



National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Consolidated Financial Statements

September 30, 2004 and 2003

(With Independent Auditor's Report Thereon)



KPMG LLP
1660 International Drive
McLean, VA 22102

Independent Auditors' Report

The Board of Directors and Stockholders
National Railroad Passenger Corporation.:

We have audited the accompanying consolidated balance sheets of National Railroad Passenger Corporation (Amtrak or the Company) and subsidiaries as of September 30, 2004 and 2003, and the related consolidated statements of operations, comprehensive loss, cash flows and changes in capitalization for the years then ended. These consolidated financial statements are the responsibility of Amtrak's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The Company has a history of substantial operating losses and is highly dependent upon substantial Federal government subsidies to sustain its operations. There are currently no Federal government subsidies authorized or appropriated for any period subsequent to the fiscal year ending September 30, 2005 ("fiscal year 2005"). Without such subsidies, Amtrak will not be able to continue to operate in its current form and significant operating changes, restructuring or bankruptcy may occur. Such changes or restructuring would likely result in asset impairments.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Amtrak and subsidiaries as of September 30, 2004 and 2003, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

August 12, 2005

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Consolidated Balance Sheets

(In Thousands of Dollars, Except Share Data)

	September 30,	
	2004	2003
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 247,400	\$ 182,054
Accounts receivable, net of allowances of \$23,029 and \$33,707 at September 30, 2004 and 2003, respectively	64,862	79,231
Materials and supplies	121,356	111,720
Other current assets	43,360	32,077
Total current assets	476,978	405,082
Property and Equipment:		
Locomotives	1,588,017	1,639,375
Passenger cars and other rolling stock	2,934,447	2,995,201
Right-of-way and other properties	8,061,148	7,717,900
Leasehold improvements	225,174	216,807
Property and equipment, gross	12,808,786	12,569,283
Less - Accumulated depreciation and amortization	(4,704,188)	(4,273,951)
Total property and equipment, net	8,104,598	8,295,332
Other Assets, Deposits, and Deferred Charges:		
Escrowed proceeds on sale-leasebacks	844,923	836,778
Deferred charges, deposits, and other	398,787	404,707
Total other assets, deposits, and deferred charges	1,243,710	1,241,485
Total assets	\$ 9,825,286	\$ 9,941,899
LIABILITIES and CAPITALIZATION		
Current Liabilities:		
Accounts payable	\$ 216,858	\$ 328,381
Accrued expenses and other current liabilities	543,069	531,551
Deferred ticket revenue	65,842	79,942
Current maturities of long-term debt and capital lease obligations	129,135	119,466
Total current liabilities	954,904	1,059,340
Long-Term Debt and Capital Lease Obligations:		
Capital lease obligations	3,233,829	3,307,522
Mortgages	264,045	274,180
Equipment and other debt	174,736	191,373
Total long-term debt and capital lease obligations	3,672,610	3,773,075
Other Liabilities and Deferred Credits:		
Deferred state capital payments	406,737	335,656
Casualty reserves	210,797	217,676
Deferred gain on sale-leasebacks	482,628	504,773
Postretirement employee benefits obligation	216,284	183,304
Environmental reserve	46,064	31,351
Other	29,718	13,136
Total other liabilities and deferred credits	1,392,228	1,285,896
Total liabilities	6,019,742	6,118,311
Commitments and Contingencies		
Capitalization:		
Preferred stock - \$100 par, 109,396,994 shares authorized, issued and outstanding at September 30, 2004 and 2003	10,939,699	10,939,699
Common stock - \$10 par, 10,000,000 shares authorized, 9,385,694 issued and outstanding at September 30, 2004 and 2003	93,857	93,857
Debt and other paid-in capital	12,328,381	11,046,225
Accumulated deficit and comprehensive loss	(19,556,393)	(18,256,193)
Total capitalization	3,805,544	3,823,588
Total liabilities and capitalization	\$ 9,825,286	\$ 9,941,899

The accompanying Notes are an integral part of these Consolidated Financial Statements

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Consolidated Statements of Operations

(In Thousands of Dollars)

	Twelve Months Ended September 30,	
	<u>2004</u>	<u>2003</u>
Revenues:		
Passenger related	\$ 1,448,591	\$ 1,397,349
Commuter	118,612	258,002
Other	276,359	320,385
State capital payments	21,844	18,615
Total revenues	<u>1,865,406</u>	<u>1,994,351</u>
Expenses:		
Salaries, wages, and benefits	1,452,418	1,517,019
Train operations	187,329	190,456
Fuel, power, and utilities	183,971	183,673
Materials	148,938	156,064
Facility, communication, and office related	129,418	134,851
Advertising and sales	77,514	74,661
Casualty and other claims	89,012	117,657
Depreciation - net of amortization	551,370	583,908
Other	218,106	193,305
Indirect cost capitalized to property and equipment	(88,114)	(50,961)
Total expenses	<u>2,949,962</u>	<u>3,100,633</u>
Net loss from continuing operations before other (income) and expense	<u>1,084,556</u>	<u>1,106,282</u>
Other (Income) and Expense:		
Interest income	(74,152)	(74,069)
Interest expense	203,747	209,617
Other expense - net	<u>129,595</u>	<u>135,548</u>
Net loss from continuing operations	<u>1,214,151</u>	<u>1,241,830</u>
Net loss from discontinued operations	94,741	32,503
Net loss	<u>\$ 1,308,892</u>	<u>\$ 1,274,333</u>

The accompanying Notes are an integral part of these Consolidated Financial Statements

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Consolidated Statements of Comprehensive Loss

(In Thousands of Dollars)

	Twelve Months Ended September 30,	
	<u>2004</u>	<u>2003</u>
Net loss	\$ 1,308,892	\$ 1,274,333
Other Comprehensive (Income) Loss:		
Unrealized loss (gain) on derivatives	(2,731)	342
Unrealized loss (gain) on minimum pension liability adjustment	<u>(5,961)</u>	<u>5,961</u>
Comprehensive loss	<u>\$ 1,300,200</u>	<u>\$ 1,280,636</u>

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National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Consolidated Statements of Cash Flows

(In Thousands of Dollars)

	Twelve Months Ended September 30,	
	<u>2004</u>	<u>2003</u>
Cash Flows From Operating Activities:		
Net loss	\$ (1,308,892)	\$ (1,274,333)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation net of amortization	569,723	606,068
Impairment related to discontinued operations	82,388	-
Sale of property and settlement of litigation	(14,307)	(29,815)
Other	(7,141)	18,280
Changes in assets and liabilities:		
Accounts receivable	21,888	(4,721)
Materials and supplies	(11,187)	(8,706)
Other current assets	(8,552)	(6,460)
Other assets, deposits, and deferred charges	(45,672)	(68,425)
Accounts payable, deferred ticket revenue, and other current liabilities.....	(374)	46,950
Deferred federal and state capital payments	(21,844)	(2,369)
Other liabilities and deferred credits	63,508	27,783
Net cash used in operating activities	<u>(680,462)</u>	<u>(695,748)</u>
Cash Flows From Investing Activities:		
Purchases and refurbishments of property and equipment	(523,326)	(280,544)
Proceeds from disposals of property and equipment	2,943	25,431
Net cash used in investing activities	<u>(520,383)</u>	<u>(255,113)</u>
Cash Flows From Financing Activities:		
Proceeds from federal paid-in capital	1,266,383	994,565
Proceeds from federal and state capital payments	108,699	56,095
Proceeds from borrowings and lease financings	10,113	10,303
Repayments of debt and capital lease obligations	(119,004)	(96,854)
Net cash provided by financing activities	<u>1,266,191</u>	<u>964,109</u>
Net increase in cash and cash equivalents	65,346	13,248
Cash and cash equivalents-beginning of period	182,054	168,806
Cash and cash equivalents-end of period	<u>\$ 247,400</u>	<u>\$ 182,054</u>
Supplemental Disclosure of Cash Payments:		
Interest paid (net of amounts capitalized and non-cash defeased capital lease interest)	157,587	163,944
Supplemental Disclosure of Noncash Investing and Financing Activities:		
Reduction in fixed assets due to settlement of litigation	55,267	-
Refinancing of equipment obligations into capital leases	21,162	21,282
Property acquired with escrowed deposit	18,882	16,000
Other non-cash increases/(decreases) in property, includes accruals of amounts due for purchases	(3,529)	10,154
Debt and capital lease reduction through use of escrow deposits	4,472	4,258
Net property acquired through capital lease obligations	584	11,379
Net proceeds from affiliate's bond issuance held in escrow	-	49,587
Debt discharged through sale of subsidiary	-	21,051
Financed property acquisitions and improvements	-	500

The accompanying Notes are an integral part of these Consolidated Financial Statements

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Consolidated Statements of Changes in Capitalization

