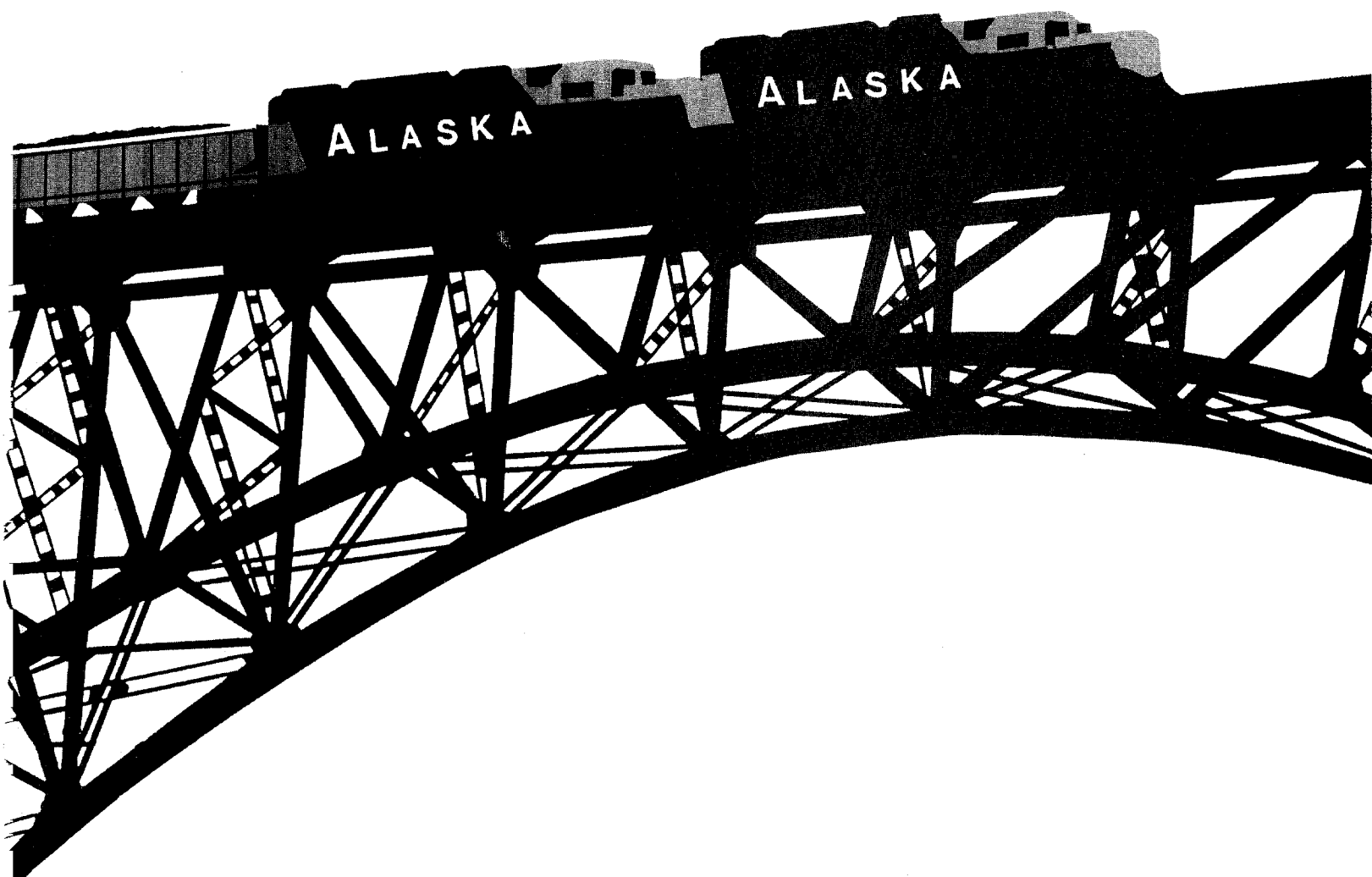

The Alaska Railroad and its Future



A Report by Commonwealth North

The Alaska Railroad and its Future

**A report by the Commonwealth North
Railroad Committee
April 1988**

Introduction

In January of 1988, the Board of Directors of Commonwealth North charged a seventeen-member committee to study the Alaska Railroad, present and future. The committee's assignment was to take a statewide view in examining:

The operations of the Alaska Railroad since the transfer from the federal government in 1985;

Whether or not the railroad should be sold to a private entity; and

How the railroad can be better utilized to assist with the diversification of the Alaska economy.

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Executive Summary

To appreciate fully the importance of the Alaska Railroad, it must be understood that Alaska is different from other states in that government owns vast tracts of land while the private sector owns little. This land contains substantial resources which, by the foresight of the founding fathers, was seen as the economic salvation of a rather small group of people in a huge and undeveloped territory.

The framers of Alaska's Constitution (Article VIII) specifically directed state government to develop and use these resources and to become the driving force in the management and development of the state's natural wealth for the benefit of Alaska's citizens.

With the advent of Prudhoe Bay, oil dwarfed other resource development initiatives, and state government did not address its responsibility to diversify Alaska's basic resource industries. Fortunately, the opportunity has not yet passed. In the Alaska Railroad, the state has an instrument with which to implement a pro-active program. It has the genesis of a transportation system which can be the beginning of a new era in Alaska.

In the Alaska Railroad, the state has the genesis of a transportation system which can be the beginning of a new era.

The major conclusions are as follows:

1. Since the transfer from the federal government three years ago, railroad management has brought a high degree of professionalism to a former governmental bureaucracy. The railroad has operated within its revenues and at no time has asked for additional funds from the legislature.
2. The leadership of Alaska must now accept the responsibility to fulfill the visionary purpose so eloquently stated in the 1914 law which established the Alaska Railroad.
3. With help from state government in terms of vision, financing and leadership, the railroad can assist with the challenge of truly diversifying Alaska's economy.

SECTION I

The History and Purpose of the Alaska Railroad

The Alaska Railroad has helped shape Alaska from a raw territory to a state with great, albeit mostly unrealized, potential.

The Alaska Railroad was created by a 1914 Act of Congress which was, in very real sense, visionary. The legislation was passed after an eloquent four-hour appeal to a joint session of Congress by Judge James Wickersham who envisioned the railroad as an instrument which would play a vital role in opening up the vastness of Alaska's wilderness. It would be a magnet to recruit pioneers of a future day to tap the enormous mineral resources of the land.

The Alaska Railroad Enabling Act (43USC 301) described the purpose of the railroad this way:

“...to connect one or more of the open Pacific Ocean harbors on the southern coast of Alaska with the navigable waters in the interior of Alaska, and with a coal field or fields so as best to aid in the development of the agricultural and mineral or other resources of Alaska, and the settlement of the public lands therein...and for other governmental and public uses, and for the transportation of passengers and property...”

In the intervening years, the Alaska Railroad has helped shape Alaska from a raw territory to a state with great, albeit mostly unrealized, potential. It has enjoyed a commanding presence in years of peace, war, depression and prosperity in southcentral and interior Alaska.

In the late 1970's the federal government proposed to transfer the railroad to the state. For six years Alaskans debated the pros and cons of assuming ownership of the railroad. Finally, with the signature of Governor William Sheffield on July 5, 1984, a value of \$22.3 million was placed on the facilities and details for the transfer were written in the federal Alaska Railroad Transfer Act. The Alaska Legislature responded by creating the Alaska Railroad Corporation Act of 1984. Alaska became the owner and operator of a railroad.

The state law addressed the role, mission and purpose of the railroad in this manner:

- “(1) It is the policy of the state to
- (A) provide safe, economical, and efficient transportation to residents, businesses, visitors, and military installations in the state;
 - (B) foster and promote the long-term economic growth and development of the state;
 - (C) develop and implement plans for a transportation network in the state;
 - (D) foster and promote the development of the state’s land and natural resources; and
- (2) The Alaska Railroad is an essential part of the state transportation network...”

The essential difference between the federal and state mission statements is that the federal act specifically described the purpose of the railroad. The State’s 1984 acceptance act outlined a policy but did not task the railroad with execution of that policy.

More specifically, under Article 2 of the 1984 legislation, neither management nor the Board of Directors was given the responsibility to implement the stated policies. Herein lies the basis for the lack of expansion orientation currently evident in the railroad’s operations and plans for the future. In addition, other than granting the railroad the right to issue bonds, there was no provision for how to access sufficient capital to undertake any growth efforts short of maintenance and upgrade of the rolling stock and track.

In other words, Alaska law, while touting a noble policy, created an inward-looking organization commissioned only to make itself self-sufficient.

While this might be appropriate in a mature economy, the Alaska Railroad was intended to have a more creative and nurturing role in this young, growing state.

Alaska law, while touting a noble policy, created an inward-looking organization.

Conclusion

Alaska's state policy, as written in the Alaska Railroad Corporation Act of 1984, is "to foster and promote resource development," however there is no clear and written mandate for the railroad to provide leadership in this area.

Recommendation

It is recommended that to remedy this situation, the legislature should amend the implementing legislation as follows:

Mission and Purpose of the Alaska Railroad

It shall be the purpose of the Alaska Railroad Corporation

- A. To provide safe and efficient transportation to residents, businesses, visitors and the military in the state, and
- B. In consonance with the plans and programs of the state
 - 1. To foster and promote the long-term economic growth of the state;
 - 2. To implement plans to open the state with a viable surface transportation network; and
 - 3. With sensitivity to legitimate regional and environmental concerns, to foster and promote the development of the state's land and natural resources.

This proposed mandate to the railroad to assume an active role in the development of the state represents a recognition of the railroad as a valuable resource and not just an entity solely oriented to making a profit.

Section II

The Long-term Role of the Alaska Railroad

Conclusion 1

In a frontier, developing area, especially in the Arctic, a rail system provides the best year-round, most cost-effective surface transportation network.

Conclusion 2

Opportunities for expansion of railroad services must be evaluated not just in terms of the railroad's balance sheet but on a total statewide benefits and costs basis.

