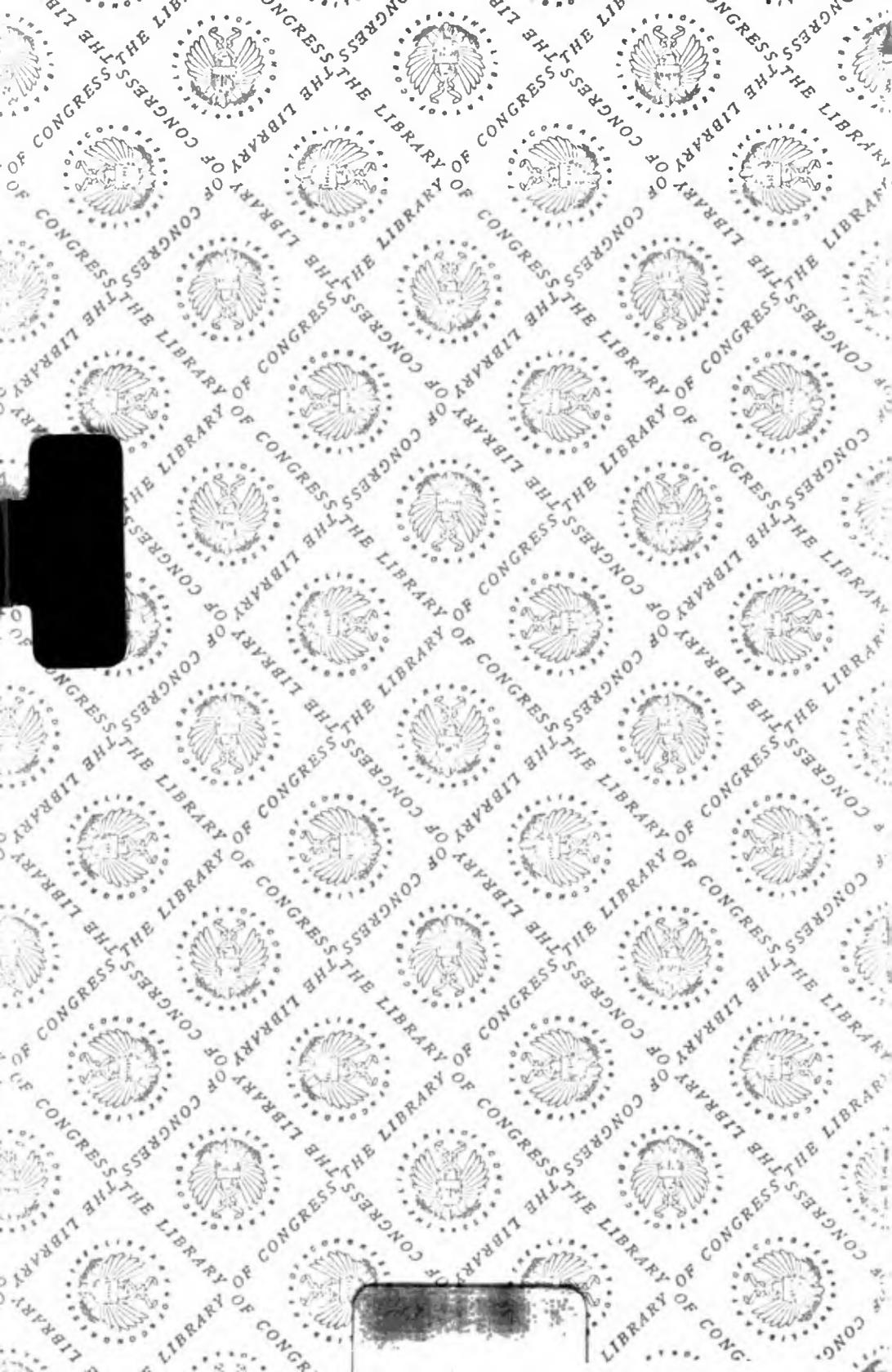
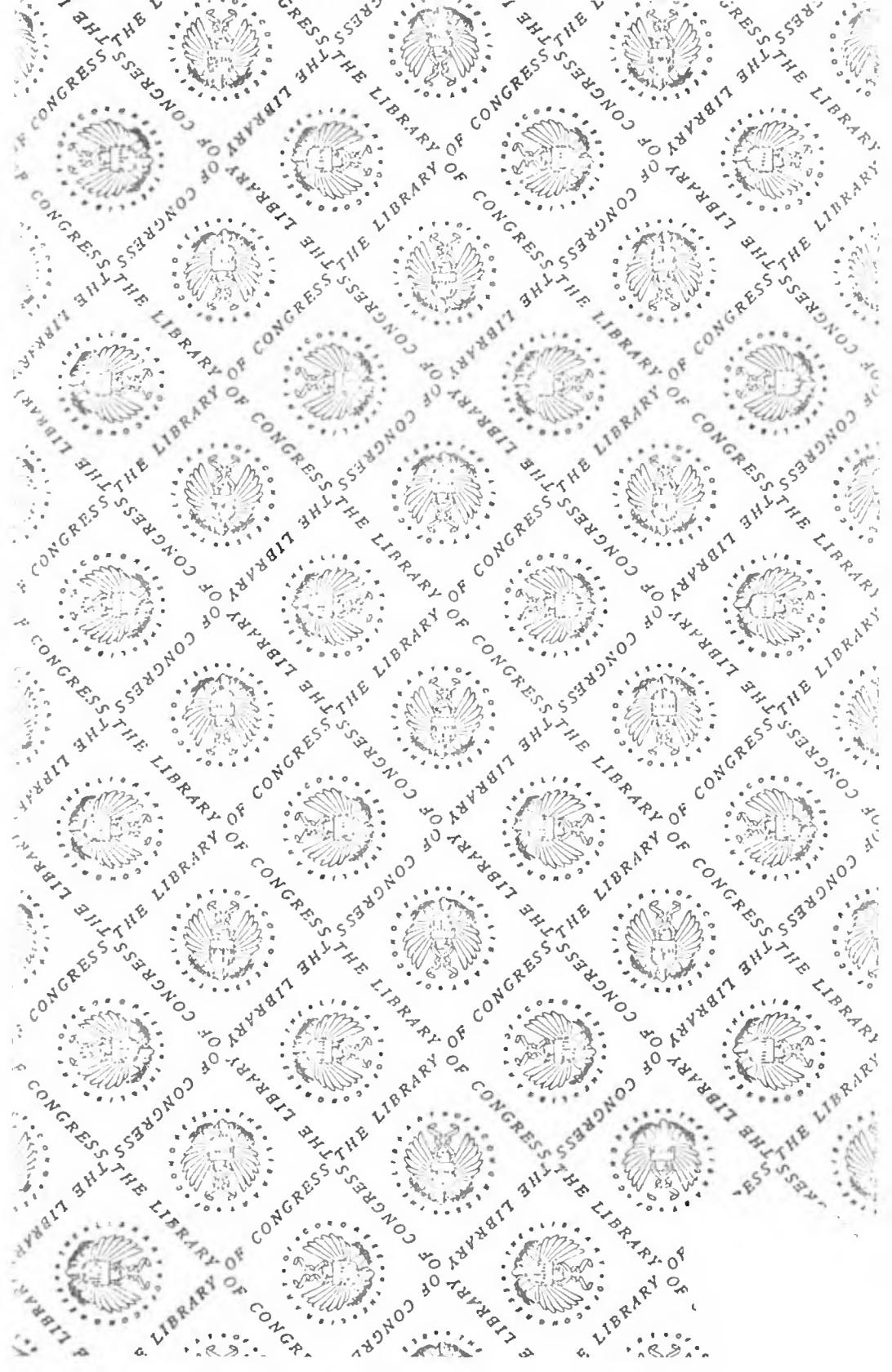


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Foreign Commerce. Subcommittee on Transportation and Commerce.

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# GUARANTEE OF DELINQUENT TAXES DUE FROM BANKRUPT RAILROADS

HEARINGS

BEFORE THE

SUBCOMMITTEE ON  
TRANSPORTATION AND COMMERCE

OF THE

COMMITTEE ON  
INTERSTATE AND FOREIGN COMMERCE  
HOUSE OF REPRESENTATIVES

NINETY-FIFTH CONGRESS

FIRST SESSION

ON

**H.R. 8882, H.R. 9015, H.R. 9023, and H.R. 9024**

BILLS TO AMEND THE REGIONAL RAIL REORGANIZATION ACT OF 1973 TO AUTHORIZE THE SECRETARY OF TRANSPORTATION TO GUARANTEE NOTES ISSUED TO STATE AND LOCAL TAXING AUTHORITIES TO SECURE PAYMENT OF REAL PROPERTY TAX OBLIGATIONS OWED BY A RAILROAD IN REORGANIZATION, AND FOR OTHER PURPOSES

SEPTEMBER 27, 28, AND OCTOBER 4, 1977

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# GUARANTEE OF DELINQUENT TAXES DUE FROM BANKRUPT RAILROADS

TUESDAY, SEPTEMBER 27, 1977

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON TRANSPORTATION,  
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,  
*Washington, D.C.*

The subcommittee met at 2 p.m., pursuant to notice, in room 2212, Rayburn House Office Building, Hon. Fred B. Rooney, chairman, presiding.

Mr. ROONEY. The subcommittee will be in order.

On June 21, 1970, the Penn Central Transportation Co. announced that it was bankrupt and filed a petition for reorganization in court. This was the largest corporate bankruptcy in the history of this country. As a consequence it is understandable that the shock waves of this unfortunate circumstance would be felt throughout the country and not merely in the particular areas of the northeast quadrant of the country in which the railroad operated.

It was obvious that in the national interest it was necessary to keep the railroad operating. As a consequence Congress passed the Emergency Rail Services Act of 1970, which, among other things, provided funds to keep the railroad operating.

It subsequently became obvious that long-range corrective actions had to be taken to restructure the fast-deteriorating rail service in this country. Therefore Congress passed the Regional reorganization Act of 1973, which, among other things, established the U.S. Railway Association and directed it to devise a plan for restructuring the railroad system in the Northeast.

Subsequently Congress passed the Railroad Revitalization and Regulatory Reform Act of 1976. This act, among other things, provided the funds for restructuring the six bankrupt railroads in the Northeast into a new railroad, to be called ConRail.

Today we are to consider another of the problems resulting from the 1970 Penn Central bankruptcy. Namely, the bankruptcy railroads owe considerable amounts of delinquent taxes to about 2,500 communities and 15 States in which it operated.

At the time the Federal court directed Penn Central to continue to operate after its bankruptcy, the court further ordered that the corporation refrain from paying its State and local taxes until it was permitted to do so by the court.

Also, when Congress directed the conveyance of a number of Penn Central railroad properties to ConRail, it also mandated that these properties should be free and clear of tax liens. That is, the delinquent taxes were left with the Penn Central Transportation Co.

Subsequently Penn Central attempted to form a new company. Part of this reorganization process which is now before the bankruptcy court provides for a compromise in the payment of delinquent taxes. I understand a number of our witnesses plan to explain the various aspects of this compromise proposal during the course of these hearings. Therefore it is not necessary to reiterate them at this time.

Suffice to say that one segment of the proposal is for the reorganized company to issue various types of notes in the amount of 80 percent of the delinquent taxes, and the question before us today is whether the Federal Government should guarantee the payment of these notes.

I recognize the plight of many local communities—and, in particular, their school districts—which have continual problems raising what is considered sufficient operating funds. Understandably they would like to receive the full amount of the delinquent taxes. Therefore it will not be necessary for us to dwell on the desirability of these communities to receive the funds.

Nor is there a question as to the fact that the taxes are due. Rather it is incumbent upon the subcommittee to find the answers to a number of fundamental questions regarding the effect on all parties if the Federal Government were to accept the proposal to guarantee the payment of the notes to be issued for the payment of delinquent taxes.

For example, we must ascertain the effect this guarantee would have on the Government valuation case. The U.S. Railway Association is presently in court trying to determine the value of the properties conveyed to ConRail.

One class of the notes to be issued by the reorganized Penn Central Co., which this bill proposes be guaranteed by the Federal Government, is to be secured by the proceeds of the valuation case. It must be determined whether, if the Government wins this case, there will be sufficient funds to pay the notes.

Similarly we must determine the effect the proposed legislation would have on the pending litigation regarding claimed erosion of assets. We must ascertain the probable cost to the Government if it were to guarantee three notes. We must determine whether the guaranteeing of these notes would constitute an undesirable precedent for the Federal Government.

We also must determine the effect that the proposed legislation would have on the future tax bases of the reorganized company. That is, it must be questioned whether the guarantee of the delinquent taxes would endanger the payment of future taxes and thereby be a pyrrhic victory.

Without objection the text of H.R. 8882, H.R. 9015, H.R. 9023, and H.R. 9024 will be printed at this point in the record.

[The text of the bills referred to follows:]

[H.R. 8882, introduced by Ms. Oakar (for herself, Mr. Moakley, Mr. Ashbrook, Mr. Vanik, Mr. Burke of Massachusetts, Mr. Mottl, Mr. Seiberling, Mr. Pease, Mr. Stanton, Mr. Conte, Mr. Applegate, Mr. Wylie, and Mr. Cavanaugh) on August 5, 1977;

H.R. 9015, introduced by Mr. Latta on September 9, 1977;

H.R. 9023, introduced by Ms. Oakar (for herself, Mr. Rodino, Mr. Whalen, Mr. Miller of Ohio, Mr. Nix, Mr. Brown of Ohio, Mr. Michael O. Myers, Mr. Guyer, Mr. Lederer, Mr. Eilberg, Mr. Edgar, Mr. Kostmayer, Mr. Flood, Mr. Ertel, Mr. Ammerman, Mr. Walgren, Mr. Hollenbeck, Mr. Markey, Mr. Lundine, Mrs. Heckler, Ms. Mikulski, Mrs. Spellman, Mr. McDade, Mr. Mitchell of Maryland, and Mr. Beard of Rhode Island) on September 9, 1977; and

H.R. 9024, introduced by Ms. Oakar (for herself, Mr. Gilman, Mr. Fish, Mr. Le Fante, Mr. Nowak, Mr. St Germain, Mr. Drinan, Mr. Forsythe, Mr. Stratton, Mr. Harsha, and Mr. Yatron) on September 9, 1977,

are identical as follows:]

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## A BILL

To amend the Regional Rail Reorganization Act of 1973 to authorize the Secretary of Transportation to guarantec notes issued to State and local taxing authorities to secure payment of real property tax obligations owed by a railroad in reorganization.

1       *Be it enacted by the Senate and House of Representa-*  
 2       *tives of the United States of America in Congress assembled,*  
 3       That the Regional Rail Reorganization Act of 1973 (45  
 4       U.S.C. 701 et seq.) is amended by adding at the end thereof  
 5       the following new section:

6                       "GUARANTEES BY THE SECRETARY.

7       "SEC. 606. (a) (1) In any proceeding for the reor-  
 8       ganization or liquidation of a railroad under section 77 of the

1 Bankruptcy Act in which the Corporation, the Association,  
2 or the Federal Government, including any agency, instru-  
3 mentality, or department thereof, asserts a priority in pay-  
4 ment out of the estate of such a railroad over tax obligation  
5 owed to State or local taxing authorities, the Secretary shall  
6 guarantee the payment according to their respective terms  
7 of principal and interest on securities and obligations, includ-  
8 ing securities and obligations issued to refinance any such  
9 securities and obligations, issued by a railroad in reorganiza-  
10 tion to such State and local taxing authorities.

11 “(2) The maturity date of such securities, obligations,  
12 and loans, including all extensions and renewals thereof, shall  
13 not be later than twenty years from their date of issuance.

14 “(3) All guarantees entered into by the Secretary  
15 under this section shall constitute general obligations of the  
16 United States of America from which the full faith and  
17 credit of the United States of America shall be pledged.

18 “(b) No guarantee made by the Secretary under this  
19 section shall thereafter be terminated, canceled, or otherwise  
20 revoked; the issuance of such guarantee shall be conclusive  
21 evidence that the guarantee complies fully with the provi-  
22 sions of this chapter and shall constitute proof of the approval  
23 and legality of the principal amount, interest rate, and all  
24 other terms of the security or obligation guaranteed, which  
25 shall be valid and incontestable in the hands of a holder

1 except for fraud or material misrepresentation on the part of  
2 such holder.

3       “(c) If at any time the moneys available to the Seere-  
4 tary are insuffieient to enable him to discharge his responsi-  
5 bilities under guarantees issued by him under subsection (a)  
6 of this section, he shall issue to the Secretary of the Treasury  
7 notes or other obligations in such forms and denominations,  
8 bearing such maturities and subject to such terms and condi-  
9 tions, as may be prescribed by the Secretary of the Treasury.  
10 Redemption of such notes or obligations shall be made by the  
11 Secretary from appropriations available under subsection  
12 (d) of this section. Such notes or other obligations shall bear  
13 interest at a rate determined by the Secretary of the Treasury,  
14 taking into consideration the current average market yield on  
15 outstanding marketable obligations of the United States of  
16 comparable maturities during the month preceeding the issu-  
17 ance of such notes or other obligations. The Secretary of the  
18 Treasury shall purchase any notes or other obligations issued  
19 hereunder and for that purpose he is authorized to use as a  
20 public debt transaction the proceeds from the sale of any  
21 securities issued under the Second Liberty Bond Act, as  
22 amended, and the purposes for which securities may be  
23 issued under that Act, as amended, are extended to include  
24 any purchase of such notes or obligations. The Secretary of  
25 the Treasury may at any time sell any of the notes or other

1 obligations as acquired by him under this subsection. All  
2 redemptions, purchases, and sales by the Secretary of the  
3 Treasury of such notes or other obligations shall be treated  
4 as public debt transactions of the United States.

5       “(d) There are authorized to be appropriated to the  
6 Secretary such amounts, to remain available until expended,  
7 as are necessary to discharge all his responsibilities under  
8 this section.”.

9       SEC. 2. The table of contents of the Regional Rail Reor-  
10 ganization Act of 1973 is amended by adding at the end  
11 thereof the following new item:

“Sec. 606. Guarantees by the Secretary.”.

I now want to call upon several of my colleagues who have cosponsored this legislation and wish to comment. Our very distinguished author of this legislation, Hon. Mary Rose Oakar, is the scheduled first witness but perhaps you may wish to yield to your colleagues. Ms. Oakar, I recognize you.

Ms. OAKAR. Thank you, Mr. Chairman. First of all we wish to thank you, Mr. Chairman, for having such a speedy hearing, and I would be delighted to yield to my colleagues before I get on with my testimony. So I will yield to Congressman Mottl, of Ohio.

**STATEMENT OF HON. RONALD M. MOTTLE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO**

Mr. MOTTLE. Thank you, Mr. Chairman, members of the committee. I would like to thank my distinguished colleague from Cleveland, Mary Rose Oakar, for being the prime sponsor of this important piece of legislation and for allowing me to go first because I have a brief statement to provide the committee and also would like to congratulate not only her but also my colleague from south Boston, Joe Moakley, for being a cosponsor of this piece of legislation.

Mr. Chairman, I welcome this opportunity to speak out against the proposal that the bankrupt Penn Central Railroad be allowed to escape its tax debt to school districts and other government subdivisions by paying only 44 or 50 cents on a dollar. The subdivisions and schools provided Penn Central and its employees with the full gamut of services and should be paid in full for those services.

The railroad's debt to Cleveland city schools alone amounts to more than \$14 million. Debts to other Cuyahoga County taxing districts, including Cleveland schools, total more than \$16 million.

With school costs continually mounting and voters resisting new levies and bond issues, it is imperative that Penn Central be made to satisfy its legitimate debt in full.

Every school district in the Nation is experiencing difficulties with financing and drastically needs these long overdue tax dollars. It is not a windfall for them but payment of a legitimate debt long overdue and long awaited.

With this in mind I have enthusiastically cosponsored legislation introduced by my colleague, Representative Oakar, guaranteeing that the Federal Government would insure payment of the taxes and interest in full.

To insure that local subdivisions and school districts get priority payment of the delinquent taxes, I will introduce legislation calling for the Federal Government to waive all claims against Penn Central until the railroad pays its tax bills in full to local and State creditors second and to the Federal Government third.

Cleveland city schools and other school districts are teetering on the brink of bankruptcy and desperately need this money. It has been too long in coming.

Thank you, Mr. Chairman, and I certainly appreciate Ms. Oakar's allowing me to go first.

Mr. ROONEY. Thank you very much for your great interest in your constituency and your fine presentation.

Ms. OAKAR. I yield now to my colleague from Massachusetts, Mr. Moakley.

**STATEMENT OF HON. JOE MOAKLEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS**

Mr. MOAKLEY. Thank you, Mr. Chairman, for giving me the opportunity to speak on behalf of H.R. 8882, Congresswoman Mary Rose Oakar's amendments to the Regional Rail Reorganization Act of 1973. Basically the above-mentioned legislation authorizes the Secretary of Transportation to guarantee notes issued to States and local taxing authorities to secure payment of real property tax obligations owed by a railroad in reorganization—in this case the Penn Central. The object of this legislation is quite simple.

It has been estimated that over \$500 million is owed some 1,100 units of government by the Penn Central Corp. As a member of the Massachusetts delegation, I can testify that Penn Central owes the city of Boston some \$13.5 million and the Commonwealth of Massachusetts some \$24.2 million in back property taxes. The drain this places on the already financially beleaguered cities of the Northeast is incalculable. I believe there must be some sort of a legislative remedy for this critical situation, one that takes into account the dire straits of the American railroad network as well as the financial abyss that so many older, hard-pressed northeastern cities find themselves in. Such a remedy is best expressed in Ms. Oakar's H.R. 8882.

As chairman of the New England Congressional Caucus' Task Force on Transportation, I believe I can speak for the majority of the urban New England congressional delegation in stating that our local hospitals, school systems, and police and fire protection services desperately need the revenue due them but which is presently tied up due to Penn Central litigation.

When the Penn Central declared bankruptcy in 1970 the Federal district court in Philadelphia ordered the trustees of the Penn Central Corp. to make no tax payments until the courts further ordered it. Obviously this action presents serious constitutional ramifications for the States. Does the Federal Government have the authority to intervene in an area such as local tax abatement, which has traditionally been an area of local or State authority?

At present Penn Central is attempting to have local and State authorities settle their back tax claims for 50 percent of postbankruptcy taxes, or about 44 percent of all taxes owed. Massachusetts officials, as is the balance of State officials in New England, are not happy with this proposal.

H.R. 8882 addresses itself to an alternative proposal currently before Judge John Fullam of the U.S. district court in Philadelphia. This proposal would provide for an immediate cash payment of 20 percent and the remaining 80 percent of taxes to be paid through the issuance of Penn Central notes to the affected parties. The crux of this legislation is that the Federal Government would provide Federal guarantees for these series C and D notes.

The history of Federal involvement in this matter is extensive. In the first place it was the Federal Government that ordered Penn Cen-

tral to pay no taxes until the litigation was settled. Second, it was the Federal Government which ordered the birth of ConRail, supplanting all old rail lines, including Penn Central. We are trying here to offset a bad precedent that has already been set, which was to insert the Federal Government between the State and local governments and a private corporation with its financial obligations and to abrogate the authority of those State and local governments. The Federal Government's administrative expenses have the first lien against the bankrupt railroad. This effectively puts State and local taxes behind those moneys that were designed to keep Penn Central running. This situation should not be permitted to continue.

The decision on which repayment option to choose must be made by October 22 of this year. The choice obviously presents great difficulties to the taxing authorities. The question is: Should the States and local governing bodies accept the only 50-cent dollar, suffering a substantial loss and effectively removing any further chance for compensation, or should they choose to accept the Penn Central notes, which, as it stands now, would be akin to accepting Confederate currency in payment of any debt? Additionally, by accepting Penn Central notes, the States would suffer serious delay since the notes would not mature until 1987, which would be a full 17 years since the State and local governments would have been able to collect on what Penn Central has owed them since 1970.

Penn Central notes are at this time deemed good. Because of the recent massive problems incurred by the railroad the notes are difficult to market. It is precisely this inability to market the notes that would make it necessary to hold them to maturity. Backed by the full faith of the U.S. Government, the notes will be immediately marketable and our States, cities, and school districts will be able to realize the money owed them.

Finally, I am sure all of you are more than aware of the plight of many American cities, especially those in the Northeast. These older cities are all too often witness to the flight of industry and commerce to the South and the West. It is just these cities that are also most acutely affected by the Penn Central bankruptcy. The Federal Government must find a remedy for this situation. I strongly believe that H.R. 8882 is part of the prescription necessary to make our cities healthy again.

Once again, Mr. Chairman, thank you very much for the speedy hearing, and I thank my colleague for allowing me to go ahead of her.

Mr. ROONEY. Thank you, and I also thank you for the great leadership you have shown on behalf of the congressional delegation in the New England area. It has been very helpful to this committee and I appreciate very much your statement.

Ms. OAKAR. Mr. Walgren, of Pennsylvania, would like, with your permission, to give his testimony.

Mr. ROONEY. It is very kind of you to yield your valuable time.

The Chair recognizes our colleague who serves on the full committee and who has made a very substantial contribution in the area of health in our committee. Mr. Walgren, we welcome you and you may proceed.

**STATEMENT OF HON. DOUG WALGREN, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF PENNSYLVANIA**

Mr. WALGREN. Thank you, and thank you, Congresswoman Oakar. I just want to very informally add my voice to the purposes of this bill and to the mechanism that this bill sets out to address this problem.

When it was first explained to me by a lawyer in Pittsburgh, I thought that there was no way that anyone could defeat his claim for those taxes; but I apparently was operating under the old adage that there are only two things that are inevitable in this world, and those are, of course, death and taxes.

But that apparently did not take into account the Federal Government and its power to intervene itself in a way that very directly threatens to deny these local communities of the revenue that they had a right to expect.

The greatest difficulty is that the mirror image or inevitable result of that is that the property taxpayers in these communities are going to have death and double taxes. From my offering myself on the platter in town meetings, I come back with one clear message, and that is that anything that can be done to alleviate the residential property tax burdens of these taxpayers is imperative on every member of the Government to pursue. It is even more so when the result of Government action is to increase the burden of those property taxes which they didn't have a right to expect to have to pay in the first place.

So I really felt that, from the Pennsylvania side and the Pittsburgh side particularly, when this kind of an issue comes up, that much should be said.

I really appreciate the efforts of my various colleagues to enact this legislation and I would urge the committee to give it the most direct attention because it is at that edge where people are hurting most. I appreciate your time, sir.

Mr. ROONEY. Thank you, Congressman Walgren.

Ms. OAKAR. Mr. Chairman, with your permission, I yield to Congressman Regula, of Ohio.

**STATEMENT OF HON. RALPH S. REGULA, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF OHIO**

Mr. REGULA. Thank you, Mr. Chairman. I am sure you have heard all of the arguments. I think it is simply a matter of equity that these notes be guaranteed. This will enable the local subdivisions of government to use them as security or, in the event they should choose to do so, as an asset salable at a discount basis. The notes will ultimately provide the local governments with the taxes they anticipated, the taxes upon which they based their budgets.

Since the Federal Government has taken the responsibility through ConRail of operating these facilities, it seems to me that this is a logical responsibility also of the U.S. Government to secure these notes.

There is nearly \$500 million in taxes that State and local governments have not yet received. An important fact is that approximately 70 percent of these funds would go to our financially strapped school systems. In my district, the 16th Ohio District, \$2,880,000 is owed to local government.

A settlement proposal opening before the U.S. district court, Judge John A. Fullam presiding, provides for the immediate cash payment of 20 percent of owed taxes, the remaining 80 percent to be paid in the form of series C and D notes issued by Penn Central. This legislation provides for the Federal Government to guarantee these notes, making them more salable.

I need not elaborate on the esteem in which Penn Central financial paper is held. Few, if any, financial institutions would consider this viable collateral on which to extend credit to those entities declaring these notes as part of their asset base.

However, by providing a Federal guarantee, the much-needed credibility is given to these notes. H.R. 8882 insures that the series C and D notes of Penn Central are financially sound instruments.

I commend you, Mr. Chairman, for bringing this matter up for consideration so promptly. I urge the subcommittee's favorable action on this important matter.

Mr. ROONEY. Thank you very much, Congressman Regula.

Now we will hear from our very distinguished colleague Ms. Mary Rose Oakar.

**STATEMENT OF HON. MARY ROSE OAKAR, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO, ACCOMPANIED BY MICHAEL K. WAGER, LEGISLATIVE ASSISTANT**

Ms. OAKAR. Thank you and members of the committee. Mr. Chairman, I appreciate your efforts in scheduling these hearings on H.R. 8882. As you know, this bill was introduced on August 5, 1977. In these 7 short weeks, you have been gracious enough to review this legislation and schedule prompt hearings. I and the 60 cosponsors of H.R. 8882 appreciate your efforts. Moreover I want to thank you and the members of the Subcommittee on Transportation and Commerce for this opportunity to relate the facts of the Penn Central Transportation Co.'s tax delinquencies and the need for remedial legislation.

On June 21, 1970, the Penn Central Transportation Co. filed a petition for reorganization under section 77 of the Bankruptcy Act. This declaration of bankruptcy shook both the private and public sectors. In the private economic realm, creditors took stock of their outstanding extensions of credit to the Penn Central. Banks and other institutional lenders were owed hundreds of millions of dollars. The Federal Government, faced with the suspension of essential rail services, pursued a course of action that would keep Penn Central afloat until a comprehensive reorganization of rail operations could be fashioned. On January 8, 1971, the President signed into law the Emergency Rail Services Act—ERSA—of 1970, Public Law 91-663.

Recognizing the need for continued Penn Central operations as part of a national railroad freight service network, the Congress, through the Emergency Rail Services Act, authorized the Secretary of Transportation to guarantee certificates issued by the trustees of Penn Central in their effort to continue service. The act provided that the certificates would be issued upon ascertaining that the, "probable value of the assets of the railroad in the event of liquidation provides reasonable protection," to the Federal Government. Under ERSA,

the Federal Government provided the funds to meet payrolls and any other expenses which, "If not met, would preclude continued provision of essential transportation services by the railroad."

These extensions of funds by the Secretary to Penn Central were treated as "expenses of administration," and given the highest lien on the railroads property and priority in payment under the Bankruptcy Act. What this meant to the State and local taxing authorities could not be immediately ascertained. However, today, more than 7 years since Penn Central filed its petition, the implication is clear. The State, county, and local levels of government have been put upon. Fifteen States and the District of Columbia are now trying to collect over \$454 million in Penn Central taxes.

I would like to call your attention to appendix A, which has a breakdown of what is owed to these States and the district [see p. 17].

Mr. ROONEY. Without objection, appendix A will be included in the record.

Ms. OAKAR. Federal action has made these collections quite difficult. State and local officials have watched as the U.S. Congress set forth in the letter of the law a new set of rules governing the bankruptcy of a private corporation.

Prior to the Emergency Rail Services Act the tax obligations of the Penn Central Railroad would have had the highest priority of payment under the Bankruptcy Act. However, under Public Law 91-663 and its reaffirmation and amplification by the Regional Rail Reorganization Act of 1973, Public Law 93-236, the moneys extended by the Federal Government to the railroad for its day-to-day operations supplanted the tax obligations as preminent lien. In this arrangement there was no tradeoff and, frankly, no equity. The liens of the States and their political subdivisions, including their school systems, were simply put behind the Federal Government's claim against the Penn Central.

As the bankruptcy proceedings took shape in the U.S. district court, it was clear that the payment of State and local taxes would be one of great difficulties in carrying out a plan of reorganization agreeable to all classes of creditors. Early action by the court in the reorganization proceeding had permitted the Penn Central to defer payment of State and local taxes and enjoining the taxing authorities from taking any action to collect such taxes. At this point, I would like to submit appendix B for the record [see p. 17].

Mr. ROONEY. Without objection, it will appear in the record.

Ms. OAKAR. There were numerous efforts by the taxing authorities to modify or reverse this court order, court order No. 70. Finally, in 1972, the Supreme Court denied these appeals by the objecting taxing authorities.

Without the ability to collect current taxes, the State and local tax collectors could only stand by idly as Penn Central tax bills mounted. Meanwhile, the Penn Central trustees were devising a plan to compromise these tax obligations. On December 17, 1976, the trustees petitioned the court for the authority to affect such a compromise. On this date the trustees also filed a plan of reorganization.

On April 11, 1977, Judge John P. Fullam of the U.S. district court in Philadelphia issued court order No. 2922. And, without objection, I would like to submit appendix C, Mr. Chairman [see p. 18].

Mr. ROONEY. Without objection, it will be included in the record.

Ms. OAKAR. This order authorized the trustees to compromise the tax obligation of the Penn Central. The compromise, as put forth in the order, allowed for the settlement of outstanding tax claims by payment of 50 percent of the postbankruptcy taxes, or 44 percent of the principal amount of all taxes owed. The court also provided the trustees with the authority to establish a cash fund to carry out the compromise and settlement of the taxes pursuant to the order.

This compromise offer created a new set of problems for the local and State taxing authorities. Many of the taxing jurisdictions had State law that prevented the acceptance of anything less than full payment of taxes. Moreover, a large number of the approximately 2,500 taxing authorities to which Penn Central owed taxes were opposed to the compromise offer. The offer had no provision for settlement of interest that had accrued or penalties. These difficulties were compounded by the lack of information or misinformation that the State, county, and local officials were to base their decisions on. County auditors, treasurers, and school board officials were being asked to make decisions with respect to millions of dollars without proper counsel or a full understanding of the options available to them.

This is not to say that the options were all that good. One could accept the partial payment compromise or put the fate of this tax collection in the hands of those who had devised and were to amend the plan of reorganization. The amended plan of reorganization provided for the payment of State and local taxes through the issuance of securities. The secured notes are to be issued in four series, of which the series C and series D notes would be issued in respect to real estate and other local and State taxes.

Series C notes would be issued as compensation for 80 percent of the principal amount of taxes owed as well as any interest accrued on property that Penn Central had conveyed to the Consolidated Rail Corporation—ConRail—in the course of the reorganization. The notes would bear interest at the rate of 8 percent from the date of consummation of the plan and would become due and payable on December 31, 1987.

These series C notes would not become the general obligation of the reorganized Penn Central Co., but would be secured and payable from the proceeds of the valuation case—that is, litigation now pending that will determine the value of the properties conveyed to ConRail. The remaining 20 percent of the principal of taxes owed on conveyed property would be compensated by an immediate cash payment from the trustees.

The series D notes, like the series C issue, would be offered in lieu of 80 percent of the principal and interest accrued. However, as these notes are to be offered as compensation for taxes owed on property retained by the reorganized company, the notes would be secured by the general obligations of Pennco. The terms of these notes would be different from those terms of the series C issue. Ten percent of the principal would be compensated by interest-bearing 1-year series D notes, while a second and third 10 percent would be settled by the issuance of interest-bearing 2-year and 3-year series D notes. Fifty percent of the principal would be compensated by interest-bearing 10-year series D notes. Once again, 20 percent of the principal amount of

taxes owed would be received by the taxing authorities as an immediate cash payment.

The choice, then, has become a "one in the hand, two in the bush" proposition. One might ask: "Do I, as the State or local tax collector, accept a partial settlement of 44 to 50 percent or do I risk collection of these delinquent taxes by accepting long-term notes secured by a valuation case that I do not fully comprehend or based on the solvency of the reorganized company?"

It was not inevitable that this choice had to be so complicated and difficult. In fact, it was the passage of the Emergency Rail Services Act and the Regional Rail Organization Act that added these complexities to the choices that now face our local and State taxing officials.

As I stated before, the ERSA put Federal administrative expenses as the highest lien on Penn Central properties, thereby reducing the probability of full payment of State and local taxes. The situation worsened when the 3-R act reaffirmed the order of liens and then provided that claims for repayment of these administrative expenses were not subject to any reduction by way of setoff, crossclaim, or counterclaim. In short, the Federal Government gets paid first and then the State and local taxing authorities can make their claims.

Faced with this unsavory choice and recognizing the need for a Federal remedy, several county and local officials visited my Washington office on June 15, 1977. The meeting was also attended by representatives of the Justice Department and the Penn Central trustees. The local officials related their need for Federal action. After much research and additional discussion with State and local officials, it was obvious that two courses of action should be pursued:

First: The Secretary of Transportation should exercise his powers as set forth in section 211(h) of the Regional Rail Reorganization Act of 1973 to place local and State tax claims ahead of the Federal Government's administrative expenses. Accordingly, on June 16, I along with five other Members of the House of Representatives and Senators John Glenn and Howard M. Metzenbaum sent a letter to Secretary of Transportation Brock Adams asking him to use his administrative powers to restructure the order of liens against Penn Central. Secretary Adams responded on August 10, 1977, stating that Federal claims must be repaid before State claims. Secretary Adams cited the ERSA and the 3-R Act as reason for his determination.

The second course of action was the introduction of legislation that would guarantee the notes that Penn Central would offer as part of the amended plan of reorganization. I introduced this bill on August 5, 1977. Upon introduction I was joined by 12 of my colleagues. Today the legislation has 60 cosponsors, some of whom are members of this subcommittee. Moreover, it has received the enforcement of the U.S. Conference of Mayors, the National League of Cities, the American Federation of Teachers and a host of other concerned citizen organizations, who will testify before this subcommittee.

Simply put, the bill amends the Regional Rail Reorganization Act of 1973 to authorize the Secretary of Transportation to guarantee notes issued to the State and local taxing authorities to secure payment of tax obligations owed by the railroad in reorganization. However, this is not intended as or to be construed simply as a measure

whereby the Federal Government will pay the taxes accumulated by the Penn Central Transportation Company. In fact, it is unlikely that this bill will cost the Federal Government a single dollar.

Representatives of the principal litigants in the valuation case—that is, the Justice Department and the Penn Central trustees—believe that the proceeds of that case will be sufficient to cover the series C notes to be offered by Penn Central. Moreover, the reorganized company in doing quite well, and it is not unreasonable to expect Pennco to live up to the terms of the series D notes. In fact the reorganized company appears to be a healthy and diversified real estate concern with assets in excess of \$1.2 billion. In recent months Pennco has made a variety of investments, which further demonstrates its liquidity and viability. The reason for this guarantee is, then, not so much to pay off these notes at the end of the 10-year period; the guarantee has a more important function.

With a Federal guarantee of the series C and series D notes, the State and local officials are in a better position to sell these notes if they so desire. I am sure that it is no surprise to the members of this subcommittee that State governments and their political subdivisions are known to face financial difficulties whereby immediate cash is needed to continue essential services to their citizenry. For example, you might find that a certain county is faced with a cash flow problem and the county executive would elect to sell the Penn Central notes that he has been given as settlements of the tax delinquency. If the notes are guaranteed, the county could sell these notes in private markets without suffering substantial discount. However, without the guarantee, Penn Central paper would be difficult to sell. Private investors would be suspicious of the notes and it is quite likely that the sale of these notes would bring a sum that would be considerably less than face value. The hardship of this discount would be felt by the people of that county. More specifically, the financial squeeze would be most acutely felt by schoolchildren as a large proportion of the tax delinquencies are funds to be used for the delivery of educational services.

This bill is not the bail-out of a private corporation nor a handout to State and local taxing authorities. As the Penn Central is a bankrupt corporation, the Federal Government is not bailing out its stockholders or any of its beneficiaries. The guarantee extends no funds directly to the Penn Central. In addition, the Federal Government will not, under the provisions of this bill, pay Penn Central taxes while the assets of the bankrupt railroad are employed by the reorganized company. The guarantee will result in the extension of Federal funds if, and only if, there is a shortfall of funds to cover the series C and series D notes. The possibility of such a shortfall is slim.

As to whether this Federal guarantee would be a handout to State and local taxing authorities, I would submit that the record speaks for itself. The Federal Government has thrice taken action that put the local and State taxing authorities at a disadvantage in the collection of its taxes. The Emergency Rail Services Act, the Regional Rail Organization Act and court order No. 70 of the U.S. District Court have prevented the normal processes of tax collection from taking their course. The Federal Government has created a grossly inequitable situation with regard to the States, counties, and municipalities.

This guarantee merely gives these taxing authorities the equitable treatment, under law, that they deserve.

For those that are concerned that we may be setting an undesirable precedent with this legislation, I simply want to point out that H.R. 8882 is an attempt to offset bad precedents that have already been set. The bankruptcy of the Penn Central is a historic and monumental proceeding. The unfolding of this case has meant the setting of precedent at the executive, legislative, and judicial levels of government. There should be no reticence to set new precedent if it can remedy some of the difficulties that prevent an approval of the amended plan of reorganization. I believe that it would be grossly unfair to allow this situation to remain as it is. The need for this legislation is all too clear.

Mr. Chairman, the settlement of the Penn Central bankruptcy has been a long and arduous process, which is still to be consummated. At every turn there has been controversy, debate, and eventually a resolution of that point of debate. This legislation is intended as a resolution to the difficulties that beset the local and State taxing authorities. The settlement of these tax claims will greatly facilitate the entire bankruptcy proceeding. Moreover, H.R. 8882 deserves the favorable consideration of this subcommittee because of the implications that a compromise of Penn Central's taxes could have for the entire tax collection process.

Mr. Chairman, all across this Nation, at every level of government, there is the stirring of a taxpayers' revolt. Increasing taxes as well as the high levels of inflation and our recent economic recession have pushed many American taxpayers to the point of questioning the taxes that are levied upon them. Other taxpayers have flatly refused to pay their tax bills.

To allow Penn Central to make partial payment on its tax obligations would exacerbate this problem. The American taxpayer must be reassured that he as well as all corporate concerns will be compelled to pay all taxes that are levied.

Finally, this legislation is important for the impact it will have on the educational services being offered to our schoolchildren. Mr. Chairman, it has been estimated that 70 percent of the total Penn Central tax delinquency are moneys that will be used for the operations of schools. If schoolchildren are the ultimate beneficiaries of this bill, I would expect some very compelling arguments as good reason to delay this legislation. To date I have not heard such arguments.

Mr. Chairman, the speedy consideration of this bill will relieve much of the uncertainty that the beleaguered counties, cities, and towns are now experiencing. There are those in 15 States and the District of Columbia, in small towns like Taneytown, Md., and Moundsville, W. Va., who are waiting for some indication from this Congress as to the treatment of taxing authorities with regard to the Penn Central delinquencies. These local officials have waited too long. They are facing an October 19 deadline by which time they must accept the partial payment compromise or cast their fortunes with the amended plan of reorganization. They need quick action by the Congress.

I urge you, Mr. Chairman and the members of this subcommittee, to give H.R. 8882 speedy and favorable consideration. I believe that an early markup is imperative.

