

DESTINATION: EXCELLENCE

2015 REPORT TO THE STATE

published December 1, 2014

CUSTOMER SERVICE



SAFETY



PROFITABILITY



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ALASKA

RAILROAD

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ABOUT THIS REPORT

STATE OF ALASKA LEADERSHIP:

Each year by December 1, the Alaska Railroad (ARRC) provides a “look ahead” report to the Governor, Alaska State Legislators, and key officials in the State government. As is traditional, the report offers an overview of the railroad’s strategic plans for the next five years.

Our strategic planning includes capital investments. The final pages of this report detail the Alaska Railroad’s 5-Year Capital Plan, which lists projects that are important to railroad safety and efficiency, and that promote growth and enhance service. The capital plan outlines anticipated funding sources and expected funding levels. This portion of the Report to the State fulfills the ARRC’s statutory requirement to inform state leadership about railroad capital improvements over the next five years.

A handwritten signature in white ink, appearing to read "Bill O'Leary".

Bill O’Leary
President and CEO

ALASKA RAILROAD LEADERSHIP



MANAGEMENT



Bill O'Leary
President & CEO



Doug Engebretson
Chief Operating Officer

Clark Hopp
VP Engineering

Bill Hupprich
General Counsel & VP Legal

Jim Kubitz
VP Corporate Planning & Real Estate

Wendy Lindskoog
VP Business Management & Corporate Affairs

Eileen Reilly
VP Advanced Train Control Systems &
Technology

Dale Wade
VP Marketing & Customer Service

Barbara Amy
Chief Financial Officer

BOARD OF DIRECTORS



Linda Leary, *Chair*



Bill Sheffield, *Vice Chair*



Susan Bell



John Binkley



Jack Burton



Jon Cook



Pat Kemp

OUR MISSION

Through excellent customer service and sound business management practices, provide safe, efficient, and economical transportation and real estate services that support and **grow economic development opportunities for the State of Alaska.**

CUSTOMER SERVICE



SAFETY



PROFITABILITY



OUR VALUES

This set of values represents the culture we are creating and the conduct we expect to share with our co-workers, customers and the public.

SAFETY

Safety is a fundamental value. We seek an accident-free, incident-free work environment in all areas of our operation. Without exception, keeping each other safe is the responsibility of each employee at every level. Employees are expected and empowered to act immediately to eliminate unsafe conditions and to prevent the risk of injury in the workplace.

SERVICE EXCELLENCE

We go the extra mile for our customers. We create long-term relationships by delivering value; helping customers reach their goals by understanding their business needs; being consistent, proactive and establishing realistic expectations for our company and those we serve.

INTEGRITY

We are honest, ethical, and transparent in all our actions. We inspire trust by saying what we mean and following through with actions that match our words. We are accountable to each other and our stakeholders acting in a manner that maintains public confidence.

TEAMWORK

We strive to be one team – engaged and aligned in mission. We participate, collaborate and use our collective skills to achieve common objectives. We share knowledge and information and focus on the success of the Alaska Railroad, our customers, our state and the communities we serve. We have fun together.

SUSTAINABILITY

We are focused on growing our business to support the Alaska Railroad's long-term financial viability and our purpose to foster economic development. We value stewardship for our environment, each other, the communities we serve and our responsibility as a state-owned enterprise.



SAFETY POLICY

The Alaska Railroad Corporation (ARRC) upholds safety as a fundamental value. Our company's most valuable assets are its people. Without exception, keeping each other safe is the responsibility of each employee at every level.

The Alaska Railroad seeks an accident-free, incident-free work environment in all areas of its operations. **We work diligently to continually improve on-the-job safety through:**

COMMUNICATIONS

TRAINING

AWARENESS

AUDITING

Safety relies on participation. Individuals and work groups must be willing to sacrifice productivity in favor of working safely. Employees are expected to act immediately to eliminate unsafe conditions and to prevent the risk of injury in the workplace.

To succeed, all employees must:

- Comply with all relevant federal, state and local rules and regulations.
- Observe all company rules and regulations related to safe work performance.
- Integrate safety into each job function.
- Report or correct unsafe equipment and practices.
- Report any and all accidents that occur while on the job, as soon as is practical.
- Foster mutual respect and cooperation between co-workers.



