

Freight Rail Infrastructure Tax Credit

ASSOCIATION OF AMERICAN RAILROADS

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WHAT SHOULD BE DONE?

Enact S. 1125/H.R. 2116 (the “Freight Rail Infrastructure Capacity Expansion Act of 2007”), which provides a federal tax credit for investments that expand freight rail capacity.

WHY?

Demand for freight transportation that is cost effective and environmentally friendly will grow sharply in the years ahead. To meet this demand, rail capacity must grow too. Freight railroads are reinvesting record amounts of their own funds into their systems, but that will not be enough to take full advantage of railroads’ potential to meet our transportation and environmental needs. A tax credit for projects that expand freight rail capacity would help bridge the funding gap and produce public benefits (like reduced highway gridlock and lower greenhouse gas emissions) that would far exceed the cost of the credit.

Overview of the Freight Rail Infrastructure Tax Incentive Proposal

Our economy cannot prosper if we do not have enough transportation capacity. Already, transportation gridlock costs our economy hundreds of billions of dollars each year in wasted time, fuel, cargo delays, and environmental degradation. Given the huge projected increases in freight transportation demand in the years ahead, this enormous tab will grow if we do not adequately address our freight transportation capacity challenges.

One way to help do this is to enact bipartisan legislation now before Congress — S. 1125/H.R. 2116, the “Freight Rail Infrastructure Capacity Expansion Act of 2007” — that calls for a 25 percent investment tax credit (ITC) for spending on new track, intermodal facilities, and other projects that expand freight rail capacity. All businesses (not just railroads) that make capacity-enhancing investments in rail infrastructure would be eligible for the credit. Under this proposal, other freight rail capital expenditures would be expensed.

A rail infrastructure investment tax credit addresses the central challenge of how to move more freight without causing more highway gridlock or environmental degradation.

Freight Railroads Are Spending Record Amounts on Capacity, But More Needs to be Done

Unlike trucks, barges, and airlines, U.S. freight railroads operate almost exclusively over infrastructure that they build, maintain, and pay for themselves. From 1980 to 2007, U.S. freight railroads invested approximately \$420 billion (more than 40 cents out of every rail revenue dollar) to maintain and improve their infrastructure and equipment.

But more needs to be done. Railroads are making record reinvestments in their systems and will spend huge amounts in the years ahead, but there is a gap between the socially-optimal level of rail capacity and what railroads are likely to be able to afford on their own.

In fact, a recent study by Cambridge Systematics found that Class I railroads need \$135 billion in investments to expand their network by 2035 to keep pace with economic growth, meet forecast growth in freight demand, and maintain rail's current market share. Non-Class I railroads need another \$13 billion in capacity expansion. (These amounts are in addition to the hundreds of billions of dollars needed to maintain and replace existing rail infrastructure, and to maintain and replace locomotives, freight cars, and other rail equipment over the same period.)

