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REPORT BY THE
Comptroller General
OF THE UNITED STATES

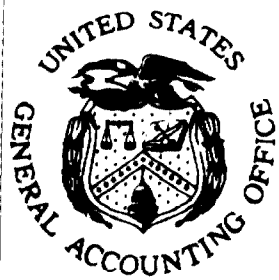
The Federal Investment In Amtrak's Assets Should Be Secured



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As of fiscal year 1980, the Federal Government had given Amtrak \$3.2 billion for its capital program. Only \$2.5 billion of this amount is subject to Federal security arrangements; that is, this part of the Government's investment would be protected should Amtrak be liquidated. Because the Government has funded Amtrak's capital assets, the Government's investment should be fully secured.

GAO recommends that legislation authorizing Amtrak's capital funding be amended so that any future Federal funding would be made available only after Amtrak and the Secretary of Transportation enter security agreements. These agreements would create a Federal claim and secure, in favor of the United States, all assets acquired in the past and future with Federal capital funding.



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COMPTROLLER GENERAL OF THE UNITED STATES

WASHINGTON, D.C. 20548

The Honorable Bob Packwood, Chairman
Committee on Commerce, Science and
Transportation
United States Senate

The Honorable Howard W. Cannon
Ranking Minority Member
Committee on Commerce, Science and
Transportation
United States Senate

This report is in response to your June 17, 1980, joint request. The report describes the degree to which the Federal investment in Amtrak is secured and recommends courses of action that can be taken to secure the continuing Federal investment. It discusses factors which have current and future impact on the Federal Government's secured position.

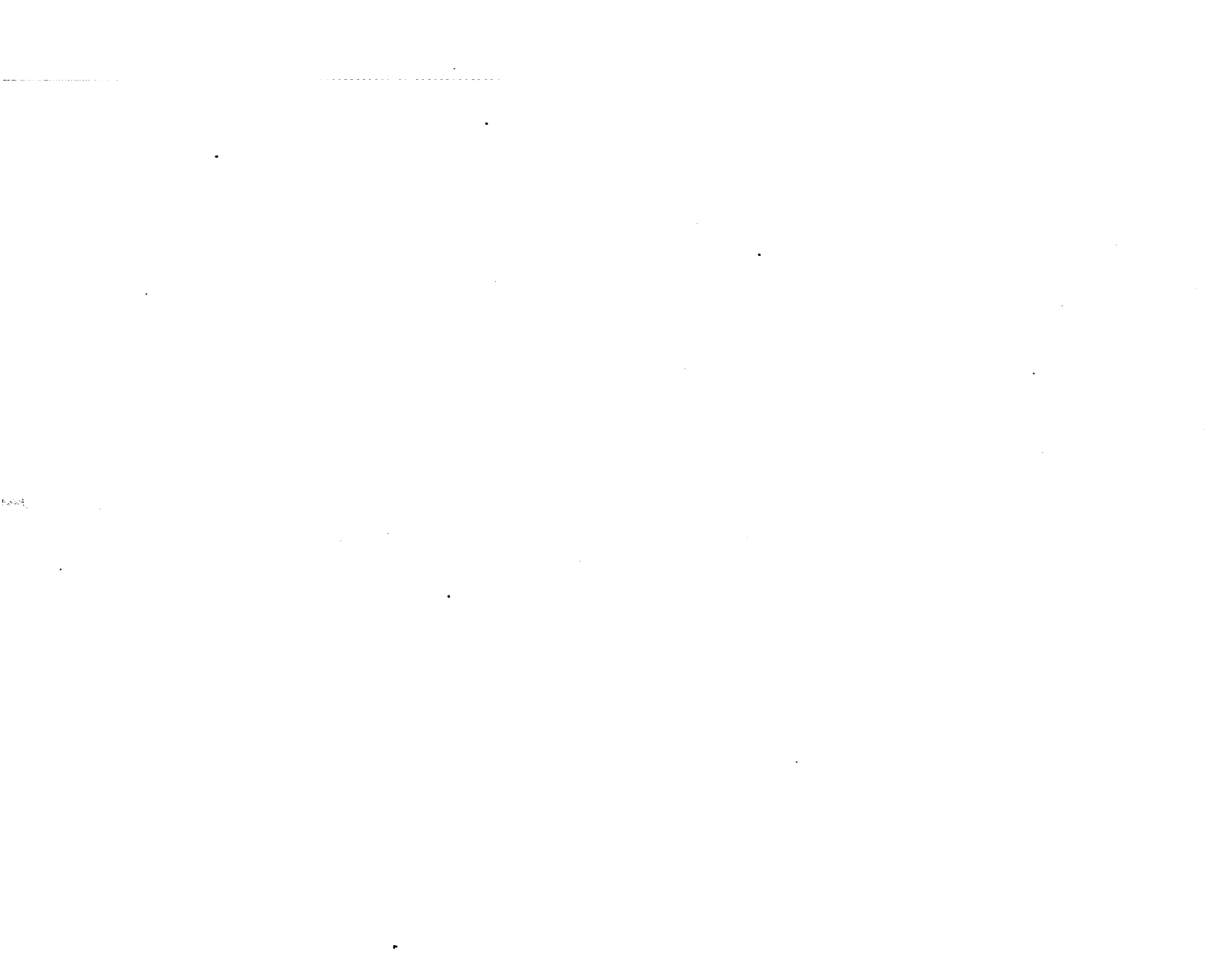
We requested agency comments from Amtrak and the Department of Transportation. Their comments along with our response to them are included in the report.

Copies of this report are being sent to the President of Amtrak, the Secretary of Transportation, and other interested parties.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Luther B. Atack".

Comptroller General
of the United States



D I G E S T

As of fiscal year 1980, the Federal Government had given Amtrak \$3.2 billion for its capital acquisition and improvement programs. This was necessary because Amtrak has not become the for-profit corporation that was planned in 1970. Instead, Amtrak has become very dependent on Federal funds and subject to greater Federal control while legally remaining a private corporation. Since Government funds have built up Amtrak's assets, it is appropriate that the Government have a security interest in the corporation. The security interest protects the Government's investment if Amtrak were liquidated. Of the \$3.2 billion provided, \$2.5 billion is subject to Federal security arrangements.

OBJECTIVES, SCOPE, AND METHODOLOGY

The Chairman and ranking minority member of the Senate Committee on Commerce, Science, and Transportation asked GAO to assess the degree of the Federal investment in Amtrak, the extent to which it has been secured, where the Government stands as a secured creditor in relation to other secured creditors, what would happen to the Government's secured position if all or part of Amtrak's debt were retired, and how the Government can continue to protect its increasing investment.

In answering the committee's questions, GAO interviewed key officials in the Department of Transportation (primarily in the Federal Railroad Administration) and Amtrak. Two representatives of Amtrak's stockholders and officials of Conrail were also interviewed. Amtrak's legal and financial records were also analyzed. (As agreed with the committee, GAO did not

independently arrive at Amtrak's asset values.) GAO then developed and analyzed alternative approaches for securing the continuing Federal investment and made judgments on the most appropriate method to use.

SECURITY ARRANGEMENTS

The Government has a security interest in \$1.5 billion (net book value) worth of fixed assets, representing the majority of Amtrak's rolling stock and all properties associated with the Northeast Corridor (NEC) purchase. Amtrak's current total fixed asset net book value (as stated by Amtrak, September 30, 1980) is \$1.7 billion. (The \$0.2 billion difference is assets secured to other creditors and unsecured assets.)

The Government uses four types of financial assistance to fund Amtrak: capital grants, operating grants, section 602 loan guarantee authority, and funding for the purchase and improvement of the NEC. While no Federal security is associated with capital grants and operating grants, section 602 guarantees and the NEC funds are secured.

The two types of secured funding are for acquisition of capital assets. Loan guarantees (section 602 authority), in the amount of \$850 million, became direct Federal loans and constitute a debt to the Government. (In fiscal year 1976 capital grants became the major capital funding mechanism--no additional guarantee authority has been provided.) The other is appropriated funds for the purchase and improvement of the NEC and associated properties stretching between Washington, D.C., and Boston, Massachusetts, and other properties conveyed in connection with the NEC purchase.

The security arrangements associated with these two types of funding provide legal security to the United States for its investment in Amtrak. In addition, they place the

Government in a position that would be superior to other secured creditors.

RETIRING AMTRAK'S DEBT

There has been recent interest in retiring Amtrak's debt to the Government (section 602 loan guarantee authority). Last year, as a result of a statutory requirement, GAO issued a report on the debt ("Alternatives for Eliminating Amtrak's Debt to the Government," PAD-80-45, March 28, 1980) and recommended that the debt be retired. GAO continues to believe that the debt should be retired, but the effect would be to reduce the Government's security interest by approximately 50 percent. The security can and should be maintained even if the debt is retired, and this can be done by adopting the recommendations in chapter 5.

An associated but less significant problem that results in reducing the Federal security in Amtrak's assets is the corporation's prior authority to use capital grants to decrease its guaranteed loan balance (see chapter 4).

SPECIAL FACTORS AFFECTING VALUE OF GOVERNMENT SECURITY

In assessing the value of the security in Amtrak, GAO believes it is important that the special relationship between the Government and Amtrak be considered. First, the relationship of Amtrak to the Government is important because Amtrak is legally a private corporation with private stockholders and creditors (see chapter 2). Amtrak remains, however, largely dependent on significant Federal funding which is primarily responsible for any asset value buildup by the corporation. This relationship is important in considering another factor: the conditions under which the Government would exercise its rights under the security arrangements. The only probable condition that would cause the Government to exercise its security rights would be under a liquidation of

Amtrak's assets. Because of the Federal commitment to rail passenger service and Amtrak's dependence on Federal funds, liquidation is only likely to occur if the Congress stops funding the railroad. If liquidation did occur, the market for Amtrak's equipment would not be good because Amtrak's equipment is unique to rail passenger service, and it is questionable whether anyone would take over this unprofitable service. There is continuing value in the NEC properties, but the majority of Federal security in the NEC is related to improvements for rail passenger service, the market for which is also questionable. This does not mean, however, that the Government should not take steps to protect its investment.

THE GOVERNMENT SHOULD FULLY SECURE ITS INVESTMENT IN AMTRAK'S CAPITAL ASSETS

Since the Government has funded the majority of Amtrak's capital assets, this investment should be fully secured so that the Government can recover as much of it as possible. Without such action, whatever value exists would go to other creditors and stockholders. In chapter 5, GAO answers the committee's final concern about how this protection could be achieved.

