Legislative Fiscal Bureau

One East Main, Suite 301 • Madison, WI 53703 • (608) 266-3847 • Fax: (608) 267-6873
Email: fiscal.bureau@legis.wisconsin.gov • Website: http://legis.wisconsin.gov/lfb

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Freight Rail Preservation Program Bonding (DOT -- Local Transportation Assistance)

[LFB 2013-15 Budget Summary: Page 458, #1]

CURRENT LAW

The Department of Transportation's freight rail preservation program provides grants or loans for the acquisition of abandoned railroad lines or the rehabilitation or construction of rail facilities on existing, publicly-owned lines. Eligible applicants include local governments, railroads, current or potential users of rail service, or rail transit commissions organized by local governments for the preservation of rail service. Applicants are required to pay at least 20% of the cost of an acquisition of railroad track or an improvement project, but the Department may provide a loan to cover up to 15% of the total cost. No match is required for the acquisition of railroad property (exclusive of the railroad tracks and other improvements). Funding for the program is provided with transportation fund-supported, general obligation bonds.

GOVERNOR

Provide $60,000,000 in transportation fund-supported, general obligation bond authorization for the freight rail preservation program.

DISCUSSION POINTS

1. The primary purpose of the freight rail preservation program (FRPP) is to maintain and improve rail service on low-traffic rail lines that may otherwise be abandoned or fall into disrepair. By assuming the responsibility for the ownership and improvement of these lines, the state can allow a railroad to continue to profitably serve these lines. That is, since the railroads do not need to invest in the ownership and improvement of the rail, they can operate at a lower rate of

return than would otherwise be necessary to maintain service.

2. The state has been providing freight rail assistance since the late 1970s, a time when many railroad companies were abandoning unprofitable lines. Throughout the late 1970s and 1980s, grants were provided to local rail transit commissions to assist in the purchase of rail lines, to maintain service for customers and shippers dependent on rail service. Then, in 1992, an amendment to the Wisconsin Constitution allowed the state to issue debt for the direct acquisition and improvement of rail lines. Today, there are over 530 miles of publicly-owned track (typically a mix of state and local ownership) and the state shares ownership with an operating railroad in 87 additional miles.

3. Although the state has acquired some lines during the past few biennia, the recent focus of the program has generally been on the rehabilitation of tracks and bridges on the existing publicly-owned lines. [Over the past decade, about 89% of funds have been used for track rehabilitation and 11% have been used for acquisition.] Many of the tracks in the publicly-owned rail network were originally built 80 to 100 years ago, and are now severely deteriorated. These tracks often cannot accommodate 286,000-pound rail cars, which is the current industry standard, and trains are limited to a speed of below 25 miles per hour on 79% of the publicly-owned network and under 10 miles per hour on 43% of the network.

4. Rehabilitation projects funded under FRPP are designed to bring the tracks and bridges up to standards sufficient to accommodate 286,000-pound rail cars and allow for speeds of at least 25 miles per hour. At those standards, shipping efficiencies are greater since a train crew may carry more cargo in a shorter amount of time, lowering both labor and fuel costs. Once upgraded to that level, the operating railroad is required to perform the maintenance work necessary to keep the rail lines at those standards.

5. Advocates of the program point to the benefits of the acquisition and improvement of freight rail lines as a justification for the expenditure of public funds. First, improved freight rail lines assist many manufacturing, agricultural, and other businesses in shipping their products and delivering inputs. Wisconsin and Southern Railroad (WSOR), which is the primary operator on the state's publicly-owned lines, notes that it serves about 180 businesses on its network, most of which is on those lines. Second, moving freight by rail is more fuel efficient than by commercial truck for many products, particularly for bulk commodities, resulting in lower air emissions. Finally, the improvement of freight rail service may reduce wear on the local road and state highway system and reduce traffic congestion, if the improvement allows some companies to choose to ship by rail rather than by truck.

6. The $60,000,000 in bonds that would be authorized under the bill is twice the amount provided in the 2011-13 biennium, although it would match the amount provided in the 2009-11 biennium. The last two biennial budgets authorized more total bonds ($90,000,000) than the prior eight biennial budgets combined ($66,500,000), extending back to the first bonds issued under the program. The following table shows the bond authorization in each biennium since bonds were first issued for freight rail acquisition and rehabilitation. The amount proposed under the bill is also shown.

Freight Rail Preservation Program Bond Authorization

Biennium	Bond Authorization
1993-95	$10,000,000
1995-97	4,500,000
1997-99	4,500,000
1999-01	4,500,000
2001-03	4,500,000
2003-05	4,500,000
2005-07	12,000,000
2007-09	22,000,000
2009-11	60,000,000
2011-13	30,000,000
2013-15	60,000,000*

*Amount proposed in the bill.

