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Testimony

Before the Committee on Transportation and Infrastructure, House of Representatives

Food and Beverage Service: Opportunities Exist to Build on Program Improvement Initiatives

Statement of Ted Alves
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AMTRAK

Good Morning Chairman Mica, Ranking Member Rahall, and Members of the Committee:

Thank you for the opportunity to discuss our work on Amtrak's food and beverage service. Losses on food and beverage service have been a long-standing issue at Amtrak. In Fiscal Year (FY) 2011, Amtrak reported a direct operating loss of almost $85 million. Long-distance routes accounted for about $74 million (87 percent) of these losses.

My testimony today will discuss three areas:

(1) actions Amtrak has underway to address our prior recommendations to improve internal controls that have left food and beverage revenues and inventories vulnerable to fraud, waste, and abuse;

(2) preliminary observations from our ongoing food and beverage service audit that indicate that program improvement initiatives can be enhanced by consolidating the fragmented management structure, which is causing weaknesses in program accountability and planning; and

(3) best business practices work we plan to complete over the next 6 months to identify ways to help mitigate food and beverage operating losses.

AMTRAK ACTIONS TO ADDRESS INTERNAL CONTROL WEAKNESSES THAT CREATE VULNERABILITY TO FRAUD, WASTE AND ABUSE

Amtrak agreed with—and has taken actions to—address our June 2011 recommendations[1] to improve internal controls that have left on-board food and beverage revenues and inventories vulnerable to fraud, waste, and abuse.

Prior to our June 2011 report, Amtrak officials had begun actions to improve internal controls over on-board food and beverage service. For example, Amtrak had established a centralized system to help automate the collection of revenue shortages and had introduced on-board electronic credit card technology. Amtrak is also deploying an on-board point-of-sale system[2] and a warehouse inventory management system[3] that should automate processes, improve data timeliness and reliability, reduce paperwork and eliminate error-prone processes.

Our report last year documented long-standing internal control weaknesses and gaps over on-board food and beverage service. We estimated that $4 million to $7 million of Amtrak's on-board food and beverage sales could be at risk of theft. Between March 2003 and January 2010, we identified 903 theft, dishonesty, and policy/procedure violations by 306 lead service attendants, and issued 447 administrative referrals to Amtrak managers. The recurring schemes described in the report involve the

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[1] *Food and Beverage Service: Further Actions Needed to Address Revenue Losses Due to Control Weaknesses and Gaps* (Report No. E-11-03, June 23, 2011).

[2] Point-of-sale is an automated system that tracks food and beverage sales and inventory on trains, in real time.

[3] The warehouse inventory management system is an automated system that was deployed in all 11 Amtrak commissaries in March 2011.

falsification of documents to conceal missing food and beverage revenues and inventories. Specifically:

- *Inflating first-class meal checks.* This scheme involves adding items to first-class passengers' meal checks—meals are provided free to first-class passengers—and selling these items to other passengers for cash.
- *Selling non-Amtrak items.* This scheme involves smuggling non-Amtrak items on board trains and selling them to passengers.
- *Shorting cash register sales.* This scheme involves selling items for their retail value and ringing up smaller amounts, with Amtrak employees pocketing the difference.
- *Stealing inventory.* This scheme involves directly taking food (rice, oil, eggs, and potatoes) and other items such as complimentary beverages, paper products, and open wine bottles.
- *Providing items at no cost.* This scheme involves providing customers with complimentary items and providing free drink refills without authorization.

Compared with industry best practices, Amtrak lacked

- a *loss-prevention unit* with dedicated staff to manage loss; investigate cash and inventory losses; and provide a visible deterrent to fraud, waste, and abuse;
- a *management-sponsored fraud-awareness program* for on-board service employees;
- *random, internal management searches* of lead service attendants and other service employees to detect possible unauthorized items;

- *random, internal management reviews* of lead service attendants' inventories of deliveries, en route transfers, or end-of-trip stocks to minimize fraud, waste, and abuse;
- *random, internal management searches* of lead service attendants and other service employees when departing the train to detect possible stolen items; and
- *cashless sales* to remove the opportunity to steal cash.

We recommended that Amtrak (1) establish a pilot project of cashless food and beverage sales on selected routes; (2) provide the resources needed to establish a loss-prevention unit; and (3) have the loss prevention unit implement an internal control plan to address weaknesses and gaps in on-board food and beverage service. As of last month, Amtrak has taken action or has plans to address two of our three recommendations.

First, Amtrak has established a loss-prevention unit and has hired four staff for the new unit. Amtrak plans to provide the staff with 3 weeks of training this month. Once the training is completed, the team will start to develop an internal control action plan, which, according to an Amtrak Transportation Department official, should be completed by December. Amtrak has not taken any action on our recommendation to establish a pilot cashless project and currently has no plan to implement our recommendation.