(In Thousands of Dollars)

	Preferred stock	Common stock	Debt and other paid-in capital	Accumulated deficit and comprehensive loss	Totals
Balance at September 30, 2002	\$ 10,939,699	\$ 93,857	\$ 10,044,339	\$ (16,975,557)	\$ 4,102,338
Federal paid-in capital	-	-	994,565	-	994,565
Federal capital and other payments	-	-	7,321	-	7,321
Net loss	-	-	-	(1,274,333)	(1,274,333)
Unrealized loss on derivatives and minimum pension liability adjustment ...	-	-	-	(6,303)	(6,303)
Balance at September 30, 2003	\$ 10,939,699	\$ 93,857	\$ 11,046,225	\$ (18,256,193)	\$ 3,823,588
Federal paid-in capital	-	-	1,266,383	-	1,266,383
Federal capital and other payments	-	-	15,773	-	15,773
Net loss	-	-	-	(1,308,892)	(1,308,892)
Unrealized gain on derivatives and minimum pension liability adjustment ...	-	-	-	8,692	8,692
Balance at September 30, 2004	\$ 10,939,699	\$ 93,857	\$ 12,328,381	\$ (19,556,393)	\$ 3,805,544

The accompanying Notes are an integral part of these Consolidated Financial Statements

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Notes to Consolidated Financial Statements

For the Years Ended September 30, 2004 and 2003

NOTE 1: NATURE OF OPERATIONS

The National Railroad Passenger Corporation (“Amtrak” or the “Company”) is a passenger railroad. The United States government (the “Federal Government”) through the United States Department of Transportation (the “DOT”) owns all issued and outstanding preferred stock. Its principal business is to provide rail passenger transportation service to the general public in the major intercity travel markets of the United States. The Company also operates commuter rail operations on behalf of several states and transit agencies, provides equipment and right-of-way maintenance services, and has leasing operations.

NOTE 2: BUSINESS CONDITION AND LIQUIDITY

Operations and Liquidity

Amtrak was incorporated in 1971 pursuant to the Rail Passenger Service Act of 1970 and is authorized to operate a nationwide system of passenger rail transportation. The Company has a history of recurring operating losses and is dependent on subsidies from the Federal Government to operate the national passenger rail system and maintain the underlying infrastructure. These subsidies are usually received through annual appropriations. Amtrak’s ability to continue operating in its current form is dependent upon the continued receipt of subsidies from the Federal Government.

The enactment on December 8, 2004 of the ‘Consolidated Appropriations Act, 2005’ (the “2005 Act”) as Public Law 108-447 authorizes the Secretary of the United States Department of Transportation (the “Secretary”) to make quarterly grants to Amtrak from a total appropriation of \$1.217 billion, subject to a 0.80% partial rescission that nets to \$1.207 billion available for distribution. The 2005 Act gives the Secretary oversight of the fiscal spending of the Company and enables the Secretary to make grants to the Company, to remain available until September 30, 2005, providing a maximum of \$717 million (reduced to \$711 million) for operating subsidy grants and \$500 million (reduced to \$496 million) for capital subsidy grants.

The Secretary may reprogram, at its discretion, up to \$2.5 million of the operating subsidy grant to fund the cost incurred by the Secretary to develop and implement a fair competitive bid process to assist states in introducing competition to provide higher quality rail service. The Secretary is authorized to retain up to \$4 million of the operating subsidy grant to be used to retain a consultant or consultants to assist the Secretary in preparing a comprehensive valuation of Amtrak’s assets. The Secretary may also reserve \$60 million, as directed by the Surface Transportation Board, to fund costs of commuter rail service should Amtrak cease operations. The \$60 million reserve is not subsidy specific and may reduce either or both amounts ultimately available to Amtrak as operating and capital subsidies. These amounts are subject to the partial rescission and may ultimately be made available to Amtrak during the fourth quarter of fiscal year 2005.

Amtrak and the Secretary are directed by the 2005 Act to agree on a schedule for the repayment in five annual installments beginning in fiscal year 2005 of the \$100 million loan grant by the Federal Railroad Administration (FRA) made in July 2002 (see Note 7) with such payments to be made within thirty days of enactment of each annual act, otherwise all principal and interest shall come due as provided for under the existing terms of the loan grant. Pursuant to this agreement, Amtrak made the first of five annual installments on January 7, 2005.

The Company has received \$1,141.3 million of the fiscal year 2005 appropriation through July 31, 2005. The Company believes that it can achieve its planned results and that it will receive the full amount appropriated under the 2005 Act. To the extent that less than the full appropriation is received from the DOT or the Company’s funding needs are greater than \$1.207 billion plus \$247.4 million of cash on hand, due to operating results or the unfavorable resolution of contingencies or other matters, the Company may not have sufficient funds to operate through the end of fiscal year 2005.

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Notes to Consolidated Financial Statements

Amtrak has requested a grant of \$1.820 billion from the Federal Government for fiscal year 2006. There are currently no Federal Government subsidies authorized or appropriated for years subsequent to September 30, 2005. To the extent that a regular appropriation has not been approved prior to October 1, 2005, the Company expects to receive interim Federal Government funding under continuing resolutions until the fiscal year 2006 funding is approved. There can be no assurances that the Company will receive adequate funding to continue operations in its current form in fiscal year 2006 and beyond. Failure to receive sufficient subsidies may result in severe operational changes and/or restructuring which would likely result in asset impairments and potential bankruptcy or reorganization.

NOTE 3: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The Consolidated Financial Statements reflect the consolidated operations of Amtrak: its three wholly owned subsidiaries, Chicago Union Station Company (CUS), Passenger Railroad Insurance, Limited (PRIL), and Penn Station Leasing, LLC (PSL); its 99.7% interest in Washington Terminal Company (WTC); and its 99% interest in 30th Street Limited, L.P. (TSL). In addition, Amtrak has consolidated certain operations owned by the Pennsylvania Economic Development Financing Authority (PEDFA) (see Note 7). All significant intercompany balances and transactions have been eliminated.

Reclassifications

Certain reclassifications have been made to the prior year's Consolidated Financial Statements and accompanying Notes to conform to the fiscal year 2004 presentation. These reclassifications have no effect on prior year reported net loss.

Cash Equivalents

All short-term investments with original maturities of less than 90 days are considered cash equivalents. Cash equivalents are stated at cost, which approximates fair value because of the short maturities of these instruments.

Accounts Receivable

Accounts receivable are recorded at the invoiced amount and do not bear interest. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing accounts receivable.

Materials and Supplies

Materials and supplies, which are stated at the lower of weighted-average cost or market, consist primarily of items for maintenance and improvement of property and equipment. An allowance for shrinkage and obsolescence is provided for materials and supplies based on specific identification and turnover rates.

Derivative and Hedging Activities

Amtrak periodically enters into heating oil contracts with durations of 12 months or less to manage a portion of the exposure to fluctuating diesel prices. Changes in the price of heating oil contracts have a high correlation to changes in the price of diesel fuel and therefore, qualify as cash flow hedges under Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Certain Hedging Activities" (SFAS 133), as amended. These derivative financial instruments, which inherently contain market risk, are generally effective in reducing fluctuations in cash flows. The market risk is the adverse effect on the value of heating oil contracts that results from a change in heating oil prices. The market risk is managed by monitoring parameters that limit the types and degree of market risk

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Notes to Consolidated Financial Statements

that may be undertaken. Amtrak does not enter into fuel hedge contracts for trading or speculative purposes.

Amtrak records the fair market value of fuel hedge contracts in "Other current assets" in the Consolidated Balance Sheets. On an ongoing basis, Amtrak adjusts the balance sheet to reflect the current fair market value of fuel hedge contracts. The effective portion of the related gains or losses on these contracts is deferred as a component of "Other comprehensive income". These deferred gains and losses are recognized in income in the period in which the related diesel fuel purchases being hedged are consumed and recognized in expense. The ineffective portion of the change in the value of the fuel hedge contracts is immediately recognized in income. Amtrak calculates the ineffective portion of the hedge performance using the dollar-offset method. The ineffective portions of the fuel hedge contracts are included as a component of "Fuel, power, and utilities" in the Consolidated Statements of Operations. If at any time the hedge no longer qualifies for hedge accounting treatment, expires, is sold, terminates, is exercised, or it becomes probable that the forecasted transaction will not occur, the net gain or loss accumulated in "Other comprehensive income" is reclassified into earnings.

For fiscal years 2004 and 2003, pursuant to SFAS 133, as amended, Amtrak recognized net decreases of \$4,895,000 and \$1,281,000, respectively, to fuel cost associated with these derivative fuel contracts. At September 30, 2004 and 2003, Amtrak had derivative fuel contracts with fair values of \$3,031,000 and \$1,352,000, respectively. The effective portions of these contracts, which qualify as cash flow hedges, amounted to an unrealized gain of \$2,389,000 and an unrealized loss of \$342,000 as of September 30, 2004 and 2003, respectively. The effective portion at September 30, 2004 will be reclassified into earnings during fiscal year 2005.

