

UNITED STATES OF AMERICA
SURFACE TRANSPORTATION BOARD

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HEARING

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IN THE MATTER OF: :

Docket No.

REVIEW OF COMMODITY, BOXCAR, : Ex Parte 704

AND TOFC/COFC EXEMPTIONS

:

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Thursday,
February 24, 2011

Surface Transportation Board
Suite 120
395 E Street, S.W.
Washington, D.C.

The above-entitled matter came on
for hearing, pursuant to notice, at 10:00 a.m.

BEFORE:

DANIEL R. ELLIOTT, III Chairperson
CHARLES D. NOTTINGHAM Vice Chairman
FRANCIS P. MULVEY Commissioner

APPEARANCES:

FEDERAL GOVERNMENT PARTIES

On Behalf of U.S. Department of
Transportation:

PETER PLOCKI, Esq.
Deputy Assistant General Counsel
1200 New Jersey Avenue, SE
Washington, DC 20590
Tel: (202) 366-4000

RAILROAD INTERESTS

On Behalf of The American Short Line and
Regional Railroad Association:

RICHARD F. TIMMONS
President
American Short Line and Regional
Railroad Association
50 F Street, N.W.
Suite 7020
Washington, D.C. 20001

Tel: (202) 585-3442

On Behalf of the Association of American
Railroads:

EDWARD R. HAMBERGER
President and CEO

ROBERT WILLIG
Association of American Railroads
425 Third Street, S.W.
Suite 1000
Washington, D.C. 20024
Tel: (202) 639-2100

SHIPPER INTERESTS

On Behalf of the Alliance of Automobile
Manufacturers:

of: JEFFREY O. MORENO, Esq.
Thompson Hine LLP
1920 N Street, N.W.
Suite 800
Washington, D.C. 20036
Tel: (202) 263-4107

On Behalf of the American Forest & Paper
Association and The Paper and Forest Industry
Transportation Committee:

BILL LOVICK, Esq.
110 Iron Street
Hurley, Wisconsin 54534

On Behalf of the National Industrial
Transportation League:

BRUCE CARLTON
President and CEO
National Industrial
Transportation League
1700 North Moore Street
Suite 1900

Arlington, Virginia 22209
Tel: (703) 524-5011

On Behalf of the Wisconsin Central
Group:

of: JOHN DUNCAN VARDA, Esq.
DeWitt Ross & Stevens SC
2 East Mifflin Street
Suite 600
Madison, Wisconsin 53703
Tel: (608) 212-1103

FREIGHT RAILROADS

On Behalf of BNSF Railway Company:

STEVE BRANSCUM
Group Vice President
Consumer Products
2650 Lou Menk Drive
Fort Worth, Texas 76131
Tel: (800) 795-2673

On Behalf of CSX Transportation, Inc.:

CLARENCE W. GOODEN
CSX Transportation, Inc.
500 Water Street
15th Floor
Jacksonville, Florida 32202
Tel: (904) 359-3200

On Behalf of Norfolk Southern Railway
Company:

DAVID LAWSON
Norfolk Southern Railway
Three Commercial Place
Norfolk, Virginia 23510
Tel: (757) 823-5358

On Behalf of Union Pacific Railroad
Company:

ERIC BUTLER
JULIE KREHBIEL
Union Pacific Railroad

1416 Dodge Street
Omaha, Nebraska 68179
Tel: (402) 544-5000
SHIPPERS

On Behalf of Holcim (US) Inc.:

TOM GIOVINAZZI
201 Jones Road
Waltham, MA 02451
Tel: (781) 647-2501
Fax: (781) 647-2516

On Behalf of Packaging Corporation of
America:

DINA CALABRO
1900 West Field Court
Lake Forest, IL 60045
Tel:(800) 456-4725
Fax:(847) 482-4545

BRUCE RIPLEY
N9090 County Road E
Tomahawk, WI 54487
Tel:(715) 453-2131
Fax:(715) 453-0470

On Behalf of Weaver Popcorn Company,
Inc.:

WILL WEAVER

Chief Operating Officer
408 W Landess St
Van Buren, IN 46991-9620
Tel: (765) 934-2101

INTERMODAL INTERESTS

On Behalf of Intermodal Association of
North America, Inc.:

JOANNE F. CASEY
11785 Beltsville Drive
Suite 1100
Calverton, Maryland 20705

Tel: 301-982-3400
Fax: 301-982-4815

OTHER INTERESTS

On Behalf of CNJ Rail Corporation:

ERIC S. STROHMEYER

81 Century Lane

Watchung, NJ 07069

On Behalf of Mercury Group:

CRAIG S. DICKMAN

The Mercury Group

201 N. Union St., Suite 510

Alexandria, VA 22314

Tel: (703) 299-9470

Fax: (703) 299-9478

On Behalf of United Transportation

Union-New York State Legislative Board:

GORDON MacDOUGALL

Beacon Consulting Group, Inc.

400 Seventh St, NW, Ste 505

Washington, DC 20004

Tel: (202) 544-7944

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1 P-R-O-C-E-E-D-I-N-G-S

2 (2:06 p.m.)

3 CHAIRMAN ELLIOTT: Good morning.

4 Welcome. Today we're going to hear testimony
5 regarding the various commodity exemptions,
6 the boxcar exemptions, and the intermodal or
7 TOFC/COFC exemptions.

8 Before I get started today, I just
9 wanted to take a moment to express our
10 condolence to the Riser family. Jack Riser,
11 who worked here as a transportation industry
12 analyst, passed away last night.

13 He's one of our newer employees,
14 he is one of our family, and it's just a very
15 sad, sad day because of that. We'll miss him
16 dearly. So if you could keep his family and
17 his wife, Chris, in your thoughts and prayers,
18 we'd appreciate that. Why don't we just take
19 a quick moment of silence just to remember
20 that. Thank you.

21 Back to the business at hand, like
22 many issues that come before the Board, these

1 exemptions have a historical context. In the
2 4R Act of 1976 and the Staggers Act of 1980,
3 Congress reduced the Interstate Commerce
4 Commission's direct oversight of railroads in
5 various ways.

6 One way it did so was by directing
7 the ICC to exempt railroad activities when it
8 found that regulation is not necessary to
9 carry out the National Rail Transportation
10 Policy, and either the exemption was of
11 limited scope or regulation was not necessary
12 to protect shippers from the abuse of market
13 power.

14 In the Staggers Act, Congress
15 directed the ICC to pursue exemptions
16 aggressively and to correct any problems that
17 arose through its revocation authority.
18 Consistent with that congressional directive,
19 the Agency exempted numerous commodities,
20 services, and types of transactions from
21 regulation.

22 An exemption excuses carriers from

1 virtually all aspects of regulation, even
2 though the Board's continuing jurisdiction
3 over exempted movements also extinguishes any
4 common law cause of action regarding common
5 carrier duties.

6 So for exempted movements, rail
7 customers can pursue legal remedies under the
8 Interstate Commerce Act only if they first
9 successfully petition the Agency to revoke the
10 exemption. There is a statutory standard for
11 revoking them.

12 Parties can come before the Agency
13 and seek partial or complete revocation of an
14 exemption. Partial revocation allows a
15 shipper of an exempt commodity to pursue
16 regulatory remedies here at the Board.

17 For example, in one case the Board
18 revoked an exemption for crushed or broken
19 stone, sand, and gravel in response to a
20 complaint that a railroad was blocking another
21 railroad's ability to fulfill its common
22 carrier obligation. A long time has passed

1 since the Agency began exempting traffic from
2 regulation.

3 Today exempt traffic accounts for
4 roughly 40 percent of all freight revenue, or
5 about \$20 billion per year, so this is a very
6 important matter. That's why the Board has
7 decided that the time has come to have a
8 public discussion about the exemptions and
9 their effect on the rail industry, its
10 customers, and the general public.

11 Just a few procedural notes
12 regarding the testimony itself. As usual, we
13 will hear from all speakers on the panel prior
14 to questions from the Commissioners.

15 Speakers, please note that the
16 timing lights are in front of me on the dais.
17 You will see a yellow light when you have one
18 minute remaining and a red light when your
19 time has expired. Please do your best to keep
20 to the time you have been allotted.

21 I assure you that we have read all
22 your submissions. There is no need to read

1 them here. After hearing from the entire
2 panel, we will rotate with questions from each
3 Board member until we have exhausted the
4 questions.

5 Additionally, just a reminder.
6 Please turn off your cell phones. I look
7 forward to hearing the testimony of the
8 parties, and I'd now like to turn it over to
9 Vice Chairman Nottingham for his opening
10 remarks.

11 VICE CHAIRMAN NOTTINGHAM: Thank
12 you, Chairman Elliott. I'll be brief. We
13 have a lot of witnesses today, and I welcome
14 everybody. Thank you for joining us. We have
15 quite a full room here, and I imagine we've
16 got some people on the internet watching via
17 the web, too.

18 I'll just note a little bit of the
19 history that the Chairman touched on. We were
20 directed to adopt exemptions in a pretty
21 sweeping way by the Congress.

22 Industries came to us and asked

1 for these exemptions years ago, and in the
2 ensuing years we've had very few cases. In
3 fact, during my tenure, none that I can think
4 of, where industries or companies have come in
5 and availed themselves of the statutory right
6 that has been in place for many, many years,
7 which is to petition the Board, as the
8 Chairman touched on, for a partial or a
9 complete revocation.

10 So I look forward to hearing today
11 as to -- regarding whether, if this is a
12 problem, why haven't people availed themselves
13 of the tool that's been available for so many
14 years to seek relief, and if there's something
15 the Board is doing or not doing that makes
16 that process untenable, I want to understand
17 that a little better.

18 I'm a big believer in self-help.
19 Too often, we encounter interested parties
20 around this town and elsewhere who would
21 rather complain about something than actually
22 take the steps necessary to correct it, and

1 I'm all about correcting problems and solving
2 problems, and that's what brings all of us, I
3 think, into public service.

4 So I look forward to hearing from
5 everyone today, and I keep an open mind on
6 this. I urge folks not to read too much into
7 it. The Board historically has conducted
8 oversight hearings on interesting, important
9 issues.

10 It doesn't mean anything in
11 particular necessarily, but it's an important
12 part of what we do to stay current, to see
13 whether circumstances truly have changed to a
14 degree that might warrant a regulatory
15 adjustment or a recommendation to Congress or
16 some other Board action.

17 So, with that in mind, I
18 appreciate again the attendance today and look
19 forward to hearing from everybody. Thank you.

20 CHAIRMAN ELLIOTT: Thank you, Vice
21 Chairman, and now we'll hear from Commissioner
22 Mulvey.

1 COMMISSIONER MULVEY: Thank you,
2 Chairman Elliott. A personal note to begin
3 with. Jack Riser was part of a team of
4 transportation specialists who briefed me on
5 the state of the railroad industry on a
6 biweekly basis, and I will tell you we will
7 very much miss his contribution. He was an
8 important part of the STB, and he will be
9 missed by all of us.

10 I am pleased today that the Board
11 is having this hearing, and I look forward to
12 hearing the oral testimony. Several years ago
13 now, I first suggested that it might be a good
14 idea to periodically review exempt commodities
15 and traffic to ensure that the exemptions were
16 still appropriate.

17 I have always thought that it's
18 important for the Board to be aware of what is
19 going on on the ground in the rail industry
20 that we regulate and the shipping industries
21 that are affected by that regulation. This
22 particular hearing allows the Board to get

1 information from industry participants on
2 whether there have been any major changes in
3 the competitive landscape that would merit the
4 Board's reconsideration of any specific
5 exemption.

6 After all, the ICC exempted the
7 first commodities more than 30 years ago.
8 That was fruits and vegetables back in 1979,
9 and the last commodity that was exempted was
10 back in 1998, and that was non-ferrous metals.

11 Between those two periods, more
12 than 100 other commodities types and traffic
13 types have been exempted from regulation
14 following a finding by the Agency that
15 regulation was not necessary, primarily
16 because there was sufficient competition from
17 other transportation modes, chiefly trucking
18 and, to a lesser degree, barge.

19 Well, much has changed since 1979
20 in the transportation competitive landscape.
21 There are changes within the railroad
22 industry, changes in the trucking industry,

1 and, to some extent, changes in the barge
2 industry, as well. Likewise, many of the
3 industries shipping exempted commodities have
4 also experienced significant changes.

5 Some of the pleadings filed in
6 this proceeding suggest that the only
7 mechanism by which the Board can or should be
8 made aware of such changes is in a specific
9 exemption revocation proceeding. I'm sure
10 that this is an issue that we will hear more
11 about today.

12 In my opinion, however, regardless
13 of any steps the Board could take, I hope that
14 our stakeholders would not have the Board turn
15 a blind eye for decades as to whether or not
16 competitive changes undercut the basis for an
17 exemption. This is particularly so when you
18 are talking about industries characterized by
19 smaller shippers who may not be inclined in
20 the first instance to initiate an exemption
21 revocation proceeding.

22 Indeed, this hearing could serve

1 as a way to develop ideas about how the Board
2 could make its exemption revocation process
3 more efficient and more accessible, an effort
4 the Board has recently undertaken with regard
5 to rate reasonableness cases.

6 Now, to echo what Vice Chairman
7 Nottingham has said, I also want to make clear
8 that this is primarily an informational
9 hearing. I have seen suggestions that the
10 Board is poised to eliminate many or all
11 exemptions, force economic regulation of every
12 commodity, or otherwise return the rail
13 industry to its pre-Staggers condition.

14 I think that such suggestions
15 encourage our stakeholders to line up with
16 their most extreme positions. Whether you
17 support a particular exemption or not, most
18 would agree that exemptions have played an
19 important role in reducing economic regulation
20 of the railroads and that reduced regulation
21 has contributed to growth and innovation in
22 the railroad industry.

1 So, from my perspective, this
2 hearing is about ensuring that the Board has
3 the most up-to-date, competitive information
4 about the industry it regulates.

5 Finally, I want to make note that
6 I believe that most regulations and most
7 regulatory practices such as exemptions should
8 be subject to periodic review to ensure that
9 they still make sense.

10 Regulations that have outlived
11 their usefulness or serve as an impediment to
12 economic progress with no concomitant benefit
13 to society should be reviewed and repealed if
14 need be. The President has made it clear that
15 he believes that regulations should be
16 efficient and be in place only when they
17 benefit the national well being.

18 I hope to hear more today about
19 what the appropriate time period should be for
20 reviewing exemptions from STB regulation.

21 Thank you, Mr. Chairman.

22 CHAIRMAN ELLIOTT: Thank you,

1 Commissioner Mulvey. Thank you, Vice Chairman
2 Nottingham. Now we'll begin our first panel,
3 starting with Panel I, Federal Government, and
4 we'll hear from the U.S. Department of
5 Transportation, Peter Plocki. You have ten
6 minutes allotted. Thank you.

7 MR. PLOCKI: Thank you, Mr.
8 Chairman, and good morning, Mr. Chairman and
9 members of the Board. My name is Peter
10 Plocki.

11 I am the Deputy Assistant General
12 Counsel for Litigation for the U.S. Department
13 of Transportation, and I am presenting the
14 views of the Department in this proceeding.
15 The Department appreciates the opportunity to
16 be heard on this important matter this
17 morning.

18 The Board has instituted this
19 proceeding in order to review certain
20 categorical exemptions from regulations,
21 specifically exemptions for certain
22 commodities, for boxcar traffic, and for

1 trailer on flat car/container on flat car
2 traffic, which I shall refer to this morning
3 as intermodal services.

4 Exemption provisions pertaining to
5 railroads go back to the enactment of the
6 Railroad Revitalization and Regulatory Reform
7 Act of 1976 and the Staggers Rail Act of 1980,
8 the latter encouraging greater use of
9 exemption authority.

10 As the Board stated in its
11 instituting notice, this proceeding arises
12 from informal inquiries questioning the
13 relevance and/or necessity of existing
14 exemptions given changes in the competitive
15 landscape and in the railroad industry that
16 have taken place over the past few decades.

17 The Board requested comments as to
18 the effectiveness of these exemptions in the
19 marketplace, whether the rationale behind any
20 of these exemptions should be revisited, and
21 whether they should be subject to periodic
22 review.

1 As noted in the Department's filed
2 comments, the Department's best data regarding
3 the railroad industry's performance in these
4 three areas that are subject to this
5 proceeding relates to intermodal services.

6 Moreover, the Department's rail
7 freight policies have recently emphasized the
8 importance of the development of intermodal
9 services. Accordingly, my comments today,
10 like the Department's filed comments, will
11 focus on intermodal services.

12 Overall, the post-Staggers Act
13 regulatory environment has allowed railroads
14 to respond to market forces that have demanded
15 lower costs, greater productivity, and more
16 innovation in the form of new transportation
17 services. A significant aspect of these
18 improvements is the growth and evolution of
19 intermodal services.

20 Over the last few decades,
21 improvements in intermodal services such as
22 double-stacking have increased intermodal

1 capacity and efficiency and have thereby
2 allowed these services to better compete with
3 other modes, particularly in the long-haul
4 market. Thus, for example, in 2007 rail
5 intermodal had a 64 percent share of the
6 market for shipments of greater than 2,000
7 miles.

8 In the Department's view, numerous
9 public benefits are to be derived from the
10 continued growth of intermodal services.
11 These include benefits in the area of safety,
12 environmental sustainability, economic
13 competitiveness, state of good repair, and
14 with the billing.

15 As to safety, rail fatality rates
16 per billion ton miles are significantly lower
17 than for trucks. By moving some of the growth
18 in truck traffic onto rail, there will be a
19 reduction in the growth of truck ton miles
20 with a likely corresponding reduction in
21 truck-related fatalities.

22 Rail intermodal services also have

1 an advantage over motor carriage in terms of
2 fuel consumption. With less fuel consumption,
3 fewer greenhouse gases and other pollutants
4 are emitted into the atmosphere. This also
5 carries with it less dependence on petroleum
6 and its sometimes unreliable sources.

7 For economic competitiveness,
8 rail's ability to offer shippers a total
9 package of lower logistics costs means that
10 savings can be passed on to consumers in the
11 form of lower prices for goods in stores. For
12 U.S. manufacturers, keeping logistics costs
13 low means goods are more competitive in
14 domestic and world markets.

15 With respect to state-of-good-
16 repair concerns, moving more freight by rail
17 will help contain the public costs of
18 maintaining and repairing the nation's
19 highways. Finally, with fewer trucks on the
20 highways, congestion is reduced, which
21 improves livability.

22 In light of the myriad public

1 benefits of intermodal services, it should
2 come as no surprise that the Federal Railroad
3 Administration's National Rail Plan Progress
4 Report submitted to Congress in October of
5 last year laid out a goal of developing
6 strategies to attract 50 percent of all
7 shipments 500 miles or greater to intermodal
8 rail.

9 To be sure, motor carriers do play
10 and must continue to play a critical role in
11 keeping freight moving safely and efficiently
12 throughout the United States, particularly for
13 pick-ups and drop-offs at the origins and
14 destinations of freight movements.

15 However, as Secretary LaHood has
16 emphasized, it is the Department's goal to see
17 more freight move via rail, and toward that
18 end the Department has begun to make
19 substantial investments in freight rail's
20 ability to build capacity as part of the Tiger
21 Grant Program created by the American Recovery
22 and Reinvestment Act of 2009, supplementing

1 the significant private investment already
2 being made by freight railroads.

3 In deciding how to allocate these
4 grant monies, the Department evaluates the
5 public benefits that would be derived from
6 their use on particular projects, and in each
7 instance federal grants have been combined
8 with private sector funds and other public
9 monies.

10 In light of its commitment to the
11 continued vitality of intermodal services,
12 how, then, does the Department view the
13 intermodal services exemption? The Department
14 observed in its written comments that its
15 ultimate views on exempt traffic, intermodal
16 or otherwise, will be informed by its better
17 understanding of the issues after a factual
18 record is developed by knowledgeable parties.

19 While the Department has found the
20 comments filed in this proceeding informative,
21 the Department's views on the intermodal
22 services exemption expressed in its written

1 comments have not changed. At this juncture,
2 it is still not clear to the Department what
3 role the intermodal services exemption has had
4 in promoting the growth in intermodal traffic.

5 While freedom from regulation has
6 allowed railroads to introduce new services
7 without being concerned about the possibility
8 of their rates and practices being regulated,
9 it is highly unlikely that intermodal services
10 would have been subject to regulation even in
11 the absence of an exemption, because
12 intermodal rates have in the past been close
13 to variable costs.

14 In the future, however, as rail's
15 competitive position is strengthened,
16 particularly on long-haul intermodal movements
17 where it has a significant cost advantage over
18 truck movements, intermodal rates may rise
19 significantly above variable costs.

20 Thus, the Department continues to
21 believe that this and the other exemptions
22 should be evaluated on their merits and that

1 each evaluation should be based on a careful
2 focused review conducted on, for example, an
3 exemption-by-exemption basis. Thank you.

4 CHAIRMAN ELLIOTT: Thank you very
5 much, Mr. Plocki. Why don't we go to Vice
6 Chairman Nottingham, if you have any
7 questions?

8 VICE CHAIRMAN NOTTINGHAM: I have
9 no questions. I just want to thank Mr. Plocki
10 for joining us. It's always good to have the
11 Department before us. Thank you.

12 MR. PLOCKI: Thank you. It's good
13 to be here.

14 COMMISSIONER MULVEY: I also want
15 to thank you for coming and speaking before
16 us. It was very informative and very, very
17 useful. I did have one question, though.

18 You did say that based upon the
19 Department's analysis, the exemptions
20 themselves cannot be credited for the
21 increased rail and intermodal traffic, that
22 the traffic would probably have not been

1 regulated, anyway, because so much of it was
2 below the threshold rates, 180 percent of
3 revenue to variable costs. Is that correct?

4 MR. PLOCKI: Well, I think the
5 latter half of that is correct. With respect
6 to the first half, I think, you know, we have
7 seen no evidence suggesting that.

8 I don't think we have definitively
9 analyzed the evidence, because we simply
10 haven't -- or definitively reached a
11 conclusion on that first point, because we
12 simply haven't seen sufficient evidence on
13 that.

14 COMMISSIONER MULVEY: The
15 exemptions, I think, would help the
16 deregulatory process. The deregulatory
17 process helped the railroads, but making the
18 link between the two I think is more
19 difficult.

20 MR. PLOCKI: Yes.

21 COMMISSIONER MULVEY: Thank you.

22 CHAIRMAN ELLIOTT: I have no

1 questions, but we do thank you very much for
2 participating. We always appreciate it when
3 the Department comes, participates in our
4 proceedings. Thank you.

5 MR. PLOCKI: Thank you, Mr.
6 Chairman.

7 CHAIRMAN ELLIOTT: I'd now like to
8 call forward Panel II, which is the Railroad
9 Interest Panel. Thank you for coming here
10 today to participate in the hearing. We will
11 hear from the American Short Line & Regional
12 Railroad Association first. We'll hear from
13 Richard F. Timmons, and you have ten minutes.

