

2014



(Photo by Frank Keller)

ALASKA RAILROAD CORPORATION

REPORT TO THE STATE

Celebrating 90 Years



BOARD

Chair Linda Leary



VChair Bill Sheffield



Susan Bell



John Binkley



Jack Burton



Jon Cook



Pat Kemp



STRATEGIC

In 2013, the Alaska Railroad marked a milestone anniversary with a year focused largely on safety, fiscal challenges, and mega projects. Similar topics likely prevailed 90 years ago, when the federal government completed nearly 500 miles of track in Alaska. Crews working in harsh conditions and terrain probably worried about safety from a practical standpoint. Government officials likely breathed a sigh of relief at the culmination of a decade-long mega project involving multiple engineering feats, while perhaps fretting over the expense of operating a railroad in a far-off and fledgling territory.

Today, the Alaska Railroad faces a serious financial challenge. Two key freight business lines — refined petroleum and export coal — declined unexpectedly, leaving a substantial operations revenue gap. On the capital side, the railroad realized a nearly 20% drop in federal grant money that had, for the past decade, been a reliable source for critical infrastructure investments. These downturns forced the railroad to accelerate cost-cutting efforts begun the year prior. This year, we eliminated about 50 positions and pursued a comprehensive re-organization of departments, personnel and leadership. Working in focused teams, railroaders at every level rallied with new initiatives to contain costs, lower expenses, boost efficiency and generate new business opportunities.

These efforts produced some remarkable developments. For example, in an impressive example of greater efficiency, crews assembled the longest ARRC freight train on record in late April. Measuring nearly two miles in length, the mixed cargo train was a testament to the ingenuity and commitment of railroaders determined to lower costs without sacrificing service or safety.

We have also successfully sought partners to bring new business to the table. Regularly scheduled and chartered passenger service saw solid growth while enticing more people to experience rail travel. Our rail marine barge service between Seattle and Whittier hauled more container/trailer freight than expected, and we saw an uptick in the movement of oilfield supplies. Recent real estate developments offer exceptional potential. In particular, a vision of Seward as a growth hotspot took shape with the advent of a revamped Master Plan that provides a concrete blueprint useful to developers and businesses. Moreover, we took tangible steps toward facilitating Seward waterfront re-development.

Thanks to multi-faceted efforts, the railroad forecasts a net income that is double the budgeted \$5 million. While still well shy of the net income needed to underwrite an adequate capital program, the better-than-budget cash flow prevents further personnel layoffs this year and avoids deferral of some critical maintenance.

Cost containment is also a function of safety. Accidents and incidents are invariably expensive, which is why the railroad continued to emphasize a safe environment for employees, customers and rail belt communities. The corporation's annual performance audit focused on our safety management system (SMS). Accomplished July through September, the audit looked at ARRC's safety program oversight, policies, tools and practices. Conducted by a third party expert, the analysis provided railroad leadership with unprecedented insight into all aspects that impact safety – from interdepartmental communications, to revealing metrics, to company culture, employee engagement, work environment, and effective action planning. Thanks to this in-depth evaluation, we are in the process of developing a more comprehensive and effective SMS.

OUTLOOK

The railroad's commitment to safety extends beyond internal stakeholders to our neighbors and communities. In summer 2013, we initiated a Rail Safety Public Awareness Campaign supported largely by ARRC in-kind contributions and a grant from Operation Lifesaver Inc. (OLI), a national/international organization that promotes rail safety. The campaign spread "Always Expect a Train" and "Stay Off! Stay Away! Stay Alive" messages through newspaper ads, trail signs, locomotive decals, public bus advertising signs, presentations and giveaways at public gatherings, bike commuting event flyers, and public service announcements (PSA) broadcast on radio, voiced at baseball games and shown on monitors in the lobby of Division of Motor Vehicle office statewide.