Property and Depreciation

Property and equipment are stated at cost, and are depreciated over their estimated useful lives on a straight-line basis. Property held under capital leases and leasehold improvements are depreciated over the shorter of their estimated useful lives or their respective lease terms. The remaining depreciable assets are depreciated under the group method of depreciation in which a single depreciation rate is applied to the gross investment in a particular class of property, despite differences in the service life or salvage value of individual property units within the same class. Upon normal sale or retirement of depreciable property, the cost less the net salvage value is charged to 'Accumulated depreciation' and no gain or loss is recognized. Significant premature retirements of depreciable property and the disposal of land are recorded as gains and losses at time of occurrence. Locomotives, passenger cars and other rolling stock are depreciated using useful lives ranging up to 35 years. Right-of-way and other properties (excluding land) are depreciated using useful lives ranging up to 105 years. Other equipment including computers, office equipment and maintenance equipment is depreciated using useful lives ranging up to 30 years. Expenditures that significantly increase asset values or extend useful lives are capitalized. Repair and maintenance expenditures, including preventative maintenance, are charged to operating expense when the work is performed. The cost of internally developed software is capitalized in accordance with Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" and amortized over its estimated useful life, which generally does not exceed 5 years. Amtrak capitalizes interest costs in connection with the construction of major facilities, locomotives, and passenger cars. Capitalized interest is recorded as part of the asset to which it relates and is depreciated over the asset's useful life. Interest of \$707,000 and \$838,000 was capitalized in fiscal years 2004 and 2003, respectively.

Casualty Losses and Claims

Provision is made for Amtrak's portion of the estimated actuarial liability for unsettled casualty and other claims. Personal injury liability and ultimate loss projections are undiscounted and estimated using standard actuarial methodologies. These actuarial methods include unasserted claims. As of September 30, 2004 and 2003, the current claims liability included in "Accrued expenses and other current

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Notes to Consolidated Financial Statements

liabilities” was \$105,500,000 and \$100,800,000, respectively. Included in “Deferred charges, deposits, and other” in the Consolidated Balance Sheets at September 30, 2004 and 2003, are estimated insurance recoveries of \$79,522,000 and \$68,364,000, respectively, which relate to loss events that Amtrak has incurred.

Advertising

The Company expenses advertising costs as incurred and reports these amounts in “Advertising and Sales” in the Consolidated Statements of Operations. Advertising expenses were \$36,216,000 and \$31,679,000 for the fiscal years ended September 30, 2004 and 2003, respectively.

Impairment of Long-Lived Assets

Properties and other long-lived assets are reviewed for impairment at a system-wide level whenever events or business conditions indicate that the carrying amount of such assets may not be fully recoverable.

If circumstances warrant, an impairment review is made at the component level for assets or groups of assets. Initial assessments of recoverability are based on estimates of undiscounted future net cash flows and include estimated future operating and capital funding expected to be received from the Federal Government over the expected lives of the assets. Where impairment is indicated, the assets are evaluated for sale or other disposition, and their carrying amount is reduced to fair value based on discounted net cash flows, or other estimates of fair value. In 2004, the Company recorded a significant impairment charge associated with exiting its ‘Mail and Express’ business (see Note 4).

The Company recorded an impairment charge, in addition to the amounts disclosed in Note 4, of approximately \$20.5 million associated with a group of locomotives and other rolling stock with a net book value of \$31.4 million that will be prematurely retired due to certain operational changes. This impairment charge is included in “Depreciation – net of amortization” in the Consolidated Statements of Operations. The impaired assets are subject to capital leases totaling \$36.7 million at September 30, 2004 and are included in “Capital lease obligations” in the Consolidated Balance Sheets. The impaired assets were reduced to their estimated fair value of \$10.9 million, based on current market quotes and values of similar assets, less costs to sell and are included in “Locomotives” and “Passenger cars and other rolling stock” in the Consolidated Balance Sheets as of September 30, 2004. The Company plans to sell or sublease some of these impaired assets, which could take longer than a year to complete.

The Company assumes future Federal Government funding at levels consistent with those discussed in Note 2 and historical funding in performing its impairment analysis. At this level of funding, the system-wide carrying amounts of the Company’s long-lived assets are recoverable. The Company believes that continued funding at historical levels is their best estimate of the future. If future Federal Government funding levels drop below these levels, substantial impairments may occur.

Revenue Recognition

“Passenger related” revenue in the Consolidated Statements of Operations, for fiscal years 2004 and 2003, includes ticket revenue, state contribution revenue associated with requested service provided by Amtrak beyond that included in the basic route system, and food and beverage revenue as shown below (in millions):

	2004	2003
Ticket	\$ 1,230.8	\$ 1,183.0
State contribution	137.4	136.0
Food and beverage	80.4	78.3
Total passenger related revenue	<u>\$ 1,448.6</u>	<u>\$ 1,397.3</u>

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

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These revenues are recognized as operating revenues when the related services are provided. Amounts received for tickets that have been sold but not used are reflected as "Deferred ticket revenue" in the Consolidated Balance Sheets.

"Commuter" revenue includes the revenues earned under contractual arrangements to operate various commuter rail services for a cost-based fee.

"Other" revenue, for fiscal years 2004 and 2003, includes other transportation revenue from use of Amtrak-owned tracks and other services, revenue from reimbursable engineering and capital improvement activities, commercial development revenue from station rent, right-of-way fees and retail rent, freight access fee revenue from the use of Amtrak-owned tracks by freight railroad companies, and one-time gains from non-recurring sales. Other revenue is as shown below (in millions):

	2004	2003
Other transportation	\$ 97.1	\$ 98.5
Reimbursable	88.9	93.7
Commercial development	58.0	55.5
Freight access fee	32.4	42.7
One-time gain	-	30.0
Total	<u>\$ 276.4</u>	<u>\$ 320.4</u>

"State capital payments" includes the amortization of state funds used to acquire depreciable assets. These state capital payments are deferred when received and amortized over the life of the related asset purchased with the funds. The unamortized amounts are included in "Deferred state capital payments" in the Consolidated Balance Sheets.

Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

Pursuant to the provisions of Title 49 of the United States Code, Section 24-301, Amtrak is exempt from all state and local taxes, including income and franchise taxes that are directly levied against the corporation. Accordingly, there is no provision for state and local income or franchise taxes recorded in the consolidated financial statements for the years ended September 30, 2004 and 2003 (see Note 9).

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Some of the most significant estimates include: estimates of casualty reserves, environmental reserves, and other postretirement employee benefits expense and obligations [including expected return on plan assets, discount rates, rate of future compensation increases, and healthcare cost trend rates (see Note 12)], reserves for uncollectible accounts receivable, estimates of fair market value of assets held for sale, estimated useful lives of property and equipment, recoverability of long-lived assets, and reserves for inventory obsolescence.

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Notes to Consolidated Financial Statements

NOTE 4: DISCONTINUED OPERATIONS

SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", requires that a disposal of a 'component of an entity' comprising operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes from the rest of the entity, be reported as discontinued operations if: 1) the operations of the component have been or will be eliminated from the ongoing operations of the entity as a result of the disposition activity, and 2) the entity will not have any significant continuing involvement in the operations of the component after the disposal transaction.

On September 3, 2004, the Company announced its intent to exit 'Mail and Express' operations to focus on its core passenger service business. The 'Mail and Express' operations meet the definition of a 'component of an entity' and have been accounted for as a discontinued operation under SFAS 144. The 'Mail and Express' operations incurred a net loss of approximately \$94.7 million and \$32.5 million in fiscal years 2004 and 2003, respectively. Included in the fiscal year 2004 results is an impairment charge of \$82.4 million.

Amtrak evaluated 'Mail and Express' long-lived assets with an original cost of \$214.5 million and a net book value of \$105.9 million and recorded an \$82.4 million impairment charge. The recorded values of these assets were reduced to \$23.5 million, which is the lower of estimated fair value or net book value less cost to sell. As of September 30, 2004, \$104.2 million is included in "Capital lease obligations" in the Consolidated Balance Sheets related to these assets. The Company expects to sell assets with a net book value of \$8.8 million during the next fiscal year. Additionally, the Company may sell or sublease assets with a net book value of \$14.7 million, which in certain instances may take longer than a year to complete. The remaining assets were abandoned during fiscal year 2004.