7. With the increase in bonding provided in the last several biennia, the state has established one of the most aggressive freight rail assistance programs in the country. In a review of the freight programs of Wisconsin's neighbors for the Wisconsin Transportation Finance and Policy Commission, the Department found that assistance for the preservation of freight rail service on low-density lines in neighboring states is typically provided in the form of low- or no-interest loans. [Wisconsin also has a revolving loan program for rail improvements (the freight rail infrastructure improvement program), providing between $5 million and $8 million in low-interest loans annually using loan repayments. In recent years, this program has primarily been used by companies that ship by rail in order to construct or make improvements on loading or storage facilities or track spurs. The freight rail preservation program can also make loans, although no loans have been made under that program.]

8. Although Wisconsin's freight rail assistance program is larger than those in neighboring states, this does not necessarily mean that Wisconsin's expenditures in this area are not beneficial to the state's economy and transportation system. As noted above, the rail acquisitions and improvements may have preserved the viability of freight rail service and, by extension, the businesses that rely on that service, that would have otherwise been lost without that assistance. The Department also notes that, historically, Wisconsin generally faced more rail abandonments than did neighboring states, affecting industries that were dependent on rail service.

9. The Governor has announced his intention to proceed with the acquisition of a 70-mile segment of track from Madison to Reedsburg (as well as associated rail yard properties). The track is owned by Union Pacific Railroad (UP), but WSOR operates on the line under a lease agreement with UP. The two railroads conducted an appraisal of the property (exclusive of the rails and other infrastructure), which placed the value at $41 million, and UP has indicated that the net liquidation value of the rails (which is the basis of acquisition price) is between $7 million and $10 million. Under FRPP provisions, a grant would cover the full acquisition cost of the property and 80% of the value of the rail. At the full appraisal value, therefore, the acquisition cost could be

approximately $47 million to $49 million. However, the actual acquisition cost would be subject to negotiations with UP. In some cases, the state has purchased rail property for less than the initial appraisal value. For instance, for a 2009 acquisition of railroad yard property near Janesville, the initial appraisal was $4,000,000, but the property was purchased for $1,650,000, or 41% of the appraised value. This may be an extreme example, however, as the price paid for other recent purchases has been within 10% to 15% of the appraisal. If the Department enters into a purchase agreement, it is possible that the acquisition payment could occur over the course of several years, although the payment schedule would also be subject to negotiation.

10. WSOR operates on the UP line under a lease that expires in 2026. While the lease would ensure that rail service could continue though that date, WSOR and some of its customers have expressed a concern that the condition of the rails, and, in particular, the condition of the bridge crossing the Wisconsin River near Merrimac, will not allow continued service, or else would decrease operational efficiency. If the state were to acquire the UP line, then the tracks and bridge would be eligible for rehabilitation grants under FRPP.

11. The Department indicates that the bridge at Merrimac is the primary concern on the UP line. The Department estimates that a bridge rehabilitation project, which would extend its useful life by 25 years, would cost $4.2 million. A full bridge replacement, which would provide a longer life and would allow for 286,000-pound rail cars, could cost $35 million to $70 million.

12. The Sauk County Development Corporation and the UW-Extension recently conducted a survey of 10 current rail customers on the portion of the UP line north of the Wisconsin River to determine the impact of the potential loss of rail service. Of those businesses, five indicated that it would be "difficult" or "very difficult" to shift from rail shipping to truck shipping if rail service were discontinued, and others indicated that making this switch would be somewhat difficult. Based on these results, and by making various assumptions regarding the likelihood that businesses would leave Sauk County without rail service, the study estimated that the county could lose between 2,753 and 2,972 jobs if rail service is lost, due to both direct and indirect employment effects.

13. While the job losses identified by the Sauk County study would negatively impact that county, it is not necessarily the case that the state would lose this many jobs with the loss of rail service. In some cases, the loss of rail service to particular businesses may create additional business opportunities for other state firms, resulting in an overall employment shift. Furthermore, if the state does not acquire and improve the UP line, funds that would have been used for that purpose could be used for a different purpose, which could have positive economic benefits in other areas of the state.

14. Although the Governor has indicated an intention to purchase the UP line, the bill would not require the Department to allocate a portion of FRPP funds for the purchase. Whatever amount of bonds are provided, the Department would determine how to allocate the funds between rehabilitation and acquisition projects.

15. When fully issued, annual debt service on the proposed $60,000,000 in bonds would be approximately $4.2 million. Due to the time normally elapsed between a project approval or

acquisition and the time that bonds are actually issued, the bill does not reflect debt service on the proposed bonds during the 2013-15 biennium.

16. Debt service on the freight rail bonds issued to date is projected to be $6.4 million in 2013-14 and $6.6 million in 2014-15. However, there are nearly $80 million in bonds authorized for the program, which, although mostly committed to projects, remains unissued. Debt service payments can be expected to increase by approximately $5.6 million once these bonds are issued, bringing the total annual debt service on existing bonds to approximately $12 million.