14 MR. TIMMONS: Thank you, Mr.
15 Chairman and Commissioners. It's good to be
16 here and appreciate the opportunity to testify
17 this morning. I am Richard Timmons, President
18 of the American Short Line & Regional Railroad
19 Association, which is the national trade
20 organization that represents approximately 540
21 Class II and Class III railroads.

22 On behalf of our members, I thank

1 the Board for inviting testimony on the
2 commodity boxcar and intermodal exemptions.
3 The Short Line Association believes that the
4 exemptions are effective, have worked exactly
5 as intended by Congress, and benefit both
6 railroads and shippers.

7 There is no need to revisit the
8 rationale underlying the exemptions, because
9 petitions to revoke provide sufficient
10 opportunities for aggrieved parties to seek
11 review of those exemptions. Moreover, the low
12 number of revocation petitions filed by
13 aggrieved parties demonstrates that the
14 exemptions are not being abused.

15 Finally, periodic reviews of the
16 exemptions would force small railroads with
17 limited resources to incur substantial costs
18 to repeatedly defend the exemptions and
19 effectively would shift the burden of proof to
20 the railroads to prove regulation of the
21 subject traffic continued to be unwarranted,
22 which approach would be inconsistent with the

1 statutory mandate in favor of exemptions and
2 certainly at odds with the current regulatory
3 scheme governing petitions to revoke.

4 The Association urges the Board to
5 refrain from taking any action that would
6 limit or otherwise dilute the effectiveness of
7 the exemptions. Instead, the Board should
8 continue to uphold the statutory mandate to
9 exempt traffic to the maximum extent possible.

10 Please refer to my extended
11 remarks regarding these points, which are
12 appended to this written testimony as
13 Attachment 2 and are therefore made a part of
14 it by this reference.

15 Since the passage of the Staggers
16 Act, almost 300 newly formed railroads have
17 acquired light density lines in communities
18 across the U.S. Many short line properties
19 suffered from years of deferred maintenance
20 and service deterioration and are candidates
21 for abandonment.

22 The short line entrepreneurs

1 acquired these properties, rehabilitated the
2 track infrastructure, hired and trained staff,
3 and revitalized service in communities that
4 faced loss of rail services.

5 Today, these small businesses with
6 median annual revenues of just under \$2.5
7 million, operate approximately one-third of
8 the nation's rail lines and play a critical
9 role in the economy of the communities those
10 carriers serve. Despite operating
11 approximately one-third of our system, small
12 railroads earn less than five percent of
13 annual freight revenues.

14 Under these circumstances, it is
15 evident that small railroads do not have a
16 meaningful market power. These small
17 entrepreneurial businesses do, however,
18 provided essential services to shippers, as
19 well as communities located on light density
20 lines, often in rural areas.

21 The Board should refrain from
22 taking any action with respect to the

1 exemptions that would adversely affect the
2 regulatory environment in which short lines
3 have been able to thrive. These exemptions
4 are of critical importance to short line
5 railroads, and in practice they have worked as
6 intended with respect to traffic handled by
7 small roads.

8 Boxcar traffic and exempt
9 commodities are subject to intense inter- and
10 intramodal competition. The vigorous
11 competition for boxcar traffic and exempt
12 commodities has kept prices extremely
13 competitive.

14 Indeed, according to the Freight
15 Facts and Figures 2009, a copy of the Federal
16 Railroad Administration Handbook, trucks
17 handled 60 percent of the freight tonnage
18 moved by the major transportation modes.

19 For the short lines, the
20 competition is particularly intense. Traffic
21 moving over shorter distances, that is, 500
22 miles or less, is particularly susceptible to

1 diversion to truck transportation.

2 In recent years, larger numbers of
3 heavier trucks and combination vehicles, along
4 with federal legislative initiatives, have
5 made the competition even more difficult.
6 Even for traffic moving longer distances,
7 short lines generally must compete with trucks
8 and waterways, as well as intermodal operators
9 and oil truck operations on the Class Is.

10 Small railroads by definition
11 operate small systems that are in close
12 proximity to the Class I carriers. Because a
13 short line generally accounts for only a small
14 portion of the mileage of any interline moved,
15 shippers frequently have an opportunity to
16 bypass a small railroad by trucking their
17 cargo to the nearest trans-load facility on a
18 Class I rail system.

19 Shippers also can bypass short
20 lines by making intermodal shipments that move
21 onto rails at intermodal facilities served by
22 a Class I carrier. These options make small

1 railroads susceptible to traffic diversion in
2 ways that generally do not affect Class I
3 railroads.

4 Under these market conditions, it
5 is clear that short lines have virtually no
6 opportunity to abuse market power, and
7 effective competition for subject traffic is
8 present. Accordingly, the exemptions are
9 appropriate.

10 It is also important to note that
11 railroads are not the only beneficiaries of
12 exemptions. By deregulating exempt traffic,
13 railroads are able to compete more effectively
14 in markets that previously were dominated by
15 trucks, for example, the classic issue of
16 fresh fruits and vegetables.

17 Short line marketing personnel
18 fight a constant battle to preserve market
19 share. The exemption of boxcar traffic and
20 exempt commodities has allowed the free market
21 to function and the short lines to be
22 competitive. Thus, the exemptions benefit

1 shippers by providing them with a competitive
2 alternative to trucks or other modes of
3 transportation.

4 Such competition forces all modes
5 of transportation to provide more efficient
6 and economical service in order to maintain
7 their market share. Shippers are the
8 beneficiaries of this competition.

9 Retaining the exemptions is
10 especially important to small railroads,
11 because much of the traffic handled by short
12 lines is covered by those exemptions. We
13 believe that more than 50 percent of small
14 railroad traffic consists of boxcar and exempt
15 commodities.

16 The exemptions for boxcar traffic
17 and exempt commodities affect a much higher
18 percentage of small railroad traffic than
19 Class I traffic. Compounding this problem has
20 been a 30-year downward trend in railroad
21 general merchandise traffic of approximately
22 30 to 40 percent. Accordingly, any action by

1 the Board to prevent or limit the exemptions
2 would therefore have a disproportionately
3 adverse impact on small railroads.

4 A curtailment of the exemptions
5 would be unwarranted with respect to small
6 railroads, because in general those carriers
7 do not have a history of abusing market power,
8 and their service is limited in scope.

9 According to Railroad Facts, the
10 nation's 556 small railroads operate 32
11 percent of the railroad miles in the country
12 but earn only 4.22 percent of railroad
13 revenue. This disparity demonstrates that
14 small roads are virtually incapable of abusing
15 market power, either in their dealing with
16 shippers or with connecting carriers.

17 Similarly, small railroad
18 operations are limited in scope. The average
19 short line operates 71 miles of rail lines and
20 handles approximately 13,000 carloads of
21 traffic per year.

22 To put these numbers in

1 perspective, the smallest Class I railroad
2 operates over 5,800 miles of rail and handles
3 over 361,000 carloads of traffic each year.
4 Accordingly, short line operations are limited
5 in scope.

6 The Board should not engage in
7 general periodic reviews of the exemptions.
8 The revocation framework provides shippers as
9 well as others with an appropriate mechanism
10 for reviewing exemptions for specific abuses.

11 In addition, because a large
12 percentage of small railroad traffic consists
13 of exempt traffic, instituting periodic
14 reviews of the exemptions would force small
15 railroads, which by definition have limited
16 resources, to repeatedly defend the
17 appropriateness of such exemptions. Small
18 railroads simply lack the resources to do so.

19 In conclusion, the Short Line
20 Association urges the Board to refrain from
21 curtailing or limiting the exemptions, which
22 would have a disproportionately negative

1 impact on small railroads, to continue to rely
2 on the revocation mechanism currently in place
3 to correct any abuses of the exemptions, and
4 refrain from engaging in periodic reviews of
5 the exemptions that would force small
6 railroads to engage in costly proceedings.

7 The ASLRRRA appreciates the
8 opportunity to submit this testimony in ex
9 parte 704 and would welcome any questions you
10 may have at the appropriate time. Thank you
11 very much.

12 CHAIRMAN ELLIOTT: Thank you, Mr.
13 Timmons, and now we'll hear from the
14 Association of American Railroads. We'll hear
15 from Mr. Hamberger and Professor Willig.

16 MR. HAMBERGER: Good morning, Mr.
17 Chairman, Mr. Vice Chairman, Commissioner
18 Mulvey. We appreciate the opportunity to be
19 here this morning.

20 As usual, I find myself in violent
21 agreement with General Timmons and wish to
22 associate myself with his excellent remarks.

1 There are four fundamental considerations I
2 hope that the Board will keep in mind as you
3 evaluate the comments and testimony in this
4 proceeding.

5 Number one, there has been no
6 change in the law or congressional policy
7 favoring exemptions. Statutory provisions, as
8 well as attendant congressional policy and
9 guidance to the Board, has not changed.

10 By law, the Board is required to
11 exercise its exemption authority to the
12 maximum extent possible. The Board and its
13 predecessor, the ICC, have followed the
14 direction of Congress with respect to granting
15 exemptions.

16 Through ICTA in 1995, Congress not
17 only validated the Agency's approach to
18 exemptions, but, in fact, actually expanded
19 the Board's mandate to be more aggressive.
20 Since the Board has appropriately followed
21 congressional policy, and that policy has not
22 changed, there is no legal or policy basis for

1 the Board to change its approach to
2 exemptions.

3 Number two, the statutory test for
4 revocation is that the reapplication of
5 regulation is necessary to carry out rail
6 transportation policy. While Congress
7 mandated the Board to utilize its exemption
8 authority aggressively, it provided for
9 exemptions to be revoked only if there is an
10 abuse of market power by the exempt rail
11 carrier.

12 Accordingly, the test for
13 revocation is not whether an exemption is
14 still necessary. It is instead whether re-
15 regulation is necessary, and that depends not
16 on the financial condition of the industry,
17 not on whether there are no longer tariff
18 filing requirements, not whether rates may be
19 higher or lower than before.

20 As my written testimony details
21 and as Professor Willig will explain more
22 fully, the test is whether there is no

1 effective competition for the exempt movements
2 at issue and that the rail carrier is abusing
3 its market power regarding those movements.

4 It is important to note that the
5 burden of showing the need for revocation
6 rests with the party seeking that revocation.
7 The statute does not provide for the Board to
8 initiate revocation proceeding on its own
9 initiative, unlike proceedings to exempt
10 traffic, which the statute does specifically
11 authorize you to initiate on your own.

12 Issue three, the testimony in this
13 proceeding does not support any conclusion
14 that there is an abuse of market power
15 regarding any exempt transportation. Even if
16 the Board could initiate a proceeding on its
17 own, the facts do not support any further
18 Board action in this proceeding.

19 The testimony presented by other
20 parties does not rise to factual presentations
21 necessary to support a petition for revocation
22 of the boxcar intermodal or any entire

1 commodity exemption. You will hear more from
2 other railroad witnesses on this issue.
3 However, I wish to highlight one factor
4 relating to competition for exempt
5 transportation.

6 As Professor Willig noted in his
7 written testimony, revenue cost ratios for
8 particular commodity or car type movements are
9 not necessarily indicative of an absence of
10 effective competition. However, a low revenue
11 variable cost ratio has been determined by
12 statute to be a conclusive presumption of
13 effective competition.

14 On the screen you can see that all
15 boxcar traffic revenue variable costs since
16 that exemption was instituted in 1987 is
17 currently at a point below the rate of the
18 RVC in 1987.

19 Similarly, for all commodities the
20 rate is at approximately 148, 149 percent, far
21 below the 180 percent level for jurisdiction
22 here at the Board, and I will point out that

1 this is matched revenue, and so the actual
2 numbers are probably lower than you see here.

3 Issue four, reexamining well
4 established and proven underpinnings of rail
5 regulatory policies both in this proceeding
6 and in Ex Parte number 705 introduces
7 uncertainty into the industry. The Board has
8 taken these actions at a critically
9 inopportune moment for the railroad industry
10 and its various constituencies.

11 After many decades of decline,
12 attributable in large measure to over-
13 regulation for much of the 20th Century,
14 America's freight railroads have succeeded in
15 achieving enviable productivity gains and
16 solid economic growth in an era of decreased
17 regulation.

18 This has resulted in the railroads
19 achieving improved returns, which in turn has
20 permitted them to reinvest heavily in their
21 systems. The very regulations or absence of
22 regulation being discussed today are the very

1 reason that railroads are such a critical part
2 of the U.S. economy and our nation's financial
3 recovery.

4 Due to the certainty governing our
5 industry today, railroads have been able to
6 invest \$480 billion since 1980 to build a
7 world-class network that reliably and safely
8 delivers for American businesses.

9 That investment, which must
10 continue unabated in the face of demands for
11 more capacity, improved service, and attendant
12 environmental job creation and other public
13 benefits, has been made possible by the
14 Board's implementation of ICTA consistent with
15 congressional directives. Reexamination with
16 the overhanging threat of possible reversal of
17 those policies introduces uncertainty into the
18 marketplace.

19 To conclude, the Board has
20 properly utilized the exemption authority
21 granted by Congress to exempt traffic from
22 regulation. These actions have contributed to

1 the ongoing rail renaissance, and there is
2 nothing in the law, in congressional policy,
3 in the testimony in this proceeding which
4 would justify the Board taking any action to
5 reverse the proper course it has followed to
6 date.

7 Thank you for the opportunity to
8 be here, and I look forward to answering any
9 questions you may have.

10 DR. WILLIG: Thank you, Mr.
11 Chairman, Commissioners. Notice that the
12 light has stayed green this whole time. I'm
13 about to change that. Maybe I have some extra
14 time.

15 I do thank you very much for the
16 opportunity to share my views on the economic
17 rationale for the Board-granted exemptions and
18 the framework for evaluating whether to revoke
19 an exemption. I underscore the phrase
20 "economic rationale."

21 I am an economist. I'm used to
22 working with lawyers all the time, but I

1 prefer to stay on the economic side of that
2 boundary line, and I welcome discussion later
3 from the economic point of view.

4 So I'd like to start with some
5 basic economic principles. In the freight
6 railroad business, regulation of prices -- I
7 feel like we're -- is only needed when there
8 is an absence of effective competition, and
9 market forces are not able by themselves to
10 generate prices that are conducive to what
11 economists call economic efficiency.

12 Even stronger than that, though, I
13 think for today's purposes is the statement of
14 principle that where there is effective
15 competition, and we know there are such
16 widespread instances in the industry, it is
17 best by far not to regulate. It's not just
18 regulation ought to be there if we don't have
19 effective competition, but where we do have
20 effective competition, I think as a matter of
21 economics that it's very important not to
22 regulate.

1 It's important, moreover, in such
2 circumstances to have as much of an
3 institutional commitment as we can to not
4 regulate, because where there is the
5 possibility of competition driving market
6 outcomes, the overhang of the possibility of
7 regulation I think is a real deterrent to
8 negotiations and market forces doing their
9 best for social efficiency for all the parties
10 involved.

11 I think only with that kind of
12 commitment not to regulate in the face of
13 effective competition, only then will market
14 decisions and negotiations work optimally to
15 create efficient outcomes. I believe that
16 exemptions can foster such good market
17 outcomes by providing some of that targeted
18 commitment through market forces.

19 From my point of view, when I
20 think about some of the issues at hand, some
21 of the costs of the hearings that may be
22 necessary to investigate the future of

1 examinations, obviously it's a costly process
2 for those involved, but I think there's real
3 economic costs involved in terms of weakening
4 the commitment to staying away from regulation
5 where most likely that regulation is not
6 needed to get competitive outcomes.

7 So, looking back, the STB's
8 regulation authority is therefore
9 appropriately focused, and it has been
10 appropriately focused on specific markets
11 where there is demonstrable evidence of abuse
12 of market power or at least a high risk of
13 such conduct. Where there is no such
14 evidence, exemptions do help and have helped
15 competition work for the public interest, and
16 that is my view as an economist looking back
17 over the history.

18 The ICC and the STB have
19 appropriately exempted particular commodities
20 and services from regulation whenever the
21 evidence demonstrated that they were subject
22 to effective competition, whatever the source

1 of that competition, whether it was based on
2 intermodal forces, intramodal, product, or
3 geographic competition. The full range, as
4 you know, has come into the assessments of the
5 degree of effectiveness of competition for the
6 purposes of assessing exemptions.

7 Your decisions in this area and
8 your predecessors' for exempting boxcar
9 traffic, intermodal traffic, lumber or wood
10 products, rock salt, and so forth, a very long
11 list, were all based, as I read the record, on
12 very well documented empirical evidence of the
13 effectiveness of all of these types of
14 competition in the marketplace. I think it's
15 a really good record as I read it from an
16 economic point of view.

17 At the same time, as I understand
18 it, your exemption decisions expressly have
19 opened the possibility of revisiting to
20 address any evidence of any specific abuses of
21 market power that might be shown to exist, but
22 you have correctly, I believe, enforced the

1 requirement that any proponent of revocation
2 of an exemption must demonstrate through well
3 supported evidence that the market conditions
4 that originally supported the grant of the
5 exemption have been altered so significantly
6 that reregulation is now required.

7 These requirements, as I
8 understand it, are well supported, pointed
9 evidence about the traffic that is made to be
10 at issue, instead of some sort of general
11 claims of, "Well, the times have changed.
12 That ought to be enough," or platitudes, if I
13 may, about exemptions "having served their
14 purposes" due to some higher view of railroad
15 profitability, instead of those general
16 platitudes -- it's not that insulting a word,
17 is it? -- but in contrast to really well
18 pointed empirical evidence going to the
19 important subject at hand.

20 Well, with those generalities
21 expressed, I want to emphasize, apart from
22 platitudes, that rising prices or improved

1 railroad profitability generally are
2 absolutely not appropriate justifications for
3 revoking exemptions. Instead, these dynamics,
4 prices going up, prices coming down, finances
5 of the railroads doing better, sometimes doing
6 worse, are ordinary and frequent outcomes of
7 competitive markets.

8 These are not signs, either upward
9 or downward, of market power necessarily,
10 because in competitive industries we see
11 finances oscillating back and forth. We see
12 prices going up and down, driven by
13 competitive market forces.

14 So, if I may -- oh, there it is.
15 Well done. Figure 1, this is in my written
16 testimony, and anybody who like me is a little
17 bit color blind, you cannot tell these line
18 graphs from each other, so I'm here to tell
19 you what my PowerPoint reveals if you have the
20 live computer.

21 So take a look from the right-hand
22 side of the picture, and I'm going to be going

1 down the list from high to low of these
2 different line graphs. So the very top one on
3 the right-hand side is a broken dark line.
4 That's a trace of the volume of rail traffic
5 as collated by the AAR.

6 The next one, which looks red even
7 to me, is the AAR's measure of rail
8 productivity. The third one is total
9 revenues, again AAR data. The fourth one down
10 is the AAR view of a broad price index of rail
11 freight traffic.

12 The next one down is revenue-per-
13 ton-mile, so a price surrogate as collected by
14 Christiansen and Associates, a word about that
15 in a moment. The last line is the marginal
16 cost of rail traffic averaged over the
17 commodities and the volumes in question, again
18 produced by Christiansen and Associates.

19 This is the Christiansen study of
20 competition that I believe was requested,
21 supported by the Board, and has been updated
22 a few times and which I feel is an absolutely

1 excellent study. Christiansen is a terrific
2 economist, and he's used real state-of-the-art
3 methods here, as well as pertinent data, in my
4 view.

5 So let's take a look at this and
6 see what it says about the dynamics of the
7 industry. A good anchor is 1980, which is the
8 passage of the Staggers Act, of course.

9 All these lines come together in
10 1986 or 1987. There is no significance to
11 that. That's just the base for these indexes,
12 so they're all -- all the indexes are 100 in
13 that year by construction.

14 What's remarkable, though, is that
15 if you start at 1980, look above 1980, all
16 kinds of good things start to happen right
17 after the passage of the Staggers Act.
18 Productivity, that red line, really jumps.
19 It's been flat all those years. It really
20 takes off right after the Staggers Act.

21 The pricing lines, they've been
22 flat. Right after 1980 they all start going

1 down in strong ways. Marginal costs start to
2 come down. All kinds of good competitive
3 dynamics begin when real deregulation or the
4 opportunity for deregulation under the
5 Staggers Act sets into the industry.

6 It's a remarkable sea change, and,
7 in fact, the textbooks on regulation all have
8 charts that look something like this and say,
9 "Oh, my goodness. Look what the Staggers Act
10 did empirically."

11 The next sea change begins around
12 2004, when new dynamics set in. Rates begin
13 to increase. Productivity starts to turn
14 down, and marginal costs begin to rise right
15 after 2003-2004, a very different dynamic
16 probably picked off by the huge increases in
17 fuel prices that begin right around those
18 years, and right around those years marginal
19 costs begin to go up, and rates go up right
20 along with the marginal costs, as one would
21 expect under competitive circumstances.

22 Yes, see, I talk loud, right? Is

1 that the problem? Big classrooms.

2 So this dynamic, prices being
3 driven by marginal costs, marginal costs being
4 driven by both productivity and the exhaustion
5 of the easy productivity gains attendant to
6 deregulation and the drivers of wildly
7 increasing fuel costs, are all things that are
8 characteristic of competitive markets and
9 competitive pricing dynamics and in no way
10 support a view of abuse of market power or
11 some generalized weakening of competition in
12 the industry.

13 Another point to help to make that
14 is, unfortunately, in 2008 or so, way over on
15 the right-hand side, the big recession begins
16 to have effect, and there is a fast decrease
17 in volume. Rates begin to soften, because the
18 demand is really soft due to the decline in
19 the economy.

20 Meanwhile, there is still capacity
21 congestion in this marketplace, and that's
22 part of the reason why rates begin to increase

1 in the middle of the decade as real congestion
2 in the railroad network, real bottlenecks that
3 raise congestion costs.

4 And even though the recession
5 really takes a lot out of the growth of
6 volume, it doesn't entirely stop that capacity
7 congestion. So we see rates softening and
8 coming down, but not nearly as much as they
9 would if the capacity congestion problems were
10 fully solved.

11 Well, hopefully that's going to
12 happen. The railroads have been investing.
13 The number I have is some \$74 billion over the
14 first decade of this millennium, despite the
15 turndown of finances during the recession
16 years, and the railroads are making, I
17 understand, significant strides to address the
18 capacity constraints that we see in these
19 data.

20 This very significant reinvestment
21 in the private freight rail network is
22 inconsistent, if you think about it, with any

1 suggestion which seems to come up in these
2 conversations, the suggestion that the
3 industry might be exercising market power
4 artificially to restrain capacity and thereby
5 drive up rates. That's just not consistent
6 with these data.

