FINANCE

A $1.6B Railway Sale Could Fund Cincinnati's Infrastructure

It's the only city in the U.S. to own an interstate railway. Now Cincinnati wants to sell to Norfolk Southern and create an infrastructure trust fund. But first, voters need to give the plan their OK.

Aug. 1, 2023 • **Jared Brey**

Rail giant Norfolk Southern has agreed to purchase the Cincinnati Southern Railway from the city for $1.6 billion. Interest payments from the sale could be used to fund badly needed infrastructure repairs. (Amy Davis/Baltimore Sun/TNS)
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In Brief:

- Cincinnati voters will vote in November on whether to sell the Cincinnati Southern Railway to Norfolk Southern, one of the biggest freight operators in the U.S.

- Norfolk Southern has been paying around $25 million a year for the lease.
- Leaders say the sale could create a trust fund that generates around $50 million a year in perpetuity — more than Norfolk Southern has been willing to pay in lease negotiations.

The people of Cincinnati will face a one-of-a-kind decision this fall when they vote on whether to sell Cincinnati Southern Railway, a 140-year-old asset that, until recently, many city residents didn't even know was theirs.

The railway, a 337-mile freight route from Cincinnati to Chattanooga, was built by the city in the 1870s, after the state constitution was amended to allow cities to build and own railroads. Today, it's the only city in the country that owns its own interstate railroad. Leaders say it's been a boon — first as a strategic investment that boosted Cincinnati's role in interstate commerce and later as a source of recurring, eight-figure lease payments. But now they say it's time to sell.

Norfolk Southern, the freight operator whose subsidiaries have been running the Cincinnati Southern Railway for more than a century, is offering $1.6 billion to buy the railway outright. That's enough to secure a permanent source of funding for infrastructure and begin to chip away at the city's growing backlog of deferred maintenance, says Cincinnati Mayor Aftab Pureval. But first, voters need to be convinced that selling the railroad is the best way to take advantage of it.

"This is really a make-or-break decision for the future of Cincinnati," Pureval says.

A Unique Asset

Ohio River commerce fueled Cincinnati's early growth. But as railroads snaked across the [illegible] and took on more economic importance, Cincinnati's riverside setting became less [illegible]portant. Railroads began carrying more freight through strategic points in Louisville and Nashville, says Paul Muething, president of the Cincinnati Southern Railway Board of Trustees. Faced with the prospect of being left behind, Cincinnati leaders decided to build their own railway, establishing a critical link between rail networks in the northeast and the south, and securing the city’s position within them.

Since 1881, the year after the first train completed the route, the railway has been operated by Cincinnati, New Orleans and Texas Pacific Railway (CNO&TP), a wholly owned subsidiary of Norfolk Southern. The company has operated the line on 25-year leases, with recent payments to the City of Cincinnati of about $25 million a year. (cincinnatisouthernrailway.org)

“The line was originally constructed for that purpose and over time it has morphed from a strategic asset to a unique financial asset that the city continued to own,” Muething says.

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The ‘Best Possible Price’?

Norfolk Southern has a right to extend the lease another 25 years, and the city began renegotiating the terms in 2020. But Muething says the parties had started negotiating in very different places — Cincinnati wanted $65 million a year while Norfolk Southern was offering $35 million a year — and soon found themselves at a dead-end. The rail company then offered to buy the railway outright, making clear to the board that the property was much more valuable to them if they owned it than if they leased it.

In a press release, Norfolk Southern said the purchase would eliminate "uncertainty around future lease costs." The company was also motivated, according to Muething, by the potential improvement to its operating ratio — a measure, highly valued on Wall Street, of how much revenue a company earns compared with how great its ongoing expenses are. (A spokesperson for Norfolk Southern shared a press release and declined to answer additional questions.)

"Our financial adviser has confirmed that these Class I [railroads] are really driven by that ratio," Muething says.

After Norfolk Southern made its initial offer to purchase the railway in July of 2021, for $865 million, the company and the board spent the next year and a half negotiating the price. Last fall, the city announced its agreement to sell the railway for $1.6 billion, pending approval by the voters via a ballot referendum. The money would be put into a trust fund, and Cincinnati would collect the interest payments each year — between $50 million and $70 million in a typical year based on conservative investment practices, according to the board, but no less than $25.5 million in any year — without spending down the principal.