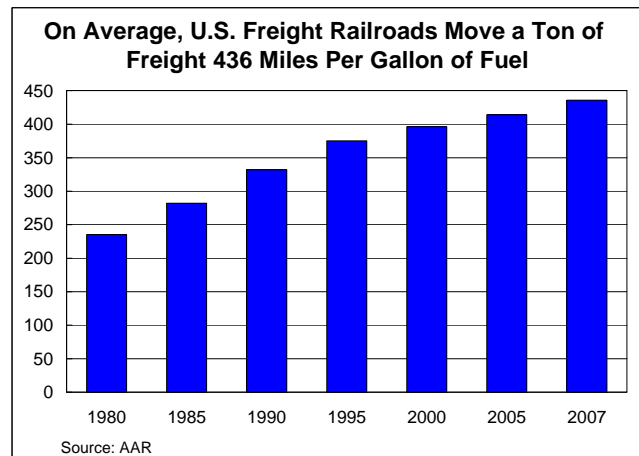
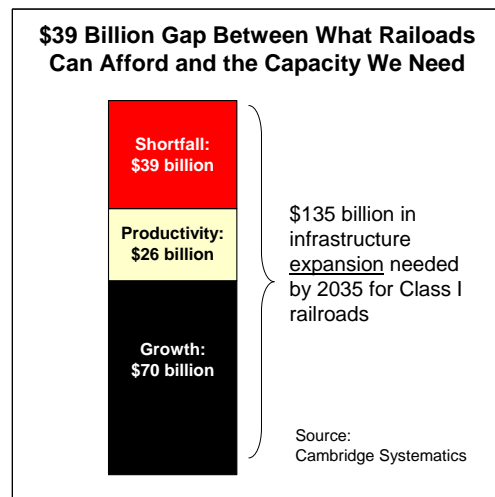
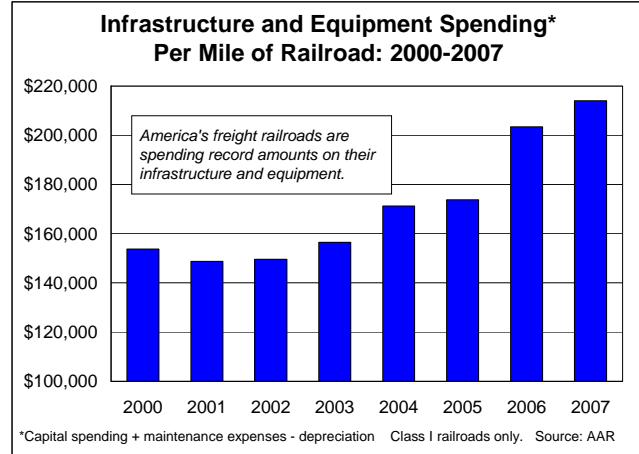
Class I railroads anticipate being able to generate approximately \$96 billion of that \$135 billion through higher earnings and productivity gains. That leaves a \$39 billion funding shortfall, or around \$1.4 billion per year, that could be accounted for by an investment tax credit or other means.

For a railroad considering whether to fund an expansion project, a tax incentive would reduce the cost of the project, raising the likelihood that the project will be economically viable. The incentive would help worthwhile projects get built sooner, but would not be enough to cause economically-unjustified projects to go forward.

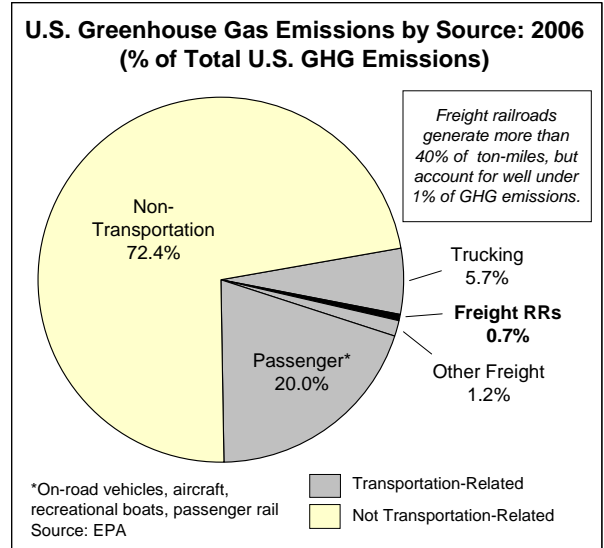
Freight Rail Expansion Would Mean Enormous Public Benefits

Public participation in freight rail infrastructure expansion projects is justified by the huge and far-reaching public benefits that rail expansion would bring:

- **Fuel Efficiency** – Railroads, which are three or more times more fuel efficient than trucks, move a ton of freight an average of 436 miles per gallon of fuel. If just 10 percent of the long-haul freight that moves by truck moved by rail instead, fuel savings would exceed one billion gallons per year.



- Greenhouse Gas Emissions – By encouraging greater use of freight rail, an ITC offers a simple way to meaningfully reduce greenhouse gas emissions without harming the economy. Because of railroads’ fuel efficiency, every ton-mile of freight that moves by rail instead of trucks reduces greenhouse gas emissions by two-thirds or more.



