This written testimony is being submitted to the Select Revenue Measures Subcommittee in connection with its March 12, 2019 hearing on “Temporary Policy in the Internal Revenue Code.” My name is Chuck Baker and I am President of the American Short Line and Regional Railroad Association (ASLRRA), the national trade association representing the nation’s 603 Class II and Class III railroads (referred to here collectively as “short lines”). I appreciate the opportunity to discuss the economic and service inefficiencies resulting from temporary and short-term extensions of this credit and why making the credit permanent will make an important and lasting contribution to the national freight rail network and the shippers it serves.

The Short Line Tax Credit, known by its code section 45G, was first enacted in 2004 and has been extended six times through 2017. Each time, stand-alone legislation to extend the credit has been one of the most heavily co-sponsored and bipartisan pieces of legislation introduced in that Session of Congress. In the last Session of Congress 23 Members of the Ways & Means Committee co-sponsored the bill almost evenly split between Democrats and Republicans. This year Congressman Blumenauer and Congressman Kelly have introduced H.R. 510, that like H.R. 721 from the 115th Congress, makes the credit permanent. The new legislation has already attracted 137 co-sponsors including 15 Members of the Ways & Means Committee.

The credit was intended to allow short lines to spend more of what they earn rehabilitating track and bridges, to make safer, more efficient and seamless rail freight connections between communities and customers on the national rail freight network. Most of today’s short line railroads were created to bring back to life what were previously under-maintained Class I branch lines headed for abandonment. Particularly for rural and small-town America these lines are the only connection to the national railroad network. To succeed they invest on average from 25 to 33 percent of their annual revenues back into their properties, making them one of the most capital-intensive industries in the country. At the same time, the combination of relatively short route distances and the lighter volumes shipped by the small businesses they serve results in limited revenues available for additional investment. The 45G tax credit is an efficient and effective way to maximize those investment dollars. Since enactment, the credit has allowed short lines to spend an additional $2.1 billion of their hard-earned revenues toward the goal of ensuring that the first and last mile of rail service in large areas of the country is as efficient, competitive and safe as the rest of the national railroad network.

The credit’s unique structure maximizes capital investment in two ways:

1. 45G requires the railroad to spend two dollars for every dollar in credit, up to a credit cap equivalent to $3,500 per track mile. Short lines must invest significant amounts of their revenue for the right to spend even more of their own revenue on rehabilitation.

2. The ability to assign eligible tax credit miles to a shipper that can use the resulting tax credit allows smaller railroads with insufficient cash flow to fund expensive rehabilitation that would otherwise be out of reach.

The right tax policy can be enormously beneficial to the American economy by incentivizing the capital investment businesses need to grow, innovate and create jobs. Those benefits are significantly reduced when tax policy starts and stops in a temporary short-term fashion. Forward planning is impossible and expensive multi-year projects are difficult to undertake. Particularly in the railroad industry the most
meaningful benefits with regard to service and safety come when we can rehabilitate an entire corridor not just a mile here and a mile there. For us, piecemeal investment is only as good as the size of the pieces and one year and sometimes even retroactive extensions are small pieces indeed.

The Blumenauer/Kelly legislation makes the short line tax credit permanent. There are seven good reasons why this approach is far better than temporary extensions. Some of these are true for all industries and some are unique to short line railroading.

1. The purpose of the credit is to maximize capital investment in the private sector which is what helps companies grow and create jobs. It is difficult to make investment decisions when there is uncertainty regarding the availability of funds. We have a reliable data point that demonstrates that fact. For decades the Railway Tie Association (RTA) has kept comprehensive statistics on railroad tie purchases. RTA has determined that the short line tax credit results in between 500,000 and 1.2 million short line tie purchases beyond their normalized annual purchases. The data shows that tie purchases are at the low end in those years when the credit was only extended for one year or retroactively at the end of a year and at the high end when the credit was extended for a longer period.

2. American shippers and by extension American consumers are the ultimate beneficiaries of railroad rehabilitation through the creation of more reliable, more competitive and safer transportation. But the maximum benefit is only realized when an entire rail corridor is rehabilitated and that takes many years. Five miles of rehabilitated track yields limited benefit when it is bookended by miles of unrehabilitated track or bridges in need of repair. Companies cannot effectively plan for an expensive multi-year project based on a one-year commitment by the federal government.

3. The promise of faster more competitive service gives shippers an incentive to invest in new on-line facilities. In South Dakota, for example, the improvements made by the 670-mile Rapid City, Pierre & Eastern (RCP&E) since it began operations in 2014 has attracted over $311 million in new facility investments by six South Dakota companies, creating over 270 new industrial and agricultural sector jobs. For years, shippers would not invest in facilities along the RCP&E’s line because of unreliable service and an uncertain future. The 45G credit helped fund the improvements that changed that reality, restored shipper confidence and became a catalyst for new industrial development.

4. The additional infrastructure investment made possible by the 45G credit has improved safety performance. Since enactment of the credit in 2004, train accidents on short line railroads have declined by more than 50 percent, from a rate of 6.84 per million train miles in 2004 to 3.18 in 2017. Short line safety performance is now approaching that of the larger Class I railroads and has improved at a faster rate than Class I railroads over the period of the 45G credit has been in existence.

5. Today’s short line railroads were created as a response to the loss of rail service, particularly in rural and small-town America. The Class I cost structure could not support the light density branch lines operating in those areas and were forced to abandon them. With the economic freedoms and flexibility provided by the Staggers Act of 1980, entrepreneurs were able to purchase these lines and run them profitably as local small businesses. In 1980 short lines operated 8,000 miles of track. Today they operate nearly 50,000 miles and the need to create
additional short line service continues as the Class I’s make decisions about their own allocation of capital between heavy and light density lines. To continue to save light density lines and preserve service short lines must borrow large sums of money to purchase the franchise and rehabilitate the track. Making 45G permanent will make the difference between saving a line and losing a line for many years to come.

6. Railroad service is the most environmentally friendly form of transportation. Railroads can move one ton of freight 479 miles on a single gallon of fuel, making trains four times more fuel efficient than trucks. A single railcar can take 3 to 4 trucks off the highway. It is estimated that taking just 5 percent of freight from truck to rail would result in nine million fewer tons of greenhouse gas emissions. Helping short lines continue to grow freight traffic through infrastructure improvements will deliver long term benefits to the environment.

7. Finally, there is a very practical reason for making the credit permanent. Congressional business and private business operate in two different worlds. Congress is a deliberative body requiring lengthy negotiations to secure agreement by a majority of Members. By necessity decisions are often made at the eleventh hour, are short term in nature, and in the case of many tax provisions, including 45G, are retroactive rather than forward looking. Short lines cannot make capital allocation decisions in that fashion. To take on expensive, long-term projects they need certainty. In a democracy it is understandably difficult for the government’s decision-making process to accommodate that certainty. The best way to reconcile these two worlds is to make the credit permanent so it can fully achieve the results for which it was intended.

For 12 years the short line tax credit has proven its worth. It has maximized capital investment by both railroads and customers, it has significantly improved competitive rail service for shippers, it has helped improve railroad safety and it has been the difference between piecemeal and corridor improvements. It has worked as intended and when you find something that works, the best thing to do is let it work. I very respectively encourage the 116th Congress Ways & Means Committee to fix the unintended but real suboptimal policy consequences of sporadic attention to the Short Line Tax Credit and make this credit permanent.