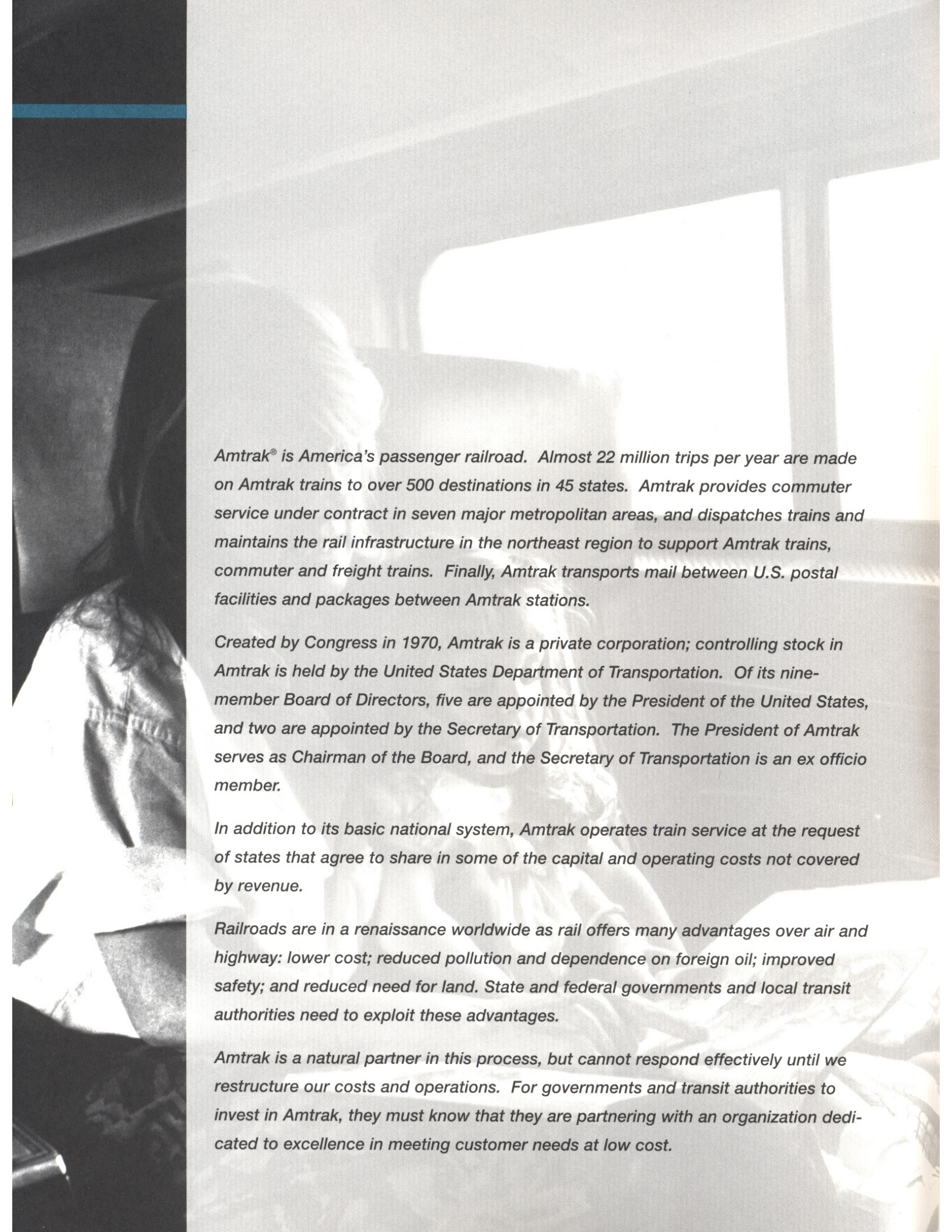


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NATIONAL RAILROAD PASSENGER CORPORATION



1994 ANNUAL REPORT

A black and white photograph of a person's profile as they look out of a train window. The person is wearing a light-colored jacket. The window shows a bright, overexposed outdoor scene. The text is overlaid on the right side of the image.

Amtrak® is America's passenger railroad. Almost 22 million trips per year are made on Amtrak trains to over 500 destinations in 45 states. Amtrak provides commuter service under contract in seven major metropolitan areas, and dispatches trains and maintains the rail infrastructure in the northeast region to support Amtrak trains, commuter and freight trains. Finally, Amtrak transports mail between U.S. postal facilities and packages between Amtrak stations.

Created by Congress in 1970, Amtrak is a private corporation; controlling stock in Amtrak is held by the United States Department of Transportation. Of its nine-member Board of Directors, five are appointed by the President of the United States, and two are appointed by the Secretary of Transportation. The President of Amtrak serves as Chairman of the Board, and the Secretary of Transportation is an ex officio member.

In addition to its basic national system, Amtrak operates train service at the request of states that agree to share in some of the capital and operating costs not covered by revenue.

Railroads are in a renaissance worldwide as rail offers many advantages over air and highway: lower cost; reduced pollution and dependence on foreign oil; improved safety; and reduced need for land. State and federal governments and local transit authorities need to exploit these advantages.

Amtrak is a natural partner in this process, but cannot respond effectively until we restructure our costs and operations. For governments and transit authorities to invest in Amtrak, they must know that they are partnering with an organization dedicated to excellence in meeting customer needs at low cost.

Board of Directors



first row from left: Celeste Pinto McLain, Sylvia de Leon, Daniel Collins, Jolene Molitoris (alternate)

second row from left: Mortimer Downey (alternate), Robert Kiley, Don Pease, Thomas Carper, Roy Neel, Thomas Downs

not pictured: Anne Canby (alternate)



Federico Peña
United States Secretary of Transportation
Amtrak preferred shareholder



Thomas M. Downs
Chairman and President of
Amtrak

Amtrak certainly will be more efficient, smaller, and better able to respond to customer needs.

I am proud to report that Amtrak is in the midst of a historic transformation and we have dedicated ourselves to being customer-focused and commercially driven.

President's Letter

Our finances and our customers are pointing to the need for change.

Financially, Amtrak ran an operating deficit in FY 1994 of close to \$600 million (after including federal subsidies received). In addition, Amtrak's cash position weakened and short-term borrowing of \$60 million in 1994 was necessary. Without structural financial changes, these deficits (cash and operating) will continue unabated in the future.

The level of service provided to customers places Amtrak revenue at-risk unless it is improved. Already, there are signs of concern. The number of passenger trips dropped last year and passenger miles are down for the third consecutive year after peaking in FY 1991. In addition, a broad-based customer survey revealed that 61% of all customers report one or more problems per trip. These survey results are both cause for concern and represent a large opportunity for Amtrak if we improve customer satisfaction.

I am, however, proud to report that Amtrak is in the midst of a historic transformation and we have dedicated ourselves to being customer-focused and commercially driven. This is not a long-term goal, but one toward which major progress must be made in the next 12-18 months. After this, Amtrak certainly will be more efficient, smaller, and better able to respond to customer needs.

Amtrak's vision and the changes taking place are detailed in "Moving to a New Amtrak." Nevertheless, a summary of some of the major changes already underway is warranted. In FY 1994 we have already **reorganized the company into three strategic business units**, devolved responsibility down to a lower level of management (closer to the train platform) and given these business units the tools and support needed to make customer-focused, strategic decisions. Refinement of this corporate reorganization will continue through 1995.

We have also begun **gathering critical information we need to make strategic business decisions**. For the first time, we are collecting baseline and ongoing data on the level of customer satisfaction. This data will help us prioritize actions for improving customer satisfaction in the future.

The transformation will continue in 1995. In the first quarter of FY 1995, we are **analyzing route profitability** in our passenger business. The study will indicate which routes, corridors or city pairings we can service commercially and what changes can be made to improve our economics. In cases where there is no potential to make money, we will eliminate this service unless policy makers agree that there is the social policy mandate to continue to provide this service and fund it.

We have already taken steps in early FY 1995 to run the company more efficiently. We offered a **voluntary severance package** for management which met the goal of reducing management staff from 2500 to 1900. We are finalizing a plan to **retire our Heritage fleet** (Amtrak's oldest and least reliable rolling stock) as aggressively as possible in order to improve the quality of service provided to customers and to lower our costs.

We will be **working with the Administration and Congress** to develop the vision of passenger rail in America and explore how Amtrak can best effect that vision. We want to ensure that Amtrak and policy makers develop a vision that is forward-thinking, pragmatic and economically achievable.

Amtrak must exploit other strategic opportunities in the next twelve months. We face major **capital decisions** regarding infrastructure upkeep on the Northeast Corridor and high-speed rail investments, among others. Amtrak must determine how best to enhance revenue in many of its businesses. Finally, Amtrak will negotiate with the unions and freight railroads (whose tracks we share).

The problems and challenges facing Amtrak are critical and sizable. I am convinced that a successful transformation will require the cooperation and assistance from all parties: state and federal governments, Amtrak's unionized employees, full costing of the use of Amtrak's track by commuter agencies, as well as the changes detailed above. I look forward to working closely with all of these "stakeholders" as we move to the new Amtrak.

Advantages of Rail Passenger Service



Rail travel provides passengers with an inexpensive, safe means of travel.

We are witnessing an international rebirth of rail. For example, the high-speed French TGV train has captured 80 percent of former air passengers on the Paris-Lyon route. In Japan, the bullet train has almost eliminated air travel between Nagoya and Tokyo.¹ Germany, for the first time ever is investing more in rail than in highways² and Sweden plans over the next decade to invest as much in railways as roads.³ European countries are collaborating to build a 4,500 mile high-speed rail network by the end of the decade stretching from Scandinavia to the Baltic to the Iberian peninsula to England.⁴

The reasons for this rebirth are straight-forward. Rail travel provides **passengers** with an inexpensive, safe means of travel. Governments support railroads worldwide since passenger rail offers many policy advantages over airline or road travel: rail alleviates congested roads and airports, and offers significant environmental benefits (taking up less space per passenger than other modes, reducing pollution, and reducing national dependence on foreign oil).

Safety Comparisons

Traveling a mile by car is over 24 times more likely to be fatal to an American than traveling by Amtrak.⁵ In its 23-year history, Amtrak has had only 88 passenger fatalities. From 1978-1992, average annual passenger fatalities⁶ by mode were:

Average Fatalities (1978–1992)

Automobiles*	24,595.9
Commercial Air	124.5
Bus	35.9
Amtrak	2.3

*excludes pedestrian and non-automobile motor vehicle deaths

¹ Wilner, Frank, *The Amtrak Story*, p.109.

² Goddard, Stephen, *Getting There*, p. 279.

³ Lowe, Marcia, D. "Back on Track: The Global Rail Revival", *Worldwatch Paper 118*, The Worldwatch Institute, p. 5.

⁴ Lowe, p. 32.

⁵ National Safety Council, *Transportation Accident Death and Death Rates, 1978-92*. Data are average FY78-92 data. Average fatality rates during this period between rail, bus and air were comparable.

⁶ National Safety Council, *Transportation Accident Death and Death Rates, 1978-92*; Amtrak Safety Department data.

Congestion Alleviation

The U.S. Department of Transportation estimates that airport congestion costs travelers and airlines \$5 billion annually, and produces 10 billion hours of delay. Highway congestion is even more costly, resulting in \$100 billion in lost productivity with \$44 billion occurring in 39 key urban areas alone. These estimates are expected to rise dramatically by the year 2000. Major highways and airports could become even more congested if rail service were not available. Amtrak is carrying 45% of the combined air-rail market between New York and Washington, DC and 70% of the combined air-rail market between these two cities when intermediate rail stops are included, such as Philadelphia and Baltimore. Over thirty percent of Northeast Corridor riders would travel by air in the absence of Amtrak. This would require numerous additional flights into already-saturated airports like LaGuardia and National. The balance of intercity and commuter travelers would likely drive, placing an additional burden on crowded highways.

Environmental Benefits

Emissions/Air pollution

Passenger rail service offers an environmentally sound alternative to other modes of transportation. Trains consume less fuel than other modes and release fewer pollutants into the atmosphere.

Data showing combined passenger and freight emissions⁷ evinces much lower fuel emission levels by railroads. Carbon dioxide emissions are the main contributor to global warming. The National Resource Defense Council reported that, for example, on Chicago to Detroit trips, Amtrak emits one-third of the carbon dioxide per passenger mile as automobiles and just over one-sixth of the carbon dioxide per passenger mile as airplanes. Passenger trains also release far lower levels of the particulate emissions that produce urban smog — volatile organic compounds and carbon monoxide:

Chicago-Detroit Corridor

(in grams of emission/passenger mile)

	Carbon Monoxide	Volatile Organic Compounds	Carbon Dioxide
Auto	10.00	0.80	260.0
Aircraft	0.91	0.27	491.0
Amtrak	0.60	0.11	85.1

Source: "On the Right Track to the Future," Natural Resources Defense Council, Feb. 1992

Amtrak also has considerable potential to help polluted areas reach Clean Air Act standards. In 1991, there were 97 areas above their ozone limits and 42 areas above their carbon monoxide limits.⁸ Amtrak provides service to 65 percent of ozone non-attainment areas and 72 percent of the areas not meeting carbon monoxide standards.

Amtrak is currently engaged in a project to bring high-speed three hour rail service between New York and Boston by the turn of the century. Amtrak estimates that up to five million passengers will use this service annually, reducing airport travel by 1.4 million trips per year and eliminating 324,000 automobile trips per year. By utilizing more environmentally-friendly fuel sources, high speed rail will thus improve air quality in a region where federal highway funds are threatened by Clean Air Act non-attainment. Projected nitrous oxide emissions will decrease 15%, volatile organic compound levels will decline by 5%, and carbon monoxide pollution will drop by 5%.⁹

Lower pollutant levels have real economic value. In an attempt to quantify the value of air pollution externalities, a 1993 German study found the costs imposed by airplane travel to be eight times that of a passenger train; and the pollution costs imposed by automobile travel to be 16 times that of a train.¹⁰

Passenger rail service offers
an environmentally sound
alternative to other modes
of transportation.

⁷ U.S. Department of Transportation-Bureau of Transportation Statistics, *Transportation Statistics Annual Report*, 1994, p. 161.

⁸ *Statistical Abstract of the United States*, U.S. Bureau of the Census, 1993, 113th edition, p. 226.

⁹ U.S. Department of Transportation-Federal Railroad Administration, Office of Railroad Development. "Final Environmental Impact Statement/Report" for "Northeast Corridor Improvement Project Electrification, New Haven, CT - Boston." Reference: DOT-V-NTSC-FRA-94-5 (10/94).

¹⁰ Wilner, p. 100, footnote 14; and Lowe, p. 37.

Land Use

Rail stations, unlike airports and highways, are less problematic to locate, since railroad stations do not usually entail lengthy siting battles and high land costs. Typically, railroad stations are rehabilitated or rebuilt on original sites — often over 100 years old. While an airport typically consumes a 15,000 acre tract¹¹ (the equivalent of 300 miles of right-of-way for rail), even the largest and most frequently utilized Amtrak station occupies less than ten acres. And one two-track right of way can carry as much traffic as 16 lanes of highway.¹²

Energy Efficiency

Amtrak provides energy-efficient transportation, reducing both dependence on foreign petroleum and the problems that a disruption in the foreign oil supply would cause: inflation, increased unemployment, and productivity declines. Trains are significantly more energy efficient than aircraft and automobiles due to superior aerodynamics and the low rolling resistance of steel wheels on steel rails. Per passenger mile, trains use one-third the energy of an airplane and one-sixth that of a single passenger automobile.¹³ In addition, airports are typically sited outside of cities generating additional pollution (beyond the flights themselves) from auto travel to and from the airport.

When Amtrak's high-speed rail service is introduced between New York and Boston, further fuel savings will be realized. Within the first decade of service, 14 million gallons of fuel will be saved annually, reducing annual oil imports by six million gallons.

Noise

Passenger rail noise disturbs fewer people than other modes. The Environmental Protection Agency estimated that aircraft and highway noise affects 50 million and 81 million people respectively, while combined passenger and freight railroad noise affects only 6.5 million.¹⁴

Social Benefits

Communities

Rail service is essential in many rural areas where alternate transportation is lacking or sparse. Sixty-two million Americans live in small towns and rural areas. While commercial air and bus carriers have found it economically infeasible to serve many smaller cities, Amtrak trains stop at areas with populations as low as 10,000-20,000 without significant cost or loss of time. Amtrak serves 33 communities with no air service, 18 communities with no bus service, and nine communities with neither air nor bus service.¹⁵ In addition, Amtrak serves 23 low-density communities whose only airline service is provided by federally-funded Essential Air Service — a program costing the government \$33.4 million in FY 1994 and a frequent target for elimination during federal budget debates.¹⁶

In many urban communities, car ownership is not a viable option. In densely populated regions, there is a critical need for diverse passenger transportation alternatives - including the rail network of intercity and commuter lines.