Mr. Chairman, thank you for this opportunity to testify today. I know this testimony was somewhat lengthy but I felt that it important to give an historical background of the dealings with Penn Central. I certainly would be happy to yield to questions.

[Appendixes A, B, and C to Ms. Oakar's prepared statement follow:]

#### APPENDIX A

##### ESTIMATED TAX CLAIMS AGAINST PENN CENTRAL RAILROAD

Penn Central Railroad owes property taxes of \$10,000 or more to some 1,100 units of government in the United States, including 16 states. We do not have a breakdown of the amount of money owed each unit of government. We do have the cumulative total by state, that is, we know how much money is owed to all governmental units in each particular state.

We do have a sample of what is owed some individual cities: New York City, \$100 million; Boston, \$13.5 million; Cleveland, \$14 million; Philadelphia, \$59.9 million<sup>1</sup>; Washington, D.C., \$1.6 million.

Here is the breakdown of money owed to governments within and including the particular 16 states:

	<i>In millions</i>
New York.....	\$143, 859
Ohio.....	79, 998
Indiana.....	49, 500
New Jersey.....	41, 019
Pennsylvania.....	<sup>1</sup> 32, 052
Illinois.....	28, 665
Michigan.....	27, 888
Massachusetts.....	24, 288
Maryland.....	11, 385
Rhode Island.....	8, 576
District of Columbia.....	1, 638
Delaware.....	1, 438
West Virginia.....	1, 435
Virginia.....	1, 085
Connecticut.....	868
Kentucky.....	273
<b>Total.....</b>	<b>453, 967</b>

<sup>1</sup> Figures are in dispute. City of Philadelphia contends Penn Central owes \$59.9 million, but figures released from bankruptcy court in Philadelphia show Pennsylvania and units of government within that state are owed a total of \$32 million.

Other units of government which the Penn Central owes include York, Erie and Harrisburg, Pennsylvania; Columbus, Toledo, Dayton and Cincinnati, Ohio; Buffalo, Rochester and Poughkeepsie, New York; Hoboken, New Jersey and New Haven, Connecticut.

#### APPENDIX B

##### ORDER NO. 70

And now, this 26th day of October, 1970, it is ordered:

1. Any taxing entity which claims (a) that the debtor's unpaid tax liability to such agency for the current year equals or exceeds 15% of the annual budget of such taxing entity for the current year; and (b) that under applicable law the budgeted revenue anticipated to be received from the debtor cannot lawfully be obtained from other sources; and (c) that deferral of payment of its said tax liability by the debtor could result in serious curtailment of essential services by such taxing entity, may present verified proof of these facts to the Trustees, not later than December 1, 1970. In all cases where such proof is presented, the

Trustees are authorized to pay the taxes then due, and shall, not later than December 17, 1970, file in this Court a report setting forth what disposition has been made or is proposed to be made with respect to the tax claims in this category.

2. Except as provided in the preceding paragraph, and except for payroll taxes and withholding taxes, the Trustees are directed to make no further payment of taxes until further order of the Court; provided, however, that the Trustees in their discretion, and subject to such further orders as the Court may from time to time enter, are authorized to pay such taxes as the Trustees shall determine, in the exercise of their business discretion, they should pay in the interests of ultimate reorganization.

3. All persons holding any interest in any property owned, leased, or otherwise used by the debtor, or the earnings therefrom, notwithstanding the provisions of any lease or other agreement, are hereby enjoined, until further order of this Court, from exercising any right of default, termination, seizure of the property, or ejection of the debtor therefrom.

4. All persons and governmental entities are hereby enjoined from taking any action of seizure, foreclosure, tax sale, or any other action which would disturb the Trustees' continued use, occupancy, and possession of the properties owned or used by the debtor, or which would deprive the Trustees of title thereto.

5. Nothing contained in this order shall be deemed applicable to the petitions heretofore filed as documents Nos. 212, 274, 275, 277, 292, 310, 311, 312, and 389, or to any of the properties mentioned in said petitions, which properties have been referred to in these proceedings as the Grand Central Area properties in the city of New York, as to all of which the jurisdiction of this Court is retained and an order will hereafter be entered.

#### APPENDIX C

IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In the matter of

PENN CENTRAL TRANSPORTATION Co., DEBTOR

In proceedings for the reorganization of a railroad

Bky. No. 70-347

ORDER NO. 2922

And now, this 22nd day of April, 1977, upon consideration of the "Petition of the Penn Central Trustees for Authority to Compromise and Pay Real Estate and Other Taxes Deferred Pursuant to Order No. 70" (Doc. No. 11767) (Tax Compromise Petition), the documents filed in support thereof, the Statements of Position filed by the various parties, the Petition of the City of Pittsburgh and other taxing authorities for modification of Order No. 70 (Docs. Nos. 10665, 10734, 10785, 10797) Pittsburgh Petitions) and hearing having been held, it is hereby ordered that:

1. The Penn Central Trustees ("Trustees") are authorized to compromise and settle outstanding tax claims against Penn Central Transportation Company ("Penn Central"), the Secondary Debtors and the non-bankrupt leased lines by payment of 50% of the principal amount of post-petition taxes, or such amount of post-petition taxes as would cause the payment in each case to equal 44% of the principal amount of all tax claims, whichever is greater.

2. The Trustees are authorized to create a cash fund for the compromise and settlement of taxes pursuant to this Order (Tax Settlement Fund) from the following sources:

(a) Monies set aside in respect of defaulted trustees certificates pursuant to Order No. 2158.

(b) Escrow deposits relating to taxes owed by tenants of the estate.

(c) Proceeds of the sale of equipment deposited under Order No. 366.

(d) Funds of Manor Real Estate Co., including monies set aside pursuant to Order No. 1889.

(e) Penn Central Securities Litigation Settlement Fund set aside pursuant to Order No. 2050.

(f) Unrestricted funds of Penn Central Transportation Co. and various subsidiaries.

3. The Trustees' request for authority to draw upon the restricted and unrestricted funds of the respective leased lines for the creation of a Tax Settlement Fund, but only to the extent of 25% of the amount of post-reorganization taxes, exclusive of interest and penalties, due in respect of such leased lines, is denied, without prejudice to renewal of such request in the event money in excess of that made available under Paragraph 2 of this Order is necessary.

4. The Trustees shall keep an accounting of all restricted and unrestricted funds of the Penn Central which are used for the creation of the Tax Settlement Fund and of the amount of all outstanding tax claims settled pursuant to this Order, and shall make such accounting available to any interested party for inspection upon reasonable request.

5. In the event that a Plan of Reorganization for the Penn Central and the Secondary Debtors is not approved by this Court and consummated pursuant to the Bankruptcy Act by June 30, 1979, the Trustees shall begin to reimburse the segregated and escrowed accounts of the Debtor which had been used in the creation of the Tax Settlement Fund with the future cash flow of Manor Real Estate Co.

6. Any tax claimant wishing to compromise and settle its outstanding tax claims against the Debtor or leased lines shall so advise the Trustees, in care of Ernest R. Varalli, Controller, Suite 3200, IVB Building, 1700 Market Street, Philadelphia, Pa. 19103, in writing within 180 days of the date of this Order. The Trustees shall serve upon each tax claimant a form or forms upon which the tax claims may advise the Trustees (1) of the amount of tax claims claimed to be due, and (2) that the compromise and settlement of such claims on terms specified in Paragraph 1 of this Order will be accepted as a full and complete satisfaction of all such claims against the Debtor and the leased lines.

7. The compromise and settlement of outstanding tax claims by and between the Trustees and any tax claimant pursuant to this Order shall constitute a full and complete settlement and satisfaction of all such tax claims against the Debtor and the leased lines, including all claims for interest and penalties, in respect of any period through and including December 31, 1976.

8. No claim against the Debtor or a leased line which is not compromised or settled pursuant to this Order shall be affected hereby, as to amount, priority or otherwise, pending the treatment of such claim in a Plan of Reorganization for the Debtor and the Secondary Debtors approved by this Court and consummated pursuant to the Bankruptcy Act.

9. The Pittsburgh Petitions for a modification of Order No. 70 are denied, without prejudice.

10. The Petition of the Penn Central Trustees and the Trustees of The Delaware Railroad Company and the Philadelphia, Baltimore and Washington Railroad Company for Authority to Compromise and To Pay Certain Taxes Owed to the City of Wilmington, Delaware (Doc. No. 10810) is granted.

11. Except as provided in this Order, the provisions of Order No. 70 shall remain in effect.

JOHN P. FULLAM.

Mr. ROONEY. Thank you very much. Let me say that your testimony certainly did give an accurate background of the problem and I commend you for submitting this very fine testimony to the committee today.

On page 9 of your statement you say that it is unlikely that this bill will cost the Federal Government a single dollar. In your letter of August 4, however, you state that securities being offered to secure the 80 percent of delinquent taxes appear to be of highly speculative value.

If these securities are highly speculative, Ms. Oakar, would it not be a fair assumption that the Federal Government would be required to make substantial compensation if this proposed legislation is passed?

Ms. OKAR. Mr. Chairman, I have tried to characterize those thoughts in two different ways because I was referring to them in two different contexts. When I said that the notes appear to be of highly

speculative value, I was discussing the marketability and the anticipated reaction of investors in private markets to notes written on Penn Central paper.

The fact of the matter is that the investment community will look suspiciously at Penn Central paper at this point in time. However, I have been told that the assets conveyed to ConRail are likely to be valued at such a level to cover all Federal, State, and local obligations of the railroad.

My statement is related to the perceptions of the notes by private investors vis-a-vis the assessment of the evaluation by the representatives of the principal litigants—the Justice Department and the trustees.

Mr. FLORIO. I am in support of the legislation obviously and I think it is good. I think you made abundantly clear that the American taxpayer is going to pay the price, one way or the other. It is a "Catch 22" situation.

If, in fact, the original valuation was correct, it seems to me that there is not going to be enough money to pay these notes and therefore the guarantees will come into play. On the other hand, if the original valuation being contested by the trustee is incorrect, that means more money is going to come forth; and the only way it comes forth is from the U.S. Treasury and, at that point, there may be enough to secure these notes.

So I think, in all candor, we have to realize the fact that the U.S. Treasury one way or the other is going to end up bailing out the municipalities. I happen to believe it is equitable and it should be done but I think it has to be clearly appreciated that that is what is going on. Thank you, Mr. Chairman.

Mr. ROONEY. Ms. Mikulski.

Ms. MIKULSKI. As it stands now, local taxing authorities have to tell Penn Central whether they want to take 40 percent of the taxes owed by October 19. If, for some reason, because of a crowded legislative calendar, we can't act on this before October 19, what are the implications?

Ms. OAKER. Of course, this is why we are so respectfully delighted to have this hearing to begin with and we are hoping and praying for early markup.

I look at the energy bill as an example of the ability of this Congress to act quickly. If my memory serves me correctly we were able to deal with that piece of legislation in, I believe, a 60-day time period; so I don't think it is impossible to have H.R. 8882 passed in short time.

The other thing is that we are in a position to ask for an extension of the deadline of the court.

Ms. MIKULSKI. Who would extend that deadline?

Ms. OAKER. It would be Judge John P. Fullam.

Mr. ROONEY. I understand that the States and municipalities will ask the courts for a 90-day extension and, in all likelihood the courts, I understand, may extend that date.

Mr. FLORIO. On this point it is also my understanding that some of the entities, the counties, are also challenging it and, in fact, there are two options, in substance, in the decisions being challenged. Do you have an information as to whether that is taking place?

Ms. OAKAR. If my colleague will allow me to defer your question, there are some other people who will be testifying before this committee who were present at the court proceeding which I was unable to attend. We do have someone who is going to comment on that issue specifically.

Ms. MIKULSKI. I am not clear about what we are talking about on page 5 regarding what would currently back up the C and D notes. Pennco backs up D, is that right?

Mr. ROONEY. Would you like to yield to your assistant?

Ms. MIKULSKI. As I understand the option, a local government could take a partial 45-percent payment or could defer and take 20 percent in cash and then either take the C or D series. Is that the way it goes?

Ms. OAKAR. No; I am going to yield to my counsel. This is Michael Wager, who is the legislative assistant who has been working on this legislation.

Mr. WAGER. The option to the State and local taxing authorities is this: You can expect the 50 percent or the 44-percent compromise payment and then you are through with regard to tax delinquency, or you can accept under the amended plan when approved by the court 20 percent in cash and accept the remaining 80 percent of the principal and interest and penalties in series C or series D notes.

Now, the series C notes will compensate those taxes that were on conveyed assets—the assets that come from Penn Central and went to ConRail. Series D notes will be issued to those taxing authorities that taxed assets retained by the reorganized corporation, Penneo.

Ms. OAKAR. If I might add, Congresswoman, that as to the assets of the newly organized corporation, Penneo, it is doing very well.

Mr. FLORIO. If I could ask, are you saying that taxes incurred prior to reorganization will be secured by C notes which are the assets of the Penn Central Transportation Co., which is the reorganized company, and that taxes incurred after the reorganization—

Mr. WAGER. No; taxes incurred before and after will be secured by series C and series D notes. Now, the overwhelming majority of these taxes levied were on assets conveyed by Penn Central to ConRail in the reorganization of the railroad. However, there is a portion of those taxes which was levied on assets retained by the reorganized corporation as real estate holdings.

New York State, for example, has a large portion of taxes levied on retained assets, and the notes they will receive will be series D notes which will be based on the solvency of the reorganized corporation and its ability to pay.

The schedule we set forth shows 10 percent at the end of 1 year, 10 percent at the end of the second year and another 10 percent at the end of the third year and the remaining 50 percent in December of 1987.

Mr. FLORIO. If I could amplify on my understanding of what is being stated now, is it, for the most part, the railroad properties in the reorganization that have been conveyed to ConRail and will be secured by the C notes? That is the subject matter of the legislation. The trustees are saying the amount assigned is not sufficient, the suggestion being that you probably couldn't pay off the C notes if everyone

took C notes with the insufficient amount of moneys that have been assigned.

It is my understanding that the D obligations are just for taxes that are on properties not conveyed to ConRail and probably are not railroad properties. Is that the case?

Ms. OAKAR. We can tell you what some of these properties or assets are of Peunco if you would be interested and I will submit this for the record. Their earnings from their continuing options include energy, the Buckeye Pipe Line, amusements, Great Southwestern Corp., real estate, and other corporations; their earnings were \$38.7 million in 1976 and are forecast to exceed \$40 million this year.

Mr. FLORIO. Isn't it correct that those properties have been paying their taxes? There aren't going to be any obligations on the assets that are owned by Buckeye Pipe Line, are there?

Mr. WAGER. The retained assets that the local taxing authorities were enjoined against collecting taxes on since October 22, 1970, when order No. 70 came out of the court—

Mr. FLORIO. Could we have a breakdown as to the amount of taxes that are owed on D-type assets as opposed to the C-type?

Ms. OAKAR. The trustees have a library, and I don't have that information before me but we can provide it for you.

Mr. FLORIO. My impression was that there is not going to be very much owed on the better type of security, which is the D-type assets, and the vast majority would be on that category. It is 50 percent more. You are talking about \$300 million versus \$150 million. Thank you very much.

Ms. MIKULSKI. Congresswoman Oakar, as a fellow former city councilwoman, without your legislation do you think your city council—and I know how my city council would feel about this—do you think that they would accept the 20 percent that goes to C and D bonds?

Ms. OAKAR. No, we know the realities of the way municipalities work and they would be foolish to do that. I respect some of my former colleagues and I am sure you do and I doubt very strongly that they would accept it without some kind of guarantee. That would build up false hopes for them. So that there is no question that they would not do that.

Ms. MIKULSKI. Thank you. I think this is a very creative way to get funds back into the local communities. I am happy to be associated with it.

Mr. ROONEY. We will stand in recess for 15 minutes. There is a vote on the floor.

[Brief recess.]

Mr. ROONEY. The subcommittee will come to order. The Chair now recognizes the very distinguished gentleman from Illinois, Mr. Madigan.

Mr. MADIGAN. Representative Oakar, as I understand the justification behind this bill, you and your cosponsors are saying that, if the Federal Government had not intervened, the Penn Central would have gone bankrupt in 1969 or 1970. The property tax claims would have been claims against or a part of the bankruptcy proceeding and you would have received your money, and the intervention of the Federal

Government prohibited you from doing that. Is that essentially the basis for this bill being brought forward now?

Ms. OAKAR. To an extent that is true, but I think it is also fair to say that the precedent was set by Federal intervention which may or may not have been the proper thing to do, and that is our response—to set another precedent by doing that.

But we realize the immediacy of the problem was obvious, that our country simply needed rail service; and so, while we recognized why there was Federal intervention and why, in fact, the President then had, a year later, signed the Railroad Act, at the same time we feel that the act could have been more equitable in essentially who would stand in line first to collect the debts owing.

Mr. MADIGAN. But that intervention was largely at the request of State and local government officials, and the Federal Government now at this point has invested nearly some \$4½ billion in this, and the total outstanding real estate taxes are something like \$450 million.

So a person could say that the Federal Government has an investment of \$4½ billion, State and local governments an investment of some \$450 million, or \$1 on \$10 by comparison, in something that the State and local government officials were arguing should be done. How do you respond to that?

Ms. OAKAR. Let me just say that in no way does this bill change the role of the Federal Government in collecting the assets that are owing and due them. Certainly for one thing, no one could predict after a 7-year period what the outcome would be of all of our economy and how it would affect the local and State taxing authorities.

I am not necessarily specifically aware of how intimately the State and local authorities were in requesting the original legislation, not having been a member. That has not been called to my attention.

I think, Congressman, your question—and I am not trying to avoid the question—I think that since we are going to have State and local officials represented here, that might be addressed to them since they are naturally supporting this legislation currently.

Mr. MADIGAN. Some States and some local governments have already accepted the proposal of the Penn Central trustees. Others, of course, Ohio included, and Illinois, my State, have not. How would you treat those who have already accepted less than what you now ask for Ohio?

Ms. OAKAR. Of course, we know that, in some cases unsolicited, Penn Central mailed the checks before any agreement came through, which was a kind of curious thing to do, and some of the municipalities raised the issue in court and, unfortunately for them, the judge did not concur.

If they feel that there is a new opportunity for them to collect, in effect, all of what is owing them, they could certainly take that issue up with the courts. It will not change their status and they have nothing to lose by this legislation if they have accepted the legislation.

Mr. MADIGAN. Do you have any idea what the market value is of properties that the Penn Central still owns in the State of Ohio?

Ms. OAKAR. Currently? I don't have it but, Congressman, I would be delighted to get that. I wouldn't want to give you misinformation; and I know that we came across that, and I would be happy to supply that.

Mr. MADIGAN. Your bill has no provision for recourse from the reorganized company for any payments made by the Federal Government in satisfaction of the guarantees. Do you believe that such a provision should be included in the bill?

Ms. OAKAR. The inclusion of such a recourse provision is a difficult issue. Such a measure would, of course, as we know, or we feel, would be opposed by the trustees. This in turn would obstruct the efforts of those who want to see the amended plan of reorganization approved and implemented; and, for this reason, I would advise against the recourse provision.

Mr. MADIGAN. Isn't that rather unfair to the Federal Government.

Ms. OAKAR. AS I have stated before, the Federal Government initiated the reorganization and it is not unreasonable to expect the Federal Government to assume the financial risks of the reorganization. However, again I want to say, or repeat, my feeling that, based upon the research we have done, with regard to series C and D notes the risk is slim.

Mr. MADIGAN. Let me just remind you that the Federal Government has already assumed some \$4½ billion in costs associated with this reorganization. These total outstanding property taxes—and State income taxes in some instances—and other local taxes amount to only about 10 percent of what the Federal Government has already assumed costwise in this reorganization.

On page 7 you say it does not appear to be particularly proper for the Federal Government to insert a claim of a higher priority than the State and local taxing authorities. Aside from the normal law and procedure in such cases, don't you believe that this should be considered fair since the Federal Government invested its money after it was known that the company was bankrupt?

Ms. OAKAR. As you know, Congressman, the payment of tax obligations is regarded as the first lien in the bankruptcy proceeding, and I see no reason why the Penn Central proceeding has not honored this arrangement. This is, of course, a historic and monumental thing and, in some cases, a kind of exceptional bankruptcy. It is neither typical nor simple.

Nonetheless, the placement of State and local tax obligations on a second priority lien is not justified, and the Congress took it upon itself to reorganize the railroad, and the Penn Central Railroad was part of a nationally integrated economic system; and it was in the national interest to reorganize rail services, and it should be the Federal Government, then, that bears certain responsibilities or not a selected group of cities, States, and towns which are in critical need.

If I might just say something in respect to my own State—and I don't think we are exceptional; I am told that other major areas and other cities such as New York and Boston and other areas, in New Jersey and so forth, have the same problem—our schools, we have been told by the Ohio superintendent of schools, are on the brink of bankruptcy. I am told that Toledo and Cleveland are going to request some immediate legislation from the State legislature which would relieve some of the problems.

Furthermore, when you talk about the fact that the Federal Government spent \$4 billion, what about the local governments? They have

had to assume the burden, and they should not have to support the railroad at the expense of the residents and the schoolchildren.

Mr. MADIGAN. What do you think would have happened if the Federal Government hadn't intervened? What do you think would have happened in Ohio?

Mr. OAKAR. I am not sure, to be truthful, if it relates to this. I don't question the fact that there was obviously a critical situation when, according to the New York Times, the Penn Central has a taste for superlatives. They say it was one of the Nation's biggest corporate bankruptcies, and they obviously made certain decisions in this respect in order to go on the brink. It was, indeed, a very dramatic occurrence.

The Federal Government came to the rescue; what we are saying is that laws are meant to be changed, and we merely want to have a simple amendment that would provide equity for all parties. I don't question the intervention; we are just correcting something that was not necessarily equitable in the original legislation.

Mr. MADIGAN. It is not the only bankruptcy proceeding involving the railroads. The Erie Lackawanna, Reading, and Lehigh railroads owe some \$80 million in outstanding real estate taxes, and they are also involved in a bankruptcy proceeding. We have the ability here to establish a precedent that certainly would have a bearing on that \$80 million.

Mr. Chairman, I have two statements; one from Mr. Devine, the ranking member of our committee, who could not stay here, and the other from the attorney general of the State of Illinois; and I have been asked if I would request permission for each of these statements to be inserted in the record, if there is no objection.

Mr. ROONEY. Without objection, that will be done.

Mr. FLORIO. Reference was made to the Bankruptcy Act and the fact that the States and localities have a lower preference in terms of their positions. Do you know of anyone else who has given thought to amending the bankruptcy law to put them in the same category as administrative costs?

Ms. OAKAR. It is not the Bankruptcy Act.

Mr. FLORIO. It is the Railroad Bankruptcy Act?

Ms. OAKAR. No. At this time, we don't want to see the Federal Government not collecting what is owing to it. And it is not a question of competition; it is a question of treating everyone equitably.

Mr. FLORIO. By saying that, you are implying you don't believe the assets are going to be enough to take care of the Federal Government's claims as well as the State and local governments' claims?

Ms. OAKAR. I would not say that.

Mr. FLORIO. If you don't say that, it seems to me that if we include all legitimate administration fees, then you wouldn't have any argument or there won't be any argument that somehow the tax claims of the States and localities are going to be secondary.

What I am suggesting, I think: It would make a good argument that these were costs incurred through the course of the administrative period and therefore they should be on the same footing with Federal claims.

Ms. OAKAR. You know, Congressman, we did ask the Secretary of Transportation to take care of that.

Mr. FLORIO. He may not feel that it is within his discretion or his discretion may not be desirable or perhaps he doesn't have the power to do so. I am just inquiring as to whether any thought has been given to doing this legislatively. With one full swoop we could resolve the problem, and the money may not be there but, in terms of the actual procedura problem as to how to go forth to classify these debts as administrative expenses, presuming the monies were available to handle the added administrative expenses, if I am reading things correctly that would take care of the problem. Thank you, Mr. Rooney.

Mr. ROONEY. I have no further questions. Thank you very much. Your testimony was excellent and your responses to the questions were very accurate and very candid and we appreciate very much your appearance here. You have made a very significant contribution to the committee with respect to such statement.

The Chair now recognizes our very distinguished member from the great State of New York.

**STATEMENT OF HON. BENJAMIN A. GILMAN, A REPRESENTATIVE  
IN CONGRESS FROM THE STATE OF NEW YORK**

Mr. GILMAN. Mr. Chairman, I am grateful for this opportunity to appear before the Subcommittee on Transportation and Commerce in support of H.R. 8882, a bill to guarantee notes issued to secure the real property obligations owed by Penn Central and other railroads.

I realize that the committee has already heard extensive testimony and, with your permission, I will summarize my testimony.

Mr. ROONEY. That my be done.

Mr. GILMAN. I have cosponsored and supported this legislation introduced by my distinguished colleague from Ohio, Ms. Oakar, because of the firm commitment in this bill to provide our financially hard-pressed local, county, and State governments optimum security for tax relief for the real property obligations owed by Penn Central and other railroads.

In sum, this bill amends the Regional Rail Reorganization Act of 1973 by providing Federal guarantees for notes that the Penn Central Transportation Corp. proposes to offer to our local and State taxing districts in lieu of delinquent taxes owed by the bankrupt railroad and its lease lines.

The long and complicated litigation surrounding the Penn Central bankruptcy has ensnared local, county, and State governments in a perplexing fiscal dilemma not of their own making. I speak of the approximately \$500 million in delinquent taxes that these tax districts are attempting to secure from Penn Central. In my own 26th Congressional District in the State of New York, at least 17 taxing authorities report that Penn Central owes them collectively over \$1.7 million in unpaid taxes. For these financially hard-pressed towns and counties, struggling to maintain adequate municipal services, while at the same time attempting to stem the current upward spiral of local tax rates, Penn Central's tax debts continue to exacerbate the fiscal plight they are experiencing.

The legal imbroglio in which the current claim to Penn Central back taxes is rooted stems to a large degree from the Penn Central bankruptcy in June 1970 and the subsequent issuance of order No. 70 by

the reorganization court on October 26, 1970. That order permitted Penn Central to defer payment of State and local taxes and enjoined State and local taxing authorities from taking any actions to collect these back taxes.

From the date of entry of order No. 70 to the end of 1976, numerous State and local taxing authorities were engaged in extensive litigation attempts to reverse or modify order No. 70, and failed.

In an effort to stem further suits contesting order No. 70, the trustees of the Penn Central Transportation Co. entered a petition seeking authority to compromise payment of unpaid taxes. Over the objection of more than 25 taxing authorities—including the city of New York, the Cleveland Board of Education, the city of Philadelphia, and the State of Maryland—the compromise was approved by the reorganization court on April 22, 1977, as order No. 2922. Order No. 2922 is currently being appealed.

The key provisions of order No. 2922 translate into the following: (1) On all tax claims for which the principal amount equals \$10,000 or less, Penn Central trustees are directed to pay 100 cents on the dollar; and (2) payment of 50 percent of the postbankruptcy principal amount or 44 percent of both post- and pre-bankruptcy claims, whichever is the larger amount, on all tax claims above \$10,000.

Widespread dissatisfaction exists over this proposal. Indeed, a national coalition has been formed of local, county, and State officials who are fighting this compromise in the U.S. district court in Philadelphia. This coalition has lobbied extensively in support of H.R. 8882, and I might add that Ms. Oaker's legislation has also received the endorsement of the U.S. Conference of Mayors and the American Federation of Teachers, who, I believe, will be testifying later this afternoon.

H.R. 8882 is the legislative complement to a settlement proposal now before Judge John A. Fullam of the U.S. district court in Philadelphia. This proposal would provide for an immediate 20-percent cash payment and would allow the remaining 80 percent to be paid through the issuance of Penn Central notes. H.R. 8882 would provide Federal guarantees for these series C and series D notes.

What would passage of H.R. 8882 mean to those local, county, and State governments whose fiscal troubles have been compounded by Penn Central's delinquent taxes? As I indicated earlier, Penn Central owes taxing districts in New York's 26th Congressional District back taxes approximating \$1.7 million. H.R. 8882 would provide these municipalities an optimal opportunity for securing full payment of these back taxes. Without this legislation, the majority of these taxing districts would be forced to settle for approximately half this amount—and in some cases less—under the terms of the Penn Central compromise.

I believe passage of H.R. 8882 to be a just and equitable solution to the matter of Penn Central's delinquent taxes. To further buttress this contention, I refer to the case of the village of Maybrook in my home congressional district.

The village of Maybrook is owed \$65,289.67 back taxes by the Penn Central Transportation Co. If the village of Maybrook is forced to accept the Penn Central's offer in compromise, Maybrook stands to receive only 44 percent of the above-mentioned amount, or \$28,727.45.

However, if Congress passes legislation such as H.R. 8882, providing for Federal guarantees, the village of Maybrook could elect to take 20 percent cash offered by Penn Central together with promissory notes for the balance of \$65,289.67 and then negotiate these notes in the market which would be created by virtue of the Federal guarantee.

Moreover the plight of the village of Maybrook is particularly difficult when one realizes that, as a result of the bankruptcy of the New Haven Railroad, the village of Maybrook lost approximately \$120,000 in unpaid taxes. The paper issued to the village of Maybrook as a result of the New Haven bankruptcy was completely worthless.

In considering the merits of H.R. 8882, there emerge two highly salient questions to which we must address ourselves: (1) Why should the Federal Government intervene in this case, guaranteeing the large-scale tax debts of a private corporation and (2) what is the likelihood that this Federal guarantee will—if we were to assume that these delinquent taxes were not paid—eventuate into a huge financial burden to be borne by the Federal Government?

In responding to the first question, I would point out that the case for Federal intervention can be tied in no small way to the Federal Government's culpability for the existence of those delinquent taxes as a result of Washington's initiative in reorganizing the railroads. The Regional Rail Reorganization Act of 1973 created ConRail, the federally related corporation which has supplanted the old rail lines. Those railroads included in the Reorganization Act were required to continue operations until conveyance could be effected. Moreover, claims for repayment of Federal grants and loans—211(h) loans enabling railroads to continue operations—were established as not subject to any reduction and superseded all other administrative claims, including State and local taxes, on the estate of the railroad in reorganization.

This arrangement, even allowing for good intentions, has created the anomalous situation of State and local taxing districts' subsidizing, in effect, the reorganization of those railroads that had failed. This onerous burden has only intensified the already precarious fiscal situation of State and local governments seeking to maintain vital services and high quality school systems.

Correspondence I have received from David Gubits, the attorney representing the village of Maybrook, illuminates not only the need for a Federal guarantee but also the glaring inequity that will continue if such a guarantee is not forthcoming. As Mr. Gubits asseverates:

We believe that the loss of the approximately \$120,000 in unpaid taxes as a result of the New Haven Bankruptcy is more than sufficient subsidy of the Nation's railroads by the village of Maybrook. It would only be fair at this time for the Federal Government to guarantee the Penn Central notes so that the village of Maybrook can be assured of nearly complete payment of its tax claims.

I know that I need not remind you of the devastating effect on the village of Maybrook of the Poughkeepsie Bridge fire. Maybrook has borne much more than its fair share of carrying our Nation's railroads. It is time for the Federal Government to give some minimal aid to the village of Maybrook in the form of guarantees for the Penn Central notes.

And, by way of notation, the village of Maybrook did have a marshalling yard that was closed down completely as a result of the

Poughkeepsie Bridge fire, a bridge that has not been repaired by ConRail, despite some prior promises.

Mr. ROONEY. Have there been any other private corporations in the village of Maybrook or in your district that might have gone bankrupt during the last 5 or 10 years?

Mr. GILMAN. Yes; several others. The Erie Lackawanna Railroad, the New Haven Railroad, and Hudson Railroad, which is involved in rail reorganization and which was dried up primarily because of the Poughkeepsie Bridge problem.

Mr. ROONEY. How about W. T. Grant?

Mr. GILMAN. And the Grant Co. has also gone bankrupt.

Mr. ROONEY. Do you think the Federal Government should guarantee their taxes also?

Mr. GILMAN. No; but the Federal Government didn't intervene to place W. T. Grant in a position where it had to withhold action or withhold their business reorganization as a result of Federal Government involvement.

I would think that that gives some basis for the Federal Government involvement in such a guarantee since the Government did intervene and take on the ownership of the railroad and placed the local municipalities in a position of taking a secondary position.

Mr. ROONEY. But the New Haven went bankrupt and you have lost \$120,000, and now the Penn Central is even giving you the option of taking 50 percent.

Mr. GILMAN. Less than 50; I guess about 40 percent at this point.

Mr. ROONEY. But they are giving you that option and they are not forcing you.

Mr. GILMAN. Of course, it places the municipalities in a very difficult position to have to make a decision to accept something less than 100 cents on the dollar and come back to the electorate and state that that is the very best that they could do at this time.

Mr. FLORIO. Does New York State have a law such as New Jersey has that you cannot compromise tax claims? Do you have authority in this municipality to accept the 50 percent?

Mr. GILMAN. I am not certain, Mr. Florio.

Mr. FLORIO. It highlights another problem: that in my own State—and, I suspect, in other States—we don't have the authority to do that without State legislation. Now, it may well be that the State legislation is not forthcoming and municipalities will be faced with a choice that they cannot accept and they cannot accept either of the two options, in which case the only two options available could not be accomplished legally, and it seems to me that unless something is done they will get nothing and they will have no recourse.

Mr. GILMAN. I think the gentleman raises a very good point, and I am frank to say I don't know the answer but I will try to provide the committee with a response to that inquiry so that you will have the benefit of the status of New York legislation.

Mr. FLORIO. Thank you.

Mr. GILMAN. We come now to the question concerning the possibility that such a Federal guarantee of Penn Central's notes would become actual obligations the Federal Government would be forced to assume. Extensive research conducted by Ms. Oaker reveals that the possibility

that a guarantee would cost the Federal Government any money is quite small. Indeed indications are that, as the reorganization plan is concluded and Penn Central properties are valued, the delinquent taxes in question will be paid in full. The guarantee would be activated in the instance of a shortfall. Again, however, all key signs indicate that the possibility of a shortfall is slim.

The United States Railway Association—USRA—which is representing the Federal Government in the complex rail reorganization and litigation, has submitted that this litigation has made great strides. While the road ahead is long and the end not yet in sight, the USRA nevertheless expects progress at a good pace. Indeed, the trustees for Penn Central also indicate that there will be a successful reorganization.

In closing, I wish to point out that the guarantee provisions embodied in H.R. 8882 are both warranted and fiscally prudent. Our State and local taxing authorities should not be subject to the current, inordinately adverse effects surfacing, in part as a result of the Rail Reorganization Act, a product of congressional design.

A Federal guarantee would provide these Penn Central notes the credibility they would need in an investment market place. It is only through such a guarantee that State and municipal governments can be accorded an equitable adjustment to the fiscal injustice to which they have been subjected.

I want to thank the Subcommittee on Transportation and Commerce for examining this issue and for the opportunity to appear before you today, and I hope that you will act favorably on this measure.

Mr. ROONEY. Thank you very much for your very fine testimony.

Mr. FLORIO. I think it was very useful to get the case study approach that Mr. Gilman provided to us to see the impact upon a relatively small municipality.

Mr. GILMAN. I thank the gentleman.

Mr. ROONEY. Thank you very much.

Without objection, the Chair wishes to place in the record, as though read, the statements of Congressmen Edward P. Boland of Massachusetts, Samuel L. Devine of Ohio, Silvio O. Conte of Massachusetts, Donald J. Mitchell of New York, Stanley N. Lundine of New York, and Douglas Applegate of Ohio.

[The statements referred to follow:]

#### **STATEMENT OF HON. EDWARD P. BOLAND, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS**

Mr. BOLAND. Mr. Chairman, I appreciate the opportunity to express my support for the legislation introduced by my colleague, Congresswoman Oakar.

I am concerned that the States, cities, counties, and towns of our Nation—especially those in the Midwest and Northeast, are being made to bear an unfair financial burden as a result of the federally mandated reorganization of the railroads. At the time of its bankruptcy in 1970, the Penn Central Transportation Co. owned a substantial tax debt to a great number of State and local taxing districts.

The Federal district court which is hearing the bankruptcy case forbids Penn Central from paying any of the tax claims until that court ordered payment. In the ensuing 7 years, the interest on the tax debt has caused the total debt to swell to \$500 million. In the State of Massachusetts alone, the amount due is \$24.2 million. This money is desperately needed to finance the operation of schools and local government in the communities to which the debt is owed. The question, Mr. Chairman, is how these communities collect what is due.

Two alternatives are being offered by the Penn Central. The communities can accept 50 cents on the dollar as full payment for what they are owed or they can accept 20 percent of the debt in cash and the remaining 80 percent in the form of interest-bearing notes. As the existence of the debt is uncontested, it does not appear just that the communities should have to settle for only half of what they are entitled to receive. The second alternative is clearly preferable but it contains a significant drawback, since the notes do not mature until 1987. While it appears that the notes are good, the bad reputation of the Penn Central in the business community is a major impediment to their marketability. If the local taxing districts are forced to wait until the notes mature for full payment, they will have spent at least 17 years trying to prepare budgets with the knowledge that they were entitled to more funds, but that those funds were unobtainable. Mr. Chairman, those districts should not be made to sacrifice any longer.

Since the Federal Government has played a role in the continuation of this delay, it seems appropriate that it play a role in the termination of the delay. Congresswoman Oaker's bill would accomplish this objective by requiring the Federal Government to guarantee the notes, thus insuring that the taxing districts could market them quickly and receive full value in return. This measure would not place the Federal Government in the position of assuming the Penn Central tax debt because the notes are secured by Penn Central assets. It would merely require that those assets be used to pay off some of the company's bills.

I submit, Mr. Chairman, that the economic stimulus which this legislation will produce, in areas of our Nation in which such a stimulus is sorely needed, mandates our support of it. The time for legislative action is short, however, as the local taxing districts must choose between the available options by October 22, 1977. Since Senator Weicker has introduced a bill with exactly the same language in the Senate, I hope that a resolution of this matter can be achieved in enough time to prevent the taxing districts from feeling compelled to choose the half payment option.

In conclusion, Mr. Chairman, I would urge the members of the subcommittee to carefully consider the benefits to our communities and States which will flow from this legislation, and to report it favorably to the full committee.

**STATEMENT OF HON. SAMUEL L. DEVINE, A REPRESENTATIVE IN  
CONGRESS FROM THE STATE OF OHIO**

Mr. DEVINE. Mr. Chairman, one always likes to support legislation which will bring financial gain to his own jurisdiction. H.R. 8882 would bring financial gain to each of the three counties in my district. I gave long and serious consideration as to whether or not I should

sponsor H.R. 8882. I came to the conclusion that I could not because in my judgment, it sets an extremely dangerous precedent for the United States. If we were to guarantee the payment of taxes in this case, we would be asked to do so in the case of every other bankrupt company which owes real property taxes. We would be asked to guarantee the payment of taxes for the bankrupt W. T. Grant Co., the Robert Hall Co., and thousands of other businesses which annually go bankrupt in the United States.

I realize that the people in my district have suffered because the Penn Central and other bankrupt railroads have not paid property taxes. In my district, school districts have often been the hardest hit because of their reliance on the real property tax. Today, I have introduced a bill which will provide relief to State and local governments who are owed back taxes by bankrupt railroads. Depending upon the facts in a particular jurisdiction, the relief I propose will cover all or part of the loss sustained by the jurisdiction. My bill will give credit to those State and local governments to accept the settlement proposed by the bankrupts. The amount of credit will be equal to the amount of property tax owed minus the amount received in settlement from the bankrupts. The credit can be applied to the State or local government's share of any rail continuation subsidy. In short, my bill will eliminate or ease the financial burden on States and local governments while at the same time it encourages better railroad service.

I realize there may be inequities under my proposal. Therefore, my bill requires USRA to report to Congress within 6 months on the fairness and equity of the State and local tax settlements. Should USRA find that additional relief is due the States, we could at that time consider the advisability of such relief.

Mr. CHAIRMAN, I believe my bill is fair and equitable and it avoids the dangerous pitfalls and disadvantages of H.R. 8882. Among other things, unlike H.R. 8882, my bill would not affect the reorganization plan of the Erie Lackawanna, Lehigh Valley, and Reading Railroads which have not yet even been filed in the court. H.R. 8882 would assure that their reorganization plan would provide State and local taxing authority with \$1 at most and leave Uncle Sam holding the bag for over \$80 million.

#### **STATEMENT OF HON. SILVIO O. CONTE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MASSACHUSETTS**

Mr. CONTE. Mr. Chairman, I appreciate the opportunity to appear before your committee today to discuss a matter that is of vital importance to many of the small communities in 16 States. I am referring to the compromise currently being considered to settle the State and local taxes owed by the now-bankrupt Penn Central Railroad. As the chairman knows, there are two proposals being discussed. The first compromise proposal put forward by the trustees of the Penn Central estate, offers the taxing authorities the option of settling all past tax claims through December 31, 1976, by accepting 50 percent of the principal amount for the postbankruptcy period, or 44 percent of the principal amount for all past due taxes, both pre- and post-bankruptcy, whichever is the greater amount. The second proposal, also put forward by the trustees, would provide for an immediate cash

payment of 20 percent of the debt owed, and the remaining 80 percent to be paid through the issuance of Penn Central notes bearing interest, to the affected parties. However, the obvious problem with this option, is that the States would suffer serious delay, since the notes would not mature until 1987. This is a full 17 years since the States and local governmental units would have been able to collect on what Penn Central has owed since 1970. It is obvious that these notes would not resolve the immediate necessity of injecting money into the local economies. To be effective, the notes would have to be worthy of marketing. By borrowing on these notes, the local units of government would be able to boost their economies, while preserving their right not to compromise on the taxes owed to them by the railroad. Thus, both worthy purposes would be served by this legislative proposal.

Mr. Chairman, for this reason, I was pleased to cosponsor the bill introduced by the gentlewoman from Ohio, Ms. Oakar. This bill would amend the Regional Rail Reorganization Act of 1973 to authorize the Secretary of Transportation to guarantee notes issued to States and local taxing authorities to secure payment of real property tax obligations owed by the railroad.

The thrust of the bill is to provide the extra margin of assurance to these notes, so that they will be deemed a sound investment. The bill only adds the "full faith and credit" of the Federal Government to these notes. It should be stated that the notes are deemed "good" at this time. The only real problem associated with them is the adverse publicity that the railroads have received recently has made the notes suspect to some. This bill is designed to remove all traces of suspect. With this backing, the State and localities will be able to pursue this taxpayment compromise involving the issuance of Penn Central notes.