17. The transportation fund, which is the source of debt service payments on freight rail bonds, includes revenue from the ad valorem tax on railroad property. Although there is no direct tie between the amount of revenue generated by any particular tax or fee in the transportation fund and the amount that is spent for the programs most closely related to that source, there may be some expectation that there should be a balance between particular revenues and their related expenditures. During the 2013-15 biennium, it is estimated that the ad valorem tax payments on railroads will be about $31 million annually, an amount that significantly exceeds the sum of debt service on freight rail bonds plus other SEG appropriations for freight rail-related programs ($3.9 million for railroad crossing installation and maintenance programs). Furthermore, even if all unissued freight rail bonds, plus the bonds proposed for the program under the bill were issued, railroad revenues would still exceed the total of debt service payments and other freight rail program funding.

18. Most of the tax is paid by the Class I railroads that operate in the state (Canadian National, Canadian Pacific, Burlington Northern, and Union Pacific), which generally do not directly benefit from freight rail preservation program projects. However, since one of the functions of Wisconsin & Southern Railroad's operations is to deliver rail cars to these larger railroad companies for long-haul shipment, the Class I railroads may indirectly benefit from the program.

19. Although revenues from railroad taxes exceed SEG funding for freight rail bond debt service and other freight rail programs, and would continue to do so if the Governor's proposed bonding level is approved, the continuing growth in total transportation fund debt service, mostly from the issuance of bonds for highway and bridge projects, has been an issue of concern over the past several biennia. Total transportation fund debt service under the bill would exceed 18% of total transportation fund revenues by the end of the biennium under the bond provisions of the bill, up from 13.4% in 2011-12. Given these concerns, the Committee may wish to reduce the overall level of bonding in the bill, including by reducing the authorization for freight rail projects.

20. The 2011-13 budget established the Transportation Finance and Policy Commission to examine transportation program funding and revenues and make recommendations on finance issues for the following ten-year period. In its review of the freight rail preservation program, the Commission based its decision on the percentage of currently-owned track that could be repaired over a ten-year period at various annual funding levels. In its final report, the Commission recommended annual funding of $15.6 million for rehabilitation, plus an additional $1.5 million annually for acquisition costs, for a biennial total of $34.2 million. At the recommended funding level, 74% of the currently-owned track could be upgraded by the end of the 10-year period, if that real funding level is maintained (increases provided to offset the effect of inflation). Compared to

the bill, this represents a reduction of $25,800,000 (Alternative 2a).

21. The Committee could decide that additional reductions are necessary to reduce the overall use of transportation bonding or to shift the use of bonds to other transportation programs. For instance, a decision to provide $30,000,000, the same amount of bonds as the 2011-13 biennium, would be a reduction of $30,000,000 relative to the bill (Alternative 2b). Establishing a more limited program, at $16,000,000, the average biennial authorization since the program's inception, would be a reduction of $44,000,000, relative to the bill (Alternative 2c). Under these alternatives, or the alternative discussed in the previous point, the Department may not have sufficient funds to complete the UP track acquisition, if the full purchase price is incurred during the biennium.

22. Although the Committee may wish to reduce the use of bonds due to concerns over the increasing share of transportation fund revenues devoted to debt service, even fairly significant reductions to the bill's proposed bonding level would not result in a decrease in this percentage in the short term. Under 10-year revenue and debt service projections prepared by the Department for the Transportation Finance and Policy Commission, debt service would approach 25% of transportation fund revenues if an average of $577 million in bonds were issued per biennium over the 10-year period. By comparison, the bill would authorize $794.2 million in transportation fund-supported bonding over the biennium (an amount that does not include $200 million in general fund-supported bonds for transportation). For additional information on transportation bonding and debt service, as well as the recommendations of the Transportation Finance and Policy Commission, see LFB Issue Paper #636.

ALTERNATIVES

1. Approve the Governor's recommendation to authorize $60,000,000 in transportation fund-supported, general obligation bonds for the freight rail preservation program.

2. Modify the Governor's recommendation by reducing the bond authorization under one of the following alternatives:

a. By $25,800,000, to provide a total of $34,200,000, which is the amount recommended for the program by the Wisconsin Transportation Finance and Policy Commission.

ALT 2a	**Change to Bill** Funding
BR	- $25,800,000

b. By $30,000,000, to provide a total of $30,000,000, the amount provided in the 2011-13 biennium.

ALT 2b	Change to Bill Funding
BR	- $30,000,000

c. By $44,000,000, to provide a total of $16,000,000 for the program, the average biennial authorization since the program's inception.

ALT 2c	Change to Bill Funding
BR	- $44,000,000

3. Delete provision.

ALT 3	Change to Bill Funding
BR	- $60,000,000

Prepared by: Jon Dyck