Conclusion 3

The railroad has no staff, budget or mandate to examine and implement major rail extensions.

Conclusion 4

Alaska's primary rail corridors run north/south; therefore logical expansions of the rail line do not necessarily mean east/west extensions of track from the main line.

Conclusion 5

The most attractive extension proposals are those in which resources are taken by the shortest rail route directly to deep water ports.

Conclusion 6

When a pioneer surface link is deemed in the public interest, a railroad is the most attractive option from an environmental point of view as well as from the standpoint of minimizing disruption of rural communities and wildlife populations.

Conclusion 7

As railroads run in two directions, expansion of the transportation network will result in substantial economies to serviced areas. Freight and passenger capabilities will make goods and services currently prohibitively expensive more accessible.

Conclusion 8

In the long run, natural resource development is the best way to improve rural economies, provide jobs and support local peoples and their needs.

Conclusion 9

The obstacles to rail corridors placed in federal law are a great impediment to expanding Alaska's transportation system.

Recommendation 1

The legislature should create an Alaska Development Board* which, in conjunction with the Alaska Railroad Board of Directors, examines the feasibility of major rail extensions that would enhance the statewide economy.

Recommendation 2

The Development Board and the railroad should examine the eight extensions presented in this report and prioritize those which are feasible.

Recommendation 3

For more effective land use and improved operations, the central railyard in Anchorage should be moved to Eagle River and the railyard in Fairbanks studied for relocation.

Recommendation 4

The state administration and the legislature should review targeted resource commodities which require access to transportation systems in order to be competitive in world markets. State government should assist these industries through capital investments in rail infrastructure rather than subsidies through "development pricing" of freight rates.

Recommendation 5

The Federal access restrictions in Alaska should be examined by the state to see if these obstructions abrogate the intent of Alaska's Constitution and the Statehood Act.

(*see the Commonwealth North report, *Using the Permanent Fund as a Positive Counter-cyclical Force in the Alaska Economy*, February 1988)

One of the primary missions of the Alaska Railroad is to assist in the economic and resource development of the State of Alaska. Under federal ownership, the implementation of that congressional mandate lost its momentum after World War II. Now that the state owns the railroad and the Alaska Railroad Corporation has proven it can run the operation profitably, there are several promising courses of action which present themselves.

The Alaska Railroad has proven to be a key to the development of Alaska. Where the railroad goes, resource extraction and economic development follow. What's needed is a leadership structure and a philosophy which encourages the use of the Alaska Railroad for this purpose.

It is necessary for our leaders to look at how best to tap the tremendous wealth which lies in our land, resources and people by utilizing many tools, such as the railroad, with which to make the best use of this wealth. There are numerous opportunities for economic expansion listed in this section, few of which can be justified purely on the basis of railroad balance sheet analysis. What must be understood is that the railroad does not operate in a vacuum. Its actions and activities dramatically impact nearly all of Alaska and its people.

The following is a proposed benefits/cost model for analyzing potential railroad expansions. This model reflects the belief that in the real world we must look at all the benefits and costs which result from such investment.

Benefit/cost model for analyzing potential economic expansion

In deciding whether to embrace a particular economic expansion strategy for the railroad, a model must be utilized which addresses all benefits and costs accruing to the State of Alaska, not just the Alaska Railroad itself. "Economic expansion" is defined broadly as any increase of service, whether involving actual physical track extensions or providing major new services within the existing operations area.

This model assumes that the Alaska Railroad is an instrument to be used by the State of Alaska for the benefit of the people through the encouragement of economic development.

The railroad does not operate in a vacuum. Its actions and activities dramatically impact nearly all of Alaska and its people.

THE MODEL

Benefits

- B1 -** Direct operating revenue to the Alaska Railroad
- B2 -** Direct revenues to the state government
 - a. Royalty fees
 - b. Lease fees
 - c. Taxation
- B3 -** Direct revenues to local governments
 - a. Property taxes
 - b. Sales taxes
- B4 -** Indirect revenues to the state
 - a. Increased employment
 - b. Formation of successful businesses
 - c. Increased sales by existing businesses
 - d. Human resource development through job training and experience
 - e. Lower freight costs due to increased volumes

Costs

- C1 -** "First" cost of extension
- C2 -** Operations cost to Alaska Railroad of providing service
- C3 -** Increased fixed cost to Alaska Railroad of additional plant and equipment

$$\frac{\text{BENEFITS}}{\text{COSTS}} \geq 1$$

This model can be used to determine if a given expansion and/or extension project will derive benefits to the state which go beyond direct monetary returns to the railroad. The subjective value of benefits divided by costs should be a value greater than 1. In other words, the project should at least break even.

Leadership structure

Central to successful evaluation and promotion of expansion of the railroad will be a leadership structure which embraces the necessity for economic expansion in general and the resolve to accomplish it.

This leadership structure must have the authority to develop detailed plans and recommendations to be submitted to the governor and the legislature for approval. An Alaska Development Board* should be created to examine the feasibility and recommend major rail extensions that would assist the statewide economy. Once a plan for economic expansion of the railroad is developed and approved, then the Alaska Railroad administration must be charged with the responsibility to carry out the project.

Currently, the railroad has no staff, budget nor mandate to examine and implement major expansion. The legislature must assist with the financing strategy to cover the cost of a line extension or other major development. In essence, this is the seed money required to develop our country. Unless this type of arrangement is established, the Alaska Railroad will never grow beyond the original 541 miles of track which were laid down early in the century, and the state's healthy economic diversification will be forever stifled.

Taking the shortest route

In reviewing the possibilities for development options for the Alaska Railroad, one must keep in mind that the goal is not limited to improving the bottom line of the railroad's financial statements. Rather, the goal is the economic good of the State of Alaska. For this reason the committee has looked at numerous opportunities which from strictly a railroad income stream point of view might not be acceptable.

In reviewing opportunities for economic expansion of the railroad within the social, economic and political framework of all the diverse groups and regions involved in the State of Alaska, several conclusions become obvious. The first of these is the realization that in many cases the most logical expansion does not necessarily mean a contiguous extension of the existing track.

As mining engineers understand, rocks don't get pleasure out of riding on trains. The idea is to get them to water as quickly and inexpensively as possible because waterborne transportation is the least costly by far.

(*see the Commonwealth North report, *Using the Permanent Fund as a Positive Counter-cyclical Force in the Alaska Economy*, February 1988)

An Alaska Development Board should be created to examine the feasibility and recommend major rail extensions that would assist the statewide economy.

The most logical expansion does not necessarily mean a contiguous extension of the existing track.

Therefore, the most attractive development schemes are those in which resources are taken by the shortest route from mine sites or forests to deep water ports. In many cases, especially in Northwestern and Western Alaska, this means that noncontiguous sections of track are far more attractive than attempting to link up to the existing rail network.

Once this aspect of the situation is accepted, numerous possibilities for development railroads become feasible.

***Alaska's primary
rail corridors run
north/south as
opposed to
east/west.***

Another truism is that, in general, Alaska's primary rail corridors run north/south as opposed to east/west. This north/south pattern results from several conditions, one of which is that many of the major drainages which provide the best routes flow north/south or northeast/southwest. Secondly, but equally as important, is the already noted need to establish direct routes to natural port locations.

Access to Alaska's mineral potential

Mining in Alaska will generate annual gross sales of over \$1 billion by 1992. Projects which are in production now, committed to go to production or in the permitting stage include:

<u>Project</u>	<u>Projected Annual Sales (millions)</u>
Cominco-NANA Red Dog	\$300
Amselco Greens Creek	\$200
Diamond Shamrock Beluga Coal	\$200
Placer U.S. Beluga Coal	\$100
Usibelli Healy Coal	\$ 39
Inspiration Nome Onshore	\$ 30
Valdez Creek Mines	\$ 15
Alaska Gold Nome Onshore	\$ 10
Present rate gravel mining	\$125
Placer mining	\$ 60

Placer mining is estimated at the 1985 rate of production (\$60m) because of the present water quality and reclamation regulations. This industry could grow to the range of \$100 to \$300 million dollars in the next 5 to 10 years if proper, attainable economic standards were developed by the State of Alaska and the federal government. With proper laws and regulations, government leadership and some engineering help, most of these people can operate in a professional, environmentally responsible, profit-making manner.

Future mines that could be on stream by 1997 include U.S. Borax Quartz Hill, GCO Lik, Doyon Alaska Asbestos, Sohio-Kennecott Bornite Arctic, Nerco Delta, Hanson Goodnews Bay, CIRI Johnson River, Echo Bay Alaska Juneau-Treadwell, Berners Bay, Queenstake West Chichagof, Union Pacific Wishbone Hill coastal, Chugach Bering River (coal), Lost River (tin), Alaska Apollo Unga Island, additional offshore dredging, additional placer mines and possibly three or four small to medium size hard rock gold mines.

For some perspective on mining in other states and provinces Arizona has \$1.483 billion dollars in sales per year, Wyoming \$3.231b, California \$2.003b, Texas \$1.715b, Nevada \$.616b, Idaho \$.412b, Utah \$.524b, British Columbia \$2.398b. These figures do not include coal, uranium and gravel in some cases.

It is important to note that Alaska has close to \$100 billion dollars in drilled mineral reserves at this time. This incredible total of proven resources, sometimes compared in size to South Africa's, includes base metals, precious metals, strategic and industrial minerals, coal and gravel. At the present rate of mining, this represents approximately 500 years of reserves. At \$1 billion per year, it represents 100 years of reserves and at \$3 billion per year, it represents 33 years.

Since much of Alaska is as yet unexplored, the state has the potential to develop many times this reserve in the future under proper state and federal policies. The key is access and a surface transportation system that can move these minerals to market.

Alaska is one of the few places in the world where a wealth of mineral resources has failed to develop significant railroad activity since the early 19th Century. Railroads are the key to developing northern countries. Canada and Russia both have demonstrated this. Only in Alaska have we been slow to take advantage of this fundamental economic truth.