Mr. Chairman, the timing of this proposal could not be better. The localities involved are in an economic slump. The Penn Central owes over \$500 million, in aggregate, to the taxing authorities. In my State of Massachusetts alone, the railroad owes some \$24.2 million, of which the city of Boston is entitled to \$13.5 million. This sum will be of tremendous benefit to the localities, in their efforts to turn around the local economies. It is estimated that over 60 percent of these moneys will go immediately into the economy, in the form of salary payments and other vital needs. This will allow the so-called multiplier to work, with its immediate and direct benefits on the economy of the locality.

I should again stress that this money is an outstanding debt of the railroad, one owed since 1970, and thus is not a form of Federal payment assistance to the governmental units. The bill, of which I am cosponsoring, will allow the units of government to successfully market these notes, thus realizing the immediate benefit.

Mr. Chairman, I would be remiss not to mention the fact that some of the governmental units, which are currently carrying the Penn Central tax debt, are constrained by their options. Some of these units are, by law, forbidden from accepting any compromises on tax debts. It appears that the affected areas in my State of Massachusetts fall under this category. Thus the only option available to them is the one involving the acceptance of the notes. This only reinforces my comments on the urgent need of this legislation.

Mr. Chairman, I urge your committee to expedite your consideration and action on H.R. 8882, as time is of the essence. With the support of your committee and the Congress the affected areas will receive an immediate and long-lasting boost in the local economies, without the direct payment from the Federal Government. In behalf of the residents of these areas, I urge your committee's favorable approval of this legislative proposal.

Thank you, Mr. Chairman.

**STATEMENT OF HON. DONALD J. MITCHELL, A REPRESENTATIVE  
IN CONGRESS FROM THE STATE OF NEW YORK**

Mr. MITCHELL. Mr. Chairman, I appreciate this opportunity to present testimony in support of H.R. 8882.

My advocacy of this measure resulted from a careful analysis of the Federal involvement and responsibility for the problem the bill is intended to help solve.

Quite frankly, I am not one who suggests a "Federal solution" to every problem that comes our way. More often, I prefer to have the initiatives for corrective action come from the local or State level.

However, there are those cases where the evidence to justify a positive congressional response is so compelling as to quickly eliminate any doubts about the need for one more plan from Washington. We have such a case before us.

The bankrupt Penn Central Transportation Co. has a \$400 to \$500 million outstanding tax liability to hundreds of local governments and school districts, an outstanding tax liability that has been on the books since 1970. Even the most casual observer of the financial difficulties facing local governments and school districts knows they are hard pressed to continue even basic services, let alone attempt to broaden the horizon of services to include emerging areas of proven need. Their problem, in a word: Money. Penn Central owes them money for back taxes. They want to collect. We have an obligation to help.

When all is said and done, we can't escape the vital fact that it was Congress which contributed to the tax delinquency which now exists.

By previous legislative action, Congress subordinated the debts owed local governments and school districts to the outstanding obligations due the Federal Government. The Federal district court has prohibited the payment of back taxes.

Consequently, since June 21, 1979, when the Penn Central Co. filed a petition for reorganization under section 77 of the Bankruptcy Act, hundreds of millions of dollars have been due to local governments and school districts by Penn Central for back taxes. Approximately one-third of the total is owed to jurisdictions in my own State of New York and a sizable portion of that amount is owed in the 31st District.

The legislative proposal before us for consideration does not represent a bailout or yet another example of an already heavily indebted Federal Government picking up another massive tab for someone. In reality, it is a low-risk, high-benefit plan which more than likely will not deplete our National Treasury at all.

We all know the present situation. Penn Central has offered its debtors one of two alternatives—take 50 cents on the dollar in full settlement of the total tax obligation or accept 20 cents on the dollar now with the remaining 80 cents coming in the form of 10-year notes maturing in 1987. Not unexpected is the quandary facing decision-makers in local governments and school districts. Naturally they want 100 cents on the dollar and have every right to expect no less. But can they afford to gamble? With the “bird in hand” theory very much in mind, some might conclude it would be better to take what’s offered now and wipe the slate clean rather than venture into a scheme under which promises are made on a piece of paper of questionable value in money markets.

I think we should take action to eliminate the roll of the dice aspect of the second option by passing this legislation providing a Federal guarantee for those notes.

It should be noted that unlike some other Federal guarantee programs under which the risk factor is extremely high and ultimately we have to make good the payment of money to back up that guarantee, in the case before us the likelihood of that happening is remote. Penn Central is not without assets, its nonrailroad holdings are extensive. The famous Waldorf Astoria Hotel in New York City comes immediately to mind.

I’m confident, in the event the worst happened, the nonrailroad assets would be liquidated and the proceeds used for the notes payoff before the Federal guarantee would be activated.

In summary, what we will be doing by passing this vital legislation is extending a helping hand rather than rubberstamping another hand-out. It makes sense to me. It means urgently needed dollars to our financially hard pressed local governments and school districts.

Time is running out. Action is needed. Soon. The day of decision, October 22, will soon be upon us. I know Congress is able to act with dispatch when a clear-cut case for such a followthrough has been made. It’s my hope you will share my view that such a case has indeed been made. Thank you for the demonstration of concern evidenced by these hearings.

#### **STATEMENT OF HON. STANLEY N. LUNDINE, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEW YORK**

Mr. LUNDINE. Chairman Rooney, I wish to express my support of H.R. 8882 to provide Federal guarantees for notes offered by the Penn Central Transportation Co., as payment for delinquent taxes. I would request that this statement be included in the record of the hearings.

Because I represent a congressional district which is primarily an Appalachian program area, I am acutely aware of the hardships faced by many school districts and other taxing authorities as a result of the large sums of money owed to them in delinquent Penn Central taxes. Dunkirk, N.Y., just one small city in my district, is entitled to over \$176,000 from Penn Central. This does not include interest or penalties. The State of New York and its political subdivisions are owed nearly \$150 million by the bankrupt railroad.

It is unfair to allow Penn Central to evade its financial obligations by offering just 44 to 50 cents on the dollar. To ask creditors to accept

such a tremendous loss is a flagrant injustice. The severe economic situations faced by many communities could be alleviated in part by payment of the moneys owed to them.

I am extremely concerned about the unfortunate situation created by Penn Central. I would hope that your subcommittee acts promptly and schedules a markup of this legislation at the earliest possible date.

**STATEMENT OF HON. DOUGLAS APPELEGATE, A REPRESENTATIVE  
IN CONGRESS FROM THE STATE OF OHIO**

**Mr. APPELEGATE.** Mr. Chairman, my name is Douglas Applegate and as a U.S. Congressman, I represent the 18th Congressional District of Ohio.

I come before this committee of my distinguished colleagues to urge favorable consideration of H.R. 8882 on behalf of not only the State and local governments that I represent, but also those people who live within these governmental jurisdictions.

As we all know, the purpose of this bill is to amend the Regional Rail Reorganization Act of 1973 to authorize the Secretary of Transportation to guarantee notes issued to State and local taxing authorities to secure payment of real property tax obligations owed by a railroad in reorganization.

I believe it would be somewhat repetitious and redundant for me to sit here before this committee and describe the circumstances that led to the necessity of this type of legislation. We are all only too familiar with the deteriorating financial condition of the Penn Central Railroad system that has led to that firm's inability to pay real property taxes to literally hundreds of our lower level governmental units.

What I would like to express to this committee is the evident need for this bill and Government-guaranteed notes. Let me cite examples that are relevant to Ohio and, in particular, that State's 18th Congressional District.

I represent a district composed of 9 of the total 88 counties of the State. According to the figures that I received from the Board of Trustees of Penn Central Railroad, my district is owed a total of \$5,971,304.65. A breakdown of this total on a county basis follows:

**NINE COUNTIES REPRESENTED**

Belmont -----	\$465, 682. 09
Carroll -----	136, 024. 48
Columbiana -----	1, 546, 426. 05
Guernsey -----	25, 002. 27
Harrison -----	903, 035. 03
Jefferson -----	1, 804, 894. 01
Monroe -----	21, 589. 64
Noble -----	9, 795. 64
Tuscarawas -----	997, 054. 60

On a statewide basis, the board of trustees claims to owe \$79 million to Ohio and its governments. This figure compares to other estimates of \$80 to \$90 million. But even assuming the lesser figure to be correct, this is an overwhelming amount owed, especially to those jurisdictions which are considerably less than affluent.

These tax moneys are needed, and needed now, in order for local governments to provide the basic services that our citizens have come

to expect. But, obviously, upon examining the financial reports of Penn Central, it is highly unlikely that the company will be able to pay its tax debt to our communities. This is the reason why legislation such as H.R. 8882 is so necessary.

Granted, it would be much better if the company could pay their own bills without any type of Federal Government financial involvement, but we all know this is impossible.

Mr. Chairman, in light of the facts as I have presented them and of the pleas I make here today on behalf of the people I represent, I urge you and the members of this forum to report the bill H.R. 8882 favorably to the Committee on Interstate and Foreign Commerce in the hopes that they, too, will approve of it.

Thank you.

Mr. ROONEY. Our next witness will be Mr. John E. Cosgrove, director of legislation, Public Employee Department, AFL-CIO, Washington, D.C. Accompanying Mr. Cosgrove will be Mr. Frank Sullivan, president of the Philadelphia Federation of Teachers; vice president of the American Federation of Teachers, AFL-CIO, Philadelphia, Pa.

**STATEMENTS OF JOHN E. COSGROVE, DIRECTOR OF LEGISLATION, PUBLIC EMPLOYEE DEPARTMENT, AFL-CIO, AND FRANK SULLIVAN, PRESIDENT, PHILADELPHIA FEDERATION OF TEACHERS; VICE PRESIDENT, AMERICAN FEDERATION OF TEACHERS, ACCOMPANIED BY GREGORY HUMPHREY, DIRECTOR OF LEGISLATION**

Mr. COSGROVE. We appreciate the opportunity to testify on H.R. 8882 which we support on behalf of our department's 29 national AFL-CIO unions which represent, in turn, over 1.5 million public employees.

I am John E. Cosgrove, legislative director of the public employee department.

This legislation, addressing bankruptcy and reorganization problems of the Penn Central Railroad, is of immense importance to some 25,000 taxing authorities—counties, cities, and school districts in the Northeast quadrant of the United States and, accordingly, to the hundreds of thousands of public employees who work for them.

Penn Central, while in bankruptcy, retains substantial properties. It also retains over \$400 million in tax liabilities to local governments. The referees managing the bankruptcy have suggested settlement of tax liabilities at a 50-percent discount which would, in effect, deny school districts and major Northeast cities, such as Cleveland, Chicago, Philadelphia, New York, Boston, and Toledo, one-half of the amount owing to them. The tax liens which would normally attach to the property of a bankrupt citizen, to satisfy the tax debt, appear not to apply in this case. To us this denies the principle of the equal protection of the law, when a huge corporation receives favored treatment.

The nonrailroad assets of Penn Central, including the Waldorf-Astoria Hotel and other profitable and valuable holdings, should ultimately provide for the payment of the debt on a more equitable basis.

In these circumstances we are urging the affected tax jurisdictions to refuse the 50 cents-on-the-dollar offer and pursue court actions if necessary to enjoin any such settlement. In addition, however, we need congressional and administrative action. One of these actions should be passage of H.R. 8882 to permit the Federal Government to provide for guarantees of notes issued by the corporation to raise funds to pay these debts until the bankruptcy is dissolved.

Our executive board took this position at a meeting last Wednesday, September 21, 1977 and accordingly we urge this subcommittee and the Congress to take the action suggested.

Mr. ROONEY. Thank you.

Mr. Sullivan, you may proceed.

### STATEMENT OF FRANK SULLIVAN

Mr. SULLIVAN. Mr. Chairman and members of the subcommittee, on behalf of the American Federation of Teachers, AFL-CIO, I want to thank you for calling this hearing on H.R. 8882, a bill which has great significance to hundreds of school districts in the Northeast section of the United States.

As you are well aware, the bankruptcy and continuing reorganization of the Penn Central Corp. has created problems not only for those who count on the railroad to move their goods and those who have responsibility for maintaining a viable rail transportation system, but now the Penn Central bankruptcy is affecting the educational opportunities of hundreds of thousands of schoolchildren in some of our Nation's largest cities.

My own city which I can describe best has just recently come through a period where it seemed possible and even likely that up to one-third of the employees of the Philadelphia Board of Education, some 9,700 people, would be without jobs this September because of a \$173 million deficit and a refusal by city banks to further finance the school system debt.

The district's response besides the previously mentioned terminations was to propose closing 32 schools, doing away with all transportation and food services, eliminating guidance and counseling services, extracurricular activities (including sports), summer schools, evening schools, libraries, and finally and most ironic, elimination of magnet school programs at exactly the time when the Federal Government is pursuing a more aggressive school desegregation policy and using the threat of fund cutoffs as a weapon. Most of this potential disaster was averted by the last minute financing of a State aid package to help the school system.

Philadelphia, however, is not yet out of the woods, and it is obvious that new revenues will be needed to solve the financial dilemma. One of the first places the city should look is at outstanding debts. While no one except the railroad really knows what it owes to the local taxing jurisdictions, there is reason to believe that payment in full of these back taxes could make a significant difference to the education program being offered to schoolchildren in my city and in other cities throughout the country.

As we look at other cities, before this year is out, we in Philadelphia

may end up appearing as lucky compared to what is happening elsewhere. For example, the Toledo school system which is also a creditor of the Penn Central will be closed from now until the end of the year because of a State law in Ohio which prohibits operating in Ohio with a deficit. Last year in Ohio, seven districts including Toledo were closed due to lack of funds.

In Chicago, most teachers went without raises last year in order to help out in a financial emergency. This year a strike appears likely. These prospects are not assisted by the fact that businesses in the Chicago area have failed to pay \$244.3 million in assessed taxes since 1971 and \$48.3 coming in 1976 alone.

We don't know how much of that is owed by the Penn Central; we do know, however, that if the railroad paid its bills, it would be easier to offer an educational plan fair to teachers and students. None of this, however, would be reason enough to ask for congressional endorsement and passage of H.R. 8882, if it weren't for the fact that the current state of affairs was caused directly by Federal action. In most bankruptcy cases, taxes are considered as administrative costs and must be paid during reorganization. In the Penn Central case, however, the Federal court has prohibited further payment of back taxes. The Rail Reorganization Act passed by this committee has placed the debts owed local governments behind the obligations owed to the Federal Government. The so-called Friday Club which consisted of all the corporations creditors except State and local government was consulted frequently during development of the reorganization plan. The result was a reorganization plan to their liking.

State and local governments were not consulted, and many in fact were unaware of the railroads state of affairs until they received a check recently which amounted in some cases to less than 44 cents to the dollar. The alternative they now faced is accepting that offer which many cannot accept because of the State laws which prohibit settlement of taxes on a discount basis or accepting a cash settlement of 20 cents on a dollar and unsecured notes which mature in 10 years for the remainder of the debt.

There is no doubt that the Penn Central has the resources to make good on all the notes its creditors hold because of its substantial non-rail properties and the sale of its rail holdings to ConRail. Unfortunately, the financial reputation of the Penn Central Corp., will make the unsecured notes virtually worthless in the securities market. This means there will be a 17-year wait in some cases before local governments collect the taxes owed to them. If any average citizen found themselves in such circumstances, their property would be seized and sold for back taxes and the matter would be quickly disposed of. But because of the Federal interest in maintaining railroad services, this is not an option State and local governments can exercise. Since the current state of affairs is largely the result of Federal action, we believe the Government now has the responsibility to secure these notes and help State and local governments dispose of these back debts.

Many cities are affected outside those we have mentioned. For example, large debts are owed to Boston, Cleveland, and Detroit, all school districts currently undergoing expensive school desegregation

plans. Pittsburgh and many other places in Pennsylvania are also faced with fiscal problems and outstanding debts. We hope the Congress will act to alleviate this injustice. It's time to stop the 7-year long practice of having State and local property taxpayers subsidize indirectly, the operation of a conglomerate like Penn Central. What we ask for here is an application of the principle of equal protection of the law. Passage of H.R. 8882 would accomplish this goal.

Thank you, and I would be happy to answer any questions.

I would like to point out if the amount owed to school districts is something like \$300 million, that is about as much as the Federal Government now spends on education for the handicapped in State grants. It is more than is involved for Government spending on desegregation aid. It is three times as much as the Federal Government spends on bilingual education and half as much as the Federal Government spends on impact aid, so it is a significant sum of money.

Mr. ROONEY. Thank you, Mr. Sullivan.

You state in your testimony that the school district had a deficit of \$173 million, is that correct?

Mr. SULLIVAN. Yes, sir.

Mr. ROONEY. I understand that the Penn Central has back taxes of school taxes due to the city of Philadelphia of \$6 million.

Mr. SULLIVAN. That is one figure I have heard.

Mr. ROONEY. Isn't your problem one of a long-range problem rather than the \$6 million?

Mr. SULLIVAN. We do have a long-range problem, that is true. But as a matter of fact, in trying to resolve that problem of \$173 million—and we did not get it—we were aggregating grants and sums of money like \$6 million here and \$10 million there and \$14 million somewhere else, so it is our feeling this is a significant amount of money.

Mr. ROONEY. Are there any other large corporations in the city of Philadelphia that have delinquent tax claims against the city?

Mr. SULLIVAN. I have not had the opportunity to study the tax picture. The city of Philadelphia is fairly successful in collecting delinquent taxes.

Mr. ROONEY. Mr. Cosgrove, you state that the nonrailroad assets of the Penn Central are valuable and should ultimately provide for the payment of the debt. Is that correct?

Mr. COSGROVE. Yes, sir, Mr. Chairman.

Our impression is there is a capacity to earn here, and the possibility of payment of some of the debt is present.

Mr. ROONEY. Then why should the Government have to guarantee these notes?

Mr. COSGROVE. The problem is the short-term issue; the immediate problem that is faced by the time structures as I understand it imposed by the bankruptcy proceedings.

Mr. HUMPHREY. If I could interject.

My name is Gregory Humphrey, director of legislation for AFL-CIO. The problem is one of public perception. I have talked in a number of places about these notes to different people, and whenever you say Penn Central, I think it was most accurately characterized by an earlier witness here who said that in most cases accepting paper from Penn Central is the equivalent of accepting Confederate money.

People look on Penn Central as a bankrupt corporation with little or no credibility, and to take those things would subject any public official to terrible second-guessing on the part of his judgment.

Certainly as I understand it, these are unsecured notes, and to do that would seem to me for a public official on the local or State level to be a terrible risk.

Mr. ROONEY. Ms. Mikulski.

Ms. MIKULSKI. I don't have any questions.

Mr. ROONEY. Thank you very much.

We appreciate your appearance before this committee this afternoon.

Our next and final witness is Dr. Dana Rinchart, county treasurer, Franklin County, Ohio, Columbus, Ohio.

#### **STATEMENT OF DANA G. RINEHART, COUNTY TREASURER, FRANKLIN COUNTY, OHIO**

Mr. RINEHART. Mr. Chairman, Congresswoman, knowing of your time constraints, let me begin by thanking you for inviting me to speak before this subcommittee. I appreciate the opportunity to present a point of view held by all of Ohio's elected county officials regarding the reorganization of Penn Central Railroad. We seek congressional action to guarantee full payment of all property tax delinquencies owed by Penn Central to Ohio and its 74 affected counties.

If I might abbreviate my statement with your permission.

Mr. ROONEY. Without objection, you may summarize your statement, and your statement will become part of the record.

Mr. RINEHART. I am just going to summarize parts so I don't repeat things that have been said before.

When the Penn Central Transportation Co. sank into our Nation's largest bankruptcy on June 21, 1970, some serious national problems arose which required the immediate attention of Congress.

Considering the potentially disastrous economic and financial consequences of liquidation of our country's largest rail system, Congress moved quickly by enacting URSA and later the Regional Railway Reorganization Act.

These acts provided the machinery to insure the stability and continued existence of railroads in the Northeastern portion of our country. If the creation of ConRail and the lending of Federal money to restore rail transportation in the Midwest and Northeast had been the only thing that Congress had done at that time, it would have acted in a manner that most reasonable men would have applauded. But that was not all that Congress did.

The property transferred to ConRail was transferred free and clear of our property tax liens, and it was that property, of course, which was security for most of Penn Central's secured creditors including local taxing subdivisions.

By legislative fiat, therefore, Congress wiped out all property tax liens of localities in the 15 affected States, although law provides that real estate taxes are a first and best lien on real property.

The result is localities like my own Franklin County, Columbus, Ohio, are at the mercy of Federal court in Philadelphia and the Penn Central trustees.

The wholesale transfer of Penn Central's real property to ConRail raised serious constitutional issues. Frankly, it amounts to a taking of property without the due process of law.

Further, the transfer of our property taxes through the reorganization scheme amounts to taxation without representation. Also, the taxing subdivisions have clearly been denied the fundamental principle of equal protection under the 14th amendment.

Under the reorganization plan now being considered by Judge Fullan in Philadelphia, Penn Central is offering taxing subdivisions no more than 50 cents on the dollar for tax delinquencies. Take it or leave it.

This is shocking.

As the second largest claimant among the 15 affected States, Ohio is owed approximately \$80 million by Penn Central. Of that total, 70 percent would go to Ohio's school districts.

I do not think I need to tell you how financially troubled our school systems are today, not only in Ohio but in many parts of the country. A settlement in Ohio of 44 or 50 cents on the dollar will clearly result in the loss of millions of dollars for our school systems.

I might add that one reason why certain large school systems in Ohio are now in a financial bind is that Federal courts have mandated massive busing to achieve desegregation, with the bulk of the expense to be incurred by the school systems. The estimated cost of mandated busing in Columbus, for example, is in excess of \$20 million.

Out of the approximately \$4 million owed Franklin County by Penn Central, nearly \$2 million of that would go to the Columbus schools. I can guarantee you that our school system would be most happy to have that money.

The obvious irony is that one Federal court orders school systems to take on a major financial responsibility, while another court and Congress deprive our schools of revenues which are rightfully theirs and which could be used to bear part of the financial burdens of desegregation.

What this all boils down to is that Congress has provided the machinery for the reorganization of Penn Central at the expense of local taxing authorities and, in Ohio, at the direct expense of our schools.

An equally frustrating irony permeating this matter is that although Penn Central purports to be bankrupt, it is in reality anything but bankrupt.

While it may be temporarily true that the assets of the Transportation Co. may not equal its liabilities, a subsidiary—the Pennsylvania Co., alias Pennco—is a thriving, multimillion-dollar corporate complex. The company owns millions of dollars in the areas of recreation (amusement parks, wax museums, and the like), energy (pipelines and an oil company), and real estate (huge amounts of acreage, hotels, a sports facility and conference center, and a retreat).

Last year, Pennco made \$38.7 million in profits, with estimates ranging higher than \$100 million annually by the early 1980's.

To make the sad tale of Penn Central's "bankruptcy" even more amazing, Pennco has recently sold seven hotels and corporate buildings in the heart of New York City's financial district for more than \$100 million and is planning millions of dollars in other sales.

The list of operations and dealings goes on and on. Frank E. Loy, the president of Pennco, confidently says that Penn Central will become a billion-dollar corporation within a few years.

Some people wonder if we are trying to "bleed a turnip" in our efforts to receive full payment of back taxes. Hardly. The Penn Central trustees are flinging millions of dollars up and down a tangled network of corporate avenues with the same vigor that an ordinary person usually does in a simple game of Monopoly.

But this time the game is real, the stakes are high, and the losers—unless something is done fast—will be the "little guys" in localities across 15 States and a lot of school districts which, in Ohio, are faced with closing their doors.

Penn Central is one of the most complex multimillion-dollar organizations in the world—and all but impossible for even an experienced lawyer to comprehend.

Listen to words of Robert Blanchette, chairman of the Penn Central trustees. He says of Penn Central's tangled reorganization that "next to the Holy Roman Empire, it's the most complicated maze of organizations and entities that my reading of history reveals."

Blanchette is apparently the only person that understands this maze, and he understands it well enough to intimidate local taxing officials like us in Franklin County.

As amazed as I am by all of this, I was even more amazed to read a full-page ad one night last week in the Columbus Dispatch which had been purchased by ConRail and which I would submit for the record.

Mr. ROONEY. Without objection.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. RINEHART. The purpose of the ad, which I have right here, was to explain to taxpayers what has been going on in ConRail's efforts to rehabilitate the rail system.

Toward the end of the ad, Congress is commended for rejecting the alternative of nationalizing the railroads. The ad says that Congress "decided that a private-sector solution was best and least costly to the taxpayers. For taxpayers would have to foot the bill if the bankrupt railroads were nationalized."

Who is ConRail trying to fool? It is clearly the intent of the reorganization plan that the taxpayers will indeed foot the bill through the loss in millions of dollars in tax delinquencies from which Penn Central has been exempted by congressional fiat.

I do not think I need to tell you where an individual taxpayer or small business would end up if they tried to pay half or less of their taxes.

Now, just how many papers has ConRail placed that ad in? And how much are they spending on this PR effort? The ad in the Dispatch cost approximately \$2,500.

I certainly must compliment the Penn Central trustees for their impeccable, brilliant strategy. They drew their battle plan with the finesse and guile that Rommel used to walk across northern Africa in 1940 and have succeeded in all respects.

The plan is as smooth as it is brilliant. I cannot escape a vision of the trustees cackling in delight as they concocted their scheme, much like the witches in "Macbeth" when they cried "Boil, cauldron, boil!"

The reorganization plan is a fantastic example of "divide and conquer." It has successfully divided administrative claimants like myself, who are owed a total of \$400 million, not simply into 15 separate States, but into the thousands of taxing subdivisions within those States. And they went one step farther. They even divided local subdivisions within counties by offering 100 cents on the dollar to claimants owed \$10,000 or less, and 44 to 50 cents to all others.

My main objective in appearing here is to communicate one message to Congress: we want our delinquent taxes owed by Penn Central to be paid in full.

I am therefore urging Congress to take immediate action to guarantee payment to Ohio of 100 cents on the dollar for all of those taxes.

The Oakar bill now before you is a step in the right direction. But more needs to be done. In calling on you for action, I would also point out that we "little guys" are in the mess we are in today because of the nature of the involvement of the Federal Government, through Congress and now the Federal courts.

I salute Congress for attempting to deal with the serious, far-reaching problems and questions raised by the Penn Central bankruptcy. But, on behalf of my constituents, I must also chastise it for allowing the best interests of the local subdivisions to be steamrollered in the solution.

Let me also point out that, in bringing this message to you, I am not just speaking for the other elected officials in Franklin County. Last week at a meeting of the Ohio Committee of County Officials, representing all elected county officials in the State, that group voted unanimously to adopt a resolution calling for, among other things, full payment of all moneys owed Ohio taxing authorities by Penn Central. I would submit a copy of the resolution for the record.

That group represents 984 elected county officials in Ohio. I think it is fair to call the action last week "a mandate."

Mr. ROONEY. Have you ever contemplated what social and economic effects of such a seizure would have on the community of Ohio?

Mr. RINEHART. I have not gotten to that yet but I presume you are ahead of me, Mr. Chairman.

Certainly I thought about that. What other alternatives do we have? This is the largest taxpayer in Franklin County who is thumbing their nose at us and we live and breathe on these dollars.

Mr. ROONEY. Have you every thought what would have happened to the bankrupt railroads in the Northeast if ConRail did not get in there, if the Federal Government did not get in there and diffuse it. You would not have had 1 nickel in taxes.

Mr. RINEHART. If Congress is going to act the baggage has to come to, and to tuck it to the local subdivisions, to use our tax dollars to reorganize a railroad simply is without precedent.

Earlier you were talking about precedent here. I heard members of the committee bring up precedent and people here talk about precedent.

Well, the people in our district in Franklin County and the State of Ohio have another precedent to discuss and that is what happens when North American Rockwell, our second largest taxpayer, goes under and you in Congress decide it is in the national interest to boost North American Rockwell?

" I hope they never do but they make a lot of claims. Do we take 44 or 20 cents on the dollar from them. Our schools are living and breathing on that money. I am listening to this county of 1 million people, to the leaders of the school system, cry daily and they are scared to death about what is going to happen with desegregation. Their doors are closing without busing. We don't have \$20 million. I heard another question that just completely astounded me.

I have never been here before, Mr. Chairman, but I am stunned by this. Someone on the committee raised the question about why Congress has put all this money into ConRail. We put all this money in here and there and you are only talking about in Mayberry \$260,000. Sir, I am telling you I am talking about only \$4 million but to us that \$4 million is a lot of money. I think what Congress attempted to do was a great thing but Congress can't have it's cake and eat it too. We are getting it tucked to us by the trustees who are doing a brilliant job but they are using the tools that this Congress set up.

Do you wish me to conclude my statement, sir?

Mr. ROONEY. You may conclude.

Mr. RINEHART. How serious are we in our quest to collect 100 cents on the dollar from Penn Central? Totally. I want you to know the schools in Ohio are closing their doors and at least part of the reason for that is the skyrocketing rate of tax delinquencies. The largest delinquent landholders in Ohio are Penn Central and ConRail, which still refuses to pay their taxes.

Despite the efforts of the trustees and their plague of attorneys, we stand united in Ohio and I want you to be assured of that fact.

As a county treasurer it is my legal responsibility to do all in my power to collect taxes. While I would rather not, I nonetheless have the authority to distrain sufficient goods or property within our county owned by a delinquent taxpayer to cover back taxes. This happens all the time with individuals and small businesses. It is about to happen with Penn Central.

I am prepared to seize Penn Central and ConRail property, including trains, if back taxes are not paid in full. Trains rumbling across the country will have to rumble around Franklin County. We are not interested in going into the train business in Columbus. But, if necessary, we will not hesitate to protect our right to tax ourselves as we see fit—and spend our tax dollars as our people direct.

In conclusion, let me restate my hope that Congress will take immediate action on legislation providing for full payment to Ohio and the other States of all Penn Central delinquencies.

What the trustees are attempting to pull off; so far with the full cooperation of the Federal Government, amounts to nothing less than a reverse version of the Great Train Robbery.

Their actions are blatantly unfair and unconstitutional. And, worst of all, the biggest losers, at least in Ohio, will be our local schoolchildren—and their parents who voted school levies now being used to reorganize a railroad.

I do not want to see that happen, and I cannot believe you do either.

Thank you.

I will be happy to respond, Mr. Chairman, to any questions you or any other members of the subcommittee might have.

[Mr. Rinehart's prepared statement follows:]

STATEMENT OF DANA G. RINEHART, COUNTY TREASURER, FRANKLIN COUNTY,  
OHIO

Let me begin by thanking you for inviting me to speak before this committee. I appreciate the opportunity to present a point of view held by all of Ohio's elected county officials regarding the Reorganization of the Penn Central Railroad. We seek congressional action to guarantee full payment of all property tax delinquencies owed by Penn Central to Ohio and its 74 affected counties.

When the Penn Central Transportation Company sank into our Nation's largest bankruptcy on June 21, 1970, some serious, related problems arose which required the immediate attention of the Federal Government. With the spectre of a dying rail system looming on the horizon, large rail-dependent industries such as steel and automobiles realized that their own survival was in part connected with that of Penn Central. There was mounting concern that if one major transportation company could go bankrupt, why could not others? Why, also, could not a mammoth utility company like Con Ed meet the same fate? Clearly, the shock waves of such occurrences could have a disastrous impact on the stability of our Nation's economy.

The unprecedented bankruptcy of the Penn Central Transportation Company obviously required unprecedented action on the part of the Federal Government. And that is exactly what took place.

In 1970, Congress enacted the Emergency Rail Services Act calling for the Secretary of Transportation to provide federal guarantees to Penn Central Trustee certificates, which in turn were accorded the highest lien on Penn Central property.

Through the Regional Rail Reorganization Act of 1973, Congress established ConRail, a separate for-profit corporation, to which most of Penn Central's best rail-related property and equipment was transferred on April 1, 1976. That Act provided the legal machinery which insured the continuous flow of millions of dollars in federal loans to ConRail to restore the decaying system it inherited thereby rejuvenating rail transportation in the Midwest and Northeast. If that were all it had done, Congress would have acted in a manner that most reasonable men would have applauded.

But that was not all. The property transferred to ConRail was transferred free and clear of property tax liens. And, it was that property, of course, which was the security for most of Penn Central's secured creditors, including local taxing subdivisions.

By legislative fiat, therefore, Congress wiped out all property tax liens of localities in the 15 affected states, although law provides that real estate taxes are a first and best lien on real property. The result is that localities like my own—Franklin County, Columbus, Ohio—are at the mercy of the Federal Court in Philadelphia and the Penn Central Trustees.

The wholesale transfer of Penn Central's real property to ConRail raised serious constitutional issues. Frankly, it amounts to a taking of property, without the due process of law. Further, the transfer of our property taxes through the reorganization scheme amounts to taxation without representation. Also, the taxing subdivisions have clearly been denied the fundamental principal of equal protection under the 14th Amendment.

Under the reorganization plan now being considered by Judge Fullam in Philadelphia, Penn Central is offering taxing subdivisions no more than 50 cents on the dollar for tax delinquencies. Take it or leave it.

This is shocking. As the second largest claimant among the 15 affected states, Ohio is owed approximately \$80 million by Penn Central. Of that total 70 percent would go to Ohio's school districts. I do not think I need to tell how financially troubled our school systems are today, not only in Ohio but in many parts of the country. A settlement in Ohio of 44 or 50 cents on the dollar will clearly result in the loss of millions of dollars for our school systems.

I might add that one reason why certain large school systems in Ohio are now in a financial bind is that federal courts have mandated massive busing to achieve desegregation, with the bulk of the expense to be incurred by the school systems. The estimated cost of mandated busing in Columbus, for example, is in excess of \$20 million. Out of the approximately \$4 million owed Franklin County by Penn Central, nearly \$2 million of that would go to the Columbus schools. I can guarantee you that our school system would be most happy to have that money.

The obvious irony is that one Federal Court orders school systems to take on a major financial responsibility while another court and Congress deprive our schools of revenues which are rightfully theirs and which could be used to bear part of the financial burdens of desegregation.

What this all boils down to is that Congress has provided the machinery for the reorganization of Penn Central at the expense of local taxing authorities and, in Ohio, at the direct expense of our schools.

An equally frustrating irony permeating this matter is that although Penn Central purports to be bankrupt, it is in reality anything but bankrupt. While it may be temporarily true that the assets of the Transportation Company may not equal its liabilities, a subsidiary—The Pennsylvania Company, alias Pennco—is a thriving, multimillion dollar corporate complex. The company owns millions of dollars in the areas of recreation (amusement parks, wax museums and the like), energy (pipelines and an oil company), and real estate (huge amounts of acreage, hotels, a sports facility and conference center, and a retreat). Last year, Pennco made \$38.7 million in profits, with estimates ranging higher than \$100 million annually by the early 1980's.

To make the sad tale of Penn Central's "bankruptcy" even more amazing, Pennco has recently sold seven hotels and corporate buildings in the heart of New York City's financial district for more than \$100 million and is planning millions of dollars in other sales. The list of operations and dealings goes on and on. Frank E. Loy, the President of Pennco, confidently says that Penn Central will become a billion dollar corporation within a few years.

Some people wonder if we are trying to "bleed a turnip" in our efforts to receive full payment of back taxes. Hardly. The Penn Central Trustees are flinging millions of dollars up and down a tangled network of corporate avenues with the same vigor that an ordinary person usually does in a simple game of Monopoly. But this time the game is real, the stakes are high and the losers—unless something is done fast—will be the "little guys" in localities across 15 states and a lot of school districts which, in Ohio are faced with closing their doors.

Penn Central is one of the most complex multi-billion dollar organizations in the world—and all but impossible for even an experienced lawyer to comprehend. Listen to words of Robert Blanchette, Chairman of the Penn Central Trustees. He says of Penn Central's tangled reorganization that "next to the Holy Roman Empire, it's the most complicated maze of organizations and entities that my reading of history reveals." Blanchette is apparently the only person that understands this maze and he understands it well enough to intimidate local taxing officials like us in Franklin County.

As amazed as I am by all of this, I was even more amazed to read a full-page ad one night last week in the Columbus Dispatch which had been purchased by ConRail. The purpose of the ad, which I have right here, was to explain to taxpayers what has been going on in ConRail's efforts to rehabilitate the rail system. Toward the end of the ad, Congress is commended for rejecting the alternative of nationalizing the railroads. The ad says that Congress "decided that a private-sector solution was best and least costly to the taxpayers. For taxpayers would have to foot the bill if the bankrupt railroads were nationalized."

Who is ConRail trying to fool? It is clearly the intent of the reorganization plan that the taxpayers will indeed foot the bill through the loss in millions of dollars in tax delinquencies from which Penn Central has been exempted by Congressional fiat. I do not think I need to tell you where an individual taxpayer or small business would end up if they tried to pay half or less of their taxes. Now just how many papers has ConRail placed that ad in? And how much are they spending on this PR effort? The ad in the Dispatch cost approximately \$2,500.

I certainly must compliment the Penn Central Trustees for their impeccable brilliant strategy. They drew their battle plan with the finesse and gulle that Rommel used to walk across Northern Africa in 1940. And have succeeded in all respects.

The plan is as smooth as it is brilliant. I cannot escape a vision of the trustees cackling in delight as they concocted their scheme, much like the witches in MacBeth when they cried "Boil, cauldron, Boil!" The reorganization plan is a fantastic example of "divide and conquer." It has successfully divided administrative claimants like myself, who are owed a total of \$400 million, not simply into 15 separate states, but into the thousands of taxing subdivisions within those states. And they went one step further. They even divided local subdivisions within counties by offering 100 cents on the dollar to claimants owed \$10,000 or less, and 44 to 50 cents to all others.

My main objective in appearing here is to communicate one message to Congress: we want our delinquent taxes owed by Penn Central to be paid in full. I am therefore urging Congress to take immediate action to guarantee payment to Ohio of 100 cents on the dollar for all of those taxes. The Okar Bill now before you is a step in the right direction. But more needs to be done. In calling on you for action, I would also point out that we "little guys" are in the mess we are in today because of the nature of the involvement of the Federal Government, through Congress and now the Federal Courts. I salute Congress for attempting to deal with the serious, far-reaching problems and questions raised by the Penn Central bankruptcy. But, on behalf of my constituents, I must also chastise it for allowing the best interests of the local subdivisions to be steamrollered in the solution.

Let me also point out that, in bringing this message to you, I am not just speaking for the other elected officials in Franklin County. Last week at a meeting of the Ohio Committee of County Officials, representing ALL elected county officials in the State, that group voted unanimously to adopt a resolution calling for, among other things, full payment of all monies owed Ohio taxing authorities by Penn Central. That group represents 984 elected county officials in Ohio. I think it is fair to call the action last week "a mandate."

How serious are we in our quest to collect 100¢ on the dollar from Penn Central? Totally. I want you to know that schools in Ohio are closing their doors and at least part of the reason for that is the skyrocketing rate of tax delinquencies. The largest delinquent landholders in Ohio are Penn Central and ConRail. Despite the efforts of the Trustees and their plague of attorneys, we stand united in Ohio and I want you to be assured of that fact.

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In conclusion, let me restate my hope that Congress will take immediate action on legislation providing for full payment to Ohio and the other states, of all Penn Central delinquencies. What the Trustees are attempting to pull off, so far with the full cooperation of the Federal Government, amounts to nothing less than a reverse version of the Great Train Robbery. Their actions are blatantly unfair and unconstitutional. And, worst of all, the biggest losers, at least in Ohio, will be our local school children—and their parents who voted school levies now being used to reorganize a railroad.

I do not want to see that happen, and I cannot believe you do either.

Thank you.

Mr. ROONEY. Thank you very much, Mr. Rinehart, for your statement.

Ms. Mikulski?

Ms. MIKULSKI. Mr. Rinehart, are you legally restricted from accepting anything less than full payment?

Mr. RINEHART. Yes; under current law, prior to very recent legislation, we were maximum, restricted. However, the Penn Central people managed to slip through our legislation very quietly, without testimony of any kind in either House, that would permit treasurers to accept less than the full amount of back taxes.

That legislation is now law, and so I can't accept less than the full amount of back taxes.

Ms. MIKULSKI. I found your statement to seize the railroads to be very interesting. I imagine that the Penn Central goes more than through Franklin County.

Mr. RINEHART. Indeed it does.

Ms. MIKULSKI. You in addition to yourself have other county treasurers in Ohio that feel they will also exercise the same strategy?

Mr. RINEHART. I believe this is a very real possibility. But I do not feel confident that I could sit here and speak for all 74 treasurers.

Mr. RUSSO. Maybe we should go in and seize Ohio and save Ohio from Ohio.

Ms. MIKULSKI. I can understand your frustration because I have gone with Penn Central trying to solve their problems. I find them arrogant, heavy, and highhanded, and I think a colloquialism would be "snotty," too, toward local government. I am sympathetic to your situation.

I think had they approached you in local government differently, perhaps your intensity would not be as great, but I think what you are saying here—and your statement is quite intense—is that you have had it.

Mr. RINEHART. Exactly.

Ms. MIKULSKI. I can understand why you have had it. They took out a \$2,500 ad in the Baltimore Sun and News American, and I, too, wondered where they got the money because I can't get railroad tracks fixed in my town or a phone call returned.

Mr. RINEHART. I think this committee should know that had Congress not passed ConRail legislation—I am sorry—had Congress not passed URSA in the form that it currently is in, our tax liens would have been first and best on Penn Central property.

Had our tax liens remained first and best on the real property, I don't believe I would be here today.

Ms. MIKULSKI. That is all I have.

Mr. RUSSO. Let me ask you this.

This committee found there were certain discriminatory taxes levied by certain States and found Ohio to have levied 32 percent higher against the railroad property than other commercial property.

Are you telling this committee you think we should make up for your indiscriminatory tax against the railroads?

Mr. RINEHART. Absolutely not, and I take issue with your statement. I can provide you sufficient facts to show you that rail property in our county was not taxed in that manner. As a matter of fact, Mr. Russo, I think you and other members of this committee should know that recently Penn Central sold to the city of Columbus a piece of land downtown for us to build a convention center on.

Now, before the 1975 reappraisal in Franklin County, that land was on the books at much less than what it was on the books for when Penn Central said we will sell it.

Had we purchased it then, I suggest that we would have been able to purchase it for much less than what we did after the reappraisal.

Now, all land in Ohio is appraised at 100 percent of its fair market value, but prior to the reappraisals, most all industrial and commercial property in Ohio was appraised by the same people and at the same rate.

There are some exceptions that are unrelated to Penn Central, but I would take issue with the basis of your statement. Therefore, I could not come up with the conclusion you did.