GAO used three criteria to measure the appropriateness of various alternatives for securing the Government's investment (all of those considered would provide full security). The criteria used are that

- the security arrangements should be easy to administer and understand,
- the unique relationship of Amtrak to the Government should be recognized, and
- the precedent established should be desirable.

We did not evaluate the option of the Federal Government assuming ownership of the corporation by acquiring the common stock currently held by four private corporations. This option would raise a wider range of policy factors than just those involving security interest (see page 35). The alternatives considered are:

- amending Amtrak's capital funding authority so that capital acquisition funding is made available only after security agreements are entered,
- including language in Amtrak's annual appropriation so that the capital funding is subject to security agreements being entered,
- entering security agreements voluntarily,
- using conventional instruments such as loans, bonds, etc., and
- executing a special note and mortgage similar to the existing one on the NEC properties and improvements.

RECOMMENDATION TO THE CONGRESS

GAO prefers the first alternative: amending Amtrak's capital funding authority. To accomplish this, the Congress should further amend section 601(b) of the Rail Passenger Service Act of 1970 (45 U.S.C. 601) so that any future appropriations for Amtrak's capital program can only be available after Amtrak and the Secretary of Transportation have entered agreements creating a Federal claim and securing, in favor of the United States, all assets acquired in the past and in the future using Federal capital funding.

AGENCY COMMENTS

GAO provided Amtrak and Department of Transportation (DOT) officials draft copies of this report for comment. Amtrak has responded in writing (see appendix VI). DOT provided oral comments.

Amtrak concurred that the Government has a need and a right to protect its investment. Amtrak believes the mechanism employed to assure this protection should be consistent with actions the Congress may take to retire Amtrak's guaranteed debt. Amtrak believes the most feasible way to retire the debt is issuing preferred stock to the Government. If the debt is not retired, Amtrak would prefer to enter security agreements voluntarily but would not object to legislation requiring such agreements.

GAO believes that it is not appropriate to predicate the method of providing security on the approach used for debt retirement. Further, Amtrak's choice for debt retirement--preferred stock--is not our recommended alternative for either debt retirement or security purposes.

DOT agreed that the Government's investment in Amtrak's capital assets should be protected and stated that GAO's recommended approach would accomplish this objective. DOT's choice, however, would be to have preferred stock issued to the Government so that the security of its investment would increase. While GAO believes that preferred stock would provide some degree of protection, it does not think it is the best alternative (see page 31).

C o n t e n t s

		<u>Page</u>
DIGEST		i
CHAPTER		
1	INTRODUCTION	1
	Objectives, scope, and methodology	1
	The Government's collateral interest discussed in prior GAO report	4
2	THE GOVERNMENT'S RELATIONSHIP TO AMTRAK; COMMITMENT AND INVESTMENT	5
	Amtrak's relationship to the Government	5
	Types of Federal funds provided to Amtrak	6
	Loan guarantees	8
	Capital grants	8
	Operating grants	8
	Funds for the NEC purchase and improvement	8
3	HOW THE GOVERNMENT'S INVESTMENT IS PROTECTED	10
	Description of the security arrangements	10
	Section 602 loan guarantee authority	11
	NEC security arrangements and effect	12
	Not all monies used to pur- chase the NEC are secured under the note and mortgage	13
	Special factors affecting value of security	14
	Value of Amtrak's rolling stock	15
	Value of the NEC properties	15
	The Government's security rights vis-a-vis other secured creditors	16
	Conclusions	17

CHAPTER

Page

4	FACTORS AFFECTING THE GOVERNMENT'S INVESTMENT PROTECTION	18
	Unsecured capital grants	18
	Retiring the section 602 debt	19
	Paying down the section 602 loan balance	19
	Conclusion	21
5	ALTERNATIVES FOR SECURING THE GOVERNMENT'S CAPITAL INVESTMENT IN AMTRAK	22
	Criteria for evaluating alternatives	22
	Ease of administration and lack of complexity	23
	Recognizing the unique Amtrak/Government relationship	23
	Desirability of the precedent established	23
	Evaluating alternatives	24
	Amending Amtrak's capital funding authority	25
	Including appropriation language securing Amtrak's capital funding	27
	Entering security agreements voluntarily	28
	Using conventional instruments	28
	Executing a note and mortgage	29
	Conclusions	29
	Recommendation to the Congress	30
	Agency comments	30
	Department of Transportation	30
	Amtrak	32

APPENDIX

I	Request letter from Senate committee	34
II	Total Amtrak funding sources	36
III	Amtrak's fixed assets as of September 30, 1980	38
IV	Properties acquired in the NEC purchase	39
V	Summary of secured/guaranteed debt as of September 30, 1980	41
VI	Amtrak letter dated February 20, 1981	42

FIGURE

1	Total Amtrak funding	7
---	----------------------	---

TABLE

1	Guarantee authority outstanding	12
---	---------------------------------	----

ABBREVIATIONS

DOT	Department of Transportation
FFB	Federal Financing Bank
FRA	Federal Railroad Administration
GAO	General Accounting Office
NEC	Northeast Corridor
NECIP	Northeast Corridor Improvement Project
UMTA	Urban Mass Transportation Administration



CHAPTER 1

INTRODUCTION

When it appeared that rail passenger service could no longer be supported by private railroad companies, the Congress created the National Railroad Passenger Corporation (Amtrak), believing that the potential loss of such service was not in the public's best interest. In support of its commitment to rail passenger service, the Congress authorized funds to Amtrak in the hope that it would become profit making. This, however, has not occurred. Amtrak has become very dependent on Federal funds and subject to greater Federal control.

While Amtrak is still legally a private corporation (four railroad companies hold all the common stock), it is Federal funding that is building up the value of Amtrak's assets. This funding should be secured. If Amtrak were liquidated and the Government were not protected, the value of assets resulting from the Federal investment would go to other creditors or to stockholders instead of to the Government. This investment is significant. As of fiscal year 1980, \$3.2 billion had been provided to fund Amtrak's capital acquisition and improvement programs. Of the \$3.2 billion, \$2.5 billion is subject to Federal security arrangements. (The difference is unsecured capital grants.)

OBJECTIVES, SCOPE, AND METHODOLOGY

In a letter dated June 17, 1980, the Chairman and ranking minority member of the Senate Committee on Commerce, Science, and Transportation asked us to assess the degree to which the Federal Government's investment in Amtrak has been protected (i.e., secured in favor of the United States). Specifically, the committee asked us to identify

- the type of security arrangements and the properties secured under them,
- the Government's priority as a secured creditor compared to other secured creditors, and
- how the Government's security would be affected if Amtrak's debt to the Government were retired.

Additionally, we agreed to analyze whether there should or could be any Federal security rights attached to past

and future capital acquisition grants. (The request letter is included as appendix I.)

To gain a proper perspective of the security issue, we feel it is necessary that the unique relationship between the Government and Amtrak be understood. Chapter 2 discusses the relationship in detail. Our discussion is only a description, however. The appropriateness of the relationship is not evaluated. Once the relationship is described, the rest of the chapter identifies the four types of Federal funding used to finance Amtrak: loan guarantees, capital grants, operating grants, and funding for the purchase and improvement of the Northeast Corridor (NEC).

In chapter 3 we show that the Government has security arrangements in connection with two of the four main types of financial assistance:

- loan guarantee authority (referred to as section 602 authority) for the acquisition of capital assets. These loan guarantees became direct Federal loans and constitute a debt to the Government.

- funds for the purchase and improvement of the NEC.

Appendixes III, IV, and V provide information on the secured properties.

Our analysis shows the degree to which the Government is legally secured and where it stands compared to other secured creditors. We also discuss in chapter 3 the conditions under which the Government could exercise its security rights and assess the practical value of these rights.

In chapter 4 we answer the committee's question on debt retirement and explain that the Government's current security in section 602 loans will end if the debt is retired. We also discuss how the Government's security is reduced because of Amtrak's past authority to use capital grants to pay down its section 602 loan balance.

Whether or not Federal security rights should be attached to capital grants is analyzed in chapter 5 along with several other alternatives. A number of criteria are used in evaluating the alternatives.

In performing our study, we interviewed key officials in the Department of Transportation (DOT)--primarily in the Federal Railroad Administration (FRA)--and Amtrak; analyzed legal and financial records; developed alternative approaches for securing the Federal investment; and made judgments about

the most appropriate method to use. In addition, we met with two representatives of Amtrak's stockholders (they are currently serving as members of the Amtrak Board of Directors) and officials of Conrail (in connection with Amtrak's purchase of the NEC from Conrail).

In assessing the value of the Government's secured interest in Amtrak's assets, we agreed with the committee that we would not independently arrive at asset values. Consequently, we used Amtrak's net book values. ^{1/} However, using the net book value presents a limitation as it does not represent the liquidation value of the assets. The actual value of the assets, at the time the Government would exercise its security rights, would depend on the assets' physical condition and marketability. We used information from Amtrak's road and property trial balance sheet statements (September 30, 1980, by equipment type), work-in-process statements, various liability and asset schedules, and other supporting data. This information was used in describing Amtrak's assets and the value of these assets and in determining which assets are secured.

We analyzed promissory notes between Amtrak and the Federal Financing Bank (FFB) with associated guarantee and security agreements between Amtrak and the FRA; a mortgage on the NEC between Amtrak and FRA; conditional sales and lease agreements of Amtrak involving Federal guarantees; Amtrak's description of the security agreements; and legislation pertaining to these transactions and documents. From these we were able to describe the types of security and the conditions and problems affecting that security.

We considered five alternatives that would secure the Government's continuing investment in Amtrak. In assessing the alternatives, three criteria were used:

- the security arrangements should be easy to administer and understand;
- the unique Amtrak/Government relationship should be recognized; and
- the precedent established should be desirable.

^{1/}To meet the committee's deadline for our report we were unable to assess the reliability of the unaudited financial data provided by Amtrak. As a basis for comparison, however, we used Amtrak's 1979 audited financial statements.

(For greater detail see chapter 5.) These criteria, in our judgment, should be and were the basis for assessing and selecting the most appropriate alternative.