Critical Service/Weather

Amtrak is known for providing passenger transport during disasters, such as the January, 1994 Los Angeles earthquake and the March, 1993 blizzard that crippled the Northeast's airways and highways. In both cases, Amtrak accommodated excess volume on many lines with extra trains, and continued to operate and expand service when dangerous conditions made driving or flying impossible.¹⁷

Amtrak serves 33 communities with no air service, 18 communities with no bus service, and nine communities with neither air nor bus service.

¹¹ Lowe, p. 7.

¹² Jessica Mathews, *Washington Post*, August 15, 1994, article "Missing Link," p. A19.

¹³ U.S. Department of Transportation-Bureau of Transportation Statistics, *Transportation Statistics Annual Report*, 1994, p. 154.

¹⁴ General Accounting Office Report on Transportation Noise; Federal Control and Abatement Responsibilities Need to Be Revised, U.S. General Accounting Office/RCED-90-11, Washington, D.C., October 1989.

¹⁵ Carl Fischer, *Federal Railroad Administration*, August 1994: *Geographical Information System analysis of Amtrak stations not within 25 miles of bus stations and commercial airports*.

¹⁶ *Amtrak Station Location List 1994*; *Essential Air Service information from FY 1995 Senate Transportation Appropriations Subcommittee Report*, pp. 13-15.

¹⁷ Goddard, p. 5.

Cost

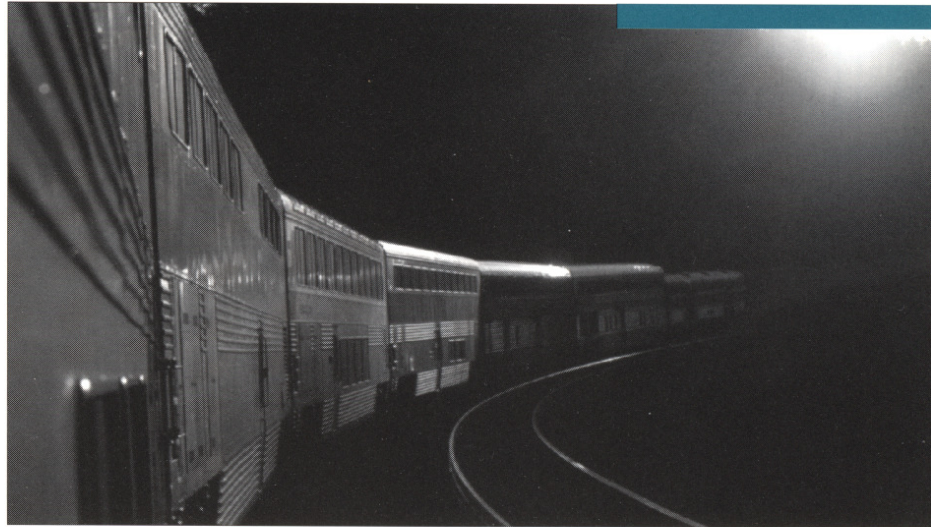
The costs of infrastructure are much lower for train than rail or air. For example, the new Century Freeway in Los Angeles (I-105) is a 17 mile eight-lane highway that is costing taxpayers \$2.2 billion or \$128 million per mile; new rail line can be installed for as little as \$1 million per mile and carry the same volume.¹⁸ "Virginia officials concluded that the cost of rail expansion is at least 40 percent less expensive than building new highway lanes — and that does not consider the higher pollution and accident costs of highway expansion."¹⁹

High-speed rail investments — to modernize the Northeast Corridor between New York and Boston and acquire state-of-the-art, built-in-America, electric trainsets to operate from Boston to Washington — will cost under \$2 billion. The investment would reduce airport congestion by eliminating over 1.4 million airplane trips annually and 2,500 daily auto trips to Boston's Logan airport alone. With one out of every six airplane trips from Logan airport headed for New York City, the high-speed rail project could mitigate the need for a new Boston airport, estimated to cost between \$5 and \$10 billion.

¹⁸ Wilner, p. 9.

¹⁹ Wilner, p. 109.

Moving to a New Amtrak



State and federal governments and local transit authorities should exploit the advantages of rail: cost efficiencies; reduced pollution and dependence on foreign oil; safety; and reduced need for land. Amtrak is a natural partner in this process, but we cannot respond effectively to this renaissance in rail until we restructure our costs and operations. For governments and transit authorities to invest in Amtrak, they must know that they are partnering with an organization dedicated to excellence in meeting customer needs at low cost.

In considering the changing environment and the role of the federal government, states and localities, Amtrak's Board of Directors has agreed that:

- Amtrak's future lies in serving densely populated corridors, commercially-oriented intercity pairs, and essential rail service corridors.¹
- the "new Amtrak" must be customer-driven² and should promote potentially profitable product lines (such as Auto Train) and incrementally profitable businesses where possible.
- state or local subsidies to support specific passenger service should approach real costs³ and not be deeply discounted.

- Amtrak should remain an *operating* company (to at least some degree) with as efficient and cost competitive operations as possible.
- in striving for an accurately costed and adequately funded passenger rail future, the Board recognizes that the system may include private segments, or segments subsidized by states, localities or the federal government.

However, Amtrak needs to change for more reasons than simply to attract partners like governments or transit providers. Amtrak now faces a large and growing structural deficit that threatens Amtrak's short-term survival.

First, Amtrak is dealing with a **rapidly changing competitive environment**. Deregulation of the airlines and increasing levels of travel (both for leisure and business) have led airlines to markedly reduce costs and offer cut-throat competitive pricing on many routes. The sophistication of their pricing structures and their commitment to meeting customer needs has put steady pressure on Amtrak's market share. This trend shows no sign of abating.

Amtrak's future lies in serving densely populated corridors, commercially-oriented intercity pairs, and essential rail service corridors.

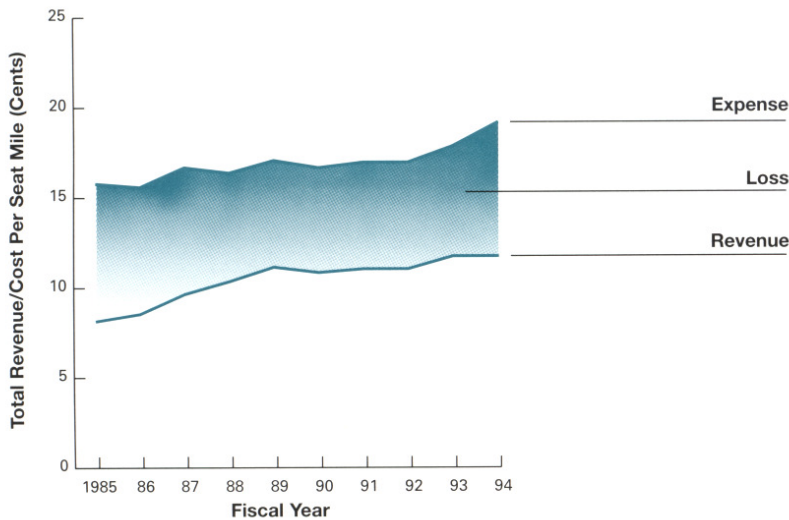
¹ Consistent with national transportation system policy.

² With customers defined as passengers and federal, state and local government entities.

³ With "real costs" meaning the long-term operating costs of providing the service and the capital costs of maintaining the infrastructure in a state of good repair.

GRAPH 1

Unit Revenue and Cost (1985–1994)



Note: FY 1994 expenses exclude \$243.8 million in one-time expenses.

Second, **chronic undercapitalization of equipment, right of way and facilities** has resulted in excessive operating costs. In many cases, Amtrak must custom-fabricate replacement parts for disabled rolling stock (since spare parts for some cars are no longer produced commercially). Equipment unreliability has forced Amtrak to increase “protect fleet requirements”—a built-in cushion against equipment unavailability. Amtrak has had to hire extra labor to ensure reliability, such as having mechanical “train riders” on some trains to handle en route problems. Finally, Amtrak has had to pay for emergency repair and construction as capital goods have deteriorated. In addition to increasing cost, equipment undercapitalization has caused service quality to deteriorate by impairing Amtrak’s on-time performance and providing inadequate passenger accommodations.

Third, **Amtrak’s business practices are antiquated and our overhead cost structure is excessive.** In an era when corporate organizations are becoming flatter and less hierarchical, Amtrak’s layers⁴ of business managers are a competitive disadvantage, preventing Amtrak from responding rapidly to challenges facing it and inexorably leading to a cash drain on the company.

The costs of these practices are being felt. Amtrak’s operating loss in FY 1994 was \$1,076.8 million. In 1994, Amtrak experienced a very high level of one-time costs: \$243.7 million. These one-time costs consist of \$71.5 million for restructuring, \$90.6 million for postretirement benefits, and \$81.6 million caused by a change in the formula used to compute casualty and accident liability costs. When these one-time costs are excluded from Amtrak’s expenses, Amtrak’s operating loss was \$833.1 million or 14% higher than 1993. When federal operating contributions (payments of \$137 million for RRTA⁵ and the federal operating subsidy of \$351.7 million) are included, the “subsidized loss” was reduced to \$588.1 million. [Footnote 6 explains the difference between this \$588.1 million “subsidized loss” and the \$77 million deficit that the Federal government records for Amtrak’s “budget result.”]⁶

Graph 1 shows the consequences of an excessive cost structure: expenses per seat mile have consistently exceeded revenue per seat mile. In the last two years, revenue per seat mile has grown at only 3.1% per year while expenses per seat mile have grown at 5.2% per year.

⁴ Up to ten levels between the President and the line in some departments.

⁵ Railroad Retirement Tax Act.

⁶ The budget result equals the total operating loss **excluding** non-cash items (depreciation and other) and including the federal operating contribution; in other words, it is the “subsidized loss” excluding non-cash items (depreciation and other). “Budget balance” (from this perspective) is achieved when this formula equals zero. The budget result is the most optimistic way of looking at Amtrak’s finances and not self-sustaining since it ignores capital depreciation and retirement costs that Amtrak must incur in the future. The budget result is anticipated to be a deficit of approximately \$200 million in 1995 (not including restructuring charges) and potentially still higher in 1996 absent major corrective action by Amtrak management (such as implementing the 1995 Amtrak business plan) and by federal, state and local public policy. An appendix to the annual report shows the numerical inter-relationship of the operating profit/loss, the subsidized profit/loss, and the budget result.

It is important for Amtrak to compare costs relative to competitors and do everything possible to reduce costs to those of its lowest cost competitor. Graph 2 compares Amtrak's costs per available seat mile to those of airlines.⁷ Amtrak's higher costs, coupled with social, political, and union pressures to continue to support a 25,000 mile national route and service structure without a rigorous commercial rationalization, have resulted in Amtrak neither being commercially competitive nor providing the quality of service desired.

Amtrak needs to be reinvented urgently. The "new Amtrak" must have three hallmarks. First, that Amtrak is dedicated to service excellence and a relentless customer-orientation. Secondly, that Amtrak provides high value service at low cost. Finally, that Amtrak enters into contractual obligations with state and federal government or transit authorities for which Amtrak is held accountable.

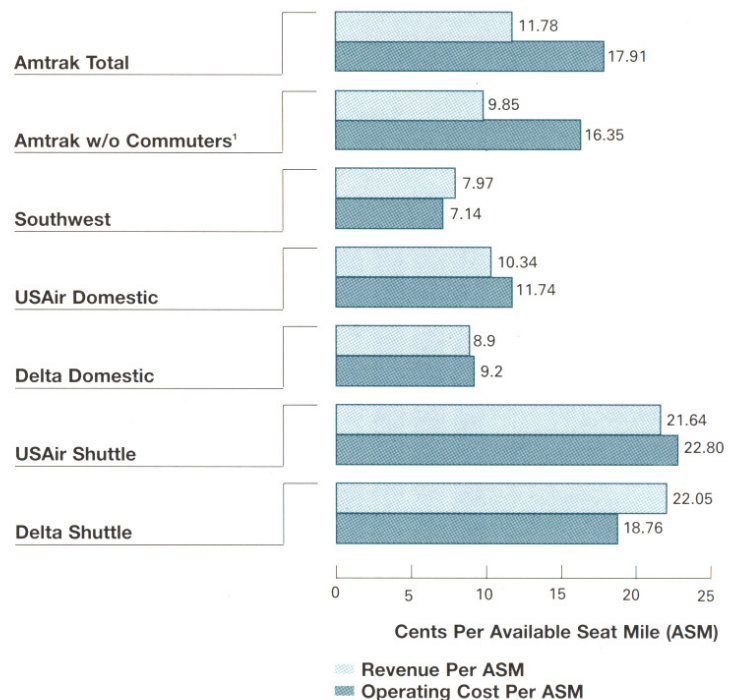
While the new Amtrak's touchstone will be to act competitively and commercially, we realize that we are not free to act *exclusively* on a commercial basis. For example, route economics might prescribe the closing of train service to a community with too few riders. Such economic imperatives often conflict starkly with social and political goals — in this case, providing train service to smaller communities. Amtrak must heed the voice and concerns of these other stakeholders: the administration, Congress, state governments, and transit authorities. However, for service that is uneconomical, these stakeholders must contract for these services directly with Amtrak, compensating Amtrak for the full cost over time that cannot be supported by farebox revenues.

How do we transition from business as usual to our vision of a new Amtrak?

The transition must be effected rapidly and 1995 is a critical start of this transformation. Six changes are in progress to head us on our way.

GRAPH 2

FY93 Unit Revenue & Cost Amtrak vs Airlines



¹ Amtrak excluding commuters and reimbursables direct costs

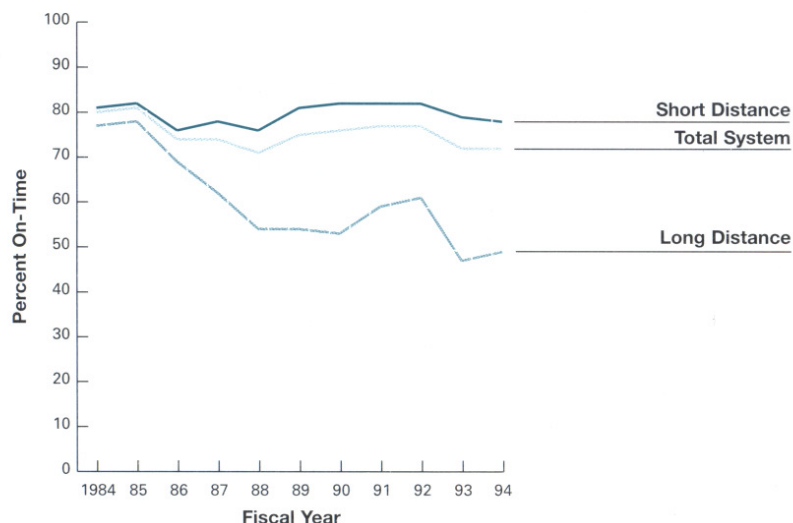
First, **we are rapidly eliminating excess overhead.** In FY 1995 we are eliminating 25% of existing management positions. This will produce annualized savings in 1994 dollars of \$44.5 million beginning in FY 1995, and a total net present value over the next 20 years of \$662 million in savings.

Second, **we are reengineering business practices from corporate headquarters to the station platform.** These practices will be consistent with the best worldwide industry practice and cost structures. We have begun this process by restructuring the company into three strategic business units (SBUs). Each SBU will have the tools, training, and support it needs to make key business decisions: to improve business practices, respond better to customer needs, and

⁷ Note: in many cases, structural issues prevent Amtrak from achieving airlines' cost structure. These structural issues include the fact that Amtrak has to maintain its track when airlines have no equivalent costs, that Amtrak's labor costs are higher because train travel is slower than air travel and thus Amtrak uses its on-board labor for more hours for a comparable length trip, etc. In some cases, the federal government is preventing Amtrak from lowering its costs by mandating that Amtrak provide an excess level of retirement benefits for its employees, by placing onerous costs on Amtrak if it eliminates routes and by locking Amtrak into a litigious and costly process for resolving employee liability claims.