Hesitancy and hope in rural villages

A number of Native village populations are hesitant to connect with major transportation systems which would link them to the rest of the state. They fear an invasion by outsiders which could overwhelm them.

"We still have images in our minds of passengers shooting buffaloes out of railroad car windows," a Native legislator told the committee.

Currently, village leaders are fighting against the influences of alcohol and drugs in their small communities. Additional transportation

It is important to note that Alaska has close to \$100 billion dollars in drilled mineral reserves at this time.

"...passengers shooting buffaloes out of railroad car windows."

***The infusion of
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links may make bootlegging more difficult to control. Finally, there is the concern of the Native corporations and Native leadership about retaining control of their own destiny financially, politically and culturally.

However, in many cases these concerns make the railroad an attractive option, certainly more so than a highway. Railroads are easier to control in terms of who uses them and frequency of operation. In addition, local people can be trained and provided jobs operating the equipment utilized on the railroad.

Some observers believe that the Native community is evolving in its reaction to this type of connection. Population pressures are real, but social problems may be more effectively addressed if steps are taken to improve local economies. The infusion of railroad related jobs may help stem the epidemic of alcoholism and attendant suicide. Some Native spokesmen recognize that in the long run, natural resource development provides what may be the only real hope to improve those economies and generate the revenues necessary to meet the needs of the local peoples.

Development possibilities without line extensions

There are numerous opportunities for “economic expansion” without physical line extensions. New services, policies, rate structures, leasing and land management policies are all possible. The railroad needs to strengthen its strategic planning in these areas.

During the course of this study, an exciting opportunity for the Alaska Railroad was identified—to move the central railyard from Anchorage to Eagle River. This prospect opens up a whole range of possibilities for enhancing the land assets owned by the railroad in the heart of downtown Anchorage. A similar situation exists in Fairbanks.

Line extension proposals

When considering a decision on a line extension, numerous political, economic, and terrain conditions play a part. Enormous investments are required and paybacks on a railroad balance sheet basis are long term.

However, when looking at total benefits to the State of Alaska, many line extension proposals have the possibility of making sense.

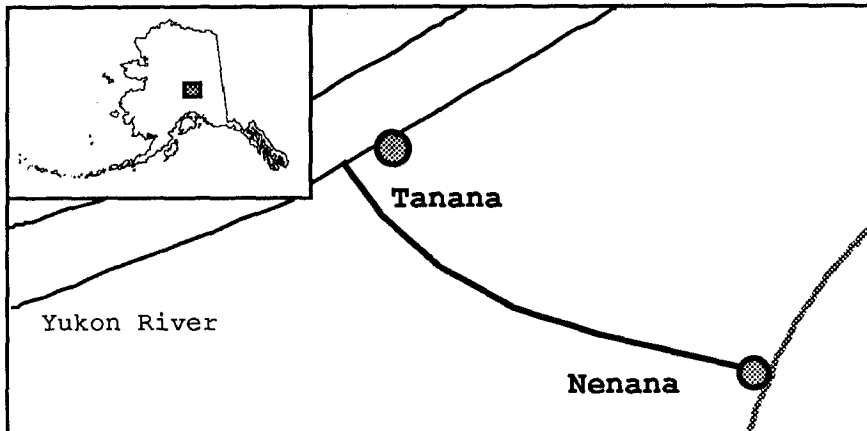
(*see the Commonwealth North report, *Redesigning the Front Door to Anchorage*, April 1988)

Some of the more attractive extension opportunities for the railroad that have been identified over the years include:

Nenana to Tanana

130 miles

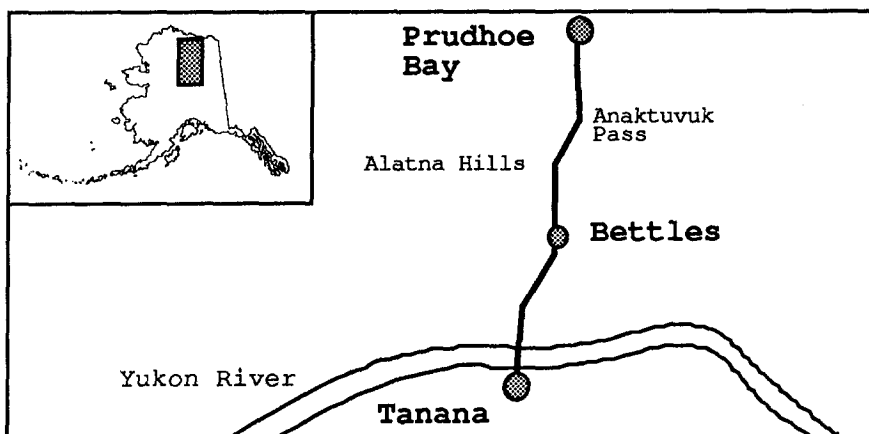
Connection of the current system to the Yukon River, adding six weeks to the shipping season for moving freight in and minerals and timber out.



Tanana to the North Slope

400 miles +/-

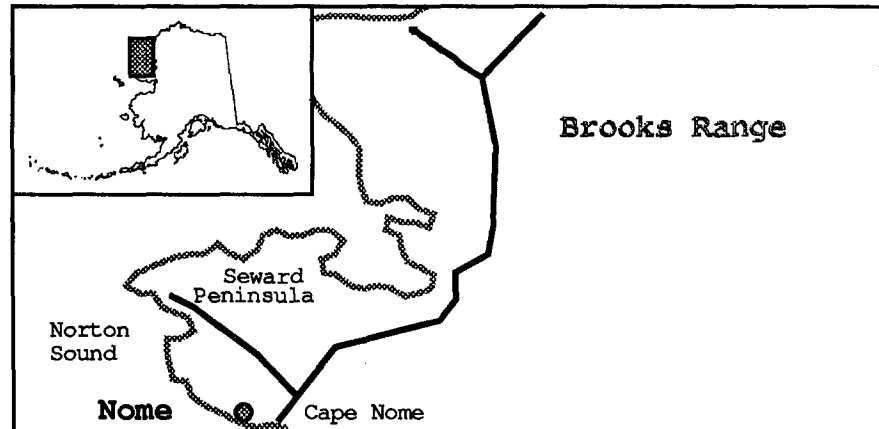
Exciting touring possibilities in the Gates of the Arctic National Park and access to numerous mineral deposits in the northern region in addition to the opportunities of a rail link to Prudhoe Bay.



Nome to the North Brooks Range and Western Seward Peninsula

400 miles +/-

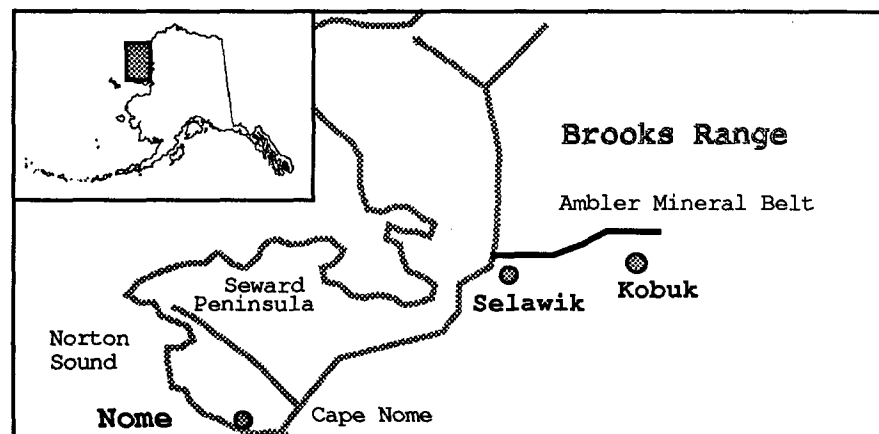
A surface system to numerous mineral deposits in the North Brooks Range and along the anticipated route to a future deep water port at Cape Nome or Port Safety with year-round usage.



Selawik to Kobuk

150 miles

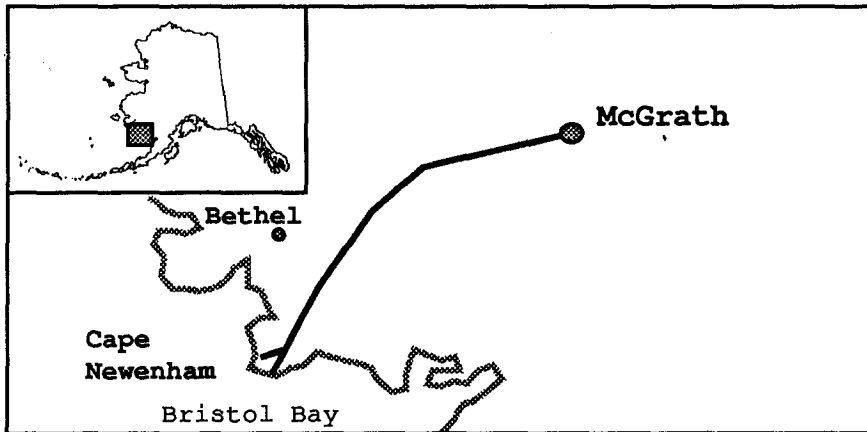
Route to the famous Ambler mineral belt, known for its enormous high grade copper resources as well as for a variety of strategic minerals.



Kuskokwim Drainage
(McGrath to Cape Newenham)

400 miles +/-

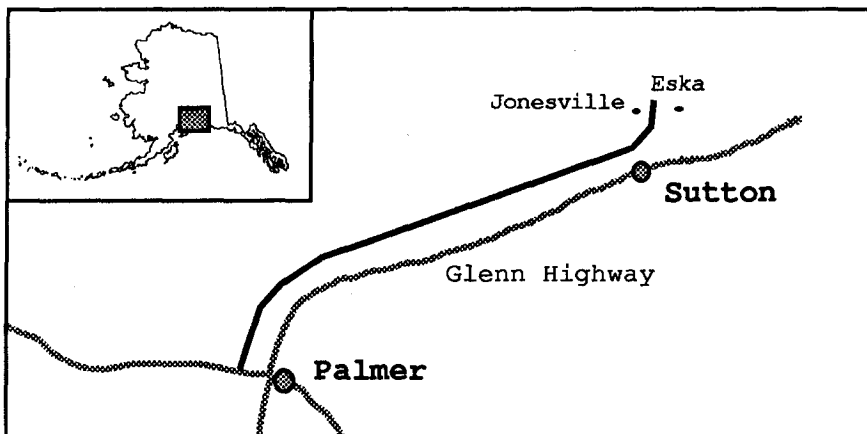
Outlet for numerous strategic and critical mineral deposits and timber along the track corridor to an excellent deep water port site at Cape Newenham.