THE GOVERNMENT'S COLLATERAL INTEREST
DISCUSSED IN PRIOR GAO REPORT

The Comptroller General was required by the Amtrak Reorganization Act of 1979 to recommend appropriate means for eliminating certain obligations of Amtrak, amounting to \$850 million. In a report entitled "Alternatives for Eliminating Amtrak's Debt to the Government" (PAD-80-45, March 28, 1980), we briefly addressed a security arrangement associated with that debt. We reported that Government funds provided to Amtrak under loan guarantees are protected by security agreements, which pledge certain equipment to the Government in case of default or liquidation. We concluded that this protection would terminate if Amtrak's loans were retired and recommended that as a condition of retirement the existing Government interest in Amtrak's assets should be continued by obtaining a continuing lien on the equipment. This same Government security interest is analyzed in depth in chapter 3 of this report.

CHAPTER 2

THE GOVERNMENT'S RELATIONSHIP TO

AMTRAK: COMMITMENT AND INVESTMENT

Before looking at the particular security interests the Federal Government has in Amtrak, we believe it is necessary to discuss the Government's total investment in rail passenger service through subsidies to Amtrak. The term "investment," as we use it in this report, is not meant to be understood as a financial investment on which monetary return is expected. Rather, we use the term to refer to Federal funds spent to reach a national objective. Rail passenger service provided is the "return" on the investment. To the extent that the Government wants to secure the portion of Federal funding which produces a tangible asset value, such funds are similar to a normal investment in the sense that they should be protected. The total Federal investment has caused an overall unique relationship to be formed with Amtrak that must be understood when considering the financial and security relationships that exist.

After describing Amtrak's relationship with the Government in the first part of this chapter, we describe the various types of funding which make up the Federal investment and identify which is secured funding and which is not.

AMTRAK'S RELATIONSHIP TO THE GOVERNMENT

Initial funding for Amtrak came from the Government and from private railroads giving up passenger service. Federal financing authorized for Amtrak in 1971 amounted to \$40 million for operating expenses and \$100 million in loan guarantees for capital acquisitions. The railroads had a choice of taking either common stock or a tax writeoff for their payments. Four railroads 1/ elected to take common stock that had a total par value of \$94 million. Today, these four remain the common stockholders.

Since 1971, a unique relationship between Amtrak and the Government has evolved. While Amtrak has remained a private corporation, it, like a public entity, supplies a service to the public and is significantly controlled and financed by the Federal Government.

1/Burlington Northern, Grand Trunk Western, Milwaukee Railroad, and Trustees of the Penn Central.

The Federal Government has been substantially involved in setting Amtrak's policies, which affect the control of its operations, since Amtrak's inception. Such involvement includes controlling the Board of Directors' selection and makeup, providing for accountability requirements related to Amtrak's status as a mixed-ownership corporation (such as annual audits by GAO), and determining route structures. Congressional decisions on Amtrak's route structures have provided primary Government control of the corporation's operations. Many of these decisions expanded routes and increased service to the public at additional cost to the Government through Amtrak's increased expenses, deficits, and dependence on Federal monies.

The Government also plays the major role in Amtrak's finances because Amtrak has never met its expenses out of operating revenues, and this condition is not expected to change in the foreseeable future. The only reason Amtrak has not become bankrupt is the direct Federal financial assistance it has received and continues to receive.

Total Amtrak funding is displayed in figure 1. A detailed table showing annual amounts by type of funding is included as appendix II. The Federal Government's share of Amtrak financing in fiscal year 1980 accounted for over 76 percent of all revenues. Since Amtrak's establishment, the total Federal financial investment has amounted to 72 percent of Amtrak's total financing (\$6.6 billion out of \$9.1 billion). A description of the major types of Federal funding to Amtrak follows.

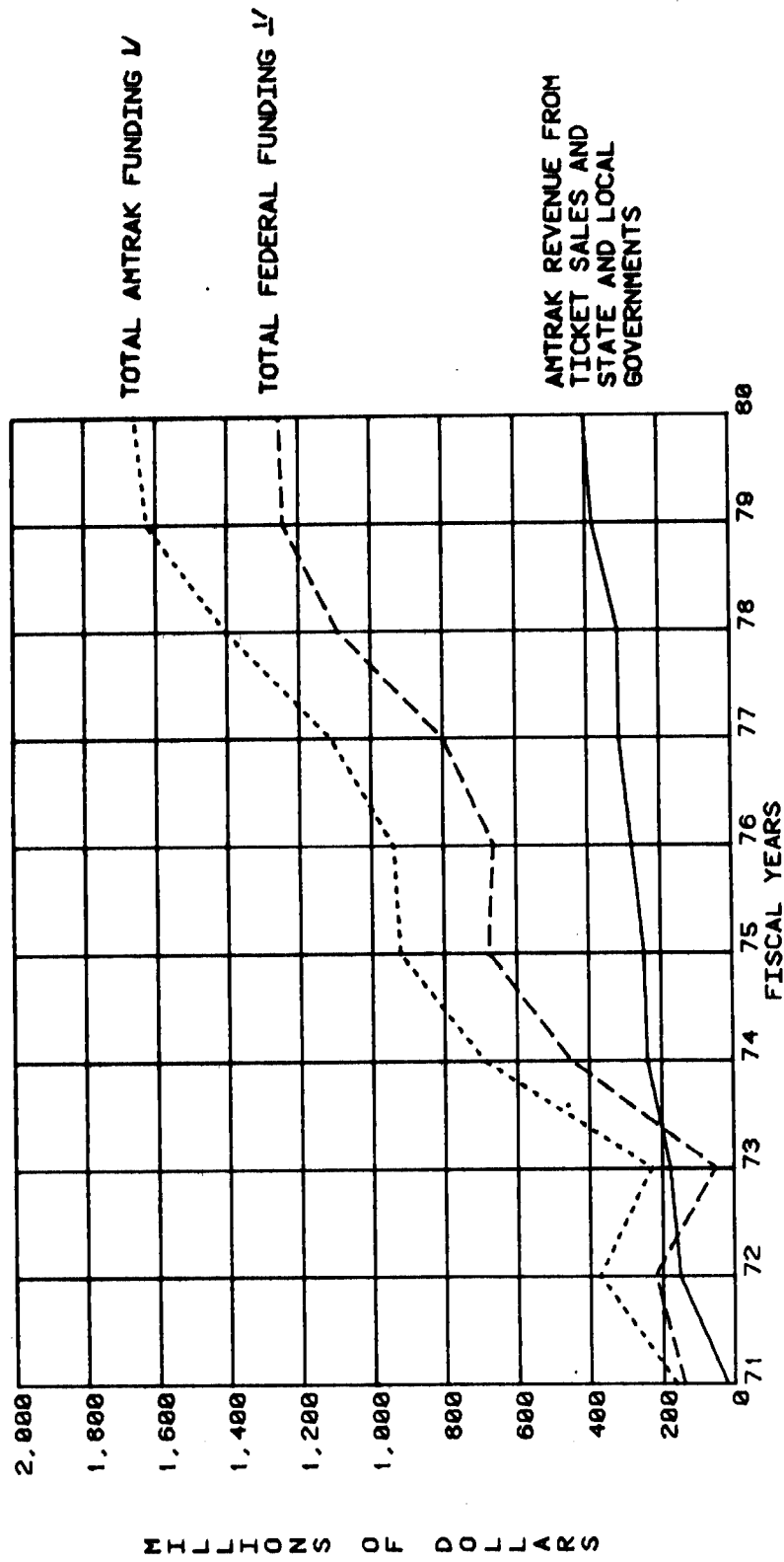
TYPES OF FEDERAL FUNDS PROVIDED TO AMTRAK

Amtrak's current Federal financing is composed of four main types:

- loan guarantee authority (involves Federal security agreements),
- capital grants (unsecured),
- operating grants (unsecured), and
- funds appropriated for the purchase and improvement of the NEC (involves a Federal security arrangement).

Capital grants, operating grants, and funds for the NEC purchase are appropriated through the budget account "Grants to the National Railroad Passenger Corporation" of the FRA-DOT.

FIGURE 1
TOTAL AMTRAK FUNDING



1/ INCLUDES AMOUNTS FOR NORTHEAST CORRIDOR PURCHASE AND IMPROVEMENTS.

Funds for the Northeast Corridor Improvement Project program (NECIP) are provided through an appropriation account in FRA-DOT entitled "NECIP."

Loan guarantees

As provided under section 602 of the Rail Passenger Service Act of 1970, Amtrak can use Federal loan guarantees to make capital acquisitions. The total loans and commitments Amtrak could have outstanding against the guarantee authority was \$900 million. The full \$900 million had been authorized by the end of fiscal year 1975 (see appendix II). Subsequently, \$50 million has been appropriated to Amtrak to reduce the debt, thereby reducing the loan guarantee authority to \$850 million. These guarantees involve Federal security agreements.

Capital grants

In fiscal year 1976 capital grants became the preferred funding mechanism for capital acquisitions, and no additional loan guarantee authority has been provided. Amtrak has received about \$686 million in capital grants for the purchase and improvement of equipment. These funds are not secured.

Operating grants

Over one-half (about \$3.4 billion) of all Federal funding for Amtrak's operations has been provided through operating grants. Operating grants include funds for day-to-day operations, and maintenance of structures, equipment, and a communication system, among other things. They comprised 29 percent or \$40 million of Amtrak's Federal funding in fiscal year 1971 and 52 percent or \$650.4 million in fiscal year 1980. There is no security associated with operating grants.

Funds for the NEC purchase and improvement

In 1976 Amtrak was authorized to purchase the NEC from Conrail. The backbone of the purchase is the 456 track miles from Washington, D.C., to Boston, Massachusetts. The purchase also includes various off-corridor trackage and property. (See appendix IV for a listing of these properties.) To date, \$86 million of the total purchase authorization (\$120 million) has been appropriated and expended by Amtrak. Since 1976, funds have also been authorized for improving these properties.

The NEC improvement program was developed to improve Amtrak's rail passenger service. Specific objectives of the NECIP are to (1) develop high speed corridor service by

upgrading road beds and (2) improve operational and non-operational facilities in the NEC. Total monies authorized for the NECIP are \$2.5 billion, of which approximately \$1.5 billion had been appropriated through fiscal year 1980. All NEC properties and improvements are secured to the Federal Government through a promissory note and mortgage.

