Midwest Regional Rail Initiative and must be reserved for that use.

*Mr. Ray Lanman
March 21, 2003
Page 2*



Please contact David Carol as soon as possible to schedule a meeting to discuss access to the Amtrak station and track facilities.

Sincerely,

A handwritten signature in black ink, appearing to read "Gil Mallery".

Gil Mallery
Vice President, Planning & Business Development

cc: David Carol
Mike Franke
Bruce Hillblom