Sutton to Palmer

20 miles

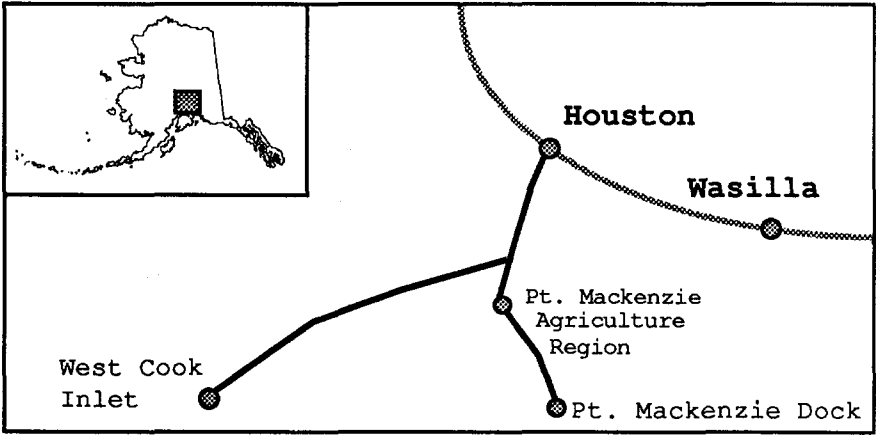
Feeder line from the Sutton coal fields.



Houston to West Cook Inlet

40 miles

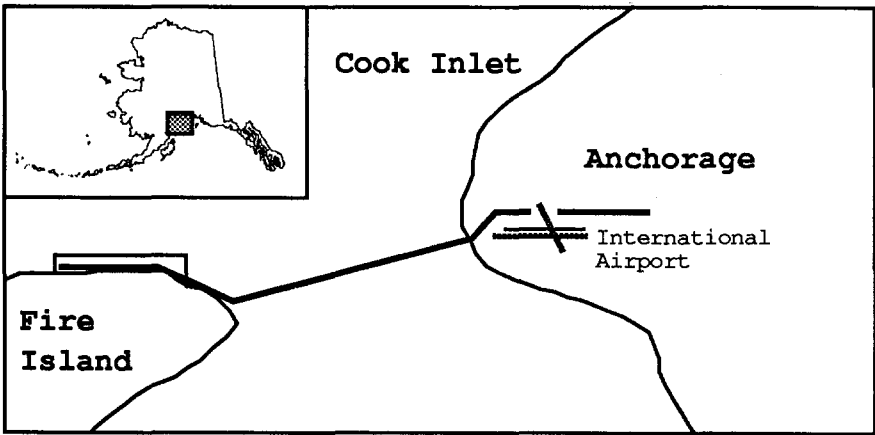
Extension from the main line to the Pt. Mackenzie agriculture project and mineral deposits of West Cook Inlet.



Anchorage Mainland to Fire Island

7 miles

A track on a gravel causeway across the shallow mud flats enabling the creation of a year-round regional port on Fire Island.



Estimating costs

In discussing the cost of line extensions in Alaska, one must be cautious. Over the years, there have been numerous estimates of various track extensions with estimated costs ranging from \$1 million to \$8 million per mile. It is tempting for researchers with limited knowledge of railroading or Alaska civil construction to publish such ballpark numbers. There are two dangers in this approach. The first is that the "rough cost" numbers may be insufficient due to unknown terrain features such as river crossings, grades and curves.

The greater danger is the likelihood that estimates are so high that further consideration is precluded. This has happened in the past particularly with regard to the 1970 North Commission routes which were highly recommended and should have been pursued at that time. Had the opportunity been embraced when that report was published, Alaska would indeed have a more diversified economy today.

Federal impediments exist

Under current federal law, few extensions of the Alaska Railroad are possible without the concurrence of the U.S. Congress. Title 11 of the Alaska National Interest Lands Conservation Act of 1980 supposedly provides "fast track" mechanisms to facilitate future transportation corridors throughout the state. In reality, the system is tortuous and virtually assures that any such corridor be decided by the U.S. Congress.

The Act does not "pre-select" routes. It sets up procedural guidelines for the administration of a system to approve transportation routes. It includes time lines for preparation of an Environmental Impact Statement and consideration of an application by the President and by Congress.

If there is already applicable law in place, Congress does not have to be consulted unless the system crosses wilderness areas. However, anti-development advocates within the federal agencies have skillfully cut off nearly all natural access routes with wilderness classifications, a process which is ongoing to this day.

The following factors must be taken into consideration in determining whether to grant or deny an application for a transportation system through a wilderness area:

1. Need and economic feasibility.
2. Alternate routes and modes of access, especially the existence of

The system is tortuous and virtually assures that any corridor be decided by the U.S. Congress.

Anti-development advocates within the federal agencies have skillfully cut off nearly all natural access routes with wilderness classifications.

an economically feasible and prudent alternative to routing a system through or within a conservation system unit.

3. Feasibility and impacts on different transportation utility systems.
4. Short and long term social, economic and environmental impact.
5. Impacts, if any, on national security interests.
6. Impacts that would affect the purpose for which the respective unit was established.
7. Measures to avoid or minimize negative impacts.
8. Short and long term public values.

If there is applicable law on a particular corridor then, in making a favorable recommendation, an agency must first determine that the system will be compatible with the conservation unit in question and, further, that there is no economically feasible alternative route. This latter criteria is an extremely high hurdle to overcome.

The agency's favorable recommendation is then forwarded to the President. If he approves, the appropriate permits are to be issued. If he denies the application, an applicant can appeal to a federal court. If an agency does not make a favorable finding, an applicant must appeal to the President before suing in federal court.

If there is no law applicable, federal agencies again report their finding to the President. If he approves, he sends the recommendation to Congress. If Congress approves the application within 120 days of receipt, the necessary permits are issued.

***...a cumbersome
procedure replete
with opportunities
for political
dealings.***

Obviously this is a cumbersome procedure replete with opportunities for political dealings which have little to do with the transportation corridor under consideration.

Those who study the pattern of ANILCA land selections and wilderness designations reach the inevitable conclusion that they were deliberately designed to obstruct the natural transportation corridors which are essential to develop the natural resources of Alaska. The state should examine that charge in the light of abrogation by Congress of the intent of the Statehood Act.

SECTION III

Should the Alaska Railroad Be Sold?

Conclusion 1

The Alaska Railroad should not be sold as long as its mission is to expand and help diversify the Alaska economy.

Conclusion 2

Among both the Alaskan public and the elected leadership of the state there is little understanding of the requirements written by Congress in the Federal Transfer Act of 1982. These provisions make it difficult and unwise for the state to sell the railroad to a private entity.

Conclusion 3

If the railroad, meaning all of its assets, is to be sold at any time, congressional action modifying or clarifying the current federal act will ultimately be necessary.

Conclusion 4

Maintaining the railroad in a state of readiness for sale to a private entity with corporate rather than governmental accounting, procurement and personnel procedures is one of the best methods of assuring that it will continue to be operated profitably.

Recommendation 1

As the expansion of the railroad is deemed in the public interest (see Section II of this report), the railroad ought to remain in public ownership in order to facilitate the financing for such expansion.

Recommendation 2

Because of the terms in the Federal Transfer Act, the railroad ought not even be considered for sale by the state under any circumstances prior to January 6, 1990.

Recommendation 3

The contemplation of a sale or sale option ought to be retained in some form without the expensive and unnecessary requirement of soliciting offers on a regular basis.

Recommendation 4

While the railroad continues as a public corporation, its operation and management ought to be insulated to the greatest extent possible from special interest and regional legislative influences and politicization.

Recommendation 5

If and when, in the public interest, it is deemed that the railroad should be transferred to the private sector, terms and conditions must include a continuation of the mission of the railroad as proposed in this report as well as requiring that all of the assets be kept intact.

Sale proceeds before 1990 will revert to the federal government

The Alaska Railroad should not be sold prior to January 6, 1990.

Section 610(e) of the Federal Alaska Railroad Transfer Act provides that if the railroad is transferred to an entity other than an instrumentality of the state prior to January 6, 1990, all proceeds from the sale, other than those amounts spent by the state on rehabilitation and improvement (including net liabilities incurred) will go to the Treasury of the United States. Further, as a practical matter within that time frame, neither the railroad nor the State of Alaska would be in a position to have the various assets properly inventoried and valued.

Proceeds from the sale will go to the Treasury of the United States.

Other impediments under federal law

Existing federal law under which the railroad was transferred to the state provides substantial impediments to the transfer of the railroad to a private entity.

A. The ten-year provision

Section 610 (a) of the Alaska Railroad Transfer Act provides that if any real property owned by the railroad is transferred in a way that prevents "the state-owned railroad from continuing to operate," that real property would revert to the United States unless the state paid the United States government fair market value of such property (again). A transfer of the assets of the railroad to a private entity would arguably "prevent the state-owned railroad from continuing to operate" and thus trigger the clause.

The phrase "state-owned railroad" is defined to mean "the authority, agency, corporation or other entity which the State of Alaska designates or contracts with to own, operate or manage the rail properties of the Alaska Railroad." While this definition could be argued to include a private corporation to which the state sold the railroad, it would be difficult to refer to the railroad as a "state-owned railroad" thereafter.

B. The discontinuance provision

Section 610 (b) of the Alaska Railroad Transfer Act provides that if, at any time after the sale (i.e., from January 5, 1985, on) the right-of-way itself is no longer used by the "state" for transportation, communication or transmission, such right-of-way will revert ultimately to the abutting land owners.