In summary, the Government's relationship to Amtrak can be described in terms of commitment and investment. The Congress has made a strong commitment to provide the Nation with rail passenger service. This commitment has resulted in a Federal investment of \$6.6 billion dollars in operating subsidies and capital acquisition funds. Amtrak, however, has remained a private corporation. As a result, the Amtrak/Government relationship has become a complex one that must be understood in considering Federal security interests in Amtrak.

CHAPTER 3

HOW THE GOVERNMENT'S

INVESTMENT IS PROTECTED

In requesting this study, the committee asked us to identify the security arrangements and secured properties. In addition, we were asked to assess the Government's position as a secured creditor in relation to other secured creditors.

In this chapter we show that some of the Federal Government's investment is protected in the form of a security interest in Amtrak's assets. Our discussion includes a description of the security arrangements and their effect. (Secured assets are shown in appendixes III, IV, and V.) In addition, our analysis in this chapter includes an assessment of the practical value and relative priority of the security created.

DESCRIPTION OF THE SECURITY ARRANGEMENTS

The Federal Government, in return for its financial assistance, has taken a security interest in the majority of Amtrak's rolling stock ^{1/} and the properties associated with the NEC purchase. As of September 30, 1980, total Amtrak fixed assets had a net book value of \$1.7 billion, and the Government had a security interest in the assets amounting to \$1.5 billion. This represents 88 percent of Amtrak's total fixed assets.

The security itself is derived from security arrangements between the Secretary of Transportation and Amtrak. These arrangements are documents that provide for Federal claims on certain Amtrak assets under specified conditions and are related to two sources of Federal funding:

- section 602 loan and other guarantee authority, and
- appropriations for the purchase and improvement of the NEC.

^{1/}Rolling stock refers to capital equipment such as locomotives, passenger cars, track maintenance equipment, etc.

Section 602 loan guarantee authority

Section 602 of the Rail Passenger Service Act of 1970, as amended, 45 U.S.C. 602, authorizes the Secretary of Transportation

to guarantee any lender or lessor against loss of principal and interest or other contractual commitments, including rentals, on securities, obligations, leases, or loans (including refinancing thereof) issued to finance the upgrading of roadbeds, and the purchase or lease by the Corporation or an agency of new rolling stock, rehabilitation of existing rolling stock, reservation systems, switch and signal systems, and other capital equipment and facilities necessary for the improvement of rail passenger service

This authority prescribes that if Amtrak should default, the Government would pay the guaranteed commitments. The security arrangements associated with this guarantee authority currently result in about 50 percent of the Federal security claims that could be made. (The remaining Federal security is tied up in real and personal property associated with the NEC purchase.)

Currently, three types of Amtrak obligations are guaranteed by the Secretary.

--Guaranteed notes. These are promissory notes issued by Amtrak to the FFB.

--Guaranteed equipment obligation. This is a conditional sales agreement between Amtrak and the FFB.

--Guaranteed lease obligations. This is a guarantee agreement that backs certain obligations of Amtrak in connection with leases for equipment.

Amounts guaranteed as of September 30, 1980, are given in table 1. The 602 guarantees cannot exceed \$850 million of the "aggregate unpaid principal amount of securities, obligations, leases, or loans outstanding at any one time."

In return for the guarantees, Amtrak entered a series of security and guarantee agreements that give the Government a security interest in the rolling stock acquired through guaranteed fundings. The security agreements also contain an "after acquired clause" that gives the Government a security interest in all of Amtrak's rolling stock acquired after the security agreements were signed. Because of these

agreements, the Government has a security interest in 92 percent of Amtrak's rolling stock, which has a book value of \$733 million after depreciation.

Table 1

Guarantee Authority Outstanding

Guaranteed notes	\$445,000,000
Guaranteed equipment obligation	18,974,101
Guaranteed lease obligations	<u>59,845,577</u>
Total guaranteed	\$523,819,678

In effect, these agreements would allow the Government to satisfy a legal claim by taking or forcing a sale of the majority of Amtrak's rolling stock. The amount of the legal claim at any one point is equal to the guarantee authority outstanding which, as of September 30, 1980, was \$524 million. Therefore, at this time the Government would have a right to force a sale of Amtrak's rolling stock, which has a net book value of up to \$733 million, in order to satisfy its \$524 million legal claim. 1/

The outstanding balance of the guarantee authority and the Government's resulting legal claim is different from the total guarantee authority committed to date. This presents a situation which adversely affects the Government's investment protection. How this situation came about and how it affects the Government's position is discussed in chapter 4.

NEC security arrangements and effect

A promissory note and mortgage protects the Government's large investment in the NEC--projected in 1976 to be \$85 million for the purchase and \$1.75 billion for improvements. This security mechanism, while important in 1976, is even more important today because the funds authorized to be appropriated for the NEC now exceed \$2.6 billion.

According to the terms of the note held by the Government, Amtrak owes the amounts expended from appropriated funds for the purchase and improvement of the NEC, pursuant to section 704 of the Railroad Revitalization and Regulatory Reform (4R)

1/The Government cannot receive proceeds in excess of its legal claim.

Act. The terms of this transaction, however, make it apparent that issuing the promissory note was done solely to secure the United States' investment and not to recognize a debt that Amtrak was realistically expected to repay. These terms include:

- no periodic payments (the note is due in one lump sum at maturity),
- interest due if the note is prepaid or accelerated, and
- a due date in 1,000 years (2975 A.D.).

As of September 30, 1980, the note was valued at \$628.7 million. Ultimately, given current and possible future authorized amounts, the note could be as much as or greater than \$2.6 billion, once the NEC improvement program is completed. (See appendix II for detailed NEC funding information.)

A mortgage was executed in conjunction with the promissory note in order to secure the Government's investment in the NEC. The mortgage gives the United States a security interest in all of Amtrak's property obtained as a result of the NEC purchase agreement. The mortgage lien covers not only the specified mortgaged property but also after-acquired property.

Not all monies used to purchase the NEC are secured under the note and mortgage

A problem in funding the NEC initial installment payments to Conrail has created a situation in which the total purchase price has been paid to Conrail; yet, the Government does not have a security interest in the NEC properties equal to the monies used to purchase the corridor, as intended. The full \$85 million purchase price was supposed to have been funded by appropriations, but \$21 million of the purchase price was instead paid by loans Amtrak made using 602 loan guarantee authority. The 602 authority was not intended to be used for NEC payments, but because Amtrak did not receive its funding in time to make its initial installments to Conrail, Amtrak was allowed by DOT to use loan guarantee authority to make the payments. This agreement was reached in order to avoid a default situation. Amtrak officials thought that using the loan guarantee authority was a temporary arrangement and that at some future date monies would be appropriated through section 704 of the 4R Act to pay off the section 602 note. To date, however, monies have not been appropriated to pay off the 602 loan guarantee note associated with the NEC payment. Therefore, the \$21 million Amtrak borrowed to

make the NEC payment plus approximately \$6 million in accrued interest is not secured under the NEC note and mortgage but is secured against Amtrak's rolling stock through the section 602 loan guarantee security agreements.

To sum up how the Government's investment is protected, it appears that the security agreements relating to both section 602 debt transactions and the NEC purchase and improvements provide legal security for a portion of the United States' investment in rail passenger service and equipment. Beyond the legal aspects of the security, however, there are questions about the practical value of Amtrak's secured assets.

SPECIAL FACTORS AFFECTING VALUE OF SECURITY

The value of the Government's security in relation to its investment can only be brought into perspective by assuming conditions under which the Government's security rights would be exercised. The most likely situation that would require the Government to exercise its security rights would be if the Federal financial support of Amtrak were withdrawn. This Government pullout would cause Amtrak to default, and its assets would probably be liquidated. When Amtrak defaulted, the Government would have to pay off the section 602 guaranteed commitments before it could exercise its rights under the security agreements. Also, the NEC note could become payable (by congressional action) and the Government could make its claims on that property. The result would be that the United States would either take physical possession of or force a sale of the secured property to satisfy the Government's claim. In the absence of continued Government subsidy, the value of the secured property becomes important. In Amtrak's case, we believe the secured value at liquidation will be much less than book value.

Before discussing the security's practical value, it is important to emphasize that regardless of its true value the Government's investment has no protection without security. This means, under a liquidation scenario, that other third parties (i.e., common stockholders, other creditors) could potentially benefit in a sale of Amtrak's assets that were built up solely with Federal funding. Therefore, the following discussion of the practical value is not intended to detract from the importance of the Government securing its investment but to provide balance. Given the assumption that Amtrak was not a going concern and that the Government had to exercise its security rights, the asset values of the rolling stock and the NEC properties would probably decline. The most notable reason the asset values would decline is that the

existence of a viable market for Amtrak's type of assets, particularly its rolling stock, is uncertain.

Value of Amtrak's rolling stock

Amtrak's asset values would decline upon liquidation of the corporation because Amtrak's mission and assets are unique. Amtrak is the sole supplier of intercity rail passenger service today. In our view, very few, if any, of the railroads that discontinued this unprofitable service would reinvest. Therefore, Amtrak's assets (passenger cars, locomotives, and facilities, etc.) would not be a highly desirable commodity which could be easily sold.

That does not mean there would be no market for Amtrak's equipment. However, we feel any market would be marginal at best. This assumption is supported by the views of various agency officials both in the Government and in the railroad industry. Agency and railroad officials pointed out that due to the highly specialized nature of Amtrak's rolling stock, the domestic market for it is limited and the foreign market is virtually nonexistent. The primary market would be the few existing domestic commuter lines. However, the officials interviewed were even skeptical of this limited market because commuter carriers would have to modify (at a considerable expense to themselves) Amtrak's passenger cars, for example, from low seating density to high seating density.

Therefore, due to the equipment's uniqueness and the lack of competitors to pick up the service, Amtrak's rolling stock, under a liquidation scenario, would probably have a value much less than the current book value.

Value of the NEC properties

The value of the NEC properties as of September 30, 1980, was carried on Amtrak's books at \$751 million: \$86 million for the purchase, \$543 million for the NEC improvements, and \$122 million for other capital improvements. 1/ The purchase

1/The true value of the NEC properties and the cost to the Government, however, are uncertain at this point. The uncertainty arises from the recent court ruling involving the Penn Central Trustees and the Federal Government. The litigation was over the value of the properties conveyed to Conrail which included the NEC properties. The court awarded the Penn Central trustees a lump sum settlement of \$2.113 billion. Because the settlement was in a lump sum, four lawyers representing various Federal agencies familiar

and improvement values are determined by the monies appropriated and expended for the NEC purchase and its subsequent improvements under the NECIP. As mentioned previously, the value of the note secured by the mortgage held by the United States as of September 30, 1980, was \$628.7 million. Ultimately, the note held by the Government will be made up of approximately 95 percent NECIP funds.