GRAPH 3

On-Time Performance (1984-1994)

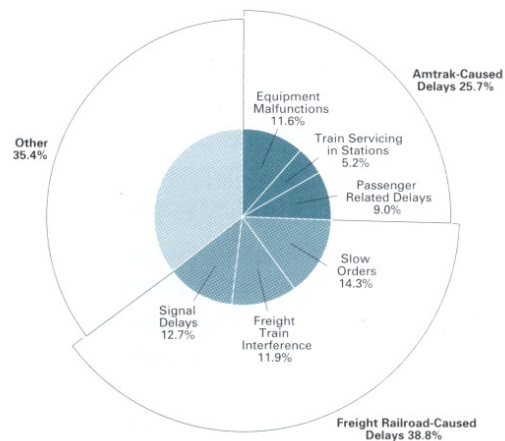


lower costs. We are also in the midst of more general reengineering of corporate functions and strategic review of the technology we need to get from here to there.

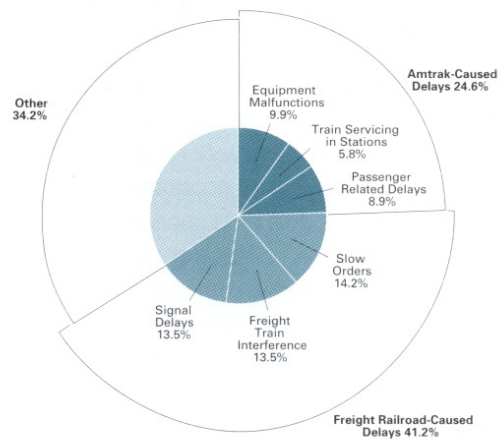
Third, ***we are instilling a customer focus and commercial orientation at all levels of the company.*** This process began with our comprehensive customer satisfaction survey that gave us a detailed baseline measure of customer satisfaction for the first time in our company's history. The data was sobering and clearly indicated our potential for improvement. Sixty-one percent of customers surveyed reported one or more "problem events" on their most recent ride. While these problems may or may not be minor in the customer's eyes, they are experiences that might dissuade customers from riding Amtrak in the future and are thus of serious concern to us. The most widely cited problem areas related to toilet problems (odor, cleanliness, etc.) or problems stemming from delays. With respect to toilet problems, Amtrak is accelerating the frequency of toilet overhauls and increasing the frequency of toilet cleaning while trains are en route. Amtrak will track customer satisfaction on an ongoing basis to chart our progress. In addition, we are tracking our on-time performance (see Graph 3) and monitoring the underlying causes of delay (Graph 4). In cases where Amtrak is responsible, we are working on underlying causes; in cases where freight railroads

GRAPH 4

Causes of Train Delay FY 1993



FY 1994



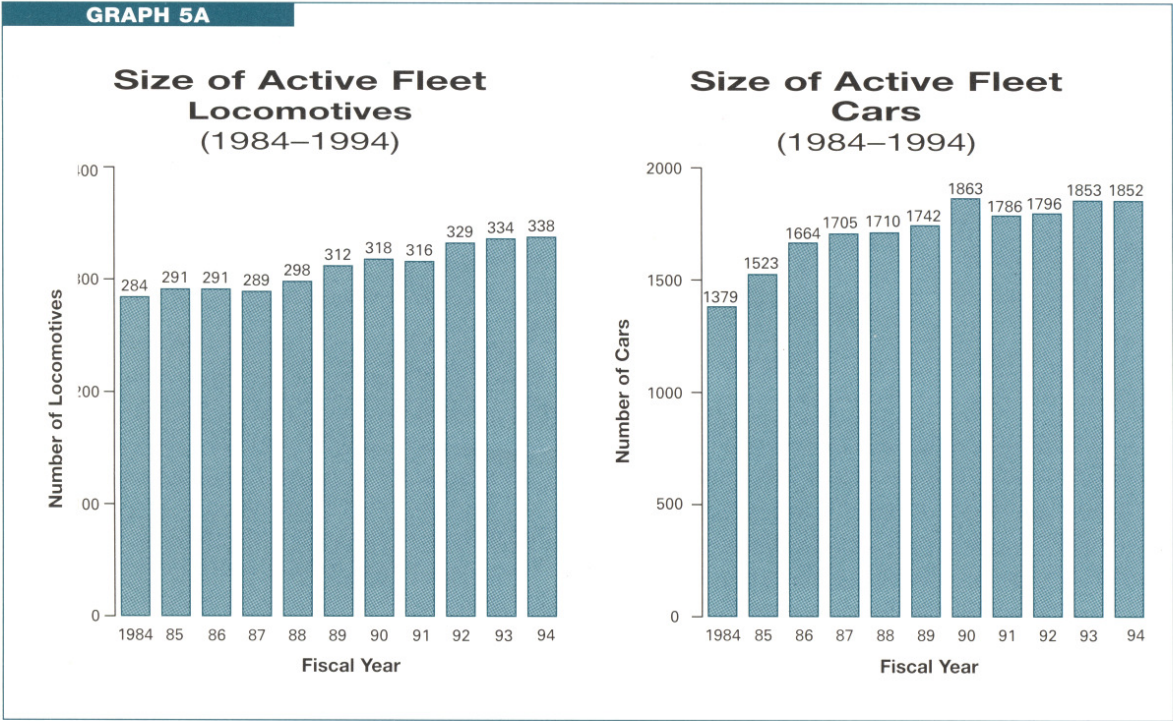
are responsible, we are working with those companies to improve on-time performance.

Fourth, ***we are eliminating costly and unreliable capital assets.*** As is evident from Graph 5, Amtrak's fleet has continued to age over the last eleven years. This has had adverse consequences on equipment availability (as seen in Graph 6). Amtrak is accelerating the retirement of our Heritage fleet (the oldest part of Amtrak's rolling stock) which will reduce costs, and improve the service provided to our customers.

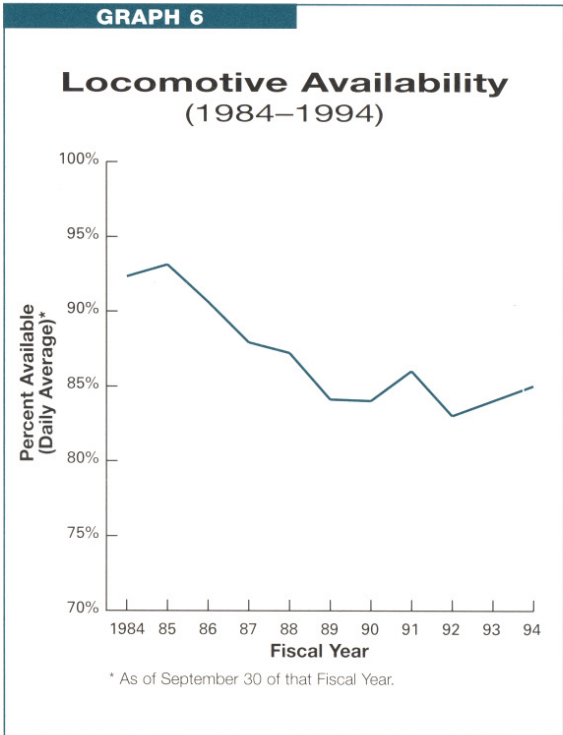
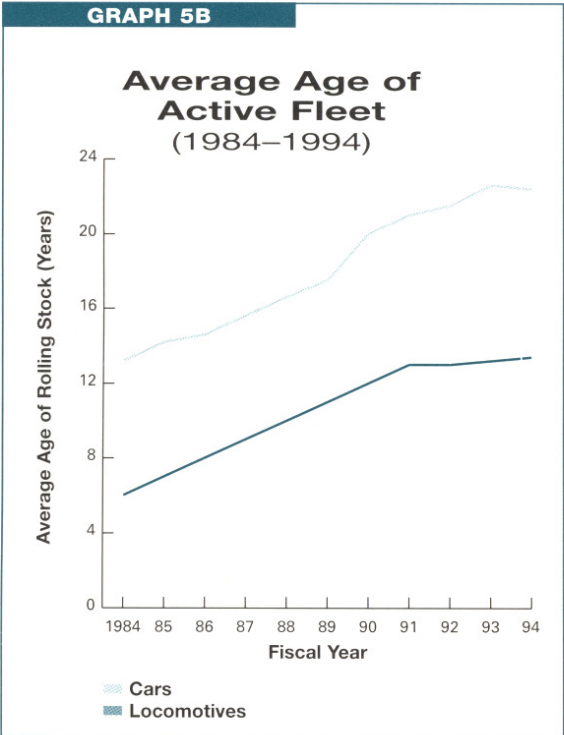
Fifth, ***we are optimizing the retained fleet and facilities across the most commercially viable routes and services.*** We are in the midst of reviewing our route structure to see if adjustments are advisable. Whatever changes are recommended will be consistent with the level of service

desired by federal, state, and local governments and their willingness to fund such service. We are tracking our labor productivity and rolling stock productivity and expect that decisions made in deploying capital assets will improve our productivity.

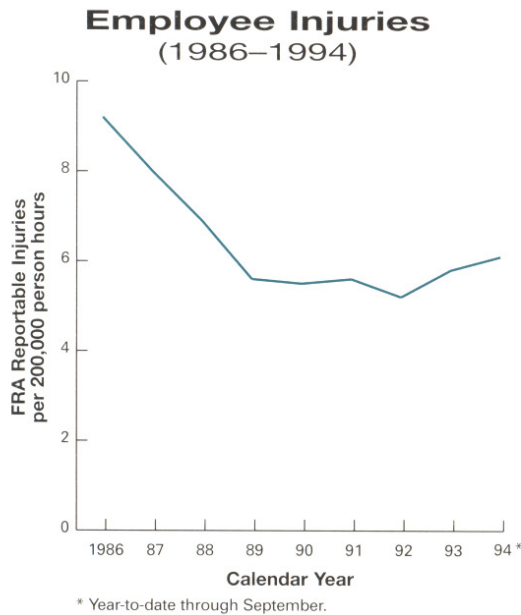
Finally, it goes without saying, that in making these strategic changes, **passenger and employee safety are always of pre-eminent importance.** Amtrak is far safer than automobile travel and as safe as airlines, and we will continue



It goes without saying, that in making these strategic changes, passenger and employee safety are always of pre-eminent importance.



GRAPH 7



to monitor this safety daily. We continue to track employee safety and are happy to report that Amtrak received its fifth straight E. H. Harriman award in recognition of our high level of employee safety. Amtrak had no passenger fatalities in the last 12 months.

As the accompanying graphs 3, 4, 6 and 7 indicate, part of making progress is quantifying and tracking our performance on an ongoing basis. We will reward business managers for our continued improvement along these dimensions. At the end of FY 1995, we will report back on our progress toward our goals.

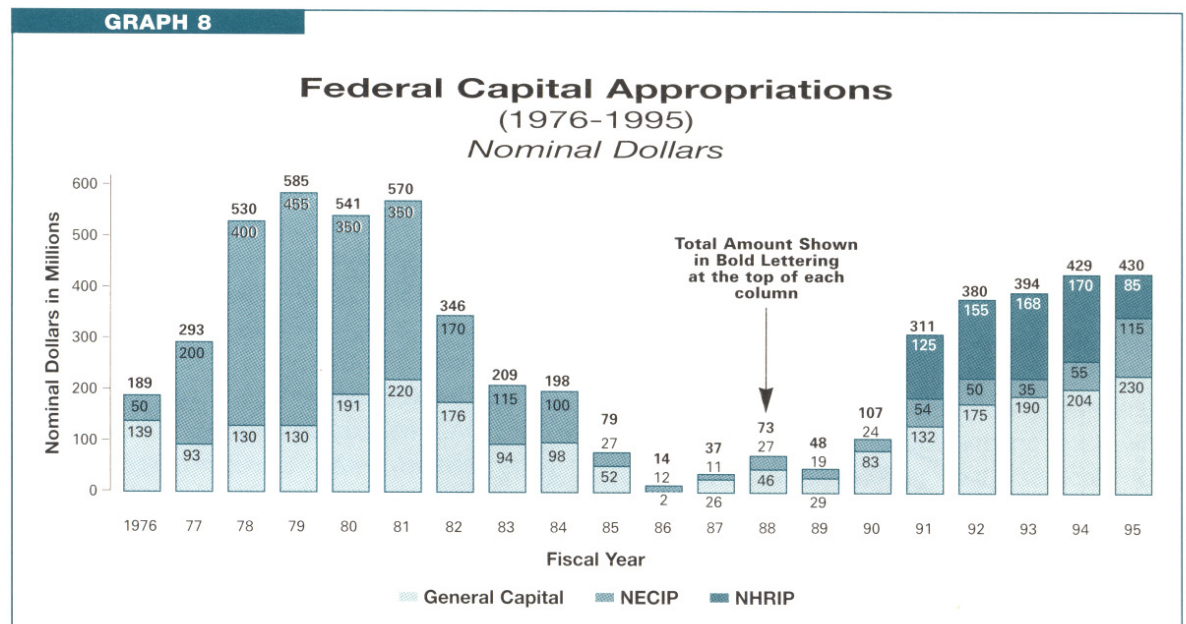
Capital

Amtrak inherited substandard infrastructure and rolling stock when it was created in the early seventies. While significant capital investments were made during the rest of that decade and into the early eighties, Amtrak's physical assets were never fully recapitalized.

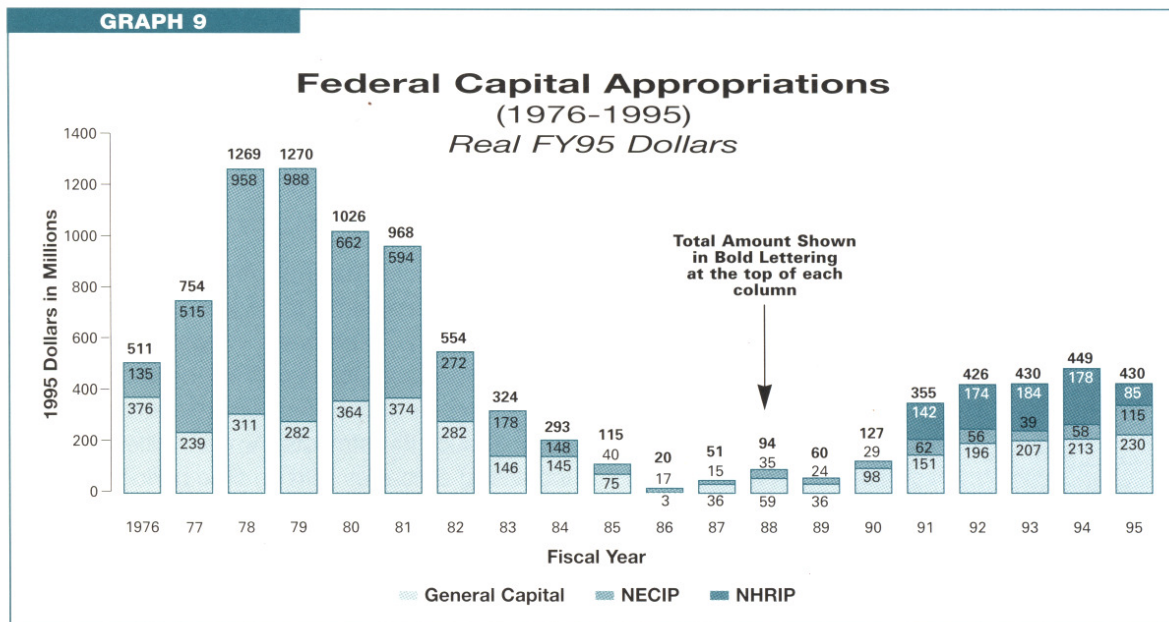
Moreover, those earlier investments, primarily in infrastructure and equipment, are now at the end of their useful life cycles and require reinvestment if Amtrak is to ensure a physical state of good repair with which to support its operations.

The primary source of Amtrak's capital funding comes from annual federal appropriations. Graph 8 presents annual capital appropriations from FY 1976 through FY 1995 in nominal dollars. As the graph reflects, substantial investments were made in Amtrak's assets in its early years, but dropped

GRAPH 8



GRAPH 9



precipitously in the 1980's. Capital funding began to increase in the 1990's, but has not reached a level that would allow Amtrak's infrastructure, facilities or passenger and locomotive fleet to be maintained in a state of good repair. In addition, as Graph 9 of federal appropriations in real dollars shows, the investment in the 1990's is much smaller than the investment in the 1970's (when adjusted for the effect of inflation).