If the right-of-way is no longer used by the "state," such right-of-way will revert ultimately to the abutting landowners.

Attempting to structure a transfer to a private entity that would purportedly circumvent these provisions would only raise substantial questions as to the effectiveness of such an effort. Thus, a transfer to a private entity would most likely require congressional clarification or modification.

The federal act clearly contemplates the continued operation of the railroad as a railroad carrier. Nothing in the federal act requires or expressly permits transfer of the railroad properties to an entity other than an instrumentality of the State of Alaska.

Legislative fears prior to transfer

The provisions in the state act establishing the Alaska Railroad Corporation that contemplate a sale to a private entity were enacted out of a fundamental belief that private enterprise should carry out proprietary activities whenever possible; out of a fear that the railroad would require annual appropriations to support operations; and without a real understanding of the impediments to a sale presented by the federal act outlined above.

There was concern in the legislature that the railroad would require annual appropriations of state money just to fund ongoing operations.

Accounts by legislators involved at the time establish that there was concern in the legislature that the railroad would require annual appropriations of state money just to fund ongoing operations, and that there would be no money for expansions. At the same time, legislative attention was not focused on the provisions in the federal act which significantly impede, if not prevent, a sale of the railroad to a private entity.

Since then, the railroad has been operated profitably and, after the initial capital infusion, without any funds from the state. On the other hand, the railroad spends approximately one and one-half man/years per year to respond to legislative initiatives motivated by private, special, and regional interests. The strongest and primary argument against public ownership of the railroad, assuming it continues to be operated profitably, is the susceptibility to influence through the legislature of private, special and regional interests.

Real estate assets must be protected

The Alaska Railroad ought not to be sold without reliable, enforceable and adequately secured provisions assuring that the railroad would continue to be operated as a railroad carrier and preventing the new owner from disposing of the land. Such provisions would include protections to the state that all federal requirements would be met and all obligations the state has to the federal government would be carried out.

If the Alaska Railroad were to be sold to a private entity, the terms and provisions should require that all assets be kept intact, including all real estate. The profitable management of the real estate contributes to the ability of the railroad to provide subsidized passenger service. Thus, the real estate should not be permitted to be stripped from the rail carrier operations.

Retaining the sale option without costly offers to sell

The sale option in the Alaska legislation ought to be retained, though the requirement of soliciting three offers every five years should be deleted.

Even though it is not advisable in the immediate future to transfer the railroad to a private entity, the option for such a sale ought to be retained so as to assure that the railroad continues to be operated as a profitable, private corporation. Such requirement in turn assures that it will continue to be in a position to be sold if such a sale is later determined to be in the best interest of the public of the State of Alaska. Further, the necessity of maintaining the railroad in a position to be sold functions as a protection against politicizing the operations of the railroad and against legislative efforts motivated by private, special and regional interests. However, the cost of valuing the assets and the inadvisability of selling the railroad in the immediate future, calls for legislative action to delete the unnecessary expense of soliciting offers according to a prescribed time schedule.

Public ownership makes expansions more feasible

If the railroad is to be expanded, either in use of existing track, in extension of track from the existing trunk, or in the laying of disconnected track connecting to established mineral reserves with open-water ports, the simplest, most economical and most productive means of achieving those goals is through public ownership.

A. It is clear that expansion of the existing right-of-way cannot be financed out of current operations by the Alaska Railroad. While a number of estimates have been made of the cost-per-mile for construction of railroad extensions, (anywhere between \$1 million and \$8 million/mile) no reliable figures can be obtained until a specific extension is identified. Nevertheless, it is clear that the cost of such construction far exceeds the railroad's ability to finance it out of current operations.

The real estate assets should not be permitted to be stripped from the rail carrier operations.

If the railroad is to be expanded, the simplest, most economical means is through public ownership.

B. For the same reasons, the Alaska Railroad would be unable to finance extensions of the railroad through its borrowing capacity.

The effective debt limit of the Alaska Railroad is approximately \$40 million and current debt approximates \$21 million. With the high cost of construction, the bonding capacity of the railroad, even given the benefits of tax-exempt financing available to it through the federal act, is insufficient to extend the railroad right-of-way.

C. For the same reasons, a private owner of the railroad would be unable to fund construction out of current operations or through private financing.

Currently in the industry, the longest term available for bonding by privately-held railroad companies is thirty to thirty-five years. Such a term is insufficient by a factor of one-half to pay back the costs of construction in Alaska. A payback period of such construction is estimated to be between fifty and seventy-five years.

Thus, if the railroad is to be expanded, either in terms of use of existing right-of-way, extension from the current tracks, or construction of unconnected tracks between established mineral resources and open ports, the initial construction cost will have to be underwritten by the State of Alaska, either through general obligation bonds, guaranties, or some other credit mechanism.

If the political decision is made that expansion serves the best interests of the public, such expansion will require state financial assistance, the return on which will not be measured in immediate revenues of the railroad but in the overall, long-term benefits stemming from development of a portion of the state.

Private financing of expansions

Under private ownership, major rail system expansion will most likely never occur because it is doubtful that any one project will be able to support the initial construction costs as well as the continued maintenance costs of the additional track. Further, private holders of resources are unlikely to develop such resources unless and until a railroad is already in place.

However, public ownership will permit the underwriting of the construction costs of extending the railroad into an area where a number of projects are likely to be developed and would be rendered feasible by the proximity of a railroad, even though at the time of construction only one resource has been actually developed.

If the railroad is to be expanded, the initial construction cost will have to be underwritten by the State of Alaska.

Under private ownership, major rail system expansion will most likely never occur.

Public ownership, as opposed to private ownership, provides the mechanism by which an expansion can be undertaken without having to rely on the revenues from a single mineral resource to justify the extension. The increased feasibility of nearby mineral resources and benefits of freight backhauls into the remote areas, which in turn promotes overall development in the area, provides the justification for the expenditure of public funds or credit.

Further, and more fundamentally, expenditure of a public fund or the use of public credit can be justified and predicated on the long-term benefits to the public treasury derived from broad-scale development of an area; whereas private investment will be made only on the basis of the current profitability of the immediate venture.

Thus, continued public ownership of the railroad maintains the option to expand the railroad when and if the political decision is made to do so while private ownership, in most cases, will foreclose that option.

A railroad is similar to a public highway in that it can be used by the public under certain tariffs and conditions to transport all types of commodities and passengers. It is customary in this country, as well as in all others, for the state to underwrite the cost of not only the construction but also the maintenance of the highways to be used by its citizens. The track and roadbed of a railroad cannot logically be distinguished from highways built for cars. When viewed as a public infrastructure for the use of all citizens for economical transportation, the appropriateness of utilizing public ownership funds and credit for the railroad becomes clear.

Public financing of expansions

The necessity of public funds or credit for expansion means that public control and protection of the public's interests can be achieved most simply and economically through public ownership.

A number of mechanisms are possible through which public financing of a project can be used, though the entity would essentially be private. Examples are the creation of an authority or a regulatory commission. But these involve an additional layer of state bureaucracy with the attendant costs. None of these is as economical as the current situation involving a corporation run as a private business with the board of directors being appointed by the governor with the approval of the legislature.

It is customary in this country for the state to underwrite the cost of the construction and maintenance of the highways used by its citizens.

The track and roadbed of a railroad cannot logically be distinguished from highways built for cars.

Additional ways of insulating the management and operation of the Alaska Railroad from the political processes of the legislature should be investigated.

A private-stock corporation, the stock of which is held by the State of Alaska, is another alternative though questions exist as to whether such a corporation would actually be a "public corporation" and whether such a corporation would be entitled to the benefits of being an instrumentality of the state provided by the federal act.

Additional practical problems exist in determining how the stock of such a corporation would be "voted" by the State of Alaska.

Because the creation of additional agencies, authorities or bureaucracies would require additional state funds without any readily-apparent benefit over the current arrangement, none of these potential schemes suggests itself as a better alternative.

Nevertheless, in view of the amount of time spent by the current railroad administration in responding to legislative efforts motivated by regionalism and private special interests, additional ways of insulating the management and operation of the Alaska Railroad from the political processes of the legislature should be investigated and implemented to the greatest extent possible.

Concessionaire alternatives for operations

Once expansion has been undertaken through public ownership, it remains as a viable option for the state to transfer the operations of the railroad to private hands under a concession agreement. This approach would be similar to those used by the National Park Service for resorts and hotels in national parks. To protect the public interest terms and provisions of the concessionaire's use could be spelled out in great detail.

The contracts could be subject to terms of five, ten or twenty-five years, depending upon what the market would support. By limiting such contracts to a definite term, the state retains the right to re-examine the situation at appropriate intervals. Further, by putting time limits on the contracts, the public's interest in availing itself of new developments is protected.

If a concessionaire did not adhere to the terms of the contract, the state would have the right to terminate it under fundamental contract principles. Finally, such contracts would be put out to competitive public bid so as to assure the best possible financial terms to the state.

Section IV

Assessment of Current Operations

Conclusion 1

In the three years since the transfer from the federal government, the board of directors and management of the Alaska Railroad have operated within their revenues and at no time have gone to the legislature for appropriations for operations. Performance audits by railroad experts have given management high marks for professionalism, enthusiasm and a "can-do" attitude.

Conclusion 2

Union agreements have been consolidated and labor and management have worked together admirably to produce an efficiently run organization.

Conclusion 3

The real estate department has brought stability to leasing policies and order out of the chaos left by the federal government. This improvement is vitally important as real estate, a major railroad asset, generated over \$5 million in revenue in 1987.

Conclusion 4

The railroad corporation has succeeded in fending off most attempts to politicize its activities through skillful communications with state leaders and a favorable bottom line.

Conclusion 5

The physical plant and safety of the facilities have been substantially upgraded. Seventy percent of the 2,400 OSHA-related problems identified at the time of the transfer have been corrected. The remainder will be dealt with by 1989. A total of \$28.3 million dollars of new equipment has been acquired and \$21.6 million in capital improvements in the track, tunnels and road bed have been made through 1987.