If Amtrak were liquidated in the near future, then continued rail passenger service would be highly unlikely, and upgrading the NEC for rail passenger service would probably not be a major selling point to the potential buyers (freight lines and short haul commuter lines) whose business and needs are different. NECIP funding is used for upgrading rail passenger service on the NEC, e.g., improving rail beds for high speed rail passenger service, paying engineering consultants' fees, etc. Since the improvements may not be a major selling point, the value of the secured properties would most likely decline.

As mentioned previously, it is important to understand the practical value of the security given to protect the Government's large investment in order to put the security issue in the proper perspective. While we believe the practical value of the security related to the NEC properties under a liquidation scenario would be less than the net book value, it is still appropriate that the Government protect its interest as much as possible: any lasting value in Amtrak's assets built up with Federal funding should accrue to the Government, not to other third parties.

The analysis to this point has centered on what is secured and on the practical value of the security under a liquidation scenario. Another important consideration in a liquidation proceeding is who has a superior claim on the secured property if there are other secured creditors.

THE GOVERNMENT'S SECURITY RIGHTS VIS-A-VIS OTHER SECURED CREDITORS

Amtrak has other secured creditors, but their total security interest in Amtrak's assets is relatively insigni-

or involved with the case say there was no specific allocation that would identify the portion of the settlement relating to the NEC properties. While this settlement actually affects what will ultimately be paid out by the Federal Government for the NEC properties, it does not, in our opinion and based on the information given us at this time, change the report's recommendations or conclusions.

ficant when compared to the Federal Government's. As of September 30, 1980, the Federal Government had a security interest in Amtrak's assets with a net book value of \$1.5 billion while the other creditors had a security interest in separate assets with a book value of \$62 million. Amtrak advises that no other creditors have interests superior to the Government's in the \$1.5 billion in assets secured to the Government. Therefore, the Government would have a prior claim on assets in which it has a security interest.

CONCLUSIONS

The two security arrangements between Amtrak and the United States provide the Government with legal security in that portion of its investment for which security was established. While the extent of that security interest now includes the majority of Amtrak's capital assets, the practical value of that security is questionable if Amtrak assets are liquidated in the near future: the corporation's unique assets and the NEC improvements have potentially low marketability. Regardless of the true value of Amtrak's assets, in a liquidation scenario, it is appropriate that the Federal Government protect its investment as much as possible so that any lasting value in the assets built up solely with Federal funds accrue to the Government.

CHAPTER 4

FACTORS AFFECTING THE GOVERNMENT'S INVESTMENT PROTECTION

While the Government seems to have a significant degree of investment protection, several factors adversely affect that position now and could reduce the Government's investment protection by as much as 50 percent. These factors are:

- the change in methods the Government has used to finance Amtrak's capital acquisition program--from secured guarantee authority to unsecured capital grants,
- the retirement of Amtrak's debt related to section 602 loan guarantee authority, and
- the authority Amtrak had to use capital grants in advance to temporarily pay down the section 602 loan balance.

The importance of these factors becomes evident when one considers that 100 percent Federal financing of Amtrak's capital program is continuing to build whatever lasting value Amtrak's assets have. A discussion of the three factors affecting the Government's investment protection follows.

UNSECURED CAPITAL GRANTS

Financing Amtrak's capital acquisition program with unsecured grants provides no protection for the continuing Federal investment: the Government does not acquire a security interest in assets obtained through capital grants. Since 1976, the Federal Government has provided Amtrak with approximately \$686 million in such grants.

While the change to grants as the principal means for funding capital equipment was made primarily because the Government recognized Amtrak's inability to repay its Federal loans, it nonetheless had the undesirable effect of limiting the Government's investment protection. For example, if liquidation occurred, the Government's legal claim would be over \$686 million less because unsecured capital grants instead of secured Federal loans had been used for financing. Furthermore, continuing with this unsecured funding arrangement has greater future implications because as the Government's investment in capital equipment grows in real dollars, the relative protection the Government has for its investment

shrinks. This is not a big problem today since Federal security interests are large relative to Amtrak's asset value. It could, however, become a bigger problem in the future if the asset value builds.

RETIRING THE SECTION 602 DEBT

Recently, the Congress has been concerned with how to retire Amtrak's section 602 debt owed to the Government. As shown in chapter 3, a substantial portion of the Government's security is tied to this debt. If the debt were retired today (this would most likely be by congressional action), the Government's related security interest in Amtrak's rolling stock would end, leaving only the security interest provided under the NEC note and mortgage agreement. Thus, the Government's current investment protection would be reduced by 50 percent or more.

Our previous report 1/ briefly addressed the security issue related to the retirement of the debt. We recommended that the Government maintain its security interest in Amtrak's rolling stock currently secured under section 602 loan guarantee authority. Maintaining the security interest would insure the continued protection of the Government's investment made with section 602 loans. Insuring the continued protection would be accomplished by adopting our recommendations discussed in chapter 5. DOT concurred that the security interest should be maintained to protect the Government's interest if the section 602 debt were retired. Amtrak officials continue to support this course of action, contingent upon the Board of Directors' approval.

PAYING DOWN THE SECTION 602 LOAN BALANCE

Until fiscal year 1981, Amtrak had statutory authority to pay down the section 602 loan balance with unsecured Federal capital grants, thereby reducing the intended amount of the Government investment protection that is tied to that loan balance. Even though current law prevents future capital grants from being used in this way, the consequences of the paydown will continue until the loan balance equals the loan guarantee authority (\$850 million). 2/ With the paydown

1/"Alternatives for Eliminating Amtrak's Debt to the Government," PAD-80-45, March 28, 1980.

2/The loan balance will rise as obligations made against the capital grants come due and the funds are drawn out again as loans. At this time, a specific date cannot be pinpointed for the loan balance to equal the authority.

authority, Amtrak used capital grant appropriations to make obligations for capital acquisitions as it normally would. However, the authority allowed Amtrak to draw out the appropriation from the Treasury in advance instead of waiting for the ordered equipment to be delivered. The monies were then used to temporarily pay off loans to the FFB (thereby reducing Amtrak's interest expense).

This arrangement has two important implications. The first is that in a liquidation situation, the Government would have provided \$850 million for capital equipment, yet would have a reduced claim of only \$524 million, as of September 30, 1980, because of the paydown. Once the Government's \$524 million legal claim is satisfied, the remainder of the asset value built up with Federal funds would go to other third parties having legal claims against Amtrak.

The second reason the paydown authority is important is related to a problem which is speculative but, in our opinion, should be addressed. While it is not clear what the Government's position would be in relation to all of the commitments made by Amtrak (both against section 602 loan guarantee authority and the advanced capital grants), under liquidation conditions, it might be argued by Amtrak's contractors that the Government would be responsible for backing all Amtrak commitments. Amtrak used appropriated capital grants to pay down their loans to the FFB instead of using the grants for meeting their purchase commitments as they came due. While Amtrak was given statutory authority to use capital grants in this way, the Government might have to appropriate additional funds to make good Amtrak's commitments made with the advance capital grants if liquidation precluded Amtrak from reborrowing them. These additional appropriations might be needed even though Amtrak's commitments never exceeded the appropriated capital grants. If the Government has to make good on Amtrak's commitments made with capital grants, whether the Government would have a security interest on that equipment is questionable. If the Government does not have a security interest, other parties would benefit under a liquidation scenario.

Even though the extent of the Government's legal responsibility for the capital grant commitments is speculative, we felt it important to point out the situation because of its potential effect. The paydown on the loan balance is not speculative, however, and needs to be fully considered in light of its effect on the Government's secured position.

CONCLUSION

Overall, these factors have had or will have an adverse effect on the Government's secured position if action is not taken to create or maintain the full protection the Government's investment should have. Alternatives and recommendations for providing the Government with full investment protection will be addressed in detail in the following chapter.

CHAPTER 5
ALTERNATIVES FOR SECURING THE
GOVERNMENT'S CAPITAL INVESTMENT
IN AMTRAK

Based on our foregoing analysis, we have concluded that the Government should protect its continued investment in Amtrak's capital assets. This can be accomplished in a number of ways. Our consideration of an approach to securing that investment is based on the unique relationship that Amtrak has with the United States, as discussed in chapter 2. All of the options discussed would fully secure Federal capital funding. To assess the alternatives systematically, we developed criteria for evaluating the positive and negative aspects of each security method. In this chapter the alternatives are described and evaluated using these criteria.

One of our main concerns in considering further protection was whether the policy of providing a national rail passenger service would be affected. We do not believe there would be any measurable effect, but want to emphasize that continued protection should be thought of in the context of the two aspects already discussed in this report:

- the conditions under which the United States would exercise its security rights (liquidation) and
- recognition that the Government would not likely realize the full value of its investment.

CRITERIA FOR EVALUATING ALTERNATIVES

The criteria used here provide a basis for evaluating any potential alternative that we have identified. The criteria are not independent of each other and cannot be considered equally. We believe that the option selected by the Congress should meet these criteria to the extent possible. Our criteria concern the following issues:

- ease of administration and lack of complexity,
- recognition of the unique Amtrak/Government relationship, and
- desirability of the precedent established.

Ease of administration and lack of complexity

We believe the Congress should use a method that involves a security interest in generally described types of capital assets purchased with Federal funds, not one associated with specific pieces of property. Using general descriptions would require little bookkeeping and would cause less accounting and legal problems. The expenses involved in keeping track of specific liens would be greater than those related to a more general approach. A general blanket security on capital funding, in our opinion, is all that is necessary.

In considering the complexity of the arrangement, we believe that whatever alternative used to protect the Government's investment in Amtrak should be simple to understand. The relationship of Amtrak to the Government is already complex (private ownership with Federal control and funding; loan guarantees that became direct Federal loans, the balance of which is temporarily paid down using Federal capital grants and so on). Securing the Government's investment, on the other hand, is a fairly straightforward concept. Establishing future security interests, therefore, should be kept as simple and easy to understand as possible.

Recognizing the unique Amtrak/ Government relationship

Much of this report has discussed the special considerations and unique interactions between Amtrak and the Federal Government because the question of Federal security in Amtrak arises from that relationship--which is little understood by those not having a working knowledge of Amtrak.