STRATEGY SUMMARY

STRATEGY 1

Expand the Business by Growing and Diversifying Revenue

STRATEGY 2

Improve Profitability by Optimizing Cost Structure

STRATEGY 3

Optimize Capital Investment Levels and Projects

STRATEGY 4

Build a Proactive Culture of Safety and Engagement

STRATEGY 5

Enhance Economic Development, Stewardship and Stakeholder Relations



STRATEGY 1



EXPAND THE BUSINESS BY GROWING AND DIVERSIFYING REVENUE

Develop and annually update detailed marketing/sales plans for freight, passenger, and real estate business lines

Provide exemplary service to all customers, measured through surveys, repeat business, and customer interaction

Freight:

- Increase revenue from existing customers by at least 5% annually
- Add at least six new freight rail customers annually
- Grow with focus on higher-margin freight commodities

Passenger:

- Increase revenue by at least 7% annually
- Grow existing and new business through aggressive marketing, introduction of new services, expansion of existing services, enhanced customer relationships, and improved use of technology

Real Estate:

- Increase revenue from all sources (leases, permits, docks, etc.) by at least 5% annually
- Increase value and desirability of developed/underdeveloped ARRC property through infrastructure upgrades, land trades, and/or acquisitions
- Leverage land holdings/development with goal of increasing rail traffic

STRATEGY 2



IMPROVE PROFITABILITY BY OPTIMIZING COST STRUCTURE



Continue to drive train operating efficiency with a focus on:

- **Longer trains** – maintain average freight train length of 4,600 ft. or better
- **Heavier trains** – maintain average GTM¹/train mile of 3,900 or better (an average of loaded and empty)
- **Locomotive Fuel Economy** – maintain average 635 GTM/gallon or better
- **Managed headcount** – maintain average revenue²/employee of \$215,000 or better

Reduce facility energy consumption by 2% annually

- Identify largest areas of utility consumption and design plans to reduce with necessary capital investment identified and quantified

Reduce vehicle and equipment maintenance and fuel expense

- Annually reduce the ratio of maintenance expense to fleet replacement cost
- Improve average fuel economy of vehicle fleet via:
 - *purchase of more fuel efficient vehicles without compromising performance*
 - *more fuel efficient driving habits*
- Report on vehicle and equipment property damage incidents and have a goal to reduce the number per year

Reduce ratio of total benefits to total compensation to 30% and reduce total benefits to total operating expense ratio to 10%

Generate and sustain company-wide cash flow, measured as earnings before interest and depreciation (EBITDA) of \$37 million by 2019. Annual targets below:

- 2015: \$32 million • 2016: \$33 million • 2017: \$34 million
2018: \$35 million • 2019: \$37 million

¹ Gross Ton Mile, ² Excluding grant revenue

STRATEGY 3



OPTIMIZE CAPITAL INVESTMENT LEVELS AND PROJECTS

- **Develop master plans, define investment roadmap and begin implementation for key asset classes**
 - Operating infrastructure system-wide (yards, sidings, other holdings)
 - Vehicles, equipment, and rolling stock
 - Real Estate holdings
- **Modernize with value-added technology to enhance operational efficiency, grow business, and improve customer service and employee engagement**
- **Achieve system certification of Positive Train Control (PTC) system by 2018**
- **Target return on invested capital of at least one full percentage point higher than ARRC's cost of money**
 - Invested capital is the debt, equity and grant funds invested in the assets of the business
 - ARRC's cost of money is a weighted-average of the cost of each of its debt, equity and grant funds

The 5-year Capital Improvement Plan starting on page 12 provides more detail on other key projects and funding.



STRATEGY 4



BUILD A PROACTIVE CULTURE OF SAFETY AND ENGAGEMENT

- Implement plan to significantly improve engagement and safety culture by 2019 measured by improved net promoter and overall engagement scores
- Reduce employee year-over-year injuries by at least 3% annually with 2014 as the baseline by the development and implementation of proactive Safety Programs
 - Workplace Inspections Program
 - Safety Committee Program
 - Risk Assessment Program
 - Supervisor Safety Training Program
 - Formal Incident Investigation Program
 - Corrective Action Program
- Implement a System Safety Program Plan (SSPP)



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STRATEGY 5



ENHANCE ECONOMIC DEVELOPMENT, STEWARDSHIP AND STAKEHOLDER RELATIONS



Promote and advance regional economic development priorities through strategic partnerships

- Strengthen and expand relationships with local and state-wide economic development and tourism partners
- Support state and military efforts to secure funding for Northern Rail Extension Phase II
- Complete and place in service the Port McKenzie Rail Extension in compliance with Matanuska-Susitna Borough plans and funding

Implement state and national advocacy campaigns

- Execute annual PTC funding campaigns until project implementation is complete
- Execute federal formula funds retention campaign if and when needed
- Work with national industry associations to manage the impact of regulatory changes