Safety is also at the core of a major capital investment project, Positive Train Control, or PTC. The Alaska Railroad continues to work on complying with the federal mandate to install technology that will override human error by using Global Positioning Satellites (GPS) and sensors in trains and tracks to slow or stop a train if a signal or switch is missed. Recent progress is thanks to state capital funding appropriated in 2013 (and requested in future years) to assist with the \$150 million overall cost of an expensive and still-developing technology. The deadline to implement PTC is December 31, 2015, however, like many railroads nationwide, ARRC is more likely to meet the deadline only if it is extended to 2018. The penalty for failing to comply ranges from daily fines to curtailing or ending passenger service.

Mega projects such as PTC are the hallmark of ARRC's current capital program, which includes two rail extensions. Ground broke and construction got underway on much of the 32-mile spur connecting Port MacKenzie to the main line near Houston. The Northern Rail Extension's Phase One (NRE-1) moved into the home stretch with construction of the bridge over the Tanana River near Salcha. NRE-1 remains on target for 2014 completion.

Aside from the three mega economic development projects that have all benefitted from state capital appropriations, federal grant funding for the railroad's regular capital program is about half of what it has been in recent years. Not only were fewer Federal Transit Administration (FTA) grant dollars available, but we had less railroad income to provide the local match to FTA and other federal grants or to underwrite capital investments that don't qualify for federal funding.

We expect more of the same in the foreseeable future. In 2012, a new federal surface transportation funding bill (MAP 21) was passed which reduced the Alaska Railroad's allocation of FTA formula funds by about 20%, while at the same time doubling the required match amount. With MAP-21 expiring in 2014, the fight to keep our FTA formula funds will likely be a very difficult challenge, putting about \$28 million at risk of additional reduction or even elimination.

The 5-year capital outlook in this Report to the State reflects the reality of shrinking capital resources, the conclusion of the three mega projects, and a continued focus on promoting safety. These concerns are as dominant today as they were 90 years ago, illustrating their enduring importance to the capital-intensive business of railroading.

Bill O'Leary
President & CEO

MANAGEMENT

Bill O'Leary



President & CEO
Bill O'Leary

Chief Operating Officer
Doug Engebretson

VP Engineering
Clark Hopp

*General Counsel
& VP Legal*
Bill Hupprich

*VP Corporate Planning
& Real Estate*
Jim Kubitz

*VP Business Management
& Corporate Affairs*
Wendy Lindskoog

*VP Advanced Train Control
Systems & Technology*
VP Eileen Reilly

*VP Marketing &
Customer Service*
Dale Wade

Chief Financial Officer
Barbara Amy

2014

OPERATING PLAN

Celebrating 90 Years

The Alaska Railroad was built by the federal government from 1914 to 1923. This year marks the 90th anniversary of the railroad's completion (*pictured on the cover is President Harding driving the golden spike in Nenana July 15, 1923*). The railroad was operated by the federal government until January 1985, when the State of Alaska purchased the asset for \$22.3 million. The Alaska State Legislature created the Alaska Railroad Corporation (ARRC) to own and operate the railroad and manage railroad property to serve Alaska businesses and communities as an engine for community development and economic prosperity.

Unlike other state business enterprises (such as the Alaska Housing Finance Corporation and the Alaska Industrial Development & Export Authority), ARRC's enabling statute specifically requires all revenues earned by the railroad be retained by the corporation. The federal transfer act also includes this provision. The intent was to ensure the railroad had the funding necessary to meet basic maintenance and capital needs, to improve safety and increase profitability, thereby avoiding dependence on the state's general fund. The corporation's annual earnings are invested entirely into its capital program.