Summarized financial information for the discontinued operations of 'Mail and Express' is as follows (in millions):

Results of Discontinued Operations:	2004	2003
Total revenues	\$ 66.1	\$ 79.6
Total operating expenses	(78.4)	(112.1)
Impairment	(82.4)	-
Net loss from discontinued operations	<u>\$ (94.7)</u>	<u>\$ (32.5)</u>
Financial Position of Discontinued Operations:	2004	2003
Current assets	\$ 1.0	\$ 2.9
Property and equipment, net	23.5	123.9
Current lease obligations	(9.0)	(10.4)
Other current liabilities	(3.1)	(3.7)
Long-term lease obligations	(95.2)	(107.2)
Net (liabilities) assets of discontinued operations	<u>\$ (82.8)</u>	<u>\$ 5.5</u>

NOTE 5: ACCOUNTING AND REPORTING FOR FEDERAL PAYMENTS

Certain funds are provided to Amtrak through federal payments for capital and operating expenditures. These federal payments, which are recorded as paid-in capital when received, totaled \$1,266.4 million and \$994.6 million for fiscal years 2004 and 2003, respectively. The remainder of the fiscal year 2003 appropriation of \$48.6 million was received in October 2003. Certain other federal funds that are provided and restricted for use on designated projects are also recorded as paid-in capital when received, and these totaled \$15.8 million and \$7.3 million for fiscal years 2004 and 2003, respectively.

National Railroad Passenger Corporation and Subsidiaries (Amtrak)

Notes to Consolidated Financial Statements

“Debt and other paid-in capital”, included in the Consolidated Balance Sheets, includes certain funding received from the Federal Government to finance acquisition of and improvements to property and equipment. In exchange for funding, Amtrak issued two promissory notes to the United States. The first note with a balance of \$4.0 billion was issued in 1976 and matures on December 31, 2975, and is secured by the real and personal property of Amtrak, WTC, CUS, PRIL, and TSL. The second note with a balance of \$1.1 billion was issued in 1983 and matures on November 1, 2082, with successive 99-year renewal terms, and is secured by all the rolling stock owned by Amtrak. Neither of the notes bears interest, unless prepaid which Amtrak does not intend to do. The Federal Government's security interest in Amtrak's rolling stock entitles it to repayment plus interest in the event Amtrak ceases operations, is acquired by another entity, or seeks relief under bankruptcy or insolvency laws. The amount due to the Federal Government on the first note may be accelerated by enactment of federal law or upon the occurrence of an event of default under the leases and mortgage entered into by Amtrak and PSL on June 20, 2001 (see Note 7), or upon the occurrence of various actions concerning an Amtrak bankruptcy, reorganization, or assignment for the benefit of creditors.

NOTE 6: PREFERRED AND COMMON STOCK

For funds received from the Federal Government prior to December 2, 1997, the Rail Passenger Service Act (49 U.S.C. 24304) required Amtrak to issue to the Secretary of Transportation preferred stock equal in par value to all federal operating payments and most federal capital payments received subsequent to October 1, 1981, as well as capital and certain operating payments received prior to that date. At September 30, 2004 and 2003, 109,396,994 shares of \$100 par value preferred stock were authorized, all of which were issued and outstanding. All issued and outstanding preferred shares are held by the Secretary of Transportation for the benefit of the Federal Government. The Amtrak Reform and Accountability Act of 1997 (the Act) resulted in significant modifications to Amtrak's capital structure. Prior to the Act, dividends were to be fixed at a rate not less than 6% per annum, and were cumulative. No dividends were ever declared. The Act abolished the voting rights and the liquidation preference of the preferred stockholder and the 6% minimum annual cumulative preferred stock dividend; and established that no additional preferred stock be issued by Amtrak in exchange for federal grants received. At the time of enactment of the Act, the minimum undeclared cumulative preferred dividend in arrears for all series issued and currently outstanding approximated \$5.8 billion and ranged between \$0.02 and \$97.08 per share.

At September 30, 2004 and 2003, 10,000,000 shares of \$10 par value common stock were authorized, of which 9,385,694 shares were issued and outstanding. The common stockholders, who acquired their stock from four railroads whose intercity rail passenger operations Amtrak assumed in 1971, have voting rights for amendments to Amtrak's Articles of Incorporation proposed by the Board of Directors. The Act also required Amtrak to redeem at fair market value the shares of common stock outstanding as of December 2, 1997, by the end of fiscal year 2002.

Amtrak has discussed the redemption of the shares, but there has been no resolution of this matter between Amtrak and the owners. Amtrak does not believe that the common stock has value. Nevertheless, in an effort to comply with the Act, Amtrak has made an offer to redeem the stock for cash at a price of \$0.03 per share to the stockholders. By letter dated November 2, 2000, counsel for the four common stockholders responded to Amtrak and rejected the offer as inadequate. Amtrak is considering various courses of action.

National Railroad Passenger Corporation and Subsidiaries (Amtrak)
Notes to Consolidated Financial Statements

NOTE 7: MORTGAGES AND DEBT

Total debt in the Consolidated Balance Sheets consisted of the following at September 30, 2004 and 2003 (in thousands):

Long-Term Debt:	2004		2003	
	Current	Long-Term	Current	Long-Term
FRA loan	\$ 17,119	\$ 82,881	\$ -	\$ 100,000
Mortgage obligations	10,135	264,045	9,518	274,180
Equipment obligations	-	1,723	2	500
Note payable	-	-	20,000	-
Bonds, net of discount	630	78,815	-	79,426
UDAG loan	130	11,317	130	11,447
Total	<u>\$ 28,014</u>	<u>\$ 438,781</u>	<u>\$ 29,650</u>	<u>\$ 465,553</u>

Credit Facilities

On September 22, 2003, Amtrak entered into a \$19 million unsecured revolving letter of credit facility that expired on June 27, 2005 and was not renewed. Commitment fees and interest rates payable under these credit facilities are similar to fees and rates available to comparably rated investment-grade borrowers. At September 30, 2004 and 2003, there were letters of credit outstanding of \$4,190,000 and \$7,807,000, respectively.

Federal Railroad Administration (FRA) Loan

On July 3, 2002, Amtrak executed a \$100 million interest-bearing conditional loan under the Federal Railroad Administration's "Railroad Rehabilitation and Improvement Financing Program" for qualified capital expenditures. The loan bears interest at 1.81% per annum and is secured by various Amtrak-owned right-of-way properties and facilities. This loan requires Amtrak's compliance with certain conditions which include: improving financial controls and accounting transparency, submission of monthly performance reports, and a list of expense reduction options to Congress and the DOT. Under the 2005 Act, Amtrak is required to repay the loan in five annual installments beginning with fiscal year 2005 (See Note 2).

Mortgage Obligations

In June 2001, PSL mortgaged a substantial portion of improvements located at Penn Station in New York, New York for \$300 million at a fixed rate of interest of 9.25% per annum, which increased to 9.50% effective October 1, 2002, receiving net cash proceeds of \$296,249,000. Of this amount, \$34,280,000 was deposited into escrow for the benefit of the lender and is reflected in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets. Semi-annual principal plus interest payments are due on the mortgage through maturity in June 2017. At September 30, 2004 and 2003, the outstanding balance due on the mortgage was \$274,180,000 and \$283,440,000, respectively.

In December 2000, Amtrak acquired land and office facilities located in Connecticut in exchange for \$2,750,000 cash and a \$2,750,000 mortgage note bearing a fixed rate of interest of 9.0% per annum. Monthly principal and interest payments were due through December 2003. The note was secured by the land and office facilities. At September 30, 2003, the outstanding balance due on the note was \$258,000. During November 2003, Amtrak paid the remaining balance due on the mortgage note and obtained a release of mortgage.

Equipment Obligations

Under separate financing arrangements, Amtrak was allowed to borrow up to \$870 million toward the construction and acquisition of high-speed locomotives and trainsets, and related maintenance facilities.

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As of September 30, 2004 and 2003, the Company had borrowed a total of \$793 million and \$761 million, respectively. Upon delivery of the locomotives and trainsets, and the completion of the maintenance facility, Amtrak refinanced the related outstanding advances under capital leasing arrangements. As of September 30, 2004 and 2003, outstanding advances made on Amtrak's behalf under these arrangements totaled \$1,723,000 and \$500,000, respectively. All outstanding advances at September 30, 2004, are secured by the final trainset. Interest charged is based on the London Interbank Offered Rate (LIBOR) and was capitalized during the construction phase.

Note Payable

Amtrak acquired a parking facility located in Chicago, Illinois in exchange for a \$20 million promissory note due in December 2003 bearing a fixed rate of interest. The seller secured the note with the parking facility as well as an irrevocable unconditional \$4 million letter of credit as collateral. In December 2003, Amtrak paid the remaining balance due on the promissory note, obtained a lien release, and cancelled the letter of credit.