7 The opposite appears to be true.
8 Volume continues to go up. That's not the
9 hallmark of market power at all, and the
10 industry seems to be investing hand over fist
11 as the investors will provide the funds, which
12 is certainly not characteristic of some sort
13 of a conspiracy or a collection of collateral
14 approaches -- I told you -- to try to keep
15 things congested and thereby more profitable.

16 So, improving profitability is
17 clearly not a sound indication of any need for
18 revocations. My economic bottom line on this,
19 and I can't state this strongly enough, no
20 matter how well or badly any railroad is
21 faring financially overall, competitive
22 services should be free of price regulation.

1 It's not about the overall
2 finances. It's about market-by-market. Is
3 there sufficient competition to feel like
4 pricing will be driven by efficiency? And
5 that's a market-by-market determination. It
6 does not have anything to do with the overall
7 finances of the railroad.

8 Likewise, regulation should be
9 considered for services that are truly market
10 dominant and subject to abuse of market power,
11 irrespective of the overall finances of the
12 railroad. This is a neutral principle. It
13 really goes in both directions. So that
14 leaves the question on the table.

15 MR. HAMBERGER: May I save my time
16 to --

17 DR. WILLIG: Thank you very much.

18 CHAIRMAN ELLIOTT: That's fine.

19 DR. WILLIG: So the question
20 remains. How should the propriety of
21 maintaining exemptions be gauged? It's not
22 overall finances of the railroad.

1 So I have an economic answer.
2 It's written out at some length in my file
3 testimony, but let me just state it here in a
4 condensed form.

5 It is if a convincing showing can
6 be made based on facts in evidence, not
7 rhetoric, that a particular movement is no
8 longer subject to the forces of effective
9 competition, resulting in abuse of market
10 power, then the Board, if presented with an
11 appropriate petition, may have grounds to
12 investigate whether reregulation is necessary
13 and appropriate to protect the public
14 interest.

15 And in such an investigation the
16 Board should, if you'll allow me to give you
17 advice, the Board should take care to focus as
18 narrowly as possible to address the concerns
19 identified and not to sweep them more broadly
20 than necessary, because, again, there are real
21 economic costs to threatening regulation
22 rather than committing to not regulating where

1 there is effective competition.

2 In other words, any revocation of
3 an exemption should be carefully limited to
4 the particular movements or circumstances as
5 to which an abuse of market power has been
6 shown by rigorous evidence to exist.

7 So I thank you for your patience.
8 Thank you for allowing me to share my thoughts
9 and concerns. I do think this is an important
10 matter, and again I urge you to proceed with
11 caution and care.

12 The downside is sending the wrong
13 signals to the marketplace, which could
14 actually threaten the availability of
15 investment funds to help keep up the capacity
16 that we need to handle traffic growth.

17 My admonition is like the
18 physician's "Do no harm," but please, as an
19 economist would say it, do not eliminate
20 exemptions that well serve the public interest
21 in competition. I thank you very much.

22 CHAIRMAN ELLIOTT: Thank you,

1 Professor. Thank you, panel, for your
2 participation. I just had a couple questions.
3 First of all, I just want to clarify on your
4 chart, Mr. Hamberger.

5 MR. HAMBERGER: Yes, sir.

6 CHAIRMAN ELLIOTT: On the second
7 part it says, "All non-boxcar commodity." Does
8 that -- does this chart include intermodal?

9 MR. HAMBERGER: It does not.

10 CHAIRMAN ELLIOTT: It does not?

11 MR. HAMBERGER: We did not --

12 CHAIRMAN ELLIOTT: So the
13 intermodal is --

14 MR. HAMBERGER: We did not put
15 intermodal here. The testimony from --

16 CHAIRMAN ELLIOTT: Okay.

17 MR. HAMBERGER: -- others
18 indicated that that was not particularly an
19 issue of contention. We do have that
20 analysis. I believe currently intermodal is
21 about 132 percent of R/VC.

22 CHAIRMAN ELLIOTT: Okay, I just

1 wanted to clarify so I understood the chart.
2 With respect to the overall numbers, the
3 amount of traffic, you know, and R/VC ratios,
4 I was -- I mean, those numbers appear.

5 Obviously, they're all under 180,
6 and I've seen -- now, in that instance, those
7 are good numbers, and then what about in
8 specific instances where a specific commodity
9 has numbers that are over 180?

10 We've -- I've had our economist do
11 some waybill analysis, and in one instance we
12 have -- of course, I'm taking the most
13 extreme, crushed limestone, which is a serious
14 commodity. You carry quite a bit of it -- is
15 at what we had for 2009 at 272.

16 In an instance like that, would
17 you think that is a good indicator of market
18 dominance that the railroads are exercising
19 their market power?

20 MR. HAMBERGER: Let me start, and
21 then I'll turn it over to the economist. Of
22 course, for you to consider it I would suggest

1 that there needs to be a filing of a petition
2 for revocation, number one.

3 Number two, as Professor Willig
4 stated, the RV/C is one indicia of whether or
5 not there is competition, whether or not there
6 is abuse of market power, but let me let him
7 to into that in more detail.

8 DR. WILLIG: Thank you. Economics
9 has a pretty well defined conclusion on using
10 revenue-to-variable cost or revenue-to-
11 marginal cost ratios as possible indicators of
12 market power.

13 I'm sure you're well aware of
14 this, but, of course, where there are
15 important fixed costs, some cost to the
16 infrastructure, and these are extraordinarily
17 high in railroad and across all industries,
18 somebody's rates are going to have to be well
19 above variable and marginal costs to even
20 begin to attempt full cost recovery on a going
21 forward, long-term basis.

22 So finding that some traffic has

1 rather larger than average ratios of revenue
2 to variable costs should not be upsetting at
3 all or in any way viewed as an indicator of
4 the kind of market power or monopoly power
5 that we look to regulation to control.

6 CHAIRMAN ELLIOTT: Okay, and
7 you're saying it could be an example of how we
8 regulate here with differential pricing?

9 DR. WILLIG: Yes, that obviously
10 is differential pricing.

11 CHAIRMAN ELLIOTT: Right.

12 DR. WILLIG: But I don't look at
13 that, an example of that kind, as necessarily
14 pointing to abuse or exercising --

15 CHAIRMAN ELLIOTT: Right, and then
16 we had other examples. We had them take a
17 look at how traffic, the amount of traffic
18 traveling, exempt traffic, by commodity
19 traveling at over 180 RV/C ratio has increased
20 from '93 to the present. 2008 was the last
21 number.

22 I'll give you another example,

1 which isn't the most extreme, but looking at
2 stone and glass products it went from 14
3 percent traveling over 180 to 41 percent. It
4 went from 14 to 17 in '98, to 30 percent in
5 2003, to 41 percent in 2008, and this is once
6 again off the waybill analysis. What about
7 that as an indicator? Same type of question.

8 DR. WILLIG: Well, I would repeat
9 the same answer but then fill it out a little
10 bit more, because in that time period,
11 particularly as we get to the middle of the
12 2000s and out to 2008, first of all, fuel
13 costs are rising very fast, and this is a
14 matter of the arithmetic for the way the
15 variable costs are calculated.

16 They're kind of slow to reflect
17 big upward movements in fuel costs, so some of
18 that changing ratio could be the impact of
19 very fast rising input costs not being fully
20 reflected in the VC data. Likewise,
21 congestion would -- has been a big factor
22 since the last eight years or so in railroad

1 operations, and, of course, the railroad
2 people can speak about that later on today.

3 Congestion is an important
4 determinant in the market for business but
5 also for economics that goes into appropriate
6 competitive rate-making that you've got a
7 scarcity of the rail resources, which could be
8 the track. It could be the cars. It's proper
9 to see prices rising under those
10 circumstances.

11 The way we figure variable costs -
12 - we all do it in this industry -- those costs
13 don't really reflect congestion the way the
14 economist's view of marginal costs do.
15 Marginal costs include congestion. It's hard
16 to measure that, but conceptually marginal
17 costs rise a lot when scarce resources become
18 more scarce and there's more congestion.

19 The VC formula does not reflect
20 that, so we might very well be seeing a large
21 revenue-to-variable cost ratios without there
22 being an enlargement of the true ratio of

1 revenue-to-marginal cost under conditions of
2 fast-rising fuel costs and also under
3 conditions of congestion. I'd be just
4 cautious in reading those tea leaves.

5 CHAIRMAN ELLIOTT: Thank you. One
6 follow-up on Mr. Hamberger's comment. With
7 respect to having to file a petition in order
8 to initiate consideration of revoking an
9 exemption, I think that's a very strong
10 argument, but at the same time I also look at
11 our cases where we reconsider decisions that
12 have been made by the Board and as a result of
13 changing circumstances or new evidence maybe
14 material error that we do reconsider past
15 decisions. Do you think that would be
16 applicable in this instance?

17 MR. HAMBERGER: No.

18 CHAIRMAN ELLIOTT: I'm surprised
19 you said that.

20 DR. WILLIG: At last, a short
21 answer.

22 MR. HAMBERGER: In general, I

1 would say -- not in general. Specifically,
2 the statute directs you to pursue granting
3 exemptions. That is what you are statutorily
4 directed to do, and it lays out a process
5 where the burden of proof is on those seeking
6 the repeal. There has to be a finding that it
7 is necessary for the transportation policy, so
8 I would stand by my statement that it requires
9 a petition to be filed.

10 CHAIRMAN ELLIOTT: Thank you. I
11 don't have any further questions. Mr. Mulvey?

12 COMMISSIONER MULVEY: Thank you.
13 Like you, I share the burden of working with
14 lawyers.

15 (Laughter.)

16 COMMISSIONER MULVEY: A couple of
17 things. Again, with this revocation of
18 exemptions, you pointed out that we've only
19 had a couple of examples where people have
20 come forth and asked for revocation of an
21 exemption, and we didn't grant it.

22 One case I'm familiar with was

1 with cottonseed oil in Texas where it was
2 charged that the particular shipper was not
3 receiving good service from a particular
4 railroad, a short line railroad. The Board
5 revoked the exemption, because cottonseed oil
6 is exempted, and then addressed the problem,
7 I think successfully.

8 But the shippers often claim that
9 it's not that they can't do it. It's that
10 it's expensive, it's burdensome, and they
11 would do it more often if they felt that the
12 procedures were simplified.

13 Do you think there is any merit to
14 that argument that the reason they don't ask
15 for more revocations of exemptions is that
16 they're unsure of the Board's process and that
17 there's an uncertainty involved? Ed, do you
18 want to address that?

19 MR. HAMBERGER: Well, there is, of
20 course, uncertainty in any legal proceeding,
21 so, you know, if what one is looking for
22 before one brings a case is an automatic

1 guarantee that one is going to win, I would
2 suggest that will never happen.

3 As far as the cost, that is
4 something that is generally between you and
5 OMB as to how you are able to set your filing
6 fees, et cetera, and we certainly have never
7 supported high filing fees. I've always
8 testified in favor of having the Board
9 processes open to the maximum extent possible.

10 COMMISSIONER MULVEY: And the
11 Board is making an attempt at doing that. We
12 have lowered our filing fees for many things,
13 and we are trying to streamline our processes,
14 so perhaps that might lead to more petitions
15 for revocation.

16 MR. HAMBERGER: Streamlined
17 processes help not only plaintiffs but
18 defendants.

19 COMMISSIONER MULVEY: One of the
20 issues that one of your charts for both boxcar
21 traffic and the other is that that's the
22 average for all the traffic in that group,

1 but, in fact, there is always a distribution
2 in any average, and, as the Chairman
3 mentioned, there are some cases that are
4 outlier, or far from average.

5 We have just some examples of some
6 commodities, some types of traffic where the
7 revenue-to-variable-cost ratio was far, far,
8 far above 180 percent and, more importantly,
9 has been climbing steadily in the last few
10 years.

11 Do you have any sense of whether
12 there are any commodities out there that are
13 currently exempt that you feel have a more or
14 better case to call for a general revocation
15 of exemption, or should it always be on a
16 case-by-case basis, and should it always be
17 for a specific movement and that there
18 shouldn't be any wholesale commodity
19 revocation? Mr. Willig could also address
20 that. You both could address that.

21 MR. HAMBERGER: To the extent that
22 a revocation submission can meet the burden of

1 showing that there is a lack of competition,
2 that there is an abuse of market power, and
3 that reregulation is necessary, if that is for
4 a commodity-wide basis or a specific movement,
5 that is up to the petitioner to decide how to
6 file.

7 What I was trying to get across in
8 these two charts is that, generally speaking,
9 there does not appear to be that kind of
10 rigorous support for commodity exemptions to
11 be revoked, but the Board has a process in
12 place to allow those who feel that their facts
13 can support such a filing to come forth and
14 make the filing.

15 COMMISSIONER MULVEY: The mean can
16 always hide a lot of outliers.

17 MR. HAMBERGER: And I will not
18 concede that there is any abuse, but
19 theoretically speaking it is possible that
20 there is an outlier there and suggest again
21 that the Board has in place a process for that
22 theoretical outlier to come forth.

1 COMMISSIONER MULVEY: Professor
2 Willig, I know that you are a strong believer
3 in the existence of competition. I spent
4 quite a bit of time in the airline business
5 looking at the issue of contestable markets,
6 and I know your views on that, but are there
7 some cases where there seems to be some bands
8 of traffic that are more or less competitive
9 with other modes?

10 For example, relatively short-haul
11 moves by the short lines. Most of the short-
12 haul traffic tends to be truck competitive,
13 and, of course, if you're near waterways, then
14 you have water competition from barges.

15 Isn't it true that for most long-
16 distance traffic, regardless of commodity
17 types, but for real long distances rail is
18 really the only option today? There have been
19 important changes in trucking markets. You've
20 got a shortage of drivers. The price of fuel
21 has risen for trucks on a relative basis and
22 relative importance of those, of course, much

1 more for trucking than for rail?

2 So have there been enough changes
3 in competitive marketplaces, especially for
4 long-distance markets, that there might be
5 some places now where we really should review
6 the overall exemption process, Mr. Willig?

7 DR. WILLIG: Well, just in terms
8 of the process of today, the railroad
9 marketing officials will be speaking, I think,
10 certainly much accurately than I can to the
11 facts involved in any particular area of
12 traffic that you'd like to ask about.

13 At the same time, I mean, I'm well
14 aware as an economist, and I know you are,
15 too, that the length of the haul matters a lot
16 in terms of the balance of cost between
17 trucking and rail, but I'm also aware that
18 when it comes to very long haul that mixtures
19 of rail and truck are very empirically
20 important and I think in general attractive to
21 the shippers.

22 And if there is going to be a

1 trucking portion of a long haul total movement
2 with rail in the middle someplace, that
3 fosters railroad-to-railroad competition for
4 providing the railroad part of the long-
5 distance haul.

6 So truck to one or two or three
7 different choices of railroads, trucks at the
8 other end, makes for a relatively more
9 competitive long haul to kind of fill in the
10 gaps that you were alluding to.

11 MR. HAMBERGER: And, I guess, I
12 would just add for the record if I could that
13 Joanne Casey will be testifying later on
14 behalf of the Intermodal Association of North
15 America. JB Hunt and the HUB Group have also
16 filed written testimony as large intermodal
17 users, and they are very much in support of
18 maintaining the current exemption.

19 COMMISSIONER MULVEY: Mr. Willig,
20 Professor Willig, you also mentioned the
21 Christiansen study that the Board commissioned
22 a while back and that it was good work. I

1 wonder if you're aware that one of the
2 principal authors of that study has recently
3 completed a paper that shows that the railroad
4 productivity gains, which in the early years
5 were passed on to shippers --

6 Virtually 100 percent were passed
7 on to shippers in terms of lower rates, but
8 today, over the last four or five years, the
9 railroads have actually kept the benefits of
10 the productivity changes instead of passing
11 them on to shippers. Would that be a
12 suggestion that there has been a shift in
13 terms of the railroad's ability to exercise
14 market power?

15 DR. WILLIG: I actually haven't
16 studied the paper that you're alluding to, and
17 you're now interesting me a lot in doing it.

18 COMMISSIONER MULVEY: We'll make
19 sure you get a copy of that paper. I think
20 it's a very interesting one.

21 DR. WILLIG: If that's what it
22 shows, but without commenting specifically in

1 that paper about the impact of competition, I
2 wouldn't jump to that conclusion just from the
3 fact that you alluded to that productivity
4 gains have continued.

5 Of course, they've dropped off the
6 last two years when there are other things
7 going on in the market like extraordinary
8 increases in fuel costs, so that would get in
9 the way of what would ordinarily earlier have
10 been that same relationship.

11 COMMISSIONER MULVEY: That's all
12 for the time being.

13 CHAIRMAN ELLIOTT: Thank you.
14 Thank you, Commissioner. Vice Chairman?

15 VICE CHAIRMAN NOTTINGHAM: Thank
16 you, Chairman Elliott. General Timmons, if I
17 could, did I hear correctly you mention that
18 currently there are about 556 short-line
19 railroads? Was that the number?

20 MR. TIMMONS: Yes, that's correct.

21 VICE CHAIRMAN NOTTINGHAM: And do
22 you happen to know, if we were to flash back

1 to 1976 when the 4R Act first raised this
2 whole exemption issue and put it very solidly
3 into statute, what the short-line industry
4 looked like back in '76?

5 MR. TIMMONS: In general numbers
6 about 250, 260, somewhere in that realm.

7 VICE CHAIRMAN NOTTINGHAM: Do you
8 think there's any connection between or is it
9 just a coincidence that the 4R Act and
10 Staggers were passed in '76, '80, and your
11 association membership has been able to grow
12 thanks to practically a doubling of the number
13 of short-lines operating?

14 MR. TIMMONS: I don't think
15 there's any question about it. I don't think
16 there was any conscious intent or awareness
17 that the short-line industry would expand as
18 rapidly as it did post-1980.

19 The interesting developments that
20 that Staggers Act produced was a growth of
21 short-line mileage at about that time of about
22 8,000 miles of short-line main line track, and

1 today it's slightly under 50,000 miles.

2 Now, as you know, there were a
3 large number of Class I railroads in 1980, and
4 they had reduced dramatically by 1990, and in
5 the decade of the eighties Class I railroads
6 divested themselves of many, many properties
7 that were less than economically feasible for
8 their purposes.

9 Small railroad entrepreneurs and
10 others gathered those pieces up, even though
11 they were a little broken down and
12 dilapidated, decided that they could with flat
13 overhead, smaller staffs, and local customer
14 interface thought that they could build them,
15 and they did, and that evolution has continued
16 to this day. Obviously, it's slowed down
17 pretty dramatically, but there is no question
18 that Staggers had a dramatic impact on the
19 small railroad industry.

20 VICE CHAIRMAN NOTTINGHAM: Thank
21 you. Professor Willig, if I could, thanks for
22 sharing and reviewing the charts. Some were

1 quite familiar, and we appreciate the
2 reference to the Christenson study, too, which
3 about a million dollars of taxpayer money went
4 into that study through the Board.

5 It's probably the, I would
6 suggest, the most important study that the
7 Board has commissioned in many decades, and I
8 do commend everyone's attention to it. I
9 think it's still very timely and relevant,
10 even though it's just a few years old now.

11 In the science of economics, how
12 do you account for, I guess I'll say -- I'll
13 just use the phrase sort of the people who
14 aren't winners? You're not here to suggest
15 that every single customer of railroads came
16 out a winner across the country as a result of
17 the deregulatory policies of the seventies and
18 eighties, are you?

19 I mean, we do hear, of course,
20 from people who say with all seriousness that
21 their situation has worsened. How do you --
22 how does the sort of science of economics kind

1 of account for that or explain that?

2 DR. WILLIG: Well, we're always
3 happy to find a situation where everybody is
4 happy, but it's a very rare occurrence in
5 today's world. The normative stance that
6 applied economists, micro-economists
7 frequently adopt takes a look at the size of
8 the pie and tries very hard to support, to
9 understand what the best policies are from the
10 point of view of the total real income
11 generated by, say, a sector of the economy
12 like the freight transportation sector.

13 The whole idea of differential
14 pricing, which goes back again to Staggers and
15 to the regulatory rule-makings following
16 Staggers, deliberately adopted the point of
17 view, I'm not sure in these words, but the
18 economists know the connection, pricing that
19 would enlarge the size of the pie of real
20 income created by a better performing railroad
21 industry than had been performing prior to the
22 Staggers Act.

1 Surely, some of those rate changes
2 were up. Some were down. On average, they
3 were way down. That's not to say that some
4 people's rates didn't go up.

5 The real interesting question,
6 though, is what's the backdrop? What are we
7 comparing what actually happened to, and if
8 the backdrop is more bankruptcies and more
9 dysfunctionality in the entire industry, lack
10 of capitalization, lack of service of the
11 quality that all the shippers need for their
12 own businesses, then it could very well be the
13 case that everybody was benefitted against the
14 backdrop of no well functioning railroad
15 industry at all.

16 We always talk that way, but here
17 we really have empirical evidence that pre-4R
18 and before Staggers the industry was basically
19 bankrupt, and so it's not wrong to say that
20 all shippers who find railroad freight
21 opportunities important to their business have
22 been benefitted by the entire movement toward

1 rationalization and deregulation.

2 VICE CHAIRMAN NOTTINGHAM: If I
3 could take a step back and maybe ask a big
4 picture question, in your line of work I
5 assume you get to hang out, for lack of a
6 better phrase, with academics and experts in
7 a variety of fields of regulated industries
8 and the economics of a variety of regulated
9 industries. I'm thinking of the financial
10 sector, energy sector, other sectors.

11 DR. WILLIG: We do hang out, yes.
12 It's academic conferences. We work hard, but
13 we also --

14 VICE CHAIRMAN NOTTINGHAM: I'm
15 curious. What's the -- you know, if you look
16 back at what's happened in our economy the
17 last ten years, some of the explosive scandals
18 in the electric utility industry with Enrons
19 of the world and more recently in the
20 financial services sector, we've seen a lot of
21 finger pointing about whether or not a variety
22 of federal and state regulatory entities fell

1 down on the job or didn't fall down on the
2 job.

3 What do you say to those
4 colleagues when you turn and look at the state
5 of the freight rail industry and how it's been
6 regulated, kind of what the results of that
7 regulatory relationship and oversight have
8 been?

9 DR. WILLIG: I'm so glad you asked
10 that question, Commissioner. I just filed
11 some testimony this week in a matter of
12 financial regulation under Dodd-Frank, and I
13 must have spent a page and three footnotes
14 saying, "And, for goodness' sakes, try to get
15 it right, the way the ICC and the STB have in
16 railroading."

17 All the bad things that went on,
18 all the pitfalls that we've learned to avoid
19 since Staggers and since the 4R Act in this
20 industry are real threats when it comes to
21 other regulatory bodies without the experience
22 and, I dare say, the skill that has been

1 developed in this industry.