Enhance and promote environmental stewardship of our land, facilities, and the environment in which we operate

- Retain Green Star certification
- Reduce carbon footprint by 1% annually
- Reduce utility consumption 2% per year

Increase the public's understanding about the Railroad and enhance our community support

- Strengthen relationships with civic and elected leaders in communities affected by the Railroad's activities
- Be a respectful, involved and responsive neighbor

5-YEAR CAPITAL IMPROVEMENT PLAN



FEDERAL FUNDING

FEDERAL TRANSIT ADMINISTRATION (FTA) FORMULA FUNDS

	2015	2016	2017	2018	2019	5-Year Total
Total FTA (with 20% match):	\$35,030,003	\$35,030,003	\$35,030,003	\$35,030,003	\$35,030,003	\$175,150,015
Preventive Maintenance	12,119,150	12,240,342	12,362,745	12,486,372	12,611,236	61,819,845
2007 Bond Debt Service	9,139,077	9,136,906	9,118,638	9,107,776	9,095,726	45,598,123
2006 Bond Debt Service	7,486,648	7,480,060	7,473,560	7,467,905	7,456,250	37,364,423
Transit Security	119,970	119,970	119,970	119,970	119,970	599,850
Transit Enhancements	119,970	119,970	119,970	119,970	119,970	599,850
Total Programmed Items	28,984,815	29,097,248	29,194,883	29,301,993	29,403,152	145,982,091
Total Grant Funds Available for Projects	\$6,045,188	\$5,932,756	\$5,835,120	\$5,728,010	\$5,626,851	\$29,167,924
Projects Funded by FTA Funds:						
Track Rehab Program	6,045,188	5,932,756	5,835,120	5,728,010	5,626,851	29,167,924
Total Projects	6,045,188	5,932,756	5,835,120	5,728,010	5,626,851	29,167,924
Total FTA Grant Projects, Net of Programmed Items	\$35,030,003	\$35,030,003	\$35,030,003	\$35,030,003	\$35,030,003	\$175,150,015

STATE FUNDING (REQUESTED)

Positive Train Control	\$21,767,322	\$16,406,240	\$15,306,240	-	-	\$53,479,802
Total State of Alaska Funding	\$21,767,322	\$16,406,240	\$15,306,240	-	-	\$53,479,802

DEBT FINANCING

Vehicle & Equipment Program	\$3,725,000	-	-	-	-	\$3,725,000
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INTERNAL FUNDING

NON-DISCRETIONARY PROJECTS

	2015	2016	2017	2018	2019	5-Year Total
Bridge Program	\$3,700,000	\$4,000,000	\$4,000,000	\$4,000,000	\$4,000,000	\$19,700,000
Track Rehab	979,900	10,567,245	10,614,880	10,721,990	12,423,149	45,307,164
Seward Passenger Dock Cathodic Protection Repairs	400,000	-	-	-	-	400,000
Whitney Rd. And C St. Storm Drain Replacement	150,000	-	-	-	-	150,000
Vehicle Program	725,000	905,000	980,000	1,040,000	1,015,000	4,665,000
Equipment Program	120,000	3,080,000	3,238,500	3,118,500	3,595,000	13,152,000
Wasilla Shops Landscaping and Paving	225,000	-	-	-	-	225,000
Explorer Creek Bridge Replacement	725,000	-	-	-	-	725,000
Subtotal - Non-Discretionary Projects	\$7,024,900	\$18,552,245	\$18,833,380	\$18,880,490	\$21,033,149	\$84,324,164