The federal government has made a substantial investment of \$350 million in Amtrak's Northeast Corridor infrastructure from FY 1989 through FY 1994. However, this investment was inadequate. Amtrak estimates that its aging infrastructure required approximately \$1.2 billion of investment during this period, resulting in a capitalization shortfall (after federal dollars invested) of around \$850 million.⁸

Similar problems exist with respect to rolling stock. Amtrak's existing fleet is kept safe, but antiquated cars and locomotives lead to customer delays, ultimately affecting Amtrak's potential to generate income. Passenger cars and locomotives that have exceeded their useful lives not only break down more often, but take longer to fix and are more expensive to maintain.

Due to Amtrak's inability to renew the majority of its fleet, the average age of locomotives has grown steadily since 1984. Sixty-six percent of the locomotive fleet, or 223 of the 338 locomotives, are at or beyond the locomotive's typical useful life. The majority of passenger cars, excluding Heritage equipment, are half-way through or at the end of their life-cycles. Heritage cars, specifically, inherited by Amtrak in 1971, rebuilt, and still in use, average 13 years beyond their typical useful lives.

Amtrak will experience some relief to its aging fleet problem as 195 new *Superliners* are delivered and put into service. This order, though, fills only a portion of Amtrak's new equipment needs. To improve productivity, Amtrak should standardize its passenger cars and replace outdated locomotives.

The most serious aspect of undercapitalization is the unhealthy spiral it fosters. Unable to afford to fully modernize its fleet, Amtrak must redirect the bulk of its limited discretionary capital dollars into its old rolling stock to keep it safe and serviceable. By doing so, it leaves little room to acquire new equipment, and thus continues Amtrak's dependence on older equipment with resultant problems. The advanced technology in new

⁸ Initial estimate by Northeast Corridor SBU staff.

equipment permits better performance and lower maintenance costs. Without such new rolling stock, Amtrak's potential to improve equipment productivity and financial performance is limited.

Amtrak is further hampered in its ability to make asset investments for three reasons:

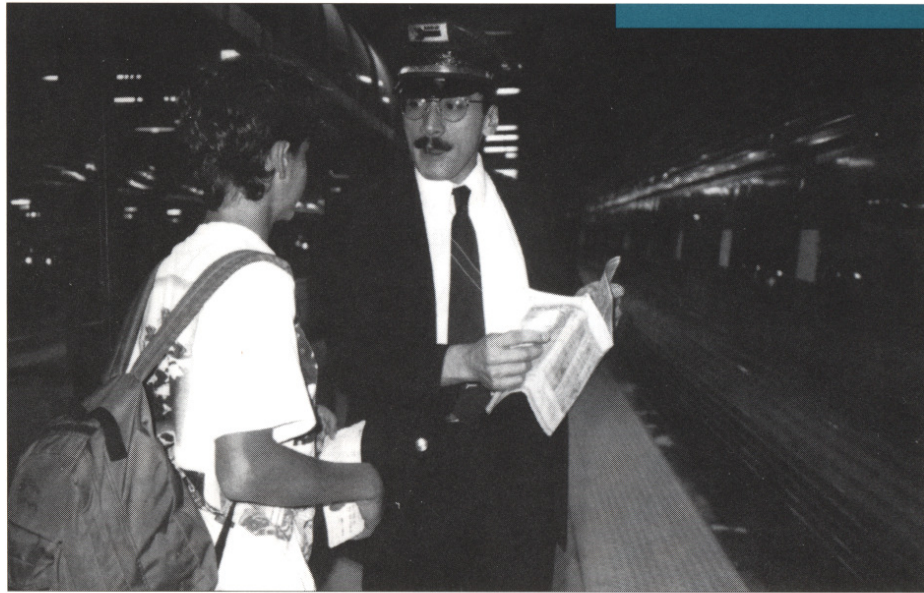
1. A growing portion of Amtrak's annual capital budget is required to meet unfunded legal mandates estimated to consume \$58 million of the \$230 general capital appropriation in FY 1995.
2. Increasing amounts of capital funds are required for previously approved projects such as debt service (principal payments) and other prior-year commitments (estimated to be \$56 million of the \$230 general capital appropriation in FY 1995).
3. Amtrak's ability to access private capital markets is limited by the lack of a dedicated capital funding source to pledge for debt repayment.

Amtrak's maintenance costs cannot be measurably improved and future revenue (attributable to lower levels of equipment reliability) cannot be made secure without acquiring new rolling stock. However, without significant increases in capital appropriations available for new investment, Amtrak is unable to modernize its aging fleet.

Amtrak estimates that it will require \$650 million per year⁹ to recapitalize its assets and keep them in good repair. These heavy investment requirements underscore the need for a dedicated and predictable funding source for Amtrak capital. Without such investments, Amtrak will experience increasing difficulties with on-time performance, maintenance costs, customer satisfaction, and consequently, Amtrak's potential to generate revenue.

⁹ Ten year forecast including costs for NECIP (the Northeast Corridor Improvement Project).

Highlights of 1994 at Amtrak



Customer Focus

In 1994, Amtrak conducted a baseline survey of 25,000 customers to gauge customer satisfaction. The results are being used to prioritize actions for improving customer service. Ongoing customer surveying will enable us to monitor progress.

Safety

“Trucker on the train”: In September, 1994, Amtrak commenced an education program to reduce grade-crossing accidents. “Trucker on the train” — cosponsored by Amtrak and a coalition of industry and government partners — put professional truck drivers in Amtrak locomotives, giving them an engineer’s view of highway-rail intersections and helping them learn the importance of stopping at grade-crossings.



Employee Safety: Amtrak received its fifth straight E.H. Harriman Award for its outstanding safety record during 1993. Amtrak, selected from among railroads whose employees worked 15 million or more hours in 1993, received the bronze medal for having the third lowest rate of injuries per hours worked.

Access for Americans with Disabilities: Amtrak installed bright-yellow tactile strips on platform edges at major stations; the strips alert passengers using canes or those with impaired eyesight to the edge of the platform.



Better Maintenance of Equipment

Toilets: Stemming from customer concerns identified in Amtrak's baseline customer survey, Amtrak's car maintenance teams redoubled efforts to meet passengers' expectations for sanitary restrooms. Car maintenance staff has developed a total-immersion process for toilets: toilets are removed from passenger cars and submerged in a special cleansing solution that reaches areas inaccessible by brush cleaning.

Car Winterization: The icy, snowy winter of 1993-94, taxed Amtrak personnel and led Amtrak's engineering to overhaul its winter maintenance program. Starting this summer, mechanical teams installed



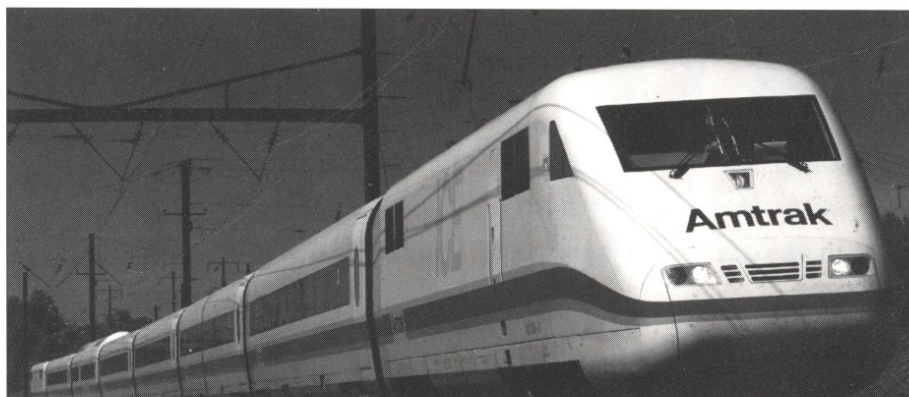
heaters on train car steps to reduce ice and snow build-up, and redirected heating ducts and insulated toilet plumbing to prevent pipe freezing. Horizon car sliding doors were replaced with swinging doors, removing the track that trapped ice and snow.



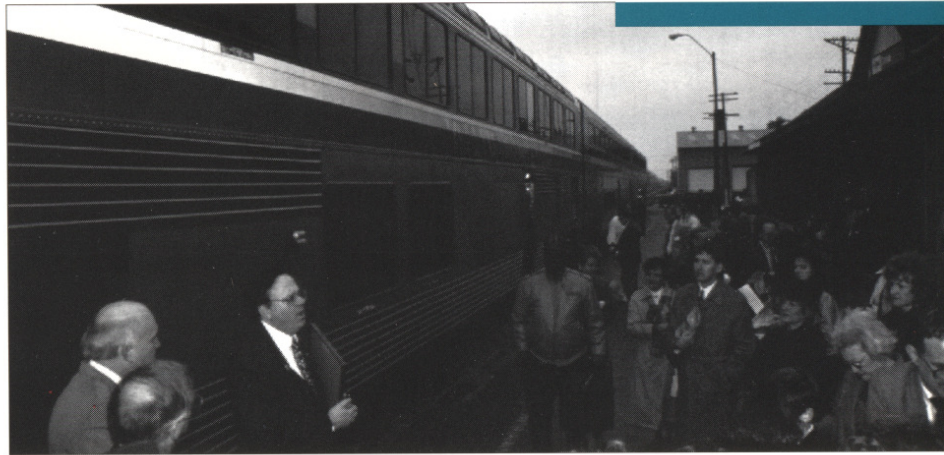
New Equipment

High-speed rail: In December of 1994, Amtrak completed the third and final phase of testing for new, higher-speed rail on the New York-Washington route. The commercial runs of the German Intercity Express (ICE) train

attracted record numbers of passengers and successfully tested a speed of 162 MPH. Four companies have been authorized to submit bids to supply 26 high-speed train sets. A contract will be awarded in 1995 and the first train will be delivered in 1997. The trains are expected to run at top speeds of 150 MPH on the Boston-Washington line.



Superliners: Sixty-five new double-level Superliner cars of a 195 car order were delivered to Amtrak in FY 1994: these 30 sleepers, 12 transdorms, 20 diners, and three lounges were placed into service on long-distance routes. Pictured, the “City of New Orleans,” offering service from Chicago to New Orleans, began using new Superliners in 1994. The luxurious cars feature first-class sleeping accommodations, lounge cars with giant viewing windows, and deluxe dining cars.



California cars: The prototype California locomotive (below) and the first California cars were delivered in the fall of 1994 to the State of California. The fleet will soon number nine locomotives and 113 passenger cars and carry thousands of daily commuters and intercity passengers. The California locomotive is among the most fuel efficient, quiet, and environmentally-friendly locomotives in service.



New Service

San Diego Commuter Service: Amtrak was selected in 1994 to operate a new commuter rail service between San Diego and Oceanside, California, commencing in February 1995. Amtrak will operate the nine station, 41-mile route for the San Diego Northern Railway under a 5-year \$25 million contract.

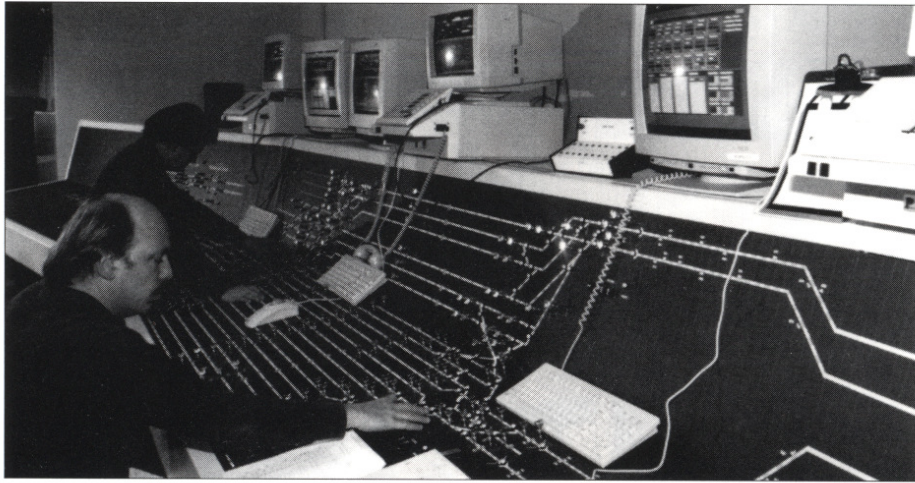
Talgo Train: Starting in April, 1994, Amtrak began operating state-of-the-art Talgo trains on the Seattle-Portland route, at the request of the Washington Department of Transportation. Spanish-made Talgo trains are among the most elegant and fastest trains in Europe and represent the first regularly scheduled high-speed passenger rail equipment employed in the Western United States. A special tilt mechanism allows the trains to navigate curves at high speed, ensuring a smoother, faster ride.



Improved Infrastructure

Beech Grove Maintenance Facility: Amtrak made further improvements to its major maintenance facility in Beech Grove, Indiana. The work includes improving the "transfer table" which routes passenger cars into 44 repair stations and upgrading 55-year old facility tracks. The overhaul will enable Amtrak to repair locomotives and cars more efficiently and reduce out-of-service car time.

Penn Station Control Center: The first phase of modernizing the Claytor/Scannel Control Center in New York City was completed, replacing Penn Station train control technology dating to the 1910's with



the latest technology. The center centralizes the control of trains throughout the Northeast, ensuring that trains can be routed and re-routed faster and more easily.

Management's Discussion and Analysis



1994 versus 1993

Amtrak's operating loss in 1994 was \$1,076.8 million. Amtrak experienced very high one-time costs in FY 1994 of \$243.7 million from the Amtrak restructuring, from a change in accounting principles that required recognition of future postretirement benefits in the year in which they accrued to employees,¹ and from a change in the formula used to compute casualty and accident liability costs. When these one-time costs are excluded from Amtrak's expenses, Amtrak's operating loss was \$833.1 million or 14% higher than in 1993. The primary causes of this operating loss increase were virtually flat revenues accompanied by expense increases of 5.3% (on a comparable basis to FY 1993).² Detail on revenue and expense variance is given below. However, at a macro level, total revenues rose 0.7% from \$1,403 million to \$1,413 million; gains in commuter revenue, 403(b) service, mail, and non-recurring one-time revenue were almost totally offset by a decline in passenger-related revenue. Expenses rose \$356 million from \$2,134 million in FY 1993 to \$2,490 million in FY 1994. \$243.7 million of this \$356 million increase was caused

by the one-time expenses noted earlier. The other \$112 million in expense increases are discussed in the "Expenses" section.

Federal direct support to Amtrak of \$351 million and federal payments for excess mandatory RRTA expenses of \$137 million reduced the operating loss to a "subsidized loss" of \$588.1 million.³

The changes from 1993 (and earlier years) to 1994 highlight several trends demanding action:

- The real expense reductions achieved over the last 17 years were small compared to our major competitors.
- Passenger-related revenues have declined in real terms for four consecutive years and, between 1993 and 1994, dropped by \$63 million in nominal dollars from \$943 million to \$880 million.
- The maximum cash deficit in 1994 was \$63 million but could be three times as large in 1995. Net of one-time nonrecurring sources of cash in 1994, the cash deficit would have been nearly \$100 million.⁴

¹ Amtrak elected to recognize all these postretirement costs for the prior years (1971-1993) in 1994 instead of amortizing them over a 20 year period.

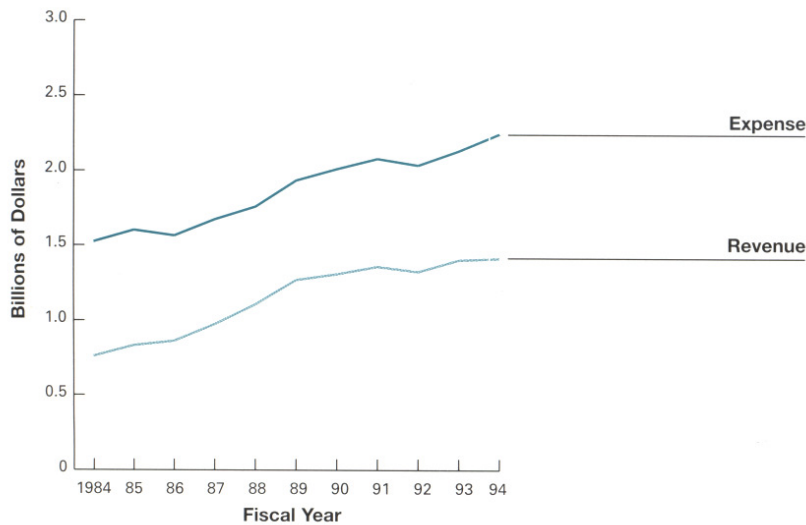
² Excluding the one-time charges in FY 1994 of \$71.5 million for restructuring, \$90.6 million for postretirement benefits, and \$81.6 million for casualty and accident liability.