Mr. RUSSO. I suggest you take a look at committee print prepared

by this staff dated December 1975 dealing with materials concerning effect of Government regulation on railroads and economic profile and railroads in the United States.

Turn to page 15, table 5, and you will find out the conclusions and reasons why I made that statement.

Mr. RINEHART. I can't understand why you made the statement, sir, but I tell you first I don't believe it and second, I have got the figures in my office which I would be more than happy to share with this committee at any time, that go all the way back to 1804 to show what that land was appraised at.

Penn Central owned some of the best land in Franklin County.

Mr. RUSSO. I would hope a lot of that information was made available to the committee at the time they made this preparation. I would like to think they operated from a knowledgeable position.

Mr. RINEHART. I certainly hope they asked the right questions because our office is open.

Mr. RUSSO. Unfortunately I was not here at the time it was prepared so I can only refer to staff counsel who was deeply involved with it.

My opinion is we should have left all the railroads go bankrupt and let all the people in your county go bananas because they don't have any service and they would jump on your back with wanting an alternative.

But we have the 4-R Act and we have to live with it and at the same time protect your taxpayers from an indiscriminate type of taxes so we have to balance the equities as to whether or not your school districts get taken care of, whether or not your taxpayers are willing to suffer more loss of dollars and it is not an easy job for us to do.

Mr. RINEHART. I understand it is a difficult job and I am sure you appreciate the difficult position we are in. But I would be more than happy to show you—my books are public record.

Mr. RUSSO. I want to refer to counsel because he was here at the time the act was put into effect. So I can ask what facts were these based on. Association of American Railroads is the source.

Mr. MOLLAY. Mr. Russo and Mr. Rinehart, at that time all the States were invited to give comment. Anyone who had any idea about how we could solve the problem or how Congress could solve the problem with the railroads in the Northeast was asked to come in.

These figures were not only checked by the American Association of Railroads but were also checked by the administration then in power and the amount of discrepancy in taxation was a significant amount and it was significant enough so both the House and the Senate passed that provision overwhelmingly and in the Senate it created a great deal of controversy because of the 10-C situation.

I don't know that anyone could look at a particular county and come up with a specific overcharge. The figures of necessity were on a state-wide basis and about the only way that you can get a valid claim on a given county is to have a long trial and long court proceeding.

But let me assure you everyone made their best effort in coming up with figures.

Mr. RINEHART. I am not sure they did not but Penn Central owns the best land in Franklin County. They own the heart of the city and they own strips that go through the best commercial and industrial land there.

To have that land underappraised would be an error. They have the prime, top-dollar property. Fine let them go bankrupt. If we had been able to foreclose on our tax liens or to bargain with those people we would not be here because that land is worth far more than our taxes that we were extracting from it.

As you well know, sir, Ohio taxes a very small portion of its available tax base and our credit rating is triple A because of that.

One other thing, Mr. Russo, if I might sir, the rate of taxation is the same unilaterally. What you are talking about is the appraised value, the variations in appraised value. I would suggest to this committee—and I will stand behind the figures in my office—that that land they sold to the city of Columbus for \$5.5 million was worth \$5.5 million and it was on the tax books for a lot less than that. A lot less than that.

But Columbus paid top dollar for it.

Trying to deal with Penn Central is like trying to deal with His Holiness the Pope. You can't even get to them.

Mr. Russo. Remember right now you are dealing with the Congress.

Mr. RINEHART. I understand that. I would also add I think I am properly reflecting the opinion of the people in Franklin County.

Mr. Russo. If the people in Franklin County came to me the way you do they would have a hell of a time getting anywhere with me.

Mr. RINEHART. Sir, we have been under the 8-ball for some time.

Mr. Russo. You haven't been under the 8-ball with this member yet. Just remember that.

Mr. ROONEY. I might say, Mr. Rinehart, you did say at one point that you wished that the railroads would have been closed down, you could have taken them over, you don't need them in Franklin County.

Mr. RINEHART. I didn't say that, sir.

Mr. ROONEY. But you do know the people in Franklin County and Columbus were before this committee seeking development of an Amtrak station as I recall.

You have thrown figures all over the place. I wonder if you can break down the \$100 million figure on page 4, the properties sold by Pennco. Do you know what the mortgages were on these properties? Do you know the net amount received by Penn Central on these properties?

Mr. RINEHART. You are talking about downtown New York property?

Mr. ROONEY. Yes. You mentioned several properties, \$100 million.

Mr. RINEHART. That is correct. They sold them for more than \$100 million. I can break that down for you.

Mr. ROONEY. Let me have it.

Mr. RINEHART. Let me see if my file is here.

Mr. Chairman, the problem with giving you a block-by-block break-down is many of the deeds have not been recorded on some of the stuff they have done.

For example, there has been an inordinate amount of—

Mr. ROONEY. You have not supplied the Chair with the information that I asked. You have given me who the buyer was, what the price was but I asked for the net figures.

Mr. RINEHART. The net on each of them? I don't know the net on each of them. I know they are taking in a lot of money and they are running a lot of money back into their companies but they are not paying taxes and we can't do anything about it because Congress wiped out our tax liens.

Mr. ROONEY. I think for the most part, Mr. Rinehart, your problems lie with the courts, not with the Congress. We are here to preserve the railroad system in this country and if you think that your county is going to seize the railroads let me tell you you have another thought coming because this is a land of the law and not lawlessness. I would admonish you to go back and try to reorganize your group that has all the problems with the Penn Central and go to the courts where you belong because I think knowing the background, after hearing your testimony today, I think you are a very loyal American but I think you should reassess your position. With that the committee stands adjourned until 10 a.m. tomorrow, room 2299.

Thank you very much.

[Whereupon, at 4:20 p.m. the committee adjourned to reconvene at 10 a.m., Wednesday, September 28, 1977.]

# GUARANTEE OF DELINQUENT TAXES DUE FROM BANKRUPT RAILROADS

WEDNESDAY, SEPTEMBER 28, 1977

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON TRANSPORTATION AND COMMERCE,  
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,  
*Washington, D.C.*

The subcommittee met at 10 a.m., pursuant to notice in room 2255, Rayburn House Office Building, Hon. Fred B. Rooney, chairman, presiding.

Mr. ROONEY. Our first witnesses will be the National Coalition Panel, the Honorable Art Holland, the mayor of Trenton, N.J., and representing the U.S. Conference of Mayors; the Honorable Herbert Pfuhl, Jr., the mayor of Johnstown, Pa., representing National League of Cities; Charles H. Merrill representing National Association of County Organizations and Lowell Davis representing International Association of School Business Officials and secretary-treasurer, Euclid Board of Education.

Gentlemen, you may proceed. You may read your statements or summarize them or continue in any way you would like.

## STATEMENT OF HON. HERBERT PFUHL, JR., MAYOR, CITY OF JOHNSTOWN, ON BEHALF OF THE NATIONAL LEAGUE OF CITIES

Mr. PFUHL. Mr. Chairman and members of the committee, it is a pleasure for me to come here to address you on behalf of this legislation.

I am Herbert Pfuhl, Jr., mayor of Johnstown, Pa., and president of the Pennsylvania League of Cities. I am here today with Arthur J. Holland, mayor of Trenton, N.J. representing the National League of Cities and the U.S. Conference of Mayors who will be here shortly. Those organizations represent virtually all the cities of the Nation. I want, first, to commend Chairman Fred Rooney for his willingness to consider this urgent matter on very short notice, also due to the fact my city was devastated by a disaster on July 19 of this year and I find it necessary to come and testify on its behalf.

So, again, Mr. Chairman, I thank you very much.

You have already heard from witnesses who have laid out the history of the Penn Central State and local taxes situation. You will also hear this morning from those whose expertise is in the technical details of the issue. I am here today to present the local elected officials point of view. And from that view we urge passage of H.R. 8882.

It is not always easy to get agreement among city officials on Federal legislation, especially when the benefits will accrue directly to some but not to others. In this case, however, the matter is so important financially for some and as a matter of principle for others, that support comes from cities of all sizes and types, located in all regions.

The issue upon which all cities can agree is that the Federal Government should not intervene to prevent the collection of State and local taxes. And, agreement is just as strong for the proposition that when the Federal Government makes decisions that have serious consequences for city budgets, city governments should be involved. In this case, both of these principles have been compromised. Faced with the Penn Central bankruptcy filing in 1970, Congress decided that Penn Central would continue operations at a tremendous loss in order to forestall a financial and transportation catastrophe. Most would agree with that basic decision. However, subsequent decisions and their consequences have not been as agreeable.

In October 1970 the U.S. district court in Philadelphia ordered that the Penn Central trustees make no further payment of State and local taxes until so ordered, separating these obligations from other administrative costs. In addition, the Federal Government has loaned the trustees of the Penn Central more than \$500 million and has ordered that the repayment of this loan shall take priority over the repayment of State and local tax claims.

For 7 years, Penn Central's taxes went uncollected until they had mounted to over \$400 million in principal and interest. In December of last year, the Penn Central trustees offered a compromise of tax claims which would have Penn Central paying 50 percent of the principal on post reorganization claims or 44 percent of the principal in all claims. Because interest and penalties were not included, the true payment would be about 30 percent of that owed. Earlier this year, it was determined that those taxing authorities that did not accept the compromise will receive a cash payment of 20 percent of their claims with 80 percent to be paid in notes redeemable in 10 years.

Today, therefore, local governments are faced with making a choice before October 22 between accepting only a fraction of the taxes owed by Penn Central or accepting an even smaller fraction and a decade's further delay in collecting the full amount. I think it fair to say that at no point in the course of the chain of decisions was the city government financial interest given serious consideration. At no point were cities able to sit at the table when the decisions were being made. But today, cities are faced with the immediate prospect of having to take partial payment of these taxes.

The precedent raises significant constitutional questions. We are seriously alarmed that the Federal Government would prevent the payment of taxes due, assert first priority on the repayment of a loan over the payment of tax obligations, and then deny relief to local tax authorities. It appears that State and local governments are being asked to relinquish their responsibility for collecting revenues duly owed, and to subsidize PennCo. If the precedent of Penn Central is allowed to stand, we can anticipate Federal policy intervention in local property tax practices in the future.

While the implications of this case are important for the future of Federal-local relations, other consequences are immediate and significant. Nearly \$500 million is owed to governments in the regions suffering the most severe fiscal strain. In my State, Pennsylvania, the total exceeds \$32 million. In New York State, it is \$144 million, in Ohio \$80 million, in Indiana \$50 million and in New Jersey, \$41 million. The total owed to the city of Cleveland is over \$14 million, to Pittsburgh \$17 million, to Boston \$14 million and, lest you think this is just a big city problem, the amount owed to Poughkeepsie, N. Y., a city of 32,000 is \$696,000 compared with a 1977 budget of \$13.7 million.

In the city of Johnstown to meet property taxes it means approximately 2 mills of taxes per year.

By the way, one of the difficulties encountered by State and local governments in this case is discovering the facts. If you ask what is owed, you are directed to Philadelphia and 16,000 documents.

As a consequence Penn Central has been able to pursue a strategy of divide and conquer which is not possible with a single, unified creditor such as Gulf Oil. Individual cities are being offered a bird in the hand and, with no knowledge of the totals involved and little knowledge about the prospects for future payment of the notes, it is reasonable to expect them to grasp the offer.

For the elected officials of our cities, this is an unpalatable situation. For those directly involved, it represents a potential loss of hundreds of millions of dollars at a time when city work forces are being cut, taxes are being raised, services are being reduced and improvements are being postponed.

Many of us are facing taxpayers' revolts. How can we compel citizens to pay hundreds when they see millions being forgiven? How can we settle for 30 percent when even 100 percent would only contribute slightly to the solution of our problems?

This legislation, it seems to me, provides an acceptable and reasonable resolution to a difficult situation. A Federal guarantee of the notes for 80 percent of the amount owed would improve their liquidity considerably. It would mean, therefore, that a city could accept the 20-percent cash payment without facing the prospect of holding the notes for 10 years. Otherwise, many cities will be compelled to accept the 30-percent payment. There is, everyone agrees, no real risk in these notes, only market perceptions, and thus the guarantee creates no risk for the Federal Government.

This action would not constitute a bailout but only an acceptance by the Federal Government of its responsibility for not damaging the integrity of State and local government revenue systems. It is, I think, a solution which adequately address both the question of principle and financial need.

At this time, Mr. Chairman, I want to thank you very much for allowing me on behalf of the National League of Cities and U.S. Conference of Mayors to present this testimony to you and to thank you very much for the consideration.

Mr. ROONEY. Mayor, I do know you have a very tight schedule and you have commitments back in Johnstown. I know the bad dilemma you have had in Johnstown in the past 3 months and I am very sympathetic. I might say the people of Bethlehem, Pa., were very generous to your community.

Mr. PFUHL. Yes, sir, Allentown also.

Mr. ROONEY. And the entire Lehigh Valley and the district representative. I can remember seeing articles in the papers how they were sending money to assist you.

I do want to ask you a few questions and then you will be excused to make that plane connection.

On page 3 of your statement you state that it is difficult for you to determine how much is owed. This is very difficult for me to comprehend because it seems to me that the taxing authority would know precisely how much moneys are due the individual municipalities or taxing authorities.

Mr. PFUHL. Sir, we are talking about generality. We are talking about lumping it all together rather than taking it separately as a single entity like Bethlehem, Pa. or Allentown and putting it all into one large package to present positively to you. That is the way I am trying to address it to you. There are times that we do have difficulties in this area.

Mr. ROONEY. How much is owed the City of Johnstown?

Mr. PFUHL. We are better than \$150,000. Harrisburg is a little better than \$175,000. I did mention Pittsburgh and Philadelphia above the \$150 million mark.

Mr. ROONEY. On page 2 you state that one of the facts that is not agreeable to the cities is that the Federal Government loaned the trustees of Penn Central more than \$500 million and has ordered that the repayment of this loan shall take priority over the repayment of State and local tax claims.

As these funds were loaned after the corporation became bankrupt don't you believe it was reasonable for the Federal Government or any other person loaning funds to a bankrupt concern to require the loan be repaid before any other repayments are made?

Mr. PFUHL. My feeling is that basically I think the amount that the Federal Government has given in this situation—you are giving, what? Fifty cents on the dollar I think is correct or something of that nature—I think that we have a right, cities, to except some of that revenue to be returned to us and that repayment should have a priority also to the constituents in that area. In that case it should be that way.

Mr. ROONEY. On page 2 you also state that at no point were cities able to sit at the table when the decisions were being made. I believe that the record will show that during the negotiations for the Emergency Rail Act of 1970, the three R Act and four R Act, the cities were very much involved in the Federal legislation and favored the legislation at that time.

Mr. PFUHL. If that needs to be corrected then we stand corrected on that issue.

Mr. ROONEY. Mayor Pfuhl, I have no additional questions for you and you may be excused.

I understand that Mayor Holland, the Mayor of Trenton was to follow you but he has not arrived yet.

Mr. PFUHL. Sir, we also have additional testimony that we would like to present that is personal testimony from the mayor of Poughkeepsie, N.Y. I would appreciate it if we could present it at this point [see p. 133].

Mr. ROONEY. Without objection it will be included in the record.

Now we will go back to our Amtrak passenger, the Honorable Art Holland representing the U.S. Conference of Mayors and who is the mayor of the city of Trenton.

Mayor, what time did you leave Trenton today?

**STATEMENT OF HON. ARTHUR J. HOLLAND, MAYOR OF THE CITY OF TRENTON, ON BEHALF OF THE U.S. CONFERENCE OF MAYORS**

Mr. HOLLAND. 7:20.

Mr. ROONEY. What time were you supposed to leave Trenton?

Mr. HOLLAND. It was on time. The problem, and it happens every time it seems between Trenton and Washington, we were due in here at 9:33 and we got in here about 10 o'clock.

Mr. SKUBITZ. You got here at what time?

Mr. HOLLAND. About 10 o'clock.

Mr. ROONEY. That is a record run for Amtrak.

Mr. HOLLAND. I thought if it had been Penn Central it might have been a conspiracy.

Mr. ROONEY. You may proceed.

Mr. HOLLAND. Thank you.

I am Arthur J. Holland, mayor of Trenton, N.J., here today with Mayor Pfuhl to speak in favor of H.R. 8882. I want, first, to reiterate the thanks expressed by Mayor Pfuhl to you, Mr. Chairman, and to the members of this subcommittee for its willingness to give prompt and serious consideration to this urgent matter. And I want to reemphasize the unity among city officials on this issue.

Beyond the reasons offered by Mayor Pfuhl for supporting this legislation, I think there are additional, strong policy justifications. It would be possible to put the city government case in extreme terms and propose extreme solutions. It might be said that the Federal Government has financed a portion of its transportation policy out of city budgets and that there should be full and direct repayment of the costs incurred by cities. In fact, the current situation is the result of inadvertence and not intent. But it is for just that reason that it is disturbing.

The amount owed to State and local governments by Penn Central is roughly one-third of the fiscal year 1978 antirecession fiscal assistance payments. Over \$400 million has been kept out of the economy over the past 7 years, and the impact has been on the regions that have been under the most severe fiscal stress. In its recent survey of the fiscal condition of cities, the Joint Economic Committee reported that it is these cities—those with high unemployment and decreasing populations—that continue to “exhibit the most acute symptoms of need.” They are cutting services, reducing much-needed maintenance expenditures, raising taxes, and running deficits.

We all might agree that preserving the Penn Central is in the national interest, but few would argue that the burden should be on the backs of the governments least able to carry it. We have here a policy decision with undesirable side effects—results produced by one government action that contradict the intent of other actions which have been taken to stimulate the economy and assist these cities. Unfortunately, we have not been alert to this sort of situation in our

thinking about urban policy or we might produce better results at a lower cost.

Mayors are often chided for coming to Washington with a tin cup, seeking to share Federal Government revenues rather than tap the cities' own sources. Here is a case where we are coming to Washington to ask that the Federal Government not prevent us from making the best use of our own revenue base; where we are asking not that the Federal Government spend money but that it put its backing behind its decisions so that we can spend our money. I think the case for this legislation is one that can be accepted by reasonable men.

If passed, H.R. 8882 will: Affirm the principle that the Federal Government should not intervene to prevent the collection of State and local taxes; make it possible for State and local governments to come much closer to the timely collection of the more than \$400 million owed to them by Penn Central; and bring significant stimulation to the Nation's most troubled regional economy and needed assistance to the cities with the most serious fiscal problems.

Rarely can so simple an act bring so many benefits. I think that principle, practicality, and good sense recommend the passage of H.R. 8882. Thank you.

Now, supplemently speaking as mayor of Trenton, my city is among the many old central cities of America's Northeast region which are struggling to compete with the flourishing communities of the Southern region for the industrial activities and capital investments which under present systems of governmental finance are the cornerstones and the foundations of a municipal property tax base.

In order to provide vital services to our ever-increasing share of America's indigent population, we are forced to compete for every scrap of funding available from Federal and State agencies—funding which is absolutely necessary to supplement the revenue available from an ever-dwindling real estate tax basis. It is against this backdrop that I state the position of the city of Trenton with respect to the merits of H.R. 8882 which, simply put, would guarantee full payment of the approximately \$90,000 in back taxes owed by the Penn Central Transportation Co. to the city of Trenton.

Our State of New Jersey is owed all told about \$41 million. From all the information available to me at the present time, it would appear that the pending bill is the only realistic means of avoiding that which amounts to a forced tax abatement for the former rail carrier in our region of the country.

H.R. 8882 represents therefore the hope that the cities represented here today will not be forced to subsidize a portion of the Nation's transportation system.

To a mayor who has for many years complained as vigorously as possible of the inequity of our present burden in having to meet the needs of the indigent citizens of this country who inhabit the central cities primarily because of the availability of our social services and other conveniences, the prospects of having to subsidize rail service, which really represent a national problem at this point, are unthinkable.

H.R. 8882 not only represents the opportunity to escape the otherwise tax abatement, but it does so without resorting to direct Federal subsidy.

I urge favorable consideration of H.R. 8882 by this committee, and in doing so I speak not only for the National League of Cities but for our city council, I have a resolution with me adopted by the city council and also for the New York Conference of Mayors which I serve as president and which also adopted a supportive resolution.

Thank you.

Mr. ROONEY. Thank you, very much, Mayor Holland.

On page 5 of your statement, you state that \$400 million has been kept out of the economy in the past 7 years, and the impact has been on the regions which have been under the most severe fiscal stress.

I might say at the same time we did keep a bankrupt railroad from going bankrupt to serve the economic needs of the people of that community. I happen to live in the heart of that area.

Mr. HOLLAND. There is no question about that.

I was in the command post of the National League of Cities when we were fighting for general revenue sharing. I fought for the public works program and most recently for a formula more oriented toward need with regard to community development money.

So I recognize that the Federal Government rescued a vital national service, but ironically almost all these stops along that line are the old central cities where we have been asked in recent decades to meet national needs.

For example, in our city of Trenton we have over 2,000 public housing units. There are no public housing units in towns surrounding our city. It is typical of the problems of the central cities.

In States like ours which until this year had no income tax and an urban State in the Nation it is especially difficult. Without the aid you have given us, we could not have survived literally.

Mr. ROONEY. Mr. Skubitz.

Mr. SKUBITZ. You just got around to getting a charter assessing an income tax in New Jersey; is that right?

Mr. HOLLAND. I was the only mayor in New Jersey—I have been mayor off and on since 1959—who advocated an income tax. We finally got it through. If Byrne is defeated in the next election, we will have a disaster in our State. Twenty municipalities will go to the State and say, "Take our cities, we can't run without it."

Mr. SKUBITZ. Mayor, you speak of forcing the city to accept responsibility national in scope. Are you referring to the welfare program now? Is that what you are talking about?

Mr. HOLLAND. Twenty percent of our population is ADC, aid to dependent children. That is because 90 percent of the counties cases—we are 1 of 13 municipals in the county—are housed in Trenton. They have been automated out of jobs in the South. They head North. They can't pitch a tent on a wide suburban lawn. They head for the cities and crowd in.

We were one of the strong cities, once a national capital. Today we don't have a self-sufficient people. We have disproportionately large numbers of dependencies.

I am here to get \$45,000 more because we need every dollar we can get.

Mr. SKUBITZ. We have a different problem here, too. I would like to visit with you on that one on the welfare program. I think something ought to be done.

Mr. HOLLAND. I think the Federal Government should assume to total responsibility for welfare, and our State government, allowing as much independent judgment as possible at the local level, assume responsibility for education costs. Those are the two major costs that are killing us. Then we could continue somehow.

Mr. SKUBITZ. I don't think it is our responsibility until the States do the best they can for themselves, and I don't think New Jersey did if they didn't have an income tax.

Mr. HOLLAND. They have not. The State of New York has been derelict.

Mr. SKUBITZ. They didn't have the guts to go and charge a tax, that is it.

Mr. HOLLAND. May I say this. If the nature of our population hadn't changed in the old central cities, we would not need an income tax. We are the fifth richest State in the Nation, 567 municipalities.

If we could adjust the socioeconomic imbalance in the central cities and have proper valuation of our real estate, we would not need an income tax.

In Bergen County, it costs \$50,000 to buy a lot and another \$50,000 to put up a house. There is a Ford plant nearby where only 15 employees can afford to buy a house there.

Incidentally, they share in general Federal sharing. They build bridle paths with it.

Mr. SKUBITZ. Those people are people who came in because of the construction of the plant.

Mr. HOLLAND. No; they are people who want to live in a suburban community. I am sure that plant helps them keep their tax rate down, but the tax rates are no problem to them. The tax rate as an indicator is misleading.

Princeton Township can afford to have a high tax rate. They can supplement their education program and can afford to pay for them. The cities that most need money for education, for example, are those who are least able to advance them.

Mr. SKUBITZ. That is all, Mr. Chairman.

Mr. ROONEY. Thank you, Mayor Holland, for your very fine statement, and I commend you for your forthrightness with respect to the taxing of income in the State of New York.

Of course, Pennsylvania does have an income tax. They have had it for the past several years, and we still have that financial dilemma facing us.

We rely on mayors like yourself to cut back so that the Federal Government won't have to send that money back to Trenton and the other cities in the country.

Mr. HOLLAND. We had to lay off 59 policemen and we need policemen.

I said any raise has to come from the reduction of the work force. We don't want to go the way of New York. We still have the highest bond rating of any of the big cities because of that.

Mr. ROONEY. Thank you very much.

Mr. SKUBITZ. Why go to policemen? Why don't you go to some of the other jobs?

Mr. HOLLAND. We didn't lay them off. The policemen had a choice of raise or laying off. They laid off their brothers.

The firemen did not. We left it up to the employees.

Mr. SKUBITZ. I think we ought to send you around the country to talk to them.

Mr. ROONEY. When are you up for reelection?

Mr. HOLLAND. Next spring.

Mr. SKUBITZ. Are you sure you don't want these remarks expunged?

Mr. ROONEY. Thank you, Mayor.

Gentlemen, you may proceed.

**STATEMENT OF CHARLES H. MERRILL, ASSISTANT COUNTY EXECUTIVE, ONONDAGA COUNTY, ON BEHALF OF THE NATIONAL ASSOCIATION OF COUNTY ORGANIZATIONS**

Mr. MERRILL. Chairman Rooney, I am Charles H. Merrill, assistant county executive, Onondaga County, New York State.

Congressman Rooney, we would like to express our appreciation to you for being able to appear here today.

I have a short statement.

I am pleased to testify before you on behalf of the National Association of Counties (NACo),<sup>1</sup> to urge your adoption of H.R. 8882 amending the Regional Rail Reorganization Act of 1973.

I am Charles H. Merrill, assistant county executive of Onondaga County, N.Y. The taxpayers of Onondaga County and hundreds of other counties, cities, States, and school districts in 15 States and the District of Columbia, have been severely impacted by the Federal Government's intervention in the Penn Central reorganization. County officials believe there should be a coordinated Federal-State-local effort to return rail service to its appropriate place in a balanced national transportation system. The Federal Government has intervened in the Penn Central Railroad's operations. Therefore, we believe there is a Federal responsibility to guarantee that local property taxes are paid by Penn Central. Thus, we support H.R. 8882—and identical bills—which will provide a Federal guarantee that counties will eventually receive full payment for taxes owed by Penn Central, and other railroads being reorganized.

Since 1970, when the railroad filed for bankruptcy, the Penn Central has paid no State, county, city, or school taxes, and in many areas there were delinquencies before that time. It is estimated that the total taxes owed are more than \$500 million.

Penn Central owes Onondaga County for the period 1971-76, \$1,437,774.64, which includes \$48,708 in interest and advertising costs. There is an additional \$1,231,878.52 owed to the county and State by Penn Central for grade-crossing elimination charges.

The Penn Central's unpaid taxes amount to \$2,669,653.16, which is 31 percent of the total \$8,638,239.74 of uncollected taxes owed to the county. The financial impact of these unpaid taxes has become increasingly severe in Onondaga County, especially since 1974. The cost

<sup>1</sup> The National Association of Counties is the only national organization representing county government in the United States. Through its membership, urban, suburban, and rural counties join together to build effective, responsive county government.

The goals of the organization are to: improve county governments, serve as the national spokesman for county governments, act as a liaison between the Nation's counties and other levels of government, and achieve public understanding of the role of counties in the Federal system.

of county government greatly increased in 1974 due to high unemployment and inflation. It was necessary to significantly increase property taxes to provide needed human services and to offset the uncollected taxes.

The county legislature is now considering a 1978 budget of \$243.3 million proposed by the county executive. If the budget needs are to be met an increase of \$5.48 in the adjusted basic county tax rate will be required, bringing the rate to \$44.55 per \$1,000 of assessed valuation. If the county were to receive the net amount of \$1,389.-066.52 owed by Penn Central, there would be a reduction of \$1.02 per \$1,000 of assessed valuation.

Onondaga County has a population of 475,000 and is the sixth largest county in New York. We feel this legislation is especially important to our county because the Northeast region of this country has been the slowest to recover from the recession and our local property taxpayers are carrying the additional burden of these unpaid railroad taxes.

In 1973, Federal law required the railroad to continue operating with tremendous losses. Federal loans were made to the Penn Central to partially cover these losses. We do not question the determination that in the national interest Penn Central operations need to be maintained. We do question the Federal determination that counties and other local taxing authorities should be forced to bear a large part of the financial burdens caused by this Federal policy.

Unless H.R. 8882 is passed before October 19, 1977, counties will be forced to accept either a small cash payment of 44 to 50 cents on the dollar now, or under the reorganization plan 20 percent now and the remainder in notes payable in 10 years, after all Federal claims are paid. There is no guarantee that the funds would be available in 10 years to meet the obligations incurred by the notes.

If counties accept 44 to 50 cents on the dollar, and one considers inflation and the loss of interest, it is estimated that we will receive (in real dollars) only 10 percent of the amount owed.

H.R. 8882 assures that counties will be paid in full by guaranteeing the Penn Central notes. The National Association of Counties urges Congress to enact this bill which recognizes that the Federal Government's intervention in the Penn Central's operations has worked a hardship on county property taxpayers.

Mr. ROONEY. Thank you very much, Mr. Merrill.

**STATEMENT OF LOWELL B. DAVIS, SECRETARY/TREASURER,  
EUCLID BOARD OF EDUCATION, ON BEHALF OF THE INTERNATIONAL ASSOCIATION OF SCHOOL BUSINESS OFFICIALS**

Mr. DAVIS. Mr. Chairman, members of the committee.

My name is Lowell Davis, representing International Association of School Business Officials of the United States and Canada.

Thank you for the opportunity of being able to present some of my views concerning the Penn Central local government tax situation as it relates to House Resolution 8882. The International Association of School Business Officials of the United States and Canada is composed of treasurers, business managers, and administrators employed by local school districts in the United States and Canada.

We, you might say, are in the trenches daily accounting to our citizens and to our various government agencies for the fiscal and business operations of the local school district. Some of the facts I put forward today are not new to the members of this committee, but I believe they bear repeating.

The property tax in the United States is, and has been, under attack from all quarters. The property tax revenues collected in the United States in 1976 represented 80 percent of all revenues for the support of local governments across the United States.

The property tax is the bullwark of the public schools from coast to coast in the United States. In 1976, nearly 81,000 local government units and special assessment districts collected approximately \$60.5 billion in property tax revenues—60 percent of those revenues collected or approximately \$36 billion went to the support of local education. Without the property tax, local education would cease to function.

Persons across the Nation in recent years have seen their property taxes take fantastic increases. Persons in California, Illinois, and Ohio have seen property taxes increase as much as 300 percent in a single year.

Persons in various States that have dared to propose increases in property taxes to support local city and school services have had irate taxpayers threaten to do everything, even to the point of threatening to tar and feather those persons supporting such measures, as happened in Bucks County, Pa. Since Massachusetts began collecting the property tax annually in 1646, that tax has been classified as unfair or the least fair of those taxes we commonly associate with modern revenue sources for local government agencies. That relief is needed in the property tax area is an accepted fact. Most of our taxpayers have been generous in their support of local education if they know businessmen and homeowners alike are paying their fair share. The schools of our Nation are facing fantastic increases in costs. These costs can be associated with the same pressures that the local businessmen face or for that matter, that the local homeowner faces.

For instance, the school system in a locale is usually one of the largest preparers of food for student and adult consumption. And the associated price increases for food and food preparation have hit us all. The increased costs of new mandated programs, either federally or State-sponsored have had their impact. Whether these rules pertain to pollution control, safety apparatus, hiring practices, et cetera, does not matter. It is common for the schools to be mandated to undertake programs in driver education, sex education, racial education, care for the retarded and bedridden child, et cetera. These are, to name a few, some of the mandated school facilities for the use of the retired, handicapped, and other special local groups who are also driving school costs up. It is not to say that these programs are not good, just and should be accomplished. The difficulty is in trying to finance these programs that are mandated with locally supported property tax revenues and explaining these tax increases to the public.

Schools are closing. Schools in big cities and small cities, townships, and crossroads are closing because of the lack of public support of the property tax and the citizen's mistrust of the concept that everyone is paying their share. We have all read of school systems such as

Toledo and Cleveland, Ohio, as well as schools in other States that have closed or are anticipating closing in 1977. Why are schools closing? There are many reasons, but the root of the problem is a lack of financial resources to keep the schools open. The Federal Government has stepped in time and time again with programs to finance special programs for large and small schools to accomplish a particular end.

If the public confidence of the local property tax for local education continues to erode as it has in recent years, the Federal Government and State governments will be thrust into the arena of the financial dilemma that many of our U.S. schools find themselves in today in 1977.

The *Penn Central* bankruptcy case, as it relates to property tax payments to local governments, is just another log that is being put on the fire of property tax discontent and mistrust in many States in the Midwest and eastern seaboard. In its simplest terms, the alternatives left to local governments and schools to select either the tax compromise or plan of reorganization set forth by the Penn Central trustees will have a significant impact on local school districts in those States involved.

The plans for possible settlements of outstanding taxes with local governments, as you know, may take one of three courses of action. The local government may choose to accept 44 percent of all taxes owed and forgive the balance if taxes were owed prior to the filing of the Penn Central reorganizational measure with the Federal courts. Second, if no taxes were owed at the time of the filing of the reorganizational measure, the local government may accept 50 percent of the taxes owed and forgive the balance. The third alternative deals with the local government agency accepting 20 percent cash of all taxes owed and the balance in notes backed by the Penn Central reorganizational plan. If we look at measures 1 and 2, we can see that the local governments are asked to forgive taxes payable by Penn Central in excess of millions of dollars.

If either option is taken by the local government agencies, who will make up the \$340 million that is owed to these local governments? The plain fact is that those taxpayers still residing in the school district, city, or township will have to absorb and pay out of their own pocket the dollars that are being forgiven Penn Central. Will the local taxing districts accept this additional burden? In many cases, the local citizen will have little to say about the acceptance or rejection of the proposal.

The city and school services must go on, probably at a reduced level of competency, surely at an increased level of burden to the local homeowner, the local businessman, and the local government.

Option No. 3, that of granting 20 percent cash of all taxes owed, and the balance in long-term notes, would seem to be the most advantageous. The resolution before you deals with that option. That option has one major defect. The school districts and local governments in the affected States are in trouble today. They need help today. They have financial demands which are outstripping their resources today. The schools in many locales are closing in 1977-78.

The schools are being placed in a position where the effective use of the carrot-and-stick routine is real. Some school districts in order to keep their doors open in 1977-78, may have to accept the compromise

in order to get as much cash as possible to alleviate their financial condition and hopefully stay open a few more days, months or possibly the year.

While they would wish to take the reorganizational plan with the hope of recouping those property taxes that were legitimately levied and in most instances, reflect the will of the local taxpayer to tax themselves, they cannot wait. They need the funds today. If the reorganizational plan could be exercised in such a way that a cash consideration of 20 percent would be forthcoming, plus high grade marketable securities could be secured for the balance of the taxes owed, the school districts would not be faced with the carrot-and-stick alternative.

The market for Penn Central notes is questionable. If a market would exist, surely that market would penalize the face value of those notes so that the local taxing district, if upon receipt of the notes, would try to borrow, using the notes as collateral, or would try to sell the notes on the open market, they would, in the opinion of those persons in the financial field, receive less than face value for the notes and consequently less than the amount of the taxes owed. Can the local governments afford to gamble on that market? Can the local governments dare turn down a partial cash settlement? Can the local schools afford to close, knowing that a partially paid tax debt to the local government agency from Penn Central might possibly keep their doors open for a period of time? Those questions, all of us in the trenches in the local school districts, have to face.

Many of our school districts have a significant population of retired workers. There is a second significant group of taxpayers who do not have children in our local schools. What do we tell these persons? The retired person knows that if his property taxes are not paid, the local taxing authority will take his house and will sell it to satisfy the taxes owed.

The young couple that is in their first home and are burdened with an impossible mortgage payment and property tax payment, how do we tell these people that the Penn Central Corp. can be forgiven their delinquent taxes, but they cannot have their taxes forgiven? In our urban centers and in our suburban, urban centers, I tell you quite frankly, our public will not understand. Our public is scrutinizing every penny going to the local government agencies, as they should. And many of these local taxpayers have been generous in the past with their support of the local school property tax measures. Increasingly, their support is dwindling. It is not uncommon for a local school district to try five, six, and seven times before a successful property tax levy is passed, if it is passed then. My local school district property tax measure was submitted five times. The tax was reduced three times before the local citizens felt they could accept the additional burden. How do I tell my citizens that they must absorb an additional burden because the Penn Central Corp. could not pay their taxes, and in fact are having a portion of their taxes forgiven?

I would submit, Mr. Chairman, that the citizens will not understand. And by not understanding, will express their displeasure and criticism at the polls when we surely go back to them for additional school support.

If we could have a positive reaction to House Resolution 8882, it is our belief that we would have a cash settlement with the balance in marketable securities which could be sold without a significant eroding of the face value of those notes and we could receive the property tax owed now which would go a long way to restoring our citizens' faith in a tax that is levied on property and should be paid by everyone equally.

I thank you, Mr. Chairman.

Mr. ROONEY. Thank you very much, Mr. Davis.

I do feel that the Federal Government has done much in the past 5 or 6 years to help alleviate the local school district problems and for that matter many of the municipalities.

Just several weeks ago we announced a \$4 billion ETA grant to the community. We have given billions of dollars to the local municipalities in the form of revenue sharing.

Now, I do think at this time it would be very difficult for the Congress to accept an additional half billion loan guarantee. I do appreciate your very fine statement, and I can assure you that this committee will give this matter its prompt attention and will act immediately as to whether or not the testimony of all of the witnesses who appeared before this committee is valid.

Mr. DAVIS. Thank you, Mr. Chairman.

Mr. ROONEY. Now, has the mayor of Trenton arrived?

FROM THE AUDIENCE. No.

Mr. ROONEY. He must have come on Amtrak.

FROM THE AUDIENCE. He did.

Mr. ROONEY. The next panel will be the Treasurers and Auditors Panel: Mr. Carl E. Eastwick, assistant attorney general, State of Maryland, Baltimore, Md.; Mr. Daniel R. Pellegrini, assistant city solicitor, city of Pittsburgh, Pa.; and Mr. Newell Cook, deputy treasurer, city of Boston, Mass.

The record will be kept open for the mayor of Trenton immediately following the previous panel.

You may proceed.

**STATEMENTS OF NEWELL COOK, DEPUTY TREASURER, CITY OF BOSTON; CARL E. EASTWICK, ASSISTANT ATTORNEY GENERAL, STATE OF MARYLAND; AND DANIEL R. PELLEGRINI, ASSISTANT CITY SOLICITOR, CITY OF PITTSBURGH**

Mr. Cook. My name is Newell Cook of Boston, Mass. I am assistant collector-treasurer of the city and am charged with the responsibility for collecting its taxes. I appreciate this opportunity to testify to H.R. 8882.

I strongly believe that this legislation provides an equitable solution to the tax collection issue facing Boston and other taxing authorities, which has arisen from the bankruptcy of the Penn Central Transportation Co.

The details of the bankruptcy and the subsequently accrued tax claims have been dealt with in prior testimony, so I will limit my remarks to this summary of the situation in Boston:

One, we have accrued tax claims in excess of \$11 million and in addition interest to date of approximately \$6 million.

Two, the compromise offer is for \$5.6 million and thus is about 32 percent of the total the city is due.

Three, the bankruptcy court has separated the land taxed from its liens, which has denied the city its normal remedy for collection.

Four, the court has barred the use of any of the other collection remedies.

Five, it is politically and fiscally impossible for the city of Boston to accept this compromise. Our property taxes, the highest in the country, have risen 28 percent in the past fiscal year; and the city's tax collection policy has been to refuse to accept less than 100 cents on the dollar from any delinquent.

We therefore look to the reorganization plan which offers the full discharge of the Penn Central obligation which we need and which we deserve. This reorganization plan is, in our opinion, a carefully drawn and responsible program for balancing all of the interest and claims of the creditors, with one exception. The securities offered to the local taxing authorities under the reorganization plan, are not marketable except at a heavy discount. Therefore, our desire to work within the reorganization plan is thwarted.

The securities, we believe, will ultimately be paid in full. However, we would have to hold the securities until they were marketable to realize the cash we need. We operate on cash and are not in the position to manage the portfolio of securities the plan offers us. This uncertainty, then, of when the securities' full value can be realized is the only barrier which prevents us from accepting the plan.

We have come to Congress then to seek a remedy whose only purpose is to make these securities marketable at full value. The proposed guarantee is not intended to interfere with the plan; indeed, it should promote the plan. It is not intended to put the U.S. Treasury at risk, as we believe these securities will be paid in full.

Nor is it intended to challenge or alter the public policy and congressional intent underlying the Rail Reorganization Act. Its sole purpose, again, is simply to allow the taxing authorities to realize full value from these securities when they are issued.

I strongly urge prompt and favorable action on the part of the subcommittee so the affected taxing authorities can realize the taxes due them.

Thank you, Mr. Chairman.

Mr. ROONEY. Mr. Cook, can you talk about full value? If it is not possible for your tax authorities to accept a compromise for a tax debt, as you pointed out, politically and otherwise, why is it possible for you to take a security offered in payment for a tax debt and discount it in the open market?

Mr. Cook. I am saying it isn't. I am saying we are caught between the rock and the hard place on the issue. We have a compromise plan on the one hand which is a discount down to 32 percent of the tax value.

On the other hand, we have a reorganization plan which requires selling the securities at a discount. Neither works for us. So we are asking for the Federal guarantee in order to make the securities marketable at par.

Mr. ROONEY. Do you think you can market them at par?

Mr. COOK. With the guarantee; yes, sir.

Mr. ROONEY. Many of the other witnesses who have appeared before this committee yesterday said that was almost impossible, and their intention was to sell them at a discount.

Mr. COOK. Without the guarantee, they would have to be sold at a discount if they could be sold at all. With the Federal guarantee, it is our opinion that they could be sold at par for full value.

Mr. ROONEY. Thank you very much, Mr. Cook.

### STATEMENT OF CARL E. EASTWICK

Mr. EASTWICK. Mr. Chairman, my name is Carl Eastwick; I am assistant attorney general for the State of Maryland. For the past 2 years, I have been representing the interests of the State of Maryland in the proceedings for the reorganization of the Penn Central Transportation Co. and certain affiliated bankrupt railroads.

The State of Maryland possesses estimated claims for corporate and other nonproperty taxes in a principal amount estimated to be between \$4 and \$5 million.

In addition, the office of the attorney general of Maryland has been authorized to represent approximately half of the county and municipal taxing jurisdictions located in Maryland, which possess tax claims for unpaid property taxes owed by the Penn Central and affiliated bankrupt railroads. None of these taxes, neither the State corporate taxes nor the local property taxes, have been paid since the middle of 1970.