Bonds and Grant

On January 7, 2003, PEDFA issued \$50 million Revenue Bonds (the "PEDFA Garage Bonds") for the purpose of financing the construction and other related costs of a parking garage located at the 30th Street Station in Philadelphia, PA. The bonds have multiple maturities ending on June 1, 2033. The bonds were issued at a discount of \$588,000 and bear interest, by individual maturities, at fixed rates ranging from 4.500% to 5.875%. The parking garage reached substantial completion by June 2004 and was constructed in air rights owned and leased by Amtrak to PEDFA. On December 15, 2002, Amtrak entered into a "Pledge and Security Agreement" (the "Pledge") with PEDFA under which Amtrak guarantees the payment of the principal and interest on the PEDFA Garage Bonds and under which Amtrak's liability is limited to a pledge of: 1) the rent received or receivable by Amtrak under the air rights lease during the fiscal year in which a demand for payment is made, and 2) the additional parking facilities revenues, as defined in the Pledge. Under these agreements (and certain other related agreements), revenue generated from the parking garage will first be used to fund the operations of the parking garage, second to pay principal and interest payments on the PEDFA Garage Bonds, third to reserve certain amounts for future repairs and maintenance of the parking garage, and fourth any excess will be paid to Amtrak subject to amounts that may be owed to the builder of the parking garage as contingent purchase price. Amtrak has recognized PEDFA's \$50 million bond obligation in "Equipment and other debt" in the Consolidated Balance Sheets. Amtrak has recorded capital expenditures in the amount of \$28,469,000 related to the construction of the parking garage in "Right-of-way and other properties" in the Consolidated Balance Sheets as of September 30, 2004. The remaining net bond proceeds are recorded in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets and was \$13,386,000 as of September 30, 2004.

Included in TSL's long-term debt at September 30, 2004 and 2003, is \$30 million of Philadelphia Authority for Industrial Development (PAID) tax-exempt private-activity bonds (the "PAID Bonds") issued by PAID for the benefit of TSL's rehabilitation of 30th Street Station (the "Station") in the city of Philadelphia (the "City"), Pennsylvania. The PAID Bonds were issued on December 30, 1987, mature on January 1, 2011, and bear interest at a fixed or variable rate payable until maturity at intervals determined under provisions in the bond indenture. No payments of bond principal prior to maturity are required. Amtrak is periodically required to make annual deposits into a sinking fund to be used to pay off the bonds when they mature. As of September 30, 2004 and 2003, aggregate deposits into the fund were \$10,432,000 and \$8,798,000, respectively, which are included in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets. The PAID Bonds are subject to optional tender by the bondholders in the case of significant events, specifically those pertaining to any damage to, destruction of, or condemnation of the Station facilities. TSL has executed a liquidity facility, which provides funds to purchase the bonds surrendered under the optional tender provisions.

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TSL has a non-interest bearing obligation of \$11,447,000 and \$11,577,000 to the City under an Urban Development Action Grant (UDAG) loan agreement as of September 30, 2004 and 2003, respectively. Principal is being repaid in \$130,000 annual installments each November through 2011, with the balance due in November 2012. The City's rights under the UDAG loan agreement are secured by a leasehold mortgage.

Interest Rates

Per annum weighted-average percentage interest rates by debt type for all interest-bearing borrowings at September 30, 2004 and 2003 are shown below (in percentages of 100%):

	<u>2004</u>	<u>2003</u>
FRA loan	1.81	1.81
Mortgage obligations	9.50	9.50
Equipment obligations	2.74	2.06
Note payable	-	9.00
Bonds	4.07	3.94

The overall weighted-average interest rate on all interest-bearing borrowings is 6.8% and 7.0% per annum at September 30, 2004 and 2003, respectively.

Scheduled Debt Maturities

At September 30, 2004, scheduled maturities of debt over the next five years and thereafter are as follows (in thousands):

2005	\$ 28,014
2006	32,147
2007	33,622
2008	35,194
2009	36,872
Thereafter	<u>301,500</u>
Total	<u>\$ 467,349</u>

Amtrak is subject to various covenants and restrictions under its borrowing arrangements. A default by Amtrak or acceleration of Amtrak's indebtedness may result in cross-default to other Amtrak indebtedness, and may have a material adverse effect on the Company. Most of Amtrak's financing transactions require that Amtrak deliver its audited annual financial statements within 90 to 120 days of the end of its fiscal year. Amtrak has not delivered within this timeframe its audited financial statements for fiscal year 2004. Amtrak has at least a 30-day grace period that commences on written notice to Amtrak of its breach. Amtrak may cure the technical default and avoid a defined Event of Default, by delivering the statements and certificates prior to lapse of this grace period. To date, Amtrak has not received any written notice of its breach. Excluding the foregoing, Amtrak is in compliance with all of its covenants.

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NOTE 8: LEASING ARRANGEMENTS

Facilities

During fiscal year 2001, PEDFA completed two separate issues of exempt facilities revenue bonds, the net proceeds of which were used to finance a portion of the costs associated with Amtrak's construction of a frequency converter facility (the "Facility"). The first series (Series A) totaling \$110,795,000 was issued in February 2001 at a \$795,000 discount, netting \$110 million. The second series (Series B) totaling \$45 million was issued in April 2001 at par. Amtrak procured the bond proceeds of each issue through a lease and leaseback arrangement with PEDFA. Under this arrangement, Amtrak awarded title to and ownership of the Facility to PEDFA until November 2041 under a ground lease, in exchange for the total net proceeds. Simultaneously, Amtrak is leasing back from PEDFA the Facility through June 2033, with an option to extend this term through November 2041. PEDFA also has the right to extend Amtrak's leaseback term through November 2041. At the conclusion of the ground lease, title to and ownership of the Facility will revert to Amtrak. Amtrak's leaseback rentals are funding PEDFA's debt service requirements for both the Series A and Series B bonds. Amtrak's rentals are due semi-annually for the Series A bonds, and monthly for the Series B bonds. With the bond proceeds, Amtrak used \$3,343,000 toward financing arrangement costs, and discharged \$85,453,000 of interim debt associated with the Facility's construction. The remaining \$66,204,000 of proceeds remained on deposit with the bond trustee and was earmarked for use toward Amtrak's leaseback payments, further Facility construction costs, and additional financing arrangement costs. Amtrak recorded a \$155 million capital lease obligation, \$3,343,000 of deferred financing costs, and \$66,204,000 of deferred deposits. Amtrak's sublease rentals consist of an interest and principal portion, with the latter scheduled to pay down this capital lease obligation over the sublease's initial and option terms.

Equipment

Amtrak leases equipment, primarily passenger cars and locomotives, under capital leasing arrangements. At September 30, 2004 and 2003, the gross amount of assets recorded under capital leases was \$3,749,581,000 (38% for locomotives, 60% for passenger cars, and 2% for other assets), and \$3,672,521,000 (37% for locomotives, 60% for passenger cars, and 3% for other assets), respectively, with accumulated amortization of \$1,177,952,000 and \$974,742,000, respectively.

During 2000, Amtrak entered into four separate defeased sale and leaseback transactions involving passenger cars. In exchange for \$915,155,000 consisting of net cash proceeds and set-aside assets in the form of defeasance instruments, Amtrak sold the cars having a net book value of \$334,690,000, resulting in a deferred gain of \$580,465,000. The defeasance instruments are held by the buyers, and Amtrak accretes value at fixed interest rates of approximately 6.8% to 8.8% per annum. Simultaneously, Amtrak leased back the cars under capital leases over terms ranging from 23 to 28 years. The set-aside assets together with future accreted interest are designated toward satisfying Amtrak's rent payment obligations under the capital leaseback arrangements. The assets economically defease, but do not legally defease Amtrak's obligations under the leasebacks. Consequently, the set-aside assets plus accreted interest are not netted against the capital lease obligations, but instead are presented as "Escrowed proceeds on sale-leasebacks" in the Consolidated Balance Sheets. The \$580,465,000 gain on the sales was deferred and is being amortized into income as a reduction to depreciation expense over the terms of the capital leasebacks.

During fiscal years 2004 and 2003, \$22,145,000 of deferred gains on these transactions was amortized in each year.

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At September 30, 2004, future minimum lease payments under capital leases including amounts from defeasance trusts were as follows (in thousands):

2005	\$ 277,955
2006	277,792
2007	280,431
2008	288,054
2009	309,808
Thereafter	<u>3,833,646</u>
Total payments	5,267,686
Less amount representing interest	<u>1,932,736</u>
Present value of minimum lease payments at September 30, 2004	<u><u>\$ 3,334,950</u></u>

The current portion of capital lease obligations at September 30, 2004 and 2003 was \$101,121,000 and \$89,816,000, respectively, and is included in “Current maturities of long-term debt and lease obligations” in the Consolidated Balance Sheets.