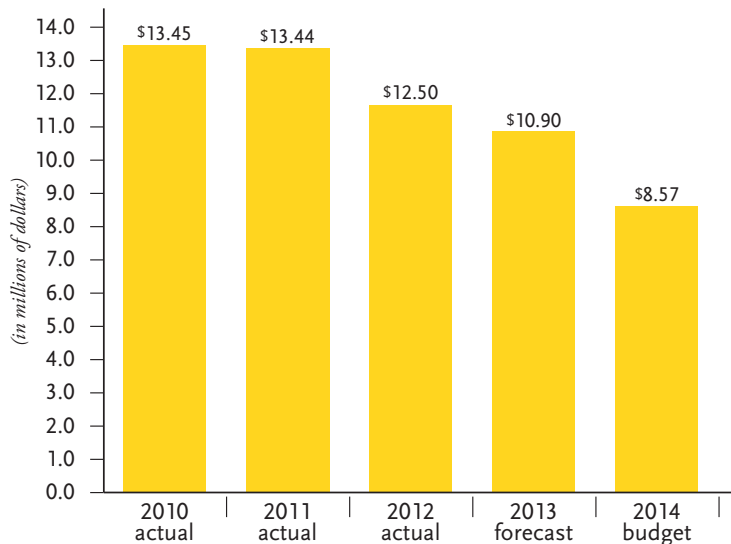
ARRC is governed by a 7-member board of directors appointed by the governor. The president/CEO reports to the board.



5-YEAR OPERATING PLAN

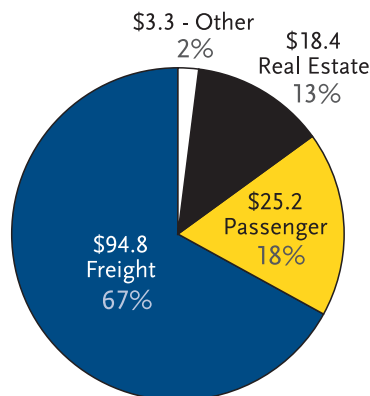
(in millions of dollars)	2014	2015	2016	2017	2018
Operating Revenue	\$ 123.27	\$ 126.26	\$ 129.78	\$ 135.40	\$ 140.75
Operating Expense	(124.37)	(127.60)	(129.58)	(133.65)	(137.38)
Net Operating Income	(1.10)	(1.33)	0.20	1.75	3.37
Net Real Estate Income	10.91	11.23	12.13	12.58	13.04
Net Other Inc. (Exp.)	(1.24)	(1.39)	(1.22)	(1.03)	(0.85)
Net Income	\$ 8.57	\$ 8.50	\$ 11.11	\$ 13.29	\$ 15.55

ALASKA RAILROAD NET INCOME



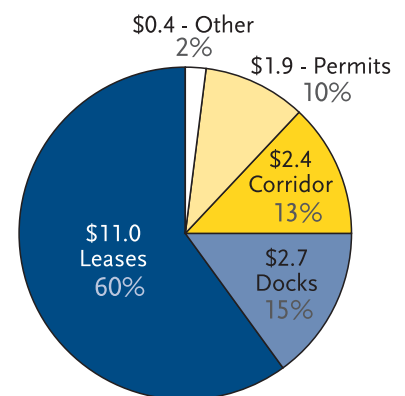
2014 BUDGET REVENUE SOURCES

(in millions of dollars)



2014 BUDGET REAL ESTATE REVENUE

(in millions of dollars)