Mr. Chairman, I would now like to describe the litigation and legislative history of the reorganization of the Penn Central in order to attempt to put H.R. 8882 in some perspective and contrast how the local taxing authorities and State taxing authorities have been treated in contrast to other high priority creditors.

The petition of the Penn Central for reorganization was approved for filing on June 21, 1970. Three months later, the court directed the trustees to defer the payment of taxes which would normally accrue during the reorganization proceedings. I have to emphasize it is the normal rule according to the court that these taxes would be paid as accrued.

The objections of a number of taxing authorities to that order were overruled on appeal. The opinions rendered by the court in approving the tax deferral order did not, however, question the validity of the claim of the taxing authorities that taxes accruing during reorganization are administrative expenses entitled ultimately to share pro rata with all claims within the first priority, meaning simply that those taxes must be satisfied out of the available assets of the debtor before any other creditors may be paid. Other claims sharing this first priority status are claims for compensation of the trustees, along with their consultants and legal advisers. Certain other creditors which extend credit to the debtor while in reorganization are also entitled to a very high priority.

Notwithstanding the deferral of the payment of taxes and other expenses of administration, the financial position Penn Central continued to deteriorate until, in 1973, it became apparent that further

attempts to reorganize the bankrupt railroad under the bankruptcy laws would be fruitless. Consequently the trustees were given until July 2, 1973, to file either a feasible plan for reorganization of the railroad, or their proposals for liquidation or other disposition of the enterprise.

I might add that if the enterprise were liquidated, the taxing authority claims as well as other first priority claims would probably be paid in full.

The evidence demonstrating that there was no alternative to the piecemeal liquidation of the Penn Central system was overwhelming. I quote from the Senate report concerning the rail reorganization legislation introduced when it became apparent that the existing bankruptcy statutes were inadequate to deal with the massive problems of the Northeast railroads:

The ability of the Penn Central Railroad to maintain operations under reorganization is critically dependent upon its ability to generate sufficient positive cash flow to sustain working capital needs, cover maturing equipment obligations, and pay for essential maintenance and capital expenses. In this most critical area, Penn Central continues to falter. It has been unable to develop a consistent positive cash flow despite court-ordered deferment of payments on debt interest, lease-line rentals, and property taxes, and the railroad's continued deferment of maintenance and capital expenditures.

As a result, the Penn Central's liquidity position (the ability to service short-term expenses) continues to wear thinner, with cash balances on the decline, and working capital standing at a deficit balance. This continued deterioration of liquid resources as a result of inadequate cash flow increases the prospect for cash crisis by the first quarter of 1974, which could precipitate a complete shut-down.

The remedial legislation, the Regional Rail Reorganization Act of 1973, was designed to provide a legislative solution to the Northeast railroad crisis, established the United States Railway Association to supervise the creation of a viable railroad network, and authorized the creation of ConRail, the railroad which would succeed the Penn Central as the preeminent railroad in the Northeast region. In launching this enterprise, Congress was very generous in its treatment of many of the creditors of Penn Central whose extension of credit enabled the debtor to continue its rail operations during the reorganization. The Regional Rail Reorganization Act of 1973 was twice amended in 1976 to provide Government guaranteed loans to ConRail so that ConRail could pay the accrued unpaid operating debts incurred by Penn Central prior to the transfer of railroad operation.

Among the creditors benefited by those loan guarantees were the suppliers of materials or services utilized or purchased in current rail operations; shippers who incurred losses as a result of current rail services; railroads to whom the Penn Central owed current interline accounts and other current accounts and obligations; employees of the railroad having claims for personal injuries and for pension and welfare benefits; persons having claims for personal injuries suffered during the reorganization period; and Amtrak, which possessed certain claims arising out of contracts with the Penn Central trustees. The taxing authorities, other than the United States, who also subsidized the continued rail operations of the Penn Central to the same extent as those who were benefited by the 1976 rail amendments, were overlooked. Moreover, the United States Railway Association

was afforded super priority over other administrative claimants, including State and local taxing authorities, under the terms of the reorganization legislation. Therefore, the normal rule that all administrative claimants share as one class pro rata in the distribution of the available assets was legislatively overturned.

In order to reorganize the remnants of the Penn Central system, the trustees must come to terms with the taxing authorities who have received virtually no tax revenue from the debtor during the 7 years that it has been in reorganization. The trustees have made two proposals. Under the first proposal, the trustees would pay only one-half of the amount of each tax claim (excluding interest and penalties), or \$10,000, whichever is greater.

The second proposal, which is included in a proposed plan of reorganization, provides for immediate payment of 20 percent of the principal amount of each tax claim in cash upon the consummation of the plan, with the remaining 80 percent of the principal plus all of the interest to be paid through the issuance of secured notes which would have a relatively high claim upon certain of the available assets of the reorganized company. Only those taxing authorities desperately in need of immediate cash could intelligently opt for the 50-percent compromise proposal.

Admittedly, the enactment of Federal guarantees for the secured notes would be of little benefit to those taxing authorities which are desperately in need of the maximum amount of immediate cash. The plan of reorganization, as presently constituted, would provide them with only cash in the amount of 20 percent of the principal amount of their tax claims. For the large number of the taxing authorities with less immediate needs, the Federal guarantees for the secured notes would make the risk analysis of those securities much simpler.

To that extent, I would anticipate that many more taxing authorities would opt for the plan of reorganization proposal if Federal guarantees for the secured notes were enacted. By that simple measure, Congress would insure that a larger number of taxing authorities would be able to maximize their recovery of taxes which have been so long deferred, and, indeed, ignored.

#### STATEMENT OF DANIEL R. PELLEGRINI

Mr. PELLEGRINI. My name is Dan Pellegrini and I am first assistant city solicitor for the city of Pittsburgh. I am in charge of the litigation for Pittsburgh concerning the Penn Central bankruptcy and have been active in efforts to secure support for House Resolution 8882.

The city of Pittsburgh has a substantial interest in securing the passage of this bill since it would insure that the city and its other coextensive local governments would receive the substantial amount of money owed to them. In total, this amount is approximately \$13 million, out of which \$7 million is owed directly to the city of Pittsburgh. It must be emphasized that these amounts largely represent post-bankruptcy claims on property that was used for nonrailroad purposes. Under the bankruptcy law these claims are of the highest priority since they are administrative expenses.

Over the past 2 days you have heard the testimony of a number of witnesses concerning the history of the bankruptcy as it relates to the

nonpayment of taxes by the trustees of the Penn Central, the detrimental impact that their nonpayment has had on local taxing bodies and the beneficial effect that this bill will have in alleviating the detrimental impact. I would like to address myself, however, to the actions that the Federal Government has taken or failed to take which have allowed these taxes to remain unpaid and the actions it took that would force the local taxing authorities to accept Penn Central notes rather than payment in cash as other taxpayers are required to make.

Before addressing myself to the responsibility of the Federal Government in this matter, I would like to impress upon you that our request is completely dissimilar to the requests for a guarantee of notes or bonds. We are not seeking a "bailout" which was the nature of the legislation concerning Lockheed or New York City. The affected local taxing bodies are not in the predicament they find themselves because of profligate spending or any action on their part but because of, in part, the actions of the Federal courts and Government. The passage of this legislation will not provide bonus tax revenues but will assure prompt repayment of taxes that other taxpayers have been forced to make up for 7 years.

In the actions taken by the Federal Government since the Penn Central went into reorganization, the Government has advanced the position both in the courts and in legislation, that it was in the national interest for the Penn Central railroad to continue operating. The basis for this national interest was the realization that the nonoperation or a breakdown of any segment of the nationwide integrated rail network would bring chaos throughout the Nation. In fact in a declaration of policy in the Regional Rail Reorganization Act states just that, that this bill was passed because it was in the national interest and, as I recall yesterday, Chairman Rooney made that same statement in his opening remarks in these hearings.

This is illustrated by the fact that when the trustees proposed liquidation, the Federal Government opposed the liquidation knowing full well the distressing effects that such action would have on the Nation. Not only did it force the trustees not to liquidate, the Congress authorized over \$500 million in loans for its continued operation. Moreover, it created the Consolidated Rail Corporation to insure that the country continued to have a national railway system since the trustees seemed either incapable or unwilling to continue the rail operation of the Penn Central Co.

However, in pursuing this laudable Federal policy, certain actions were taken both administratively and legislatively that effectively deprived local municipalities of the prompt payment of their much needed taxes. The Regional Rail Reorganization Act contains several provisions that adversely affected the collection of taxes by local taxing bodies. This act provides hundreds of millions of dollars to the railroad. While this act authorized that other administrative expenses could be paid, such as the salary of the trustees and legal fees, it forbade the payment of local taxes. While this provision produced the initial shock of the continued denial of the immediate payment of local taxes, another provision of the act has proven to be even more disastrous to local taxing bodies.

This is the provision in the Regional Railroad Reorganization Act which requires that the loans made by the Federal Government to the

Penn Central must be repaid prior to anyone else receiving money that is owed to them. The effect of this provision has been to stop payment of postbankruptcy taxes owed by the trustees to local governments.

In a meeting with Brock Adams, the Secretary of Transportation, and representatives from a number of cities affected by the nonpayment of taxes, the Secretary stated that when, as a Congressman, he helped draft the Regional Railroad Reorganization Act the purpose of this provision was not to deprive State and local governments of their taxes but to prevent shareholders and large institutional investors, who had prebankruptcy claims, from receiving any money before the Federal loans were repaid. In large part this provision has backfired. It was used as a shield by the trustees not to pay their taxes because the trustees said that they could not pay local taxing bodies until they had repaid the Federal Government's loan.

After ConRail took over the operation of the railroad, the Federal Government could have forced the trustees from this position because of the enormous leverage that the Government had as a result of the trustees' obligation to repay immediately the \$500 million which the Government had advanced to the Penn Central. The leverage was strengthened by a provision in the Regional Rail Reorganization Act that allowed the Secretary of Transportation discretion on how the loan was to be repaid.

Instead of using the leverage for a purpose that was advantageous to help repay local taxes, it was used to formulate a compromise with the trustees resulting in a plan of reorganization that is the sword with which the trustees are attempting to deprive the local governments of their taxes and enrich the shareholders of the reorganized company.

A recounting of how this occurred was supplied in affidavits filed in the bankruptcy court in Philadelphia. These affidavits state that representatives of the Friday morning group, which is composed of the trustees, banks, and other large institutional investors, met with representatives of the Department of Transportation to work out a compromise on the repayment of Government loans. The compromise was reached and was approved by Secretary of Transportation Coleman on December 26, 1976.

Interestingly enough, this settlement dealt with other matters that also accrued to the benefit of the Friday morning group.

Beside the resolution of the matter of the loans, the settlement contained a provision that would allow a compromise of, among other things, postbankruptcy taxes owed to local taxing bodies. It provided that local taxing authorities were to receive only 50 percent of the principal of their claim, and did not allow anything for penalty and interest. This provision of the compromise was completely superfluous to any claim that the United States had for the repayment of its loans. Why the Department of Transportation, if it wanted to deal with this matter, did not demand full payment of the local taxes, including penalty and interest, is completely incomprehensible.

Even more incomprehensible than the result of this compromise is the method by which it was reached. As stated, while the Department of Transportation met with the Friday morning group, the large prebankruptcy creditors, it never even consulted with local governments

as to whether the compromise was acceptable. Contact with representatives of State and local governments would not have been difficult since there is in the possession of attorneys for the Government, an official list of individuals to contact. It appears, however, that they did not want any input from local governments, since when a large number of cities and States expressed their opposition, the Federal Government joined forces with the trustees to have the compromise approved.

This compromise has been a disaster to the efforts of State and local governments to receive full payment of their taxes.

In dealing with the trustees, the State and local governments are confronted with the trustee's position that they cannot offer more under the plan of compromise because the Federal Government is now behind their plan. States and cities seeking taxes are now confronted with a union of the trustees whose conduct can be described at best as unbending, and seemingly disinterested Federal Government. This union puts the Federal Government in a position of telling beleaguered local governments to write off possible \$250 million in back taxes which dollars would accrue to the benefit of the reorganized company. This position, after local governments have subsidized the national rail transportation system, is unconscionable.

This involvement of the Federal Government does not end there. As the Government was aware when it entered into the compromise, it is the keystone of the plan of reorganization. Under this plan the notes are issued for which we are seeking the guarantee through H.R. 8882. Under this plan, the local taxing entities, after waiting 7 years, are now to wait a minimum of 10 years for their taxes. Without the approval of the plan by the Federal Government, State and local governments would have to be paid because no plan could sustain attacks by both State and local governments and the United States.

Federal responsibility in this area is not limited to actions that it took or failed to take which placed local governments in their dilemma. The Government has a responsibility to insure that inequitable burdens are not placed on the local governments to advance national goals.

As this committee is aware, demands on revenues of local governments did not diminish just because the Penn Central did not pay their taxes. Other taxpayers were required to pay more taxes to offset the loss of Penn Central revenues and, in effect, subsidize the operation of the Penn Central segment of the national rail system. Moreover, it was not the more affluent regions called upon to make this sacrifice, but the poorer Northeast and Midwest States. But more particularly, it was the poorer residents of the region, the residents of the central cities who were required to subsidize the national rail operation. Affluent suburban communities do not have railyards or warehouses in them. So in the last analysis, the burden fell on the poorest of the poor. To alleviate this situation where the poor are subsidizing the more affluent, calls for passage of this legislation.

In conclusion, the Federal Government has a great deal of responsibility for the plight of the local taxing bodies. With no cost on their part they can rectify this situation and pump \$500 million of private sector money into the economy.

I urge your favorable consideration of H.R. 8882.

Mr. ROONEY. Thank you very much, Mr. Pellegrini.

As I previously stated, the Federal Government has not been ignoring the needs of the local municipalities in this country and I have talked about the revenue sharing. I have talked about the EPA grants that came out several weeks ago, almost \$4 billion.

Let me ask the panel this question:

This has been going on, as you say, for 7 years and all of the witnesses the last 2 days have come here before the Congress after a 7-year wait.

What prompted all of the witnesses to come to Washington in the closing days of the 1st session of the 95th Congress to support this legislation?

Does anyone wish to comment?

Mr. COOK. It had been difficult for the taxing authorities to have anything to work against until the reorganization plan was proposed. The reorganization plan which we are suggesting would be attractive to the taxing authorities with the guarantee from the Federal Government is even yet not ordered. Therefore, we are in some sense at risk, even now, asking for this legislation whereby we could let the October 19 deadline come and go, the organization plan comes to naught.

It has been difficult for the taxing authority to deal with this monolithic bankruptcy as we are disparate, spread around the country and find it difficult to talk to each other. But until the reorganization plan was proposed we had nothing against which we could work in determining what resolution of our claims would be appropriate.

Mr. EASTWICK. Mr. Chairman, if I might add a few remarks.

We didn't learn until December 1976 the intention of the trustees to take care of this tax liability. We learned for the first time then that they planned to issue secured notes in partial payment of that liability.

The first plan of reorganization offered a package of secured notes which was even less favorable than what we are getting now. We attempted at that time through an informal group of taxing authorities to negotiate with the trustees, to see if we could get a better deal voluntarily with court approval.

The trustees did come up with a better deal. They offered us 20 percent cash and a slightly more favorable package of secured notes.

We attempted to further negotiate with the trustees and when it became apparent that those negotiations would become fruitless it was at that time we turned to what we considered to be one of our last alternatives and that is to turn to Congress to see if we can get Federal guarantees.

Mr. ROONEY. Mr. Skubitz.

Mr. SKUBITZ. Mr. Chairman, I regret very much I have not had an opportunity to read this testimony. Had it been sent in before today or not? It is rather difficult to ask questions when you sit here and listen to witnesses. Any reason why you didn't have your testimony in beforehand.

Mr. PELLEGRINI. Mine was in, Mr. Skubitz.

Mr. SKUBITZ. Just listening to it, I am a little surprised. Mr. Pellegrini, how long have you been city solicitor for the city of Pittsburgh?

Mr. PELLEGRINI. Seven years but two years were spent in the Army. I have 7 years' credit.

Mr. SKUBITZ. When did you take over your position?

Mr. PELLEGRINI. As assistant city solicitor?

Mr. SKUBITZ. Yes.

Mr. PELLEGRINI. In November 1970. I went to the Army in January of 1971 and came back 2 years later.

Mr. SKUBITZ. I am asking that for a purpose.

How long have you been with the city of Boston?

Mr. COOK. The spring of 1976.

Mr. SKUBITZ. The reason I ask that is that I was rather shocked in listening to the testimony of you gentlemen. Apparently you don't know anything about the background of this.

As I recall, Mr. Chairman, when these railroads were going into bankruptcy we had representatives from all of these areas beating on out back door, "For God's sake, don't let this railroad system go down the drain by bankruptcy and close their doors because we are all in sad shape."

I can't remember a single person west of the Mississippi coming in and saying that it is in the national interest of this country to keep them going, for God's sake keep them going.

Now all at once nothing has been said about that. You wait until we do something, now you are sending in a new flock of fellows, saying "Boy, we want these taxes paid."

Mr. PELLEGRINI. I don't disagree with you that there was a crisis. There was a crisis when the Congress passed the Regional Rail Reorganization Act and helped the Nation when it took the action it did.

Mr. SKUBITZ. It helped the Nation. I am not saying it didn't. What I am trying to say to you is that I was beat over the back by folks out in that area saying, "Let them go down the drain, they got into this mess."

But in the interest of the Nation I moved ahead and I did things because of the urgency that ordinarily I wouldn't do.

Now you folks come in here saying, "We want the tax money."

Mr. PELLEGRINI. We agree with you. The difference is that when Gulf Oil or Exxon gave diesel fuel to the Penn Central they were paid.

Under the bankruptcy law, which is the congressional law also, taxes are administrative expenses. They should be paid concurrently with diesel fuel or the counsel fees for the trustees which are about \$440,000 a quarter and so on. They should be paid in the same framework. They weren't paid. What happened was that we had a national rail system that we are trying to get going because if you have lettuce in California that can't get to Pittsburgh it is going to rot in Chicago. This area of the Nation was required to subsidize it.

As my statement indicated it was the poor cities that had to subsidize this rail operation. In the city of Pittsburgh, except for a few portions of what we know as the old city, we don't tax rail properties. Our taxes are on property that was held for speculation by the Penn Central. This is very valuable property.

For instance, the general State authority of Pennsylvania in our behalf paid \$5.5 million for a small portion of the land they owned in Pittsburgh about 2 years ago to the Penn Central Railroad.

We could not get our taxes on that money. We are not saying that what you did was not extremely beneficial to the Nation. What we are

saying is in that crisis certain things occurred, especially administratively, that caused us not to collect our taxes which we expended in services.

We are just asking for money that is due us. We are not criticizing the Federal Government.

Mr. SKUBITZ. Should you not go to the bankrupts for this money? Why do you come to us? I thought we were stepping in the same position as the bankrupts stepped in. It seemed to me these are accumulations that took place when the railroad was in bankruptcy. Penn Central refused to pay the money, is that correct?

Mr. COOK. Penn Central was operating under the orders of the bankruptcy court.

Mr. SKUBITZ. They were still under the railroad?

Mr. COOK. Yes; under the general umbrella created by the reorganization Act these taxing authorities have foregone the payment of taxes in the past 7 years. This has been in the public interest and has served the public interest.

However, we have subsidized the reorganization of the surviving corporation to the extent of \$500 million.

Mr. SKUBITZ. They were precluded by us but in turn they were still liable for their taxes. They are getting some money out of this. Why don't you go against them?

Mr. COOK. That is what we would like to do. They have offered us out of the bankruptcy court securities to pay off their debt.

The problem for us is that these securities are not marketable. We are in a cash outlay business. We pay for services for our citizens. We need the cash to operate. We can't manage a portfolio of securities. We are not asking for Congress to put up any money. We don't believe it will cost Congress any money at all. What we are asking for is the guarantee from Congress that will make these notes marketable now so that local arrangements can be consummated.

The Penn Central has the assets to pay their taxes. The Federal Court in Bankruptcy has set up a program under which they are going to pay those debts. It does not work without the guarantee because those securities are not marketable for us. We don't want money from Congress. We want the guarantee which will enable us to sell the securities for cash to pay our bills.

Mr. SKUBITZ. I want to look into this. I have the deepest sympathy for the city of Pittsburgh because my hometown was named after Pittsburgh, Pa. But we dropped the "H"; we spell it correctly.

So I want to look into this further and see what your rates are if you have any. By the same token, I have been around this Hill for 34 years, not always as a Congressman, only 16. I could not have stood it for 34 years as a Congressman. I am nearly ready to leave the place. I have heard that old argument so many times, it is not going to cost Government a cent. Every time I think of it I look at this stadium out here and look at a few other things, the subway system, and a few others that were not going to cost us a cent either.

So I get a little suspicious of this "It is not going to cost you a cent" because anything worthwhile usually costs you something. I learned that years ago.

Mr. PELLEGRINI. Congressman, could I make one comment about that?

Mr. SKUBITZ. I have one other question to ask you.

Would you have the Government also guarantee every bankrupt, including W. T. Grant?

Mr. PELLEGRINI. No.

Mr. SKUBITZ. They are in this thing too.

Mr. PELLEGRINI. No. It is completely different.

Mr. SKUBITZ. Why is it different?

Mr. PELLEGRINI. In 1970, the Federal court in Philadelphia said that we couldn't collect our taxes. In W. T. Grant's case they liquidated. If the Penn Central would liquidate today we would get full payment.

One of the problems we have in the bankruptcy court is that the Justice Department, which is part of the Federal Government, goes in and they are behind this plan of reorganization. They are saying, "City, State, take these notes, you are going to get your money, you are going to get it eventually, you don't have anything to worry about, they are fully backed and you should take this plan of compromise in the plan of reorganization."

So they go up there and they say "You should take this, this is great. We have a letter that says they are fully secured and you don't have anything to worry about."

What we are doing, you know, if the administration and the Justice Department is telling that to the court, we are coming down and saying to Congress, the other branch. "It is not going to cost you a dime, it is not going to cost you anything."

In a way it is almost putting your money where your mouth is. There is a whipsaw going on, the Federal Government saying that it is not going to hurt you, but here somebody says, "Well, it might cost us money."

The Federal Government can't have it both ways.

I would like to address myself to a comment that Congressman Rooney made about guaranteeing notes. The energy bill that went through guaranteed something like \$10 billion in loans for coal operations and other things.

Mr. ROONEY. The energy bill has not gone through.

Mr. PELLEGRINI. There was a loan provision in it, it has guaranteed \$10 billion.

One of the beneficiaries of this is the reorganized Penn Central Railroad because they have large coal operations. Whoever is pushing that is able to get that type of loan guarantee through which might cost Government money and we are coming down here to ask for a guarantee which the Government says won't cost the Government any money.

Mr. SKUBITZ. Mr. Chairman, I would like to ask permission to let counsel ask a few questions. Do you have any objection?

Mr. ROONEY. I have no objection. Before he does the Chair recognizes Ms. Mikulski.

Ms. MIKULSKI. Mr. Eastwick, I have a question for you. I am sorry I did not hear your oral testimony. Your written testimony gives a rather succinct summary of the situation but I am not clear of the position you are taking. Could you reiterate it?

Mr. EASTWICK. The position of the State of Maryland, Congresswoman Mikulski, is that we are at the present time up in the air about

whether to accept this 50-percent compromise offer which would give us immediate cash or whether we could do better under this plan of reorganization which would be a 20-percent cash provision plus 80 percent on these secured notes.

I might add at this point that a rudimentary fiscal analysis—

Ms. MIKULSKI. Does the State have a position or does it not?

Mr. EASTWICK. Yes; we are in favor of H.R. 8882 for the reason that it would make the risk analysis of the plan of reorganization so much easier for us to know that the Federal guarantees would be there for the secured notes.

We would at that time be in a position of either holding on to these notes and realizing the cash flow from them or these notes would presumably have market value and we could sell them immediately and thereby maximize our recovery of the taxes which have been deferred since 1970.

Ms. MIKULSKI. I have a following question for both you and other members of the panel. I presume you are here under instruction of some other administrative or legislative branch within your own political jurisdiction.

I would like to know, No. 1, who did instruct you to take the position which you did? Was it the mayor, city council, State legislators? And, No. 2, what were those instructions?

Mr. EASTWICK. I can start. I am here simply as a lawyer for the State. I have been advising the board of public works in the State of Maryland which is composed, as you know, of the Governor, the State comptroller, the State treasurer. These gentlemen will be the gentlemen who make the ultimate decision. They have not instructed me to take a position. I am here as an ongoing member of the informal group of taxing authorities who are trying to make those gentlemen's jobs as easy as possible and I think the enactment of Federal guarantees would make the pathway clearer for them.

Ms. MIKULSKI. When you say you are in favor of this legislation then are you speaking for the State of Maryland or are you speaking as a member of an informal coalition examining alternatives?

Mr. EASTWICK. My precise position here is as a technician actually.

Ms. MIKULSKI. That does not answer my question to my satisfaction. Are you speaking here for the Governor of the State of Maryland and its comptroller?

Mr. EASTWICK. No, ma'am. I am not.

Ms. MIKULSKI. Are you speaking for the attorney general?

Mr. EASTWICK. Yes; I am.

Ms. MIKULSKI. Is it his position to recommend this but he has not cleared this, for example, with the Board of Public Works?

Mr. EASTWICK. That is correct.

Ms. MIKULSKI. I understand.

What about you, Mr. Pellegrini and Mr. Cook?

Mr. PELLEGRINI. Congresswoman Mikulski, I am here on the express instructions of Mayor Calgeril who was here last week and met with Mr. Adams. The city treasury, the Republican candidate, is also behind it. He went to Cleveland for a meeting. We are unified. It is really a nonpartisan issue.

Ms. MIKULSKI. Had the mayor discussed this with his city council?

Mr. PELLEGRINI. The council is aware of it. In Pittsburgh we have a strong mayoral form of government. We don't operate that way. My indications from the account and finance people is first of all we can't accept anything less than a hundred cents on the dollar by legislation.

Ms. MIKULSKI. Is that municipal or State legislation?

Mr. PELLEGRINI. State legislation. We don't have any problem. In Philadelphia we don't know if we can take the notes. The Federal Government notes we could probably take. No one has ever considered the plight of people who can't do either legally.

One of the thing we have been looking at is if the legislation went through we could say it is a Federal note and not a Penn Central note. Otherwise we are in a kind of strange legal—

Ms. MIKULSKI. What about you, Mr. Cook?

Mr. Cook. I am here both on my own authority and on the mayor's authority to support the legislation. Similarly in Massachusetts and in the city of Boston we have no option. We can't legally accept the compromise offer or the reorganization plan without special legislation.

Ms. MIKULSKI. Could you accept this?

Mr. Cook. With the Federal guarantee it is the opinion of our counsel that the law can be satisfied.

Mr. SKUBITZ. Will the gentelady yield?

Ms. MIKULSKI. Just one second and I will yield.

The reason I have asked the questions the way I have is that many people testified before us and have indicated this has local support. Yet, very often, it is a particular individual within the executive branch who has taken a position without consultation with other members of the executive branch or with the legislative body. I just wanted to know for whom really you were speaking.

Thank you. I will be happy to yield.

Mr. SKUBITZ. I have one question. Both of you said legally you can't accept a compromise; is that right?

Mr. Cook. Nor this plan as proposed, sir.

Mr. SKUBITZ. If you turn it down completely, do you have a legislature there in the city that will get busy and do something about the compromises? I think we went through this whole thing once already.

Mr. Cook. In the case of Massachusetts, sir, it is the State legislature which often does not see the wisdom of the city of Boston's needs.

Mr. SKUBITZ. If you can't get Big Papa to act, you are really in trouble.

Mr. Chairman, I have no further questions.

Can Mr. Molloy ask some questions?

Mr. MOLLOY. Thank you, Mr. Chairman.

I have just one question for anyone to answer on the panel.

As I understand it, there are still some other bankrupt railroads in the Northeast that have not filed reorganization plans. If H.R. 8882 was enacted, would those railroads tend to make an offer of a dollar, for example, in order to get settlement of their taxes which are some \$80 million, thereby leaving Uncle Sam holding the bag?

Mr. PELLEGRINI. The only way I can answer that, I think one of the other witnesses is going to address that directly, but if the determination is made by the Federal Government as in this case, that it won't cost Federal Government a dime, I can see no reason.

One of the things is that we are dealing in a vacuum. We don't know what they will come out with. We don't know what their assets are. The assets here will cover it. If they are in the same situation, I see no reason why the guarantee could not be extended to them. If the fact situation is identical, yes.

Mr. COOK. I think it is the purpose of the legislative remedy we are speaking of here to apply only to the Penn Central bankruptcy which is distinct from the others. We had the Boston & Maine bankruptcy in Boston, Mass. Here, however, we find something unique. We find an asset base which is large and substantial, and indeed an earning stream which is large and substantial and ongoing which can cover the tax liability which has accrued.

In order to effect the reorganization plan, they have a program which defers the payment of the accrued taxes over time. I think it is wise; I think it is an appropriate reorganization plan.

The problem for the cities is that those things are not liquid, they are not marketable at par. We need the money. We can't manage a portfolio. We are looking to trigger the liquidity of those securities against asset base which is large enough to cover.

In a bankruptcy situation like W. T. Grant or another railroad where there is not that asset base, we, too, like other creditors, have to live with the law.

Mr. MOLLOY. One final comment. I know you haven't had a chance to look at it, but Mr. Davis put in a bill yesterday that provides an alternative approach to help these States and city governments—you might want to take a look at that—in that it embodies a grant that will equal the shortfall that you might have in taxes and avoid some of the problems that you have been mentioning.

Mr. ROONEY. It is a branch-line subsidy. Any tax loss can be considered as the State share in a branch-line subsidy. Is that correct?

Mr. MOLLOY. Yes.

Mr. ROONEY. It is an in-kind benefit legislation.

Ms. MIKULSKI. I will follow that up.

Mr. SKUBITZ. One other question, Mr. Chairman.

A breakdown of the estimated property taxes by States here—I think the total taxes are \$435,967,000—if you break those down, ConRail's share would be \$299,726,000. I will restate it. The total amount is \$435,967,000. These are the taxes up to 1976. ConRail has been paying their share of the taxes since. The breakdown of that \$299,726,000 would be assessed on the property that ConRail took over, is that right, as their share?

The other \$134 million would be Penn Central. That is not only taxes; that is taxes and penalties.

Can you tell me what the penalties are on the total \$435 million?

Mr. COOK. It varies State by State because each State has its own legislation which provides penalties.

Mr. SKUBITZ. What is it in Maryland and what is it in Pennsylvania?

Mr. PELLEGRINI. In Pittsburgh, it is 6-percent penalty, a half percent a month, the same as the interest.

I would like to point out during the period that the bankruptcy was going on the prime interest rate was 9 and 10 percent during that period. So the interest was substantially below the going prime rate at that time.

Mr. SKUBITZ. Let me put it another way then.

If we are bargaining, if a bankruptcy says, "I want to bargain with you on this, I will pay the taxes and not the penalty," how much would it reduce your claim?

Mr. PELLEGRINI. About \$235,000.

Mr. COOK. In Massachusetts, the total claim of the city of Boston, \$17-odd million, \$5 to \$6 million of that is interest and penalty.

Mr. SKUBITZ. Yours is \$17 million?

Mr. COOK. Approximately \$17 million.

Mr. SKUBITZ. It would reduce it about—

Mr. COOK. \$5 to \$6 million.

Again by statute in Massachusetts, the interest and penalties provided for by statute become a part indistinguishable from the tax, and the local authorities, and indeed the State, have no power to waive those.

Mr. SKUBITZ. Does that apply to Pennsylvania, too?

Mr. PELLEGRINI. Yes.

Mr. COOK. One of the questions that has come up is the uncertainty of the tax claims, and you asked why taxing authorities might not know. It has been a problem and it is a problem because in April 1976 ConRail assumed assets that were transferred to it by Penn Central.

In Massachusetts, no deeds have as yet been recorded. It has been difficult to determine who owns what. Previous to the ConRail transfer, there was also Amtrak and our local transit authority which took over property.

Again, deeds have not been recorded. The ability to determine exactly what Penn Central owned and when they surrendered has been confused.

Mr. SKUBITZ. Just one more word and then I am through, Mr. Chairman.

As I say in the beginning, it was the cities and all of you who came down here begging and pleading for God's sake don't stop the railroads.

I told you that west of the Mississippi they were on our backs to let them go broke. I went along with our chairman and the committee because I thought it was in the best interest of the country.

Because of the pressure we were under at that time, I did not think then that I would ordinarily do this to keep the railroads running. I will be looking at these claims in the light of that because I want to see you dealt with fairly. It seems to me we went through this whole thing at that time.

If you are entitled to something, I want to see that you get it. If we have covered this thing already, you will have to get your votes somewhere else.

That is all.

Mr. ROONEY. Thank you, gentlemen, for your appearance before the committee and your testimony.

Our next witnesses can either appear as a panel or individually. Our next witness will be Mr. Francis E. Gaul, treasurer, Cuyahoga County, Cleveland, Ohio. It is rather unique that the two witnesses appearing before us now, Mr. Skubitz, one is for and one is against this legislation.

**STATEMENTS OF FRANCIS E. GAUL, TREASURER, CUYAHOGA COUNTY, OHIO, AND VINCENT C. CAMPANELLA, AUDITOR**

Mr. GAUL. Mr. Chairman and members of the Subcommittee on Transportation and Commerce, I deeply appreciate this opportunity to address the subcommittee on the vital issue of the Penn Central tax payment. As treasurer of Cuyahoga County, I represent 1,700,000 residents who are in overwhelming agreement that no compromise should be accepted from the trustees of the Penn Central Transportation Co. "No Compromise!" is the absolute sentiment in Cuyahoga County.

Some public officials, with whom I respectfully differ, are so concerned by the deficits forced by the lack of Penn Central tax dollar flow, that they feel a Federal guarantee of notes is the surest and most certain way to receive 100 percent local tax payment.

In spite of the general agreement that 100 percent of the tax delinquency must be collected, there is disagreement as to the means to effect that collection.

Congress, in their wisdom, passed the Rail Reorganization Act of 1973, which gave birth to ConRail. ConRail, and not Penn Central, is the entity that protects the public need of rail service.

Penn Central, devoid of the rail operating authority, does not protect public necessity for rail service. Penn Central is a private corporation whose assets greatly exceed their Federal and taxing district debts. Therefore, there is no need to accept any compromise—local or Federal.

The true difference of opinion lies in whether Federal guarantees should finance private corporation tax payments. Particularly when, as a result of the creation on ConRail, the reorganized corporation no longer protects public necessity.

There has been no concern about the true asset value of the bankrupt entity, and their ability to pay. By their own testimony, the trustees have embarked on a valuation case, claiming that the assets conveyed to ConRail under the Rail Reorganization Act of 1973 were undervalued. In the meantime, assets are being liquidated continually, and yet nothing is paid on their outstanding tax liability. While the Federal and local tax district liability is in the neighborhood of \$1 billion, the trustees boast of asset valuation exceeding \$10 billion.

I find it inconsistent that we permit a private corporation to receive special treatment when the public necessity for rail transportation has been provided under ConRail. As treasurer of Cuyahoga County, I find it incongruous that we permit a private corporation the privilege of enjoying special treatment through the use of taxpayer funds, and, additionally expose the Federal Government to the possibility of further expense by underwriting the proposed notes to pay off their tax liability.

I, therefore, respectfully request that you reject the proposed U.S. House bill 8882 as not being in the best interests of the general public.

Thank you, Mr. Chairman, and members of the Subcommittee on Transportation and Commerce, for the opportunity to express my views as reflected by the vast majority of my constituents.

Mr. Chairman, I should add although I am county treasurer of Cuyahoga County, I am representing myself as a taxpayer. I am not

here at government expense. I am articulating my personal opinion on the principle of government that is involved.

Mr. ROONEY. I commend you for your very fine statement.

There was a treasurer from Franklin County, Ohio here yesterday who took an opposite view of yours. Is that contiguous?

Mr. GAUL. No, sir, it is 180 miles away. It is Columbus, Ohio.

Mr. ROONEY. What is your town?

Mr. GAUL. Cleveland, Ohio.

Mr. ROONEY. You may proceed.

#### STATEMENT OF VINCENT C. CAMPANELLA

Mr. CAMPANELLA. Mr. Chairman, my name is Vincent Campanella, auditor of Cuyahoga County. I request my statement be made part of the record and I will summarize it for you.

Mr. Chairman, as you indicated there was a treasurer from the next largest county in Ohio who differed yesterday from what Mr. Gaul's position was.

I found myself amusingly in kind of a dilemma. I was not sure whether I should have flown back to Cleveland to seize the railroads or to come here and testify before you today. It is amusing and perhaps confusing that Mr. Gaul, who is 12 feet away from me in our offices, chose to be at this same table because it highlights the confusion that all taxing authorities throughout the country have suffered over the past 7 years with Penn Central.

I would like to share our problem with this Congress and our problem is this—that some of the finest legal minds representing the major cities and States in this country who have Penn Central property have taken every legal remedy available in the Federal District Court of Pennsylvania handling the bankruptcy case.

The only thing we can share with you is the fact that if there is not something done, some action, if some action is done we would hope it would be this committee and this Congress, does not come to our aid, there is a great possibility that local taxing authorities will indeed subsidize that new corporation that Mr. Gaul so adequately explained. That new company which now has three petroleum companies, which owns large real estate investments in Florida and in Texas, has asked us by October 22 to say "OK, representing the taxpayers of Cuyahoga County, I will take 44 cents."

Incidentally the figures in Cuyahoga County work out to 36 cents on the dollar. We are asked to take that or without any allies from the Congress we are asked to go into the court again and overturn the plan of reorganization, indeed which we are going to be forced to do and forced to go 7 more years maybe before we get any amount of money because of legal ramifications indicated about an hour ago by those States that are unable to accept payment.

The other creditors have staying power. It is important to note that the other creditors have staying power, the other secured creditors. I don't know if it has been brought before this panel but indeed they will finish, if this plan of reorganization goes through, with a 30-percent equity interest in what will amount to 1 of the 400 largest corporations in the United States.

I submit to you we can debate all day about the wisdom of a bill, of involvement on the part of the Federal Government. The only thing I can tell you is that the bottom line is that I believe and my colleagues from States throughout the country believe that without your help we are actually going to be made a victim of that corporation.

As a matter of fact, I would submit to this committee if indeed you have another solution for us that we have not already exercised before the courts or any other solution which will provide for payment of our tax dollars, then all of us will be open to listening to that.

I thank you very much for having this opportunity to speak before you. I am open to any questions you may have.

[Mr. Campanella's prepared statement follows:]

STATEMENT OF VINCENT C. CAMPANELLA, AUDITOR OF CUYAHOGA COUNTY, OHIO

Chairman Rooney and Members of the Subcommittee. I greatly appreciate your kindness in extending to me the opportunity to speak to you today on the pressing issue of Penn Central tax delinquencies.

As indicated, I am the County Auditor of Cuyahoga County, Ohio whose county seat is Cleveland. Under Ohio Law a county auditor is charged with the appraisal of property for taxation purposes and, as the presiding officer for our county budget commission, is also responsible for deciding between the options for settlement which have been presented by Penn Central to all taxing authorities.

The total tax debt owed by Penn Central in Cuyahoga County amount to over \$16 million. As is the situation with all other taxing authorities, this tremendous debt has been accruing for the past seven years to the detriment of our schools, cities and governmental bodies.

In fact, the Cleveland School District is now faced with the prospect of closing its Schools before the end of 1977. The \$8 million in taxes which Penn Central owed to it represents the difference between life and death for the educational process in the City of Cleveland.

The Cleveland schools are not the only taxing authority in Cuyahoga County which is financially hard pressed. A number of our taxing authorities have been facing continually increasing opposition to property tax increases of any sort. Property tax levy after property tax levy are voted down throughout the country. Taxpayers are becoming increasingly sophisticated in our country as well as other parts of the nation. It is just not possible to explain to them how a larger corporation can escape payments of its taxes for seven years and add that they would lose their property for being delinquent for the same period of time.

Immediately after I became County Auditor in February of this year, numerous individuals and citizens groups as well as taxing authorities came to me and requested that I investigate the Penn Central matter. They were very concerned as to whether or not Penn Central's tax debts would ever be paid to Cuyahoga County. Moreover, they were incensed over the possibility that Penn Central would escape the responsibility of paying their tax debts in full. This is where my involvement began in the Penn Central case.

Upon my initial investigation, I discovered that the offer for compromise of tax claims and the plan of reorganization that had been ordered by the Penn Central trustees were totally unsatisfactory in dealing with the cities and schools. Both of these settlement offers put forth by Penn Central completely ignore the long accepted principles of bankruptcy law whereby taxes are an administrative expense and thereby are accorded the highest priority of payment from the estate of the debtor. Much to my chagrin and anger, I discovered that the cities and schools were being asked to accept as little as 35 percent of the taxes owed to them by Penn Central and were being given a much lower priority for payment than were a number of banks and other institutional creditors. These other creditors, it is important to note, are not administrative claimants and, pursuant to the bankruptcy statutes, should be given a much lower priority for a payment of their claims. That is simply not the case.

Basically, the compromise of tax claims provides for an immediate cash payment to a taxing authority when it notifies the Penn Central trustees that it is

willing to settle its entire claim in return for partial payment. An accepting taxing authority would receive a cash amount equal to the greater of (1) 50 percent of the taxes accrued since Penn Central filed for reorganization or, (2) 44 percent of the taxes due both prior to and after the time that Penn Central filed for reorganization. In no case is a taxing authority of interest or penalties which have been assessed against Penn Central over the past seven years. It is this fact which makes the compromise worth only 35 percent of total delinquent Penn Central taxes to the taxing authorities in Cuyahoga County.

Any taxing authority, not settling its tax claim pursuant to this compromise, will receive payment for its tax claims under the terms of the plan of reorganization submitted by the trustees. This plan has yet to be finally approved by the Federal District Court in Philadelphia which is hearing the reorganization proceedings. Final argument on the plan is scheduled for October 6th of this year. At that time, a large number of taxing authorities who I have been working with over the past few months, will be continuing their objections to the present plan of reorganization. These objectives are based, as I indicated earlier, upon the fact that the taxing authorities are not receiving the priority of payment that is called for by the bankruptcy statutes.

Upon implementation of the plan, taxing authorities will receive payment of their claims in the following manner:

A cash payment amounting to 20 percent of the total principle of the taxes due to the taxing authority, and

Securities issued by the reorganized Penn Central Company for the remaining 80 percent of the principal and for 100 percent of the interest accrued on that principle for the seven year period.