2 And I actually wrote, "Don't make
3 the mistakes today that the rail industry has
4 learned to avoid in the last 20, 30 years."
5 Maybe your ears were turning red with
6 embarrassment at the praise, but I just filed
7 that the other day.

8 VICE CHAIRMAN NOTTINGHAM: I
9 wasn't aware of it, but --

10 DR. WILLIG: Yes, I'll send you a
11 copy.

12 VICE CHAIRMAN NOTTINGHAM: Please
13 do. Thank you. Mr. Hamberger, what do you
14 say to your members' customers who sincerely
15 feel that they were not the winners as an
16 outgrowth of the 4R Act, Staggers, and the
17 trend towards deregulation of the rail
18 industry?

19 Professor Willig has confirmed
20 that there are people who don't come out
21 winners in these circumstances. What should
22 they do? What options do they have, and what

1 can --

2 MR. HAMBERGER: Well, I have tried
3 to make the same point that the professor
4 made, obviously not as eloquently as he did
5 here this morning, but the point being that a
6 remember system that is 20 percent in
7 bankruptcy with 25 percent of its track on
8 slow orders, which takes too long to get
9 across the country, cannot provide the service
10 needed for this economy.

11 The President has said he wants to
12 double exports. We take a third of all
13 exports to port. Without the freight rail
14 industry, we're not going to double exports.

15 We're not going to get the
16 increased employment that the President is
17 looking for out of doubling those exports, and
18 that comes because we were able to pour \$480
19 billion back into the network in the last 30
20 years.

21 So that, in my opinion, benefits
22 anybody who ships by rail. Whether or not a

1 particular R/VC ratio for a particular
2 shipment may have gone up or down, I think the
3 professor's point that the pie has grown for
4 everybody is the appropriate way to look at
5 it.

6 VICE CHAIRMAN NOTTINGHAM: And
7 your members, when they're operating under an
8 exemption, presumably, obviously, they're not
9 dealing with tariffs. They're dealing in the
10 world of contracts, I assume, or various
11 pricing agreements, service agreements with
12 their customers?

13 MR. HAMBERGER: I'll leave that
14 for the rail panel.

15 VICE CHAIRMAN NOTTINGHAM: Okay,
16 because I do want to explore what the real
17 world options are for rail customers in the
18 exempt commodity area if they have a problem.
19 I do also want to throw out, and I confirmed
20 this with our people here, that just because
21 one works in an exempt commodity field does
22 not preclude a shipper from coming to this

1 Board for informal relief through our Rail
2 Consumer Assistance Program.

3 So I do want to commend -- I'll
4 probably be repeating this a couple times
5 today, because it will be a long day, and I
6 want to make sure folks who are coming in
7 later for later panels hear it, too.

8 If you are in the exempt commodity
9 field and you have a problem with the way
10 you're being treated by a freight railroad,
11 let the Board know about it. We're working
12 with the freight railroads every day. We have
13 a variety of relationships and a variety of
14 ways to get the railroad's attention.

15 It's not all bound in statute, and
16 sometimes it's informal, and it's a successful
17 program, the Rail Consumer Program. We
18 resolve thousands of complaints a year, and I
19 did want to commend everyone's attention to
20 that, as well. Thank you. That's all I have.

21 CHAIRMAN ELLIOTT: Just one quick
22 follow-up question. With respect to the

1 standard for revocation, it's consistently
2 been termed by you to show an abuse of market
3 power as the standard.

4 As I read the statute, which
5 someone put in front of me, the statute seems
6 to be broader, and I just wanted to clarify
7 why you had chosen, I guess, that aspect of
8 the Rail Transportation Policy.

9 But the statute requires
10 regulation where it's necessary to carry out
11 the transportation policy of Section 10101 of
12 this title, and is there a reason why you
13 specifically were referring to abuse of market
14 power?

15 MR. HAMBERGER: Yes. If you'll
16 take a look at the legal appendix to my
17 statement, that comes from prior ICC and STB
18 decisions. That has become the accepted
19 standard.

20 CHAIRMAN ELLIOTT: All right,
21 thank you, and one final question that I had,
22 this is just a concern I had about the whole

1 process in place at the present time.

2 Hypothetically, if you have an
3 exempt commodity and they want to come to us,
4 they have a complaint, and as a result they
5 have to seek revocation. They can't go to the
6 state courts or go to the federal courts,
7 because we still have jurisdiction over it.

8 What would happen in an instance
9 if there was a service problem under a
10 contract, and the party wanted to seek
11 revocation to come to us to deal with that?
12 However, the revocation process, as I
13 understand it, doesn't let you look backward
14 at all.

15 Do you think there is a void there
16 for a remedy for parties that have a complaint
17 about service or other issues not regarding
18 money? I know with respect to money you come
19 to us, and you have to go prospectively, but
20 doesn't that open itself up for abuse on other
21 issues like service matters and things of that
22 nature? Do you think there's a void there

1 from your understanding of the way the process
2 works?

3 MR. HAMBERGER: I would prefer, I
4 think, to respond to that in writing.

5 CHAIRMAN ELLIOTT: Sure. That's
6 fair. I don't have anything further. Do you?

7 COMMISSIONER MULVEY: A couple of
8 minor questions. Mr. Timmons, welcome back.

9 MR. TIMMONS: Thank you.

10 COMMISSIONER MULVEY: You talked
11 about the importance of not getting rid of the
12 exemptions, and isn't it also true that -- you
13 talked about the problems of determining
14 market dominance.

15 Isn't the 180 percent revenue
16 variable cost ratio the deciding factor?
17 Doesn't that give you protection? When you
18 have relatively few people complaining about
19 short-line movements because most of those
20 would move well below the 180 percent
21 threshold, and so therefore that serves as an
22 effective screen against too many suits being

1 filed especially against short-line railroads?

2 MR. TIMMONS: Let me just make a
3 general comment about that and then ask Mr.
4 Sidman to comment further, but it seems to me
5 that in the experience that we've had, the 180
6 percent threshold for short lines may not be
7 as pertinent as it is for Class I railroads.

8 The very, very short moves that
9 they make and a variety of conditions that
10 they experience and, to be sure, while we do
11 many of the same things the Class I railroad
12 industry does, the small railroads are not
13 mirror images of Class I railroads.

14 There are vast differences in a
15 variety of things, whether it's operational
16 tempo or hours of service or revenue
17 generation or the settlement mechanisms that
18 are used between the Class Is and their
19 interchange partners, the short-line
20 railroads.

21 There are vast differences, and so
22 the 180 may not be an appropriate measure or

1 barrier to protect us in that sense. Mark, do
2 you have anything other?

3 MR. SIDMAN: Commissioner Mulvey,
4 I think I agree with your observation that
5 most short-line traffic would be below the 180
6 percent variable-cost ratio, revenue-to-
7 variable-cost ratio, but it's really important
8 to understand that with respect to abuse of
9 market power, short lines really are not
10 positioned to do that structurally.

11 That reflects a couple things,
12 first, that many short lines, perhaps the
13 majority of short lines created since 1980,
14 have ceded pricing authority to their Class I
15 sellers, so they're actually not a pricer in
16 terms of origin-to-destination moves. They
17 have no interaction whatsoever with the
18 customer, and they have a contractual
19 allowance to which they're entitled for every
20 car they handle.

21 As to those who do have pricing
22 authority, and there is a population of short

1 lines that do have that authority, there are
2 really two constraints on that. One is that
3 they are pricing only a very small portion of
4 the typical move.

5 So, you know, the rule of thumb
6 number we would normally use as a short line
7 typically is looking at 20 percent or less of
8 the total revenue, but in cases in which it is
9 a pricer of that portion, it has to negotiate
10 typically with the connecting carrier.

11 That's where the negotiation takes
12 place, and their leverage in those
13 negotiations is really quite limited. So, you
14 know, as a structural matter, short line --
15 and short lines are completely different from
16 the Class Is, I think, in this discussion.

17 Having said all of that, they
18 really do need the protection of the
19 exemptions, because the exemptions create a
20 buffer between them and rate cases. You know,
21 before the question was asked of whether maybe
22 there could be a streamlined exemption

1 process, and there was allusions made to the
2 small rate case, which made it more affordable
3 for shippers to bring rate cases.

4 It's true that it had that effect.
5 What didn't happen in the small rate case is
6 that there were no protections put into place
7 for small railroads that end up as collateral
8 damage in rate cases.

9 There is a pending case right now
10 where a shipper brought a rate case against
11 two Class I railroads who were named as
12 defendants. A small portion of that traffic
13 actually terminated on a whole bunch of small
14 railroads. What happened in that case was the
15 shipper got on the phone with each small
16 railroad and demanded rate concessions, or it
17 was going to be named as a defendant in the
18 case.

19 I advised two short lines in that.
20 One had annual car loads of that traffic of
21 less than 100, and the other had less than
22 ten, so, you know, the threat of being dragged

1 into a rate case for a small railroad,
2 certainly under those types of circumstances,
3 is just a complete disaster.

4 As General Timmons said earlier,
5 the median revenues for a short-line railroad
6 today are \$2.5 million per year. These are
7 not companies that can afford to participate
8 in rate cases in which they have no
9 significant traffic at stake or in revocation
10 of exemption proceedings, which might really
11 be important to them, but they just don't have
12 the resources.

13 You know, those resources today
14 are going to upgrading track to handle
15 286,000-pound cars, to bridge replacement, to
16 PTC obligations. You know, you have this
17 whole -- this whole laundry list of capital
18 investment that you're asking a \$2.5 million
19 a year company to do.

20 So, you know, as you go forward
21 with this, I would ask that you keep in mind,
22 especially in the rate -- in the small rate

1 case context, keep in mind that very often
2 short lines can end up being very badly abused
3 in those cases without much public benefit,
4 actually, for including them.

5 COMMISSIONER MULVEY: Thank you.

6 On the short lines, some of the testimony that
7 was in some of the pleadings that we have
8 received has suggested that the exemptions
9 have caused some of the Class Is to be
10 reluctant to interline with the short lines.

11 Do you care to comment on that,
12 the exemptions that the Class Is say, "Well,
13 we don't want that particular traffic, and so,
14 therefore, since it's exempted, it's not going
15 to be a problem for us to just refuse to
16 interline with the short lines for certain
17 traffic types"?

18 MR. TIMMONS: My only observation
19 on that would be that would be that that issue
20 of deciding not to take some kind of traffic
21 is clearly -- has clearly existed, but whether
22 that can be tied to exemptions or not, I'm not

1 aware of it.

2 In other words, the rationale for
3 deciding not to take some kind of traffic or
4 work some kind of arrangement for moving goods
5 is generally in my experience not tied to an
6 exemption, per say.

7 COMMISSIONER MULVEY: We've heard
8 a lot today about the importance of
9 competition. As economists, we all have
10 paeans to the importance of competition in the
11 marketplace and getting efficient economic
12 solutions. So would you agree, Professor
13 Willig, that agreements that perhaps limit
14 competition would not be in the public
15 interest?

16 DR. WILLIG: That's a loaded
17 question. You'd have to get more specific, I
18 think. I mean, clearly --

19 COMMISSIONER MULVEY: I'm talking
20 about -- obviously, I'm getting off the
21 subject here, so I was talking about paper
22 barriers, which, of course, Mr. Hamburger and

1 Mr. Timmons --

2 MR. HAMBERGER: Interchange
3 commitments, if you will.

4 COMMISSIONER MULVEY: Interchange
5 agreements would limit the short line's
6 ability to interchange with a Class I when
7 it's spun off.

8 DR. WILLIG: No.

9 COMMISSIONER MULVEY: It was a
10 loaded question, so I'm not going to expect an
11 answer.

12 DR. WILLIG: As you know and I
13 know, in general often there are agreements
14 which somebody might characterize as limiting
15 competition which are actually an important
16 part of competition, where there are
17 commitments made to deal with one another,
18 which is mutually beneficial and allows more
19 efficiency and lower prices, but a concomitant
20 of that is not dealing so much with the next
21 guy who's complaining about it, so, yes.

22 COMMISSIONER MULVEY: Thank you

1 all very much.

2 CHAIRMAN ELLIOTT: Thank you very
3 much. We really appreciate your participation
4 today.

5 DR. WILLIG: Thank you for
6 listening.

7 CHAIRMAN ELLIOTT: Now we'll hear
8 from the third panel, the Shipper Interests.
9 You can please come forward. We will first
10 hear from the Alliance of Automobile
11 Manufacturers. Appearing on their behalf will
12 be Jeffrey Moreno. You have ten minutes.
13 Thank you.

14 MR. MORENO: Good morning. Thank
15 you. My name is Jeff Moreno, and I am here on
16 behalf of the Alliance of Automotive
17 Manufacturers.

18 The 12 members of the Alliance
19 constitute 77 percent of all car and light
20 truck sales in this country. The commodities
21 that are shipped are basically all fall within
22 STCC Class 37, which are almost all exempt

1 commodities.

2 I am sure the Board would prefer
3 to be hearing directly from those who are
4 affected by this particular exemption. My
5 presence here today is indicative of a general
6 or greater concern by Alliance members with
7 the potential for railroad retribution.

8 That concern is lessened by my
9 speaking here today on behalf of the Alliance
10 collectively. This concern is probably the
11 best example of at least a perception among
12 automotive producers of railroad market
13 competition for portions of their automotive
14 traffic.

15 I will do my best to answer any
16 questions that you may have this morning.
17 However, if I'm unable to do so, I would be
18 glad to take those questions back to the
19 Alliance and submit supplemental responses in
20 writing.

21 The STCC 37 automotive traffic has
22 been exempt since 1992. The history here is

1 a little important, because the exemption
2 procedure in that case was not initiated by
3 the railroad industry or any form of petition.
4 It was one of the proceedings that was
5 initiated, self-initiated by the ICC at the
6 time.

7 Most inbound parts even at that
8 time were already exempt traffic under the
9 intermodal or the boxcar exemptions.
10 Therefore, the ICC in its proposed -- in its
11 decision proposing to exempt automotive
12 traffic focused on what were long-haul,
13 predominantly rail movements that the time and
14 concluded that widespread geographic
15 competition constrained railroad market power
16 at that particular time.

17 There was almost no opposition at
18 all to that proposal by the ICC. It was
19 supported by both the railroads and the
20 automotive industries, and therefore there was
21 really no serious challenge posed to any of
22 the ICC's assumptions stated in the notice.

1 The auto industry in particular
2 was relatively unconcerned with the exemption
3 at that particular time in history, because
4 the railroads were, in fact, aggressively
5 competing for automotive traffic, and the
6 exemption purported to make this competition
7 even easier by removing such restrictions that
8 were in place at the time as tariff and
9 contract filing requirements.

10 Since 1992, railroad mergers have
11 increased the number of auto plants that are
12 captive to the same railroad. I believe there
13 were about 12 Class I railroads in '92, and
14 we're down to seven today, but what we really
15 have is large regional duopolies in the
16 eastern and western United States, which have
17 made it easier, effectively not to compete.

18 There are longer bottlenecks,
19 also, as a result of these mergers, which have
20 increased the distance to the nearest
21 alternative railroad to the extent there is an
22 opportunity to perhaps truck around these

1 bottlenecks.

2 Legislative changes only three
3 years after this exemption was enacted removed
4 most of the benefits for shippers, because
5 tariffs no longer had to be filed, and neither
6 did contracts, and that was the primary
7 benefit from the shipping perspective.

8 Furthermore, what we have seen,
9 particularly in the last decade, is that
10 railroad rate increases have rendered trucks
11 cost-competitive at even longer distances.
12 Back in `92, trucks were relatively
13 competitive up to about a 250-mile radius.

14 Today, trucks are actually
15 competitive up to about a 500-mile radius.
16 That, however, is not due to more efficient
17 truck competition, but it's due to railroads
18 increasing their rates up to the levels of
19 which trucks have been pricing.

20 During this time, both trucks and
21 railroads have, in fact, raised their rates,
22 but rail rates have increased at a much

1 greater pace, and truck rates have responded
2 to recent economic declines, whereas railroad
3 rates have continued to increase.

4 I am not here today to advocate a
5 blanket revocation of the STCC 37 exemption.
6 There are substantial intermodal competitive
7 options for large portions of the automotive
8 traffic. There are, however, significant
9 subsets of the STCC 37 that are, in fact,
10 captive to the rail industry.

11 Focusing first upon finished motor
12 vehicles, trucks dominate the short-haul
13 distance hauls directly to dealers, so today,
14 if a dealership is typically within 500 miles
15 of a production facility, it will typically
16 move by truck to that dealership.

17 Rail, however, dominates the long
18 hauls to what we call transload ramps, vehicle
19 distribution centers, different -- they're
20 called different names, but essentially these
21 are facilities where the cars are off-loaded
22 from the rail car -- where automobiles are

1 off-loaded from the rail cars, loaded onto
2 trucks, and then continue on to the ultimate
3 dealership, and rail dominates that
4 transportation.

5 Auto manufacturers cannot simply
6 cost-effectively transload around a rail
7 bottleneck except in very isolated instances
8 when moving their finished motor vehicles. It
9 does occur.

10 It occurs in very isolated lanes
11 when there is a service problem on that lane,
12 but there simply is not the truck capacity,
13 and, furthermore, there are significant
14 additional costs with adding that extra
15 transload layer. Therefore, it cannot be done
16 in large volumes to bring any competitive
17 pressure upon railroads.

18 A good example of that is what's
19 happening right now in the automotive
20 industry. Since the beginning of the year,
21 the car supply has been about 14 percent below
22 what is needed for loading cars.

1 Now, if it were simply an easy
2 task to truck around these rail bottlenecks,
3 most of this deficiency in rail car supply
4 would be addressed by shifting that traffic to
5 truck. It's not happened at local plants.
6 What happens is those cars end up having to go
7 to storage lots and waiting until rail cars
8 are available that can be loaded.

9 Auto manufacturers also cannot
10 easily or cost-effectively shift their
11 production from a plant served by one railroad
12 to a plant served by a different railroad,
13 even when that theoretically is an option, and
14 it's not an option as much as it was before
15 because of the consolidation of the rail
16 industry.

17 A second group of traffic is the
18 inbound shipment of auto parts. Now, this is
19 highly truck-competitive for 75 percent of
20 this volume, but there is a 25 percent segment
21 of inbound parts that's moved by rail because
22 it must move by rail.

1 These are what we call the
2 oversize or the heavy parts, anything such as
3 frames and axels, transmissions. The bulk of
4 that moves by rail, because truck is simply
5 not an efficient alternative option.

6 We believe the review of the auto
7 exemptions is appropriate to address traffic
8 that is not competitive and that the Board
9 should recognize that due to changes since
10 1992 that in both the rail and in the auto
11 industries that it should at least undertake
12 a review to evaluate whether the blanket
13 exemption on STCC 37 traffic is currently
14 appropriate or whether some subsets of that
15 traffic should actually still be subject to
16 regulation.

17 I would like to address one thing,
18 comment that has been in most of the railroad
19 comments and which was raised earlier today in
20 the AAR's testimony, and it was one that
21 surprised me, the statement that the statute
22 does not authorize Board-initiated

1 revocations.

2 I was baffled to hear that, and I
3 went back to read the statute to see if I had
4 been missing something, but the statute says
5 in 10502(b), "The Board may, where
6 appropriate, begin a proceeding under this
7 section," this section meaning 10502, "on its
8 own initiative or on application by the
9 Secretary or an interested party."

10 Well, by reference to 10502,
11 they're referring -- 10502 covers both grants
12 of exemptions and revocations of exemptions,
13 and the statute says the Board can do this on
14 its own initiative.

15 Now, perhaps my railroad
16 colleagues are focusing on the fact that this
17 appears in Subsection (b), which deals with
18 grants, as opposed to Subsection (d), which
19 deals with revocation, but in the statute
20 itself, when Congress intended to refer to a
21 subpart, it used the term "subpart." Here, it
22 used the term "section," referring to all of

1 10502.

2 With that, I see my time is coming
3 to a close, but I'll be glad to answer any
4 questions at the appropriate time.

5 CHAIRMAN ELLIOTT: Thank you, Mr.
6 Moreno. Next we'll hear from the American
7 Forest and Paper Association and the Paper and
8 Forest Industry Transportation Committee, Mr.
9 Lovick. You have ten minutes.

10 MR. LOVICK: Good morning,
11 Chairman Elliott, Vice Chairman Nottingham,
12 and Commissioner Mulvey. My name is Bill
13 Lovick. I am the Director of Transportation
14 at Temple-Inland for our building products
15 businesses.

16 In this role, I am responsible for
17 all inbound and outbound shipments of goods
18 and materials that are transported by rail and
19 highway to and from our building products
20 plants. I have worked in various roles over
21 the 16 years that I've been employed at
22 Temple-Inland.

1 Temple-Inland is a low-cost,
2 highly efficient manufacturing company focused
3 on corrugated packaging and building
4 materials. More than 117 years ago, our
5 company started with a single sawmill and has
6 grown to operate 82 facilities, which are
7 consistent of seven container board mills,
8 also known as paper mills, 59 converting
9 facilities or box plants, and 16 building
10 products plants.

11 Our company has approximately
12 11,000 employees and has annual revenue of
13 approximately \$4 billion. Our corporate
14 headquarters is located in Austin, Texas.

15 Our building products business
16 supplies solid wood lumber, gypsum wall board,
17 and fiber products for residential and
18 commercial construction projects. In
19 addition, we produce particle board and
20 medium-density fiber board, also known as MDF,
21 for manufacturing of furniture, flooring,
22 fixtures, cabinets, molding, mill work, and

1 various other uses.

2 Of all of our businesses, our
3 container board mills, the paper board mills,
4 are the most dependent on rail service. Of
5 our seven paper mill facilities, seven are
6 captive to a single shipper, single railroad.

7 Many of our paper mill customers
8 are also reliant on rail service, especially
9 those customers whose facilities are
10 constructed specifically to receive rail
11 delivery.

12 I'm appearing before you today on
13 behalf of the American Forest and Paper
14 Association, also known as the AF&PA, and the
15 Paper and Forest Industrial Transportation
16 Committee, also known as PFITC for short.
17 Accompanying me is Ms. Karen Booth. She's in
18 our audience, counsel for these organizations.

19 I appreciate the opportunity to
20 share the views of these organizations with
21 you on the important question of whether the
22 STB should undertake a more formal review of

1 the existing exemptions applicable to the
2 paper and forest products industry.

3 For the reasons explained in our
4 written comments and as expressed here today,
5 we believe that the time has come for this
6 Agency to reevaluate whether the exempting
7 rail transportation of paper and forest from
8 government oversight continues to make sense
9 based on the substantial changes that have
10 occurred in the rail industry since these
11 exemptions were adopted two decades ago.

12 The benefits of exempt status no
13 longer exist. Our written submission detailed
14 the various commodity exemptions and the
15 boxcar exemption that currently apply to most
16 paper and forest products, as well as the key
17 findings of the ICC that led to the granting
18 of these exemptions.