³ As mentioned in a footnote in "Moving to a New Amtrak," the "budget result" (i.e., the "subsidized loss" excluding non-cash items like depreciation and retirement benefits) was \$77 million in 1994.

⁴ \$29 million in one-time revenue from the Lone Star concrete tie case settlement and other miscellaneous revenue.

GRAPH 10

Financial Performance (1984–1994)



Note 1: FY85 includes approximately \$6 million Chicago Union Station intercompany transactions

Note 2: FY94 expenses exclude \$243.8 million in one-time expenses.

■ While Amtrak has been successful in reducing real operating losses by 36.6% from 1977–1994,⁵ the cumulative impact of these losses over time is large. Total nominal operating losses for Amtrak have been more than \$7.4 billion in just the last ten years. Federal operating and capital subsidies have totaled \$6.6 billion. The difference reflects almost \$800 million in unfunded depreciation and other long-term liabilities.

Other long-ignored factors are finally being recognized as critical issues which Amtrak must address: the magnitude of passenger revenue foregone due to poor product quality and loss of market share; the excessive cost burdens (relative to the competition) associated with meeting statutory and regulatory requirements; the costs in reliability and service quality of chronic undercapitalization of plant and equipment; and the cost of operating with antiquated business practices and technology. While it is difficult to

precisely estimate the impact of these combined factors, recent customer survey data, consultant analyses, and internal cost and performance studies suggest that a large “economic drag” (of several hundred million in excess costs and foregone revenues) may be occurring.

Revenues

Passenger-related revenue (including transportation revenue and food and beverage revenue) dropped by 6.7% from \$943 million in FY 1993 to \$880 million in FY 1994. While it is difficult to precisely quantify the causes, several factors were at work. Passenger trips declined 1.0% from 22.1 million passenger trips in 1993 to 21.8 million in 1994.⁶ The extensive survey of Amtrak customers in 1994 highlighted baseline customer dissatisfaction with Amtrak’s quality of service. Sixty-one percent of customers surveyed experienced one or more complaints per trip. This perception of poor service leaves customers open to taking alternate means of transportation or suddenly deciding to no longer ride Amtrak. In addition, Amtrak experienced several other factors potentially driving customers to use other transportation providers or to not travel at all: air-fare competition, Amtrak derailments,⁷ severe winter weather, and continued mediocre on-time performance (partly Amtrak’s responsibility and partly the fault of freight railroads).

The decline in passenger trips was much larger in the long-distance segment where passenger trips dropped 11.3% from 6.2 million in 1993 to 5.5 million in 1994. In addition, the number of passenger miles overall dropped 4.5% from 6.2 billion in 1993 to 5.9 billion in 1994. This passenger mile total is the lowest since 1989.

The decline in passenger miles would likely have accounted for a decline of approximately 4.5% in revenue as well if other factors had not changed. But airline fare competition eroded Amtrak’s revenue, forcing Amtrak to institute promotional 55% off fares in FY 1994 and 2-for-1 Companion

⁵ If one-time expenses are excluded from FY 1994 expenses. Even including these one-time expenses of restructuring costs, postretirement benefits, and casualty and accident liability costs, real operating losses decreased 18.1% from FY 1977 to 1994.

⁶ This 1.0% decline as reported actually represents a 2.9% decline in rail passenger trips. The discrepancy is accounted for by Amtrak separately ticketing the segments of interconnecting bus-rail trips and hence counting each as two trips.

⁷ None of these derailments has been deemed by the National Transportation Safety Board to have been caused by Amtrak.

fares starting Labor Day 1994. Final implementation of the more restrictive no-smoking policies in May is estimated by some to have cost the company an additional \$2 million per month in lost revenue.

Commuter-related revenue (from commuter operations and commuter fees for use of Amtrak's right of way) increased 10.3% from \$246.3 million in 1993 to \$271.8 million in 1994. The commuter business continues to be a highly successful operation for Amtrak. Amtrak recently signed a *contract* to operate the San Diego commuter train service and now runs all the contracted commuter trains in the United States except for one. Amtrak has continued to receive on-time incentive payments for exceeding the on-time standards in the contracts with these commuter train agencies. Amtrak management believes that commuter-related revenue holds significant further growth potential.

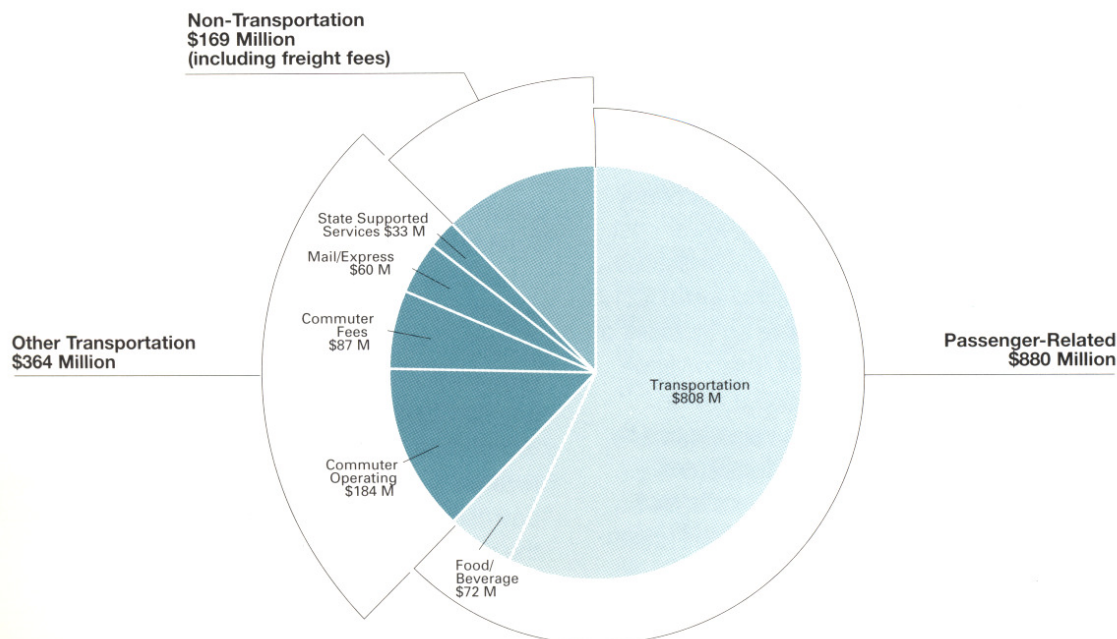
Commuter operating revenue increased from \$162.2 million in 1993 to \$184.3 million in 1994.

Most of this \$22.1 million increase was the result of three commuter operating contracts: those with MBTA (Boston), Metrolink (located in the Los Angeles metropolitan area), and the Peninsula Commute Service (in the Bay Area of Northern California). MBTA revenues increased \$9.0 million corresponding to increased capital work performed for the MBTA. Metrolink revenue increases of \$10.4 million were driven by extension of a rail line to Lancaster and work done for Metrolink after the earthquake to rebuild the rail system and upgrade it for faster passenger service. Revenues from the Peninsula service (PCS) rose \$2.8 million due to increased capital work requested by PCS. Other commuter operating revenue contracts experienced only minor increases or decreases in revenue.

Commuter fees revenue⁸ increased from \$84.2 million in 1993 to \$87.5 million in 1994. The increase was primarily attributable to increased revenue from SEPTA (the Southeastern Pennsylvania Transit Authority), New Jersey Transit, and the Baltimore & Ohio Railroad.

GRAPH 11

Sources of Revenue (FY 1994) Total \$1413 Million



⁸ Revenue received for use of Amtrak's right of way by commuter rail companies.

SEPTA revenue increased \$0.7 million from \$24.5 million to \$25.2 million; the increase was half attributable to inflation in Amtrak's contract with SEPTA and half attributable to increased payments to Amtrak since SEPTA incurred more train miles than were in the contract with Amtrak. New Jersey Transit's revenue increased from \$40.3 million to \$41.9 million or \$1.5 million; Amtrak's new contract with New Jersey Transit provided for a \$2.1 million increase in fees, which was partially offset by a \$0.6 million reduction in electrical propulsion costs billed to NJ Transit. Revenue from Baltimore & Ohio increased \$0.9 million primarily due to higher level of activity by the B&O.

403(b) state subsidies increased 26.4% from \$25.8 million in 1993 to \$32.6 million in 1994. These state subsidies vary inversely with Amtrak's performance as these payments are a partial reimbursement, tied to the level of Amtrak unrecovered short-term or long-term avoidable costs. \$5.1 million of the \$6.1 million reimbursement increase stemmed from Amtrak's declining ridership. The other \$1.0 million of reimbursement increase was driven by two factors: \$0.5 million of increase was driven by Amtrak installing wheelchair lifts on common carrier buses for the state of California; and \$0.5 million of the increase was driven by two new trains being added mid-year in FY 1994 from Los Angeles to Santa Barbara, California.

Mail, baggage and express revenue increased 13.1% from \$52.6 million in 1993 to \$59.5 million in 1994. Amtrak's *mail* business has continued to expand at a healthy rate because Amtrak offers the U.S. Postal Service a high quality, lower cost means of transporting mail (largely second class mail) effectively. Mail revenue has increased \$21.3 million from FY 1990 to FY 1994 or an increase of 61.7%. Between 1993 and 1994, mail revenue increased from \$49.0 million to \$55.9 million. Most of this \$6.9 million increase was caused by four contracts signed with the United States Postal Service to convert Amtrak periodic mail business into regular mail contracts. \$0.7 million of the increase was mail revenue received in 1994, that corresponded to mail delivered in 1993. A strong program to deliver mail at Christmas time brought in an additional \$0.5 million of mail revenue relative to the 1993 level.

Finally, \$0.3 million of the increase was a rate increase which Amtrak received under its USPS contract. *Express* revenue rose from \$3.4 million in 1993 to \$3.5 million in 1994, corresponding to an Express rate increase (of 3% in general) and flat volumes. *Baggage* revenue was flat; it was \$0.2 million in 1993 and 1994. There were no baggage rate increases from 1993 to 1994.

Freight Railroad Operating Fees increased 3.1% from \$16.1 million to \$16.6 million. Revenue from Conrail decreased by \$0.6 million from 1993 to 1994 reflecting decreased activity over Amtrak-owned rail. Delaware and Hudson revenue increased \$1.0 million from 1993 to 1994. The revenue from other freight railroads was relatively flat from 1993 to 1994.

Reimbursable revenues increased 16.2% from \$55.0 million to \$63.9 million. Most of the increase stems from increased Maintenance of Way support for Long Island Railroad, New York City, New Jersey Transit, Massachusetts Department of Public Works, and other miscellaneous agencies in Massachusetts. Amtrak undertook more projects for Long Island Railroad and New York City in 1994 than 1993. In 1994, Amtrak signed on to New Jersey Transit's "New Initiatives" agreement and continued to do other work for New Jersey Transit. For the Massachusetts Department of Public Works, Amtrak's project volume greatly increased in 1994 due to support work for the Central Artery Project.

Real Estate Operations and Development revenues decreased 7.9% from \$41.7 million in 1993 to \$38.4 million in 1994. The U.S. Postal Service is building a new postal facility next to Amtrak's Chicago Union Station; in FY 1993, Amtrak received \$5.8 million from the Postal Service for right of way payments and for work done by Amtrak personnel. The revenue from this project was minimal in FY 1994 since the project work is done. Partially offsetting this \$5.8 million revenue decline was \$2.3 million of first-time revenue received from parking revenue and lease payments from retail outlets on the ground floor of the new Chicago South Parking garage for Chicago Union Station.

Interest revenue increased 21.2% from \$3.3 million to \$4.0 million. This \$0.7 million increase was caused by accrual of interest on the Long Island Railroad joint venture of \$0.9 million, partially offset by declines on income from Amtrak's investment portfolio (due to declining interest rates).

Safe Harbor revenue decreased 2.4% from \$8.5 million in 1993 to \$8.3 million in 1994. The payments are dictated by a safe harbor payment schedule agreed to between Amtrak and a lessor of equipment in the early 1980's to provide contingent payments for long-term leases through a trust. Amtrak's draw on this fund has decreased because of declining interest rates and because the interest on the remaining principal balance has declined as the balance declines.

Other revenue increased 257.9% from \$10.7 million in 1993 to \$38.3 million in 1994. This increase reflects one-time revenue from a settlement of the Lone Star tie litigation; Amtrak had sued Lone Star (the manufacturer of concrete ties for Amtrak's Northeast Corridor) for defective ties.

Expenses

Train Operations expenses increased 3.8% from \$491.7 million in 1993 to \$510.4 million in 1994. Of the \$18.7 million increase from 1993 to 1994, \$15 million was the result of higher labor and benefits costs for Amtrak's direct train operations. These cost increases resulted from contractual wage increases, the impact of severe winter weather, derailments, and annualization of new service (such as the extension of the Sunset Limited train to Miami).

\$10.9 million of Train Operations expense increases stemmed from increases in commuter services operations for California (Metrolink and PCS) and the MBTA which are described in the "Commuter Operating" revenue section above. Labor costs increased in all areas due to contractual wage increases, particularly the 11% increase with the United Transportation Union effective October, 1993.⁹ Metrolink experienced an increase in operations and ridership stemming from FEMA-covered services offered in the wake of the Los Angeles earthquake; this level of service may not continue in the future. In addi-

tion, FY 1994 Train Operations reflect a full year of costs for service on the *Sunset Limited* begun mid-year in FY 1993 and thus triggering higher cost levels in FY 1994.

Partially offsetting these \$25.9 million of expense increases were expense decreases of \$7.2 million from 1993 to 1994. On-time performance payments made to freight railroads decreased \$3.1 million due to the freights' poorer performance in FY 1994 in ensuring that Amtrak trains were on-time. Passenger inconvenience costs (incurred because of late Amtrak trains) declined \$2.3 million from an extraordinarily high FY 1993 level; however, these passenger inconvenience costs are still \$5 million higher than Amtrak had budgeted in 1994. In addition, the cost of power decreased \$2.2 million from FY 1993 levels as a result of lower power rates. Finally, there was a \$1.1 million decline in miscellaneous other areas such as train fuel, small tools, and other costs.

Maintenance of Equipment expenses increased 1.5% from \$422.9 million in 1993 to \$429.2 million in 1994. Of the \$6.2 million increase from 1993 to 1994, \$5.5 million was the result of higher labor and benefits costs for Amtrak's direct train operations. These cost increases resulted from a 3% contractual wage increase, the impact of severe winter weather (leading to increased overtime and use of parts), derailments, and other factors.

\$4.0 million (or 64% of the Equipment Maintenance Cost increase) resulted from Commuter activities (reflected in Commuter revenue); some is due to labor increases from a 3% contractual wage increase; the remainder reflects the direct impact of increased commuter services for Metrolink and Maryland Department of Transportation (which added four frequencies on the Penn line and added four train sets on the CSX line).

Partially offsetting these cost increases, facility expenses declined \$1.5 million. In addition, in accordance with accounting principles, the increased capitalization of major maintenance allowed Amtrak to transfer overhead associated with this maintenance into the capitalized maintenance cost accounts.

⁹ This 11% increase was a retroactive increase for the two prior years in which there was no wage increase.

Maintenance of Way expenses increased 6.5% from \$220.6 million in 1993 to \$234.9 million in 1994. The entire increase in Maintenance of Way is directly associated with work performed by Amtrak for other parties. The MBTA and Metrolink required \$7.0 million of maintenance of way work in 1994 (these costs were reimbursed to Amtrak on a cost-plus basis and are found in the \$22.1 million increase in Commuter Operating revenue). Also Amtrak did \$9.6 million of work in 1994 on the Long Island Joint Venture which is reimbursed to Amtrak through Reimbursable revenue. Amtrak's direct operating expenses for Maintenance of Way actually decreased by some \$2.3 million relative to FY 1993 costs as a result of Amtrak personnel being redeployed on these reimbursable projects.