Pureval says the offer represents the "best possible price" for the railway, and will secure a long-term revenue stream for Cincinnati that would be unique among American cities.

"In my view it's really not a sale. It's really a transfer of a physical property into a $1.6 billion trust fund that we'll have in perpetuity," he says.

Investing in 'Bread and Butter' Infrastructure

Since the 1980s, Cincinnati has spent the revenue from its lease with Norfolk Southern on infrastructure maintenance. And according to the deal struck last year, the sale would only move forward if state law was changed to require trust fund payments to be spent on existing infrastructure as well, a rule which was included in Ohio's most recent transportation bill. The reason why the revenue needs to be restricted to existing infrastructure maintenance is to avoid “a feeding frenzy,” Pureval says.

“There are a lot of needs that the city has that $1.6 billion could go to,” he says. “$1.6 billion is a lot of money, don’t get me wrong. But it can also be spent very, very quickly. What we want to avoid is selling a railroad that is incredibly valuable and then in 10 years having very little to show for it.”

The city has a deferred maintenance backlog of about $400 million, Pureval says, including a fleet garage that is “falling down” and would cost around $43 million to fix. The interest payments from the proposed sale would allow the city to address more of its infrastructure needs — fixing potholes, upgrading parks and recreation centers, repairing bridges and so on — and catch up to the backlog over time, he says.

“It really just boils down to apple pie, bread-and-butter city services,” Pureval says. “It’s not fancy stuff, but it’s critically important stuff that affects people’s daily lives.”

Should the City Sell?

Some railroad workers and local activists oppose the sale. Railroad Workers United, an advocacy group made up of members of various railroad unions, has called the $1.6 billion offer “paltry,” and encouraged local voters to oppose the sale in November. The group says freight companies like Norfolk Southern have prioritized their own short-term profits over the long-term health of the railroad system generally — for freight as well as for passengers. It has also called for public ownership of all the railways in the U.S.

In Cincinnati’s case, says Ron Kaminkow, a Reno-based organizer for Railroad Workers United, the city has a uniquely valuable asset that it shouldn’t surrender to a private corporation. It stands to gain more from Norfolk Southern by keeping the rail then by selling it, he says.

“Norfolk Southern has no alternative — there’s no alternative route that they can just say, ‘Hey, we can’t reach a contract with the city of Cincinnati on this railroad so we’ll use a different route,’” Kaminkow says. “It seems to me that Cincinnati has a lot of cards to play here and can actually make a lot more money leasing this railroad to Norfolk Southern than they have historically.”

Joshua Junker, a local college student and activist, also opposes the sale, saying the Cincinnati Southern Railway is “pretty priceless and can’t be built again.” There are [illegible]efits in owning the right of way, which the city could use for utilities like fiber-optic [illegible]es for broadband, and in keeping the real estate over the longer term. While $1.6

billion is a huge sum, the value of the railroad is almost certain to increase over time, he argues.

“[Norfolk Southern] is not winning the short-term battle — they’re winning the medium- and long-term battle by making this acquisition,” Junker says.

Pureval says those views miss some important facts. While it’s true that Norfolk Southern has no viable alternative route outside the Cincinnati Southern Railway, it’s also true that the railway connects to railroads that are primarily controlled by that company. Its main competitor in the region, CSX, has a parallel line in its own network, so it’s not clear who else the city could sell or lease the property to: Norfolk Southern is “the entity in the position to value it the highest,” Pureval says.

Beyond that, he says, it’s already the case that Cincinnati has no operational control over the railway, which is federally regulated and operated entirely by Norfolk Southern’s subsidiary. The city can’t force the company to make safety improvements or run passenger service as is, he says.

Still, the politics of the sale aren’t clear cut. Norfolk Southern is also the freight operator behind the East Palestine derailment earlier this year, which caused a major release of hazardous chemicals in a small Ohio town. While some voters may hesitate to sell to the company responsible for that disaster, Pureval argues it’s better for the city to sever its connection with the company altogether. If the spill were to happen on the Cincinnati Southern Railway today, he says, the city could be held partly liable.

It’s a lot for voters to take in over the next few months.

“The more people learn about [the sale], the more positive they are, but it’s by no means a slam dunk either way,” Pureval says. “I think it’s going to be a close call. But I am convinced this is the best thing for the city right now.”

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