Because the situation that has resulted is so different from what was planned, special care must be taken to recognize the realities of the relationship: (1) practically all of Amtrak's capital program is funded with Federal money and (2) the Government and Amtrak do not have a normal business relationship. Not providing recognition of the relationship could be misleading. It could be misleading, for example, if secured loans were used, giving the appearance of a normal business relationship where funds are repaid.

Desirability of the precedent established

The decision to relate Federal security to funds provided essentially as Federal grants could set a precedent for future Federal security arrangements. The method of protecting the Government's interest should be considered not just for its

immediate effect, but also for setting a standard. Setting this standard becomes more important if Federal backing and funding of discrete, business-like ventures continues.

EVALUATING ALTERNATIVES

The Government's capital investment in Amtrak can be protected in many ways. We identified six possible alternatives but have evaluated only five. We did not evaluate the option of the Federal Government assuming ownership of the corporation by acquiring the common stock currently held by the four private corporations or by assuming any other type of ownership. This alternative would eliminate the security interest issue but would also raise a wider range of policy factors than just those involving a security interest. In fact, the Congress already has recognized the need for a comprehensive evaluation of the common stock ownership of Amtrak. Section 12 of the Amtrak Improvement Act of 1978 (P.L. 95-421, 92 Stat. 923, October 5, 1978) charged the Secretary of Transportation to submit a report 1/ to the Congress setting forth recommendations with respect to retention, retirement, or conversion of the common stock.

The five alternatives we did evaluate assume continuation of the present institutional relationship with the stockholders and therefore require some approach limited to securing the Government's investment in Amtrak. These five options are to:

- amend Amtrak's capital funding authority so that capital funding is available only after security agreements are entered;
- include language in Amtrak's annual appropriation so that the availability of capital funding is subject to security agreements being entered;
- enter security agreements voluntarily;
- use conventional instruments such as loans, bonds, etc.; and
- execute a special note and mortgage similar to the existing one of the NEC properties and improvements.

1/The report was published January 16, 1981. We were in final processing of this report, however, and time did not permit us to do an in-depth analysis.

Amending Amtrak's capital
funding authority

The Congress could pass legislation that would amend the current authority for Amtrak's Federal capital funding. The legislation could state explicitly that all such funding would be secured in favor of the United States against capital assets purchased and improved with those funds. Such funding would not be available until security agreements between Amtrak and the Government were entered.

We are providing language that could be used for amending current legislation to establish the security under discussion. The legislation itself could be the legal basis for the protection of the Government's investment.

Section 601 of the Rail Passenger Service Act of 1970, as amended (45 U.S.C. 601) could be further amended by adding at the end of subsection (b) thereof a new paragraph as follows:

"(4) In order to protect and secure the expenditure of funds by the United States on account of the Corporation's acquisition of and improvement to capital equipment and facilities, and because such funds amount to practically all of Amtrak's capital funding, and notwithstanding any other provision of this subsection (b), no funds hereafter appropriated shall be available to the Corporation for the payment of capital acquisitions or improvements and capital expenses until the Corporation and the Secretary enter into appropriate agreements establishing a claim and securing the United States, on such terms and conditions as are deemed appropriate by the Secretary, in the equipment and facilities, and any improvements to same, previously obtained or to be obtained with funds for capital acquisitions, improvements or expenses, or by obligations guaranteed by the Secretary pursuant to section 602 of this title; provided, that this provision shall not be effective until 90 days after its enactment; provided further, that the amount of the claim to be secured to the Government is equal to the aggregate of (a) amounts of Federal funds heretofore and hereafter provided and expended for capital acquisitions or improvements and capital expenses and (b) any amount paid at any time by the Federal Government to retire obligations of the Corporation guaranteed by section 602 of this title."

It should be noted that we have included language to secure "equipment, facilities, or other property previously obtained." This would secure equipment, etc., acquired with capital grants since 1976. As discussed in chapter 2, a secured method of funding--loan guarantees--was changed to the unsecured method of providing capital grants because the loans could not be repaid. It appears that the loss of security was not considered at that time. We believe that, because of the unique relationship that has evolved between the Government and Amtrak, it is appropriate to now secure the \$686 million in capital grants already provided. This would also provide security for that portion of the loan guarantee funding not now secured because of the capital grant paydown of the loan balance.

Such agreements need not be complex. If they were made similar to the existing ones, they would be fairly easy to administer. We believe it is easy to understand because its intent is simply and clearly stated.

This option also meets our criterion of recognizing the Amtrak/Government relationship by stating that all of Amtrak's capital program is funded by the Federal Government. It also recognizes the relationship by what the option does not do. It does not create an appearance of a normal business relationship. The language of the amendment makes it clear that the Government is providing all of Amtrak's capital funding and desires security for it.

In considering whether to attach Federal security rights to Amtrak's capital grants, we asked whether or not the concept of a grant would be altered. We felt the need to address this issue because Federal grants are not usually given with the idea that the United States might someday get a portion of the funds back. In the case of attaching security to Amtrak's capital grants, the intent is to return to the Government any remaining asset value--built up with Federal funds--in the event that the grantee is liquidated. Therefore, we asked the question, would the grant concept be affected if security rights were attached to Federal funds provided as grants? Actually, this factor has to be discussed in the context of our third criterion--desirability of the precedent set. While officials we interviewed did not have any major problem with the concept of secured grants, we looked for an existing program involving some type of Federal security associated with capital grants and equipment. We found something similar in a program of the Urban Mass Transportation Administration (UMTA) which uses a type of grant with a protective feature for the Government. These grants are made to cities for the purchase of buses. Under the grant agreement, the city must pay to UMTA certain amounts based on the value of the buses

and on other factors, if for some reason the buses are not bought or put into use as intended. The United States, then, is returned a portion of the value of Federal capital grants if the objective of those grants is not met.

We realize that UMTA's arrangement is not a security interest, but based on the approach used with these grants, it appears that the precedent of protecting the Government's investment has already been set. The Government wants its money returned if the capital purchased is not used for the intended purpose. In Amtrak's case, agreements creating security interests are very much the same as UMTA's agreements in intent and effect. Therefore, we believe that using a secured grant concept would not be establishing an undesirable precedent but would be furthering a precedent that, in our opinion, if the circumstances are similar, is desirable.

To sum up the option of securing capital grants by amending Amtrak's capital funding authority, we believe that complexity and administrative difficulty are minimized. The approach adequately recognizes the Amtrak/Government relationship and it reinforces a desirable precedent. Thus, we believe this alternative is the best for securing the Federal investment.

Including appropriation language
securing Amtrak's capital funding

The Congress could include language in Amtrak's appropriation which makes capital funding available only after security agreements are entered. The language could be the same as that recommended for the previous option. As a matter of fact, this alternative is similar to amending Amtrak's current capital funding authority with two exceptions. First, if there were no authorizing legislation, this approach could be subject to a point of order in the legislative process. Secondly, because appropriation legislation occurs annually it would not have the permanence that amended authorizing legislation would have. Each year the security provision would have to be written into the appropriation act. While this is not a major problem, Federal security could be lost if the provision were deleted in the legislative process. For this reason we do not think this approach is as desirable.

As far as the criteria are concerned, this option is closest to our preferred one. Complexity and ease of administration are not problems. The Amtrak/Government relationship is recognized and a desirable precedent is reinforced. We think the appropriation language approach is acceptable but not as good as amending authorizing legislation.

Entering security agreements voluntarily

Another alternative we considered, but which we do not think is viable, was an approach involving security agreements being entered without any change in legislation. This could come about by Amtrak and the Secretary of Transportation simply entering an agreement that creates a Federal claim and secures all capital equipment, improvements, etc., acquired with Federal funds to the Government in the past, present, and future.

As far as meeting the criterion of complexity, this approach is simple and easy to understand. If the agreements were made similar to the current loan guarantee security agreements, they would be easy to administer. The degree to which this option would recognize the relationship between Amtrak and the Government would depend on how the agreements were written, but there is nothing inherent in the approach that precludes adequate recognition. As far as setting a precedent, we believe this alternative is the same as the others which attach security to Amtrak's capital funding; it reinforces a desirable precedent. However, there is nothing to ensure that Amtrak would actually enter such an arrangement. DOT could not force an arrangement on Amtrak because a statutory requirement does not exist. An additional disadvantage to using this approach is that the Congress would not have made a policy judgment about the security issue.

Using conventional instruments

Because Amtrak is a privately owned corporation and because secured investment is common in the business world, it is natural to consider conventional ways to secure investments. These include loans, bonds, preferred stock, etc. In applying our criteria, however, we rejected all conventional instruments for several reasons.

First, we primarily objected to their use because they do not recognize the unique relationship that exists. Conventional methods of protecting the Government's funds would give a false impression that Government involvement was more of a normal business-type relationship. Loans, for example, would imply a reasonable expectation of repayment. Whatever is done with regard to Amtrak should be a step toward recognizing that Amtrak is largely a federally funded and controlled entity and not a normal, private, for-profit business. Using conventional business instruments to provide protection to the Government would be a step in the wrong direction.

Use of such methods would create unnecessarily complex considerations (such as terms for repayment) that would

have no real bearing on the security situation. Finally we believe it would set a bad precedent to use unrealistic approaches that might cause more confusion than help in solving the security issue. Therefore, we judged conventional instruments unacceptable.

Executing a note and mortgage

Another alternative we considered was a note and mortgage on capital property acquired with Federal capital funds. We considered this method because a precedent has already been established in the NEC note and mortgage. The amount of the note would be the sum appropriated for capital acquisitions. Terms would include repayment that would not be realistically expected. One condition would be that the note would be payable upon liquidation of Amtrak. The mortgage secures in favor of the Government all capital assets acquired with Federal capital funds.

Our assessment of this option is that it fails to meet our criteria: (1) It introduces complexity into the security arrangement by including unnecessary conventional terms and conditions. (For example, like the NEC note and mortgage, there would most likely be an interest rate, repayment schedule, and penalties established.) (2) It gives the appearance of a relationship that does not exist, i.e., expecting repayment of a debt. While it is true that this approach reinforces a precedent established by the NEC 1,000 year note and mortgage arrangement, we believe the first two alternatives for securing the Government's investment more fully meet all three criteria.