ADDRESSING THE FRAGMENTED MANAGEMENT STRUCTURE CAN ENHANCE PROGRAM ACCOUNTABILITY AND PLANNING

Our work on food and beverage program management is ongoing, but we do have some preliminary observations and a suggested action, which we have discussed with Amtrak. We will issue a final report on these issues in the next couple of months.

Amtrak's food and beverage service incurred a reported direct operating loss of almost $85 million in Fiscal Year (FY) 2011. Amtrak made some progress in reducing reported direct operating losses—increasing its recovery of costs from 49 cents to 59 cents on the dollar between FYs 2006 and 2011. Amtrak has also identified initiatives for FY 2012 and beyond to help further increase cost recovery, such as lengthening the selling period on trains and reducing check-in/check-out times for on-board service personnel. We encourage these initiatives, but note that they will result in relatively small efficiency gains because they are being applied to the existing business model for food and beverage service.

We believe Amtrak's initiatives could be enhanced with improved program management to include consideration of different business models. Food and beverage management activities are carried out in a fragmented and somewhat uncoordinated manner by two Amtrak departments. The Marketing and Product Development Department manages commissary and support operations, while the Transportation Department manages on-board service personnel. Two key management weaknesses stem from this fragmented program management structure: a lack of (1) accountability for program results and (2) program-wide planning. The absence of clear accountability for results and program plans that address the primary reasons for operating losses hinder the company's efforts to improve cost recovery and service.

Accountability for Program Results

As noted, two departments share responsibility for food and beverage service, but neither is accountable for improving service and/or reducing direct operating losses—let alone eliminating them. And initiatives to improve cost recovery are not well-coordinated.

According to Marketing and Product Development's Chief of Food and Beverage Service, cost recovery is the most important metric for measuring food and beverage results. However, no cost-recovery goal has been established for this metric in Amtrak's 5-year financial plan. The Transportation Department likewise has no cost-reduction goal for food and beverage labor costs. Without a clear program-wide goal, and an official accountable for achieving that goal, Amtrak decreases the likelihood that direct operating losses will be reduced while maintaining the quality of service.

As shown in Table 1, the responsibilities for cost-recovery initiatives are divided among several departments, principally Marketing and Product Development and Transportation.

Table 1. Initiatives to Improve Food and Beverage Cost-Recovery

(dollars in millions)

	Initiative/Implementation Responsibility[a]	Low Estimate	High Estimate
Revenue Increases	Increase revenue by increasing selling period on trains, improving sales data, and targeted pricing (T and MPD)	$3.7	$7.4
	Enhance revenue loss-avoidance (T)	0.6	1.4
	Subtotal, Revenue Increases	**$4.3**	**$8.8**
Cost Decreases	Decrease on-board labor costs by reducing check-in/check-out times (T)	2.5	5.1
	Decrease warehouse costs by eliminating manual data entry (MPD)	0.8	1.4
	Reduce staff and eliminate manual data entry at accounting center (F)	1.5	1.5
	Increase crew base productivity (T)	1.0	2.1
	Subtotal, Cost Decreases	**$5.8**	**$10.1**
Total Impact on Cost-Recovery		**$10.1**	**$18.9**

Source: Amtrak Food and Beverage briefing to Amtrak Board of Directors, January 20, 2011

[a] **MPD** stands for Marketing and Product Development, **T** stands for Transportation, and **F** stands for Finance.

In discussing these initiatives with officials from these departments in March of this year, we learned that these initiatives were not well coordinated. For example, Marketing and Product Development estimated in January 2011 that between $2.5 million and $5.1 million could be saved yearly by reducing check-in/check-out times for some on-board food and beverage service personnel. However, these estimates were developed without input from the Transportation department, which manages on-board labor. Transportation officials stated that they had already begun implementing similar efforts. As a result, this raised questions as to whether these estimates were realistic, since some projected labor savings may have already been realized.

On July 19, 2012, the Vice President for Operations announced the establishment of a Chief of Customer Service position within the Transportation Department. The Vice President explained that this position will help align the company's new business lines with Amtrak's September 30, 2011 strategic plan. He stated that the Chief of Customer Service will have accountability (with multiple layers of cascading metrics within his or her organization) for improving Amtrak's food and beverage service program. On July 30, he further stated that the Marketing and Product Development's food and beverage services activities will be transferred under Operations as of October 1, 2012. We are encouraged by these two recent developments and believe that once these actions are fully implemented Amtrak will have in place a more effective and efficient framework for managing food and beverage services.