Conclusion 6

In spite of criticisms from independent truckers that the railroad is able to use "predatory pricing practices" because it is tax exempt, an ICC investigation in 1981 found that railroad rates covered direct operating expenses in addition to indirect burdens not required of the trucking industry such as the maintenance of track roadbed. These same burdens are still carried by the Alaska Railroad out of earnings.

Recommendation 1

The concept to designate seats geographically on the board of directors, recently introduced as legislation in the state legislature, threatens to fragment and politicize the railroad rather than ensure that the best people available be chosen to lead it. This approach is not in the best interest of the railroad or the state.

Recommendation 2

Rather than regionalize the individuals serving on the board of directors, the legislature should support railroad management's efforts to use the Community Briefing Council as a mechanism to hear local concerns and input.

Recommendation 3

Since the railroad must operate within its own income-generating capabilities, business acumen should be a prerequisite for those chosen by the governor to serve on the board. If the mission of the railroad is upgraded as recommended in this report, the governor should also seek individuals with statewide knowledge and vision.

Recommendation 4

In the interest of increasing financing flexibility for leaseholders of railroad properties, the Corporation Act should be amended to allow for long-term leases in excess of 35 years.

Recommendation 5

Management should continue its recent efforts to improve the marketing arm of the Corporation, both to benefit the users in the Railbelt as well as to encourage development of new industries and services.

Recommendation 6

While retaining a strong commitment to buying Alaskan products and services, the Alaska Railroad should be once again deleted from the State Procurement Act because the bureaucratic procedures required make it more difficult and costly for the railroad to operate.

Much of the success of the railroad since the transfer is the result of excellent top level management. To continue in this positive direction the Board must insure that second-level management is selected and groomed for future top leadership responsibilities.

Review of operations

The operations of the Alaska Railroad have been conducted in a highly professional and efficient manner since the acquisition of the railroad from the federal government in January 1985. Members appointed to the original board of directors have distinguished themselves with a non-political, businesslike approach to the task of converting a governmental organization to a "bottom line oriented" business operation.

The strong membership of the board of directors resulted in the hiring of a highly-qualified executive to administer the business operations of the railroad. The positive approach of the board and management in conjunction with farsighted labor leadership has carried over to railroad operating personnel. Working together, board, management and labor have taken those actions necessary to ensure that the railroad, in a period of declining revenues and reduced economic activity levels, produced positive bottom line results.

The initial team was confronted with a myriad of tasks and challenges which they have handled in an efficient and businesslike manner, much to the credit of the individuals involved. The following operating statistics demonstrate current management's ability to produce positive results in a time when revenues declined a full 20%.

Profit/loss information

The Alaska Railroad Corporation has achieved the following economic results in the 1985-1987 period:

	1987*	1986*	1985*
Revenue	\$53,703	\$58,133	\$67,234
Expense	<u>45,604</u>	<u>56,068</u>	<u>58,085</u>
Operating Income	8,099	2,065	9,149
Interest Expense	1,661	613	561
Depreciation	<u>3,421</u>	<u>2,437</u>	<u>1,455</u>
Net Income (Loss)	\$ 3,017	\$ (985)	\$ 7,133

* in thousands

The members of the original board of directors have distinguished themselves with a non-political, businesslike approach.

Review of Major Revenue Components

Revenue from operations can be broken down as follows:

	1987*	1986*	1985*
Freight	\$39,371	\$41,676	\$51,978
Passenger	\$5,434	\$4,574	\$4,344
Real Estate	\$5,206	\$5,174	\$4,322
Other	\$3,692	\$6,609	\$6,590

* in thousands

Review of Major Expense Components

The following are the major expenses of the railroad:

	1987*	1986*	1985*
Salary and benefits	\$30,309	\$35,071	\$35,219
Fuel	\$2,931	\$3,911	\$5,047
Depreciation	\$3,421	\$2,437	\$1,455
Bad debt expense	\$655	\$1,129	\$912
Other	\$13,370	\$15,617	\$16,680

*in thousands

Intelligent labor and management negotiations were conducted on the basis of what was best for the railroad and Alaska, not just for the benefit of the separate parties concerned.

Constructive labor/management initiatives

One of the reasons for the railroad's positive bottom line in spite of the economic recession has been the reduction of expenses, especially in the area of salary and benefits. This development is the result of some intelligent and informed labor and management negotiations conducted on the basis of what was best for the railroad and Alaska, not just for the benefit of the separate parties concerned. The federally-owned railroad had five labor unions with seven different agreements, each containing different pay and benefit provisions. Now, the railroad has only one contract with five unions, and each union has its own appendix for items that pertain to that specific group.

A high wage structure still exists, but costly rules are reduced or eliminated. Significantly, all crews are now paid on an hourly instead of a mileage basis. Amtrak is the only other major railroad to have taken this step.

Currently several arbitrations are in progress as the new contract is being ironed out. But both labor and management agree that they have succeeded in working together to produce a model agreement which helps to make the railroad a viable, profit-making enterprise in many ways.

Professional management controls

The Alaska Railroad Corporation Act of 1984 created an independent corporation to operate the Alaska Railroad. The Act established a seven-member board of directors to control the corporation. The Act included several oversight provisions which balance the railroad's mandate to operate freely in the transportation marketplace while at the same time assuring accountability.

For example, the board must provide an oversight report to the governor and the legislature before undertaking certain actions, including requests for funding and expanding, reducing or diversifying services. The legislature must approve leases in excess of 35 years and also must approve any sale of land. Annual reports are required as are the costs of providing each category of service and the associated income generated by that category. Audited financial reports prepared by a CPA are required as is an annual performance audit. The corporation submits a five-year capital improvement program to the governor and legislature each year. The corporation must notify the Department of Law before initiating legal action. The corporation operates under the jurisdiction of the Interstate Commerce Commission.

The seven member board includes the Commissioner of Transportation and Public Facilities, Commissioner of Commerce and Economic Development, and five public members appointed by the governor for staggered five-year terms.

While the board delegates responsibilities to the chief executive officer, actions requiring Board approval include adopting the long-range capital improvement and program plans, adopting annual reports, deciding major changes in service levels, expanding the rail system, entering into collective bargaining agreements, and adopting annual budgets. The board provides management direction by adopting rules to carry on the functions and purposes of the Corporation Act. So far, the record in this respect has been excellent.

Both labor and management agree that they have succeeded in working together to produce a model agreement.

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Board appointments

Board appointments should reflect statewide vision and business skill. It is a mistake to "Balkanize" the board by designating seats for certain communities. The appointments by our recent governors to the Permanent Fund and the Railroad Corporation boards have been outstanding. Perhaps lessons were learned from the mistakes made by the Alaska Renewable Resource Corporation and other state enterprises in the late 70's and early 80's. The more recent trend toward competence rather than political insiders must be continued.

It is recommended that the present board of directors of the Alaska Railroad Corporation submit several names of qualified individuals to the governor whenever he is faced with filling a board seat. In this way, the governor will receive names of individuals who are competent in business, knowledgeable about railroads, and dedicated to a state-wide perspective.

In order to insure that the currently constituted board is responsive to local needs, the Community Briefing Councils (referred to later) should be better publicized and utilized. In this way, local input can be received by management without politicizing the board.

Established Policies

Ethics and conflict of interest

The Alaska Railroad Corporation has adopted a Code of Ethics for its directors and employees (Rule 14). A director or employee or the immediate family of such person may not directly or indirectly derive a benefit from dealing with the Corporation under most circumstances.

Potential conflicts of interest are outlined and the rule includes provisions for administering the Code of Ethics, enforcement of the provisions, and a clear statement of the responsibilities of directors and employees.

Industry procurement rules needed

The objective of the Alaska Railroad's procurement policy is to assure that needed goods and services are obtained in a manner which treats vendors fairly and equitably and provides the best value to the Corporation. When purchasing goods and services having a value of \$1,000 or more, a competitive bid basis is utilized.

*Community
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Historically, policy of the federal government-run railroad was to purchase on the basis of lowest the bidder. After the Alaska Railroad Corporation Act was passed, management was directed to “assure the procurement procedures of the corporation meet accepted railroad industry standards.” This language gave the railroad the opportunity to operate in a private sector manner, balancing price with quality.

But in 1987 the State of Alaska’s procurement rules were amended to give preference to local products and services. The railroad was directed to adopt substantially equivalent rules and procedures mandated by the state law.

The purpose of this provision was the outgrowth of political pressure for the railroad to buy Alaskan wood for railroad ties, even at a much higher price than outside competitors could offer.

The intent of the legislation was well meaning, but the railroad is now saddled with a cumbersome, bureaucratic process which makes it more difficult and costly for the railroad to operate.

Hiring and personnel

Since the transfer, there has been an overall reduction in the labor force. The contract requires that all laid-off employees are placed on a “seniority-based recall list.” When employees are needed, the individuals on this list have first call for all “represented” (union) jobs.

If a non-represented position is available, railroad management tries to hire from within the ranks with a special eye for people who, with training, have the potential for advancement. The second rule of thumb is to respond to the urgent need to hire Alaskans whenever possible. Finally, if those two sources do not produce the talent needed, the best qualified individuals are sought wherever they can be found.

Real estate operations dramatically improved

Real estate assets are vital to the railroad. In 1987, the railroad generated net income of approximately \$3 million, and real estate revenues contributed over \$5 million. In fact the five-person department generated \$5.2 million in revenue with a direct operating expense of \$441,000.

Total railroad property is 36,249 acres. Some 13,759 acres are included in rights-of-way, 8,125 acres are used for rail operations, 12,288 acres are available for either lease or operations, and 2,077 acres are revenue-producing leased land.

The railroad is now saddled with a cumbersome, bureaucratic procurement process which makes it more costly to operate.

The five-person department generated \$5.2 million in revenue.

Before looking at how the railroad might seek additional revenues from its properties, the public should note the tremendous improvement in real estate operations since 1985. Under federal control, lease terms were 55 years with reappraisals every 5 years. Both the rate and the fee value could be altered. The lessee could terminate leases on 90 days notice.

