

AGENDA ITEM 9-J
ACTION ITEM

TO: CHAIRMAN JENKINS AND THE VRE OPERATIONS BOARD

FROM: DALE ZEHNER

DATE: JUNE 20, 2008

**RE: AUTHORIZATION TO SELL THIRTEEN KAWASAKI RAILCARS
AND TO PURCHASE TEN NEW GALLERY STYLE CARS**

RECOMMENDATION:

The VRE Operations Board is being asked to recommend that the Commissions authorize the VRE Chief Executive Officer to sell thirteen Kawasaki railcars to the Maryland Transit Administration and to concurrently purchase ten new Gallery style cars from the Sumitomo Corporation of America.

BACKGROUND:

In March of 2008, the Operations Board authorized the Chief Executive Officer to pursue the sale of thirteen Kawasaki railcars and issue an RFP for the purchase of ten new Gallery cars to potentially replace the Kawasaki cars. The two transactions were linked because the Kawasaki railcars could not be sold unless sufficient funds were available to purchase replacement cars.

Following that authorization, VRE posted both the Intent to Sell and RFP on the VRE web site. In response to the RFP for new cars, VRE received one proposal from the Sumitomo Corporation of America. VRE and Sumitomo Corporation of America negotiated a purchase price of \$22,000,000 for ten Gallery style railcars. The total cost of the new cars, with construction oversight and contingency is estimated at \$24,980,000. VRE recommends the purchase contingent upon the sale of thirteen Kawasaki railcars under the terms described below. A separate

action item for construction oversight of the manufacture will be brought before the Operations Board at an upcoming meeting.

The funding for the ten new railcars would come from two sources: (1) the net cash generated by the sale of the Kawasaki cars; and (2) the remaining available loan funds previously authorized by the Commissions and included in the Federal Railroad Administration (FRA) financing that was used for the purchase of the 50 railcar option. The increased payments for the FRA loan would then, in turn, be paid for using funding originally allocated for the repayment of the Kawasaki bonds.

The FRA approved a loan to VRE for \$72.5 million in 2005. However, only \$57.5 million of the total loan amount was needed for the 50 railcar option order and subsequently approved by the Commissions. Additional grant funds were provided by the state prior to completing the purchase which further reduced the loan amount to \$55 million, leaving an available loan balance of over \$17 million. FRA has approved the addition of ten cars to the current loan in principle and the paperwork is forthcoming.

With respect to the sale of the thirteen Kawasaki railcars, VRE publically posted and initiated discussions with four commuter rail agencies to stimulate interest in the sale and received one written offer from the Maryland Transit Administration (MTA) for \$22 million, inclusion of associated spare parts, and their assumption of the remaining federal interest. After reviewing the terms of that offer, VRE staff recommends acceptance. PFM, VRE's financial advisor, estimates that \$14.3 million is needed to defease (put funds aside to service the remaining debt) the outstanding Series 1997 bonds used to finance the Kawasaki railcars. The MTA offer provides sufficient funds to defease the bonds and pay for a portion of the purchase price of the replacement cars. The remainder of the purchase price will be funded using the FRA loan. Loan payments will be made via federal formula funds currently used for the debt service on the Series 1997 Kawasaki bonds.

Total funding for the ten new railcars will be provided for as follows:

Cash remaining from sale of Kawasaki railcars	\$ 7,700,000
FRA loan	<u>17,280,000</u>
Total	\$24,980,000

The financial details of both transactions are provided in the attached chart. The FRA loan capacity is already in place and can be accessed immediately, providing the Commissions and jurisdictions have approved the assumption of this debt. The loan carries a 4.74% interest rate and allows prepayment at any time without penalty.

Benefits of Kawasaki Sale

- a. Standardizes VRE's fleet to all Gallery style railcars. If the sale and purchase is approved, VRE will have 71 new Gallery style railcars and 30 older Gallery style railcars in the fleet. The fleet would provide sufficient railcars for up to 14 consists and 36 trains. Today VRE operates 11 consists and 30 trains. Replacing 13 Kawasaki railcars with 10 new Gallery style railcars does not impede VRE's ability to expand the service to 36 trains as outlined in our fleet plan through FY 2016 as more of the Pullman gallery fleet is being retained.
- b. Reduces railcar maintenance costs. The 13 Kawasaki railcars are more mechanically complex than the Gallery railcars. Historically, these cars have had an average of 11% higher maintenance costs than VRE's Gallery railcars. They are designed for 125 mph service and have dual braking systems compared to the Gallery coaches which are rated at 79 mph and have a single brake system. Currently, both CSX and NS limit VRE's operating speed in the corridor at 79 mph.
- c. Increases fleet flexibility. Currently, the Kawasaki railcars have limited compatibility with the Gallery railcars and are functionally, a stand-alone fleet. Thus, VRE is limited to using the Kawasaki railcars in unique consists and can only achieve two six-car consists or one eight-car and one four-car consist. In either configuration, VRE only has a one car contingency for maintenance – which is considered too low for VRE's level of service reliability.
- d. Provides exceptional sales price for the Kawasaki railcars. The total sales price for the Kawasaki railcars is nearly what we paid for the railcars nine years ago. VRE staff does not believe a higher price will be achieved in the future. Thus, the time to sell the railcars is now.

NEXT STEPS

The Notice to Proceed (NTP) for the Gallery railcar purchase must be granted no later than September 26, 2008, with VRE's best effort made to issue a Notice by August 31, 2008, under the terms of Sumitomo's response to the RFP. In addition, the Amended Offer from MTA for the purchase of the Kawasaki cars is only valid until early October. As a result, the required Commission and jurisdiction approvals must be secured as rapidly as possible.