- Highway Congestion – Highway gridlock already costs the U.S. economy more than \$78 billion per year just in wasted fuel and time. But because a typical train takes the freight of several hundred trucks off our highways, freight railroads reduce highway gridlock, the costs of maintaining existing highways, and the pressure to build costly new highways.
- Pollution – The EPA estimates that for every ton-mile of freight carried, a train typically emits substantially less nitrogen oxides and particulates than a truck.
- Safety – Fatality rates associated with intercity trucking are four times those associated with freight rail transportation. Railroads also have lower employee injury rates.

A Rail Infrastructure Investment Tax Credit Would Help Stimulate the Economy

The budgetary cost of a rail infrastructure ITC would be about \$300 million per year, but the stimulatory benefit to the economy would be much greater. U.S. Department of Commerce data indicate that every dollar of freight rail infrastructure investment that would be stimulated by a rail infrastructure ITC would generate more than three dollars in total economic output because of the investment, purchases, and employment occurring among upstream suppliers.

Thus, \$300 million in tax credits for additional freight rail capital investment would result in nearly \$1 billion in overall economic stimulus, most of which would begin to occur very quickly as upstream suppliers expanded capacity to meet the increased demand for rail projects. Each \$1 billion of new rail investment induced by the ITC would create an estimated 20,000 jobs nationwide. The benefits to our economy would be broad based and long lasting.

A Rail Infrastructure Investment Tax Credit Would Partially Level the Playing Field

As noted above, U.S. freight railroad operate over infrastructure that they build, maintain, and pay for overwhelmingly themselves — in contrast to other modes. According to the Congressional Budget Office, “large trucks pay only about 50 to 80 percent of the costs attributed to them” for federal highway use, and “barge operators pay taxes that cover only about 20 percent of the amount the Corps of Engineers spends on navigation projects.” Likewise, the National Surface Transportation Policy and Revenue Commission noted in its January 2008 report that “heavy trucks pay less than their share of highway costs.” Moreover, because roads and waterways are publicly provided, trucks and barges do not bear any risk if a new highway or waterway project turns out to be uneconomical.

This is not the case for railroads. A tax incentive for rail capacity enhancement projects would thus help level the playing field vis-à-vis other transportation modes.

Support for a Rail Infrastructure Investment Tax Credit is Widespread

Numerous key businesses, business groups, ports, governments, and others support a rail infrastructure ITC. Supporters include the National Surface Transportation Policy and Revenue Commission, the U.S. Chamber of Commerce, the Waterfront Coalition, the National Retail Federation, the Association of Metropolitan Planning Organizations, the American Association of Port Authorities, and many others.

In its Freight-Rail Bottom Line Report, the American Association of State Transportation and Highway Officials (AASHTO) confirmed the benefits of public investments in rail infrastructure. By analyzing several scenarios that differ according to the level of rail infrastructure investments made over 20 years, AASHTO demonstrated that “Relatively small public investments in the nation’s freight railroads can be leveraged into relatively large benefits for the nation’s highway infrastructure, highway users, and freight shippers.”

A Separate Tax Credit for Short Line Railroads Should Be Enacted

In 2004, Congress enacted a tax credit to help short line railroads upgrade their tracks to handle the 286,000-pound rail cars that are becoming the industry standard. This tax credit has been instrumental in helping short lines upgrade their tracks, and in encouraging rail customers to make new investments in their own facilities to take advantage of the short lines’ ability to move longer and heavier trains. Unfortunately, this tax credit expired at the end of 2007. S. 881 and H.R. 1584 (“The Short Line Railroad Investment Act of 2007”) now before Congress would extend this tax credit.

If short lines cannot handle heavier rail cars, thousands of communities in small town America will be cut off from the national mainline rail system. Congress should extend this credit and further encourage critical investment in America’s freight rail network.