This situation caused inconsistent treatment. For example, a leaseholder investing in fill for his property would not be given credit for the value added and yet would be charged at a higher rate. Issues such as this led to a lawsuit with the leaseholders. To its credit, the Alaska Railroad management has settled the suit against it, while the federal government is still being pursued by the leaseholders.

Other problems inherited by the Alaska Railroad included the fact that the federal government had surveyed none of the lands it owned. Rents tended to be low in the 1960's, and it was not until a General Accounting Office audit in 1976 that the railroad attempted to charge fair market value.

To deal with these problems, the railroad established a lease policy and now utilizes a standard master lease so that prospective tenants will see a consistent approach.

Prior to 1985, the railroad used a manual billing system. This cumbersome process has been replaced by a computerized system, and the railroad has also computerized its data base to allow for proper control and inventory of real estate holdings. The railroad has set up new operating systems, including standard forms and permits. It now has survey and appraisal guidelines where none existed previously. During this process, the department experienced an almost total personnel change.

While the real estate leasing office is intent on developing its marketing and development functions, it might yet be called a contract administration office. This results from the need to renew or negotiate 173 leases which have expired. The office also administers some 1,200 permits, and the combined workload tends to minimize the ability of the group to enhance the value of the railroad's real estate.

However, much of the needed work to correct past problems has been completed. Within the next several years there will be an opportunity to improve the return on assets.

The federal government had surveyed none of the lands it owned.

Much of the needed work to correct past problems has been completed.

Internal management controls

Management has established a set of controls governing authority, expenditures and employee expenses. The Approval Authority Guide is the president's formal delegation of authority and specified authority granted to each position.

The Authorization for Expenditure (AFE) process is a tracking mechanism for all capital expenses and major expense activities. The process is designed to ensure that all alternatives are considered and that planned expenditures are economically justified.

The Employee Business Expenditure Guide defines railroad policy to pay the reasonable and necessary expenses incurred by employees in the performance of authorized corporation business. The policy establishes the procedure for reimbursement of employees' business expenses.

Balancing the mandate to be self-supporting with the responsibility of a public entity

Board meetings are open

Although the board is required to meet at least quarterly, it has consistently met at least every other month. The meetings are public and are advertised. The board has been highly sensitive to the need for public input. Although rules allow for executive sessions, the board is reluctant to utilize closed meetings except when necessary for sensitive personnel and financial subjects.

The first year after the transfer the public turnout at board meetings was high. Currently, unless there is an issue of great public interest, few members of the public attend.

Involvement in the community

At times, when the federal government ran the railroad, there were written orders for personnel not to get involved in the community. The current leadership, however, encourages its executives in community efforts such as supporting the arts, serving on citizen group boards, and fund-raising for worthwhile causes. Management operates under the concept that the railroad is meant to be a "good corporate citizen."

A railroad Citizens Advisory Committee has been created which recommends how to allocate Alaska Railroad contributions to worthy causes.

The current leadership, encourages its executives to become involved in the community.

Interface with local, state, federal officials

The railroad has ongoing communication with various federal, state and local government agencies. At the federal level, it has regular contact with the Army and the Air Force and has developed agreements concerning rights-of-way, maintenance of military-owned rail equipment and the use of military land for railroad purposes.

The record of the railroad working with the state departments of Natural Resources, Transportation and Public Facilities, Labor, and Environmental Conservation as well as with local governments in Anchorage, Fairbanks, Whittier, Seward, Talkeetna, Nenana and Wasilla is ample evidence of the corporation's desire to fulfill its responsibility as a public entity.

Management regularly visits the state capitol during legislative sessions, and a monthly activity letter is sent to those legislators especially interested in transportation and economic development issues.

The Community Briefing Council

Much to its credit, in 1987 the board of directors established a Community Briefing Council to provide a quarterly forum for communications between the corporation and the communities served. This council includes representatives from the Fairbanks North Star Borough, City of Nenana, Matanuska-Susitna Borough, the Municipality of Anchorage, City of Whittier and the City of Seward. Items discussed include land use and land policy, railroad operations, tourism and community events, passenger service needs, road and highway crossings, port operations and community emergency services.

This council can and should play a growing role in communicating local needs to railroad management and the board of directors. Meetings of the council should be more widely advertised, and the findings of the group should be directly and thoroughly presented to the board of directors.

Examples of public/private issues

Passenger service

Providing passenger service is considered "an essential government function" of the Alaska Railroad Transfer Act of 1982. A public subsidy? Yes, but no passenger railroads are operated privately, not in the South 48, nor anywhere else in the world. Railroad passenger service is more of a social service than a business. "Fares cannot be raised sufficiently to cover the true cost of the service." (Joint Report by State

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of Alaska and United States Department of Transportation, July 14, 1983, Appendix K, page 28).

As a requirement of the Transfer Act, the U.S. Department of Transportation and the State of Alaska were required to prepare a report on various aspects of the transfer. This report was issued July 14, 1983, including a 35 page appendix, which examines the railroad's passenger service. The appendix was written by the Institute of Social and Economic Research (ISER) of the University of Alaska.

This document pointed out that the passenger service was the "principal source of the substantial losses shown in the railroad's annual reports. Such a result is consistent with the problems experienced by other North American railroads during the past thirty years."

The fundamental reason is obvious—there are simply too few passengers to cover the costs of operating passenger service. The costs, according to the ISER report, are not excessive when compared with operating costs of other railroads. Because of other modes of transportation, primarily between Anchorage and Fairbanks, the number of passengers is simply too small to cover even operating costs. This analysis does not take into account capital costs or depreciation. Raising prices to cover these full costs would dramatically reduce the number of passengers further.

According to ISER, the subsidy provided by other operations of the railroad was \$38.41 per passenger in 1978, \$29.87 per passenger in 1979, and \$36.57 per passenger in 1980.

While the railroad was operated by the federal government, its accounting procedures did not separate the costs between passenger and freight service. Since the state has taken over, the accounting procedures, both with respect to current operations and the five-year plan, separate both costs and revenues between passengers and freight.

A public interest deficit

According to the five-year plan of June 1987, for the period from 1988-1992, total passenger revenue is forecast at \$43.4 million while the total costs for providing passenger service is \$51.9 million, or a deficit of approximately \$8.5 million. According to the same five-year plan, it is anticipated that this deficit between revenues and expenditures for passenger service for 1987 will amount to \$2.9 million. This shortfall is expected to drop to \$1.6 million per year for the years 1989, 1990, 1991, and 1992. Operation of freight service plus the benefits of the railroad's real estate revenue, will result over the same period in a total surplus of \$48.3 million. Thus, the income from real estate

There are simply too few passengers to cover the costs of operating passenger service.

operations and freight service is projected to more than make up for the passenger losses.

While the passenger service provided by the Alaska Railroad, particularly between Anchorage and Fairbanks, has substantial competition from the highways and air, the competition is either substantially reduced or does not exist at all with respect to interim stops along the railroad's route.

Essentially the same situation exists with respect to transportation between Anchorage and Seward. Further, at present, there is no competition for the rail transportation between Girdwood and Whittier.

However, while passenger service produces a net deficit, little question exists as to its benefit to the public. After 65 years of operation, the only substantially developed area in Alaska is along the Railbelt. Thus, the railroad has, in fact, carried out the essential purpose of its origin in the 1914 Alaska Railroad Enabling Act. In other words, operation of the passenger as well as the freight service does lead to private development of areas that would otherwise not be developed.

Donations of railroad property

The railroad frequently donates railroad property and services to local governments and public service organizations. As examples, the Wasilla and Nenana depots and Wasilla section house were donated to the respective communities. The Potter section house was donated to the state. Railroad equipment was donated to the State Transportation Museum. Historical materials have been given to the Anchorage Fine Arts Museum.

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Herbicide application

Controversy exists over the Alaska Railroad's use of herbicides to control vegetation which grows along the right-of-way, deteriorating the rail system and threatening safety. All railroads carrying heavy freight loads such as coal or gravel in the United States and Canada must and do use herbicides to destroy this type of growth. Specialized equipment is utilized which directs the herbicides downward into the ballast. A drift retardant is added to the mixture to prevent mist-type spray from reaching beyond the roadbed.

Responding to public criticism, railroad management is seeking realistic alternatives. This issue is being brought into focus because the railroad has let four years pass without treating the ballast. Prior to 1983, herbicides were used every year. Currently the railroad estimates that an optimum treatment is every two years.

The Alaska Department of Fish and Game is assisting the railroad in identifying areas sensitive to fish habitat where herbicides will not be applied. Additionally, measures will be taken to prevent herbicides from entering any body of water. Currently, the railroad estimates that about 40% of the roadbed sidings from Seward to Fairbanks will need to be treated.

Are railroad tariffs fair?

The committee interviewed several large railroad users as well as representatives of the independent trucking industry. The independent operators are highly critical of the railroad, claiming that \$5 to \$6 million of trailer/container business is being lost by them each year to the railroad because of the railroad's tax exempt status.

The Alaska Railroad Corporation, by state and federal law, is subject to the jurisdiction of the Interstate Commerce Commission. It is required to file its contracts and tariffs with the ICC and obtain its approval prior to implementation. In spite of public scrutiny of the contracts and tariffs, portions of these documents are proprietary and not available to the general public by federal law. An example is data which may reveal the specific cost of a service rendered by a carrier.

In 1981, in response to charges of "predatory pricing practices" by the Alaska Railroad, the ICC conducted a confidential investigation. The ICC found that the rates charged by the railroad not only covered direct operating costs but also many indirect burdens such as the maintenance of track and roadbed which is solely supported by railroad earnings. On the other hand, state highways utilized by the trucking industry are maintained entirely with public funds.

It is important to note that major trucking companies in Alaska as well as Sealand and Tote, all of whom use the services of the Alaska Railroad, have not complained about the railroad's pricing practices.