The requests for authorization to sell the Kawasaki cars, defease the associated debt, purchase the Gallery cars and increase the loan amount for this purpose will be presented to the Commissions at their July meetings. In order to expedite the process, the Operations Board is being asked to authorize the Chief Executive Officer to approach each jurisdiction following Operations Board approval to attempt to gain jurisdictional approval for the purchase of the Gallery cars and the issuance of additional debt prior to August 31, 2008.

Finally, prior to the sale of the Kawasaki railcars, FTA must approve the transfer of remaining federal interest in these railcars to MTA. Preliminary discussions with FTA have occurred and formal approval for the transfer will be sought. These discussions would resume with urgency following Operations Board approval.

FISCAL IMPACT:

The financial impact of the sale of thirteen Kawasaki railcars and purchase of ten new Gallery railcars is projected as follows:

Decrease in outstanding debt	\$13,535,000
Increase in new debt	<u>17,280,000</u>
Net increase in total debt	\$3,745,000
Decrease in annual debt service costs	\$712,151

An analysis was done which compared the costs of debt repayment and maintenance for the 15 year period from FY 2009 to FY 2023 for the purchase of the new railcars and the retention of the existing railcars. The decrease in gross costs for the period, as a result of the requested purchase, is estimated at approximately \$4.0 million. The decrease in costs on a net present value basis for the same period is approximately \$5.3 million, as both the maintenance and financing costs are lower in the near term if the new Gallery railcars are purchased.

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DATE: JUNE 20, 2008
RE: AUTHORIZATION TO SELL THIRTEEN KAWASAKI RAILCARS
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RESOLUTION
9J-06-2008
OF THE
VIRGINIA RAILWAY EXPRESS
OPERATIONS BOARD

WHEREAS, VRE has been presented with a unique market opportunity to sell the Kawasaki fleet; and,

WHEREAS, such a sale could standardize VRE's railcar fleet and reduce overall railcar maintenance costs; and,

WHEREAS, the requirements for VRE's fleet size can be sustained through the acquisition of ten more Gallery style cars to replace the Kawasaki cars; and,

WHEREAS, through competitive advertising and solicitation, buyers and sellers have been identified and two separate, but linked transactions are being recommended by VRE staff; and,

WHEREAS, the Master Agreement provides that VRE shall utilize reasonable debt financing to the extent that such financing is advantageous and is in the interest of the parties to the Master Agreement, but requires that VRE not assume debt without the consent of all Participating and Contributing Jurisdictions.

NOW, THEREFORE, BE IT RESOLVED THAT, the VRE Operations Board recommends that the Commissions authorize the Chief Executive Officer to execute a sales agreement for the sale of thirteen Kawasaki railcars and associated spare parts to the Maryland Department of Transportation for \$22 million and their assumption of the remaining federal interest; and,

BE IT FURTHER RESOLVED THAT, the VRE Operations Board recommends that the Commissions authorize the Chief Executive Officer to purchase ten new Gallery railcars from Sumitomo Corporation of America for \$22 million, plus a contingency of \$660,000, for a total amount not to exceed \$22,660,000; and,

BE IT FURTHER RESOLVED THAT, the VRE Operations Board recommends that subject to approval by all VRE Master Agreement signatory member jurisdictions, the Commissions authorize an increase to the FRA loan in an amount not to exceed \$17,350,000, with a term not to exceed 25 years, an interest rate of 4.74%, and a credit risk premium of 1.88%; and,

BE IT FURTHER RESOLVED THAT, the VRE Operations Board recommends that the Commissions authorize the Chief Executive Officer to negotiate, complete, execute and deliver documents required to achieve said FRA financing and pay any associated financing costs to a related payee; and,

BE IT FURTHER RESOLVED THAT, the VRE Operations Board recommends that the Commissions authorize the Chief Executive Officer to negotiate, complete, execute and deliver documents required to defease the 1997 Kawasaki bonds and pay any associated financing costs to a related payee; and,

BE IT FURTHER RESOLVED THAT, in order to expedite the process required for implantation of the loan, the VRE Operations Board authorizes the Chief Executive Officer to approach each VRE member jurisdiction in an effort to gain jurisdictional approval of debt prior to August 31, 2008.

Sale of Kawasaki Railcars and Purchase of New Gallery Railcars

Sale of Kawasaki Railcars

Comments

Series 1997 Bond Issue

Amount of issue - 7/1/1997	23,000,000
Amount outstanding after 7/1/2008	13,535,000
Cost of defeasance	14,300,000

Proceeds from Sale

Estimated sale price	22,000,000
Cost of defeasance	14,300,000
Cash remaining after defeasance	7,700,000

Current Loan Costs for Kawasaki Railcars

Current annual debt service costs	1,950,000	Varies each year; \$1.95 is aver.
Number of years remaining	9	Last payment on 7/1/2017
Amount outstanding after 7/1/2008	13,535,000	

Purchase of New Gallery Railcars

Number of cars needed	10	
Base Price per car	<u>2,200,000</u>	
Total cost for railcars	22,000,000	
Oversight of construction	2,100,000	
Contingency	<u>880,000</u>	
Total cost for new railcars	24,980,000	
Amount to be financed	17,280,000	Provided by FRA RRIF Loan
Annual debt service, RRIF loan	1,237,849	
Number of years based on existing loan origination date	23	Last payment on 3/19/2033

Cost Comparison - Result of Sale of Kawasaki Cars and Purchase of Gallery Cars

(Decrease) to annual debt service costs	(712,151)	
Increase to total debt	3,745,000	
For 15 year period - FY 2009 to FY 2023:		
(Decrease) to gross costs	(4,038,234)	
(Decrease) to costs - net present value	(5,277,472)	NPV limited to 15 years as projections beyond this term are extremely uncertain. VRE's financial advisor concurred.