19 I will not repeat that information
20 here but would simply note that these
21 exemptions were all adopted by your
22 predecessor, the Interstate Commerce

1 Commission, between 1983 and 1993.

2 Over 29 years ago when these
3 exemptions were being considered by the ICC,
4 the railroads and the paper forest industry
5 companies jointly supported the exemptions
6 based on the mutual commercial benefits that
7 could be achieved from removal of burdensome
8 regulatory requirements such as tariff and
9 contract filing which existed at that time.

10 By exempting our commodities from
11 regulation, railroads could be more responsive
12 efficiently to the market and compete more
13 effectively with trucks by avoiding regulatory
14 delays, which prevented price changes from
15 taking effect immediately.

16 CHAIRMAN ELLIOTT: Mr. Lovick,
17 would you mind talking into a mic? I just --
18 I'm concerned that people can't hear.

19 MR. LOVICK: Is that better?

20 CHAIRMAN ELLIOTT: Maybe it's the
21 -- is the mic on? Okay. Maybe our mics are
22 affected.

1 MR. LOVICK: Is that better?

2 CHAIRMAN ELLIOTT: It's not great.

3 MR. LOVICK: Better?

4 CHAIRMAN ELLIOTT: That's better.

5 All right. Thank you.

6 MR. LOVICK: However, in 1995,
7 Congress adopted changes to law in the ICC
8 Termination Act which eliminated tariff and
9 contract filing and other regulatory burdens
10 that limited the responsiveness of railroads
11 and therefore provided the benefits obtained
12 by exempt traffic to all shippers.

13 While we strongly supported the
14 reforms adopted in the ICCTA and still do
15 today, several of the key reasons that led to
16 our support for an exempt status evaporated
17 with its passage. Thus, in today's post-ICCTA
18 environment, our exempt status provides no
19 regulatory benefits but, even worse, results
20 in the loss of access of existing regulatory
21 protections.

22 Regulatory protections on rates

1 and service have become increasingly important
2 to many shippers across multiple industries
3 based on the current structure of the rail
4 market. We believe that paper and forest
5 product companies should have those same
6 rights.

7 Between 1983 and 1995, paper and
8 forest companies also were not concerned about
9 insufficient rail competition for their
10 shipments, since there were many more
11 railroads in 1983 than currently exist. While
12 there were still over 40 Class I railroads
13 when the Staggers Act was adopted, we've
14 witnessed the reduction in the number of
15 providers to only seven Class I railroads
16 today.

17 The consolidation of the rail
18 industry has resulted in many paper mills
19 across the country being captive to only a
20 single railroad. The situation has
21 substantially reduced intramodal and
22 geographic competition for paper and forest

1 products.

2 The reduced rail competition and
3 captive status of many companies has allowed
4 the railroads to impose double-digit rate
5 price increases and to impose take-it-or-
6 leave-it contract terms based on their
7 substantial market power.

8 Although truck transportation is
9 an option for shipping paper and forest
10 products, rail transportation is more
11 efficient and cost-effective, particularly for
12 long-haul movements. Many paper mills were
13 built to receive inbound logs and ship
14 outbound products via rail and thus were not
15 designed to handle substantial volumes of
16 trucks.

17 Weight and size limitations of
18 trucks are also a constraint, and in some
19 regional markets there are truck capacity
20 shortages. Other factors adversely affecting
21 motor carrier costs and competitiveness
22 include driver shortages, increasing cost due

1 to higher fuel, and regulatory changes
2 involving driver's hours of service and the
3 new CSA safety program.

4 Finally, this Agency cannot ignore
5 the changes in the financial health of the
6 railroads, which has occurred between 1983 and
7 today. As explained in our written testimony,
8 by any measure the railroads are more
9 profitable than ever and have achieved strong
10 financial health.

11 The railroad's weak financial
12 condition in the early 1980s and 1990s was
13 clearly a factor that the ICC considered when
14 it adopted the exemptions decisions. The very
15 substantial changes in the railroad's economic
16 status is another factor supporting a review
17 of the paper and forest products exemptions.

18 In conclusion, although there was
19 a broad support from our industry for the ICC
20 to grant the paper and forest products
21 exemptions, in the past 25 years that support
22 has diminished greatly based on the

1 substantial changes that have occurred in the
2 rail industry.

3 AF&PA and PFITC members are no
4 longer confident that regulation is not
5 necessary to meet the public interest
6 considerations of the National Rail
7 Transportation Policy or that regulation is
8 not needed to protect shippers from market
9 abuses, which I understand are the exemption
10 requirements contained in the law.

11 We are not asking STB to revoke
12 the commodity exemptions involving paper and
13 forest products at the conclusion of this
14 hearing. Rather, we believe that it would be
15 appropriate for the STB to initiate a more
16 formal review of these exemptions to determine
17 if they are still justified under the current
18 market conditions in the rail industry.

19 Thank you for the opportunity to
20 present the views of the AF&PA and PFITC here
21 today. I'll be glad to answer your questions
22 at the appropriate time.

1 CHAIRMAN ELLIOTT: Thank you, Mr.
2 Lovick. Next we'll hear from the National
3 Industrial Transportation League, and we'll
4 hear from Mr. Carlton. You have ten minutes.

5 MR. CARLTON: Thank you very much,
6 Mr. Chairman, and good morning to you, Vice
7 Chairman Nottingham, Commissioner Mulvey. We
8 really do appreciate the opportunity to be
9 here this morning.

10 My name is Bruce Carlton. I'm the
11 President of the National Industrial
12 Transportation League. Also accompanying me
13 this morning is Ms. Karen Booth, the League's
14 General Counsel, although she is not sitting
15 here next to us. We have an empty chair,
16 apparently.

17 Again, thank you for letting us
18 appear before you today to provide the
19 League's views on the very important issue of
20 railroad traffic that is currently categorized
21 as exempt from the oversight of this Board.
22 We warmly commend you for initiating this

1 proceeding to review the existing commodity
2 boxcar and TOFC/COFC exemptions.

3 The League represents over 600
4 member companies that range from some of the
5 largest users of the nation's and world's
6 transportation systems to smaller companies
7 engaged in the shipment and receipt of goods.

8 Rail Respondent is vitally
9 important to many of our members, and within
10 this group are shippers of commodities or
11 users of rail services such as intermodal that
12 are currently exempt from STB oversight.

13 At the outset, the League would
14 note that in this proceeding the Board is
15 posing an extremely important but very narrow
16 question. The Board is not asking whether it
17 should eliminate or modify all or any one of
18 the existing exemptions at the conclusion of
19 this hearing.

20 Rather, the Board is simply asking
21 whether, one, it should look at these
22 questions based on very substantial changes

1 that have taken place in the railroad industry
2 since many of the exemptions were adopted,
3 and, two, whether it should begin one or more
4 future proceedings to determine if the
5 Agency's current exemptions should be
6 eliminated or revised.

7 The League believes that the
8 answer to that narrow question is very clearly
9 yes. Apparently, any number of other
10 witnesses and those who have offered testimony
11 and statements to the Board have already
12 advanced this issue to the second and third
13 round before you have even decided whether
14 you're going to take this matter up for
15 further consideration.

16 More than 15 and as many as 30
17 years have passed since the Board's
18 predecessor, the ICC, approved these
19 exemptions. The notion that the conditions
20 that caused the Agency to take these actions
21 have remained unchanged is counterintuitive,
22 to say the least.

1 As detailed in our written
2 testimony, an examination of the facts shows
3 that over the past two decades major changes
4 have occurred in the rail industry, including
5 substantial reductions in intramodal rail
6 competition, substantial improvements in the
7 financial health of the railroads, and
8 statutory changes to further deregulate the
9 rail industry adopted in the ICC Termination
10 Act of 1995.

11 Based on the breadth and scope of
12 changes that have taken place since these
13 exemptions were granted and the two to three
14 decades ago, it is completely proper and
15 responsible government action for the Board to
16 examine whether these exemptions should be
17 eliminated or revised.

18 We believe that the Board should
19 initiate one or more proceedings to evaluate
20 the utility of the existing exemptions based
21 on current market conditions in the rail
22 industry and the governing statute. The

1 League believes that the National Rail
2 Transportation Policy calls for a fair balance
3 between the interests of shippers and
4 carriers.

5 When this Agency or its
6 predecessor decides to remove a category of
7 rail traffic from government oversight, it
8 must look at these policies and determine
9 whether an appropriate balance exists and that
10 the interests of the affected parties are
11 protected.

12 Between 1981 and 1995, when
13 virtually all of these exemptions were
14 approved, there were positive benefits to both
15 shippers and carriers that resulted from the
16 exemptions.

17 Despite deregulation brought about
18 by Staggers Act, the rail industry was still
19 subject to tariff and contract filings and
20 other pricing regulation during this time
21 period. Exemption from regulation removed
22 paperwork burdens, cut carriers' costs, and it

1 eliminated requirements that made rail pricing
2 practices less responsive to shipper business
3 needs.

4 Shippers and carriers both
5 benefitted from the granting of the
6 exemptions, and many shippers jointly
7 supported the grant of the exemptions in the
8 ICC proceeding, along with their railroad
9 partners, but when ICTA was passed in 1995,
10 Congress eliminated virtually all railroad
11 tariff and contract filings, along with other
12 limitations on rail pricing practices. ICTA
13 conferred the benefits obtained by shippers of
14 exempt traffic on all shippers.

15 Today, shippers whose commodities
16 are subject to an exemption receive no
17 tangible benefits from the exemption at all.
18 They simply lose the regulatory protections
19 otherwise available to other shippers. This
20 circumstance, coupled with other major changes
21 in the rail industry, would appear to upset
22 the balance of interest achieved when the

1 exemptions were granted.

2 The Board has asked in this
3 proceeding whether the basis for the existing
4 exemptions should be revisited. We strongly
5 question whether it is proper to continue the
6 exemptions for some commodities on the basis
7 of benefits that are no longer meaningful. It
8 is time to reevaluate whether some or all of
9 the existing exemptions continue to make
10 sense.

11 Another key factor underlying the
12 grant of each of the exemptions was the state
13 of competition, but very substantial changes
14 in the structure of the rail industry have
15 occurred in the last 15 years, which have
16 impacted the extent and effectiveness of
17 competition.

18 Given the substantial
19 consolidation of the rail industry since 1990,
20 the extent of rail-to-rail and geographic
21 competition is surely diminished from where it
22 was 20 years ago. Other modes, especially the

1 trucking industry, are facing both capacity
2 constraints in certain markets and new
3 regulatory requirements.

4 In particular, the trucking
5 industry is dealing with initiatives from the
6 U.S. Department of Transportation, the CSA
7 1010 Initiative, possible changes in the hours
8 of service rules, and next up the electronic
9 on-board recorder requirement.

10 All of these may render the
11 trucking industry a less effective competitor
12 than they were 20 years ago, especially at
13 longer distances. Just last month, the League
14 held a webinar for our members that examined
15 the productivity losses that will flow from
16 DOT's recent hours of service proposal.

17 Further, the recently issued
18 Senate Commerce Committee financial report on
19 the freight rail industry quotes Wolff
20 research, a very respected industry observer,
21 to the effect that railroads will "likely
22 continue to take market share from the less

1 fuel efficient and increasingly less
2 productive trucking industry."

3 By all accounts, rail pricing
4 since 2004 has increased well in excess of
5 inflation, an important indication that
6 competition is less effective than it has been
7 in the past.

8 The League believes that given
9 these and other changes described in our
10 written comments, the Board cannot assume that
11 competition is as vigorous as it was 20 years
12 ago. The changes in the competitive landscape
13 further justify a more formal review of these
14 exemptions.

15 Finally, another purpose for
16 granting the exemptions was to assist
17 railroads in achieving revenue adequacy by
18 cutting carrier costs and permitting more
19 responsive and efficient pricing practices,
20 but it is very clear that the rail industry is
21 in a much more favorable position economically
22 compared to where it was decades ago when

1 these exemptions were granted.

2 Thus, it is entirely appropriate,
3 again, for the Board to examine whether these
4 exemptions are still necessary for carriers to
5 achieve financial health when by all accounts
6 they are one of the healthiest industries in
7 America.

8 While the railroad's testimony
9 asked the Board to ignore the substantial
10 improvements in their financial condition, it
11 unquestionably was a factor reflected in the
12 ICC exemption decisions, and currently it is
13 a factor to be balanced as part of the
14 National Transportation Policy.

15 In conclusion, it is entirely
16 appropriate, we believe, responsible
17 government action for the Board to examine
18 more thoroughly whether the existing
19 exemptions should be eliminated or modified
20 based on substantially changed circumstances.

21 Of course, the decision to
22 initiate such a review does not pre-judge what

1 the findings might be. The ultimate findings
2 would need to be based on the evidentiary
3 submissions made in any such future proceeding
4 or proceedings. Again, thank you very much
5 for the opportunity to be here this morning,
6 and we'll answer any questions that you have.

7 CHAIRMAN ELLIOTT: Thank you, Mr.
8 Carlton. Now we will hear from the Wisconsin
9 Central Group, and speaking on their behalf
10 will be Mr. Varda, and you have ten minutes.

11 MR. VARDA: Mr. Chairman, members
12 of the Board, thank you for the opportunity to
13 be heard on this subject today. I am legal
14 counsel to the Wisconsin Central Group, an ad
15 hoc rail shippers coalition operating under
16 the auspices of the Wisconsin Paper Council,
17 Wisconsin Manufacturers in Commerce, and the
18 Michigan Forest Products Council.

19 Our group, under various names,
20 was present, including participation in
21 various ICC proceedings, for the transition
22 following Staggers and the Motor Carrier Act

1 of 1980. In the mid-1980s through the early
2 1990s, we were present for the withdrawal of
3 the Class Is from Wisconsin and upper Michigan
4 through various spin-offs.

5 In the late 1980s and through the
6 1990s, we were present for the creation,
7 consolidation, and successes of the
8 independent Wisconsin Central System, and, of
9 course, we were present for grant of control
10 of the WC system to Canadian National and its
11 aftermath.

12 The goal of our group is to
13 persuade the Canadian National or by whatever
14 means to assure restoration of Wisconsin
15 Central System level of service and
16 competition for market share for traffic that
17 originates and/or terminates on lines of the
18 former Wisconsin Central System and for CN's
19 main line between Superior, Wisconsin, and
20 Chicago, a transparent plan to mitigate the
21 impact of the increasing international traffic
22 and to provide ample capacity for serving

1 traffic that originates and/or terminates on
2 the lines of the former Wisconsin Central.

3 From our perspective, the problem
4 today is a failure of competition and
5 competition policy. From our perspective, the
6 primary competitiveness problem is not with
7 captive traffic but rather with non-captive
8 traffic.

9 Freight competition in our region
10 has changed dramatically since the exemptions
11 were granted and since Class I's have reached
12 their present level of consolidation. The
13 Class I Canadian National, which this Board
14 granted control of the WC system in 2001, has
15 utterly failed to compete for market share on
16 traffic originating and/or terminating in our
17 region on lines served by the former Wisconsin
18 Central System.

19 CN has strong incentives to not
20 compete for, in fact, to suppress such
21 traffic. Ironically, the Board's efforts to
22 require mitigation of the impacts of the

1 operational changes arising from Canadian
2 National's control of EJ&E, an application
3 that we in Wisconsin and the Upper Peninsula
4 supported, has added incentives for CN to
5 suppress traffic originating and terminating
6 on lines of the former Wisconsin Central
7 System.

8 Given the exemptions shippers and
9 other stakeholders in our region, including
10 those in the public sector such as the states
11 of Wisconsin and Michigan and communities like
12 those who are in the process of forming the
13 Blue Line Coalition, have no realistic means
14 to get CN's attention to the problem, to say
15 nothing of holding CN accountable or otherwise
16 restoring rail competition in our region.

17 The Board should investigate
18 potential revocation of the exemptions. CN's
19 treatment of the former Wisconsin Central as
20 described in Wisconsin Central Group's
21 statement illustrates, and we provided a
22 number of very specific examples, illustrates

1 why the Board should do so.

2 Wholesale revocation of the
3 exemptions is almost certainly not the answer.
4 Small adjustments or targeted revocation of
5 exemptions may better serve to, A, give
6 competition another chance were failure of
7 competition has been the unintended
8 consequence of Class I consolidation, and, B,
9 provide adequate oversight and effective means
10 by which individual shippers might bring
11 attention to such problems on a case-by-case
12 basis.

13 The independent Wisconsin Central
14 System is a model for the competitive impacts
15 of Staggers' deregulation, specifically in
16 providing first-mile, last-mile retail
17 railroad service competing successfully mostly
18 for non-captive freight.

19 The independent Wisconsin Central
20 System successfully won back boxcar freight
21 that the Class I's serving Wisconsin and upper
22 Michigan lost to highway in the 1980s. The

1 independent Wisconsin Central System even
2 successfully provided short-haul intermodal
3 services, an example, from Green Bay to
4 Chicago, which with the largest customer and
5 most devoted customer being the nation's
6 largest truckload motor carrier. CN
7 terminated those services.

8 There is considerably more to this
9 story. That's the reason for our request for
10 investigation. We ask that the Board
11 investigate specifically to conduct an in-
12 depth investigation of the effectiveness of
13 the exemptions, changed circumstances and
14 implications of revocation of the exemptions,
15 and in particular to consider the pros and
16 cons of limited and/or targeted revocation to
17 address failures of competition policy and
18 failures of conditions imposed on Class I
19 consolidations such as those illustrated by
20 the ten years of Canadian National's control
21 of the Wisconsin Central system. Thank you
22 for your consideration.

1 CHAIRMAN ELLIOTT: Thank you, Mr.
2 Varda. Commissioner Mulvey, do you have any
3 questions?

4 COMMISSIONER MULVEY: I have a
5 few. Let me begin with Mr. Varda. Are you
6 suggesting that the acquisition by CN of the
7 Wisconsin Central System was not so much
8 designed to incorporate them as part of CN but
9 rather to eliminate them as a competitor and
10 that this is really almost more of a merger
11 issue than anything else, or --

12 MR. VARDA: Not at all. Excuse
13 me.

14 COMMISSIONER MULVEY: Okay.

15 MR. VARDA: Not at all. The
16 Canadian National was quite clear in the
17 proceeding, Docket 34,000, that its purpose
18 was to acquire the Superior-to-Chicago line.

19 It also promised that I was going
20 to maintain the local characteristics of the
21 Wisconsin Central System, maintain it as a
22 separate division to maintain those local

1 characteristics, the most prominent of which
2 was their -- Wisconsin Central's
3 competitiveness for market share in our
4 region.

5 COMMISSIONER MULVEY: Compared
6 against trucks, for the most part, you're
7 saying.

8 MR. VARDA: Yes.

9 COMMISSIONER MULVEY: Yes. Mr.
10 Moreno, you're here along with the forest and
11 paper products people. Those two industries
12 which particularly have suffered from the
13 current economic turndown.

14 Are you suggesting at all that the
15 conditions in certain industries need to be
16 considered when the Board makes a decision as
17 to whether or not it's appropriate to revoke
18 exemptions or, for that matter, any other
19 consideration by the Board of a rail shipper
20 matter that should the conditions in your
21 industries should be a factor?

22 MR. MORENO: I'm not here to

1 advocate that the exemptions should be revoked
2 because of the financial condition of the
3 automotive industry. In fact, it's hard to
4 draw a broad description of the auto -- across
5 the entire automotive industry in terms of
6 their financial condition.

7 A couple of years ago, it was
8 primarily the domestics that were in financial
9 straits that fortunately they have recovered
10 and improved and emerged from bankruptcy in a
11 very -- in a much stronger position.

12 I think it's the ability. It is
13 relevant to the ability of the railroads to
14 exercise their market power. It does suggest
15 that if railroads are continuing to exercise
16 market power even when the industry's own
17 survival is at stake that there could be --
18 that could be a indicator of market power or
19 the fact that the railroads don't feel that
20 there is competition that's emerging,
21 effective geographic competition, for example.
22 They don't see the threat of imported

1 vehicles, for example, to the domestic
2 industry.

3 COMMISSIONER MULVEY: Mr. Lovick?

4 MR. LOVICK: In answer to your
5 first question is that what we're implying, a
6 revocation based on the economic circumstances
7 of our particular markets, no, we're not.

8 COMMISSIONER MULVEY: Many years
9 ago, back in 1925, I guess, the peak of
10 regulation, the Congress passed what was
11 called the Hoch-Smith Resolution, which
12 required that the ICC take into account
13 conditions in industries, primarily in
14 agriculture, in making its regulations.
15 Fortunately, that never became law, but other
16 things did.

17 Again to you two, do you see any
18 procedural barriers for filing for a
19 revocation? Someone suggested that it's
20 difficult to bring an exemption revocation
21 proceeding before the Board because of its
22 cost or the complexity, et cetera, and that's

1 why the Board hasn't seen any.

2 The railroads say we haven't seen
3 any because there is no need for it. Exempt
4 commodities should remain exempt. Do you have
5 any opinions on that, views on that?

6 MR. LOVICK: I'll share my
7 feelings on that. Specific to building
8 products, it's not movements of a size and
9 scale that you would see for coal and grain.
10 It's much more of a -- I classify it to my
11 management as retail purchasing of
12 transportation, general merchandise type of
13 movements, and we don't have the time.

14 You can't file for a petition and
15 get it turned around in time to help us for a
16 100-car movement a year. It just -- there's
17 not a cost benefit to that proposition. When
18 these exemptions were put in place, it was on
19 a macro scale.

20 I think what we're asking for is
21 to look at it again from a macro scale
22 approach and then, if not revoked, then

1 certainly look at how we could adjust them to
2 better fit into the current and foreseeable
3 market conditions, because market conditions
4 have drastically changed in this nation in the
5 past 20 years. We see things that nobody
6 could have forecast.

7 MR. CARLTON: Commissioner, could
8 I add just a comment to that footnote? It was
9 earlier suggested by one of the witnesses that
10 the there is no barrier, because your filing
11 fees have come down.

12 Number one, we salute you. The
13 League salutes this Board for taking the
14 action to reduce filing fees. I think it's
15 the right and proper thing to do in providing
16 some access to the public, improved access,
17 but that's not the issue.

18 It's not your filing fee, as was
19 suggested earlier. It is the cost involved of
20 diverting executive, corporate executive time
21 to focusing on this issue. There is a real
22 cost to that.

1 Number two, there is a cost in
2 hiring counsel. With all due respect to the
3 bar that practices here, their intelligence
4 does not come cheaply.

5 Number three, there is the cost of
6 hiring consultants, perhaps not Professor
7 Willig but others who practice the dismal
8 science, to make these arguments. That is a
9 very costly undertaking, and I would say
10 that's a very high barrier to bringing these
11 types of matters to your attention.

12 Again, that's why the League is
13 very pleased that you've asked the question,
14 "Should we take a look?" and, again, we think
15 you should take a look. Together.