The Company, as lessee, has entered into equipment leasing agreements for which the underlying leased equipment is the collateral and is required to be maintained in good operating condition. Estimated repair costs for damaged leased equipment was \$50,741,000 and \$38,078,000 at September 30, 2004 and 2003, respectively, and is recorded in “Accrued expenses and other current liabilities” in the Consolidated Balance Sheets. The amounts expensed relating to these items is reflected in “Materials” expense in the Consolidated Statements of Operations in the period in which the damage occurred.

Amtrak is subject to various covenants and restrictions under its leasing arrangements. A default by Amtrak or acceleration of Amtrak’s indebtedness may result in cross-default to other Amtrak indebtedness, and may have a material adverse effect on the Company. Most of Amtrak’s leasing transactions require that Amtrak deliver its audited annual financial statements within 90 to 120 days of the end of its fiscal year. Amtrak has not delivered within this timeframe its audited financial statements for fiscal year 2004. Amtrak has at least a 30-day grace period that commences on written notice to Amtrak of its breach. Amtrak may cure the technical default and avoid a defined Event of Default, by delivering the statements and certificates prior to lapse of this grace period. To date, Amtrak has not received any written notice of its breach. Excluding the foregoing, Amtrak is in compliance with all of its covenants.

Operating Rights and Leases

At September 30, 2004, Amtrak was obligated for the following minimum rental payments, principally for station and office space, under operating leases that have initial or remaining non-cancelable lease terms in excess of one year (in thousands):

2005	\$ 12,063
2006	11,408
2007	11,036
2008	8,554
2009	4,128
Thereafter	<u>26,931</u>
Total	<u><u>\$ 74,120</u></u>

Rent expense for the years ended September 30, 2004 and 2003 was \$38,039,000 and \$41,388,000, respectively, and it is expected that future rent expense will be comparable.

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Most of the rights-of-way over which Amtrak operates are owned by other railroads some of which own Amtrak's common stock. Amtrak uses such trackage under contracts with these railroads. The terms of the agreements range from 5 to 15 years and costs incurred are based on usage. The total amount incurred for use of the railroads' rights-of-way in 2004 and 2003 totaled \$83.4 million and \$96.2 million, respectively. The majority of these expenses are reported in "Train operations" and "Fuel, power, and utilities" in the Consolidated Statements of Operations.

NOTE 9: INCOME TAXES

No provision for federal taxes has been recorded as the Company incurred net operating losses for the years ended September 30, 2004 and 2003. As of September 30, 2004, the Company had net operating loss carryforwards of approximately \$7.4 billion, which begin to expire January 1, 2010.

The provision for income taxes differed from the income tax benefit that would be computed based upon the statutory federal tax rates as a result of the recording of a valuation allowance equal to the increase in net deferred tax assets.

Net operating losses are the main component of net deferred tax assets. Based upon the Company's history of operating losses, it is management's judgment that it is not likely that the net deferred tax assets will be realized in future years. As a result, management has applied a full valuation allowance against the net deferred tax assets at September 30, 2004 and 2003.

NOTE 10: COMMITMENTS AND CONTINGENCIES

Insurance Claims

Amtrak maintains various insurance policies to cover its liability to employees and other parties for injury or damage resulting from accidents and to cover Amtrak's loss resulting from damage to Amtrak property. The insurance policies contain large deductibles; losses within the deductibles are self-insured by Amtrak.

The Amtrak Reform and Accountability Act of 1997 limits the amount railroad passengers may recover from a single accident to an aggregate of \$200 million. Since non-passenger liability is not so limited, Amtrak purchases excess liability insurance limits beyond this statutory cap. Amtrak operates a majority of its long distance passenger rail service on tracks owned by freight railroads. Amtrak indemnifies these railroads for certain liabilities that arise as a result of its operations on freight tracks. Its indemnity applies to bodily injury and property damage claims made by its employees and passengers; and third parties struck by its trains, and for damage to its equipment. The freight railroads indemnify Amtrak for bodily injury and property damage claims made by freight railroad employees and third parties off railroad property; and for damage to freight railroad equipment, lading and property.

Labor Agreements

Approximately 90% of Amtrak's labor force is covered by labor agreements. During fiscal year 2004, Amtrak reached an agreement on a new labor contract with one of the 14 labor organizations and joint councils representing Amtrak workers. The new contract affects approximately 2,000 employees, or 11 percent of Amtrak's labor force and covers the period of January 1, 2000 through December 31, 2004. As a result of agreements reached during fiscal years 2004 and 2003, approximately 35% of Amtrak's employees are now covered under new labor agreements. All other labor agreements currently in force were amendable as of January 1, 2000, and will remain in effect until new agreements are reached or the Railway Labor Act's procedures are exhausted.

Legal Proceedings

In December 1995, Amtrak entered into a \$321 million fixed-price contract with a joint venture consisting of Balfour Beatty Construction, Inc. and Mass. Electric Construction Co. ("BBC/MEC") for the

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design and construction of an electrified catenary system along Amtrak's Northeast Corridor right-of-way between New Haven, Connecticut and Boston, Massachusetts. To date BBC/MEC has made various claims alleging, among other things, problems with site conditions, design, owner-directed changes, work interference, and work schedule acceleration. The total value of the claims is approximately \$75 million, of which Amtrak has already paid approximately \$35 million. Therefore, the value of the unresolved claims is approximately \$40 million. Amtrak is vigorously defending all of the claims, none of which has been resolved finally by a court. Amtrak is asserting its own claims against BBC/MEC for a variety of contract non-compliance issues and is holding \$11 million in retainage against Amtrak's claims. No additional provision for claims against Amtrak is reflected in the accompanying Consolidated Financial Statements.

On November 8, 2001, Bombardier Corporation ("Bombardier") filed a complaint in the United States District Court for the District of Columbia against Amtrak alleging that Amtrak through various actions and failures caused Bombardier (as partner to a consortium along with Alstom Transportation, Inc., hereinafter, the "Consortium") to incur substantial additional costs related to the contracts for design and manufacture of high-speed electric trainsets and locomotives, and the related maintenance facilities (the "Contracts"). On March 16, 2004, Amtrak and the Consortium executed a settlement agreement resolving all outstanding issues between them in connection with the Contracts and dismissing the outstanding litigation between the parties. As part of the settlement, the Consortium agreed to complete specified modifications to the equipment, resolve outstanding technical issues, extend the warranty, and made certain commitments regarding the reliability of the equipment. The parties also agreed to transition the maintenance of the equipment to Amtrak on October 1, 2006 rather than in 2013 as originally agreed. Accompanying this transition were certain commitments by the Consortium to turn over source code, train employees, and provide options to Amtrak for the purchase of parts and inventory needed to maintain the equipment for the ten years following settlement. Amtrak agreed to pay up to \$42.5 million to the Consortium from funds previously withheld, as certain milestones are met between the settlement date and October 1, 2006. During fiscal year 2004, the Company recognized reductions of \$17.3 million to "Materials" expense in the Consolidated Statements of Operations and \$55.3 million to 'Property and Equipment' in the Consolidated Balance Sheets as a result of this settlement.

On October 23, 2003, ERC Frankona Ruckversicherungs-AG ("Frankona"), a reinsurer of portions of the excess liability and property insurance coverage which PRIL provides to Amtrak, filed suit against PRIL in the New York Supreme Court alleging that PRIL made material misrepresentations and omissions regarding Amtrak's loss history and seeking an order declaring the contracts null, void and rescinded. Subsequently, Frankona agreed to dismiss its New York action without prejudice. On November 21, 2003, PRIL and Amtrak filed suit against Frankona in the United States District Court for the District of Columbia for a declaratory judgment, breach of contract, bad faith, and other relief against Frankona resulting from its claim that the reinsurance contracts are rescinded, and Frankona filed a counterclaim seeking substantially the same recovery as in its New York action. If the contracts are declared null, void and rescinded, Amtrak would have additional uninsured liability and property claims of up to \$34.0 million and \$11.7 million, respectively, for certain accidents which occurred during the policy periods from October 1, 1998 to December 31, 2002 for liability, and from December 1, 1998 to December 1, 2002 for property coverage. Amtrak and PRIL have filed a motion for summary judgment seeking to require Frankona to make payments required under the reinsurance contracts while the action is pending, but the Court has not yet ruled on the motion. Fact discovery is currently being conducted by both sides. At this stage of the litigation, it is Amtrak's assessment that an outcome adverse to its interest, while possible, is not probable.

On August 19, 2003, former employees filed a class action lawsuit involving Amtrak's 2001 Voluntary Early Retirement Plan (VERP) in the United States District Court for the District of Columbia seeking to void a September 2001 amendment to the Amtrak Pension Plan that eliminated a monthly Railroad Retirement Supplement and replaced it with a one-time lump sum payment of \$15,000 per eligible employee. Additionally, the complaint seeks to "reopen" the window period to allow eligible employees to apply for the original benefits. Amtrak, the Retirement Plan Committee, and the Retirement Income Plan

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are also named as defendants. The ultimate outcome of this matter cannot be reasonably estimated at this time.