For taxes which accrued on properties transferred to ConRail by the RRR Act of 1973, series C notes will be issued. These notes will be secured only by the proceeds of the Valuation Case. That case pits Penn Central against the U.S. Government in an Argument over the value of the rail properties which were taken from Penn Central and used to create the U.S. Consolidated Rail Corporation.

For taxes which had accrued on properties which have been retained by Penn Central, series D General Obligation Notes would be issued by the reorganized Penn Central Company. These notes would be secured by the full faith and credit of that reorganized corporation.

During that meeting in Cleveland, I reported to the forty-plus taxing authorities in my county as to the situation in the Penn Central case. I stated my opinion that both the compromise and plan seem to be totally satisfactory in protecting their interests. They requested that I pursue any and all avenues to insure that their tax claims would be paid in full by Penn Central. At my suggestion, we then approached members of the Cuyahoga County congressional delegation and sought their aid in protecting our tax claims. They recommended that we first explore the avenue of administrative remedies which might aid our cause. They wrote and signed a letter to Secretary of Transportation, Brock Adams, requesting on our behalf that he subordinate the federal claim in favor of our tax claim. Secretary Adams declined to do so on the grounds that the federal claim must be repaid before state and local claims in accordance with the requirements of the RRR Act of 1973.

Representative Mary Rose Oaker then agreed to introduce Legislation based upon my idea of a Federal guarantee on the series C and series D Notes which are to be given to the taxing authorities in settlement of their claims.

That Legislation, embodied as H.R. 9402 and S. 2000, is the only viable opportunity for the taxing authorities to receive the full amount of their claims against Penn Central within the near future.

The issue here is not whether those securities will ever be retired in full upon their maturity by Penn Central. As I will demonstrate, there appears to be no question whatsoever that both C and D Notes will eventually be made good by Penn Central.

We are faced here with the issue of when the taxing authorities will receive full payment for the delinquent taxes owed to them by Penn Central. You must keep in mind that these taxing authorities have for seven years been financing and subsidizing the continued operations of both Penn Central and ConRail. To ask these financially pressed governmental bodies, as the Penn Central Trustees are doing, to wait at least another ten years for the full payment of their delinquent taxes is blatantly wrong. Therefore, some method must be found by which to

provide the taxing authorities with all the taxes owed to them by Penn Central right now.

The issue then comes down to the marketability of those C and D Notes which Penn Central will be issuing to us. There is no question that the name "Penn Central" or "Pennsylvania Company", which will appear on those securities, will greatly detract from the ability of the taxing authorities to sell them on the open market. All the promises in the world that the notes are fully secured will not mean anything to the general securities market. What is needed is a federal guarantee behind these securities so that the negative connotation which the Penn Central name will give them can be counteracted.

To provide this guarantee will insure that the taxing authorities will be able to take those notes and immediately sell them on the open market to receive the delinquent taxes owed to them now—not in ten years as the Penn Central Trustees propose. It must be made clear that the prior intervention of the Federal courts and progress, though well meaning as it undoubtedly was, has placed the burden upon the local and state taxing authorities to finance the operations of Penn Central and ConRail. Particularly distasteful is the fact that it is the schools of our nation which have been asked to bear the greatest amount of this burden in supporting Penn Central. To ask them, not to force them, to wait at least an additional ten years to receive the taxes which they have already waited seven years for is simply unthinkable. The guarantee must be given in all fairness to the taxing authorities.

The most important issue which I feel you should consider in making your decision on this legislation is the fact that the Federal government will not have to spend one penny as a result of its guarantee. The Penn Central Trustees themselves, through the financial documents submitted with their plan of reorganization, have detailed the fact that there will be ample cash in their hands to certify all of the series D notes which they will issue even if there were no taxing authorities accepting the tax compromise.

With regard to the series C notes, the Department of Justice has indicated in communications to me that there is every reasonable expectation that the ultimate settlement in the valuation case will provide more than sufficient funds to retire the C notes. That statement has been independently verified by the accounting firm of Ernst and Ernst who believe that the \$525 million base offer made by the U.S. Rail Association on behalf of the Federal Government will more than cover both the Federal claim and the state and local tax claims against Penn Central.

On the issue of the value of the series D Notes, testimony has been given by well respected financial and securities analysts which independently verifies the figures put forth by the Penn Central Trustees. Isabel H. Benham of the firm of Shearson, Hayden, Stone, Incorporated, one of the largest securities brokerage and investment banking firms in this country, has publicly testified as to the ultimate worth of the series C and D Notes. Her testimony has been validated by a number of other well respected financial analysts.

In closing I must again emphasize the two most important points with regard to the guarantee which we are seeking from you.

First, the guarantee is absolutely necessary if we—the taxing authorities—are to finally receive the fair treatment which we have been denied for the past seven years. You cannot allow us to be penalized any longer. We must receive the taxes so long due to us now if we are to continue to function on a fiscally sound basis.

Second, I feel that it has been adequately demonstrated that this guarantee will NOT cost the federal government any money whatsoever and will go a long way to right the wrongs which the initial federal intervention has brought down upon our schools and cities.

Mr. ROONEY. Thank you.

As you very well know, one of the outspoken proponents of this legislation is from the great State of Ohio, the City of Cleveland.

I am talking about Congresswoman Mary Rose Oakar who has done an outstanding job in getting Members of Congress to support this legislation. I believe there are something like 60 cosponsors which she single handedly corralled to sign.

Mr. Skubitz?

Mr. SKUBITZ. I would like to ask this gentleman a question. If I understand you correctly what you are saying to this committee is that unless we do something some way, somehow Penn Central will chisel you out of the money. Is that correct?

Mr. CAMPANELLA. No, that is not correct. I have described how they will do it. They are doing it and it is done. That is the big difference between the two positions. I am saying that I believe that indeed if you don't do something, not some way, somehow, through the plan of reorganization which was approved by the Department of Justice and actually partially engineered by the Department of Transportation, we will subsidize that new corporation.

Mr. SKUBITZ. The gentleman that were here before you from Maryland and Massachusetts, two of them, told this committee that this would not cost us a cent.

Mr. CAMPANELLA. I don't believe it will.

Mr. SKUBITZ. "You give us a guarantee and it will take care of it"?

Mr. CAMPANELLA. Absolutely. I believe it is well documented by one of the most prestigious east coast certified public accounting firms, documented by articles in the Wall Street Journal, New York Times, Forbes magazine, and even by some investment banking firms that the new corporation emerges as one of the most profitable 400 largest corporations in the United States. Now that is testimony presented before the bankruptcy court.

Mr. SKUBITZ. I had the impression that Penn Central would certainly have enough money to take care of their taxes. They have enough assets to take care of their debts here. It is only a case of waiting for it. What you are saying is that Penn Central is smart enough to get out of it as far as you folks are concerned but not smart enough to get out of it as far as we are concerned.

Is that right?

Mr. CAMPANELLA. Mr. Congressman, I indicated that it wasn't a question of smart enough or not smart enough. I indicated through the efforts of the Department of Transportation, in fact in December 1976, and through using that very fine Four R Act which did indeed help the east coast and the Midwest and I don't doubt that but in fact twisting what you so carefully put together they have been able to take advantage of schools and cities.

There have been many facts and many explanations about the details and I do not want to bore you with the details although I would be more than delighted to go into them.

Again I appeal to you in a sense of justice to say that some of the things that you so ably have done have been twisted and we need your help again.

Mr. ROONEY. Mr. Gaul would like to respond.

Mr. GAUL. Mr. Chairman and Congressman Skubitz, in partial answer to that question there are four areas we have identified where the taxpayer will be disenfranchised.

If I may offer one comment here, what seems to go unnoticed is the fact that this is a reorganization plan presented by the self-serving trustees of the Penn Central. I will be happy to make this a part of the record.

It is an ad in the paper. It is a plan which has been offered by the trustees. Now if the taxing districts do not accept, it is expected to go back to the Federal court in Philadelphia. The reason that some of those are looking to take the acceptance of the Federal guarantee is because they are thinking that the Federal court rather than ordering liquidation will order the least palatable of the three offers that were made by the trustees.

So therefore my position is Penn Central should be treated like any other taxpayer. If in fact they cannot pay their taxes they no longer protect public interest because in their wisdom Congress has taken care of that with ConRail and liquidate their properties like Joe Slocum, a taxpayer in any county, and Penn Central has no priority because they no longer protect public interest, therefore they should be liquidated and there are plenty of assets to pay off the claims of all, first the Federal Government and the taxing districts as soon as possible.

Mr. CAMPANELLA. We agree with that position. Many of the attorneys have been arguing for that for 2 years. I submit to you we have been turned down in that court. That position is tantamount to the position of the treasurer yesterday.

If, in fact, you want this to happen then you would have to in a sense be an anarchist and say to the Federal court, "Look, we should have liquidated. You didn't want to liquidate. We are going to liquidate anyhow."

Mr. SKUBITZ. I would like Mr. Gaul to respond.

Mr. GAUL. I think it is rational to jump to a court. The courts treat everybody the same under the laws. The only reason that Penn Central had a sacrosanct position is because they protected the public interest.

I have heard people sit at the table and say they protect the public interest. Congress in their wisdom took care of that. They conveyed the properties that did protect the public interest, lent them \$500 million in the meantime and now we have that over here.

On the other hand we have the residues, Penn Central which is a private corporation for profit that does not protect the public interest. When the plan of the trustees is not accepted by the creditors it shall go back to the Federal court and the Federal court will treat the Penn Central devoid of the public need and necessity just like any other taxpayer in the county.

Mr. CAMPANELLA. He did not answer your question. I have indicated to you that there are several attorneys in this room who have indeed argued that position. To date the court in its wisdom has deemed that new company shall exist.

We will indeed argue it should not have existed under the present circumstances.

What I have suggested is that the collective judgment of those of us who have been working on this for the past several months and not the past week, and that is the only place where we do disagree, Mr. Gaul, that this was the best method possible and apparently no cost to the Federal Government.

I have heard you say—and I was involved in a couple of instances with the Federal Government—I have heard that position placed

forward and in fact, it did cost Federal Government a lot of money, but Mr. Gaul even agrees that that is a profitable, viable corporation.

Now perhaps this Congress by making a presentation to the court can persuade the court to liquidate. We would be very happy if you would help us in that area, too.

Mr. GAUL. Mr. Chairman, if I may, and tying into Mr. Campanella's remarks, one of the most important factors we have to consider here is that at the time of the conveyance of the property from Penn Central to ConRail the Federal Government established \$525 million as a fair and equitable price.

Immediately thereafter the Penn Central filed a claim for \$7.4 billion as the takeover price.

Now, to the degree that we give them corporate strength by virtue of guaranteeing their financing of their new corporate structure we are giving them lifeblood to come back and fight us in the appropriations case of the \$7.4 billion.

So, it not only will cost us billions of dollars in terms of incidental cost that these people don't look at now, we will really put muscle in that weak corporation as it stands now if they have to address themselves to the debt and make them a giant against us in the \$7.4 billion takeover case.

Mr. CAMPANELLA. Mr. Chairman, I thank you very much for giving me the opportunity to appear before this committee. Anything you can do for all of us who are indeed in dire straits will be greatly appreciated.

Mr. ROONEY. For two people who are only 12 feet apart you are very congenial enemies.

Mr. GAUL. We have gotten along at city hall for a few years.

Mr. ROONEY. The Chair recognizes the distinguished author of this legislation, Congresswoman Oaker.

Ms. OAKER. I want to thank you and the members of the committee for permitting me to ask my friends and colleagues from my great city of Cleveland one question that seems to be at issue here.

I think the bottom line is that we all want to see Penn Central come forth with the resources that are really due our city and municipalities across the country. I wanted to know how we could liquidate and seize many of these properties that Penn Central owes our areas, in Ohio for example, when many of these have already been conveyed to ConRail and they are viably being used.

As we know, ConRail is extremely successful in our city. In fact, they are adding on passenger service currently as I understand it. I would like to know how we can do something that is viable and it does not seem like an immediate practical solution. It seems as if it would be held up in court ad infinitum.

Mr. CAMPANELLA. I don't believe it is possible. I think your point is well taken, that we are without legal redress except through the courts and the courts have already approved the sale for the conveyance of much of that property. This in essence is our court of last resort.

Mr. GAUL. I will say this. We can't mix ConRail and Penn Central and that is the unfortunate factor in this whole thing. As we indicated, the conveyed properties are here and that protects public neces-

sity. The assets here are worth in excess of \$5 billion. The debt is \$1 billion. The corporation itself is in a self-liquidation program of \$1.7 billion.

If directed by the court that \$1.7 billion would meet all of the debt of the Federal Government and all taxing districts by far. So we are saying this. We cannot prejudge that Federal court. We have to give the Federal court the opportunity to treat Penn Central, residue Penn Central, treat them like any other taxpayer and say liquidate to the extent of properties to pay a billion dollars, which is \$500 million in round figures to the Federal Government, the money they lent you when you were forced to operate from 1970 to 1973 until we put ConRail in existence.

The second \$548 million is the taxing district liability. The \$1.7 billion selloff program they have identified, let them pay that money to the creditors and they can go on their way as a private corporation thereafter. They do not need Federal money. We can't say no compromise likely but run to Washington and get the money. We can't say that and be honest to ourselves.

Mr. CAMPANELLA. At this point the hope is unreasonable in light of the fact they have already ruled against your position. They indeed have ruled against your position and part of your position has been litigated all the way up to the Supreme Court. That was denied in the Supreme Court of the United States.

Ms. OAKAR. Thank you, Mr. Chairman.

Mr. SKUBITZ. Mr. Gaul, I commend you on the statement and the position you have taken.

Mr. GAUL. Thank you.

Mr. ROONEY. Our final witness this morning will be Mr. James Young, deputy mayor for financial affairs, city of Boston, and Mr. James Howell, Sr., vice president of the First National Bank of Boston.

**STATEMENT OF JAMES V. YOUNG, DEPUTY MAYOR FOR FINANCIAL AFFAIRS, CITY OF BOSTON, ACCOMPANIED BY JAMES M. HOWELL, SENIOR VICE PRESIDENT AND CHIEF ECONOMIST, FIRST NATIONAL BANK OF BOSTON**

Mr. YOUNG. Mr. Howell is ill and cannot be here this morning.

I would like to request on his behalf that the record be held open until sometime tomorrow at which time his statement will be entered.

Mr. ROONEY. You may proceed.

Mr. YOUNG. Thank you, Mr. Chairman.

I appreciate the opportunity to testify on behalf of the bill that is before you. The previous speakers have done perhaps far better than I could in identifying the issues and the facts here and I will not waste the committee's time by a recitation of that.

In terms of my personal view I do differ from some of the previous speakers in the sense of the Federal involvement in the present problem.

I do not take exception to the role of the Federal Government in the railroad reorganization proposal. It is clear that it would be an

economic catastrophe to the Northeast to allow the demise of the Penn Central system and a disaster to the Nation as a whole if that occurred.

It did not occur because of the action of the Congress and executive branch of the Government. What we have here is a situation which I would describe as one of unintended consequences and of opportunity.

In terms of the unintended consequences I would like to refer to a question, if I may, that you raised previously and that is, why, since the Federal Government has loaned approximately a half billion dollars to Penn Central's possible bankruptcy, should they not, as any other lender in that situation, take a preferred position.

As I am also the treasurer of the city of Boston I can sympathize with that, and indeed we would not as a general proposition do it.

The unintended consequence here is that I think it is fair to describe the situation that there has been approximately \$1 billion of public sector financing directly in the Penn Central reorganization, a half billion is in terms of Federal loans from the Federal Government and a half billion is which is in the form of a forced loan because of a forced deferral of real estate and personal property taxes due to State and local governments.

Indeed the public sector has \$1 billion in it.

Mr. ROONEY. Excuse me. Are you summarizing your statement?

Mr. YOUNG. Yes.

Mr. ROONEY. Do you wish to have your statement become part of the record?

Mr. YOUNG. Yes; I think so.

Mr. ROONEY. Without objection.

Mr. YOUNG. It is clearly a loan on the part of local government, a fact symbolized by the fact that we are going to get notes for it. It is a loan by and large by the central cities in the Northeast region. That is to say those concentrations of the poorest of our citizens and where we have the greatest concentration of minorities.

With respect to opportunities I would like to comment on two inter-related factors.

First, there is a great deal of debate in Washington, across the country, in the Congress, as to the proper measures to continue the economic recovery program. There is a growing realization that the economy of the country is weakest, that those people who are our constituents—that is the residents of central cities and minorities, are not participating as much as the rest of the country is in terms of economic recovery.

What we have before us in terms of opportunity, is a mechanism which I would hope would be latched on to as part of the urban policy of the Congress and of the administration which would provide an immediate infusion of cash by making notes liquid to those points where it is almost precisely most needed.

It is a program in terms of economic stimulus that could not be better targeted. Mr. Howell, who I think is properly described as an expert on the economy of the Northeast, will in his statement expand to a considerable length on that.

The other problem is the financial stability of our cities, particularly the cities in the Northeast. Boston has had a lot of well publicized difficulties in the last 2 years. Boston's problems are unique. They are primarily a function of the imbalance of State/local tax structure, not a Federal policy.

However, Boston is unique in its dependence on the real estate tax. It has suffered a great deal in terms of the characteristics of the national economy in the last 5 years in terms of inflation and there has been since the beginning of the Penn Central bankruptcy approximately 50-percent inflation.

We have had those pressures on our costs. The recessionary aspects of the economy, have meant that our citizens incomes have by no means kept up with that and particularly since we are dependent on the real estate tax real estate values have not kept up with that.

Inflation can be viewed as tax on the order of \$100-to-\$150 million a year in terms of the revenue resources available to the city.

Against this the general revenue sharing, while a step in the right direction, has not, at least in the context of the city of Boston, offset the impact on the national economy.

To deal with this problem we have in the last several years first reduced our work force and that includes everything from hospitals to the Animal Patrol Commission through police, firemen, and public works, by 20 percent.

Second, in each and every year in the last 5 or 6 years our employees have settled for collective bargaining settlements that have been significantly less than the cost of living. They have taken a real decline in income. In spite of this we had to raise real estate taxes by more than 25 percent last year. The bottom line, if you will, is that 15 months ago the city had an accumulated operating deficit of approximately \$80 million through the actions I have described it has been reduced to \$45 million of which the Penn Central liability by itself represents over one-third.

To the extent there is any interest in doing those things that are consistent with the Federal policies to shore up both the financial stability and the economies of Northeastern cities this fits very nicely.

I would like to comment on one other aspect. There are approximately 30,000 unemployed people in the city of Boston. We have reduced the work force by 3,000. Indeed one-tenth of the unemployment problem of the city has been caused by city problems and to paraphrase Pogo, "we have met the enemy and they are us."

It is also interesting to look at whom we did not hire. The city has made a major commitment to affirmative action and equal opportunity. As a practical matter it is clearly done by new hires. It is precisely in terms of the minority unemployment problem in Boston which is severe, a quarter to a third or more of the people that we did not hire would have come from those ranks.

Let me conclude with one comment: I think there has been some sense that the proposed guarantees would in some way upset the relationship of ConRail and the reorganization of Penn Central.

I am not an expert on the bankruptcy proceedings but it is my understanding that nothing in this legislation would upset any of the particular relationships.

I would conclude by saying as far as the city of Boston is concerned we would very much like your attention to see if this could indeed be worked out.

[Messrs. Young and Howell's prepared statements follow:]

STATEMENT OF JAMES V. YOUNG, DEPUTY MAYOR FOR FINANCIAL AFFAIRS,  
CITY OF BOSTON

My name is James V. Young of Boston, Massachusetts. I am the Collector-Treasurer of the City and its Deputy Mayor for Fiscal Affairs. I appreciate very much this opportunity to testify regarding H.R. 8882. I would like to describe briefly the importance of this legislation to Boston, in light of the City's present condition, and then speak to the more general merits of this legislation.

Boston, like other central cities, was very hard hit by recession of the 70's. Over the past five years we have cut our work force by 20 percent, and still have had to increase property taxes by 25 percent, all of this to reduce accumulated deficits in order to insure the long term financial health of the City. While we are out of the woods yet, Boston is well on its way to financial stability. But this has come at great expense. As I mentioned, in the last five years we have either laid off or failed to replace approximately 3,000 employees. In a sense, the City itself can be said to have created one-tenth of the unemployment problem facing the City, as roughly 30,000 City residents are currently unemployed.

And in a sense this is only part of the problem. While the City has a strong commitment to affirmative action and a detailed plan for making improvements in this area, it is very difficult to increase the proportion of minorities working for the City while undergoing a decrease of 20 percent in the City's workforce.

The receipt of Penn Centrals' overdue taxes made possible by this legislation, will mean a lot to Boston, a City which is more heavily dependent on the property tax than any other city in the country. It will constitute a major step forward in my efforts to put the City in the position where it can begin training and hiring residents to fill vacant positions and provide services to its population, a population which contains nearly 50 percent of the low and moderate income persons in the metropolitan area, but which constitutes only 20 percent or less of the total population of the metropolitan area.

Generally, the Amendment to the Regional Rail Reorganization Act of 1973, has several attractive features both to those of us who are charged with the responsibility for the fiscal health of cities in the Northeast and Midwest and to Federal Officials, and Members of Congress, charged with the responsibility for the fiscal health of the whole country. This legislation will at last allow taxing jurisdiction to collect taxes which are up to seven years overdue, rather than suffer further delay and uncertainty. While this is the primary benefit to officials in position similar to mine, and cities in conditions similar to Boston's, there are at least two additional, more indirect benefits. First this complements the commitment and interest of the U.S. Government in insuring that ConRail becomes a viable transportation enterprise, a result which is as important to the health of the country as it is to the health of these cities and their region. Second, there will be a quick stimulus to these cities and regions which will come in a manner that is much less inflationary than a direct federal grant program of a similar magnitude. And I assure you, controlling inflation is of critical importance to all of us who are trying to minimize increases in local budgets.

I also believe that this legislation has several strong, positive points from the Federal view. First, the legislation will allow the Penn Central reorganization to proceed expeditiously. Secondly, the legislation addresses one very serious weakness of the reorganization plan as presently constituted. In effect, the reorganization of the bankrupt has had a billion dollars worth of initial financing, one-half billion dollars explicitly advanced from the Federal Government and one-half billion implicitly advanced from local jurisdictions in foregone taxes with the great bulk of this "local financing" coming from central cities, with large concentrations of low and moderate income persons and families. Under the proposed plan of reorganization, the Federal Government will get its one-half billion dollars back from itself through the ConRail Valuation Case while the central cities, which are without question much weaker financially, will have an uncertain claim maturing 10 to 15 years down the road to recover their share of the financing. I submit to you that it is very difficult to justify this

situation without the legislation, Northeast and Midwest cities, and their residents will provide an equal amount of financing in exchange for a much less certain program of recovery. However, with this legislation, the Federal Government and the cities, both of which have strong interests in a successful reorganization, become much more equal partners, in light of their relative financial positions. Finally, the legislation will provide a quick, direct economic stimulus to the central cities in the Northeast and Midwest, areas which most people acknowledge are not fully sharing in the general economic recovery of the country, and provide this stimulus in a relatively non-inflationary manner.

In closing, let me strongly urge you to recommend passage of this legislation.

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STATEMENT OF DR. JAMES M. HOWELL, SENIOR VICE PRESIDENT AND CHIEF ECONOMIST, THE FIRST NATIONAL BANK OF BOSTON

Mr. Chairman and members of the Subcommittee, I very much regret that I cannot be with you but I did want to take the opportunity to make a statement concerning the legislation before you today: H.R. 8882, H.R. 9015, H.R. 9023, H.R. 9024, to amend the Regional Rail Reorganization Act of 1973, to authorize the Secretary of Transportation to guarantee notes issued to State and local taxing authorities to secure payment of real property tax obligations owed by a railroad in reorganization. I am pleased to join Boston's Deputy Mayor and City Treasurer James Young in support of this legislation.

This legislation for Federal guarantees to pay off the delinquent taxes would ensure that Boston and other Massachusetts cities and towns would receive 100 percent of the tax money owed to them by the bankrupt railroad. The delinquent Penn Central property taxes have accumulated since June, 1970, when the Penn Central Transportation Company filed for reorganization under Section 77 of the Federal Bankruptcy Act. In addition, cities and towns have not been paid for other taxes that accumulated prior to 1970 when the Penn Central Railroad began to encounter serious financial difficulties.

Passage of this legislation would mean that the City of Boston could receive up to \$17 million in additional revenue. Although, Massachusetts citizens and towns are owed \$24.8 million in back taxes.

As matters now stand, the plan for Penn Central reorganization stipulates that the affected cities may receive payment for back taxes through partial cash payment and the issuance of 10-year notes. Without the Federal guarantees contained in this legislation, these financially hard-pressed cities would undoubtedly have to wait up to 10 years to receive full payment of the back taxes owed.

Given the serious deterioration of the economic bases of these cities, this is clearly a second-best solution. Partial payment is simply inadequate to redress those cities' current financial needs. The Federal Government guarantee would clear the way to the selling of the notes into the capital market, thereby providing the all-important one shot cash infusion into these cities. Recent economic analysis of Northeastern cities conducted by the Bank's Economics Department suggests that the Federal guarantee of Penn Central notes is a sound and highly desirable method to infuse added dollars into our older industrialized cities without any additional outlays of federal funds.

Our analysis of leading economic indicators in Northeastern cities—especially the older industrialized cities—confirms the extent to which these cities get into financial trouble because of eroding tax bases. Over the past several years, the affected cities in the Northeast have been forced to raise property taxes and in many cases to curtail public services because of severe strains on their tax revenues.

For cities in Massachusetts which are trying to preserve—and indeed to expand their tax bases, it is imperative that tax revenues which are already due them be paid so as to maintain the fiscal integrity of local units of government. Moreover nonpayment of these property taxes would pose serious social as well as economic problems.

The cities affected by the Penn Central Reorganization Plan are laboring under a court-ordered October 19th deadline to decide whether to accept a partial payment plan for the taxes that were owed to them. Therefore, Congress should move speedily to enact this legislation. I also urge the Trustees of the Penn Central to seek a delay from the Federal Bankruptcy Court in Philadelphia in the implementation of the Court-ordered plan in order to give Congress enough time to consider this important legislation.

**Mr. ROONEY.** Thank you very much, Mr. Young. We appreciate very much your presence here today. I do know your mayor personally. I know the very difficult job that he has in Boston.

Again I want to thank you for appearing before this committee.

There is one thing that I can't seem to understand.

You have all survived the crisis of the 1970's and now you are looking for the back taxes. The back taxes will eventually come. But why does the Federal Government have to guarantee the repayment of back taxes? That is as simple as this problem seems to me.

Are you getting paid now on your property taxes by ConRail?

**Mr. YOUNG.** Yes; they are current.

**Mr. ROONEY.** For 7 years you did not get one nickel. Now you are getting what you should have gotten 7 years ago every year.

**Mr. YOUNG.** That is true.

First of all there is the question of definition of survival in the sense that a 20-percent reduction in the city work force and the attendant reduction in the level of services and a great increase in real estate taxes may not be a stable situation over time.

**Mr. ROONEY.** How much is the city of Boston owed by Penn Central?

**Mr. YOUNG.** Including principal and interest, approximately \$17 million.

**Mr. ROONEY.** \$17 million.

Do you think you can put that 20 percent back on the work force; do you think you can reduce taxes if you get that?

**Mr. YOUNG.** Obviously, Mr. Chairman, this is not a panacea but it does to the extent the city is spending every nickel it gets. No one makes a profit on the cities.

Seventy-five percent of our expenditures are for employees. What this does is save the city over the next couple of years from having to fund out of current taxes that portion of the accumulating operating deficit that is attributable to Penn Central. Inflation has subsided to some extent but it is still 6 percent. That is costing the city something on the order of \$39 million a year, a cost that won't show up. We try to cut that in half by cutting the work forces and hard bargaining. It is not a panacea but it is a step in the brief direction.

**Mr. ROONEY.** Thank you very much, Mr. Young.

That will conclude our hearings until Tuesday at 10 a.m., October 4, in room 2322. The committee stands adjourned.

[Whereupon at 12:15 p.m. the committee adjourned to reconvene at 10 a.m., Tuesday, October 4, 1977.]



# GUARANTEE OF DELINQUENT TAXES DUE FROM BANKRUPT RAILROADS

TUESDAY, OCTOBER 4, 1977

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON TRANSPORTATION AND COMMERCE,  
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,  
*Washington, D.C.*

The subcommittee met at 10 a.m., pursuant to notice, in room 2322, Rayburn House Office Building, Hon. Fred B. Rooney, chairman, presiding.

Mr. ROONEY. The committee will come to order.

Our first witness this morning is Mr. Roger C. Altman, Assistant Secretary of Domestic Finance, Department of the Treasury, Pennsylvania Avenue, Washington, D.C.

Mr. Altman, you may proceed.

[No response.]

Mr. ROONEY. Our second witness is Mr. Robert Gallamore, Federal Railroad Administration.

Mr. Gallamore.

Obviously, the Administration fails to recognize that the chairman convenes these meetings promptly at 10 o'clock.

## STATEMENT OF ROBERT GALLAMORE, DEPUTY ADMINISTRATOR, FEDERAL RAILROAD ADMINISTRATION, DEPARTMENT OF TRANSPORTATION, ACCOMPANIED BY RAYMOND K. JAMES, CHIEF COUNSEL

Mr. GALLAMORE. Good morning.

We will be providing a good deal of background information, so perhaps this order is not all that bad.

It is a pleasure to appear as one of the Administration's witnesses on H.R. 8882. With me on my right is Raymond K. James, the Chief Counsel of the Federal Railroad Administration.

H.R. 8882 would require the Federal Government to guarantee securities issued by railroads in reorganization to State and local taxing authorities if ConRail, the U.S. Railway Association, or the Federal Government asserts a priority in payment over such tax claims. The purpose of the guarantee is to enable the securities to be sold immediately without the discounts they might otherwise bear.

The bill is primarily directed toward the settlement of State and local tax claims against the Penn Central Transportation Co., amounting to approximately \$523 million in principal and interest calculated

through December 31, 1977. Of that amount, approximately \$300 million relates to properties conveyed pursuant to the 3R Act and approximately \$223 million to retain properties. Approximately 14 percent of the claims are prebankruptcy claims. This bill would also be applicable to the satisfaction of approximately \$81 million in tax claims pending against the six other bankrupt railroads which reorganized under the 3R Act.

In each of these reorganizations the Federal Government has either loaned funds under section 211(h) of the 3R Act or guaranteed trustee certificates under the Emergency Rail Services Act of 1970. Both of these statutes provide the Federal Government with a first priority lien status. In the Penn Central reorganization, the Government has guaranteed \$100 million in trustee certificates—\$50 million of which have been defaulted on—and will ultimately loan approximately \$350 million in 211(h) funds, of which not more than \$243 million will be outstanding at any one time.

The Penn Central trustees currently are paying taxes for the period subsequent to January 1, 1977. For the period prior to that time, however, the trustees were authorized by the courts to defer the payment of taxes as part of an effort to maintain rail operations. Such a deferral of taxes is common in recent railroad reorganizations, due to the problem of inadequate cash flows.

As the committee is aware, representatives of State and local governments in the Northeast argued strongly against the liquidation of the Penn Central. Continued operation of the Penn Central was vital to the economy of those areas. This dependency is vividly illustrated by the action of the States of Connecticut, New York, Massachusetts, and Rhode Island in supplying \$7 million annually in cash payments, and the States of Connecticut and Rhode Island in affording complete tax relief to keep the New Haven Railroad—the predecessor of Penn Central—running. In connection with the Penn Central, the Northeast States supported passage of both the Emergency Rail Services Act of 1970 and the 3R Act in order to provide Federal assistance to maintain rail services. These States opposed any discontinuation of Penn Central operations and urged the reorganization of Penn Central under the 3R Act in petitions and appearances before the reorganization court.

The reorganization of Penn Central under the 3-R Act, however, raised numerous and extremely complex legal issues. In order to avoid years of protracted litigation, to everyone's detriment, most claimants, including the United States, have agreed to compromise their claims. Many State and local taxing authorities, however, have not concurred in the treatment of their claims proposed by the trustees.

The Penn Central reorganization court has authorized the trustees to pay all tax claims up to \$10,000 and to offer other tax claimants the choice of two alternative options for the settlement of their claims. The first option, which expires on October 22, 1977, is a cash payment of the greater of 50 percent of the principal amount of postbankruptcy tax claims or 44 percent of the principal amount of total tax claims. Those claimants who do not accept the first option will have their

claims handled in accordance with the plan of reorganization ultimately approved by the court.

The plan of reorganization submitted by the trustees presently authorizes payment of 100 percent of all principal and interest for both prebankruptcy and postbankruptcy claims. The plan provides for cash payment of 20 percent of the principal amount of tax claims—about \$74.4 million—with the remaining 80 percent of principal, plus 100 percent of all interest due on the principal to be paid through the issuance of interest-bearing series C and series D notes.

The series C notes, which would be issued to secure payment of the tax claims relating to property conveyed to ConRail, are payable only out of the valuation case proceeds. The series D notes relate to the tax claims pertaining to assets retained by Penn Central and are general obligations of the reorganized company. Thirty percent of the series D notes (or about \$47.6 million) is payable in the period between 1978–80, with the remainder maturing in 1987, except that if the valuation case proceeds are insufficient to pay these Notes, they would be repaid over a five year period ending in 1992.

The taxing authorities have opposed the plan on the grounds that they are entitled to a prompt cash payment of their tax claims for 100 percent of principal, interest, and penalties. The matter has been extensively briefed before the reorganization court and oral argument is scheduled for October 6. In this connection, the Penn Central trustees have noted defenses against the validity of many of these tax claims which could be raised if the matter were litigated. The courts will be in a position to weigh these claims and defenses, and to insure that the taxing authorities receive all they are entitled to legally and equitably.

In pursuing its own claims against the Penn Central, the Federal Government has accepted less favorable terms than it could have demanded. Historically, and now by statute, the Federal Government's claims against a bankrupt have the highest priority. In the interest of a settlement, however, the Government did not insist on an immediate cash payment of all or a majority of its outstanding claims under the 3R Act and the Emergency Rail Services Act of 1970, amounting to some \$400 million. Instead, repayment of \$115 million was scheduled over the first five years with the remainder being deferred until as late as 1987. In fact, under the proposed reorganization the Government would receive less cash through the first 5 years than would the taxing authorities.

Some \$200 million in cash held in escrow was instead freed for use by the Penn Central trustees in making a settlement offer to State and local tax jurisdictions.

The Government also succeeded in securing payment for personal injury claimants and some 17,000 small, unsecured creditors which probably were not in a position to present their position forcibly to the reorganization court. We have considered the arguments advanced on behalf of H.R. 8882 and while we are sympathetic to the financial plight of the Northeast's cities, we find the case for H.R. 8882 not persuasive. The case for the bill is premised on a finding of culpability on the part of the Federal Government which we do not find to exist. While the continued operation of the Penn Central was made possible

by the Federal Government, the taxing authorities are in a far better position overall because of the continuation of rail services than they would have been if their tax claims had been paid out of liquidated Penn Central.

It is true that the financial assistance advanced by the Federal Government to keep Penn Central operating does by statute have priority over local taxing claims. As I indicated previously, however, the Federal Government, rather than demand first payment of its claims, authorized the use of the estate's assets for a cash settlement to the taxing jurisdictions. It should be noted, too, that the Federal Government provided \$263 million in grants under section 213 of the 3-R Act to the bankrupt railroads, \$293 million in loans under section 215 of the 3-R Act—of which all but \$43 million was forgiven—and \$25 million in low priority loans in connection with Hurricane Agnes, all of which were designed to keep the bankrupt railroads operational.

Moreover, the secured position of the notes given the taxing authorities is sufficiently high so that payment of all or substantially all of their claims is likely. As a consequence, the priority of treatment of notes given in satisfaction of Federal claims does not jeopardize the taxing authorities and is not a sound basis for the enactment of H.R. 8882.

It also has been contended that the Federal Government should have used its bargaining position to obtain more favorable treatment of local tax claims from the Penn Central trustees. The claims against Penn Central and the relative position of the claimants are exceedingly complex. Moreover, the size of the asset base will not be known until completion of the valuation litigation. Whether the trustees' proposed plan fairly and equitably treats local tax claims should properly be resolved by the reorganization court, rather than by the Federal Government, which is itself a major claimant against the Penn Central assets.

Finally, it is argued that the United States should have advanced funds to pay local taxes just as it did for other expenses of maintaining rail services. This argument assumes that the United States should have borne the entire burden of continuing rail operations. In view of the substantial benefits realized by State and local governments from the continuation of rail services, we do not accept this assumption. This suggested form of relief was proposed by Senator Taft during deliberations on the 4-R Act and was soundly rejected by the Senate.

In all likelihood, the taxing authorities will realize 100 percent of their Penn Central claims over a period of time. However, it must be recognized that a Federal guarantee of Penn Central notes would nevertheless expose the United States to some risk because of the uncertain outcome of the valuation case.

In addition, the availability of a Federal guarantee will discourage the taxing authorities from accepting cash offers at less than a 100-percent return, thereby increasing the Federal Government's potential liability for unconstitutional erosion. The 3-R Act special court is currently considering whether the forced operation of the bankrupt railroads at a loss, attributable in part to the accumulation of tax claims, resulted in a taking of property. If this were found to be the case, the Federal Government would have to pay due compensation.

The risks of guaranteeing notes in connection with the reorganization of the other railroads under the 3-R Act are more substantial than those for the Penn Central. Each of these railroads possesses considerably fewer assets with which to meet tax claims and other claims than the Penn Central estate.

Mr. Chairman, I concur fully with the position that I presume that Treasury Department will be taking that there is no sound basis for the Federal Government to step into reorganization or bankruptcy proceedings as guarantor of State and local tax payments. Federal assistance to financially pressed local governments is best provided through programs carefully designed for the purpose.

Mr. ROONEY. Thank you, Mr. Gallamore.

Mr. Gallamore, in testimony last week from the first assistant secretary solicitor of the city of Pittsburgh, I don't know whether or not you read the testimony, but it was contended that in working out a compromise under repayment of Government loans the Department of Transportation agreed to the settlement proposal regarding State and local tax discussed in your testimony.

He also stated that it was completely incomprehensible to him that your department did not demand full payment of local tax and in fact stated the compromise was completely superfluous to any claim the United States had for the repayment of its loans.

I wonder whether or not you would like to comment on those statements?

Mr. GALLAMORE. Let me try and, if I may ask my counsel to assist with the answer.

First of all, there are over 2,000 local taxing jurisdiction involved and it would have been very difficult for the Federal Government to adequately have represented each of their interests. As I mentioned, there were some 17,000 other minor claimants and the Government did attempt to work out a settlement where those could receive some compensation. But it would have been a very difficult matter for the Federal Government to have adequately represented each of those jurisdictions.

The Government did feel it should protect the various elements, as it did, in seeking to resolve the administrative claims other than the tax claims, although that was treated. It did agree to lift its claim on the escrowed assets and it did insist that personal injury claims be paid in full.

Whether or not there was fair and equitable treatment of the State and local taxing jurisdictions is a matter yet to be litigated. We do understand that a staff report from the SEC now has said that they believe the plan of the trustees is equitable, but in the final analysis it is the court which will have to determine whether or not all the claimants were treated fairly.

Mr. ROONEY. The city solicitor for the city of Pittsburgh also testified that the Department of Transportation met with the Friday Morning Club which I assume are the large prebankruptcy creditors and never even consulted the local governments as to whether or not a compromise was acceptable. Is that true?

Mr. GALLAMORE. I wasn't there at the time. Mr. Chairman. My understanding is that information was flowing between the various parties

at that time although that is hearsay as far as I am concerned. I wasn't there personally, nor was my counsel.

I would say in characterizing the Government's position that the crucial matter was to reach agreement with the trustees and to develop from that a plan that provided for settlement of the matter in some way in which some cash would be made available, but since the total resources available at that time were inadequate, the remainder of that obligation had to be met through the longer term notes, as I described in my testimony.

Mr. ROONEY. Mr. Florio.

Mr. FLORIO. Yes, Mr. Chairman, apologies for being late.

I am almost reluctant to ask questions that may have been answered already.

Is it your considered opinion that the claims of the States and the municipality tax due and owing to them can or cannot be paid out of existing settlement that has been offered to the trustees.

Mr. GALLAMORE. It is our anticipation that 100 percent of the claims can be paid eventually.

Mr. FLORIO. Well, eventually. Is that contingent upon an awareness in excess of what has been offered to the trustees?

Mr. GALLAMORE. No, sir, it is not.

Mr. FLORIO. So you feel the amount that has been offered to the trustees is satisfactory to clear all debts, including those of the municipalities, the countries, and the States?

Mr. GALLAMORE. Yes; that is correct.

Mr. FLORIO. Thank you very much.

Mr. ROONEY. Thank you.

The first witness, I understand, has finally arrived.

Mr. ALTMAN. I apologize for being late, Mr. Chairman.

Mr. ROONEY. Mr. Roger C. Altman, and you wish to identify your colleague.

**STATEMENT OF ROGER C. ALTMAN, ASSISTANT SECRETARY OF DOMESTIC FINANCE, DEPARTMENT OF THE TREASURY, ACCOMPANIED BY STEPHEN J. FRIEDMAN, DEPUTY ASSISTANT SECRETARY FOR CAPITAL MARKETS POLICY**

Mr. ALTMAN. Yes; I am accompanied by Stephen J. Friedman, who is Deputy Assistant Secretary of the Treasury for Capital Markets. Again, I am sorry for being late.

I do appreciate this opportunity to present the administration's views on this bill. As you know, it would amend the Regional Rail Reorganization Act of 1973 to require the Federal Government to guarantee any notes issued by certain railroads in reorganization in settlement of their unpaid State and local taxes. The guarantee would be required in cases in which the Federal Government, certain Federal agencies or ConRail assert any priority over State and local claims.

Mr. Chairman, as you know, the amount of deferred taxes involved here is large. In addition, these funds are owed to those State and local governments which probably are experiencing the greatest fiscal strain in the United States. In fact, the administration is devising urban and regional policies to assist these areas right now. Some of these policies will be announced by the President in just 3 or 4 months.

In short, we are highly sympathetic to the fiscal difficulties of this region and we would like to help the States and localities involved receive these back taxes. Yet, Mr. Chairman, there are fundamental reasons why this legislation is not the way to do it.

In our view, the U.S. taxpayer simply cannot bear the responsibility of insuring that private railroads in reorganization pay their State and local taxes. This argument is overriding and the administration cannot support this bill as a result of it.