CONCLUSIONS

The Congress has made a strong commitment to provide the Nation with rail passenger service. This commitment has resulted in a Federal investment of \$6.6 billion in operating subsidies and capital acquisition funds. In fact, the Congress has virtually provided 100 percent of Amtrak's funding for capital expenses since the corporation was formed in 1971.

Amtrak, nevertheless, has legally remained a private corporation. As a result, the relationship between Amtrak and the Government has become a complex one which must be understood in considering Federal security interests in Amtrak. Because the corporation is privately owned and has other creditors, that portion of the Federal investment which might have been recovered would be lost if Amtrak were liquidated and the Government were not protected.

The Government has some protection now through its funding for guaranteed loans and the NEC purchase and improvements, both of which are building lasting value in Amtrak's assets. The other type of Federal funding which builds asset value, capital grants, is not secured.

Currently the net book value of the assets in which the Government has a security interest exceeds the Federal funding that is secured. In considering the value of those assets, however, under a scenario in which the United States would exercise its security rights, that value is questionable because of Amtrak's unique mission--the market for its assets would be poor. An exception may be some NEC properties, but their actual value is still uncertain.

An action being considered by the Congress, retirement of the section 602 loans, could cause the Government to lose about half of its current security. Retirement of the section 602 loans would also retire the attached security agreements. We believe this security should be continued even if the loans are retired. In addition, the security reduced by Amtrak's capital grant paydown authority should be restored.

Because of the size and nature of the Federal investment in Amtrak--and the relationship that exists--we believe the Government should protect its investment in Amtrak's capital assets. This should be done as easily as possible and in a manner that recognizes the unique Federal relationship to Amtrak.

RECOMMENDATION TO THE CONGRESS

The Congress should further amend section 601(b) of the Rail Passenger Service Act of 1970 (45 U.S.C. 601). This amendment would allow future appropriations for Amtrak's capital program to be available only after Amtrak and the Secretary of Transportation have entered agreements that create a Federal claim and secure in favor of the United States all assets acquired in the past and in the future using Federal guarantees and capital funding.

AGENCY COMMENTS

The Department of Transportation and Amtrak reviewed the draft of this report. Amtrak provided a written response (see appendix VI). DOT officials provided oral comments.

Department of Transportation

DOT agreed that the Government's investment in Amtrak's capital assets should be protected and stated that our

recommended approach would work. Their choice, however, for securing the Federal investment would be to have preferred stock issued by Amtrak to the Government. Issuance of preferred stock is already authorized in legislation, but none has been issued to date. DOT cited several reasons for their suggested approach. They believe preferred stock

- would be easier to administer than security agreements,
- properly reflects what they believe is an equity investment by the Government in Amtrak,
- is a well-known and established instrument, and
- would have subsidiary advantages not related to the security question.

We believe issuing preferred stock to secure the Federal investment in Amtrak's assets is not the best solution for two reasons. First, it would not provide the degree of protection to the Government that our recommended approach does. If our recommendations were adopted, the Federal investment would be secured against all current and future creditors. This would not be the case if the Government were simply a preferred stockholder since creditors (under liquidation, for example) would have a superior claim on the assets. At this point there is nothing to preclude Amtrak from entering arrangements with other creditors.

Our second reason for choosing our recommendation instead of preferred stock concerns the Amtrak/Government relationship. We question whether Government ownership of stock would properly reflect that relationship. As stated on page 24 of this report, we believe that considering Federal ownership raises a wider range of policy factors than just those involving security interest. In our opinion, it would not be appropriate to consider using preferred stock for securing the Federal investment without looking at these other factors.

We agree with DOT that preferred stock would be easier to administer than the security agreements recommended in this report. We stated in our assessment that the security method used should be easy to administer but dismissed preferred stock because we do not feel it is the best alternative for other reasons. Despite the relative ease of administering preferred stock, the current security agreements do not cause any major problems in this area. In addition, preferred stock would not provide the Government certain controls it now has over secured assets (current security agreements require DOT approval before disposal of secured assets).

Amtrak

Amtrak concurred that the Government has a need and a right to protect its investment. It believes that the mechanism employed to assure this protection should be consistent with actions the Congress may take to retire Amtrak's guaranteed debt. According to Amtrak, the most feasible way to retire the debt is by issuing nonvoting and nonconvertible preferred stock. 1/ If this is done, Amtrak argues that it would be logical and appropriate to issue preferred stock in the amount of the Government's capital investment, thereby providing protection and consistency.

Amtrak's response makes whatever is done in regard to security in general dependent on how the debt is retired. We do not believe that an approach to securing the Federal investment in Amtrak should be predicated on debt retirement. There is no assurance that retirement will take place. The Government should provide security for its investment, debt retirement notwithstanding. In any case, our recommendation for securing Federal capital funding would continue the protection that now exists on the guaranteed debt so that security would not be an issue whether the debt was ever retired, or how it was retired.

If the debt is not retired or if GAO's recommendation for retirement is followed, Amtrak agrees that security agreements are appropriate. Amtrak prefers to enter them voluntarily but would not strongly object to legislation requiring such agreements.

1/In our earlier report on Amtrak's debt, we recommended retirement be accomplished by a one-time appropriation and stated our belief that preferred stock was inappropriate.

APPENDIX		<u>Page</u>
I	Request letter from Senate Committee	34
II	Total Amtrak funding sources	36
III	Amtrak's fixed assets as of September 30, 1980	38
IV	Properties acquired in the NEC purchase	39
V	Summary of secured/guaranteed debt as of September 30, 1980	41
VI	Amtrak letter dated February 20, 1981	42

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United States Senate

COMMITTEE ON COMMERCE, SCIENCE,
 AND TRANSPORTATION
 WASHINGTON, D.C. 20510

June 17, 1980

Honorable Elmer B. Staats
 Comptroller General of the
 United States
 Washington, D. C. 20548

Dear Mr. Staats:

As you are aware, the National Railroad Passenger Corporation (AMTRAK) is owned in the form of stock in the corporation by the private railroads which contributed to Amtrak's original capital and equipment needs after passage of the Railroad Passenger Service Act of 1970. It is our assumption that the substantial amount of capital improvements funded with government grants have substantially increased the value of the underlying assets and hence the stock of the corporation. Of specific note is the acquisition of the Northeast Corridor by Amtrak in fee simple and its continuing \$2.5 billion rehabilitation and equipment acquisition program funded by the federal government.

Our particular concern is the degree to which the federal investment in Amtrak has been secured, if at all, by the value of the corporation's assets and relative priority of that security vis-a-vis Amtrak's other secured creditors. Further, to the extent that the federal government has a security or other interest in Amtrak's assets, how will that be affected by the retirement of all or part of Amtrak's debt to the federal government?

Prior to the publication of the recent report "Alternatives for Eliminating Amtrak's Debt to the Government," the Commerce Committee staff conveyed its desire for the report to address the issue of how the government's investments in Amtrak are secured. Unfortunately, we note that this matter was not covered in your report. Therefore, the Commerce Committee would appreciate your prompt appraisal of the government's degree of security or ownership in Amtrak's real as well as personal property.

Honorable Elmer B. Staats
Page Two
June 17, 1980

We would appreciate your attention to this matter at your earliest convenience and look forward to your response.

With best wishes, we are

Sincerely yours,


HOWARD W. CANNON


BOB PACKWOOD

HWG/BP:kwt

Total Amtrak Funding Sources
(\$ in millions)

<u>Fiscal Year</u>	<u>Loan Guarantees</u>	<u>Operating Grants</u>	<u>Capital Grants</u>	<u>NEC Purchase</u>	<u>NECIP Program</u>	<u>Total Federal Funding a/</u>	<u>Amtrak Revenue b/</u>	<u>Total Funding</u>
1971	\$ 100.0	\$ 40.0	\$	\$	\$	\$ 140.0	\$ 22.6 b	\$ 162.6
1972	50.0	170.0				220.0	152.7	372.7
1973	50.0	c/				50.0	177.3	227.3
1974	300.0	146.6	2.5 d/			449.1	240.1	689.2
1975	400.0	276.5				676.5	246.5	923.0
1976+TQ		462.0 e/	139.2 e/		50.0	660.9	277.8	938.7
1977		482.6	93.1 f/	25.0	200.0	800.7	311.3	1,112.0
1978		536.0	130.0	25.0	400.0	1,091.0	313.0	1,404.0
1979		600.0	130.0	24.0	490.0 g/	1,244.0	381.3	1,625.3
1980		650.4 h/	211.0 i/	12.0	381.0 j/	1,254.4	405.0	1,659.4
TOTAL	\$900.0 (50) k/ \$850.0	\$3,364.1	\$715.5 (29.7) l/ 685.8	\$86.0	\$1,521.0	\$6,586.6	\$2,527.6	\$9,114.2

a/ Fiscal year 1981 appropriations for Amtrak were passed on October 9, 1980 (P.L. 96-400) and are not included in this chart since Amtrak's 1981 revenue figures are not available. The 1981 appropriations consist of \$668 million in operating grants, \$213 million in capital grants, and \$350 million for the NEC.

b/ Includes ticket and sales revenue, and subsidies from states and other railroads.

c/ \$9.1 million was authorized but never appropriated. The authority was rescinded in FY 74 so \$9.1 million is not included in the totals.

d/These capital grants are not in place of 602 loan guarantee authority as has been the case with capital grants since fiscal year 1976. Of this \$2.5 million in fiscal year 1974, \$0.5 million was for station construction at New Carrollton, Maryland and \$2 million for new service initiated under section 403 of P.L. 91-518.

e/Amtrak received a \$10 million appropriation in fiscal year 1976 for NEC start-up costs. Of this, \$7 million was utilized for operating expenses and \$3 million for capital expenditures.

f/Funds provided to Amtrak for emergency maintenance on the NEC. The emergency maintenance program is a continuation of a program originally funded to Penn Central through FRA and is a funding source outside the normal Amtrak appropriations.

g/Includes \$35 million for grade crossings.

h/Includes \$20 million for payment of capital and operating expenses resulting from services pursuant to section 403(b) of the Rail Passenger Service Act.

i/Includes \$20 million for labor protection.

j/Includes \$31 million for grade crossings.

k/\$25 million in both FY 1978 and 1979 was provided to Amtrak to reduce the loan guarantee debt.

l/To arrive at the figure of \$685.8 million (capital grants provided for capital acquisition and improvements), we reduced the total \$715.5 by \$20 million h/ in labor protection grants and the \$9.7 million for emergency maintenance.