16 COMMISSIONER MULVEY: So, are
17 there any suggestions as to what the Board
18 could do to lower the barriers, to streamline
19 the process, and to make it less costly from
20 a resource standpoint.

21 We have the same thing in our rate
22 cases. We've lowered our rate case filing

1 fees down to a fraction of what they were, but
2 the filing fees were trivial compared to the
3 millions of dollars that it costs to bring a
4 large rate case.

5 We've tried some other approaches.
6 We have small rate case approaches now, but
7 there may be other things we can do to
8 simplify the process, accelerate the process,
9 and make access to the Board simpler, cheaper,
10 and more effective.

11 Let me see here. I think that
12 that's all I have for the moment. I might
13 have other questions later. Thank you.

14 CHAIRMAN ELLIOTT: That's fine.
15 Vice Chairman?

16 VICE CHAIRMAN NOTTINGHAM: Well,
17 thank you. I thank the panel for being with
18 us today. Mr. Moreno, I think you probably
19 are familiar, this Board has had a very close
20 and positive, long-term working relationship
21 with the auto industry.

22 I know we've met as a group out in

1 Auburn Hills in the Detroit area on the
2 premises of one of your big members. I've
3 personally met privately with the CEOs of the
4 auto industry talking about this issue and
5 related issues.

6 I personally called Class I rail
7 CEOs at the behest and urging of auto industry
8 CEOs to talk about ways to resolve some of
9 these concerns, and we appreciate your being
10 here. I know you represent a diverse group of
11 companies.

12 Remind us, though, who doesn't the
13 Association, the Alliance, represent? You
14 said you've got 77 percent. Are there a
15 couple of big household names we would
16 recognize that aren't part of the group, just
17 so we know?

18 MR. MORENO: Well, let me just --
19 the group is comprised of BMW, Chrysler, Ford,
20 GM, Jaguar, Mazda, Mercedes Benz, Mitsubishi,
21 Porsche, Toyota, and Volkswagen. I mean,
22 that's --

1 VICE CHAIRMAN NOTTINGHAM: Right,
2 so just, I guess, Honda is one of the ones
3 that's not there.

4 MR. MORENO: Honda, yes. Honda is
5 not on this list.

6 VICE CHAIRMAN NOTTINGHAM: They do
7 their own thing or have a different group.
8 Got it. Mr. Lovick, similarly, I think you're
9 probably familiar. This Board has had a very
10 close and longstanding interest and working
11 relationship with the forest and paper
12 industry.

13 Some of the most difficult and
14 time-consuming cases we've wrestled with in
15 recent years, including -- include the
16 abandonment out in the Coos Bay line out in
17 Oregon where the entire Board in an almost
18 unprecedented fashion took staff out to
19 Eugene, had a hearing in a federal courthouse,
20 and made sure that our processes worked to
21 keep that line running under new ownership.

22 Similarly, we were up in far

1 northern Maine in Presque Isle together,
2 thanks to our Chairman's leadership, looking
3 into the very difficult circumstances
4 surrounding the recent abandonment of the MN&A
5 line up in northern Maine that was a
6 particularly tough impact to the forest and
7 paper industry, and we're pleased that that
8 line is going to stay open thanks to the
9 taxpayers of Maine and the folks there.

10 So we do -- many of these concerns
11 are not completely new to us, and I think we
12 do have some record upon which to understand
13 both what's going on in the auto industry and
14 the paper industry, and, Mr. Carlton, I just
15 want to say thank you for being here.

16 You and I have had a chance to
17 work very closely together back at DOT
18 headquarters, and I just want to say for
19 everyone's benefit Bruce Carlton was without
20 a doubt one of the top, top tier career civil
21 servants and leaders and just an example of
22 the best of the best there at DOT, and the

1 work you did at the Maritime Administration
2 for many years in advising many Secretaries of
3 Transportation was just incredibly valuable.

4 I had the privilege of traveling
5 with you internationally with former Secretary
6 Mineta, and we just appreciate the NIT League,
7 having you and having you here today, and
8 thank you.

9 Mr. Varda, thank you for being
10 here. I understand these are remarkable times
11 in Wisconsin. We're reading more and more,
12 and not just in the sports section but front
13 pages of international papers now, and I'm
14 glad you're not on strike and you fled the
15 state. You fled it for a reason. You're
16 working, and I'm not sure what happened to Mr.
17 Zulger.

18 MR. VARDA: He had to --

19 VICE CHAIRMAN NOTTINGHAM: I worry
20 he may be on strike or in hiding, but if he
21 comes late, we hope --

22 MR. VARDA: He's not on strike,

1 but they have to figure out what they're going
2 to do for shared revenues from the state, so
3 the communities are in a lot of trouble.

4 VICE CHAIRMAN NOTTINGHAM: I do
5 understand, but that's really all I've got for
6 this panel.

7 CHAIRMAN ELLIOTT: Thank you, Vice
8 Chairman. Just a couple questions. Back to
9 the question that I had earlier for the
10 railroad interests: do the shipper interests
11 see any concerns, a possible void in their
12 ability to recover because of the revocation
13 process?

14 My example had been that you're an
15 exempt commodity, so in order to come before
16 the Board you have to seek revocation, and
17 once you do that, are there things that you
18 believe that you can't recover or receive a
19 remedy because of this process? Is there
20 something, I guess, that's not working in our
21 progress, I guess, is my question.

22 MR. VARDA: I'd like to answer in

1 a little different direction. It's out
2 concern is not so much of rates but getting
3 service, and that's the heart of it, and we're
4 not going to recover for the customer
5 dissatisfaction because we had to go by truck
6 rather than rail to facilities that are
7 designed to receive by rail, having to
8 rearrange our outbound shipping because we
9 don't have the capacity to ship by truck where
10 the facility was designed to ship by rail.
11 We'll never recover that.

12 CHAIRMAN ELLIOTT: Thank you.

13 MR. MORENO: It's not so much a
14 recovery cost, because what you may save is
15 difficult to quantify by having access to
16 regulation, but I think there is even a value
17 just in knowing that there is a regulatory
18 safety net in those -- in your -- in those
19 situations when you are dealing with railroads
20 where you feel you have no other option and
21 you're in a take-it-or-leave-it situation.

22 Right now, when you're negotiating

1 a contract or negotiating over some sort of
2 dispute, you can't say -- or you can't take
3 this to the Board. You're basically at the
4 mercy of what you're being dictated in that
5 circumstance, and there is value in at least
6 having that sort of leverage, that option,
7 because then the railroad also knows you have
8 that option, and it takes that into
9 consideration, as well.

10 CHAIRMAN ELLIOTT: Thank you.

11 Along those same lines, let's say in the
12 instance of if you wanted to challenge a rate,
13 it seems somewhat confusing, because at the
14 present time your rates are under contract as
15 an exempt.

16 How would you go about challenging
17 a rate in the instance if you sought
18 revocation, because it would seem like since
19 your rates are all under contract, those would
20 be automatically exempt?

21 MR. MORENO: The rate, because the
22 rates are in a contract, they are not

1 challengeable, but contracts come up for
2 renewal every so many years, and during those
3 contract negotiations, regulated traffic, if
4 you don't like that contract offer, you can
5 always say, "Give me a tariff rate."

6 The railroad is required by law to
7 give you a tariff rate, and you have the
8 option to challenge the reasonableness of that
9 rate if you do not like it. An exempt shipper
10 does not have that option.

11 CHAIRMAN ELLIOTT: Well, yes, and
12 if the shipper is exempt, how would they go
13 about -- I mean, can they challenge a rate?

14 MR. MORENO: Not without
15 specifically getting the exemption reworked.
16 Now, there is the possibility of a case-by-
17 case exemption, as opposed to revoking the
18 class exemption.

19 CHAIRMAN ELLIOTT: Would they have
20 to go about revoking it first, obtaining a
21 tariff, and then challenging it?

22 MR. MORENO: Yes, and that's kind

1 of the -- that literally is the problem here.
2 It adds an extra layer in seeking regulatory
3 productions, and there is kind of a
4 backwardness to this in the context of rates.

5 We discussed that one of the
6 standards that the railroads have said would
7 apply here is abuse of market power. Well,
8 how do you prove abuse of market power when
9 the proof is in the unreasonableness of the
10 rate?

11 So it gets circular. In order to
12 be able to challenge the rate, you have to
13 prove it's unreasonable, but you can't prove
14 it's unreasonable until you get the -- until
15 you prove abuse of market power.

16 CHAIRMAN ELLIOTT: Thank you.

17 MR. VARDA: Mr. Chairman?

18 CHAIRMAN ELLIOTT: Sure.

19 MR. VARDA: Many of us don't have
20 contracts in the sense of a contract. It's
21 simply if I'm a log cutter hauling to a
22 landing, you know, the rate is what the

1 railroad tells me it is. It's out there
2 someplace in an exempt publication, but it's
3 not a contract with me. I didn't sign
4 anything.

5 I'm told what it is, and so there
6 is sort of a void in there between, well, is
7 it a contract? Yes, because it's a bill of
8 lading contract, but is it a contract in the
9 sense of being a transportation contract on
10 which the parties had a meeting of the minds
11 over the, you know, terms and conditions? No.
12 It's much more like a tariff.

13 CHAIRMAN ELLIOTT: Thank you. I
14 think I'd be remiss -- I asked the rail
15 interests about the R/VC, the amount of
16 traffic that runs over 180 R/VC in my
17 questions to them, and I used some pretty
18 strong examples of where the amount of traffic
19 has increased over time from '93 to 2008, the
20 R/VC, the amount of traffic running over 180.

21 I looked in the STCC 37 for
22 transportation equipment, and it appears that

1 the R/VC has, in fact, gone down. The amount
2 of traffic over 180 has gone down over time.
3 How do you explain that as an economic
4 indicator with respect to the industry you're
5 representing?

6 MR. MORENO: Well, that gets back
7 to the issue of the blanket exemption versus
8 the specific subsets. I mean, if you're
9 looking at entirely STCC 37, we don't question
10 or even challenge the fact that there are
11 significant areas where there is competition
12 with the rail industry, but there are also
13 other -- with the truck industry, but there
14 are other areas where the competition does not
15 exist, and I think we would need to drill down
16 deeper into that data in order to see if that
17 holds true at the subsets that we're most
18 concerned about.

19 CHAIRMAN ELLIOTT: Thank you.
20 Just one final question from me. The railroad
21 interests raised the issue the health of
22 industry. I'm not going to quote them

1 directly but paraphrase it, is not really
2 relevant to this analysis. Do you see that
3 the same way?

4 MR. MORENO: No, it's not
5 completely irrelevant. As a matter of fact,
6 if you go back to the original grant, the
7 decision granting the automotive exemptions,
8 there is a reference to the financial health
9 of the industry as a reason for granting the
10 exemption.

11 You can't have it both ways. Now,
12 having said that, it's not the only reason,
13 but it is one of the rail transportation
14 policies, and you're required to examine the
15 rail transportation policies.

16 CHAIRMAN ELLIOTT: Thank you.

17 COMMISSIONER MULVEY: Just
18 following up a little bit on that, you
19 mentioned that there are a lot of differences
20 within the transportation equipment sector and
21 that, again, a lot of things are hidden by
22 averages, as we mentioned before. Would you

1 advocate or would you think it would be worth
2 us considering whether or not we ought to
3 revoke the exemptions for certain kinds of
4 traffic that move beyond a certain distance?

5 I think you mentioned in your
6 testimony that the changes in the industry
7 have caused shipments to become much, much
8 longer, making certain kinds of traffic like
9 oversized pieces, et cetera, and long-distance
10 movements of finished cars, that there should
11 be these distinctions, including some for
12 movements over a certain distance. Do you
13 think that's something the Board should
14 consider looking at?

15 MR. MORENO: Absolutely. I mean,
16 the Board should be looking at what portions
17 of the traffic are still perhaps captive and
18 require regulatory protection, and if that is
19 based on a distance threshold and the evidence
20 supports that, by all means that would be
21 acceptable.

22 COMMISSIONER MULVEY: Bruce would

1 you want to comment on that, also?

2 MR. CARLTON: No, I would agree.
3 You know, I don't look at this issue as, you
4 know, a single matter. It's the entire
5 collection of the issues that have been
6 discussed here this morning, and, absolutely,
7 it's possible to segment markets and find
8 greater and lesser degrees of competition
9 within what might be seen as a single market,
10 but the segments are very important.

11 I was astounded by some of the
12 submissions to you and to the staff to the
13 degree of reference to reregulation. I mean,
14 I overwork sports analogies, but it's a head
15 fake. You know, if you watch where my head's
16 going, you think that the basketball player's
17 going there, and, of course, he goes over here
18 and he scores the three-pointer.

19 It's not about reregulation. The
20 NIT League is not a proponent of regulation of
21 American industry. It is about, you know,
22 providing appropriate statutory relief for

1 shippers, a relief that 30 years ago they gave
2 up willingly, because there were other
3 benefits, and today conditions have changed,
4 and, again, we commend the Board to take a
5 look deep inside that process.

6 MR. VARDA: Likewise, I'd like to
7 caution that market abuse can occur in short-
8 haul markets. It's a different kind of market
9 abuse. What we're suggesting is the market
10 abuse is you have enough market power
11 elsewhere.

12 You don't want to compete in that
13 market. You don't want to accept that
14 traffic. That's something you should look
15 into, as well.

16 COMMISSIONER MULVEY: Just one
17 last question. We have an awful lot of
18 commodities, traffic types, et cetera, that
19 are subject to the exemption, a very daunting
20 task for the Board to review all of those. I
21 was wondering if you had any suggestions as to
22 what rule of thumb the Board might follow in

1 deciding what groups of traffic commodities,
2 et cetera, we might spend some time examining.

3 Should it be the revenue-to-
4 variable-cost ratio, or do you have something
5 else that you think would be useful for us to
6 consider in looking at whether or not we ought
7 to reexamine a particular exemption? Anybody
8 can answer that.

9 MR. CARLTON: I wish I had been
10 smart enough to think of that question before
11 you asked it, and I say that with only a
12 little bit of a facetious tone only because if
13 individually exempted shippers and commodity
14 groups and service classes, if we are to
15 believe, as I do, that some of them are quite
16 concerned about retaliation from their
17 carriers, if you were to put a sign-up sheet
18 out in the lobby saying, "If you would like us
19 to look at your particular class or commodity,
20 just sign here," I think that is going to not
21 be attractive to a lot of shippers.

22 So I think I'm respectfully coming

1 back around to say I hope you guys come up
2 with a process that allows for a good
3 quantitative assessment that sort of starts to
4 separate the groups into some natural zones
5 for further examination, because I think
6 there's going to be a reluctance from the
7 shipper community to come in and say, "Well,
8 take us."

9 COMMISSIONER MULVEY: We always
10 hate to hear that retaliation argument. We
11 used to have these meetings every year between
12 the railroads and the shippers, and we asked
13 for comments and questions, and we were told
14 that nobody would raise their hand, because
15 they were afraid of retaliation.

16 Then we tried to have the
17 questions submitted beforehand without names
18 on them. We tried bags on people's heads, but
19 there is always that argument, albeit the
20 railroads claim that they do not retaliate.
21 It's not in their business interest to do
22 such, but, anyway, thank you very much for

1 your answers.

2 VICE CHAIRMAN NOTTINGHAM: I just
3 wanted to follow up, if I could, on this issue
4 that's been raised a couple times about
5 concerns about railroad industry retaliation
6 against customers. It's a very -- that's a
7 very serious allegation.

8 I just wanted to say that in my
9 five years on the Board, almost five years, I
10 have not seen a single documented case. We've
11 asked. We've asked people in prior hearings
12 to please come to us confidentially if they'd
13 like to come to us and explain how that
14 happens and why railroads would want to injure
15 their customers.

16 And I'm not naive. I understand
17 that in the hustle and bustle of international
18 commerce and competition, you know, tough
19 things can happen occasionally, but we're the
20 regulatory agency. We need to know about that
21 kind of stuff, and there are ways for us to
22 know, but we need people to step forward, and

1 just coming into a hearing and kind of
2 throwing it out there, that's a concern.

3 With all due respect, I mean,
4 we've got to have a little more than that, and
5 I do appreciate the fact that all of you
6 represent large numbers of constituents and
7 stakeholders, and they've got a variety of
8 major issues on their plate, especially in
9 today's complex economic and regulatory world.

10 You know, for us, we have to as a
11 Board, and the Chairman's, you know, deeply,
12 intimately familiar with this, we have an
13 allocation of resources issue internally
14 ourselves. We've got to figure out which
15 major issues we're going to take on as a 140-
16 person, give or take a few employees, agency.

17 And I would say just as one
18 Commissioner speaking for myself, it doesn't
19 help us set priorities if individual
20 stakeholders are not willing to come forward
21 and actually explain to us what the problem
22 is. It's helpful to have associations come

1 forward and say that there could be a problem
2 and we should look at it generally, and maybe
3 we might find out that there is really more of
4 a problem, but we need people.

5 I mean, many of you represent --
6 not all of you. Many of you represent
7 companies that are far bigger than any of the
8 railroads and talk about market leverage and
9 all that and with far more influence,
10 probably, in the halls of Congress, some of
11 you, and I just think, you know, we need to --

12 This Agency would need to see, I
13 believe, as one Commissioner, folks to step
14 forward and actually explain to us the
15 specific problem for you to be able to
16 effectively get this issue, you know, on the
17 front plate. Other Commissioners may have a
18 different opinion. I respect that. I just
19 need to say that. Thank you.

20 MR. VARDA: Mr. Chairman, I can
21 give you an example. The Consumer Protection
22 Office was kind enough to send a delegation in

1 2004 to Green Bay to talk to a room full of
2 Wisconsin Central shippers who voiced their
3 concern.

4 The meeting was at the Railroad
5 Museum, and it was indeed a room full, and
6 they explained their services and the
7 availability. I hesitate to tell you that I
8 don't think there was a single informal
9 complaint that resulted from that.

10 Everybody walked out of the room
11 with an, "I'm not going to put myself in the
12 way of it," because all of those shippers,
13 while they have non-captive traffic, also
14 have some captive traffic, and they're not
15 just going to -- they're not going to put
16 themselves in that situation.

17 VICE CHAIRMAN NOTTINGHAM: Well, I
18 appreciate that, but I've been to Wisconsin as
19 a guest of Congressman Petri, who is, I
20 believe, a champion of shipper and
21 transportation issues generally, and I visited
22 with a large group of the Badger-CURE folks,

1 a number of people very interested and
2 concerned about the Wisconsin Central.

3 I've heard loud and clear how many
4 Wisconsinites deeply miss the good service of
5 the Wisconsin Central and kind of that good
6 attitude they seem to have had to just chase
7 down business, whether it was highly
8 profitable or minimally profitable, and serve
9 all of the customers, and I understand that.

10 At the same time, in those
11 meetings I made myself available to speak
12 privately with people afterwards, gave them my
13 card, phone number. Nobody called me or
14 pulled me aside privately and said, "This is
15 what I need to tell you," and so I just --

16 We need to hear a little more
17 specifics about something as serious as
18 retaliation, because I think this Board would
19 stop everything we're doing and dig into that.
20 We've, you know, recently had at least one
21 significant case I can think of taking serious
22 action against a Class I that we felt didn't

1 adequately abide by STB processes, and I'm
2 sure the Board would do similarly if we had a
3 reason to.

4 MR. VARDA: I think part of the
5 problem is that it may not be that there is
6 retaliation. It's a perception, and so I
7 wouldn't want to be saying I'm pointing a
8 finger at the railroad saying that you
9 retaliated or would retaliate. It's just what
10 the feedback we have on the perception.

11 MR. MORENO: I would echo it is
12 the fear of retaliation, and no one is willing
13 to put themselves out there to be the guinea
14 pig, become the example, and in many cases
15 retaliation isn't done in a blatantly obvious
16 form.

17 It can be done in subtle ways,
18 which there are often a dozen or other
19 alterative explanations for it, and it's very
20 hard to say, "Yes, that's the reason the
21 railroad did this," but yet there is a feeling
22 and a perception that that is the reason.

1 VICE CHAIRMAN NOTTINGHAM: Thank
2 you.

3 COMMISSIONER MULVEY: I would like
4 to get back to the contestability theory
5 again. You don't really have to actually
6 retaliate. Just a threat of retaliation or
7 the fear of retaliation can be sufficient to
8 discipline the behavior.

9 CHAIRMAN ELLIOTT: I'd like to
10 thank the panel for their presentations, and
11 I think we'll take an hour lunch break. So
12 why don't we meet back here around 1:05, and
13 we'll start off with Panel IV with the freight
14 railroads. So we'll be in recess for about an
15 hour.

16 (Whereupon, the foregoing matter
17 went off the record at 12:06 p.m. and resumed
18 at 1:07 p.m.)

19 CHAIRMAN ELLIOTT: We'll come back
20 into session. We're on Panel IV, who are all
21 before us now, the Freight Railroad Panel, and
22 we will begin with BNSF Railway Company, and

1 we'll have on their behalf Steve Branscum, and
2 you have ten minutes.

3 MR. BRANSCUM: Okay. Good
4 afternoon, Chairman Elliott and Vice Chairman
5 Nottingham, Commissioner Mulvey. My name is
6 Steve Branscum. I'm Group Vice President of
7 Consumer Products at BNSF Railway. I'm
8 responsible for the overall marketing and
9 development of intermodal business on the
10 railway.

11 Just making sure everyone's awake
12 after lunch. Okay, anyway, I'm responsible
13 for the overall marketing and development of
14 intermodal business at the railway. I'm also
15 the immediate past Chairman of the Intermodal
16 Association of North America, and I'm the
17 current Chairman of the Intermodal
18 Transportation Institute that's affiliated
19 with the University of Denver.

20 I have 31 years of experience in
21 the railroad industry, the last 22 of which
22 have been in the intermodal field. I want to

1 thank you for giving me the opportunity to
2 appear here today on behalf of BNSF and to
3 address the value and the importance of the
4 intermodal exemption.

5 In brief, we believe that this
6 exemption has been an essential element of the
7 development and growth of rail intermodal
8 transportation in the last 30 years. There is
9 no question that the exemption has fostered a
10 highly competitive marketplace across modes,
11 and it has benefitted shippers, motor
12 carriers, ocean carriers, railroads, and
13 consumers.

14 BNSF offers an array of intermodal
15 services and pricing combinations to our
16 customers, which has been enabled by the
17 exemption and required in the marketplace to
18 grow intermodal as a transportation
19 alternative.

20 In this climate, we have made
21 substantial investments in our plant and
22 facilities to serve intermodal customers. We

1 believe that the intermodal exemption reflects
2 a successful regulatory policy, which has been
3 effective for over 30 years, and that it
4 should continue.