I know that you are aware that this legislation arises out of the complicated reorganization proceedings of seven Northeast and Midwest railroads, of which the largest by far is Penn Central. It owes roughly \$326 million in principal amount of unpaid State or local post-bankruptcy tax to 17 States and numerous localities, as well as the District of Columbia.

The Federal District Court presently has under consideration a proposed plan of reorganization of the Penn Central on which it probably will rule later this year. That plan, of course, provides for paying some of these taxes in cash and the rest in securities. This bill, H. R. 8882, however, would facilitate the payment of essentially all of them in cash.

Mr. Chairman, I will submit for the record the discussion of the reorganization proceeding itself as well as the compromise offer which has been made to the State and local taxing authorities.

The CHAIRMAN. Without objection, it will become part of the record.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. ALTMAN. Let me turn to the factors which are motivating the taxing authorities and their representative State and local governments to urge Congress to consider this bill. Most of these State and local governments, Mr. Chairman, support the bill because they essentially object to the proposed reorganization plan.

For example, some local taxing authorities argue that they are prohibited by State law from accepting the securities offered. They have raised doubts about the fairness and constitutionality of the reorganization plan. These are questions that should be and are being determined by the courts. We have made no independent judgment on them and it would not be appropriate for us to do so. Rather, let me discuss briefly what we see to be the public policy implications of this proposed bill.

First, Mr. Chairman, it would give to State and local authorities a claim against the United States in addition to the claim against Penn Central. Accordingly, those taxing authorities would have a claim which is better than that of the United States because our claim must be satisfied against Penn Central alone. That result would violate the general principle that claims of the United States against bankrupt estates are superior to those of State and local governments.

Second, the sole value of the series C notes to the United States depends upon the value ultimately accorded to the assets which the Penn Central transferred to ConRail. That value, as you know, is presently being determined in a special proceeding in which the United States is in the position of arguing for a lower, rather than a higher, value. The basic purpose of that special proceeding is to determine the amount of any additional compensation payable by the United

States to the Penn Central in exchange for these assets the United States would be maintaining a position in proceeding that would result in a lower payment by the in respect to these series "C" and "D" notes even though anteing their full face amount.

Mr. FLORIO. Mr. Chairman, just to get a point clear United States is arguing for a lower rather than a high the valuation proceedings. You don't mean the lower than you mean a lower than was requested?

Mr. ALTMAN. Well, what I basically mean is that the of the United States is better off the lower the valuation transferred to ConRail is.

Mr. FLORIO. The United States is not in court and amount paid should be lower than was offered, lower than by—

Mr. ALTMAN. That is correct; that wasn't my intent.

Mr. FLORIO. Thank you. Mr. Chairman.

Mr. ALTMAN. The third basic point I want to make Chairman, is that, subject to the supervision of the Federal court, the Penn Central trustees are engaged in a complex task of balancing the claims and interests of each group. The provisions of the plan of reorganization and the series of compromise are an integral part of that balancing. A general guarantee would mean that no State and local tax accept the offer of compromise because, of course, the guarantees would be immediately salable.

We understand the desire of State and local government a fair and equitable settlement of their tax claims on roads. We realize that the value of the series C notes the outcome of pending litigation which is testing the assets transferred by the bankrupt railroads to ConRail. The outcome of this litigation is not certain. Nevertheless, in the outset, we are concerned that the U.S. taxpayer not be of insuring the private railroads in reorganization and local tax bills.

In addition, we are concerned that the Federal Government increase its liability exposure in connection with reorganization. In the case of Penn Central, the Federal Government has claims totaling approximately \$390 million exclusive of \$60 million. The proposed legislation, Mr. Chairman, would guarantee the Federal Government a potential \$800 million of principal and interest on series C and series D Penn Central. Finally, the effect of the proposed bill would be to prevent the Federal Government from guaranteeing municipal security interest revenue anticipation notes.

For the foregoing reasons, the administration supports H.R. 8882. We believe that the rights of all creditors should be protected with by the courts under the framework established by the Emergency Rail Services Act of 1970 and the Reorganization Act of 1973.

If some States are precluded by State law from offering secured notes, and if they did not find the pro-

acceptable, they ought to seek a change of law at the State level, Mr. Chairman.

Thank you and I would be happy, of course, to answer any questions.

Thank you and I would be happy, of course, to answer any questions.

[Mr. Altman's prepared statement follows:]

STATEMENT OF ROGER C. ALTMAN ASSISTANT SECRETARY OF THE TREASURY

Mr. Chairman, I appreciate this opportunity to present the views of the Administration on H.R. 8882. That bill would amend the Regional Rail Reorganization Act of 1973 to require the Federal government to guarantee any notes issued by certain railroads in reorganization in settlement of their unpaid state and local taxes. The guarantee would be required in cases in which the Federal government, certain Federal agencies, or ConRail asserts any priority over state and local claims.

Mr. Chairman, the amount of deferred taxes is large. In addition, these monies are owed to those state and local governments which probably are experiencing the greatest fiscal strain in the United States. The Administration is devising urban and regional policies to assist these areas. Indeed, certain of these policies will be announced by the President in just three or four months. In short, we are highly sympathetic, therefore, to the fiscal difficulties of this region. We would like to help them receive these back taxes. Yet, Mr. Chairman, there are fundamental reasons why this legislation is not the way to do it. The U.S. taxpayer simply cannot bear the responsibility of ensuring that private railroads in reorganization pay their state and local taxes. This argument is overriding, and the Administration cannot support H.R. 8882.

This legislation arises out of the lengthy and complicated reorganization proceedings of seven Northeast and Midwest railroads. The largest of these by far is the Penn Central Transportation Company. It owes approximately \$326 million in principal amount of unpaid state or local post-bankruptcy taxes to 17 states and many localities within them and the District of Columbia. The Federal District Court presently has under consideration a proposed plan of reorganization of the Penn Central on which it probably will rule later this year. That plan includes provisions for paying some of these taxes. This bill, however, would facilitate the payment of essentially all of them.

Until recent years, treating of state and local tax claims as they are being treated in the Penn Central reorganization proceeding would have been unusual. In earlier cases, when a railroad company was reorganized, the taxes accruing after the reorganization proceeding were usually paid currently, as expenses of administration. In the case of the Penn Central, I understand that the Court enjoined payment of these taxes. That injunction remained in effect for all periods through January 1, 1977.

Then, in 1973, the Congress adopted the Regional Rail Reorganization Act. That statute, as amended by the Rail Revitalization and Regulatory Reform Act of 1976, provided, among other things, for the priority payment of certain administrative claims against the Penn Central under Section 211(h). Under this procedure, Federal money is loaned to ConRail to pay certain classes of administrative claims against Penn Central. ConRail then obtains a priority claim against Penn Central in the same amount as the claim it has paid, to insure repayment of its loan. Labor and supplier claims against Penn Central are the principal claims eligible for payment under this procedure. \$350 million is authorized under Section 211(h) for loans to ConRail to pay these claims. Currently, such loans, together with accrued interest, aggregate approximately \$234 million.

The proposed plan of reorganization of the Penn Central provides for the payment of state and local tax claims as follows: cash payments equal to 20 percent of the principal amount of unpaid taxes; and secured Series C Notes and Series D Notes equal to 80 percent of the principal amount plus accrued interest. The Series C Notes, which are issued to satisfy state and local taxes on properties conveyed to ConRail, are not general obligations of the reorganized company, but are secured by, and are payable from the proceeds of the assets conveyed

to ConRail subject to the prior claim of the United States. Series D Notes are issued in satisfaction of state and local taxes on property not conveyed to ConRail. The Series D Notes are general obligations of the reorganized company and also have a secondary lien on the proceeds of the assets conveyed to ConRail.

The Penn Central trustees have made an alternative offer to each taxing authority. In exchange for surrender of all its outstanding tax claims, a taxing authority would be paid 50 cents in cash for each dollar of the principal of tax claims arising after the Penn Central filed for bankruptcy, or 44 cents in cash for each dollar of the principal of pre- and post-filing tax claims, whichever is higher. Claimants having claims of \$10,000 or less will be paid in full. State and local tax authorities have until October 19 to accept this offer. Those who did not accept will be able to pursue their rights under this plan of reorganization referred to above.

The state and local governments now urge the Congress to enact legislation that would provide a Federal guarantee of the secured notes which they would receive under this plan of reorganization. It also would operate in any similar provisions of future plans of reorganization for the other six railroads.

One of the reasons that state and local governments support this Bill is because they object to the proposed reorganization plan. For example, some legal taxing authorities argue that they are prohibited by state law from accepting the securities offered. They have raised doubts about the fairness and constitutionality of the reorganization plan. These are questions that should be, and are, being determined by the courts. I have made no independent judgment on these questions and it would not be appropriate for me to do so. Rather, I would like to discuss briefly the public policy implications of H.R. 8882.

What would be the effect of this legislation? First, it would give to state and local taxing authorities a claim against the United States in addition to a claim against the Penn Central Transportation Company. Accordingly, those authorities would have a claim far better than that held by the United States, since the claim of the United States must be satisfied against Penn Central. That result would violate the general principle that claims of the United States against bankrupt estates are superior to those of state and local governments.

Second, the sole value of the Series C Notes to the United States depends upon the value ultimately accorded to the assets that the Penn Central transferred to ConRail. That value is presently being determined in a special proceeding, in which the United States is in the position of arguing for a lower, rather than a higher, value since the basic purpose of the proceeding is to determine the amount of any additional compensation payable to the Penn Central in exchange for these assets. Accordingly, the United States would be maintaining a position in the valuation proceeding that would result in a lower payment by the Penn Central in respect of these notes, even though the United States is guaranteeing their full face amount.

Third, subject to the supervision of the Federal District Court, the Penn Central trustees are engaged in the complex and difficult task of balancing the claims and interests of each group of creditors, taking into careful account possible weaknesses in the legal position of each group. The provisions of the plan of reorganization (and the alternative offer of compromise) are an integral part of that balancing process. A Federal guarantee would mean that no state and local tax creditor would accept the offer of compromise because the guaranteed securities would be immediately salable.

We understand the desire of state and local governments to obtain a fair and equitable settlement of their tax claims against the railroads in reorganization. We know that the value of the Series C Notes is dependent on the outcome of pending litigation which is testing the value of the assets transferred by the bankrupt railroad to ConRail, and that the outcome of that litigation is not certain. Nevertheless, as I said at the outset, we are concerned that the U.S. taxpayer not bear responsibility of insuring that private railroads in reorganization pay their state and local tax bills.

In addition, we are concerned that the Federal Government not increase its liability exposure in connection with railroads in reorganization. In the case of the Penn Central, the Federal Government presently has claims totalling approximately \$390 million, excluding the Federal Government's tax claim of \$60 million.

The proposed legislation would have the Federal Government guarantee a potential \$800 million in principal and interest on Series C and Series D Penn Central notes alone. Finally, the effect of the proposed statute would be to create the equivalent of a Federally guaranteed municipal security if the holders issue revenue anticipation notes.

For the foregoing reasons, the Administration does not support H.R. 8882. We believe that the rights of call creditors are best dealt with by the courts under the framework established by Congress in the Emergency Rail Services Act of 1970 and the Regional Rail Reorganization Act of 1973. If some states are precluded by state law from accepting the offered secured notes, and if they do not find the proffered compromise acceptable, they should seek a change of law at the state level.

Mr. ROONEY. Thank you.

I note the author of this legislation has arrived.

If you would like, you may sit at the table, Ms. Oakar.

Mr. Altman, on page 1 of your testimony, you talk about the deferred taxes and how large they are, and you say the administration is devising urban and regional policies to assist these areas.

I didn't know about this. Tell me something about it.

Mr. ALTMAN. Well, I am sure you are aware that the President has pledged to develop a comprehensive urban policy, and the current timetable for that, Mr. Chairman, is that he will refer to it in the state of the Union message obviously just after the turn of the year and then unveil it in detail in a special message just after that statement.

Mr. ROONEY. What is that going to cost.

Mr. ALTMAN. No decisions have been made yet, Mr. Chairman, on the components of that policy or of course, the costs. The proposal of that new set of programs to Congress is still 4 or 5 months away. The point I was making in the testimony is that we are working on a coherent urban policy. Most of the States involved here have a heavy urban character, and we are very sympathetic to the fiscal difficulties which they experience. These difficulties have, of course, increased their natural interest in seeing this legislation enacted because it would enable them to obtain now essentially 100 cents on the dollar of their tax claims rather than having to wait for the notes to be paid.

As I have said in the testimony, however, we don't think this is an appropriate way to do it. But we understand why the State and local governments have a strong interest in this bill, and we sympathize with their concerns.

Mr. ROONEY. Mr. Florio.

Mr. FLORIO. Just following up on that point, not being unkind, but the fact of the matter is, there is very little relevance of one to the other, the fact we have outstanding tax bills, you are talking about the fiscal dilemma of the urban area and now saying there is going to be an urban policy with your assistance and there are those who make the arrangement. Those things are necessary and long overdue. I am not sure you can offer the fact we are becoming aware of the cities and urbanized areas; that is, therefore quid pro quo or compromising or forgetting about the tax bills. I understand what you are saying, the administration is to be commended for coming up with the urban policy. I am not sure the relationship of the one to the other is very persuasive in terms of just saying that we are not going to support this approach because we are coming up with some other approach to assist the cities.

Mr. ALTMAN. That, though, was really not my point. We would not support this legislation, regardless of whether we were developing a serious urban policy, because of the reasons I set forth. My point was that there is a group of us in the administration—I happen to be one—who are spending a lot of time, 7 days a week, working on a possible urban development bank and certain fiscal relief measures for the cities. The Administration's urban policy will have many components which will deal precisely with some of the reasons why many of the States and localities involved here are under serious fiscal strain. Many of them are arguing, understandably, that a simple way for the administration to provide fiscal relief would be to support this bill. But we think a fiscal relief program ought to be developed and considered as well.

Mr. Florio. The point I am making is supporting this bill and providing the relief is not providing any additional relief, it is providing to the municipalities the revenues that they relied upon and were duly entitled to and have a right to expect. We are talking about a certain category of taxpayer here that is somewhat unique. If you don't pay your taxes and I don't pay my taxes, that works a hardship upon municipalities we come from.

Let me raise a couple of other points.

One, if you place any credence in the comments of the representative of FRA, as I am willing to do, that there is an expectation that the existing level of valuation will pay off the debts that are owed.

Now, you have indicated you are not seeking any less money. I don't think there is any realistic expectation that less money will be provided by the courts. If anything, more money will be provided by the courts for the trustees which will provide that much more added security to the Federal Government that they will not be required to pay off on the loan guarantees.

If that is the case, I am not really sure where I see the Federal Government being jeopardized by providing loan guarantees.

Now, you went into a couple of esoteric arguments about increasing the security of the municipal bondholders because they now have Federal guarantees and the Federal Government wouldn't have a Federal guarantee.

Well, I think that is nice; I think it is somewhat academic; the bottom line is whether we think the Federal Government is going to have to pay off on these notes that may be issued. I am willing to accept the gentleman's comments. Unless you have evidence to the contrary, it doesn't look like the Federal Government would have to pay off on the notes.

Do you have any evidence to the contrary?

Mr. ALTMAN. No; I agree with the position that he took, but I don't think that that is decisive in terms of supporting or not supporting this legislation. Among other things, there is the question of whether there would be sufficient cash to avoid a default on the guaranteed notes in the case of the railroads other than Penn Central. The answer to that question is not at all clear, and this legislation, of course, would pertain to them.

Second, it seems to us that in other railroad reorganizations there may be, as I just stated in the case of the other six railroads, substantial risk of default and we believe that the U.S. Government should not be put in the position of making investment decisions.

In other words, the U.S. Government should not be required to decide that it will facilitate the payment of back taxes in cases where it believes that the risks under its guarantees are not substantial, and not help in cases where there are serious risks of default so that the Government might have to honor its guarantees by providing the funds to pay the railroads' State and local tax obligations.

It just seems to us that this would be a politically impossible and inequitable position for the Federal Government to be put in.

Mr. FLORIO. Are you saying then you don't seem to have any question about the solvency, so to speak, of the assets of the Penn Central; you have questions about the other railroads?

Mr. ALTMAN. That is right.

Mr. FLORIO. If in fact this was modified since the Penn Central is clearly the largest debtor, that would eliminate one of your major objections?

Mr. ALTMAN. No; I don't think so because I think the conceptual and precedential arguments that I tried to make in my testimony are overriding.

Mr. FLORIO. Notwithstanding the fact you seem to concede that there seems to be no financial obligations which will flow to the United States as a result of the Penn Central guarantees.

Mr. ALTMAN. First of all, I don't think anyone can be certain of that. I am not certain of it. In the absence of that kind of certainty I frankly don't think that we could support this bill. Fundamentally, it does come down, to a large extent, to the question of the role of the general taxpayer vis-a-vis taxpayers in certain areas. We don't think the U.S. taxpayer ought to be in the position of requiring or insuring that railroads in reorganization pay their tax obligations to certain State and local governments.

Mr. FLORIO. Let me make one final observation. Correct me if I'm wrong, I get the clear impression that you were indicating you felt that there was some value to the settlement agreement and that there you had some interest in seeing the settlement agreement be carried out. Is this the official policy of the Department, that the settlement agreement is something that is in the public interest and should be carried out?

Mr. ALTMAN. No; it is not a matter of policy at all. I didn't mean to imply that.

Mr. FLORIO. Well, the only point is I think that the substantial difference, I will realize it is acceptable business practice to compromise claims, general business claims, but I am not sure that anybody should be in the position of urging lesser levels of government to be compromising tax bills.

Mr. ALTMAN. We agree with that.

Mr. FLORIO. As you indicate, there are a number of States, my own included, that haven't got the statutory authority to accept compromised tax bills if they wanted to. So many of our municipalities and the counties are in the unusual situation where they have been told here is the option, you can take this if you want to, even though the law doesn't allow you to, and if you don't take it there is no guarantee provided pursuant to this type of legislation, you have no remedy, therefore, you lose all the money. You can appreciate that is a somewhat unfortunate position to be in as far as municipalities are concerned.

Mr. ALTMAN. Well, we agree and are not urging any action of one type or another on the part of the State and local governments with respect to the compromise or original proposed plan or any other action.

Mr. FLORIO. Thank you, Mr. Chairman.

Mr. ROONEY. Ms. Oakar.

Ms. OAKAR. Thank you, Mr. Chairman.

Mr. Chairman, again I want to thank you for having this hearing. I do have quite a few questions, but I will try to limit it and you cut me off when you think it is appropriate.

Mr. ROONEY. The gentlelady from Ohio is recognized for 5 minutes.

Ms. OAKAR. I shouldn't have said that.

But I do appreciate your courtesy very much, Mr. Chairman.

Mr. Altman, first, as you can imagine, I am very dismayed both by the administration's position, not so much for myself but for all of the municipalities that are affected. Your testimony that I have just had a chance to read just now, the whole tone of your testimony indicates that you really feel it would be a great risk to the Government. You quote a figure of \$800 million if the Government would guarantee these notes. Where did you get that figure?

Mr. ALTMAN. That is, as I understand it, the total amount of pre-bankruptcy and postbankruptcy tax claims including interest.

Ms. OAKAR. It is really \$523 million, but we won't debate that because it is a substantial amount.

Mr. ALTMAN. Let me clarify that.

Mr. FRIEDMAN. I wonder if I could add something to that. That number is calculated by taking the principal amount of the securities that would be issued, which is approximately \$500 million, plus the interest that would be payable on those securities until maturity—up to 10 years. I don't think there was intention to say that was a measure of the Government's exposure, but it is a measure of what the Government is undertaking.

Ms. OAKAR. I want to assure you, Mr. Chairman, and members of this committee, that members of the Justice Department have said that there will be little, if any, risk as it relates to this particular issue.

I am concerned about the urban problem of the policy of the President, based on my work on another committee. Is this urban policy going to affect towns like Moundsville, W. Va., and Taneytown, Md., that are also in line and support this legislation? Is the President going to come out and help these little towns, because there are more than urban areas affected?

Mr. ALTMAN. I appreciate that. I can only say that, frankly, this set of policies is actually in the middle or perhaps latter stages of evolution, but there have been no decisions on the various components which will make up the essential urban policies to be proposed by the President. I don't know if it is a total answer, but I assure you that I am personally working on a couple of aspects of this, which are taking up most of my time, and that we are quite sensitive to the fact that there are equivalent rural development problems.

Ms. OAKAR. If you don't mind, I really want to get to my other questions. I want to call your attention to the fact that some of us

are hoping that over and above the problems that are affecting our urban areas we want a policy that is new and different, not just to cope with the current kind of backlog type of problems, and it is a little disappointing this is going to include this problem.

The other point I want to make, and this was really illustrated very well, I think, by an editorial that appeared in one of our local newspapers the other day about Lockheed, is that it is a fact that there are 163 Federal loan guarantee programs and that the risk of guaranteeing series C, and series D notes would be as little risk, if not lesser risk, as these existing programs that in no way have ever cost the Federal Government a penny.

And a good example of that is the editorial that was in one of our Washington papers citing Lockheed as an area in which the Government had guaranteed some notes and in fact these were doing very well and there was not a problem.

So if you could cite me an instance where the Federal Government guaranteed a loan program where they went under, I would like to hear it.

Mr. ALTMAN. An instance of where a guarantee—

Ms. OAKAR. Guaranteed by the Federal Government.

Mr. ALTMAN. Unfortunately, there are quite a number of instances like that. For example, the \$100 million of trust certificates issued by the Penn Central and guaranteed by the Federal Government under the Emergency Rail Services Act at the outset of this postbankruptcy proceeding. Of that \$100 million of guaranteed certificates, \$50 million are presently in default. The Federal Government has had to make the principal and interest payments. The other \$50 million, it appears, will also be in default. Thus, in this case, you have an example of a Federal guarantee in which the Federal Government has had to step up and pay the interest and principal which, in most guarantee programs, it is hoped the borrower will do. I would also say there are a couple of clear differences between this instance and Lockheed, although I don't want to get into that.

Ms. OAKAR. I don't either. I wanted to cite that point.

How would the administration view the bill? Do you think it would change if the Federal Government had recourse with the reorganization companies if the Secretary of Transportation indeed had to pay some of these series C notes?

If we had added an amendment to the bill to that effect, how would you view it then?

Mr. ALTMAN. I don't know how the administration would come out on that because I can't speak for the administration on a new piece of legislation. I think, though, that it would be difficult for the administration to support it even if the notes were with recourse because of the basic relationship I talked about earlier between general taxpayers and local taxpayers and what this would do to that relationship.

But I can't say definitively either way. We would take a look at it in a good spirit.

Ms. OAKAR. You see, you understand the problem that these municipalities are in. They are second in line against the lien. You are first in line, and there is a decisive thing that the Federal Government has over the local municipalities.

Mr. ALTMAN. I realize that, of course, though the Federal Government almost always is first in line by general statute and by specific statute.

Ms. OAKAR. It doesn't make it right.

Mr. ALTMAN. There is an enormous body of law over decades which has established that principle.

Ms. OAKAR. Mr. Chairman, I wanted to just reiterate the fact that in no way is there direct dollars involved. And I think there is an implication that this is the case and I think that many of the municipalities are not willing to wait 3 or 4 months until the President gets around to an urban policy. You know, I think that that is really a problem and that kind of notion that this would satisfy these municipalities, many of which are going under right now in terms of their school systems. Toledo, Ohio has already announced that in October they are closing their doors unless there is some kind of critical legislation passed. Cleveland, my own city; this is happening in New Jersey, the State of New York, the State of Massachusetts, and so forth. I don't think the arguments, Mr. Chairman, and members of this committee, warrant this kind of opposition to the legislation.

Mr. ALTMAN. Let me reiterate with respect to that last point you made that I am not trying to emphasize that the localities involved don't need to worry about this particular piece of legislation because we will be dealing with this problem out of another hand in the forthcoming urban policy. That is not my point. My point simply was we have been studying very hard the fiscal difficulties of these State and local governments. We are trying to devise a policy which will assist them. But in fairness, whether or not we were doing that would have no effect on our position on the basic merits of this bill.

Ms. OAKAR. Mr. Chairman, just one last point, and that is that if there is this shortfall between \$500 million and \$800 million, without this legislation wouldn't we see problems with the loss of the jobs and revenue and so forth that comes in because all of our institutions, like our educational system is operative; I mean, are you considering that cost to the Federal Government, it is going to take place without some kind of guarantee with these notes. That option, has that occurred to you, do you know what costs that would imply?

Mr. ALTMAN. Yes; we have taken that into account. In fact, that is why in the first page of my statement I pointed out that we are not only aware of the fiscal difficulties in these areas which are impinging, among other things, on school systems, but are doing our best in another forum, the urban and regional policy group, to come up with ways that will provide fiscal relief to these areas or provide incentives for them. So I can only say, and hope you take it in good faith, that we are sensitive to this problem and that is precisely why I wanted to emphasize that point at the outset of my testimony.

This, in general, is a matter of legal precedent and I could agree and do agree with almost all the points you have made about the fiscal difficulties of these regions and the effect they are having on individual localities, but that is another set of factors in addition to the legal factors which in this case have to be overriding.

Ms. OAKAR. Well, if the bill is limited only to Penn Central, wouldn't the precedent then be to examine the situations on a base-by-base basis, however?

Mr. ALTMAN. Let me simply say if the bill is amended to limit it to Penn Central we will take a good faith look at it. There will be a lot of other agencies which will have to be involved, including the Justice Department, as it has been involved in developing this position. We will do our best to develop a quick position on it.

Ms. OAKAR. Mr. Chairman, just one point for the record. And that is that if, since I know you have indicated that the committee may have a markup soon, I had to wait several months for a response from the Department of Transportation as to the administration's position. Could you within the next few days give to the chairman and myself perhaps a response to the question I asked about a possible amendment to the legislation that would grant the Federal Government a resource with the organized companies?

Mr. ALTMAN. Yes; we will do that.

Ms. OAKAR. Thank you, Mr. Chairman.

Mr. ROONEY. Thank you, Ms. Oakar.

You mentioned six other bankrupt railroads could possibly be involved in this. How much is outstanding with the six railroads? You said \$523 million with the —

Mr. ALTMAN. I don't know specifically, Mr. Chairman, but I would be happy to supply that for the record.

Mr. ROONEY. We would appreciate it very much.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. ROONEY. Thank you, Mr. Altman, Mr. Friedman, for appearing.

Mr. FRIEDMAN. To clarify your question, it is the amount of loans under 211(h) and other obligations to the United States that you would like furnished to the committee?

Mr. ROONEY. Yes.

Mr. FRIEDMAN. Thank you.

Mr. ROONEY. Thank you.

Our next witness will be Mr. Dickieson, General Counsel, USRA. I would appreciate it very much if you would introduce your colleagues for the record.

**STATEMENT OF CARY W. DICKIESON, GENERAL COUNSEL, UNITED STATES RAILWAY ASSOCIATION, ACCOMPANIED BY EDWIN RECTOR, ASSISTANT GENERAL COUNSEL, AND ALBERT J. FRANCESE, LEGISLATIVE COUNSEL**

Mr. DICKIESON. Yes, Mr. Chairman.

Mr. Chairman, I appreciate this opportunity to present the views of the United States Railway Association on H.R. 8882. With me on my right are Mr. Edwin Rector, Assistant General Counsel—Finance; and on my left is Mr. Albert Francese, legislative counsel. Other witnesses have described the proposed bill and some of the complexities involved. I will endeavor to be brief and not repeat what has already been described.

The association's interest in H.R. 8882 stems from its status as holder of the claims of the United States arising under section 211(h) of the Regional Rail Reorganization Act of 1973, as amended, and from

its responsibility for conducting the valuation litigation resulting from the Rail Act. We perceive problems with H.R. 8882 that could affect adversely the interests of the association and the United States in both of these areas. I will discuss the section 211(h) problems first, and the valuation case second.

The association agreed to a settlement of its section 211(h) claims against the Penn Central estate as part of the outline of settlement between the United States and the Penn Central trustees. There, the Federal Government agreed to accept for its claims, including the association's section 211(h) claims, series B notes maturing in 1987. These series B notes are quite similar to the series C and D notes, which the State and local taxing authorities are so reluctant to accept. The major differences are that the series B notes are secured by a lien against all assets of the reorganized company, while the series C notes have a lien only on the proceeds of the valuation case, and the series D notes are general obligations of the reorganized company. The superiority of the treatment given the Federal claims over that of the State and local claims follows directly from the high priority Congress provided in section 211(h) and the Emergency Rail Services Act of 1970 (which authorized the Federal guarantee of trustees' certificates) and decisions under the bankruptcy laws.

Despite the somewhat better security provided series B notes, the Federal Government is still being asked to accept the same deferral in payment as the State and local taxing authorities. Nor has any special recognition been given for the more than \$500 million in aid provided under sections 213 and 215, or for the prompt implementation of the final system plan which created a new taxpaying railroad on April 1, 1976, all of which provided substantial benefits to those States and localities.

The major problem with H.R. 8882 as now drafted insofar as it might affect the Government's settlement with the Penn Central, is that it could produce new objections to the trustee's plan, a plan which the United States supports. While I have not been advised that any specific creditor group has objected, it is always risky for Congress to interfere with pending litigation by imposing in midstream some new ground rules. The trustees' plan represents a carefully and exhaustively negotiated compromise of an extremely complex set of legal issues. The plan has been tested in hearings before the reorganization court and has been reviewed in a report prepared by the staff of the Securities and Exchange Commission. It still must be passed upon by the reorganization court, and perhaps by the court of appeals and the Supreme Court. Throughout, the States and local taxing authorities have had ample opportunity to present their positions and obtain a court determination as to the fairness and equity of the treatment they have been offered.

Passage of H.R. 8882 could also affect adversely the Government's position in the reorganization of the other six bankrupt railroads. The Government has not yet negotiated settlements of its claims against those bankrupt estates. But in each of those reorganizations, the Government has been asserting the priorities afforded its claims under Federal law, and as H.R. 8882 is now drafted, the guarantee provisions would be triggered by that assertion even if the plans themselves do not recognize the Government's priority position. Moreover, the proposed legislation would require the guarantee of any

notes used to settle State and local tax claims without regard to their terms, thereby providing a sure incentive for the quality of the paper offered State and local taxing authorities to be low since there would be a Federal guarantee behind the notes. In short, this bill would require the Federal Government to buy a pig in a poke.

H.R. 8882 would also adversely affect the interests of the United States in the complex valuation proceedings now being conducted before the special court as a result of the Rail Act. First, the bill would reduce the benefit to the Government of a successful outcome in the valuation case since, at least in the case of the Penn Central estate, the lower the outcome in the valuation case, the greater the probability the Government might be required to honor its guarantee of the series C and D notes. With respect to the other estates, it can be assumed that the relative risk of that result is greater because the other estates are less well endowed with assets than the Penn Central.

Second, assuming that series C and D notes backed by a Federal guarantee could be sold for more than 50 cents on the dollar, passage of H.R. 8882 might influence more taxing authorities to accept the series C and D notes rather than the alternative cash settlement, a result which increases the Government's potential liability with respect to the bankrupt estates' claims for alleged pre-conveyance erosion. The offer of a cash settlement to the State and local tax claims was an important benefit for which the Government bargained in its settlement with the Penn Central, a benefit which this bill would give away.

That concludes my comments concerning H.R. 8882. I will be happy to answer any questions.

Mr. ROONEY. Mr. Florio.

Mr. FLORIO. Yes, sir.

Tell me how other creditors would be deferred by the loan guarantee provided to the State municipalities?

Mr. DICKIESON. The essence of the Penn Central plan as indeed the essence of any plan in a reorganization as complex as that of Penn Central is compromise. The Federal Government had to accept numerous compromises. The lower level claimants also accepted compromises, and they did this in the context of the overall plan. If you now provide better treatment for one of the groups of claimants, you potentially will make others unhappy with the compromise as they accepted it. You have changed the specific—

Mr. FLORIO. Somebody may be happy. You are not talking about taking from the assets giving to one group of creditors more of the assets than anyone else. All you are doing is insuring that the—

Mr. DICKIESON. Lower level claimants might argue that since there is now a Federal guarantee behind the C and D notes, the assets of the reorganized company dedicated to the payment of those notes should be made available to them.

Mr. FLORIO. You are anticipating someone else coming in and asking for a loan guarantee for a lesser group, lesser level group of creditors.

Mr. DICKIESON. No; I am not anticipating anything and I am not aware that anyone has done so far; but whatever you do in the middle of great complicated litigation such as this reorganization plan you interfere with the circumstances under which compromises are reached and you raise the potential of opening up the whole issue again.

Mr. FLORIO. I am not overly impressed with the argument behind that. I think if there was something more specific I would be happy to

listen, but I don't think there is any lesser category of creditors that are realistically going to say, well, the States and localities got loan guarantees, therefore, maybe we can get loan guarantees and maybe we won't accept because of that possibility.

Mr. DICKIESON. I don't know that they would be asking for loan guarantees. I would think they would be asking for a restructuring of the plan that would provide them with a claim, a greater claim on the valuation case proceeds or would otherwise reduce the security behind the C and D notes to their benefit.

Mr. FLORIO. Reduce?

Mr. DICKIESON. The security behind the C and D notes. They would argue, why should such a great portion of the estate's assets be dedicated to payment of C and D notes now that they have a Federal guarantee, why shouldn't they be made exclusively available for us?

Mr. FLORIO. Thank you, Mr. Chairman.

Mr. ROONEY. Ms. Oakar.

Ms. OKAR. You mentioned that this was worked out in a compromise and one of the reasons I introduced the bill was because State and local authorities from across the country told us that they felt that they had very little input in the compromise. I mean, frankly, cities like my own Cleveland don't believe it is an equitable compromise to get 36 cents on the dollar. Could you be more precise in how every municipality and what kind of input did they have in and resource in compromising?

Mr. DICKIESON. I cannot directly answer that question. The associations involvement in the negotiations that led to the Government settlement with the Penn Central trustees was quite limited, it only related to the section 211(h) claims that we were holders of so I can really not answer your question. We certainly in those negotiations represented simply the interests of the association, not that of anyone else.

Ms. OKAR. Would you like me to yield?

Mr. FLORIO. What is the status of the litigation now? It is my understanding some of the Attorneys General were considering going back and asking either for an extension or by petition asking for other alternatives. Has there been any initiation of repeal by any of the Attorneys General?

Mr. DICKIESON. Which litigation are you referring to?

Mr. FLORIO. Litigation with regard to the compromise.

Mr. DICKIESON. With regard to the plan of reorganization of the Penn Central?

Mr. FLORIO. Yes.

Mr. DICKIESON. My understanding is that case has been briefed to the reorganization court; oral argument to the reorganization court will be held later this month.

Mr. FLORIO. Thank you.

Ms. OKAR. It is my understanding, just for the benefit of the members of the committee and yourself, that in fact the State and local taxing authorities were not involved in the outline of settlement so when you use the term "compromise" they were all involved. I think we ought to be a little more specific about that issue.

Mr. DICKIESON. The compromise with respect to the State and local taxing authorities would not have taken place in the negotiations concerning the outline of settlement. We were simply settling the Federal claim. That compromise would have taken place in the negotiations by the Penn Central trustees with the various claimant interests.

Ms. OAKAR. But the overall outline of settlement was drawn up, apparently they were not specifically involved and that is why they feel they did not have the input they would have liked to have because obviously they would have been in a sense attempting to get a more equitable settlement for them. It is not equitable.

Mr. DICKIESON. Well, whether the settlement is equitable or not, they have the legal right to have determined by the reorganization court and that is where they now stand.

Ms. OAKAR. Has Congress ever interfered with—you mentioned that you feared Congress interfering with pending legislation or litigation of the Railroad Act. Have we ever interfered in the past in litigation?

Mr. DICKIESON. It is something which Congress does very rarely, I believe.

Ms. OAKAR. Have we ever done it as it relates to this act?

Mr. DICKIESON. As it relates to this act?

Ms. OAKAR. If you don't know the answer, would you give me the answer?

Mr. DICKIESON. Yes.

Ms. OAKAR. OK.

I don't have any further questions, but I just want to make it very clear that the municipalities, State and local governments, do not feel they were not involved as precisely as they wanted to be as it relates to the so-called compromise that you invoked yourself and do not know the answer to, which is the thrust of one of your arguments as to whether or not there have been bills that somewhat relate to pending litigation. That is, I would like that answer for the record.

Thank you, Mr. Chairman.

[The information requested was not available to the subcommittee at the time of printing.]

Mr. ROONEY. Thank you, gentlemen.

Our next and final witness is Robert W. Blanchette, chairman of the board of trustees and chief executive officer, Penn Central Transportation Co., Philadelphia, Pa.

Mr. Blanchette, the committee welcomes you.

**STATEMENT OF ROBERT W. BLANCHETTE, CHAIRMAN OF THE BOARD OF TRUSTEES AND CHIEF EXECUTIVE OFFICER OF THE PENN CENTRAL TRANSPORTATION CO., ACCOMPANIED BY ERNEST R. VARALLI, COMPTROLLER OF PENN CENTRAL; CHARLES A. HORSKY, SPECIAL COUNSEL; AND JAMES HOWARD, ASSOCIATE GENERAL COUNSEL**

Mr. BLANCHETTE. Thank you, Mr. Chairman.

Members of the committee, Ms. Oakar, accompanying me at the table on my right is Mr. Ernest Varalli, who is comptroller of the Penn Central; on my immediate left is Mr. Charles A. Horsky, special counsel; and to his left is Mr. James Howard, associate general counsel of the Penn Central.

With leave of the Chair, Mr. Chairman, I will ask that my prepared statement be made a matter of the record.

Mr. ROONEY. Without objection.

**Mr. BLANCHETTE.** Included with it is a memorandum and two tables of figures.

I will summarize my testimony.

**Mr. ROONEY.** Without objection, the testimony will become part of the record along with the memorandum and tables of figures.

**Mr. BLANCHETTE.** The treatment of State and local taxes in the plan of reorganization is contained in the memorandum accompanying my statement. I should call specifically to your attention that in the reorganization plan the trustees assume the validity of all tax assessments in the past on these tax properties; and the trustees, as part of the plan of reorganization, waive any right that they would otherwise have under the Bankruptcy Act to challenge the assessments of those past taxes. I think the treatment in the plan of these State and local taxes has been amply described to this committee. We obviously as trustees believe that the plan is fair and equitable.

Furthermore, the Securities and Exchange Commission, which was asked by the reorganization court to evaluate the plan, concluded in a 117-page report to the court last Friday that the provisions of the plan relating to State and local tax claims are indeed fair and equitable.

We have copies of the SEC report which we would be pleased to file with the committee.

**Mr. ROONEY.** Without objection.

[The report referred to can be found in the subcommittee files.]

**Mr. BLANCHETTE.** Of course, ultimately it is the reorganization court which will decide whether the trustees and the Securities and Exchange Commission are correct. Its decision should be announced in November.

Also attached to my statement, Mr. Chairman, is a description of the proposed offer of compromise outside of the plan. That offer is scheduled to expire on October 22, 1977.

However, on next Thursday, October 6, we propose to recommend to the court that in view of this proposed legislation the offer be extended to 10 days following the adjournment of this session of the Congress.

**Mr. ROONEY.** How will that offer affect States like New Jersey and I think Ohio that can't accept a compromise?

**Mr. BLANCHETTE.** We have always felt that under the Supremacy Clause of the Constitution a compromise under the Bankruptcy Act can be accepted. Obviously some taxing authorities feel to the contrary. But this is an offer of compromise to those taxing jurisdictions which can or are willing to accept the offer. There is nothing compulsory about it.

In some instances, where the local counsel for the taxing jurisdiction felt that there was inability under the Bankruptcy Act to settle this disputed claim, legislation was introduced and passed to permit such an acceptance. Legislation was passed in Indiana, it was passed in Connecticut, and, I believe, in Ohio, subject to certain procedures. So there is an ability proven on the record to correct this deficiency.

With respect to H.R. 8882, it is undoubtedly true that the Federal guarantee of notes to be issued under the Penn Central proposed plan should remove any objection by any taxing authorities to the provisions of the plan.

In that sense the proposed legislation would remove one obstacle to a plan which the trustees and the SEC believe to be fair and equitable to all of Penn Central's numerous creditors. Nevertheless, it is our judgment that it is probably inappropriate for us as trustees to express an opinion on a matter which is essentially one between the Government of the United States and the local taxing authorities.

I will note that under our calculations, Mr. Chairman, the C and D notes could be paid if the offer of the United States Railway Association is sustained by the court. We don't believe that that offer is adequate but if that offer were sustained the C and D notes would be paid in accordance with their terms.

Finally, I am compelled to emphasize that the comments contained in this testimony are directed only to the present bill, which does not affect the payments provided under the plan. Were that bill to be changed in any way, that would affect the payment schedule, we would respectfully plead to have a further opportunity to explain to the committee what the conditions of such a change would be.

Thank you, Mr. Chairman.

[Mr. Blanchette's prepared statement and attachments follow:]

STATEMENT OF ROBERT W. BLANCHETTE, CHAIRMAN OF THE TRUSTEES OF THE  
PENN CENTRAL TRANSPORTATION CO.

I am Robert W. Blanchette, Chairman of the Trustees of the Penn Central Transportation Company. I am speaking today not only for myself, but for the other Trustees as well.

H.R. 8882 would provide a Federal guarantee of the securities issued by a railroad in reorganization to State and local taxing authorities in payment of claims by such authorities against the railroad. I have attached to this statement a brief outline of the securities which the Plan presently pending before the Reorganization Court in Philadelphia proposes for the portion of the State and local taxes which are not paid in cash when the Plan becomes effective. I should call specifically to your attention that the Plan accepts the validity of the assessments on which the taxes are computed, and waives any rights which the Trustees have under the Bankruptcy Act to challenge the assessments, which they would be required to consider doing if there were no Plan.

As you can see from the attached memorandum, the Plan proposes somewhat different treatment for taxes which on the one hand are attributable to properties which were left with Penn Central after the transfer of its rail properties to Conrail on April 1, 1976, and on the other hand taxes attributable to properties which were conveyed away from Penn Central to Conrail or other railroads on that date. The Trustees believe that these provisions of the Plan are fair. The Securities and Exchange Commission, which was asked by the Reorganization Court to evaluate the Plan, has also concluded, in a 117-page report to the Court filed last Friday, that the provisions of the Plan relating to State and local tax claims are fair and equitable. I have copies of the SEC report which I will be happy to file with the Committee. Of course, it is the Reorganization Court which will decide whether the Trustees and the SEC are correct. Its decision should be announced in November.