Program-wide Planning

A key management best practice for helping to reduce food and beverage service losses is a program-wide plan for improving cost recovery while maintaining service levels. However, such a plan does not exist at this time. As previously discussed, the planned initiatives will only result in small efficiency gains because they are being applied to the existing business model. Specifically, the initiatives do not adequately address losses on long-distance routes or alternative business models for food and beverage service.

We believe a comprehensive plan to improve cost recovery would include a focus on reducing costs in those areas in which losses are the greatest. As shown in Table 2, long-distance routes accounted for about $74 million (87 percent) of FY 2011 food and beverage service losses.

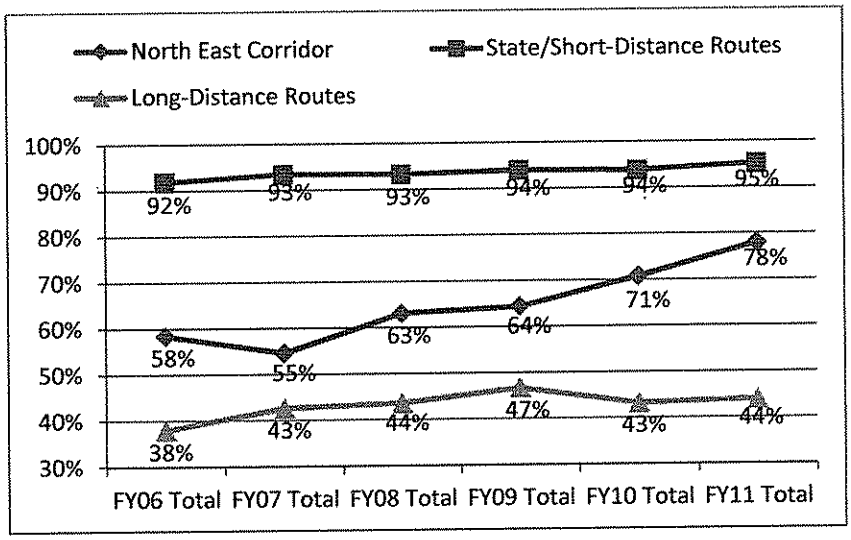
Table 2. Reported FY 2011 Food and Beverage Service Direct Operating Losses
(dollars in millions)

Routes	Revenue	Direct Costs			Loss	Percentage of total loss
		Labor	Commissary	Total		
Northeast Corridor	$ 31.8	$ 19.6	$21.2	$ 40.9	($9.0)	11
State-supported	31.7	19.4	13.9	33.3	(1.6)	2
Long-distance	57.9	78.0	53.9	131.9	(73.9)	87
Total	**$121.5**	**$117.0**	**$89.0**	**$206.0**	**($84.6)**	**100**

Source: Amtrak Finance Department, Food and Beverage Marketing Report for FY 2011
Note: Numbers do not all add due to rounding.

Further, between FYs 2006 and 2011, long-distance routes had the lowest cost-recovery rate for food and beverage service among all Amtrak routes. For example, in FY 2011, Amtrak's 15 long-distance routes collectively recovered only 44 cents of every dollar of food and beverage cost. (See Figure 1.)

Figure 1. Reported Cost-Recovery by Route, FYs 2006–2011



Source: OIG analysis of data from Amtrak and U.S. Bureau of Labor Statistics

NOTE: Amtrak operates 27 short-distance routes. On 21 of these routes, food and beverage service breaks even because of state subsidies, which Amtrak counts as revenue. Thus any operating losses come from the remaining six short-distance routes that no states subsidize.

However, there is no integrated plan for improving cost recovery and none of Amtrak's current initiatives adequately address losses on long-distance routes

Suggested Action

Our suggestion at this time is that the Vice President of Operations develop a 5-year plan for reducing the operating losses. The plan should include specific initiatives and annual operating loss reduction goals while retaining needed services.

FUTURE OIG WORK WILL FOCUS ON BEST PRACTICES TO HELP MITIGATE DIRECT OPERATING LOSSES

Over the next 6 months, our food and beverage work will focus on identifying ways to help mitigate the food and beverage service direct operating losses while at the same time continuing to provide high-quality service. The need for similar efforts has been identified previously. For example, in addition to our prior work, a 2005 Department of Transportation Office of Inspector General report on alternatives for providing service on long-distance routes recommended that Amtrak implement pilot projects to decrease losses.[4] However, the food and beverage service business model remains largely unchanged.

Our ongoing work will focus on identifying and reviewing best practices used by other public- and private-sector entities that provide food and beverage services to passengers, such as foreign passenger railroads, cruise lines, and airlines. While we are in the early planning stage of this work, some initial concepts that we have identified for review include the following:

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[4] CR-2005-068, *Analysis of Cost Savings on Amtrak's Long-Distance Service*, July 22, 2005.