5 Now, having said that, I would
6 like to go briefly through a short
7 presentation to try to demonstrate three
8 points. One is that there has been
9 significant growth in intermodal as a result
10 of the exemption, it also has allowed
11 substantial investment by BNSF and other
12 railroads to facilitate the intermodal growth,
13 and that there is significant competitiveness
14 in the intermodal marketplace.

15 Now, the first couple of slides
16 are fairly elementary, but I think they're
17 important that we can have the right context
18 on intermodal, so just some definitions.
19 Intermodal transportation is transportation by
20 more than one form of -- more than one mode
21 during a single journey. Obviously, the
22 context of the hearing here today is that at

1 least one of those modes has to be rail.

2 The term "intermodal" has been
3 around for a long time. It's been in the
4 marketplace for 50 years plus, but intermodal
5 has been a significant factor in the
6 marketplace for the last 30 years. Lastly,
7 intermodal is most commonly used to describe
8 the movement of freight in standardized
9 containers and trailers, highway trailers,
10 using at least two modes.

11 One of the most important aspects
12 of intermodal and probably the least
13 understood is that intermodal -- my slide
14 actually says works best in markets with large
15 concentrated volumes, and I'm almost inclined
16 to say it works only in those markets, and
17 it's not efficient in lower volume markets.

18 I say that because if you think
19 about intermodal, it is multi-modal. It
20 requires rail and truck connectivity, and it
21 requires that in order to have the proper
22 service levels in the marketplace in order to

1 be able to compete effectively with over-the-
2 road transportation.

3 Today, intermodal service is very
4 good across the nation. On average, it runs
5 an equivalent to single driver or solo driver
6 highway transportation of about 500 miles a
7 day.

8 It's pretty commonly accepted out
9 in the marketplace that there are four major
10 benefits to intermodal transportation. One is
11 cost efficiency. It's rare that we are --
12 that an intermodal solution is not cheaper
13 than a sole highway solution.

14 Intermodal, because of its scale,
15 has the ability to mitigate highway gridlock,
16 to some extent. It certainly is not a sole
17 solution to highway -- the growing highway
18 gridlock, but it is a way to mitigate.

19 Third, fuel efficiency. On
20 average, intermodal rail is two to three times
21 more fuel efficient than truck, and because of
22 that fuel efficiency, largely it's also much

1 more environmentally friendly than other forms
2 of transportation, order of magnitude about 50
3 percent less carbon emissions and
4 particulates.

5 I think this slide clearly
6 demonstrates the success of the exemption. In
7 the last 30 years, intermodal across this
8 country has grown from about three million
9 shipments a year to almost 13 million, which
10 is a little less than a five percent compound
11 annual growth rate.

12 Even with that significant growth
13 and substantial volume of intermodal, rail
14 today is still a relatively small portion of
15 transportation modal share, and if you look at
16 only the intermodal portion of rail, it
17 represents about a third of what's shown on
18 this pie chart for rail.

19 Now, as to competitiveness, it is
20 highly competitive, as I said a moment ago.
21 I know this slide is very busy, but I would
22 focus your attention on the middle column, and

1 that probably best demonstrates the
2 competitiveness.

3 Intermodal involving rail, there
4 are essentially two types of freight that are
5 involved, international freight, import and
6 export, and domestic freight, and within each
7 of those two broad categories there's a
8 further breakdown of freight into full
9 truckload and less than truckload categories.

10 In the international sector, in
11 the less than truckload category, almost all
12 freight is moved by air, but in the full
13 truckload sector of international freight,
14 it's moved over the water, obviously, to its
15 destination country, the U.S.

16 From there, freight has the option
17 of moving to destination markets with hundreds
18 of thousands of trucking companies or those
19 same trucking companies in combination with
20 the major Class I railroads.

21 Domestic works in a similar
22 manner, but it's a little bit more complex and

1 a little bit more competitive. Domestic you
2 still have the full truckload and less than
3 truckload breakdown.

4 On the less than truckload
5 freight, a lot of it still even within the
6 confines of the country moves by air, or it
7 moves on the ground with around 700 trucking
8 companies that operate in the LTL and parcel
9 sectors. Again, that freight can move solely
10 over the highway, or it can move in concert
11 with the major Class I railroads.

12 For the full truckload sector of
13 domestic, again, it can move with -- I don't
14 know what the feedback issue is.

15 CHAIRMAN ELLIOTT: Why don't we
16 try the second mic? I think that was working
17 in the past.

18 MR. BRANSCUM: Right.

19 CHAIRMAN ELLIOTT: I apologize.

20 MR. BRANSCUM: Is that better?

21 CHAIRMAN ELLIOTT: Much better.

22 MR. BRANSCUM: Okay. On the

1 domestic freight, the last comment here on the
2 domestic freight in the full truckload sector,
3 obviously that freight can move with hundreds
4 of thousands of trucking company all over the
5 country.

6 There is also a large number,
7 thousands -- I don't have the exact number --
8 of brokers, intermodal marketing companies,
9 and non-asset providers that play in that
10 particular market, and they work with hundreds
11 of thousands of trucking companies to move
12 this freight.

13 They also can work in conjunction
14 with the railroad, so bottom line to this
15 complex slide is that shippers have a lot of
16 options when they want to move freight on the
17 ground in the U.S.

18 I'd like to just demonstrate
19 further levels of competition. On the
20 international freight from Asia, for instance,
21 represented by the orange arrows here, coming
22 to the U.S., the freight can come to the West

1 Coast.

2 If it comes to the West Coast of
3 the U.S., then it can be distributed by those
4 hundreds of thousands of trucking companies or
5 those companies and the brokers working in
6 concert with rail, or it can go completely
7 around to the East Coast, where in most cases
8 it's delivered solely by truck.

9 This slide shows the major markets
10 in the U.S. and how the interstate highway
11 system overlaps all those markets, so just to
12 demonstrate truck competitiveness, and then
13 here is the North American rail system laid on
14 top of that, which shows that they serve all
15 these markets, as well.

16 The important point here relative
17 to intermodal is that all this rail cannot be
18 used effectively in a competitive environment
19 of truck competition, so railroads have
20 developed these high-density corridors with
21 big markets to serve all the markets in the
22 U.S., and it looks something like this.

1 You're probably familiar with
2 these corridors. You can recognize the BNSF
3 Transcontinental corridor, the UP Sunset
4 corridor, and so forth. Through these major
5 corridors, virtually every market in the U.S.
6 can be served in combination of rail and
7 truck.

8 The last few slides here that I'll
9 skip through just simply demonstrate the
10 massive investment that BNSF has made and
11 other railroads have made in intermodal
12 infrastructure and the productivity gains that
13 we've been required to implement in order to
14 stay competitive in the market.

15 So, in conclusion, I want to say
16 that the intermodal marketplace is very highly
17 competitive. We've invested heavily in our
18 network and will continue to pursue greater
19 efficiencies as we provide an array of service
20 offerings to our intermodal customers.

21 The exemption, intermodal
22 exemption, has been truly a success story

1 benefitting customers, motor carriers, ocean
2 carriers, consumers, and shippers. The
3 exemption policy should continue so as not to
4 jeopardize the flexibility to provide the
5 essential vitality and the competitive
6 transportation marketplace. Thank you.

7 CHAIRMAN ELLIOTT: Thank you, Mr.
8 Branscum. Now we're hear from CSX
9 Transportation, Inc. We'll hear from Mr.
10 Gooden. You have ten minutes.

11 MR. GOODEN: Good afternoon,
12 Chairman Elliott, Commissioner Mulvey, and
13 Commissioner Nottingham. My name is Clarence
14 Gooden. I'm Executive Vice President and
15 Chief Commercial Officer, CSX Transportation.

16 My career in the railroad industry
17 began in 1970 as a laborer for the Seaboard
18 Coastline, and over the next 40 years I worked
19 in a variety of positions, including President
20 of CSX Intermodal, Senior Vice President of
21 the Merchandise Service Group before assuming
22 my current position in 2004.

1 I would like to formally thank the
2 STB for this opportunity to express my views
3 on the question presented for today. That is,
4 whether the current exemptions have continuing
5 relevance given the changes in the competitive
6 landscape and the railroad industry.

7 The answer is a resounding yes.
8 Exemptions remain very important, and my first
9 slide addresses four broad points as to why
10 that is.

11 The first principle of the Rail
12 Transportation Policy makes clear that there
13 is congressional and economic preference for
14 market-driven solutions. We know this to be
15 true not only from a purely economic
16 perspective as addressed by Professor Willig,
17 but we also know this makes sense from our own
18 practical experience.

19 Current regulatory scheme has been
20 and remains successful. Railroads and
21 shippers have both benefitted from the
22 exceptional progress made over the last 30

1 years. We are concerned that any reregulation
2 of the exempt commodities or classes of
3 traffic would threaten to unravel that great
4 success story.

5 Further, reregulation is also
6 unwarranted because it is clear that
7 competition within the transportation industry
8 is pervasive and abundant. We work every day
9 to win business from trucks, other railroads,
10 and other competitors.

11 The trucking industry remains the
12 dominant player in the transportation
13 business, as has been the case over my 40-year
14 career. Winning market share from trucks is
15 already an uphill battle, and we're concerned
16 that reregulation will only make that battle
17 tougher.

18 Finally, an essential ingredient
19 to winning market share and getting freight
20 onto our system is our ability to reinvest and
21 grow for the future. It is our relatively
22 recent financial progress that has made our

1 current unprecedented level of reinvestment
2 possible.

3 Congress established the principle
4 that market demands and competition should
5 determine rates to the maximum extent
6 possible. That makes economic and common
7 sense, since it's the market that guides
8 virtually every aspect of ours and most
9 businesses.

10 The markets help us determine what
11 capacity to increase, what services to offer,
12 what equipment to buy, what rates to charge.
13 If we're hindered in our ability to respond to
14 the market, we will make less efficient and
15 therefore wasteful decisions regarding where
16 to put our next dollar.

17 Knowing where to efficiently and
18 productively put our resources benefits both
19 our customers and the consumers, which is what
20 Congress envisioned. Congress knew that
21 railroad success would be to the benefit of
22 customers and consumers, and that is exactly

1 what we've seen over the last 30 years.

2 This slide tells the story in
3 dramatic fashion. Prior to Staggers, bankrupt
4 railroads accounted for more than 21 percent
5 of this nation's rail mileage.

6 Railroads were unable to
7 adequately maintain their systems. More than
8 47,000 miles of track operated at reduced
9 speeds, and investment in additional or
10 improved infrastructure was difficult to
11 support both strategically and financially.

12 Now look at what has happened with
13 Staggers. Productivity has skyrocketed. In
14 fact, productivity gains since Staggers are
15 over 11 times the pre-Staggers rate. Volume
16 has increased steadily and ultimately doubled
17 until the dip associated with the great
18 recession.

19 While I understand that some
20 shippers of exempt commodities are complaining
21 today about their rates, the general facts
22 don't support their story. As you can see

1 from this slide, rates today adjusted for
2 inflation are 55 percent less than what they
3 were when Staggers was passed.

4 This is the historical context
5 that the Board must confront head-on before it
6 considers whether to reverse course. Today,
7 we have established history of mutual gains
8 and mutual benefits, a history that has
9 allowed railroads to reinvest a remarkable
10 \$480 billion in their network and equipment
11 since Staggers.

12 All of these various advances are
13 interrelated, and they are all threatened to
14 be unraveled by unwarranted regulation.
15 Staggers caused a number of changes for the
16 good, but I'd like to highlight for you the
17 cultural transformation we witnessed from the
18 commercial perspective.

19 Prior to Staggers, shippers had
20 grown accustomed to relying on public rates
21 and traditional service. On the railroad
22 side, any proposed change in rates or services

1 were delayed by internal regulatory reviews,
2 and that naturally resulted in a slow and
3 conservative approach to change. There was,
4 in essence, a general impediment to trying
5 anything new and creative.

6 Following Staggers, we shifted to
7 a market-based environment with a new sense of
8 urgency and creativity. Normal market
9 incentives drove new innovations that improved
10 service to our customers and allowed us to
11 operate more efficiently and ultimately
12 profitably.

13 The intermodal market is a
14 wonderful example of this phenomenon.
15 Intermodal traffic has nearly quadrupled over
16 the last 30 years, rising from three million
17 trailers and containers in 1980 to just under
18 12 million today.

19 Presently, intermodal accounts for
20 about 21 percent of U.S. rail revenue, second
21 only to coal and all other rail traffic
22 segments. This would not have been possible

1 without substantial innovations and
2 reinvestment into clearing of the right-of-
3 ways for double-stacked containers, new
4 terminals, and expanded port facilities.

5 We view our new intermodal
6 terminal in northwest Ohio, which actually
7 began its first day of successful operations
8 yesterday, as a prime example of the
9 innovative transformation we're seeing in the
10 industry.

11 It will effectively serve as the
12 hub for all intermodal traffic moving across
13 the northern tier of our network. It features
14 a state-of-the-art terminal design with five
15 wide-span cranes, each as wide as a football
16 field is long.

17 These cranes are the latest in
18 green technology, taking up less space,
19 creating less noise, and running on
20 electricity, resulting in an 80 percent
21 emissions reduction compared to diesel cranes.
22 In fact, the cranes actually generate

1 electricity as they lower containers. The
2 crane significantly improves car-to-car
3 loading, resulting in increased delivery times
4 and greater service reliability for our
5 customers.

6 Now I'd like to turn to another
7 reason why reregulating exempt commodities
8 would be wholly unwarranted. Competition is
9 pervasive.

10 As I said in my opening comments,
11 we compete hard against all of our
12 competitors, but as the statistics on overall
13 tonnage from the Department of Transportation
14 make clear, the trucking industry is by far
15 the dominant player. It commands 67 percent
16 of the total transportation market based on
17 tonnage.

18 Rail, on the other hand, currently
19 holds a modest ten percent of the
20 transportation pie, only marginally more than
21 the eight percent enjoyed by pipelines.
22 Trucks have been the dominant mode of

1 transportation for as long as I've been in the
2 business.

3 What's been exciting to see in
4 recent years is the progress we've made in
5 earning business that historically belonged to
6 trucks. We are concerned that reregulating
7 the exempt commodities will re-handicap our
8 ability to compete with the trucking industry
9 and make it all the more difficult to get
10 loads off the highway and onto the rail
11 system.

12 Now I'd like to turn to a few of
13 the shippers' comments that have focused on
14 the improved financial performance within the
15 rail industry. They assert that financial
16 progress is a justification for reregulation,
17 and that's just flat wrong.

18 In passing Staggers, it was the
19 goal of Congress to strengthen the railroad
20 industry's financial position and with it the
21 nation's transportation network. That we're
22 closer to that goal than we were 30, 20, or

1 even ten years ago is an affirmation of the
2 course charted by Congress, not a
3 justification for reversing course.

4 Improved financial performance has
5 laid the foundation for the recent dramatic
6 increases in reinvestment by the railroads in
7 their network and equipment. As you can see
8 on this slide, CSX capital expenditures have
9 closely followed operating income results.

10 When operating income dipped in
11 2009, so, too, did the amount that we were
12 able to reinvest in the business, but in 2010
13 we were able to return to the 2008 level of
14 \$1.8 billion, and we plan to increase that
15 amount to an unprecedented \$2 billion in 2011.
16 It is precisely this kind of upward trend in
17 reinvestment that's required to meet the
18 projected demands of the future.

19 This slide shows the most recent
20 projects for freight demand from the
21 Department of Transportation. Demand is
22 expected to increase 68 percent by 2040.

1 Absent a change in market share, the
2 railroad's portion of that increase would be
3 1.3 billion tons.

4 By anyone's standards, that's a
5 big jump from current levels, but as an
6 industry we continue to hear from federal and
7 local governments, from customers and from
8 communities we serve that there is a real need
9 to get more tons off the highway and onto the
10 rail system. In other words, there is an
11 expectation for railroads to grow our current
12 market share, not simply maintain it.

13 We at CSX view the 1.3 billion ton
14 increase as the floor. We're planning and
15 building for more in the future that well
16 exceeds it. Given our country's growing
17 expectations for rail, as well as our own, we
18 anticipate more competition, not less, as we
19 work to win more business.

20 We look to reinvest an increasing
21 amount into our network, not less, as we
22 strive to meet future demands, and, as we

1 know, the country is asking for more rail, not
2 less, as we target new goals that go well
3 beyond the volume and productivity increases
4 achieved to date and which also seek to
5 further advance the landmark success we've
6 seen in safety, service, and environmental.

7 In closing, I appreciate this
8 opportunity to speak on this important topic,
9 and CSX Transportation looks forward to
10 working with the Board in ensuring that the
11 fair, balanced, regulatory scheme envisioned
12 by Congress will continue to allow the
13 railroads to serve the need of its customers
14 and its customers in the future. Thank you
15 very much.

16 CHAIRMAN ELLIOTT: Thank you, Mr.
17 Gooden. Now we'll hear from Kansas City
18 Southern. You have ten minutes.

19 MR. OTTENSMEYER: Okay. Good
20 afternoon, Chairman Elliott, Vice Chairman
21 Nottingham, Commissioner Mulvey. My name is
22 Pat Ottensmeyer, and I am Executive Vice

1 President of Sales and Marketing for Kansas
2 City Southern and the Kansas City Southern
3 Railway Company.

4 I appreciate the opportunity to
5 present KCS oral testimony on this topic. The
6 Board's notice requested comments on the
7 effectiveness of the exemptions in the
8 marketplace and whether the rationale behind
9 any of these exemptions should be revisited.

10 KCS experience shows that the
11 intermodal and boxcar exemptions have allowed
12 us to compete more effectively. These
13 exemptions have given us the flexibility to
14 improve the use of our assets and to price our
15 services according to market conditions,
16 equipment availability, and customer demand.

17 As a result of this market
18 flexibility and several other factors,
19 including our acquisition of Kansas City
20 Southern Dominico, our share of intermodal
21 traffic has grown substantially and is now one
22 of our fastest growing sectors of all of our

1 business.

2 Okay. As this slide shows, you
3 can see over the recent years, the past three
4 years, our intermodal traffic has grown by
5 about 40 percent since 2008, and if you took
6 this slide back further, you would see
7 tremendous growth from virtually no intermodal
8 traffic to where we are today. In spite of
9 this growth, our market share of intermodal
10 traffic, particularly for cross-border
11 traffic, is still quite small, and I'll talk
12 more about that in a moment.

13 Similarly, over the past few years
14 there has been a resurgence in transporting
15 commodities in boxcars made possible by a
16 higher percentage of round-trip back-hauls and
17 other equipment utilization improvements made
18 possible through the exemption.

19 As this slide shows, our boxcar
20 traffic has grown considerably over the last
21 few years, and this growth has been made
22 possible to a large extent through back-hauls

1 and other equipment practices, as I mentioned
2 earlier. The existence of the exemption has
3 allowed us to price our boxcar traffic to
4 encourage utilization of equipment that would
5 otherwise move empty back to its head-haul
6 point of origin.

7 As an example, we adjust rail
8 rates frequently to respond to truck rates at
9 some of the paper mills that we serve. As
10 trucks bring inbound scrap into paper mills,
11 they are constantly quoting spot or market
12 prices to get the outbound loads.

13 By being able to respond to these
14 market changes, we have been successful in
15 security a higher proportion of round-trip
16 moves through similar pricing strategies.
17 This enables us to significantly reduce empty
18 miles and improve our overall return on
19 investment per boxcar.

20 If you look at this slide, you can
21 see the red line at the top measure loaded
22 boxcar miles, and the yellow line is empty car

1 miles. We look at this for many different
2 types of equipment, and you can see there is
3 a divergence in those two lines, so our goal
4 is to manage our business this way to improve
5 the proportion of loaded to empty miles.

6 It is interesting to note in their
7 comments Packaging Corporation of America
8 points to the fact that they often have
9 difficulty reloading boxcars and that some of
10 the Class I railroads serving their facilities
11 are unwilling to or willing to forego this
12 back-haul revenue.

13 This has not been our experience,
14 and, indeed, at many of the paper plants we
15 serve we have an active boxcar reload program,
16 and we believe if boxcars were to be
17 reregulated, Kansas City Southern would likely
18 lose the ability to pursue these reloads at
19 the mills, because we would not be able to
20 respond to market conditions as rapidly and
21 that we would lose some of this traffic to
22 truck.

1 The return on the investment on
2 our boxcar fleet would more likely drop to the
3 point where we would need to reduce our fleet
4 or possibly considering withdrawing from some
5 of these markets.

6 PCA's comments actually support
7 one of the points made by Kansas City Southern
8 in our testimony, and that is that the Board
9 should not assume that all shippers and
10 railroads share the same practices with
11 respect to the effectiveness of these
12 exemptions.

13 Some of our greatest successes in
14 generating growth in loaded boxcars has been
15 due to our concentrated efforts to develop
16 reloads, improve the way we utilize our fleet,
17 reduce empty miles and the costs associated
18 with repositioning equipment.

19 With respect to the second
20 question, whether the rationale underlying the
21 exemptions remains valid in today's
22 marketplace, we believe the answer is yes.

1 The exemptions were granted on the basis that
2 government regulation was not needed, because
3 the railroad's pricing and services would be
4 constrained by competition provided by other
5 modes, especially trucks, as well as
6 competition from other railroads.

7 These reasons remain valid today.
8 Indeed, Kansas City Southern faces more truck
9 and rail competition than ever before. This
10 can be shown empirically by examining KCS's
11 market share data in a few commodity groups.

12 As example, one of our fastest
13 growing businesses is international intermodal
14 traffic moving through the Laredo, Texas,
15 gateway between the United States and Mexico.
16 KCS has a small market share when compared to
17 trucks and the containers being interchanged
18 with other railroads.

19 As you can see on this slide, the
20 blue line, these re percentages. The blue bar
21 represents truck traffic crossing the border.
22 The yellow line is traffic that we interchange

1 with other railroads at Laredo.

2 The red line -- there is a red
3 line on this chart. You can barely see it,
4 but it's traffic that we actually move on both
5 sides of the border on the Kansas City
6 Southern network.

7 While we are competing hard for
8 this cross-border franchise to grow, our
9 market share continues to be small. Trucks
10 continue to dominate this market. At most of
11 the paper mills that we serve, we also face
12 competition from other modes, including truck,
13 and from other railroads.

14 Again, likewise for intermodal
15 traffic, KCS faces intense competition from
16 other railroads. This slide shows our
17 international intermodal network with the
18 icons representing the locations where we have
19 intermodal facilities.

20 This next slide shows those same
21 markets in the United States where we have
22 intermodal facilities, and this highlights

1 that in every one of the markets that we
2 operate our competitors also have intermodal
3 facilities. In addition, in some cases there
4 are three or four competing rail intermodal
5 facilities in the same market.

6 In addition to that, there would
7 be multiple truck terminals in all of these
8 markets. The presence of these other
9 terminals means that the shippers have
10 numerous choices for their trailer and
11 container traffic.