CONTINUING PROGRAMS

Avalanche and Slide Zone Risk Mitigation	\$230,000	\$6,330,000	\$475,000	\$14,215,000	\$475,000	\$21,725,000
Gravel Corridor Pony Truss Replacement	2,000,000	3,300,000	3,300,000	3,300,000	3,300,000	15,200,000
Capital Locomotive Overhaul Program / PM Plan	1,050,000	1,896,000	1,659,000	1,427,000	1,134,000	7,166,000
Capital Locomotive Truck Overhaul Program	180,000	180,000	\$180,000	180,000	180,000	900,000
Docks and Slips Maintenance	1,000,000	1,500,000	1,500,000	1,500,000	1,500,000	7,000,000
MP 356-357 Stabilization	150,000	475,000	150,000	150,000	150,000	1,075,000
Rip Rap Program / Drainage Maintenance	400,000	500,000	500,000	500,000	500,000	2,400,000
Yard and Branch Improvements	400,000	1,000,000	1,000,000	350,000	687,500	3,437,500
Trespass Mitigation	35,000	35,000	35,000	35,000	35,000	175,000
Defect Detector Upgrades	400,000	465,457	479,421	375,898	-	1,720,776
Passenger Rolling Stock Rehab Program	627,800	\$500,000	500,000	500,000	500,000	2,627,800
Roofing Upgrades	110,000	225,000	225,000	225,000	225,000	1,010,000
Seward Coal Loading Facility Upgrades	375,000	375,000	375,000	375,000	375,000	1,875,000
Electrical Upgrades	75,000	100,000	100,000	100,000	100,000	475,000
B-26 Air System Replacement	280,000	-	-	-	-	280,000
191 Heavy Maintenance	210,000	158,000	-	-	-	368,000
Building Maintenance	50,000	75,000	75,000	75,000	75,000	350,000
General Repair	55,000	55,000	55,000	55,000	55,000	275,000
Section Improvements	25,000	25,000	25,000	25,000	25,000	125,000
Capital Locomotive Compressor Overhauls	150,000	-	-	-	-	150,000
Crossing Signal Event Recorders	108,000	108,000	108,000	-	-	324,000

<i>(Continued...)</i>	2015	2016	2017	2018	2019	5-Year Total
Tenant Improvements	75,000	75,000	75,000	75,000	75,000	375,000
Energy Management	150,000	150,000	150,000	150,000	150,000	750,000
Land & Utilities	50,000	75,000	75,000	75,000	75,000	350,000
IT Server/Storage Budget	519,500	-	-	-	-	519,500
Power Distribution and Monitoring	50,000	80,000	80,000	100,000	100,000	410,000
Network Services	214,650	214,000	214,000	214,000	214,000	1,070,650
Copier Fleet Replacement	40,000	30,000	10,000	-	-	80,000
Alcatel Equipment	200,000	75,000	75,000	-	-	350,000
Subtotal - Continuing Programs	\$9,209,950	\$18,001,457	\$11,420,421	\$24,001,898	\$9,930,500	\$72,564,226
STRATEGIC BUSINESS INITIATIVES						
APU Spur Rehabilitation	\$284,000	\$91,000	-	-	-	\$375,000
MP 59 Skookum Creek Flood Mitigation	-	2,500,000	-	-	-	2,500,000
IFRA Measure	85,000	-	-	-	-	85,000
Surge Tester	60,000	-	-	-	-	60,000
Summit Detector Relocation	92,400	-	-	-	-	92,400
Diesel Generator Upgrade to SOFC	223,700	223,700	447,400	447,400	-	1,342,200
Talkeetna Driveway Approach Pavement Repairs	80,000	-	-	-	-	80,000
Wayside Rail Lubricators	200,000	50,000	50,000	50,000	-	350,000
Voice Recorder Replacement	100,000	-	-	-	-	100,000
Upgrade of Access Control Panels	76,550	-	-	-	-	76,550
Post Road Sewer Construction - Finish Phase 2	420,000	-	-	-	-	420,000
Post Road Sewer Construction - Start Phase 4	415,000	-	-	-	-	415,000
JD Edwards Rollout Effort	350,000	-	-	-	-	350,000
Subtotal - Strategic Business Initiatives	\$2,386,650	\$2,934,700	\$497,400	\$497,400	-	\$6,316,150
Total Internally Funded Project Requests	\$18,621,500	\$39,488,402	\$30,751,201	\$43,379,788	\$30,963,649	\$163,204,540
Estimated Funds from Internal Cash flow	\$18,621,500	\$22,127,920	\$24,374,763	\$27,153,100	\$30,426,137	\$122,703,420
Total Internal Funding Shortage	-	(17,360,482)	(6,376,438)	(16,226,688)	(537,512)	(40,501,120)
TOTAL GRANT FUNDS AVAILABLE FOR PROJECTS	\$6,045,188	\$5,932,756	\$5,835,120	\$5,728,010	\$5,626,851	\$29,167,924
TOTAL DEBT FINANCING	3,725,000	-	-	-	-	3,725,000
TOTAL STATE FUNDING	21,767,322	16,406,240	15,306,240	-	-	53,479,802
TOTAL INTERNAL FUNDING AVAILABLE	18,621,500	22,127,920	24,374,763	27,153,100	30,426,137	122,703,420
TOTAL CAPITAL PROGRAM	\$50,159,010	\$44,466,916	\$45,516,123	\$32,881,110	\$36,052,988	\$209,076,146