On August 13, 2004, the State of New York filed a federal court complaint against Amtrak. The complaint alleges that Amtrak breached a March 2000 contract relating to the remanufacture of seven Turboliner trainsets and improvements in infrastructure and facilities along the Empire Corridor in New York. New York seeks an injunction requiring Amtrak to specifically perform remanufacturing and infrastructure work, or in the alternative, damages in the amount of \$477.3 million, plus costs, disbursements and interest. Amtrak has filed an answer and affirmative defenses, denying New York's claims. In addition, Amtrak notified the State that the contract was terminated, to the extent not previously voided, rescinded, and/or Amtrak's obligations discharged. A scheduling order was issued on December 22, 2004, which gives the parties until March of 2006 to complete discovery. Amtrak is vigorously opposing the claims brought by New York and believes that the claims, even if found to be meritorious, are vastly overstated.

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

Commitments

Amtrak has entered into various agreements with states, cities and other local transportation authorities and private companies for railroad facility and infrastructure improvements and for the remanufacture and supply of railroad passenger equipment. The largest commitment arises from an agreement with the State of Pennsylvania. Under this contract, Amtrak agreed to fund a portion of the costs with a remaining scope of work at September 30, 2004 of approximately \$53.2 million. Amtrak has the right to terminate future work contemplated by this contract. In addition to the foregoing, Amtrak has a commitment of approximately \$32.0 million for infrastructure improvements whose term extends through project completion.

NOTE 11: ENVIRONMENTAL MATTERS

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

In 1976, Amtrak acquired its Northeast Corridor properties. It is Amtrak's policy to accrue estimated liabilities and capitalize such amounts of remediation costs relating to properties acquired with existing environmental conditions (not to exceed the net realizable value of the related property), and to expense remediation costs incurred on properties for environmental clean-up matters occurring after acquisition. The liability is periodically adjusted based on Amtrak's present estimate of the costs it will incur related to these sites and/or actual expenditures made. At September 30, 2004 and 2003, the reserve was \$57,494,000 and \$40,795,000, respectively. At September 30, 2004 and 2003, the current portion of the reserve was \$11,430,000 and \$9,444,000, respectively and is reported in "Accrued expenses and other current liabilities" in the Consolidated Balance Sheets. Of the reserve, \$48,873,000 and \$34,588,000 relate to estimated capitalizable costs to be incurred as of September 30, 2004 and 2003, respectively. Costs of future expenditures for environmental remediation obligations are not discounted to their present value. At September 30, 2004 and 2003, a deferred charge for each amount is included in "Deferred charges, deposits, and other" in the Consolidated Balance Sheets. Amtrak has not recorded any receivables for recoveries from other parties or from insurance because such recoveries are not sufficiently certain.

The ultimate liability for remediation is difficult to determine with certainty due to, among other factors, the number of potentially responsible parties, site-specific cost sharing arrangements, the degree

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and types of contamination, potentially unidentified contamination, developing remediation technology, and evolving statutory and regulatory standards. Amtrak's management and counsel believe that additional future remedial actions for known environmental matters will not have a material adverse effect on the results of operations or financial condition.

On November 8, 2004, Amtrak executed a settlement that resolves its entire outstanding polychlorinated biphenyl (PCB) cleanup cost claims against American Premier Underwriters (APU, the successor to Penn Central), Conrail, and Southeastern Pennsylvania Transit Authority (SEPTA) relating to the rail yard in Paoli, Pennsylvania. In February 2005, APU paid Amtrak \$15 million, in settlement of all of Amtrak's cleanup cost contribution claims. In addition, Amtrak's future liability for any further cleanup that the Environmental Protection Agency (EPA) may require for the Paoli rail yard will be limited to 15 percent. Amtrak will have no liability for any required cleanup of the non-rail yard properties, including the residual areas and the 400-acre watershed. Amtrak is formulating plans to pursue development of the clean portions of the 28-acre Paoli rail yard that Amtrak still owns. Accordingly, Amtrak agreed to perform and pay for the post-cleanup Operation and Maintenance program required by the EPA, which will continue for several decades.

NOTE 12: POSTRETIREMENT EMPLOYEE BENEFITS

Amtrak has a qualified noncontributory defined benefit retirement plan whose assets are held in trust covering nonunion employees and certain union employees who at one time held nonunion positions.

Amtrak provides medical benefits to its qualifying retirees and life insurance to some retirees in limited circumstances under its postretirement benefits program. Railroad agreement employees' life insurance benefits are covered by a separate policy purchased by Amtrak. Under Amtrak's postretirement benefits program, substantially all salaried employees may become eligible for medical benefits if they meet the service requirement and reach age 55 while they are working for Amtrak. Company-provided medical benefits are reduced when covered individuals become eligible for Medicare benefits or reach age 65, whichever comes first. Medical benefits are subject to co-payment provisions and other limitations.

Amtrak uses a June 30th measurement date for its postretirement benefit plans' actuarial valuations.

Obligations and Funded Status

The following tables provide a reconciliation of the changes in the plans' benefit obligations and fair value of assets over the two-year period ending September 30, 2004, and a statement of the funded status as of September 30, 2004 and 2003 (in thousands):

Reconciliation of Projected Benefit Obligation:	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Obligation at October 1,	\$ 194,510	\$ 164,738	\$ 397,544	\$ 228,478
Service cost	6,686	6,330	15,557	8,053
Interest cost	11,478	11,723	22,887	16,295
Actuarial loss (gain)	(6,042)	18,698	80,916	164,225
Effect of curtailment	-	(774)	-	(12,221)
Benefit payments	(6,793)	(6,205)	(11,476)	(7,286)
Change due to Medicare Part D subsidy	-	-	(39,525)	-
Obligation at September 30,	<u>\$ 199,839</u>	<u>\$ 194,510</u>	<u>\$ 465,903</u>	<u>\$ 397,544</u>

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Reconciliation of Fair Value of Plan Assets:	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Plan assets at October 1,	\$ 158,073	\$ 157,470	\$ -	\$ -
Actual gain on plan assets	19,225	6,808	-	-
Employer contributions	-	-	11,476	7,286
Benefit payments	(6,793)	(6,205)	(11,476)	(7,286)
Plan assets at September 30,	<u>\$ 170,505</u>	<u>\$ 158,073</u>	<u>\$ -</u>	<u>\$ -</u>

Funded Status:	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Funded status at October 1,	\$ (29,334)	\$ (36,437)	\$ (465,903)	\$ (397,544)
Unrecognized prior service cost	864	1,061	14,851	15,977
Unrecognized loss	16,915	30,917	226,161	196,438
Additional minimum liability	-	(7,022)	-	-
Net liability recognized in Consolidated Balance Sheets	<u>\$ (11,555)</u>	<u>\$ (11,481)</u>	<u>\$ (224,891)</u>	<u>\$ (185,129)</u>
Accumulated Benefit Obligation (ABO) at September 30,	<u>\$ 174,648</u>	<u>\$ 169,554</u>	<u>\$ 465,903</u>	<u>\$ 397,544</u>

Amtrak recorded an additional minimum pension liability of \$7,022,000 to other long-term liabilities as a result of the ABO exceeding the fair value of plan assets at September 30, 2003. Offsetting this liability was \$1,061,000 of unrecognized prior service cost recorded as a deferred charge and \$5,961,000 of unrealized comprehensive loss recorded as a reduction to equity. No additional minimum pension liability was required for 2004.

Pension and other postretirement benefit amounts recognized in the Consolidated Balance Sheets at September 30, 2004 and 2003 are as follows (in thousands):

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Accrued liability	\$ (11,555)	\$ (11,481)	\$ (224,891)	\$ (185,129)
Intangible assets	-	1,061	-	-
Accumulated other comprehensive loss	-	5,961	-	-
Net amount recognized	<u>\$ (11,555)</u>	<u>\$ (4,459)</u>	<u>\$ (224,891)</u>	<u>\$ (185,129)</u>
Plus: Additional minimum liability	-	(7,022)	-	-
Total amount recognized	<u>\$ (11,555)</u>	<u>\$ (11,481)</u>	<u>\$ (224,891)</u>	<u>\$ (185,129)</u>

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Information for pension plans with an accumulated benefit obligation in excess of plan assets (in thousands):

	Pension Benefits at September 30,	
	2004	2003
Projected benefit obligation	\$ 199,839	\$ 194,510
Accumulated benefit obligation	\$ 174,648	\$ 169,554
Fair value of plan assets	\$ 170,505	\$ 158,073

Components of Net Periodic Benefit Cost

The following table provides the components of net periodic benefit cost for the plans for fiscal years 2004 and 2003 (in thousands):

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Service cost	\$ 6,686	\$ 6,330	\$ 15,557	\$ 8,053
Interest cost	11,478	11,723	22,887	16,295
Expected return on plan assets	(12,389)	(12,354)	-	-
Amortization of prior service cost	197	203	1,126	1,203
Amortization of net loss	1,123	-	11,667	1,690
Curtailment loss	-	28	-	1,093
Net periodic benefit cost	<u>\$ 7,095</u>	<u>\$ 5,930</u>	<u>\$ 51,237</u>	<u>\$ 28,334</u>

The prior service costs are amortized on a straight-line basis over the average remaining service period of active participants for both plans. Gains and losses in excess of 10% of the greater of the benefit obligation or the market-related value of assets are amortized over the average remaining service period of active participants.