2013 OPERATING STATISTICS

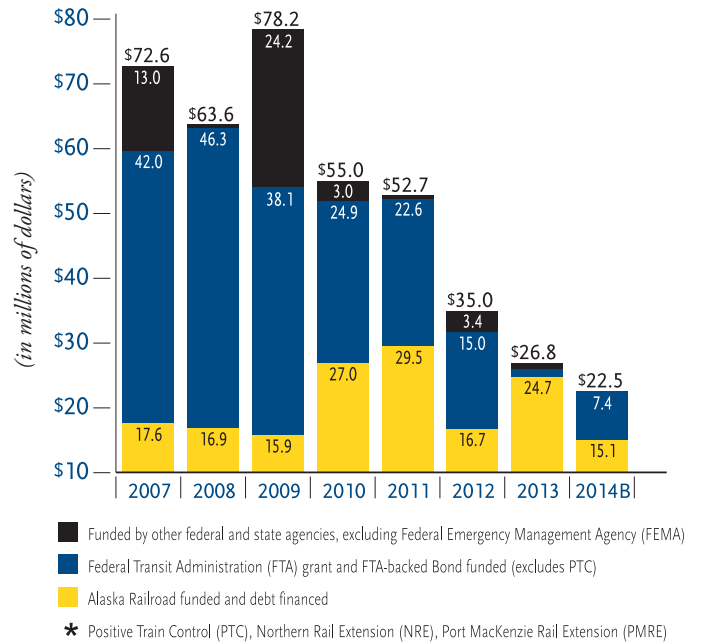
OPERATING ASSETS

- Miles of main line: 467
 - Miles of branch line: 54
 - Miles of yards and sidings: 135
 - Total miles of track: 656
 - Freight cars (owned and leased)*: 1,193
 - Passenger cars: 44
 - Locomotives: 51
- * Includes 275 tanker cars owned by Flint Hills Resources

2013 TRAIN SERVICE ACTIVITY

- 2013 Ridership**: 418,000 passengers
 - 2013 Freight tonnage**: 5.8 million tons
- ** January 1 - Dec. 31, 2013, Projected

ALASKA RAILROAD CORE CAPITAL PROGRAM NET OF MEGA PROJECTS (PTC, NRE, PMRE*)



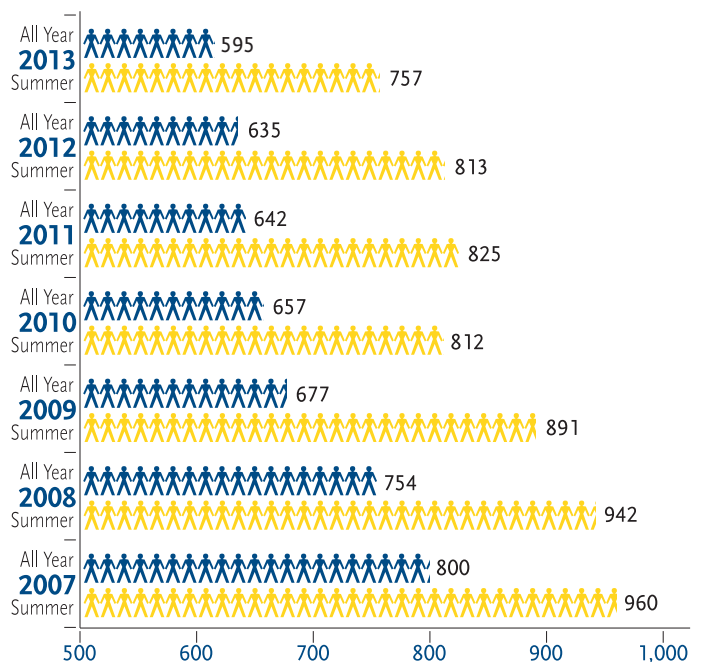
EMPLOYEES (November 2013)

- Year-round employees: 595
- Additional seasonal employees: 110
- Average years of service: 12.1
- Average age: 44.8
- Male (Year-round & Seasonal): 580 (82%)
- Female (Year-round & Seasonal): 125 (18%)
- Veterans: 127 (18%)
- Percentage of Alaska Hire: 90+%

Three-fourths (77%) are represented by five unions:

- United Transportation Union: 160
- Transportation Communication Union: 43
- Int'l Brotherhood of Teamsters Local 959: 58
- American Federation of Gov't Employees: 274
- American Train Dispatchers Department: 11

ALASKA RAILROAD WORK FORCE PRE-ECONOMIC DOWNTURN 2007 TO 2013



- ♀ All Year = lowest employee count during winter months, representing year-round employees only.
- ♂ Summer = highest employee count during summer months, representing year-round + seasonal employees.