Amtrak's Fixed Assets 1/
as of September 30, 1980
(\$ in thousands)

	<u>Owned</u>	<u>Leased</u>	<u>Total</u>
<u>Equipment</u>			
Locomotives	\$ 203	\$ -	\$ 203
Passenger cars	644	-	644
Work equipment	2	-	2
Miscellaneous equipment	-	-	-
Total	\$ <u>849</u>	\$ -	\$ <u>849</u>
<u>Road Property 2/</u>	36	\$10	\$ 46
<u>Work in process</u>	\$ 983	-	\$ 983
(NEC)		-	(746)
(Rolling stock)			(107)
(All other)	-	-	(130)
Total property	\$ <u>1,868</u>	\$ <u>10</u>	\$ <u>1,878</u>
<u>Accumulated Depreciation and Amortization</u>	\$ 173	\$ 1	174
(NEC)			(2)
(All other)	-	-	(172)
Net book value of all properties	\$ <u>1,695</u>	\$ <u>9</u>	\$ <u>1,704</u>

1/Includes the NEC figures obtained from Amtrak's year-end property and equipment trial balance (without year-end adjustments).

2/Road property includes such things as engineering, land, grading, bridges, track, fences, buildings, fuel facilities, maintenance and storage facilities, communication systems and signals, power plants and transmission systems, machinery and tools, and other miscellaneous items.

Properties Acquired in the NEC Purchase

<u>Type</u>	<u>Quantity</u>
<u>Stations 1/</u>	
Boston-Washington corridor	77
Philadelphia-Harrisburg route	26
New Haven-Springfield, Mass.	5
<u>Off-Corridor Stations</u>	
Illinois:	Chicago Union Station (50 percent stock ownership)
Indiana:	Gary, Michigan City (Elkhart--small building near station)
Massachusetts:	(Worcester--land across from old station)
Michigan:	Albion, Battle Creek, Chelsea, Jackson, Niles, Ypsilanti (Ann Arbor parking lot only; Detroit--tracks and platforms)
New York:	Amsterdam, Colonie-Schenectady, Hudson, Rensselaer, Rhinecliff, Rome, Schenectady, Syracuse (Buffalo--tracks in station)
Ohio:	Canton, Crestline, Lima, Sandusky (Cleveland--additional land adjacent to site of new Lakefront Station)
Pennsylvania:	Greensburg, Huntingdon, Johnstown, Latrobe, Lewistown (Pittsburgh--dead end tracks only in station)
<u>Amtrak-owned maintenance facilities 2/</u>	12
<u>Rolling stock and equipment conveyed</u>	
GG-1 Electric Locomotives	10
Diesel-electric Locomotives	73
T-3 3rd Rail Electric Locomotives	1
Coaches (Clocker Service)	33
Lounge Cars (Clocker Service)	2

1/Includes passenger stations, shelters, and station sites.

2/Boston; Buffalo; Chicago; Detroit; Harrisburg; Long Island City, New York; New Haven; New York; Newark; Philadelphia; Rensselaer, New York; Wilmington, Delaware.

Parlor Cars (Clocker Service)	2
Baggage Cars	46
Railroad Post Office Cars	8
Heat Trailer Cars	5
Derricks	3
Hopper Cars	54
Camp Cars	26
Snow Fighting Equipment	7
Cabin Cars	20
Store Cars	10
Other Maintenance-of-Way Rolling Stock	<u>63</u>
TOTAL ROLLING STOCK AND EQUIPMENT CONVEYED	363

Additional maintenance-of-way equipment includes 100 items such as track tampers, spike pullers, tie inserters and cranes. Other equipment includes over 200 items such as electric generators, drills and saws used on rails, water pumps, air compressors and electric welders.

Amtrak-purchased rail lines or operating rights

<u>End-points of line</u>	<u>Miles</u>
Boston-Washington <u>1/</u>	455.9
Philadelphia-Harrisburg <u>1/</u>	103.6
New Haven-Springfield, Mass. <u>1/</u>	60.7
Kalamazoo-Michigan City	83.5
Schenectady-Hoffmans, N.Y.	6.8
Post Road-Rensselaer, N.Y.	<u>12.2</u>
TOTAL	<u>722.7</u>

Railroad line under lease

Waldron Road-Sheldon, Ill.	26.5
----------------------------	------

Equipment leased by Amtrak 2/

Over 300 motor vehicles including pickup trucks, vans and buses used to transport maintenance-of-way crews, 49 metroliner cars and the obligation on 3 encumbered pieces of maintenance-of-way rolling stock.

1/These 3 rail lines (620 miles) are considered the NEC.

2/The Government's security rights are subordinated to lessors.

National Railroad Passenger Corporation
Summary of Secured/Guaranteed Debt
September 30, 1980
Preliminary Subject to Audit

<u>Creditor</u>	<u>Debt</u>	<u>Security</u>	<u>Outstanding Balance 9/30/80</u>
	G - Government Guaranteed		
	S - Secured		
Federal Financing Bank - Note #21	S-G	All NRPC Rolling Stock	\$ 95,000,000.00
Federal Financing Bank - Note #24	S-G	All NRPC Rolling Stock	250,000,000.00
Federal Financing Bank - Note #25	S-G	All NRPC Rolling Stock	100,000,000.00
U.S. Government (NRPC NECIP Incurred Costs)	S	NEC Properties	340,801,938.62
U.S. Government (FRA NECIP Incurred Costs)	S	NEC Properties	201,852,000.00
U.S. Government (Note due in the year 2975 - NEC Purchase)	S	NEC Properties	86,000,000.00
Continental Illinois National Bank	S-G	33 Locomotives	10,476,061.41
First Security Bank of Utah	S-G	29 Locomotives	10,091,989.77
Seattle First National Bank	S-G	25 G/E Diesel Locomotives	11,331,787.72
Manufacturers Bank of Detroit	S-G	4 Turboliners	11,387,290.09
First Security Bank of Utah	S-G	25 E60 Locomotives	16,393,868.21
New England Merchants	S	49 Metroliners	10,571,587.32
The Budd Company	S	12 Metroliners	2,038,400.00
American Fletcher National Bank	S-G	Computer Equipment	164,579.48
Federal Financing Bank (CSA)	S-G	81 Locomotives	19,856,960.45
Farmers New World	S	L.A. Commissary	125,933.42
TOTAL			\$1,166,092,39.49

The Amtrak logo consists of the word "Amtrak" in a bold, sans-serif font, followed by a stylized black arrow pointing to the right.

February 20, 1981

Mr. Henry Eschwege
Director, Community and Economic
Development Division
U.S. General Accounting Office
Washington, D. C. 20548

Dear Mr. Eschwege:

I have reviewed the draft of a proposed report, prepared at the request of the Chairman of the Senate Committee on Commerce Science and Transportation, entitled "Assessment of the Federal Security Interest in Amtrak's Assets" dated January 28, 1981.

As a member of Amtrak's management, as a businessman and as a taxpayer, I certainly concur with the concept that the U.S. Government, as an investor in and lender to Amtrak, has the need and right to protect its investment. However, I also believe that the mechanism employed to assure this protection should be consistent with the actions Congress takes with respect to retiring Amtrak's guaranteed loans.

In the GAO report to Congress dated March 28, 1980 entitled "Alternatives for Eliminating Amtrak's Debt to the Government", it was recommended that Amtrak's debt be retired through the appropriation of \$850 million. In a letter dated March 14, 1980 from Amtrak to the Comptroller General included as Appendix I in the March 28, 1980 report, Amtrak recommended that the debt be retired "off-budget" by writing the loans off the Treasury's books or by issuing preferred stock. Amtrak continues to support an "off-budget" approach and believes that the issuance of a nonvoting and nonconvertible preferred stock would be the most feasible way of retiring the debt. In that letter, Amtrak also expressed a willingness, subject to the Board of Directors' approval, to grant a lien on equipment and capital improvements similar to that which currently exists under existing security agreements.

February 20, 1981
Page Two

If Congress acts to retire Amtrak's guaranteed debt either by an appropriation as recommended by the GAO or by specific legislation or if Congress takes no action with respect to debt retirement, then Amtrak would agree that the appropriate means for protecting the Government investment would be a security agreement granting a lien against Amtrak's title to capital assets purchased with guaranteed loans as well as those assets purchased with capital grants. In that regard, Amtrak would prefer to enter into such agreements voluntarily and would proceed in good faith to work out terms acceptable to both the Department of Transportation and Amtrak. Amtrak, however, would not strongly object to legislation that required these agreements.

If, on the other hand, Congress acts to retire Amtrak's guaranteed debt through the issuance of nonconvertible preferred stock, which would also protect the Government's investment in the assets purchased with the debt, then it would be logical and appropriate to issue preferred stock in the amount of the Government's capital grant investment also. Under either case, the Government's investment would be protected and there would be consistent treatment for the total Government investment. 1/

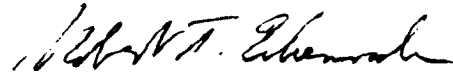
On a technical matter, there appears to be a misunderstanding in the report in the section entitled "Paying Down the Section 602 Loan Balance". In the last paragraph on page 29, carrying over to page 30, it is correctly stated that Amtrak has contractual legal obligations to contractors. It is incorrectly stated that, in the event of liquidation, "the Government might have to appropriate additional funds to make good Amtrak's commitments . . ." The total of Amtrak's commitments do not exceed the total of capital funds available (the sum of capital grants and guaranteed loan authority) and therefore, assuming all previously appropriated funds were available to Amtrak at the time of liquidation, no additional appropriations would be required to make good on Amtrak's commitments. *

1/ With respect to the NEC properties and improvements thereto the government is already protected under a note and mortgage.

February 20, 1981
Page Three

In summary, Amtrak agrees that the Government investment in Amtrak should be fully protected. The form of this protection ought to be uniform with respect to all assets and consistent with the methods Congress employs to retire Amtrak's guaranteed debt.

Sincerely,



Robert T. Eckenrode
Group Vice President-
Finance/Administration

* The section Amtrak is referring to in its letter (Paying Down the Section 602 Loan Balance) now appears on pp. 19-20. We changed our report to state explicitly that Amtrak's commitments do not exceed the appropriated capital grants. Our assumption, however, was that because some of the capital grant funds were paid into the Federal Financing Bank, that under liquidation, all of the grant funds may not be available.

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