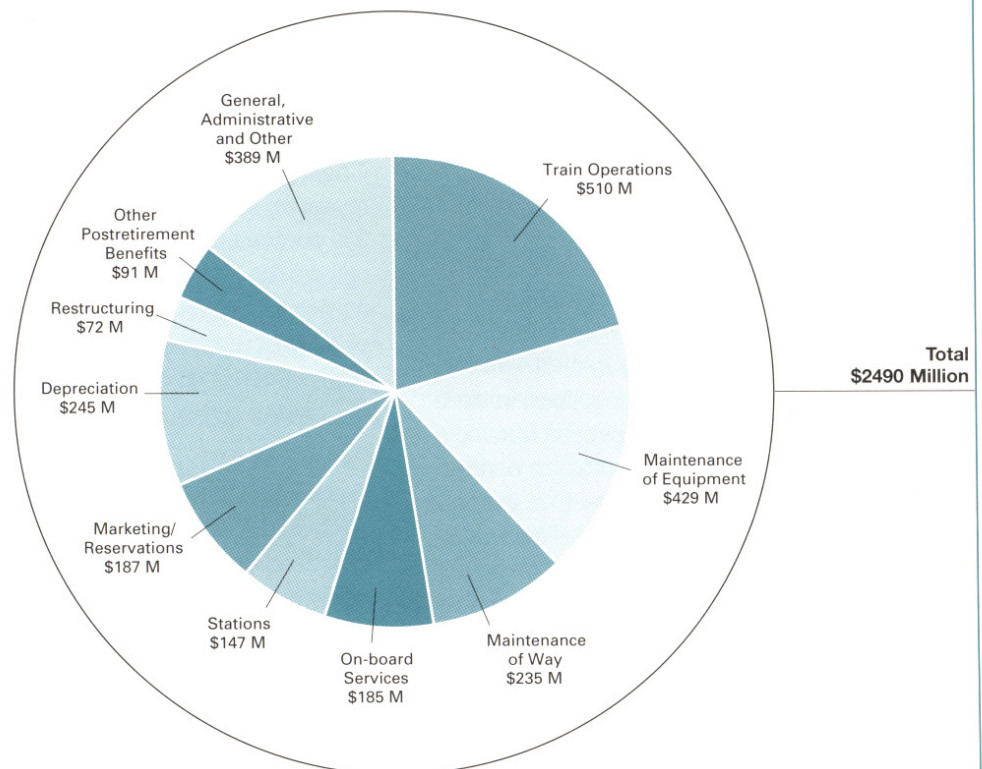
On-board Services expenses increased 1.8% from \$181.8 million in 1993 to \$185.2 million in 1994. This \$3.3 million increase was accounted for by the 3% contractual labor increase on October 1, 1993; this added \$3.5 million to Amtrak's labor and benefit costs. Also FY 1994 reflects a full year

of operation of the Sunset Limited train extension to Miami; FY 1993 only shows six months of operation. These increases were offset by reductions in overtime from FY 1993 (which had very high overtime costs stemming from the mid-Western floods).

Station Services expenses increased 2.3% from \$143.4 million in 1993 to \$146.6 million in 1994. This \$3.2 million increase was driven by cost increases at 30th Street Station and Washington Union Station. Philadelphia's 30th Street Station incurred \$2.3 million of costs more than FY 1993 to operate a station office and support retail operations. 30th Street Station also incurred \$1.9 million of costs more than FY 1993 (in building material and building maintenance) to improve the facility to house retail shops and transfer the property to a Property Manager. Partially offsetting these increases, passenger inconvenience for emergency exchange vouchers was \$0.5 million lower in FY 1994 than in 1993, reflecting a lower level of vouchers for inconvenienced passengers from a high FY 1993 level.

GRAPH 12

Expense Categories (FY 1994)



Marketing and Reservation Services expenses increased 0.9% from \$185.6 million in 1993 to \$187.3 million in 1994. Most of the increase is traceable to a \$3.1 million advertising and sales promotion for the year-end fare program to generate ridership and reverse declining passenger revenue. In addition, specific other costs increased \$0.9 million: professional fees (\$0.2 million), relocation expenses (\$0.2 million), and delivery/distribution expenses (\$0.5 million). Professional fees increased to pay for the TARP Baseline Customer Survey and Service Review. Relocation expense increases are a function of opening a new Reservation Sales Office in Corona, California. Delivery/distribution expense increases are costs of delivering express packages to customers for which Amtrak is reimbursed.

Partially offsetting these cost increases, Marketing and Reservation Services costs decreased \$2.5 million in reduced commissions to travel agents. These cost decreases are the function of lower ticket sales.

General Support expenses increased 13.9% from \$131.8 million in 1993 to \$153.1 million in 1994. The \$21.3 million increase was driven primarily by \$10.8 million of first-time postretirement benefits and \$8.8 million in additional costs from the outsourcing of information services' data processing and communications functions. In addition, union health insurance costs increased \$4.8 million (or 4.8%) from 1993 to 1994; premium rate increases accounted for 1.5% of this 4.8% increase and the remainder was caused by an increase in the number of employees covered.

Postretirement Benefits expense is a one-time cumulative charge of \$90.6 million to effect a change in the accounting for postretirement benefits. In the first quarter of FY 1994, Amtrak adopted the provisions of Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions" which is further discussed in Note 9 in the Financial Statements on page 39.

Insurance, Taxes, and Interest expenses increased 82.4% from \$99.7 million in 1993 to \$181.9 million in 1994. A one-time expense of \$81.6 million for casualty and accident liability was the major cause of the increase. In addition, interest expenses increased \$10.5 million from 1993 to 1994, largely as a result of increased rolling stock equipment deliveries, such as Superliners. The cost of federal train fuel taxes also increased \$2.6 million, due to federal rate increases. Offsetting most of these increases, charges to claims insurance dropped \$14.5 million from 1993 to 1994 reflecting lower expectations of personal injury and property claims in 1994.

Depreciation expenses increased 18.8% from \$206.3 million in 1993 to \$245.1 million in 1994. \$9.6 million of the increase from 1993 to 1994 is accelerated depreciation for rebuilt locomotives retired in earlier years. \$5.7 million of the increase is for first-time depreciation of the Northeast Highspeed Rail Improvement Project. \$6.9 million of the increase is for depreciation on new AMD locomotives and Superliner II cars. A \$10.7 million write-off was taken in 1994 for computer equipment related to the outsourcing of various information services functions. The remainder of the increase is net depreciation adjustments, including retirement of old Heritage, Metroliner, and switching cars in FY 1994.

Restructuring Costs expenses are a one-time cost of \$71.5 million in 1994 associated with Amtrak's corporate restructuring. The costs are \$33.1 million for a voluntary employee buyout package for 600 management positions, \$37.7 million in equipment retirement, and \$0.7 million for administrative and support costs.

General and Administrative expenses increased 7.9% from \$50.1 million in 1993 to \$54.4 million in 1994. This \$4.3 million increase is primarily driven by an increase in legal fees of \$2.6 million associated with the Saraland accident at the end of FY 1993 and labor-related cost increases of \$1.6 million from 1993 to 1994.

Impact of Restructuring on Reporting Financials

As part of Amtrak's restructuring, Amtrak is moving toward reporting expenses and revenues on a strategic business unit (SBU) basis. Although the Northeast Corridor (NEC) SBU did not officially start operations until October, 1994, costs and revenues have been assigned to the NEC. 54.2% of revenue in FY 1994 (or \$766.4 million) and 41.2% of Amtrak's costs (or \$1,026.6 million) would have been the NEC's; these costs do not include the allocation of corporate overhead costs to the NEC.

To understand the economics of our constituent businesses, Amtrak has prepared profit and loss statements for the following businesses: Commuter Contract; Mail and Express; and AutoTrain. While these P&Ls will be incorporated into SBU-level reporting in our annual reports, they are being used internally to guide strategic decision-making.

Cash

Amtrak's underlying cash position was extremely strong in the late eighties and early nineties (due to large amounts of one-time revenues from real estate and business developments, very favorable interest rates, and generally strong passenger revenue performance). Since that time average annual monthly cash balances have decreased from more than \$390 million to less than \$40 million. Amtrak's cash position is now being further weakened by the impact of federal OMB and CBO scoring constraints on federal capital drawdowns. This year for the first time, short-term private borrowing of \$63 million was necessary to pay payroll and vendors in the last two months of the fiscal year. Without substantive changes in operations (such as implementation of the 1995 business plan), the cash shortfall is predicted to grow in the coming years. Immediate action is being taken to stop the cash drain and return to cash surpluses: we have reduced spending through a voluntary management headcount reduction, and we are examining route structure, service delivery, and equipment utilization for further cash savings.

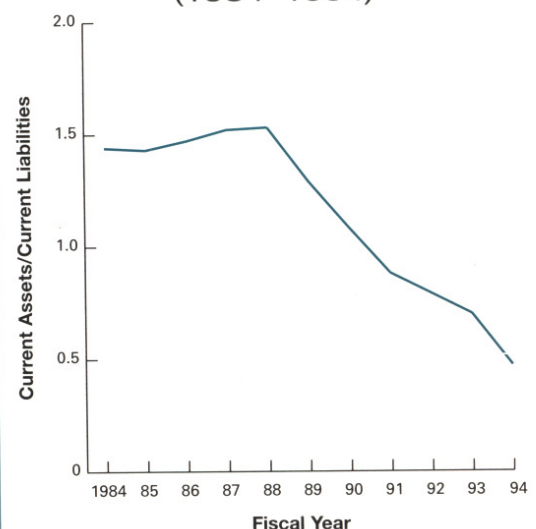
The deficit in working capital increased from \$100.7 million in 1993 to \$227.2 million in 1994. \$32.2 million of this change reflects management's effective reduction in inventories and accounts receivable. \$49.6 million of this change is due to the establishment of a reserve to record the cost of corporate restructuring taken in FY 1994. An additional \$37.2 million of this change is due to an increase in current debt and capital lease obligations. Graph 13 shows the decrease in the working capital ratio from FY 1984 to 1994; this decrease is due largely to the decline in cash balances discussed previously, and an increase in accrued liabilities and short-term debt.

From cost recovery ratio to operating ratio

Congress set a benchmark for Amtrak's success of achieving a 50% or better "cost recovery ratio." The definition and calculation of the ratio has changed over time. Even if it had been constant, this financial target would never have provided long-term financial success for Amtrak without ongoing massive federal, state, and local assistance.¹⁰ The "costs" reflected in the cost recovery ratio include only 80% of Amtrak's total expenses.

GRAPH 13

Working Capital Ratio (1984–1994)



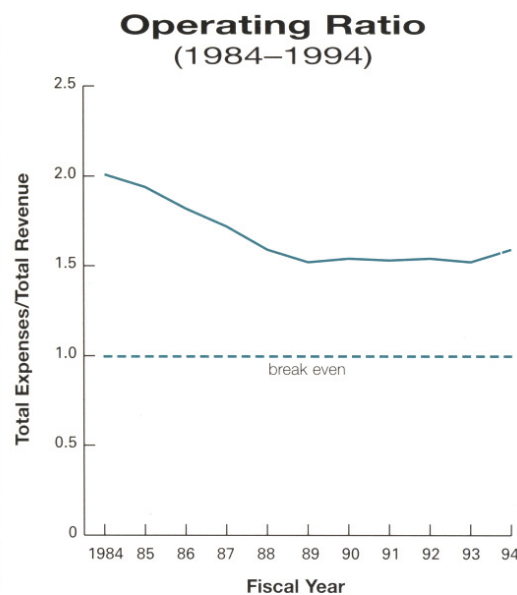
¹⁰ The cost recovery ratio measures Amtrak's ability to cover certain expenses with its revenue. The expenses included are total expenses less RRTA payments by the federal government, less federal contribution, less depreciation and other non-cash expenses, less certain 403(b) operating losses.

Amtrak and Congress' focus on short-term avoidable costs and short-term avoidable losses, have impeded Amtrak's ability to act commercially. Many routes that appear profitable on a short-term avoidable cost basis are not profitable when one examines long-term avoidable costs or fully allocated costs. Even the Rail Passenger Services Act (which established Amtrak) set a "short-term avoidable loss per passenger mile" standard that must be met in order for Amtrak to eliminate train service to an area. The loss standard is so high that none of Amtrak routes has qualified. Amtrak believes that by focusing on operating ratios, we can make decisions that are more commercially-driven.

A second example of the problems of short-term avoidable costs is 403(b) service: service provided at the request of states. Amtrak is compensated for 403(b) service based upon a proportion of either short- or long-term avoidable contributions or losses as calculated by the company's cost allocation system. In this system – the Route Profitability System – total short-term avoidable costs equal less than 40% of Amtrak's FY 1994 total expenses and long-term avoidable costs equal less than 50% of Amtrak's FY 1994 total expenses (excluding FY 1994 one-time expenses).

Amtrak has now been in existence for nearly a quarter century and has gone through what for any other capital intensive transportation service company would have been the equivalent of at least one full life cycle. Nevertheless, the long-term variable and "fixed" costs of the system as a whole have never been squarely addressed either internally or externally. Moreover, the consequences of that lack of long-term focus are now clearly catching up with the system.

GRAPH 14



Amtrak has shown improvement under the "cost recovery" ratio yardstick; Amtrak increasingly raised its cost recovery ratio from 56% in fiscal year 1984 to 80% in FY 1993. The cost recovery ratio slipped in fiscal year 1994 from 80% to 77%.¹¹ Nevertheless, for the reasons stated above, during this same period, the more instructive financial indicator—its operating cost ratio [the ratio of total expenses to total revenue]—improved from 2.01 in 1984 to 1.52 in 1993, but then slipped to 1.59 in FY 1994,¹² an increase of 4.6% over 1993. GAO recommended that "all relevant costs, both capital and operating, should be included in any performance measurement."¹³ Amtrak agrees, and in the future, plans to track its financial progress using the operating cost ratio indicator.

¹¹ On a comparable basis (excluding one-time FY 1994 costs of \$243.7 million for restructuring, postretirement, and casualty and accident liability).

¹² On a comparable basis (excluding one-time FY 1994 cost).

¹³ General Accounting Office testimony before the Subcommittee on Transportation, Committee on Appropriations, House of Representatives on March 17, 1994.

Consolidated Balance Sheets

Assets

September 30,
1994

September 30,
1993

(Thousands of dollars)

Current Assets:

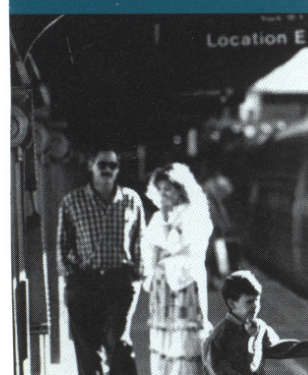
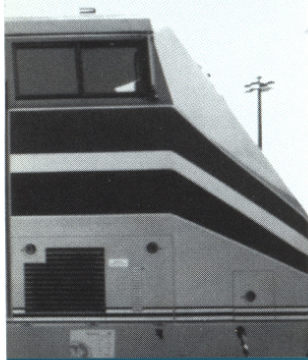
Cash and cash equivalents	\$ 23,800	\$ 25,436
Accounts receivable, net of allowance for doubtful accounts of \$4,224 and \$3,158 in 1994 and 1993, respectively	60,103	68,134
Materials and supplies	110,384	134,571
Other current assets	4,974	5,512
Total current assets	199,261	233,653

Property and Equipment:

Property and equipment	6,453,203	6,046,689
Less—Accumulated depreciation and amortization	(2,175,202)	(2,011,534)
	<u>4,278,001</u>	<u>4,035,155</u>

Other Assets and Deferred Charges:

Escrowed proceeds from sales of tax benefits	44,571	51,093
Deferred charges and other	71,292	73,394
	<u>115,863</u>	<u>124,487</u>
Total assets	\$ 4,593,125	\$ 4,393,295



Liabilities and Capitalization
**September 30,
1994**
**September 30,
1993**
(Thousands of dollars)
Current Liabilities:

Accounts payable	\$ 144,361	\$ 149,617
Accrued expenses and other current liabilities	131,018	120,196
Deferred ticket revenue	12,491	12,740
Restructuring charge reserve	49,586	—
Current debt and capital lease obligations	89,036	51,806
Total current liabilities	426,492	334,359

Long-Term Debt and Capital Lease Obligations:

Capital lease obligations	491,540	268,442
Equipment and other debt	189,743	172,053
	<u>681,283</u>	<u>440,495</u>

Other Liabilities and Deferred Credits:

Casualty reserves	142,103	58,501
Deferred revenue—sales of tax benefits	44,571	51,093
Advances from railroads and commuter agencies	27,568	49,345
Postretirement employee benefits obligation	110,743	4,779
Environmental reserve	32,975	—
Other	13,027	17,812
	<u>370,987</u>	<u>181,530</u>
Total liabilities	1,478,762	956,384

Commitments and Contingencies

Capitalization (see Consolidated Statements of Changes in Capitalization)	3,114,363	3,436,911
Total liabilities and capitalization	\$4,593,125	\$4,393,295

The accompanying notes are an integral part of these consolidated balance sheets.