5-YEAR CAPITAL PLAN: EXTERNAL FUNDING

FEDERAL TRANSIT ADMINISTRATION (FTA) FORMULA FUNDS

	2014	2015	2016	2017	2018	5-Yr Total
FTA Formula Fund Grant Estimate	\$ 28,700,000	\$ 28,987,000	\$ 29,276,870	\$ 29,569,639	\$ 29,865,335	\$ 146,398,844
Alaska Railroad 20% Match	7,175,00	7,246,750	7,319,218	7,392,410	7,466,334	36,599,711
Total FTA Formula Grants	\$ 35,875,000	\$ 36,233,750	\$ 36,596,088	\$ 36,962,048	\$ 37,331,669	\$ 182,998,555
Less Programmed Items (PI):						
Preventive Maintenance	11,609,448	11,725,541	11,842,797	11,961,225	12,080,837	59,219,848
2007 Bond Principal & Interest	9,140,152	9,139,077	9,136,908	8,835,425	8,824,846	45,076,408
2006 Bond Principal & Interest	7,503,586	7,486,648	7,480,060	7,237,573	7,232,002	36,939,869
Transit Security	127,300	128,573	129,859	131,157	132,469	649,358
Transit Enhancement	127,300	128,573	129,859	131,157	132,469	649,358
Total Programmed Items (PI)	28,507,786	28,608,412	28,719,483	28,296,538	28,402,623	142,534,841
FTA Funds Available for Projects	\$ 7,367,215	\$ 7,625,338	\$ 7,876,605	\$ 8,665,511	\$ 8,929,046	\$ 40,463,714
Projects Funded by FTA Funds:						
Track Rehabilitation Program	6,790,215	7,625,338	7,876,605	8,665,511	8,929,046	39,886,714
Passenger Rolling Stock Rehab	577,000	—	—	—	—	577,000
Total FTA Grant Projects (net PI*)	\$ 7,367,215	\$ 7,625,338	\$ 7,876,605	\$ 8,665,511	\$ 8,929,046	\$ 40,463,714

STATE OF ALASKA APPROPRIATIONS

Positive Train Control	\$ 3,495,000	\$ 19,615,104	\$ 17,717,322	\$ 16,223,240	\$ 12,658,840	\$ 69,709,506
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* Federal grant money minus funds allocated to Programmed Items (see above). This net amount equates to federal funds available for capital projects.



Above: The first span of 165-foot girders are placed on two piers as part of the Northern Rail Extension (NRE) Phase 1, the Tanana River bridge near Salcha. Cover top photo: Construction on the NRE Phase 1 bridge stretches across the Tanana River in early November 2013.