Attached to this statement is also an explanation of an offer, authorized by the Reorganization Court for Penn Central, in discharge of a tax claim, to pay immediately 50 percent of the principal amount of taxes which have accrued since the petition for reorganization was filed, or 44 percent of the total principal amount of taxes claimed, both pre- and post-petition. This offer, as the attached shows, has been open for about five months, and the attachment shows the number of taxing authorities which have accepted it and the amounts. The offer also permits Penn Central to offer taxing authorities with small claims (under \$10,000) 100 percent of the principal amount of their taxes in discharge of their tax claims. The figures with respect to acceptances in that category are also contained in the attachment. On next Tuesday, October 6, the Trustees propose to recommend to the Court that, in view of this proposed legislation, the offer be extended to 10 days following the adjournment of this session of Congress.

With respect to H.R. 8882: It is undoubtedly true that the Federal guarantee of the notes to be issued under the Penn Central proposed plan would, or certainly should, remove any objection by any taxing authorities to the provisions of the Plan. In that sense, the proposed legislation would remove one obstacle to a plan which the Trustees—and the SEC—believe to be fair and equitable to all of Penn Central's numerous creditors. Nevertheless, it is probably inappropriate for the Trustees to express an opinion on a matter which is essentially one between the Government of the United States and the local taxing authorities.

Our comments are, of course, directed to the present bill, which does not affect the payments provided under the Plan. Were the bill to be changed in any way that would affect the payments to be made, the Trustees should have a further opportunity to explain to the Committee what the consequences would be.

#### MEMORANDUM

The Plan of Reorganization (copy submitted) provides that all parties forgo any and all challenges to the validity of the claims for taxes filed by State and local taxing authorities, that the United States forgo in substantial part its claim to be paid in cash the amounts due to it, and that both property and corporate taxes owed to State and local taxing authorities be paid as follows:

1. On the day the Plan becomes effective (Consummation Date) all taxing authorities will be paid 20 percent of the principal amount of their claims in cash.

2. With respect to taxes allocable to property which was taken by Conrail or other railroads on April 1, 1976, pursuant to the RRRRA, and for which Penn Central will be paid when the amount due it is determined in the proceeding now under way in the Special Court (Valuation Case), notes will be given ("C" Notes) for the remaining 80 percent of the principal amount claimed and all the interest claimed. The "C" Notes bear interest at 8 percent compounded annually, and are payable from the proceeds of the Valuation Case. The notes have a lien on those proceeds second only to the lien to satisfy amounts due or guaranteed by the United States.

3. With respect to taxes allocable to properties which the estate retained on April 1, 1976, whether or not since sold, and with respect to all corporate taxes, 30 percent of the principal amount in serial notes payable in annual installments during the first three years from Consummation Date, and bearing 7 percent interest ("D" Serial Notes), plus "D" Term Notes for the remaining 50 percent of the principal amount claimed and all interest claimed, payable from the proceeds of the Valuation Case, but also secured by all of the assets of the reorganized company.

The Plan of Reorganization has been submitted to the Reorganization Court: hearings have been held on it; briefs have been filed; oral argument is scheduled for October 6. The Securities and Exchange Commission, which was requested by the Court to advise it on the feasibility and the fairness and equity of the Plan, has reported that it is both fair and equitable, and feasible. The target date for Consummation of the Plan is December 31, 1977.

Apart from the Plan of Reorganization, the Court has approved a proposal by the Trustees to make to all State and local tax authorities an offer to pay immediately 50 percent of the principal amount of all State and local taxes, including corporate taxes, due from Penn Central since the petition under Section 77 was filed, or, alternatively, 44 percent of the principal amount of all State and local taxes, including corporate taxes, both pre-petition and post-petition, in return for a complete release. The offer also provides the payment of 100 percent of the principal amount of all taxes if the amount is \$10,000 or less. The offer was made last spring, and was to be open for six months, and expires on October 22, 1977. The Court has reserved decision on whether it should be extended for an additional period.

Thus far, the offer has been accepted by 734 taxing authorities, and Penn Central has paid out \$19.6 million in discharge of the liabilities of \$43.5 million. Of these amounts 640 are taxing authorities settling for less than \$10,000, which have been paid \$1.5 million.

There are approximately 2,400 taxing authorities with tax claims against Penn Central. Of these, there are 1,436 whose claims are for \$10,000 or less.

Classified by States, the claims (including claims which have been discharged by acceptance of the Trustees' compromise offer), are shown on the attached sheet.

## PROPERTY TAXES PROGRESS REPORT—OFFER OF ACCEPTANCE OF COMPROMISE AS OF OCT. 3, 1977

State	Penn Central total unpaid liability (1)	Total number of claims	Total amount paid <sup>2</sup>	Total number of claims paid	Amount paid under \$10,000	Number of claims	Amount of volume reduced to \$9,999	Number of claims	Penn Central unpaid liability (settled)
Connecticut.....	\$607,000	96	\$153,311.88	58	\$113,315.98	54	\$39,996	4	\$186,929.69
District of Columbia.....	1,187,000	1	0	0	0	0	0	0	0
Delaware.....	1,042,000	36	31,599.15	29	31,599.15	29	0	0	32,423.55
Illinois.....	19,500,000	47	0	0	0	0	0	0	0
Indiana.....	37,500,000	75	16,171,822.70	74	10,025.67	4	9,999	1	36,759,467.28
Kentucky.....	198,000	3	0	0	0	0	0	0	0
Massachusetts.....	17,600,000	173	240,884.67	66	153,065.88	59	49,995	5	303,385.77
Maryland.....	8,250,000	71	245,306.64	42	58,424.48	30	39,996	4	441,426.16
Michigan.....	17,430,000	156	28,475.29	17	18,476.29	16	9,999	1	40,703.46
New Jersey.....	24,936,000	119	12,611.10	7	12,611.10	7	0	0	12,600.53
New York.....	96,158,000	678	636,709.13	139	298,016.32	112	179,982	18	901,768.73
Ohio.....	60,605,000	86	9,999.00	1	0	0	9,999	1	17,234.64
Pennsylvania.....	24,282,000	779	376,286.01	275	288,935.03	267	69,993	7	413,487.25
Rhode Island.....	6,497,000	56	1,663,969.06	19	25,772.63	13	19,998	2	4,379,113.85
Virginia.....	786,000	19	20,109.77	7	6,297.13	6	0	0	34,006.33
West Virginia.....	1,040,000	14	0	0	0	0	0	0	0
Total.....	317,618,000	2,409	19,591,064.40	734	1,016,539.66	597	429,957	43	43,525,457.24

<sup>1</sup> As of December 31, 1976, principal amount only.<sup>2</sup> Amount paid under \$10,000, and amount voluntarily reduced to \$9,999 are included in total amount paid.

## PENN CENTRAL CO. CORPORATE TAXES

States	Total unpaid taxes per plan of reorganization	
	Number of authorities	Amount
Pennsylvania (Philadelphia, Pittsburgh).....	3	\$23, 195, 000
Connecticut.....		
Delaware.....	1	26, 000
District of Columbia.....		
Illinois (Chicago).....	2	570, 000
Indiana.....	1	2, 656, 000
Kentucky.....	1	1, 000
Maryland.....	1	3, 866, 000
Massachusetts.....		
Michigan.....	1	781, 000
New Jersey.....	1	247, 000
New York (New York City, Buffalo).....	3	5, 284, 000
Ohio.....	1	9, 324, 000
Rhode Island.....	1	351, 000
Virginia.....	1	3, 000
West Virginia (Wheeling).....	2	784, 000
Taxes not allocated by State.....		7, 274, 000
Total.....	19	54, 382, 000

## CORPORATE TAXES SETTLED UNDER THE TAX COMPROMISE

(As of Sept. 21, 1977)

	Dn books	Settled	Under \$10,000
Florida.....	\$33. 3	\$33. 33	1
New York (Buffalo).....	281. 36	281. 36	1
California.....	6. 21	6. 21	1
Kentucky.....	700. 09	700. 09	1
Total.....	1, 020. 96	1, 020. 96	4

Mr. ROONEY. Thank you, Mr. Blanchette.

On page 2 of your statement, you commented about the court dismissing without prejudice the 90-day extension that the municipalities have requested. Do you believe that your proposal for an extension would have a better chance for approval by the court?

Mr. BLANCHETTE. Well, we never bat a thousand before the court, but we think that it is a fair extension. We say this bill is pending before this session of the Congress, some of the State and local taxing authorities are in an obvious dilemma, and were the bill not to become law, then they have 10 days after the adjournment of this session of Congress within which to make their election.

Mr. ROONEY. Mr. Florio.

Mr. FLORIO. Yes; thank you very much.

A couple of points. I appreciate your candor in admitting, as I thought you did, that this bill will really have no impact upon the proceedings; that is, the payment schedule as such, and I would think that the logical extension of that is that it would have no real impact upon other creditors' determinations as to whether they are going to accept the schedule and the terms of the schedule. I think that is a bit at variance from other testimony that we have heard today, that also I assume what you are doing is verifying other testimony we have heard today, that under the current valuation amount that is under challenge by itself under challenge to go up, it is not under challenge to go down, you feel the C and D notes can be paid off. Again

that gives me real difficulties as far as the Treasury Department suggestion that the Federal Government is in any way realistically perhaps liable. I don't see that as a definite possibility.

Mr. BLANCHETTE. Mr. Florio, I must say, pressing the candor point, there has been some rhetoric that the USRA award could be decreased in the valuation case. We don't take it seriously, but I have to tell you that there are some people who get up in court and make noises about decreasing that paltry award, by conferring other benefits, so to speak, on the Penn Central. We don't take that seriously, but I have to tell you and put on the record the fact there has been that assertion made.

Mr. FLORIO. Let me also make a comment. Your opening comment was in effect you have waived your right as to challenge the assessments. I thought the implication was that you could have challenged the assessments, and I am not sure what the law is in other States, but I would think in my own State you probably couldn't because the statute is already passed. On August 15 of each year, the assessment has to be challenged, and I am sure you are going back a while. So in fact you may have waived something you didn't have a right to not waive.

Mr. BLANCHETTE. This is not under State law, Mr. Florio. The Bankruptcy Act has a specific provision that preserves to bankruptcy trustees the right to contest tax assessments. The battle would be that if in the absence of our plan, which I think is the only plan that can be structured for this estate, there would be a contention made that if all of the railroad was worth was what the USRA said it was worth, than these tax assessments were far in excess of the real market value of the property. Then you would have to wait until the outcome of the valuation case and the trustees would then, some set of trustees, not this set, go in under the Bankruptcy Act and assert a right to have the assessments reduced. And we just found that was to no one's interest so we are not asserting that right under the Bankruptcy Act.

Mr. FLORIO. Is that not academic, that supersedes State law?

Mr. BLANCHETTE. Under the Federal Supremacy Clause.

Mr. FLORIO. Thank you very much.

Mr. ROONEY. Ms. Oakar.

Ms. OAKAR. Thank you, Mr. Chairman.

Mr. Chairman, just for the record, Ohio is by law permitted to accept partial payment. I would like to ask the gentleman through, what sort of input did the State and local taxing authorities have on the compromise offer? Is it not true or is it true that the trustees in the Friday morning group devised the compromise?

Mr. BLANCHETTE. Well—

Ms. OAKAR. And that was accepted?

Mr. BLANCHETTE. Well, the actual compromise was negotiated. Mr. Horsky calls my attention to two things. First, is the 50-percent compromise or the 44-percent compromise. And, second, is the section 211 (h) compromise with the United States.

Referring to the latter, that compromise was negotiated among certain members of the Friday group which constitutes the bulk of the secured creditors, the U.S. Government acting through the Department of Transportation, and the trustees. With 2,500 States and local taxing

authorities, it was—at the time they were not organized in any fashion really—physically impossible to bring them to the table. Furthermore, because the Government had through section 211(h), a strong-arm clause around us unless we could secure agreement with Mr. Barnum, acting for Secretary Coleman, it just wasn't possible for us to go public with anything because we were at the mercy of the priorities established under section 211(h).

Thereafter, we immediately did all that was necessary to go public on that particular offer.

Now, with respect to the 50 percent—

Ms. OAKAR. May I just interrupt you there for a second. You know we have had many national organizations endorse this bill, the National League of Cities, the Association of Mayors, County Commissioners and et cetera, et cetera. They found it fairly easy to get together to have a spokesman to come before this committee, and I am just wondering why you feel it wasn't humanly possible to involve them in the compromise despite the fact that there were 2,500 individual municipalities at stake here? I think they would have found a spokesman if you had given them the opportunity to be involved. I am not saying it was your responsibility. I want to make this point clear. You have clarified it they were not involved in one of the plans.

Mr. BLANCHETTE. They were not organized at that time.

With respect to the 50-percent offer, there is a history of a 50-percent settlement with State and local taxing authorities, and that is one where there had been some consultation. For example, in the city of New York, with respect to the sale of the defunct Commodore Hotel, if that sale is consummated, we had negotiated with New York City a 50-percent compromise of taxes on that parcel. We had also negotiated a 50-percent compromise with the city of Wilmington, Del. So that we had a feeling that there was a favorable precedent for that kind of settlement outside of the plan.

Ms. OAKAR. Mr. Chairman, just one question.

Mr. Blanchette, you said you felt that the plan was fair and equitable, if I am not mistaken. But if you were owed money and you appeared to be obviously a good businessman, you planned on it in your budget and instead of the cash payment you were given 50 percent of the money owed, 7 years from today, assuming that inflation continued over the next 7 years at the rate that we have witnessed over the past 7 years, do you know or have an option as to what the real worth today would be of the 50-percent payment to be received by you in 7 years?

Mr. BLANCHETTE. Well, the 50-percent payment right now is immediate cash. As a business proposition, if I had not received a nickel on account of the State and local tax for 7 years, I think I probably would have figured in my budget planning that maybe there is a certain amount of writeoff that has already occurred. I am not justifying the plan on that basis, but it is not new that the taxes have been delinquent for 7 years.

Mr. FLORIO. Just to make it 100 percent.

Ms. OAKAR. It means 36 cents on the \$1 in Ohio.

Mr. FLORIO. Just to get your position on the legislation, I am going to contest at this point the equity of the plan. It may be the finest plan. It may be beneficial to the municipalities when the alternative is nothing, but in no way does the passage of this legislation, in your opinion,

jeopardize the plan, jeopardize the status of various debtors, rather creditors, and that the plan to go forward if this legislation is passed.

Mr. BLANCHETTE. Well, it does not alter the payment schedule if not one semicolon, jot, or tittle is changed. There is no alteration of the payment schedule and we as trustees would not represent to the court that the plan has been jeopardized.

Mr. FLORIO. Talking about the reasonable expectation of the intent of this plan being affected or not being affected by the passage of this legislation.

Mr. BLANCHETTE. In my judgment, it would not be affected and one obstacle we said has been removed. I have not thought about Mr. Dickieson's points and I am not commenting on whether somebody else would say since there is a firm guarantee, let's dilute the C and D notes. In my judgment if not one iota of the present bill was changed, there would be no alteration of the payment schedule that has been so delicately negotiated and arrived at. And, therefore, we would not say that the plan has been jeopardized, but only as the bill is presently written.

Mr. FLORIO. I thank you for a very important observation.

Ms. OAKAR. Can I just ask one more question. That is: Of the 2,500 taxing authorities who are owed some of approximately \$350 million, how many have accepted the offer?

Mr. BLANCHETTE. If you will refer to the exhibit.

Ms. OAKAR. I just got the exhibit now, I am sorry.

Mr. BLANCHETTE. We have paid \$19,591,000 to settle liabilities of \$43,525,000.

The number of claimants who have settled was 734. Others have expressed a desire to await the outcome of these sessions to make their determination. That is the reason we are extending the offer to 10 days beyond the adjournment of this session of the Congress.

Ms. OAKAR. Thank you very much. You have extended it.

Mr. BLANCHETTE. We are going to recommend it to the court.

Mr. ROONEY. Last week, Mr. Blanchette, we had a witness testify before this committee that you recently sold \$100 million worth of Penn Central property. Is that true?

Mr. BLANCHETTE. Well, I know we have sold \$100 million worth of property. I think that reference was to the property in midtown Manhattan.

Mr. ROONEY. What was your net value of that \$100 million?

Mr. BLANCHETTE. The net value, sir?

Mr. ROONEY. Right.

Mr. BLANCHETTE. It was \$100 million. We received \$100 million.

Mr. ROONEY. Did you have any mortgages on it?

Mr. BLANCHETTE. We haven't even paid the mortgages. These properties are all encumbered. The proceeds are not enough to pay the mortgages or the administration claims. In the absence of a plan such as ours that \$100 million won't be available to anybody. In fact, it would go first under the statute to the U.S. Government. Part of that would be freed for taxes under our proposal.

Mr. ROONEY. I have read in recent articles in the press that Penn Central Co. had tremendous profits in recent quarters: is that correct?

Mr. BLANCHETTE. I think one quarter there was a profit. When we sold the Waldorf there was a book profit for that period. If you accrue

the mortgage debt, we are running at a deficit. However, there is value in the Penn Central system which will be used in part, Mr. Chairman, to pay off State and local taxing authorities under the plan.

Mr. ROONEY. How long have you been chairman of the trustees?

Mr. BLANCHETTE. Since 1975.

Mr. ROONEY. Whether or not this bill is passed, in your opinion, do you feel that the municipalities will eventually be paid in full?

Mr. BLANCHETTE. Yes, they will. We believe they are going to be paid in full and that is the full intent of our plan.

Mr. FLORIO. That is if they don't accept the compromise?

Mr. BLANCHETTE. Well, if they accept the compromise offer, they get paid right now and they don't have to wait whether this plan goes to the Supreme Court or otherwise is scheduled. If that plan is approved they will be paid in full.

For those whose claims are represented by retained assets and which we have a better feel for the values, and there is no litigation outstanding, they will receive 20 percent in cash up front and then they will receive 30 percent of the principal amount in cash over the next 3 years. Thereafter there will be a term note which will pay the remainder of their principal and interest accruing at 7 percent maturing in 1987.

With respect to those properties that were conveyed to ConRail and in which there is some uncertainty as to the outcome or value of those properties, again there is 20 percent cash payment up front. And then the remainder of the principal and interest will accrue interest at 8 percent compounded, which is the same rate as the CV's bear and they will mature in 1987, which is the contemplated maturity of the CV's and they are second only to the United States out of the certificates of value which are guaranteed by the Government.

Mr. FLORIO. May I ask perhaps your opinion, your business judgment, you have indicated that the D notes seem to be fairly secure on the prospect of business opportunities. We have had a couple of people say the valuation aspects are sufficient to pay off the C notes. What would be your determination as to whether the municipalities could do without the Federal loan guarantees, discount the notes that are given in order to get some immediate cash?

Mr. BLANCHETTE. I think—

Mr. FLORIO. Is there any prospect of that?

Mr. BLANCHETTE. I think on the D notes—I am not an investment banker, Mr. Florio, but I have heard enough to suspect that on the D notes there would be a great ability to discount those notes.

On the C notes the testimony of record is that they would be highly speculative and would probably not have a market.

Now, if they were to carry an 8-percent coupon and a Federal guarantee they could conceivably ride quite high, but I haven't inquired into that.

Mr. FLORIO. Thank you, Mr. Chairman.

Mr. ROONEY. Ms. Mikulski.

Ms. MIKULSKI. Mr. Blanchette, the question I have pertains to possible liquidation. I am pleased that we did adopt the national policy we did that set up ConRail. There are those, however, who believe Penn Central should now be liquidated. If you think that the money would be gained by liquidation of Penn Central would not cover all

of the responsibilities to the Federal Government and other taxing authorities, would you then say to those who advocate that policy that it is a foolish one to be pursuing continually?

Mr. BLANCHETTE. The liquidation policy?

Ms. MIKULSKI. Yes.

Mr. BLANCHETTE. The liquidation policy is absolutely irresponsible. Nobody gets anything. It is a 100-year war. The matter will go on endlessly while everyone litigates. And there is no business, legal, or other sense to a liquidation policy.

Ms. MIKULSKI. Thank you.

I just wanted that on the record because I have a few foolish folks who would like to pursue that.

Mr. ROONEY. Thank you very much for your appearance before the committee.

That concludes our hearings on H.R. 8882.

[The following letters and statements were received for the record:]

CONGRESS OF THE UNITED STATES,  
HOUSE OF REPRESENTATIVES,  
Washington, D.C., September 28, 1977.

HON. FRED B. ROONEY,  
*Chairman, Transportation and Commerce Subcommittee, House Office Building,  
Annex 2, Washington, D.C.*

DEAR MR. CHAIRMAN: I am enclosing a copy of a letter dated September 22, 1977, which I received from the Assistant Superintendent of Schools, City of Chicago.

Since this letter concerns H.R. 8882 which is presently before the Transportation and Commerce Subcommittee, I am forwarding the letter with the attachments and request that they be included in the Hearing Record.

With every best wish, I am

Sincerely,

RALPH H. METCALFE,  
*Member of Congress.*

Enclosures.

BOARD OF EDUCATION,  
Chicago, Ill., September 22, 1977.

Congressman RALPH H. METCALFE,  
*Rayburn House Office Building,  
Washington, D.C.*

DEAR CONGRESSMAN METCALFE: On Tuesday, September 20, I spoke with your Legislative Aide Coleman Conroy, concerning our interest in H.R. 8882, which will come before your committee next Tuesday. The Council of Great City Schools, of which Chicago is a member, is interested in a legislative resolution to this problem, as provided under this bill.

A fact sheet and background data concerning the case involving receipt of full payment for taxes owed by the Penn Central and other railroads now in reorganization is attached for your information. This material has been well researched by the attorneys of the Cleveland Public Schools, and, I believe, represents a very valid case.

It is estimated that Chicago would receive approximately \$5 million through this legislation due to the loss we have experienced because of the failure of the Penn Central to meet its obligation to school districts. You will note that Appendix A indicates that the State of Illinois would receive approximately \$28,665,000 if this legislation is enacted.

Your favorable consideration and support of this measure will be greatly appreciated.

Sincerely,

ARTHUR R. LEHNE,  
*Assistant Superintendent.*

## H.R. 8882 FACT SHEET

H.R. 8882 would guarantee that state and local taxing authorities will eventually receive full payment for the taxes owed by the Penn Central and other railroads now in reorganization. Passage of this legislation is urgently needed, for the reorganization of the Penn Central Railroad has created severe financial difficulties for state and local tax authorities, difficulties created largely by the actions of the Federal government.

The Railroad filed for reorganization in June, 1970, and has since then paid no state or local taxes. As of December 31, 1976 the total delinquency was more than half a billion dollars. The Federal government is primarily responsible for the magnitude of these delinquencies because it required the railroads to continue operations, although that continued operation insured tremendous operating losses.

Properly, the Federal government should bear the cost of meeting that national interest. However, unless H.R. 8882 is enacted, Taxing Authorities, including hundreds of school districts, large and small, will be forced to choose between either a cash compromise, or payment under a plan of reorganization after the Federal government, which is asserting a first priority claim for loans it made to permit continued deficit rail operations. In either case, local Taxing Authorities have no assurance of full settlement of outstanding claims.

If they accept the compromise, Taxing Authorities will receive between 44 cents and 50 cents on the dollar, without interest or penalties. Given inflation, combined with loss of interest, this represents actual payment of less than 10 cents on the dollar. Under the Plan of Reorganization, as presently proposed, Taxing Authorities will receive 20 percent of their claim in cash, the remaining 80 percent in ten year notes that lack guarantees.

H.R. 8882 assures that Taxing Authorities would be paid in full by means of a federal guarantee. It should be stressed that H.R. 8882 is not a "bailout" of a private corporation, but rather is a mechanism to assure that state and local taxing authorities receive their tax payments, tax payments which are now threatened by the priority claims asserted by the Federal government.

[Additional information attached.]

## H.R. 8882 BACKGROUND INFORMATION

## I. HISTORY OF FEDERAL INVOLVEMENT

The Penn Central Railroad filed for reorganization in June, and by order of the Federal reorganization court, has since then paid no state or local taxes; in many jurisdictions, Penn Central had large pre-bankruptcy delinquencies as well. Delinquencies now exceed \$500 million (including interest) in the 16 states in which the railroad formerly did business; Appendix A lists the total claims for the States involved.

In order to maintain rail service in the Northeast, a substantial portion of the operating rail assets of Penn Central and other railroads in reorganization<sup>1</sup> were conveyed, pursuant to federal law, to the Consolidated Rail corporation ("Conrail") in April, 1976.<sup>2</sup> That federal law, passed in 1973, also required that, in the national interest, Penn Central continue operations at an enormous loss until the transfer to Conrail could be made. The federal government made loans to the railroad to partially cover those losses. It also guaranteed Penn Central Trustees Certificates, to enable the trustees to obtain cash from private sources to continue operations.<sup>3</sup> The federal government now asserts a priority for repayment over all other claims, including those of state and local government units.

## II. PROPOSED TREATMENT OF TAXES

The federally required railroad operations resulted in a federal claim of approximately \$500 million. Pursuant to a "settlement" between Penn Central and the United States, Penn Central is now trying to obtain federal court and creditor approval of a Plan of Reorganization ("Plan") which would give the

<sup>1</sup> The following discussion will deal only with Penn Central. A number of Northeastern railroads are in reorganization and both existing federal legislation and H.R. 8882 apply to all such railroads. Penn Central is by far the largest portion of the system and is farthest along in its reorganization proceeding.

<sup>2</sup> Regional Rail Reorganization Act, as amended, 45 U.S.C.A. § 701 *et seq.*

<sup>3</sup> 45 U.S.C.A. § 661 *et seq.*

federal government a first priority for repayment of that amount. Taxing Authorities would be forced to choose between the alternatives described below: either a partial settlement of their claims or secondary treatment under the Plan, which treatment as presently proposed could preclude their ever being paid in full.

#### *A. Compromise of tax claims*

Under the Compromise, taxing authorities which accept the compromise would receive cash payment of either (1) 50 percent of the principal amount of their post-reorganization petition tax claim, or (2) 44 percent of the principal amount of their total tax claim, whichever is greater. Provision for settlement of penalties and interest is specifically excluded. Given the rate of inflation during the seven years, in which no taxes have been paid, combined with loss of interest, this represents an actual payment of less than ten cents on the dollar. Taxing authorities must indicate their intention of settlement pursuant to the Compromise by October 19, 1977, or be accorded treatment of their claims under the Plan of Reorganization (see B, below).

The Cleveland Board of Education and a number of other Taxing Authorities objected to this compromise when it was proposed to the District Court, and the District Court's approval is now on appeal. Most recently, the Federal District Court refused the petitions of the Cleveland Board of Education and the State of New Jersey, joined by various other Taxing Authorities, to extend the deadline for acceptance of the compromise to provide time to permit passage of H.R. 8882 (see Fact Sheet).

#### *B. Plan of reorganization*

Pursuant to the Plan, as last amended by the Trustees on May 2, 1977, those taxing authorities that do not accept the Compromise will initially receive a cash payment of 20 percent of the principal amount of their total tax claim. Each claim would then be split between taxes due on properties retained by Penn Central and taxes due on properties transferred to Conrail. Settlement of the remaining 80 percent of the principal claims would be as follows:

1. Taxes on retained assets would be paid with interest-bearing general obligation Series "D" notes of the reorganized Penn Central Company. In each of the first three years, 10 percent of the notes for the principal would mature. Series "D" general obligation interest-bearing notes would then be issued for the remaining 50 percent of the principal and for 100 percent of the interest of the claim. These notes would mature on December 31, 1987, or later if the Valuation Case has not been settled or has not produced sufficient proceeds for retirement of the notes.

2. Taxes on transferred assets would be paid with Series "C" notes, which are to be secured only by the proceeds of the "Valuation Case", the lawsuit between Penn Central and the United States to determine the value of the assets conveyed to Conrail. In the Valuation Case the U.S. is seeking to reduce the valuation claim of Penn Central. As federal statutes now mandate that the claim of the U.S. be paid prior to all other claims, taxing authorities which receive these Series "C" notes will never be paid unless the Valuation Case produces enough to enable Penn Central to pay both the federal claims and the taxing authorities' claims. In a number of states, including Ohio, Illinois, Indiana, Massachusetts, and Michigan, where a very large portion of Penn Central assets were conveyed to Conrail, settlement under this Plan would conceivably result in a severe revenue loss. These Series "C" notes are scheduled to mature on December 31, 1987, or later if the Valuation Case has not been concluded by that time.

#### *C. Summary*

State and local taxing authorities are thus now faced with the choice of settling for a fraction of their total tax claims under the Compromise or settling for payments of their total claims with securities which, without H.R. 8882, will be of speculative value. This choice must be made by October 19, 1977.

### III. FEDERAL ASSISTANCE NEEDED

The present alternatives require Taxing Authorities to bear a large portion of the cost of rail operations which were continued in the national interest. Since the national interest should be an equal responsibility upon us all, the federal government should be that cost and assure that all Taxing Authorities will be

paid in full, including both principal and interest. H.R. 8882 will produce this result by requiring that the federal government guarantee these notes. Such a guarantee recognizes that the Federal Government's extraordinary intervention has effectively prevented the state and local taxing authorities from collecting their rightful taxes:

First, by barring their normal remedies against the real estate tax delinquencies: and

Second, by subordinating these taxes to its own later claim.

H.R. 8882 would remedy the already severe financial effects on state and local taxing authorities and would avoid a dangerous tax credibility precedent of unequal, inequitable treatment of delinquent property tax owners as well as the established right of local taxing authorities to levy and collect tax on land in their districts.

## APPENDIX A

ESTIMATED STATE AND LOCAL TAX CLAIMS<sup>1,2</sup>

[In thousands of dollars]

State	Property taxes <sup>3</sup>				Corporate and other taxes <sup>4</sup>			
	Class t pre- bank- ruptcy	Class E post- bank- ruptcy	Interest	Total	Class t pre- bank- ruptcy	Class E post- bank- ruptcy	Interest	Total
Pennsylvania.....	\$1,444	\$22,938	\$7,770	\$32,052	\$968	\$22,227	\$6,749	\$29,944
Connecticut.....	63	544	261	868				
Delaware.....	38	1,004	396	1,438	1	25	12	38
District of Columbia.....		1,187	451	1,638				
Illinois.....	4,915	14,585	9,165	28,665		570	164	734
Indiana.....	10,961	26,539	12,000	49,500	100	2,556	731	3,387
Kentucky.....		198	75	273		1		1
Maryland.....		8,250	3,135	11,385	4	3,882	1,038	4,924
Massachusetts.....	2,545	15,055	6,688	24,288				
Michigan.....	2,623	14,807	10,458	27,888		781	370	1,151
New Jersey.....	3,804	21,132	16,083	41,019		247	30	277
New York.....	1,103	95,055	47,701	143,859	780	4,504	2,605	7,889
Ohio.....	15,858	44,747	19,393	79,993		9,324	2,467	11,791
Rhode Island.....	442	6,055	2,079	8,576	5	346	111	462
Virginia.....	67	719	299	1,085	3		1	4
West Virginia.....		1,040	395	1,435	63	721	196	980
Taxes not allocated by State <sup>5</sup>						7,174	220	7,494
<b>Total.....</b>	<b>43,863</b>	<b>273,755</b>	<b>136,349</b>	<b>453,967</b>	<b>1,924</b>	<b>52,458</b>	<b>14,694</b>	<b>69,076</b>

<sup>1</sup> The interest on all State and local tax claims is calculated through Dec. 31, 1977. The taxes, however, reflect the amounts due through Dec. 31, 1976, the end of the compromise period. The interest calculations on property taxes are estimates based on the average interest rates used by major taxing entities in the various States.

<sup>2</sup> As filed by the trustees on May 9, 1977, pursuant to their plan of reorganization.

<sup>3</sup> See pp. 2 through 5 of this exhibit for further details.

<sup>4</sup> Represents amounts accrued, on an estimated basis, for which tax returns have not yet been filed.

Note: Counsel for the trustees have requested that all inquiries as to amounts owed particular taxing authorities be directed to Louis G. Hurrelbrinck, Penn Central Transportation Co., IVB Building, 1700 Market St., Philadelphia, Pa.

CHICAGO, ILL., September 26, 1977.

HON. FRED B. ROONEY,

Chairman, U.S. House of Representatives, Committee on Interstate and Foreign Commerce, Subcommittee on Transportation and Commerce, Washington, D.C.

DEAR MR. CHAIRMAN: On June 21, 1970, the Penn Central Transportation Company filed for reorganization under the Federal Bankruptcy Act. Since that time, taxes owed by Penn Central have gone unpaid to sixteen states throughout the country. State and local tax claims against Penn Central now total, including interest, over \$500 million dollars. The loss of this tax revenue over the past seven years has created severe financial difficulties for the affected taxing authorities. The State of Illinois is currently due approximately \$20 million dollars in state and local property, franchise and income taxes.

Local and state tax authorities in Illinois were currently faced with a choice between two settlement options, a choice which was to be made by October 19, 1977. The first settlement option or "Compromise Plan" called for roughly a

50 percent cash payment of the principal amount of the past due taxes excluding all consideration of penalties and interest. I have advised all state and local officials in Illinois that such a compromise is totally unacceptable as a matter of Illinois law. Additionally, such a settlement places unnecessary and additional financial burdens on the already hard-pressed Illinois taxpayers who pay their taxes on time. The second option currently existing under Penn Central's Amended Plan of Reorganization affords full payment by way of a 20 percent cash payment with the balance, including penalties and interest, in Notes maturing in 1987. The security attaching to these Notes is speculative to say the least. Although my office on behalf of the entire State is currently challenging the Plan's offer in the U.S. District Court in Philadelphia, employing our efforts in concert with those of other taxing authorities to effect a 100 percent cash payment, it is clear that both options are totally unacceptable. This is principally caused because the Notes, as presently offered, are vastly speculative making their ultimate marketability quite doubtful.

H. R. 8882 was introduced in the House of Representatives on August 5, 1977, to correct the shortcomings of these options. In essence, this legislation will provide a federal guarantee for the securities which Penn Central is offering in full payment of the tax claims.

It is quite significant to note here that Penn Central representatives as well as Justice Department representatives have stated that in their opinion there is every reasonable expectation that the Penn Central Notes would be redeemed in full in 1987. This being the case, the pending legislation presents minimal risk to the federal government.

More importantly however, I feel completely justified in asking the federal government to intervene by means of this legislation since the initial federal intervention was instrumental in causing the accumulation of the tax delinquencies.

First, the federal reorganization court in Philadelphia ordered in October 1970, that the Penn Central Trustees make no further payment of taxes until further order of the court.

Second, Congress legislated that Penn Central continue operations although tremendous losses would be incurred, and since 1970, federal appropriations to Penn Central have been made in excess of \$500 million dollars, the repayment of which currently has priority over the payment of local tax claims.

Third, the property to which the State tax liens attached has been conveyed, free and clear of any liens, to the quasi-federal corporation ConRail.

In light of (1) the initial federal intervention in the Penn Central case, (2) statements made by Penn Central and Justice Department representatives, (3) the conveyance of Penn Central's railroad property free and clear of any tax liens to ConRail, and (4) the groundswell of local support for H.R. 8882, I strongly urge that you, Mr. Chairman, and this committee act swiftly and favorably in support of the pending legislation.

Respectfully,

WILLIAM J. SCOTT,  
*Attorney General, State of Illinois.*

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THE ACADEMY FOR CONTEMPORARY PROBLEMS,  
*Columbus Ohio., September 28, 1977.*

HON. FRED B. ROONEY,

*Chairman, Subcommittee on Transportation, Committee on Interstate and Foreign Commerce, U.S. House of Representatives, Washington, D.C.*

DEAR MR. CHAIRMAN: At the request of several witnesses in your hearings on the Penn Central property tax question, I submit the following statement for the record based on a recent survey of economic problems in the northeastern United States conducted by this Academy. The Academy is a public policy research center operated by the Council of State Governments, International City Management Association, National Association of Counties, National Conference of State Legislatures, National Governors' Conference, National League of Cities, and U.S. Conference of Mayors.

Sincerely yours,

RALPH R. WIDNER, *President.*

STATEMENT OF RALPH R. WIDNER, PRESIDENT, THE ACADEMY FOR CONTEMPORARY PROBLEMS

The loss of property tax revenues from railroad properties will severely affect many northeastern cities currently in financial trouble. Many of the largest railroad yard operations in the Northeast are located within these cities.

A national study of cities in trouble by David Stanley at the Academy for Contemporary Problems surveyed the financial and economic development challenges faced by urban areas with declining economic bases. Stanley reported that until recently the central cities bore the sole brunt of increasing concentrations of poor residents in the face of a declining economy and tax base. New York, Baltimore, Pittsburgh, Buffalo, and Newark are cities with declining or no-growth taxable property bases already. Yet the declining cities also tend to be high cost cities. Muller compared costs among seven large growing cities and 14 large declining cities plus New York and found substantial discrepancies between them in terms of municipal expenditures per capita, municipal employees per 1,000 residents and the average monthly wage of municipal workers.

Nearly all of these older cities are "land-locked", that is surrounded by other incorporated municipalities. They can not solve their economic and financial problems through territorial annexation as in the case of newer, growing urban areas elsewhere.

RIISING COSTS

Declining cities are high cost cities. The fact that population, business, and jobs are reduced does not mean that municipal services and facilities to provide them have been reduced correspondingly. Costs within the troubled cities have risen sharply in recent years, as have costs in all large cities and indeed in state and local governments generally. Spending per capita grew 163 percent from 1962 to 1972 in all state and local governments and 198 percent in 28 big cities. (Of the 28, seven were growing, 14 were declining, six were formerly growing and are now declining, and one, New York, was considered separately.)

The main components of the cost increases were:

*More employees.*—An 11 percent increase in per capita employment from 1969 to 1972 in the largest declining cities and a 13 percent increase in the largest growing cities. Cities generally had employment increases in these years followed by a sharper rise in 1972-73 and a slowdown in 1974. Employment went up mainly because of increasing demand for services to city residents, stimulated in part by the availability of Federal and state grants and normal bureaucratic accretion ("Parkinson's Law"). Instead of reducing the demand, the 1974-75 recession stimulated it, at the same time impairing the cities' ability to pay for the added workers.

*Higher pay in the state and local government sector (up 69 percent compared to 56 percent in private industry).*—According to another study, pay for common municipal services increased from 12 to 20 percent between 1970 and 1973 alone. These increases were partly the consequence of a general rise in pay levels nationally and partly a result of the advances in public sector unionism, which enabled employees to bargain effectively for "their share" of public resources, even to the point of higher pay than the private sector offered for comparable work.

*Increases in fringe benefit costs, which add about 30 percent to every payroll.*—In several cities these increases ranged from 18 to 31 percent between 1970 and 1973. Retirement contributions alone went up 9 percent a year from 1967 to 1972 and over 10 percent a year in 1973 and 1974. These fringe costs are also a reflection of unions' effectiveness. As pay became competitive, the unions turned to benefits as a means of increasing compensation. Pensions are a particular cause of fiscal concern because enormous cost increases are built in for future years when unfunded or partly funded obligations come due as employees retire.

According to Roy Bahi and Bernard Jump at Syracuse University, about 27 percent of city cost increases in 1967-72 was attributable to inflation. Another 17 percent was due to "real compensation growth"—what employees received in excess of cost of living increases. The remaining 55-plus percent resulted from "input quantity"—more employees, materials, and supplies. The inflationary factor was 25 percent in 1972-74, resulting in a loss of over \$2 billion in municipal purchasing power.

## LAGGING REVENUE GROWTH

Revenues are not keeping up with rising costs. Tax revenues would have increased only 15 percent (compared to the 25 percent increase in expenses) if cities had taxed at 1972 levels the 1972-74 inflationary increase in their tax bases. Cities face a losing battle, with expenses responding more to inflation than do revenues.

Perversely, among cities studied by the Urban Institute for the 1969-72 period, "growing cities managed to cut their effective property tax rates by more than 25 percent . . . while the declining cities were obliged to raise their rates by nearly 25 percent." Between 1967 and 1973, large declining cities increased per capita revenues by 113 percent (compared to growing cities' 95 percent) despite slower increases in per capita income and wealth.

In the District of Columbia government's annual study of tax burdens in the nation's 30 largest cities, among the top eight in estimated burden of major taxes for a family of four with a \$10,000 income were Boston, New York, Buffalo, Philadelphia, and Baltimore.

The fiscal squeeze in cities was aggravated by the 1974-75 recession which cut growth in sales and earnings taxes dampened potential growth in the property tax base, increased tax delinquencies, and raised the work load of city servlees as inner-city unemployment rose.

The recession made revenue-raising efforts especially counterproductive in the declining cities. A rise in the property tax rate or the imposition of some new tax might not be the only reason for a company's leaving the city or deciding not to move in, but it would be an important consideration. Even for firms remaining in the city, the higher taxes would soak up funds that might otherwise be used for more economically stimulating purposes.

Clearly, whatever action is taken with respect to property taxes owed by Penn Central should take into account the potentially severe affects which non-payment may have on the fiscal viability of these older manufacturing cities.

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STATEMENT OF HON. ROBERT E. AHMED, MAYOR OF POUGHKEEPSIE, N.Y.

I am Robert Ahmed, Mayor of Poughkeepsie, New York. Poughkeepsie is a city of some 32,000 people. Our annual budget for FY '77 is \$13.7 million.

Penn Central Transportation Company and its predecessors and interests owe us some \$359,000 in real property taxes. Since this obligation has been accruing since 1961, total real property tax liens, including principal and interest total approximately \$696,000.

If the City is able to participate in the proposed reorganization plan of the Penn Central trustees, a participation which will only be possible if the payment of the Series C notes is guaranteed by the government, the City stands to receive at the end of the proposed 10-year maturity schedule approximately \$1,420,000.

If the City is forced to accept the settlement figure proposed by Penn Central, the amount received will be approximately \$157,000, a fraction of the outstanding tax lien.

The Penn Central tax hiatus has had a debilitating effect on our already declining tax base. The \$537,000 difference between what has been offered by the Penn Central and what is actually owed to us would provide funds for much needed housing rehabilitation and would permit the City to bolster its declining level of services.

Under the aegis of the Federal Bankruptcy Court and by Act of Congress the Penn Central and the National Railroad System has been saved, in the federal interest. A small, struggling city like Poughkeepsie must not be compelled to shoulder unduly the financial burden necessary to promote that interest. That is what we will be required to do if we are forced to accept the Penn Central settlement. It is unjust, unfair, and contrary to our local laws. We support Congresswoman Oakar's bill, H.R. 8882.

[Whereupon, at 11:30 p.m., the subcommittee adjourned.]

















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