Plan Assets

The pension plan's assets consist primarily of U.S. equity investments, U.S. fixed income investments, and international equity investments. The other postretirement benefits program has no plan assets. Amtrak funds the other postretirement benefits program on a pay-as-you-go basis. Amtrak's pension plan asset allocations at September 30, 2004 and 2003 by asset category are as follows:

	Plan Assets at September 30,	
	2004	2003
U.S. equity securities	52.7%	47.0%
International equity securities	10.6%	11.1%
U.S. fixed income securities	34.4%	38.8%
Other	2.3%	3.1%

Amtrak's trust asset investment strategy is to invest the assets in a manner whereby long-term earnings on the assets provide adequate funding for retiree pension payments. The investment objectives of the pension fund are to: (1) promote stability and, to the extent appropriate, growth in funded status, (2) minimize reliance on contributions to the plan as a source of benefit security by investing plan assets to

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maximize plan funded ratios over the long-term while managing the downside risk that funded ratios fall below some specified threshold level, and (3) achieve the greatest reward for the plan consistent with a prudent level of risk and achieve, as a minimum over time, the passively managed return earned by market index funds, weighted in the proportions outlined by the asset class exposures identified in the plan's strategic allocation targets.

Amtrak's mixture of plan assets is based on an optimization study that identifies asset allocation targets in order to achieve the maximum return for an acceptable level of risk while minimizing the expected contributions and pension expense. To perform such an optimization study, Amtrak hires an outside consultant to provide the analysis of historical market characteristics of the various asset classes over all of the different economic conditions that have existed, and to project the economic conditions expected to prevail over the study period. Finally, the historical characteristics to reflect the expected future conditions are adjusted to produce the market characteristics that will be assumed in the study.

The following table shows the asset allocation targets for the pension plan:

	Plan Assets	
	2004	2003
U.S. equity securities	50% - 60%	38% - 52%
International equity securities	8% - 12%	3% - 17%
U.S. fixed income securities	30% - 40%	34% - 46%
Other	0.0%	4% - 6%

Estimated Future Benefit Payments

Based upon the assumptions used to measure the pension and other postretirement benefit obligations at September 30, 2004, and including pension and other postretirement benefits attributable to estimated future employee service, Amtrak expects that pension benefits and other postretirement benefits to be paid over the next ten years are as follows (in thousands):

	Pension Benefits	Other Benefits
2005	\$ 6,714	\$ 13,449
2006	6,931	15,218
2007	7,285	17,583
2008	7,928	20,531
2009	8,866	24,338
2010-2014	\$ 62,150	\$ 194,280

Contributions

In 2005, Amtrak does not expect to make a contribution to its pension plan; however, it does expect to contribute \$13.4 million toward other postretirement benefits.

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Assumptions

Weighted-average assumptions used to determine benefit obligations at September 30, 2004 and 2003 are as follows:

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Discount rate	6.25%	6.00%	6.25%	6.00%
Rate of compensation increase	4.00%	4.00%	N/A	N/A

Weighted-average assumptions used to determine net periodic benefit cost for years ended September 30, 2004 and 2003 are as follows:

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Discount rate	6.00%	7.25%	6.00%	7.25%
Expected long-term return on plan assets	8.00%	8.00%	N/A	N/A
Rate of compensation increase	4.00%	4.00%	N/A	N/A

Assumed healthcare cost trend rates at September 30, 2004 and 2003 are as follows:

	Other Benefits	
	2004	2003
Healthcare cost trend rate assumed for next year	12.00%	12.00%
Rate to which the cost trend rate is assumed to decline (the ultimate trend rate)	5.00%	5.00%
Year that the rate reaches the ultimate trend rate	2012	2011

Assumed healthcare cost trend rates have a significant effect on the amounts reported for the healthcare plan. A one-percentage-point change in assumed healthcare cost trend rates would have the following effects (in thousands) on the Other Benefits plans:

	1%	1%
	Increase	Decrease
Effect on total of service and interest cost component	\$ 5,920	\$ (5,193)
Effect on postretirement benefit obligation	\$ 56,842	\$ (51,588)

Prescription Drug Benefits

On December 8, 2003, the Medicare Prescription Drug, Improvement, and Modernization Act of 2003 (the "Medicare Act") was signed into law. The Medicare Act introduced a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. As allowed by FASB Staff Position No. FAS 106-1, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003", Amtrak has elected to record an estimate of the effects of the Medicare Act in accounting for its postretirement benefit plans under SFAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions", and in providing

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disclosures required by SFAS No. 132 (revised 2003), “Employers’ Disclosures about Pensions and Other Postretirement Benefits”.

Based on actuarial analysis of prescription drug benefits, estimated future Medicare subsidies are expected to reduce the September 30, 2004, accumulated postretirement benefit obligation by \$39.5 million. For the year ended September 30, 2004, the impact of the Medicare Act on net postretirement cost was a \$2.5 million reduction. When specific guidance on accounting for the federal subsidy is issued, these estimates could change.

401(k) Savings Plan

Amtrak provides a 401(k) savings plan for nonunion employees. Under the plan, Amtrak matches a portion of employee contributions up to five percent of the participant’s salary, subject to applicable limitations. Amtrak’s expenses under this plan were \$6,580,000 and \$6,192,000 for the years ended September 30, 2004 and 2003, respectively.

NOTE 13: FAIR VALUE OF FINANCIAL INSTRUMENTS

For cash and cash equivalents, receivables, accounts payable, and accrued expenses and other current liabilities, the carrying amounts approximate fair value because of the short maturities of these instruments. The carrying amounts of a portion of bonds and equipment obligations also approximate fair value. All charge interest at rates that are periodically adjusted to market.

The estimated fair values of the mortgage obligations, FRA loan, remaining bonds, and notes payable were based upon discounted cash flow analyses using interest rates available to Amtrak at September 30, 2004 and 2003 for debt with the same remaining maturities. The UDAG loan, although interest free, was also valued based upon a discounted cash flow analysis using September 30, 2004 and 2003 market interest rates. The estimated fair values of these financial instruments are as follows (in thousands):

	2004		2003	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
FRA loan	\$ 100,000	\$ 99,315	\$ 100,000	\$ 103,106
Mortgage obligations	274,180	316,678	283,698	324,797
Equipment obligations	1,723	1,723	502	502
Note payable	-	-	20,000	20,000
Bonds	79,445	85,192	79,426	84,969
UDAG loan	11,447	10,327	11,577	10,629
	<u>\$ 466,795</u>	<u>\$ 513,235</u>	<u>\$ 495,203</u>	<u>\$ 544,003</u>

NOTE 14: SUBSEQUENT EVENTS

On April 14, 2005, during an FRA inspection of an Acela Express train, cracks were discovered in spokes of the disc brake rotors that resulted in the voluntary removal from service of all 20 trainsets. Amtrak is adjusting train schedules and to the extent possible, using other equipment to accommodate passengers due to this disruption in service. Amtrak is not able to determine the impact on fiscal year 2005 financial results at this time. The long-term impact will depend in part on the successful implementation of a reliable permanent solution.

On April 21, 2005, Amtrak announced a comprehensive strategic reform initiative to revitalize U.S. passenger rail service. The initiative seeks to transform the funding and development of passenger rail

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service, and introduce competition, efficiency and cost-savings. The four fundamental objectives of the strategic reform initiative include the: (1) development of passenger rail corridors utilizing federal and state capital matching, (2) return of the Northeast Corridor infrastructure to a state of good repair and operational reliability, (3) continuation and possible addition/elimination of certain national long-distance routes based on the establishment of phased-in financial performance thresholds, and (4) creation of markets for competition and private commercial participation in all passenger rail functions and services. To achieve the objectives embodied in Amtrak's strategic reform initiative, it is essential that Congress provide adequate funding as well as the necessary legislative reform. Congress is currently considering the reform initiative in conjunction with their hearings concerning Amtrak's fiscal year 2006 appropriation.



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