- **Alternative levels of service.** In this area we will look at applying best practices using Amtrak personnel to provide food and beverage service. For example, one option may be to use café cars instead of dining cars, thus reducing staff but still providing food and beverage service that the travelling public depends on. Currently, Amtrak offers dining-car service on 14 of its 15 long-distance routes. The only long-distance route without a dining-car is the *Palmetto*, which had the lowest food and beverage service loss of any long-distance route in FY 2011.

- **Alternative means of service**. In this area we will look at applying best practices using Amtrak personnel to furnish food and beverage service through alternative methods, such as vending machines and food carts. Other methods could include offering food and beverages at boarding gates or platforms, and displaying items for passengers to select and having lead service attendants scan bar codes. For example, according to a North Carolina official, that state has used vending machines since early 2011 on the *Piedmont*, a state-supported Amtrak route.

- **Third-party provider**. A best practice used by many public and private entities is to use a third party to carry out non-core-business services. A third party provider could be used to offer different levels and methods of food and beverage service in conceptually the same, or other, ways as just described. For example, Maine has contracted with a third-party provider to furnish food and beverage service since 2001 on the *Downeaster*, another state-supported Amtrak route. We recognize that any initiatives in this area would have a significant impact on the existing labor force and would have to be carefully considered in any new approaches to providing food and beverage service.

We will be reviewing the pros and cons of these and other best practices to identify food and beverage service alternatives that Amtrak could pilot test or adopt on various routes. Our analysis will focus on key factors such as cost, quality of service, workforce, and revenue impacts.

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In summary, Amtrak has taken action to address some of our June 2011 recommendations related to fraud, waste, and abuse. Further, Amtrak has initiatives underway to increase cost-recovery on food and beverage service. Additionally, Amtrak has actions underway to improve program management and accountability. However, steps can be taken to improve planning.

Mr. Chairman, in closing I want to thank the Committee for its support of the Amtrak OIG. This concludes my testimony and I would be glad to answer any questions that you or other members of the Committee may have at this time.

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

Truth in Testimony Disclosure

Pursuant to clause 2(g)(5) of House Rule XI, in the case of a witness appearing in a nongovernmental capacity, a written statement of proposed testimony shall include: (1) a curriculum vitae; and (2) a disclosure of the amount and source (by agency and program) of each Federal grant (or subgrant thereof) or contract (or subcontract thereof) received during the current fiscal year or either of the two previous fiscal years by the witness or by an entity represented by the witness. Such statements, with appropriate redaction to protect the privacy of the witness, shall be made publicly available in electronic form not later than one day after the witness appears.

(1) Name: Ted Alves

(2) Other than yourself, name of entity you are representing: Amtrak Office of Inspector General

(3) Are you testifying on behalf of an entity other than a Government (federal, state, local) entity?

Yes

(4) Please list the amount and source (by agency and program) of each Federal grant (or subgrant thereof) or contract (or subcontract thereof) received during the current fiscal year or either of the two previous fiscal years by you or by the entity you are representing: None

Signature

8/1/12

Date

Amtrak's Inspector General

Theodore (Ted) Alves

Theodore (Ted) Alves was appointed Amtrak's Inspector General in November 2009. Mr. Alves was the Deputy Inspector General at the U.S. Department of Transportation (DOT) when he retired in January 2009 after 35 years of Federal service. DOT is the federal agency responsible for achieving a safe, efficient, and effective transportation system that enhances the quality of life of the American people. As the Deputy Inspector General, Mr. Alves was responsible for providing executive level leadership and direction of all Office of Inspector General (OIG) audits and investigations as well as overseeing operational support activities such as human resource, information technology, accounting and budgeting, and procurement activities for the OIG.

He served the DOT OIG for over eight years in several executive positions, including Principal Assistant Inspector General for Audits and Evaluations, Assistant Inspector General for Financial and Information Technology Audits, and Assistant Inspector General for Surface Infrastructure Audits.

Before joining DOT, Mr. Alves led the Financial Management Audits Branch at the Federal Emergency Management Agency (FEMA). He was responsible for overseeing financial statement, financial management, and information technology audits. Prior to joining FEMA, Mr. Alves spent 4 years as the Director of Information Technology and Special Audits at the U.S. Agency for International Development and 22 years with the U.S. Government Accountability Office.

Mr. Alves was born in Medford, Massachusetts and has a bachelor's degree in Management from Northeastern University, in Boston. He is a Certified Inspector General and a Certified Government Financial Manager. He is also a member of the Association of Inspectors' General, the Association of Government Accountants, and the Institute of Internal Auditors.