5-YEAR CAPITAL PLAN: INTERNAL FUNDING

Non-discretionary Projects	2014	2015	2016	2017	2018	5-Yr Total
Bridge Program	\$ 3,450,000	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000	\$ 4,000,000	\$ 19,450,000
Track Rehabilitation Program	129,786	6,144,757	10,936,686	9,384,412	8,543,917	35,139,558
Equipment Program	3,135,000	3,196,000	2,685,000	2,628,500	2,525,500	14,170,000
Vehicle Program	1,365,000	1,095,000	1,060,000	1,275,000	1,225,000	6,020,000
Fairbanks Roundhouse Fire Alarm	75,000	—	—	—	—	75,000
Healy Roundhouse Demolition	250,000	—	—	—	—	250,000
Hurricane Siding Signal Foundation	10,000	—	—	—	—	10,000
Portage Section Facility	—	1,000,000	—	—	—	1,000,000
Total Nondiscretionary Projects	\$ 8,414,786	\$ 15,435,757	\$ 18,681,686	\$ 17,287,912	\$ 16,294,417	\$ 76,114,558
Continuing Programs						
Yard & Branch Improvements	\$ 650,000	\$ 1,000,000	\$ 1,000,000	\$ 1,000,000	\$ 350,000	\$ 4,000,000
Avalanche / Slide Zone Risk Mitigation	175,000	300,000	625,000	615,000	85,000	1,800,000
Rip Rap / Drainage Maintenance	500,000	500,000	500,000	500,000	500,000	2,500,000
Docks and Slips Maintenance	800,000	1,557,500	1,907,500	1,307,500	2,082,500	7,655,000
Defect Detector Upgrades	318,000	406,600	406,600	445,000	356,000	1,932,200
Capital Locomotive Overhaul/PM	814,000	1,896,000	1,659,000	1,427,000	2,406,000	8,202,000
Capital Locomotive Truck Overhaul	180,000	180,000	180,000	180,000	180,000	900,000
191 Heavy Maintenance	240,000	155,000	155,000	124,000	—	674,000
Facility Roofing Upgrades	150,000	334,000	375,000	260,000	—	1,119,000
Facility Electrical Upgrades	165,000	100,000	100,000	100,000	100,000	565,000
Section Improvements	20,000	50,000	50,000	50,000	50,000	220,000
Power Distribution and Monitoring	80,000	80,000	80,000	80,000	—	320,000
Trepass Mitigation	35,000	35,000	35,000	35,000	35,000	175,000
Seward Coal Loading Facility Upgrades	450,000	375,000	375,000	375,000	375,000	1,950,000
Building Maintenance	20,000	50,000	50,000	50,000	50,000	220,000
General Facility Repair	55,000	55,000	55,000	55,000	55,000	275,000
B-26 Air System Replacement	30,000	280,000	—	—	—	310,000
Energy Management	25,000	75,000	75,000	75,000	75,000	325,000
Tenant Improvements	50,000	50,000	50,000	50,000	50,000	250,000
MAC Motor Driven Air Compressor	150,000	154,000	—	—	—	304,000
Premises Equipment Refresh	85,000	80,000	80,000	80,000	80,000	405,000
Network Services Upgrades	500,000	500,000	500,000	500,000	500,000	2,500,000
Land & Utilities Improvements	75,000	75,000	75,000	75,000	75,000	375,000
Copier Fleet Replacement	42,000	26,500	40,000	40,000	—	148,500
Records Management Vital Records	—	469,000	21,600	—	—	490,600
Purchase of End-of-Train Devices	—	—	36,000	36,000	36,000	108,000
Total Continuing Programs	\$ 5,609,000	\$ 9,284,100	\$ 8,930,700	\$ 7,959,500	\$ 7,940,500	\$ 39,723,800
Strategic Business Initiatives						
APU Spur Rehabilitation	\$ 150,000	\$ 150,000	\$ 150,000	\$ 150,000	\$ 150,000	\$ 750,000
Fairbanks Ramp Expansion	50,000	700,000	—	—	—	750,000
ASCTD Access Plates	21,000	22,200	—	—	—	43,200
188xx series Flat Cars Modification	16,000	—	—	—	—	16,000
Healy Generator / UPS	90,000	—	—	—	—	90,000
Radio Controller Console Refresh	55,400	—	—	—	—	55,400
Passenger Online Booking Features	40,000	—	—	—	—	40,000
Post Road Sewer Construction	415,000	425,000	425,000	425,000	425,000	2,115,000
Passenger Website Redesign for Mobile	65,000	—	—	—	—	65,000
SQL High Availability & Standardizing	121,000	—	—	—	—	121,000
Applications Replacement, Cold Fusion	60,200	—	—	—	—	60,200
Applications, Crew Mgmt/Timekeeping	—	500,000	—	—	—	500,000
Other Legacy Systems Replacement	—	150,000	184,500	—	—	334,500
Total Strategic Business Initiatives	\$ 1,116,600	\$ 1,947,200	\$ 759,500	\$ 575,000	\$ 575,000	\$ 4,973,300
Total Internal Capital Requests	\$ 15,140,386	\$ 26,667,057	\$ 28,371,886	\$ 25,822,412	\$ 24,809,917	\$ 120,811,658
Est. Funds from Internal Cash Flow	15,140,386	17,440,000	20,900,000	24,170,000	28,590,000	106,240,386
Internal Funding Shortfall	\$ —	\$ 9,227,057	\$ 7,471,886	\$ 1,652,412		\$ 18,351,356
FTA Formula Funds (net PI*)	\$ 7,367,215	\$ 7,625,338	\$ 7,876,605	\$ 8,665,511	\$ 8,929,046	\$ 40,463,714
State of Alaska Appropriations	\$ 3,495,000	\$ 19,615,104	\$ 17,717,322	\$ 16,223,240	\$ 12,658,840	\$ 69,709,506
Internal Funds Available	\$ 15,140,386	\$ 17,440,000	\$ 20,900,000	\$ 24,170,000	\$ 28,590,000	\$ 106,240,386
Total Capital Program	\$ 26,002,600	\$ 44,680,442	\$ 46,493,927	\$ 49,058,751	\$ 50,177,886	\$ 216,413,605