National Railroad
Passenger Corporation
and Subsidiaries
(Amtrak)



Consolidated Statements of Operations

For the Years Ended September 30,

1994

1993

(Thousands of dollars)

Revenues:

Intercity related	\$ 972,089	\$1,021,384
Commuter related	271,813	246,346
Other	<u>169,489</u>	<u>135,250</u>
Total revenues	<u>1,413,391</u>	<u>1,402,980</u>

Expenses:

Train operations	510,397	491,712
Maintenance of equipment	429,183	422,900
Maintenance of way	234,903	220,561
On-board services	185,174	181,844
Stations	146,613	143,402
Marketing and reservations	187,298	185,595
General support	153,050	131,838
Restructuring charges	71,503	—
Taxes and insurance	149,965	79,113
Depreciation and amortization	245,078	206,325
General and administrative	54,408	50,104
Interest	<u>31,955</u>	<u>20,560</u>
Total expenses	<u>2,399,527</u>	<u>2,133,954</u>
Loss before cumulative effect of accounting change	986,136	730,974
Cumulative effect of change in accounting for postretirement benefits other than pensions	<u>90,646</u>	<u>—</u>
Net loss	<u>\$1,076,782</u>	<u>\$ 730,974</u>

The accompanying notes are an integral part of these consolidated statements.

Consolidated Statements of Cash Flows

For the Years Ended September 30,

1994

1993

(Thousands of dollars)

Cash Flows From Operating Activities:

Net loss	\$(1,076,782)	\$(730,974)
Adjustments to reconcile net loss to net cash used in operating activities:		
Cumulative effect of change in accounting for postretirement benefits other than pensions	90,646	—
Provision for restructuring charges	70,996	—
Depreciation and amortization	245,078	206,325
Provision for inventory loss and obsolescence	6,100	13,600
Provision for losses on accounts receivable	7,200	3,100
Retirement and unemployment taxes paid by Federal Railroad Administration	137,000	146,000
Other	—	705
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	1,627	(11,924)
Decrease (increase) in materials and supplies	18,087	(1,599)
Decrease (increase) in other current assets	538	(621)
(Increase) decrease in other assets and deferred charges	(19,954)	13,800
Increase in accounts payable, deferred ticket revenue, and accrued expenses and other current liabilities	5,317	14,332
Increase (decrease) in other liabilities and deferred credits	105,221	(17,962)
Net cash used in operating activities	(408,926)	(365,218)

Cash Flows From Investing Activities:

Purchases and refurbishments of property and equipment	(322,686)	(296,167)
Proceeds from disposals of property and equipment	14,767	1,454
Cash released from restricted proceeds of tax benefits sales	8,312	8,513
Net cash released for capital spending	20,683	26,591
Cash investments	(61)	(990)
Proceeds from dispositions of cash investments	61	990
Net cash used in investing activities	(278,924)	(259,609)

Cash Flows From Financing Activities:

Proceeds from issuance of preferred stock	491,158	465,000
Proceeds from federal paid-in capital	113,707	123,063
Proceeds from federal and state capital payments	11,570	12,759
Proceeds from debt and lease financings	124,995	57,725
Repayments of debt and capital lease obligations	(55,216)	(44,999)
Net cash provided by financing activities	686,214	613,548
Net decrease in cash and cash equivalents	(1,636)	(11,279)
Cash and cash equivalents—beginning of year	25,436	36,715
Cash and cash equivalents—end of year	<u>\$ 23,800</u>	<u>\$ 25,436</u>

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The accompanying notes are an integral part of these consolidated statements.

Consolidated Statements of Changes in Capitalization

	Preferred stock	Common stock	Other paid-in capital	Accumulated deficit	Total
<i>(Thousands of dollars)</i>					
Balance at September 30, 1992	\$7,650,089	\$93,857	\$4,305,940	\$ (8,631,179)	\$ 3,418,707
Issuance of preferred stock	465,000	—	—	—	465,000
Federal paid-in capital	—	—	269,063	—	269,063
Federal and state capital payments	—	—	15,115	—	15,115
Net loss	—	—	—	(730,974)	(730,974)
Balance at September 30, 1993	8,115,089	93,857	4,590,118	(9,362,153)	3,436,911
Issuance of preferred stock	491,158	—	—	—	491,158
Federal paid-in capital	—	—	250,707	—	250,707
Federal and state capital payments	—	—	12,369	—	12,369
Net loss	—	—	—	(1,076,782)	(1,076,782)
Balance at September 30, 1994	<u>\$8,606,247</u>	<u>\$93,857</u>	<u>\$4,853,194</u>	<u>\$(10,438,935)</u>	<u>\$ 3,114,363</u>

The accompanying notes are an integral part of these consolidated statements.

Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The financial statements reflect the consolidated operations of the National Railroad Passenger Corporation (Amtrak), its wholly-owned subsidiaries Chicago Union Station Company (CUS) and Washington Terminal Company, and its 99% interest in 30th Street Limited, L.P. (TSL). All significant intercompany transactions have been eliminated. Certain reclassifications have been made to the prior year's statements to conform with the 1994 presentation.

Ticket Revenue

Ticket sales are recognized as operating revenues when the related transportation services are furnished. Tickets which have been sold but not used are presented as "Deferred ticket revenue" in the Consolidated Balance Sheets.

Contracted Services

The Consolidated Statements of Operations include the gross revenues earned and expenses incurred under arrangements to operate various commuter rail services, to provide access to the Northeast Corridor and other Amtrak-owned facilities, and to perform services for freight railroads.

Fuel Swaps

Amtrak enters into fuel swap arrangements as a hedge against train fuel market price fluctuations. Gains and losses result to the extent that fuel market prices differ from the swap strike price. Realized and unrealized gains and losses are included in "Train operations" in the Consolidated Statements of Operations.

Cash Equivalents

Amtrak considers all financial instruments purchased with a maturity of three months or less to be cash equivalents.

Materials and Supplies

Materials and supplies, which are stated at weighted average cost, consist primarily of items for maintenance and improvement of property and equipment.

Property and Depreciation

Property and equipment are stated at cost, and are depreciated over their estimated useful lives using the composite straight-line method. Under this method, ordinary gains and losses on dispositions are recorded to accumulated depreciation. Property acquired through capital lease agreements are recorded as assets and are amortized over their estimated useful lives or the lease terms.

Casualty Losses

Provision is made for Amtrak's portion of the estimated liability for unsettled casualty and accident claims. The current portion of this liability is included in the Consolidated Balance Sheets under "Accrued expenses and other current liabilities." The non-current portion is classified as "Casualty reserves." As of September 30, 1994 and 1993, the current claims liability included in accrued expenses and other current liabilities was \$55,600,000.

During 1994, Amtrak changed its method of estimating the unsettled casualty and accident liability from a method that estimates the year-end liability based on recent payments for similar claims to an actuarial method that estimates the future payments to be made after September 30, 1994 for all incidents occurring prior to that date. This change resulted in an additional charge of \$82 million to earnings in 1994. This charge is included in the Consolidated Statements of Operations under "Taxes and insurance."

National Railroad
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Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

NOTE 2: FEDERAL AND STATE FUNDING

Funds are provided to Amtrak through federal and state payments for operations and for capital acquisitions and improvements. For funds received from the federal government, Section 304 of the Rail Passenger Service Act (45 U.S.C. 544) requires Amtrak to issue to the United States Secretary of Transportation preferred stock equal in par value to all federal operating payments and most federal capital payments received subsequent to October 1, 1981, as well as capital and certain operating payments received prior to that date. Public Law 103-331, approved on September 30, 1994, provides \$972,000,000 in federal funds to Amtrak for fiscal year 1995, of which \$392,000,000 is for operating purposes, and the balance for capital acquisitions and improvements, and designated mandatory passenger rail service payments.

Federal paid-in capital, included in the Consolidated Statements of Changes in Capitalization, includes certain funding received from the federal government to finance acquisition of and improvements to property and equipment. In exchange for past and prospective funding, Amtrak issued two promissory notes to the United States. The first note matures on November 1, 2082, with successive 99-year renewal terms, and is secured by certain Amtrak rolling stock. The second note matures on December 31, 2975, and is secured by Amtrak's real property. Neither of the notes bears interest, unless prepaid (which Amtrak does not intend to do). The federal government's security interest in Amtrak's real property and certain rolling stock entitles it to repayment plus interest in the event Amtrak ceases operations, is acquired by another entity, or seeks relief under bankruptcy or insolvency laws.

Federal paid-in capital also includes payments made on Amtrak's behalf by the Federal Railroad Administration (FRA). During the years ended September 30, 1994 and 1993, the FRA deposited \$137,000,000 and \$146,000,000, respectively, with the Internal Revenue Service in payment of Amtrak's excess Railroad Retirement Tax Act tax liabilities, excess Railroad Unemployment Repayment Tax payments, and excess Railroad Unemployment Insurance Act payments.

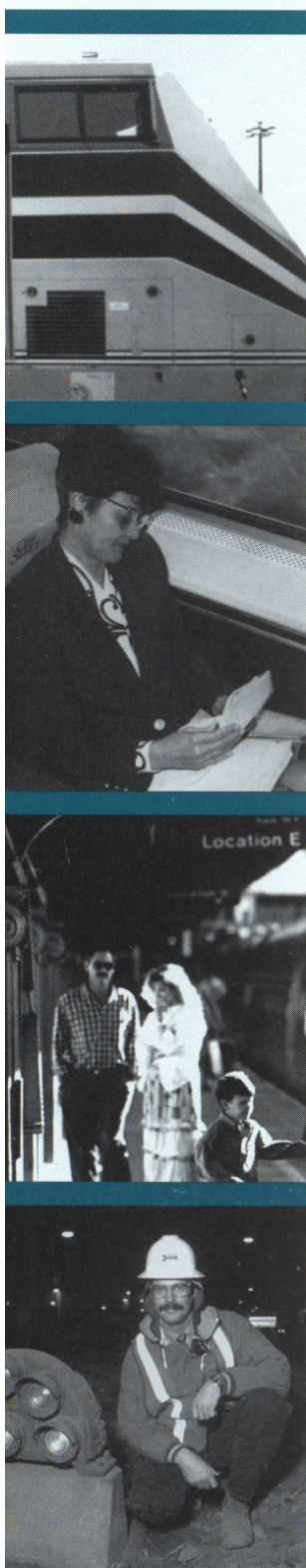
Amtrak remains dependent upon federal subsidies for a portion of its operations and most of its capital improvements. During the past five years, Amtrak has experienced operating costs in excess of revenues and federal funding for operations causing a deterioration of working capital and cash flow problems. While management instituted cost reductions and had success in controlling cost increases, passenger related revenues generally have not increased sufficiently over the past several years to offset the cost increases experienced, and have declined since 1993. Furthermore, management has projected that continuing at the 1994 operating and staffing levels would significantly worsen the working capital and cash position in 1995. Therefore, the operating plan for 1995 includes strategies to enhance revenues, reduce costs, implement route service adjustments, increase unsecured lines of credit, and as discussed in Note 12, to vigorously develop and implement a restructuring of the corporation to increase revenues and reduce costs to make them more consistent with expected resources, and to increase productivity.

NOTE 3: PREFERRED AND COMMON STOCK

At September 30, 1994, 86,062,478 shares of \$100 par value preferred stock were authorized, all of which were issued and outstanding. On October 31, 1994, 3,440,000 shares were issued at par value increasing the total number of authorized shares issued and outstanding to 89,502,478. At September 30, 1993, 81,150,895 shares were authorized, all of which were issued and outstanding. All issued and outstanding preferred shares are held by the Secretary of Transportation for the benefit of the federal government. Dividends are to be fixed at a rate not less than 6% per annum, and are cumulative so that no dividends may be paid on the common shares prior to the payment of all accrued but unpaid dividends on the preferred shares. No dividends have been declared. The preferred stockholder is also entitled to a liquidation preference over common shares involving a payment of not less than par value plus all accrued unpaid dividends. Each share of preferred stock is convertible into 10 shares of common stock at the option of the preferred stockholder.

At September 30, 1994 and 1993, 10,000,000 shares of \$10 par value common stock were authorized, of which 9,385,694 shares were issued and outstanding.

National Railroad
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Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

NOTE 4: PROPERTY AND EQUIPMENT

Total fixed assets presented in the Consolidated Balance Sheets consisted of the following at September 30, 1994 and 1993 (in thousands):

	1994	1993
Locomotives	\$ 584,975	\$ 513,445
Passenger cars	1,627,267	1,431,548
Other rolling stock	98,240	99,713
Right-of-way properties	2,979,610	2,846,390
Other properties	966,665	961,434
Leasehold improvements	196,446	194,159
	6,453,203	6,046,689
Less—Accumulated depreciation and amortization	(2,175,202)	(2,011,534)
Net property and equipment	<u>\$ 4,278,001</u>	<u>\$ 4,035,155</u>

NOTE 5: BORROWING ARRANGEMENTS

Total equipment and other debt presented in the Consolidated Balance Sheets consisted of the following at September 30, 1994 and 1993 (in thousands):

	1994		1993	
	Current	Long-term	Current	Long-term
Equipment obligations	\$ —	\$ 72,162	\$ —	\$ 86,751
Credit agreements	68,500	15,000	38,000	21,000
Notes payable	5,540	43,079	—	—
Bonds	—	30,000	—	30,000
Construction loan	4,670	16,885	4,670	21,555
UDAG loan	130	12,617	130	12,747
	<u>\$78,840</u>	<u>\$189,743</u>	<u>\$42,800</u>	<u>\$172,053</u>

In 1991, Amtrak entered into an agreement with a manufacturer for the construction of 140 passenger cars. In December 1993, Amtrak exercised an option to have 55 additional cars constructed. Under the terms of a loan agreement with a third-party lender, Amtrak borrows funds in the form of advances made by the lender to the manufacturer toward the base order cars' and option cars' construction. Interest on amounts advanced is being charged to Amtrak during construction, is payable quarterly, and is being capitalized. Interest capitalized during the years ended September 30, 1994 and 1993 totaled \$8,350,000 and \$8,367,000, respectively. Principal repayments of all outstanding advances pertaining to the 140 base order cars are due in 80 consecutive quarterly installments commencing the earlier of when the last base order car is delivered or June 30, 1996. Principal repayments of all outstanding advances pertaining to the 55 option cars are due in 80

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Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

consecutive quarterly installments commencing the earlier of the third month following the last option car's delivery or September 30, 1997. Currently, reductions to principal owed are taking place as portions of principal relating to delivered cars are then refinanced under a separate capital leasing arrangement. During 1994, such principal reductions totaled \$101,292,000 relating to 65 delivered cars. Altogether, Amtrak has taken delivery of 67 cars at September 30, 1994. All amounts borrowed by Amtrak under the remaining debt are secured by those finished passenger cars not yet refinanced under the capital leasing arrangement.

Amtrak and CUS have \$115,000,000 of unsecured lines of credit with banks expiring in December 1994, which are subject to certain conditions. Borrowings under these agreements bear interest based on the London Interbank Offered Rate (LIBOR), Eurodollar rate, certificate of deposit rates, prime rate, or rate offered by the lender. Amtrak pays various fees on its credit lines. At September 30, 1994, Amtrak and CUS had \$62,500,000 in outstanding draws under these agreements. Under a credit agreement, Amtrak has a \$21,000,000 outstanding balance at September 30, 1994, bearing interest at the LIBOR. This amount is being repaid in \$1,500,000 quarterly installments through March 1998.

Under a term note, Amtrak has a \$11,115,000 outstanding balance due at September 30, 1994, bearing interest at the LIBOR. This amount is being repaid in \$585,000 quarterly installments through June 1999. In December 1993, Amtrak acquired a parking facility located in Chicago in exchange for a \$20,000,000 promissory note bearing fixed rates of interest and due in full in December 2003. The seller has secured a mortgage on the facility as well as an irrevocable unconditional \$4,000,000 letter of credit as collateral.

In September 1994, CUS converted \$17,504,000 of long-term advances payable into a noninterest bearing note payable. The note is being repaid in \$3,200,000 annual installments each October 31st through 1997, and on November 2, 1998. The remaining balance is then due on November 1, 1999. Amtrak is guaranteeing payment of all amounts due.