Because of the limited transportation infrastructure, the people of Alaska have historically benefited whenever the railroad and the trucking industries form a cooperative relationship to develop more business for both. It is hoped, especially in these times of economic stress, that this type of cooperative activity (within legal constraints) may be encouraged.

The independent truckers are highly critical of the railroad, claiming that \$5 to \$6 million of trailer/container business is being lost by them each year to the railroad.

Political involvement

Intent of the Alaska Railroad Corporation Act

The railroad is a constant target of political pressure. The best way to ensure that the railroad operates with the separation envisioned in the Act is to run the line as mandated, with a positive bottom line.

This Act provided for the corporation to be separate from state government and made the board responsible for railroad management. It also defined the role of the governor and legislature in railroad operations. However, as a state-owned entity, the railroad is a constant target of political pressure. The best way to ensure that the railroad operates with the separation envisioned in the Act is for the board and management to run the line as mandated, with a positive bottom line.

Real estate leasing

Legislation was introduced to modify the corporation Act by making major changes in requirements affecting railroad leasing, easement and permitting practices. Before this legislation is adopted, the real estate leasing policies instituted by management should be given a chance to work.

The caboose bill

Legislation requiring cabooses was introduced after the railroad initiated an overnight "caboose-less" express train from Anchorage to Fairbanks. During the debate, the railroad was able to answer the critical issues which revolved around safety. The caboose bill was defeated and thereby substantial wage and operating costs were eliminated.

Free service to seniors

In 1985 legislation was introduced that would require the railroad to provide free passenger service to persons 65 years of age or older.

As some 72% of Denali Park passengers are over 65 years of age, the implementation of this requirement was estimated by the railroad to result in increased losses on passenger services by 292%. In addition, the railroad is subject to the jurisdiction of the Interstate Commerce Commission which prohibits providing free passenger services.

The moose bill

Legislation has been introduced to require the railroad to salvage moose that are killed when the animals gravitate toward the railway right-of-way in order to avoid heavy snow. Railroad procedures direct employees to salvage moose meat and donate it to charitable organiza-

tions as directed by State Fish and Wildlife officials. Other legislation introduced would amend the corporation Act by adding specific operational requirements designed to minimize moose kills. The railroad has made and continues to make a good faith effort to solve this problem which is common to all railroads in northern countries.

Is the Alaska Railroad aggressively marketing railroad services?

Users and potential users of the Alaska Railroad readily criticize the slow response from marketing personnel as well as their rigidity and lack of imagination. Some say things have not improved since the transfer from the federal government. "They are not user friendly," commented a longtime freight client.

The board of directors and management recognize this problem and have recently taken steps to correct it. A new Vice President for Marketing has been hired and new equipment to market passenger services better has been acquired.

In 1985, specialized service was added to provide overnight delivery of high-priority highway trailers between Anchorage and Fairbanks using specially designed railcars. The railroad is involved in exploring development of the export coal market and is working with the timber industry to provide test shipments for potential timber exports to Pacific Rim countries.

In some cases the railroad has absorbed the cost of retrofitting cars for shipping timber and other products and has begun to exhibit the creativity necessary to assist clients who are establishing new industries in the state.

What has the Alaska Railroad done to maintain/upgrade railroad equipment and facilities?

When the state purchased the railroad, much of the equipment and rolling stock were outdated. There was concern about the adequacy of track maintenance activities, and many of the railroad facilities did not meet government (i.e., OSHA) safety standards. Since transfer, the corporation has replaced much of the outdated equipment, has improved the track and tunnels and thirty percent of the roadbed, and is in the process of resolving safety problems.

The railroad has begun to exhibit the creativity necessary to assist clients who are establishing new industries in the state.

Since transfer, the railroad has made a major effort to upgrade equipment. It has acquired \$28.3 million worth of new equipment on lease-purchase agreements. Major items include:

The railroad has acquired \$28.3 million worth of new equipment on lease-purchase agreements.

Equipment Purchases

- 13 locomotives
- 45 triple TOFC cars
- 5 self-propelled passenger coaches
- track maintenance equipment (\$5 million)
- 3 locomotive cranes
- 130 ton crane
- computer hardware
- 8 passenger coaches

During the same period, 40 pieces of outdated equipment were retired.

The railroad has invested \$21.6 million in capital improvements to the track, tunnels and roadbed. In the first two years of state ownership, the railroad replaced 52,939 cross ties, 134,276 feet of rail and 125,650 cubic yards of ballast.

The 1986 Performance Audit Report noted that the general condition of the track had improved. Automated track inspections by an independent contractor in May 1985 and September 1986 showed an overall improvement in the condition of the track.

The capital program was reduced for 1987 and 1988 to accommodate budget reductions and flood damage repair, but plans for the 1989-1993 period call for the replacement of 179,000 ties, 190,000 feet of rail and 480,000 cubic yards of ballast.

The Alaska people are fortunate to have the railroad intact and operating as a viable, profit-making entity. To date, railroad management has skillfully addressed the task of revamping a government agency into a public-private corporation. Ahead lies the equally challenging assignment of expanding the railroad system to tap a wide range of resources which otherwise will be unavailable for use and export.

The public must ensure that Alaska's elected officials insulate the corporation's operations from political meddling. At the same time, those who set policy in this "owner state" must take the initiative to enlarge the railroad's contribution to the overall statewide economy.

Methodology

The seventeen-member Commonwealth North Railroad Committee was chaired by Loren Lounsbury, businessman, engineer and former Commissioner of Commerce and Economic Development at the time of the transfer of the Alaska Railroad from federal to state ownership. The Vice-chairman was Frank Danner, Tax Partner with Peat, Marwick, Main & Company.

The committee was made up of community leaders including engineers, CPA's, attorneys, mineral geologists and mining experts, business executives and individuals with experience in commercial real estate.

Over 800 hours of volunteer time was dedicated to the project. Some 50 individuals including most of the executives at the Alaska Railroad, key legislators, railroad users and critics were interviewed.

The subcommittee charged with exploring future extensions for the Alaska Railroad relied heavily on the experience of the Canadian National Railway and met at length with CN executives. The Canadian National has explored a wide range of strategies for financing and constructing rail systems for the purpose of moving minerals, timber and freight to market.

The report was written in draft form by three subcommittees: operations, sale option and economic development. The draft was then refined by the full committee and taken to the board of directors of Commonwealth North for review and finalization.

The committee is grateful to the many individuals who gave their time and effort to the project, with special thanks to the Alaska Railroad leadership, both management and labor, for their assistance and input.

The following is a list of individuals interviewed for the purposes of this study:

Individuals Interviewed for this Report

Senator Mitch Abood	Chairman, Senate State Affairs Committee; Member, Senate Transportation Committee
Rep. Al Adams	Chairman, House Finance Committee
Robert Ballow	Vice President, Anchorage Sand and Gravel, Inc.
Jim Blasingame	Director of Administration, Alaska Railroad
Rep. H. A. Boucher	Member, House Transportation Committee
Thomas J. Brewer	Attorney with Heller, Ehrman, White and McAuliffe, Seattle, Washington
Jim Campbell	Chairman of the Alaska Railroad Board of Directors
Bruce Carr	Manager of Financial Services, Alaska Railroad
Rep. Bette Cato	Chairman, House Transportation Committee
Myron Christy	Member of Alaska Railroad Board of Directors
James Clinton	Chairman, Alaska Railroad Leaseholders Association, Anchorage
Senator Jack Coghill	Chairman, Senate Resources Committee; Vice-chairman, Senate Transportation Committee
Lewis Dickinson	Member of the Alaska Railroad Board of Directors
John Duffy	Planning Director, Mat-Su Borough
Senator Bettye Fahrenkamp	Member, Senate Transportation Committee
Stan Hall	General Manager, Marketing, Canadian National Railways
Joe Hayes	Former Speaker of the State House of Representatives
Mark Hickey	Alaska Commissioner of Transportation and Public Facilities.
Larry Houle	Director, Real Estate, Alaska Railroad
Rep. Bill Hudson	Member, House Transportation Committee
Dorothy Jones	Mayor, Matanuska-Susitna Borough
Senator Lloyd Jones	Chairman, Senate Transportation Committee
Richard Knapp	Vice President, Marketing, Alaska Railroad
Herb Lang	President, Anchorage Sand and Gravel, Inc.
William L. Noll	Vice President, Suneel Alaska Corp. (Seward)
Rep. Drue Pearce	Member, House Transportation Committee
Jack Richardson	President, Craig Taylor Equipment, Inc. (Anchorage and Fairbanks)
Ron Sheardown	A member of the committee and a recognized authority in mineral development in both Alaska and Canada
Rep. Henry Springer	Chairman, Community and Regional Affairs Committee; Member, House Transportation Committee
T.J. Thrasher	Executive Director, Alaska Truckers Association
Mead Treadwell	Co-author of a 1982 Harvard Business School study of the Alaska Railroad and a proponent for privatization.
Ted Trueblood	Borough Engineer, Mat-Su Borough
Frank Turpin, Sr.	President and CEO of the Alaska Railroad
Jerry Valinske	Conductor for the Alaska Railroad and member of Alaska Railroad Board of Directors
Ross Walker	Vice President for Western Canada, Canadian National Railways
Obie Weeks	Chief Engineer, Alaska Railroad
Richard Whitbeck	Spokesman for the Alaska Truckers Association
Marvin Yetter	Vice President, Finance, Alaska Railroad

Commonwealth North is a nonprofit corporation organized and existing under the laws of the State of Alaska. Non-partisan in nature, its purpose is to inject enlightened vitality into the world of commerce and public policy.

In addition to providing a forum for national and international speakers, working committees study critical issues facing the state and nation and prepare well-researched action papers, such as this one.

The Commonwealth North Railroad Committee

Loren Lounsbury, Chairman
Frank Danner, Vice Chairman
Dick Barnes
Bob Bulmer
Robert Dickson
Joe Griffith
Joe Hayes
David Heatwole
John Herring

Walter J. Hickel
Max Hodel
Ray Latchem
Jeff Lowenfels
Jim McElroy
Malcolm Roberts
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