* Federal grant money minus funds allocated to Programmed Items (see previous page). This net amount equates to federal funds available for capital projects.

ARRC CAPITAL PROGRAM INFO

More Information about the Alaska Railroad's capital improvement program — including capital project fact sheets — is available on the Alaska Railroad's web site.



ALASKARAILROAD.COM

Contact and Connections

Alaska Railroad Corporation

P.O. Box 107500 • Anchorage, AK 99510-7500

327 W. Ship Creek Avenue • Anchorage, AK 99501

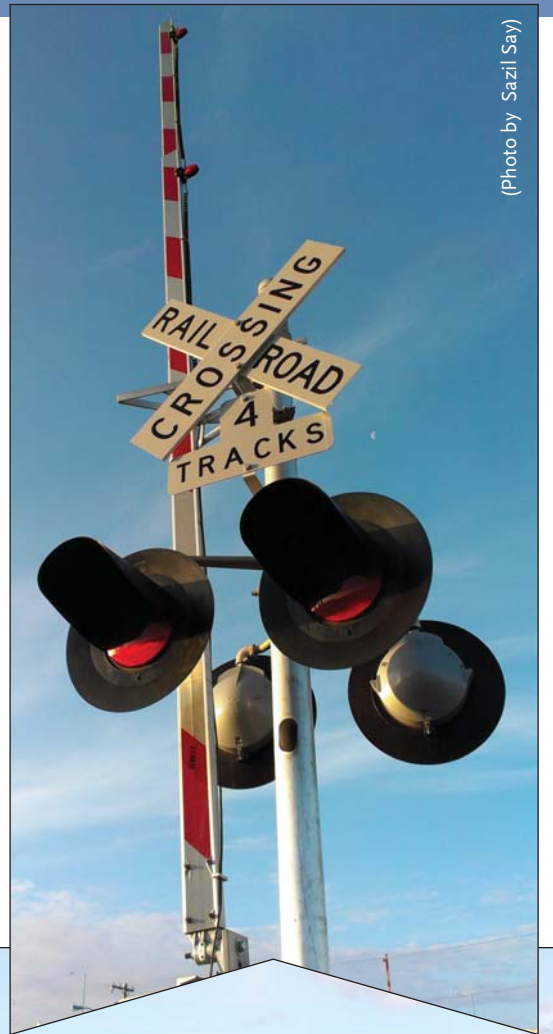
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(Photo by Sazil Say)

(Photo by Stephenie Wheeler)



The governor, several legislators, Mat-Su Borough and Alaska Railroad officials were on-hand to celebrate a ground-breaking ceremony for the Port MacKenzie Rail Extension project in June 2013.