Included in TSL's long-term debt at September 30, 1994 are \$30,000,000 of Philadelphia Authority for Industrial Development tax-exempt private-activity bonds (Bonds) issued for the benefit of TSL's rehabilitation of 30th Street Station (Station) in the city of Philadelphia, Pennsylvania (City). The Bonds were issued on December 30, 1987, mature on January 1, 2011, and bear interest at a fixed or variable rate as stipulated in the bond indenture. Interest is payable until maturity at intervals determined under provisions in the bond indenture. No amortization of bond principal prior to maturity is required. Amtrak is required to make annual deposits into a sinking fund to be used to pay off the bonds when they mature. As of September 30, 1994 Amtrak's aggregate deposits into the fund were \$900,000. Since the Bonds are subject to optional tender by the bondholders, TSL has executed a Liquidity Facility which provides funds to purchase the Bonds surrendered under the optional tender provisions.

TSL has a construction loan agreement which at TSL's option bears interest at the LIBOR or the prime rate. Principal repayment is due in annual installments each April to be paid in full by November 17, 1998. The loan is secured by a leasehold mortgage on TSL's right and interest in the Station.

TSL has an obligation to the City under an Urban Development Action Grant (UDAG) loan agreement as of September 30, 1994. Principal is being repaid in \$130,000 annual installments each November 29th through 2011 with the balance due on November 29, 2012. The City's rights under the UDAG loan agreement are secured by a leasehold mortgage. The UDAG loan bears no interest.

The weighted average interest rate on all interest-bearing borrowings was 5.9% and 6.1% per annum at September 30, 1994 and 1993, respectively.

Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

At September 30, 1994, scheduled maturities of long-term equipment and other debt over the next five years were as follows:

Year Ending September 30	Amounts (In Thousands)
1995	\$ 78,840
1996	16,742
1997	17,359
1998	15,067
1999	9,755
Thereafter	<u>130,820</u>
	<u>\$268,583</u>

NOTE 6: LEASING ARRANGEMENTS

Capital Leases

Amtrak leases items of equipment, primarily passenger cars and locomotives, under capital leasing arrangements. At September 30, 1994 and 1993, the gross amount of assets recorded under capital leases was \$557,483,000 and \$301,303,000, respectively, with accumulated amortization of \$69,296,000 and \$46,738,000, respectively. At September 30, 1994, future minimum lease payments under capital leases were as follows:

Year Ending September 30	Amounts (In Thousands)
1995	\$ 43,352
1996	49,052
1997	42,154
1998	43,493
1999	47,442
Thereafter	<u>716,003</u>
	941,496
Less amount representing interest	<u>439,760</u>
Present value of minimum lease payments at September 30, 1994	<u>\$501,736</u>

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Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

Operating Leases

At September 30, 1994, Amtrak was obligated for the following minimum rental payments under operating leases that have initial or remaining noncancelable lease terms in excess of one year:

Year Ending September 30	Amounts (In Thousands)
1995	\$ 6,944
1996	6,935
1997	6,704
1998	6,692
1999	6,254
Thereafter	<u>38,736</u>
	<u>\$72,265</u>

Rent expense for the years ended September 30, 1994 and 1993 was \$24,140,000 and \$23,227,000, respectively.

NOTE 7: CONTINGENCIES

Amtrak is involved in various litigation and arbitration in the normal course of business. While the outcome of these matters cannot be predicted with certainty, it is the opinion of management and counsel that the disposition of these matters will not materially affect Amtrak's consolidated financial statements.

Amtrak has self-insured certain risks with respect to losses for third-party liability and property damage. Insurance coverage for liability losses from \$25 million to \$100 million is provided by insurance companies owned by Amtrak and various other railroads and transit authorities.

NOTE 8: ENVIRONMENTAL MATTERS

Some of Amtrak's past and present operations involve activities which are subject to extensive and changing federal and state environmental regulations which can give rise to environmental issues. As a result of its operations and acquired properties, Amtrak is from time to time involved in administrative and judicial proceedings and administrative inquiries related to environmental matters.

In 1976, Amtrak acquired its Northeast Corridor properties. These properties had been occupied and used for many years by a railroad which had declared bankruptcy during the early 1970's. It is Amtrak's policy to capitalize recoverable remediation costs for properties acquired with existing environmental conditions. During fiscal year 1994, Amtrak established a \$33 million reserve for sites where environmental agencies have initiated legal action, where Amtrak has held discussions with environmental agencies regarding remediation and other possible actions, or where management has concluded that Amtrak will have to perform remedial actions. This reserve is based on Amtrak's present estimate of the costs it will incur related to these sites. Amtrak has not recorded any receivables for recoveries from other parties or from insurance because such recoveries are not sufficiently certain.

Amtrak's management and counsel believe that additional future remedial actions that might be taken or required, if any, will not be material to Amtrak's financial position.

Notes to Consolidated Financial Statements

For the Years Ended September 30, 1994 and 1993

NOTE 9: RETIREMENT BENEFITS

Pension Plan

Amtrak has a qualified noncontributory defined benefit retirement plan held in trust covering nonunion employees and certain union employees (Plan). Benefits are based on years of credited service, and the employee's average compensation during the five highest consecutive years. Amtrak's funding policy is to periodically contribute amounts recommended by outside actuaries. Pension expense for 1994 and 1993 was \$4,371,000 and \$4,345,000, respectively. Included in the 1994 expense are a \$659,000 curtailment gain and \$3,769,000 in termination benefits resulting from restructuring activities. These items are reflected as components of total restructuring charges (Note 12). The following tables set forth the Plan's funded status, amounts recognized in the Consolidated Balance Sheets at September 30, 1994 and 1993, and components of the net pension expense for 1994 and 1993 (amounts in thousands):

	1994	1993
Actuarial present value of benefit obligations:		
Accumulated benefit obligation, including vested benefits of \$67,753 and \$57,357, respectively	<u>\$ 68,572</u>	<u>\$ 58,089</u>
Plan assets at fair value, primarily fixed income investments and listed stocks	\$ 97,021	\$ 95,801
Projected benefit obligation for service rendered to date	<u>90,269</u>	<u>85,501</u>
Plan assets in excess of projected benefit obligation	6,752	10,300
Unrecognized prior service cost being amortized over 11.8 years	4,205	5,009
Unrecognized net gain	(12,961)	(13,781)
Unrecognized net asset existing at October 1, 1986 being amortized over 11.6 years	<u>(3,827)</u>	<u>(4,872)</u>
Accrued pension expense recognized in Consolidated Balance Sheets	<u>\$ (5,831)</u>	<u>\$ (3,344)</u>
Net pension expense for 1994 and 1993 included the following components:		
Service cost—benefits earned during the period	\$ 4,045	\$ 4,233
Interest cost on projected benefit obligation	6,262	6,112
Actual return on Plan assets	(1,895)	(11,215)
Net amortization and deferral	(7,151)	5,215
Curtailment gain	(659)	—
Termination benefits	<u>3,769</u>	<u>—</u>
Net pension expense	<u>\$ 4,371</u>	<u>\$ 4,345</u>

The weighted average discount rate used in determining the projected benefit obligation was 8.0% in 1994 and 1993. The projected rate of increase in future compensation levels was 5.0% and 6.0% in 1994 and 1993, respectively. The assumed long-term rate of return on Plan assets was 8.00% and 6.25% in 1994 and

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1993, respectively. The unfunded accrued pension cost at September 30, 1986, is being amortized over the remaining average service life of Plan members, and \$1,127,000 and \$1,435,000 net of amortization, is included under "Postretirement employee benefits obligation" in the Consolidated Balance Sheets at September 30, 1994 and 1993, respectively.

Other Postretirement Benefits

Amtrak provides medical benefits to its retirees and life insurance to some retirees in limited circumstances. Substantially all salaried employees may become eligible for medical benefits if they meet the service requirement and reach the normal retirement age while still working for Amtrak. Company-provided medical benefits are reduced when covered individuals become eligible for Medicare benefits or reach age 65, whichever comes first. Medical benefits are subject to copayment provisions and other limitations. Amtrak continues to fund its postretirement benefits program on a pay-as-you-go basis. Cash payments on these benefits were \$1,679,000 and \$1,538,000 for 1994 and 1993, respectively.

In fiscal year 1994, Amtrak adopted the provisions of Statement of Financial Accounting Standards No. 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions." As part of adopting this standard, Amtrak elected to immediately recognize in the first quarter, a one-time, noncash transition obligation of \$90.6 million. This cumulative catchup adjustment as of October 1, 1993 represents the discounted present value of expected future retiree health and life insurance benefits attributed to employees' service rendered prior to that date. The effect of this change on fiscal year 1994 after recording both the cumulative effect for prior years and the current year's provision, was a noncash expense of \$101,403,000. As a result of restructuring activities, a \$6,194,000 curtailment loss was also recognized increasing the total noncash expense to \$107,597,000. The curtailment loss is reflected as a component of restructuring charges (Note 12). The pro forma effect of the change on years prior to fiscal year 1994 was not determinable. Railroad agreement employees' healthcare and life insurance benefits are covered by a separate multiemployer plan, and therefore are not subject to the provisions of this statement. The following tables set forth the liability recognized in the Consolidated Balance Sheet at September 30, 1994 and components of the net postretirement benefits expense for 1994 (amounts in thousands):

	1994
Accumulated postretirement benefit obligation:	
Former employees	\$ 38,964
Fully eligible active employees	22,029
Other active employees	<u>44,292</u>
Total postretirement benefits liability	<u>\$105,285</u>
Net postretirement benefits expense for 1994 included the following components:	
Service cost—benefits earned during the period	\$ 3,598
Interest cost on accumulated benefit obligation	7,159
Full transition obligation	90,646
Curtailment loss	<u>6,194</u>
Net postretirement benefits expense	<u>\$107,597</u>

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The weighted average discount rate used in determining the accumulated benefit obligation was 8.0%. For measuring the expected benefit obligation, a 12.5% annual rate of increase in the per capita claims cost was assumed for fiscal year 1994. This rate was assumed to gradually increase to 14% in 1997 and 1998, then decrease by 1.3% per year on average to 5% in 2005, and remain at that level thereafter. If the assumed healthcare cost trend rate were increased by one percentage point, annual net postretirement benefit expense and the related accumulated benefit obligation would both increase by \$17.3 million.

NOTE 10: SALE OF TAX BENEFITS

Pursuant to provisions of the Economic Recovery Tax Act of 1981, Amtrak sold the rights to the tax benefits associated with certain qualified assets. Cash proceeds from these sales plus accrued interest are subject to certain restrictions, and therefore are presented as a non-current asset and deferred revenue in the Consolidated Balance Sheets. Revenue is recognized to the extent restrictions have been lifted and funds released to Amtrak. For the years ended September 30, 1994 and 1993, Amtrak recognized revenue of \$8,313,000 and \$8,512,000, respectively, from these restricted funds.

NOTE 11: FAIR VALUE OF FINANCIAL INSTRUMENTS

For cash and cash equivalents, short-term cash investments, and accounts receivable, the carrying amount approximates fair value because of the short maturity of these instruments. The carrying amount of escrowed proceeds from sales of tax benefits also approximates fair value since all of the escrowed proceeds are invested in instruments having short maturities. The carrying amounts of the lines of credit, bonds, construction loan, and portions of notes payable and equipment obligations approximate fair value. All charge interest at rates that are periodically adjusted to market.

The estimated fair values of remaining equipment obligations and notes payable were based upon discounted cash flow analyses using interest rates available to Amtrak at September 30, 1994 and 1993 for debt with the same remaining maturities. Although by nature interest free, the UDAG loan was also valued based upon a discounted cash flow analysis using a September 30, 1994 market interest rate. The estimated fair values of these financial instruments are as follows (amounts in thousands):

	1994		1993	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Notes payable	\$48,619	\$35,761	—	—
Equipment obligations	\$72,162	\$67,281	\$86,751	\$105,489
UDAG loan	\$12,747	\$ 4,209	\$12,877	\$ 6,724

NOTE 12: RESTRUCTURING CHARGES

In 1994, Amtrak announced its plan for a major operational reorganization of the corporation around definable strategic business units (SBUs). The SBUs will focus accountability on train service which will provide better service to customers, increase operating performance, and effectively manage business performance. Amtrak has recorded restructuring charges in operations and has provided a reserve based on the best information available when the decision was made to undertake the restructuring activities. The 1994 restructuring plan includes a provision of \$33 million relating to severance and other personnel reduction costs, including \$12 million relating to net curtailment losses from the pension plan and the other postretirement benefit plan, and special termination benefits. The net curtailment losses recognize actuarial charges that otherwise might have been amortized over future periods and charges for supplemental benefits that cover employees from the dates of early retirement and severance to normal retirement age. Approximately \$29 million of the \$33 million

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personnel reduction charge will be disbursed in 1995 and the balance over the next six years. Substantially all of the \$38 million balance of the 1994 restructuring charge relates to the writedown of old and inefficient rolling stock which has been or will be disposed of as routes and services are adjusted.

NOTE 13: SUPPLEMENTAL CASH FLOW INFORMATION

For the years ended September 30, 1994 and 1993, Amtrak engaged in the following investing and financing activities that affected recognized assets, liabilities, and capitalization, but did not result in a change in cash and cash equivalents (amounts in thousands):

	1994	1993
■ Net reduction in obligation due to a third-party lender in connection with the construction and lease refinancing of passenger cars	\$ 14,589	\$ 418
■ Interest earned on escrowed proceeds of tax benefits sales	\$ 1,790	\$ 1,794
■ Expenditures made for projects along the Northeast Corridor from funds established specifically for those purposes	—	\$ 711
■ Capital lease obligations incurred in connection with the leasing of new equipment	\$233,369	\$ 84,010
■ Obligation reduced in connection with the return of conditionally purchased locomotives	—	\$ 3,666
■ Promissory note issued in connection with the acquisition of a parking facility	\$ 20,000	—
■ Federal paid-in capital from Federal Railroad Administration payments of excess retirement and unemployment taxes	\$137,000	\$146,000

Cash interest of \$24,273,000 and \$20,489,000 was paid during the years ended September 30, 1994 and 1993, respectively.

Management Report

Management is responsible for the preparation and integrity of the consolidated financial statements presented in this Annual Report. These statements have been prepared in accordance with generally accepted accounting principles applied on a consistent basis, except for the adoption of FAS 106, Employers' Accounting for Postretirement Benefits Other Than Pensions, and necessarily include some amounts that are based on management's best estimates and judgement. Management considers that the financial statements present fairly Amtrak's financial position, results of operations, and cash flows.

To meet its responsibility, management maintains a comprehensive system of internal controls, policies and procedures to assure the proper authorization of transactions, the safeguarding of assets and reliability of financial information. The system provides reasonable assurance, not absolute, that the related records fairly reflect all transactions in accordance with management's authorization, and are properly recorded so that reliable financial records are maintained and reports can be prepared. The concept of reasonable assurance is based on the recognition that the cost of a system of internal controls must be related to the benefits derived.

An important part of the internal controls system is Amtrak's intent to maintain a high standard of ethical conduct in all business activities. Internal accounting controls, operating controls, as well as a corporate rules of conduct and a business ethics policy, are documented and communicated to all levels of management.

The Board of Directors reviews the system of internal controls and financial reporting. The Board meets and consults regularly with management, the internal auditors and the independent accountants to review the scope and results of their work. The accounting firm of Price Waterhouse LLP has performed an independent examination of the financial statements and has full and free access to meet with the Board, without management representatives present, to discuss the results of the audit.



Thomas M. Downs
Chairman and President



Elizabeth C. Reveal
Chief Financial Officer

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Report of Independent Accountants

To the Board of Directors of
National Railroad Passenger Corporation

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of operations, cash flows, and changes in capitalization present fairly, in all material respects, the financial position of National Railroad Passenger Corporation (Amtrak) and its subsidiaries at September 30, 1994, and the results of their operations and their cash flows for the year then ended in conformity with generally accepted accounting principles. These financial statements are the responsibility of Amtrak's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with generally accepted auditing standards which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the opinion expressed above. The financial statements of National Railroad Passenger Corporation for the year ended September 30, 1993 were audited by other independent accountants whose report dated November 12, 1993 expressed an unqualified opinion on those statements.


As discussed in Note 2, Amtrak continues to experience deteriorating working capital and cash positions. In recognition of the current trends and projections, management has developed interim plans, entered into borrowing agreements, and commenced other actions intended to assure continued operations during 1995. In the longer term, management has begun restructuring Amtrak's operations as discussed in Note 12.

As discussed in Note 9 to the financial statements, Amtrak adopted FAS 106, *Employers' Accounting for Postretirement Benefits Other than Pensions* at October 1, 1993.

Price Waterhouse LLP

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