12 Competition is further intensified
13 in that the numerous third-party intermodal
14 marketing companies and long-haul trucking
15 companies have all established relationships
16 with other railroad competitors and provide
17 competitive alternatives to KCS's service.

18 As someone who is frequently in
19 contact with shippers of all size, I can
20 certainly confirm to you that the competition
21 facing KCS for the movement of intermodal and
22 boxcar traffic is intense.

1 The fierce rail and truck
2 competition that justified the boxcar and
3 intermodal exemptions remains powerful
4 constraint on our pricing and service today.
5 This competition has intensified as the IMC
6 and third-party logistics companies have
7 matured since the adoption of the exemptions,
8 and, of course, competition with other
9 railroads continues to be intense.

10 Finally, I'd like to comment on
11 the next steps to be taken by the Board.
12 Because the exemptions have an effective --
13 have been an effective competitive tool, we do
14 not believe this Board needs to take any steps
15 further to revoke, either in whole or in part,
16 any of the exemptions covered by this
17 proceeding.

18 Instead, the Agency should
19 continue with its existing policy of reviewing
20 complaints about exempt traffic on a case-by-
21 case basis and, where appropriate, revoking
22 the exemption solely to the extent necessary

1 to review and rule on those individual
2 situations. If the Board does intend to take
3 further steps, it needs to consider the
4 different impacts that revocation could have
5 on railroads of different sizes.

6 As an example, again, in PCA's
7 written testimony, that the industry has not
8 made efforts to develop boxcar reloads. I
9 can't speak for the rest of the industry, but
10 that has certainly been not the case at Kansas
11 City Southern, as we have made significant
12 efforts to develop such reloads.

13 KCS is especially concerned about
14 the potential unintended consequences to it
15 and other smaller railroads that could result
16 from wholesale revocation of these. From the
17 testimony of the American Short Line &
18 Regional Railroad Association, I understand
19 that they share this view, as well.

20 As pointed out in their comments
21 and ours, if not done carefully, any efforts
22 to the Board -- by this Board to undo

1 exemptions could actually have the unintended
2 consequence of harming the smaller railroads
3 whose shippers have benefitted from the
4 service and competitive alternatives developed
5 as a result of the exemptions.

6 Thank you for this opportunity,
7 and I'd be happy to answer questions at the
8 appropriate time.

9 CHAIRMAN ELLIOTT: Thank you, Mr.
10 Ottensmeyer. We will now hear from Norfolk
11 Southern Railway Company. Mr. Lawson, you
12 have ten minutes.

13 MR. LAWSON: Thank you. My name
14 is David Lawson, Vice President, Industrial
15 Products for Norfolk Southern. Mr. Chairman,
16 Vice Chairman, Commissioner Mulvey, appreciate
17 the time and also the opportunity to come and
18 speak before you today.

19 In my 23 years of experience at
20 marketing rail services, I have never heard a
21 customer mention, much less complain about,
22 the existence of any commodity exemptions or

1 class of service or equipment. Many of the
2 filings that are requesting a review or
3 revocation of the commodity exemptions are
4 very general and lack specifics.

5 They suggest that the railroads
6 have enjoyed a brief, relative brief period of
7 financial viability and now impose -- now want
8 to impose the very regulations that, quite
9 frankly, caused the very need for Staggers.

10 What I can say is based upon my
11 experience is that there is no general need
12 for regulation of any kind to prevent the
13 abuse of market power by railroads with
14 respect to the exempt commodities due to the
15 pervasive competition from rail, trucks,
16 barge, product, geographic, and source
17 competition.

18 In Norfolk Southern's experience,
19 the transportation markets for exempt
20 commodities like cement, paper, and forest
21 products, as well as for intermodal traffic,
22 are highly competitive among railroads and

1 between railroads, as well as other modes.

2 I'll share with you one example in one of our
3 markets, our paper markets.

4 Norfolk Southern serves over 50
5 paper mills. Two-thirds of those paper mills
6 are located in the southeastern part of the
7 country. As many of us all know, the Florida
8 market is a huge consuming market but doesn't
9 produce a lot in terms of outbound
10 opportunity.

11 Every day that we compete in the
12 southeastern part of our country serving these
13 paper mills, we're either competing against
14 our Eastern Rail competitor, or in most cases
15 it's against the trucks who are coming out of
16 Florida looking to find back-haul
17 opportunities and thus competing with every
18 opportunity that we have. It's a fiercely
19 competitive market, the paper market.

20 I spent 11 years, seven of which
21 were in Detroit, managing the accounts of Ford
22 and General Motors in marketing our

1 transportation services to the automotive
2 industry, and I do have to tell you that we
3 find that the comment about the retaliation or
4 the threat of retaliation with regard to
5 dealing with the automotive manufacturers, in
6 our opinion, baseless and reckless to make
7 that kind of a comment without any examples.

8 Having dealt with Ford and GM for
9 the number of years, I can assure you there is
10 no concern about the fear of retaliation with
11 Ford against the railroads or specifically
12 with Norfolk Southern.

13 The intramodal competition of
14 finished vehicles is also highly competitive.
15 First of all, the destination facilities and
16 rail cars to finish -- to haul finished
17 vehicles to the unloading facilities or ramps,
18 as we refer to them, are typically owned and
19 have been capitalized by the railroads, not
20 the haul-away carriers.

21 They are typically bid out by the
22 auto manufacturers, and the railroads

1 intensively compete for this business.

2 Additionally, as far as sole-served assembly
3 plants, I'd like to share with you a couple of
4 examples where there is truly intramodal
5 competition.

6 More than 25 years ago, our
7 railroad, our company built a loading facility
8 in Detroit. We refer to it as Melfindale on
9 the outside of Detroit. That facility was
10 built to attract vehicles that were
11 manufactured in Canada and Detroit area
12 assembly plants that are trucked away from
13 those assembly plants to that facility to be
14 loaded direct on the rail.

15 We also have other examples, for
16 example, in Doraville, Georgia, an assembly
17 plant that GM had on the outskirts of Atlanta.
18 One of our competitors built a auto loading
19 facility about 20 miles outside of the
20 assembly plant and trucked every one of the
21 assembly -- every one of the vehicles to that
22 load-out facility 20 miles away from the

1 assembly plant. This was an assembly plant
2 that Norfolk Southern served directly.

3 Another example where this existed
4 is in Norfolk, Virginia, where Ford Motor
5 Company had a pickup truck plant there.
6 Again, another competitive plant offsite load-
7 out facility was built not far from the
8 assembly plant.

9 For a number of years, Ford
10 trucked those vehicles to our competitor's
11 site. After the termination of that contract,
12 Norfolk Southern built another facility in
13 order to truck those vehicles away.

14 So the examples that we have, and
15 there are others, as well, that exist in the
16 automotive marketplace as it relates to
17 finished vehicles, are such that there is
18 truly intramodal competition in the automotive
19 marketplace.

20 I'd also like to turn and just
21 make a comment about auto parts. The auto
22 parts market is a highly truck-competitive

1 market.

2 There was mention earlier in
3 testimony today about certain components of
4 auto parts where the rails enjoy a larger
5 share and had to do with, I believe trucks not
6 being competitive in certain markets as it
7 related to engines, transmissions, frames.
8 There's a simple reason for that.

9 The reason for that is that those
10 components are loaded into highly customized
11 racks that require a round-trip move. The way
12 we price our services is such that that move
13 on the head haul to haul the parts from the
14 component plants to the assembly plant include
15 the return of those racks.

16 The motor carriers see that as a
17 two-way move and price it as two separate
18 moves. The equipment that we put into these
19 components plants are dedicated to those
20 component plants to haul those specific parts
21 in these highly customized containers from the
22 component plants to the assembly plants and

1 then the empty returns of those racks right
2 back to the component plant.

3 It's the same thing on the frames.
4 That's the simple reason as to why that's a
5 market that we have participated in for so
6 many years.

7 The closure of Detroit's big three
8 and the outlying assembly plants has
9 concentrated the remaining parts flows for the
10 short-haul and near-Michigan markets, which is
11 also highly truck-competitive.

12 NS would respectfully suggest that
13 the proper course of action for the Board to
14 take as a result of these hearings would be to
15 commence proceedings to exempt additional
16 commodities from unnecessary regulation, as
17 suggested in Norfolk Southern's comments.
18 Otherwise, we think this inquiry should be
19 terminated. Thank you for your time.

20 CHAIRMAN ELLIOTT: Thank you, Mr.
21 Lawson. Now we'll hear from Union Pacific
22 Railroad Company. Mr. Butler?

1 MR. BUTLER: Good afternoon. Good
2 afternoon. My name is Eric Butler, and I'm
3 the Vice President and General Manager of the
4 Industrial Products Business for Union Pacific
5 Railroad.

6 Thank you for the opportunity to
7 testify before you today and express my view
8 of the current exemptions and how I believe
9 they assist me in being responsive to my
10 customers in what is a very competitive
11 marketplace.

12 Today we have the ability to offer
13 creative, rapidly responsive solutions to
14 customer requests for transportation options.
15 During any given week, my team is responding
16 to 125 new requests or proposals for service
17 from customers.

18 In 2010, my median response time
19 to those customer requests was one day, with
20 the majority of my customers getting a
21 response from us within three days. Naturally
22 speaking, some we could respond to

1 instantaneously. Others may take even a week
2 or longer due to the complexity and the need
3 to be creative, to be competitive.

4 However, with this rapidly
5 changing marketplace it is imperative that we
6 respond quickly. I believe a revocation of
7 the exemptions will cause an adverse impact on
8 my ability to be responsive to this
9 marketplace.

10 One indication of the
11 competitiveness of my business is that less
12 than ten percent of the proposals that I get,
13 customer inquiries that I get, result in
14 business shipped on Union Pacific. I define
15 competition as the fact that 90 percent of the
16 customer transportation requests that I get,
17 the customer finds another, more suitable,
18 more competitive option.

19 I operate in a very competitive
20 business environment. Approximately ten to 12
21 percent of my business churns annually, and
22 not only do I have effective rail competition,

1 truck competition, and barge competition, but
2 I'm also subject to product source and
3 geographic competition.

4 In the few remaining moments that
5 I have, I want to share a couple of on-the-
6 ground stories and examples of the competition
7 that I face on a daily basis. My aggregate's
8 a rock business. It's perhaps one of the most
9 competitive markets out there.

10 While Union Pacific is extremely
11 proud of our aggregates franchise and the fact
12 that a number of customers have chosen to open
13 facilities on our network, rail competition is
14 fierce, and rail still has a very small market
15 share versus truck in the Texas aggregates
16 market, my largest market.

17 We estimate that trucks have 75 to
18 85 percent of the total Texas aggregates
19 market share. There is also strong barge
20 competition, particularly barge shipments from
21 the Yucatan Peninsula and Mexico, going to the
22 heart of Houston and the heart of South Texas.

1 Texas Crushed Stone in Georgetown,
2 Texas, who is also a respondent in this
3 hearing, is a great example of the significant
4 competition in the aggregates market. They
5 are located on a short line that connects to
6 both the PU and the B in Santa Fe.

7 Not only is there effective rail
8 competition, and I have lost market share to
9 my Western Rail competitor, but there is also
10 significant trucking competition from other
11 quarries in the same geographic area.

12 We have worked hard to regain the
13 portion of business that we have lost from
14 them, but they have consistently identified
15 that they have had more other competitive
16 options.

17 Another example of the fierce
18 competition in the marketplace involves
19 another respondent in this hearing, Holcim
20 Cement. In 2009, they opened a four million
21 ton cement facility in St. Genevieve,
22 Missouri, which is estimated to be almost

1 twice as large as any other cement facility in
2 U.S.

3 This one facility we estimate by
4 our internal estimates can meet half the
5 entire cement requirements for the states of
6 Kansas, Missouri, Minnesota, Nebraska, and
7 Arkansas.

8 It is our understanding that when
9 this facility was designed and opened, which
10 is closed on the B end, it was designed to
11 have the majority of the shipments barged up
12 and down the Mississippi or the Missouri
13 Rivers and a minority of it railed. However,
14 due to the softness of the housing market and
15 the cement market, Holcim has now broadened
16 their market reach to increase the utilization
17 of this large facility.

18 They are active with their
19 transportation and product pricing options.
20 They have entered into markets further west
21 than our territory from this one facility and
22 even into Texas, and, as a result, they have

1 taken market share from other UP customers.

2 This is a great example of the
3 source and geographic competition that we face
4 in our markets. As a result, between 2008 and
5 2010, my cement business has experienced a 15-
6 point loss in market share just predominantly
7 due to this one situation.

8 My final example involves a very
9 creative solution we provided to a steel
10 manufacturer moving long-haul steel products
11 by truck from Chicago to Mexico. We designed
12 a multi-modal product using truck, transload,
13 and rail that had a transit time from Chicago
14 to Mexico within two days of the team truck
15 transit time, and it was priced 50 percent
16 below the truck rates.

17 Despite this, we were still only
18 able to gain about half the market share, the
19 truck market share from this customer moving
20 truck long-haul to Mexico. As you can see,
21 there are a lot of factors, and they're in
22 fierce competition each and every day.

1 I've learned in my 25 years in the
2 railroad business and in my seven years as a
3 senior commercial office that having the
4 ability to design responsive, flexible,
5 creative, and unique transportation solutions
6 for individual customers is critical to being
7 competitive in this multi-modal environment.

8 Supply chains are rapidly
9 changing, and in order to ensure the viability
10 of rail, the viability of rail transportation
11 for my customers, I likewise believe we need
12 the ability to remain flexible, creative, and
13 responsive and provide unique solutions for
14 individual customs, and I believe that the
15 current regulatory structure allows us to do
16 so. Thank you for your time.

17 MS. KREHBIEL: Good afternoon. My
18 name is Julie Krehbiel. I'm the Vice
19 President and General Manager for the
20 Automotive Business Team at Union Pacific, a
21 position I've held for close to six years, and
22 I appreciate your time today.

1 I'm here to talk about the
2 movement of finished vehicles and automotive
3 parts via rail and other modes of
4 transportation. A few of the automotive
5 shippers have suggested that we are not facing
6 competition in these markets, so I want to
7 talk about the competition that we are facing
8 and how it's changed the way that we do
9 business.

10 We see competition really in three
11 key areas, three key modes: truck and rail,
12 which I'll talk more about, but also in
13 vessel. The vessel competition is
14 specifically related to the movement of
15 finished vehicles.

16 There are finished vehicles that
17 could off-load on the West Coast and move rail
18 inland. Instead, they go around the horn and
19 off-load on the East Coast.

20 We also see vessel competition in
21 short-range markets such as Mexico to the East
22 coast. Obviously, vessel has got a

1 significant cost advantage over rail, so we
2 focus on our speed to market and our damaged
3 redelivery to win this business from vessel.

4 The truck competition really is
5 pervasive for both finished vehicles and
6 automotive parts. They offer some obvious
7 advantages, speed, flexibility, access to more
8 locations, components that are very
9 attractive, especially now given the tight
10 inventory situations that the automotive
11 customers are facing for both vehicles and
12 production parts.

13 You would expect that competition
14 in short-range markets, but we also see it in
15 very long-haul markets that may surprise you.
16 We compete fiercely for automotive parts that
17 move between the Upper Midwest and Mexico. In
18 fact, automotive parts move 85 percent by
19 truck, a clear indication of the competitive
20 level that we face.

21 In the longer range vehicle
22 markets we have fought for years to try to

1 move vehicles via rail from the East Coast as
2 far west as Colorado and Utah, and they have
3 failed repeatedly. The vehicle market on the
4 used side, over 99 percent of that market
5 moves long-haul truck, again a testimony of
6 the competitive level that we face.

7 It's important that we are able to
8 provide a premium service and to do it at a
9 savings to truck. In order to ship and
10 convert traffic from truck to rail, our
11 customers expect significant savings.

12 Certainly, the rail competition is
13 very fierce. We compete head-to-head with the
14 Burlington and Santa Fe in the western two-
15 thirds of the United States.

16 On the parts side, that business
17 can move easily, obviously, via truck but also
18 via rail. Finished vehicle side, we compete
19 head-to-head by offering competing
20 distribution facilities in every key major
21 geographic market in the West, enabling
22 customers options.

1 It is -- we also have another
2 fierce competitor, of course, in the Kansas
3 City Southern, specifically on movements of
4 vehicles and parts to and from Mexico, and in
5 our business, Union Pacific, that's
6 significant. It's over 40 percent of my
7 annual volume.

8 I also wanted to talk just for a
9 minute about the issue the Alliance raised
10 about the sole-served facilities contending
11 that because of rail mergers that the number
12 of sole-served facilities has increased, and
13 the facts just don't bear it out.

14 There has been no facility that
15 has lost an option because of a merger. If
16 any facility is sole-served, it's because it
17 was either that way before the merger or has
18 located since.

19 In fact, if you look at the most
20 two recent plants built in the U.S., one of
21 those manufacturers chose to locate on a
22 single-serve facility, and I would contend

1 they did that for the same reason that I would
2 do it, because I think there is competition
3 there.

4 It is not unusual, as Mr. Lawson
5 indicated, for a manufacturer to choose to
6 truck away from a serving railroad to get to
7 a competing railroad. In fact, that's how we
8 served the Oklahoma City plant for a number of
9 years before it closed.

10 It's obvious that all this
11 competition has changed the way that we do
12 business. We have invested over \$688 million
13 in the last 12 years just in automotive.
14 That's either in equipment, facilities, or
15 technology, all focused at improving our
16 service liability and ensuring that we do it
17 in a damage-free basis.

18 We invest over \$33 million
19 annually in equipment. We have the innovative
20 auto-plex, which enables us to move either bi-
21 levels, which hold SUVs, or tri-levels, which
22 hold vehicles, with the same investment

1 dollars. We patented that technology and made
2 it available to other railroads.

3 We're very focused on offering a
4 premium service that's as close to truck as we
5 can. We have taken 7/10 of a day out of our
6 delivered vehicle transit time, almost a 12
7 percent reduction last five years, and in 2010
8 we handled over a quarter of a million of
9 loads of production parts, over 95 percent on
10 time, a testimony that our customers know we
11 can support their just-in-time networks.

12 So, in summary, it's our customer-
13 focused investment, our ability to offer
14 premium service at competitive rates, and our
15 customers recognize that. In 2010, they rated
16 us a 95 out of 100 in customer satisfaction.

17 This investment is very specific
18 to automotive, and it's a testimony that we
19 don't take our customers for granted. In
20 fact, I only have five customers, and they
21 represent over 90 percent of my revenue base.
22 Obviously, I can't take them for granted.

1 We feel this investment is
2 directed at ensuring that we offer premium
3 service, and we do not believe that regulation
4 will do the same. In fact, we think it
5 ultimately will deter investment going
6 forward. Thank you.

7 CHAIRMAN ELLIOTT: Thank you very
8 much, Mr. Butler and Ms. Krehbiel. As far as
9 questions, Vice Chairman?

10 VICE CHAIRMAN NOTTINGHAM: Thank
11 you, Mr. Chairman, just a couple. Mr. Lawson,
12 thank you for your remarks. You mentioned
13 near the end that you would support our
14 consideration of additional exemptions.

15 I guess that begs the question do
16 you have any nominations as to what types of
17 commodities ought to be added to the exempt
18 commodity list or in your experience any
19 particular direction you want to point our
20 attention to as far as looking at additional
21 opportunities for exemptions?

22 MR. LAWSON: Yes, sir. We

1 mentioned the specific commodities in our
2 filing, but they would include industrial sand
3 and hydrostethyl alcohol, phosphate fertilizer
4 solutions, and asphalt, and the reasons for
5 that are fairly simple.

6 We see, based on our experience,
7 that there is intense market competition for
8 these commodities, and there seems to be
9 enough capacity and opportunities for us to
10 compete more effectively, so we would ask the
11 Board to take that under advisement.

12 VICE CHAIRMAN NOTTINGHAM: Thank
13 you. Mr. Butler, thank you for being here.
14 It's a pleasure to see you. I'm not used to
15 seeing you on the witness stand.

16 We worked closely together, along
17 with my colleagues, on the Rail Shipper
18 Transportation Advisory Commission, which many
19 people know as the congressionally chartered
20 In-Statute Advisory Commission that does
21 really outstanding work.

22 Eric, you've been a leader for

1 years now on that advisory commission. I just
2 want to say thank you. What you've brought to
3 the table there day in, day out at every
4 meeting has been just tremendously useful to
5 our agency but also to shippers. I've
6 received many compliments from small and not-
7 so-small shippers about the usefulness and
8 helpfulness of your contributions to that
9 committee, so thank you.

10 Thank you to your railroad for
11 making you available at no cost to the
12 taxpayer but at some cost to -- at some great
13 cost to UP as you aren't able to do your
14 regular job and you're with us.

15 That begs a question. Are you --
16 with this group here, who's running the
17 railroads, I guess I should say, today, and
18 are we going to have to see a productivity
19 adjustment for the lost productivity today?

20 MR. BUTLER: Mr. Chairman, maybe
21 we need to do some kind of special proceeding
22 on that, because we've got an awful lot of

1 senior people here to help us understand the
2 history and current daily realities of what
3 the exemption process has meant to shippers
4 and to railroads.

5 Let's see. I think, really, I'm
6 going to pause there and let my colleagues
7 throw out some questions. Mr. Chairman, I'll
8 send it back to you.

9 CHAIRMAN ELLIOTT: Sure. Now
10 we'll go to the Commissioner.

11 COMMISSIONER MULVEY: Thank you.
12 We're looking to see what the revenue-to-
13 revenue cost ratios are for the commodities
14 you suggested.

15 I found all your testimonies
16 interesting, but they range from how wonderful
17 intermodal is, how great Staggers has been,
18 that boxcar reloads are still important, and
19 that there is plenty of competition,
20 intermodal competition and competition in
21 general. All of that is true, and I think
22 that there is no disagreement between anybody

1 in this room on those facts.

2 The question, I think, though, is
3 whether there are any commodities at all where
4 there has been enough change in the
5 competitive environment that it might be a
6 valuable exercise for the Board to look and
7 see whether or not the commodity exemption put
8 forward back in 1979 and in the eighties are
9 as sensible as they are today?

10 The other question I have is why
11 are the exemption process or lack of process
12 so critical to the railroad's ability to meet
13 competition?

14 It strikes me that much of what
15 the railroads do and much of how the railroads
16 can respond to trucking competition, can be
17 done without the exemptions. Finally, how
18 much traffic, after all, are we really talking
19 about?

20 It is true that most of the
21 traffic either moves under contract or is well
22 below the threshold of 180 percent revenue-to-

1 variable-cost ratio. That traffic is assumed
2 competitive.

3 It would not be brought to the
4 Board in terms of a rate or service case, so
5 we're probably only talking about a small part
6 of the traffic, but I would like to be
7 educated as to specifically why the exemption
8 process is so critical to the ongoing success
9 of the railroads. Anybody? The whole group.
10 Anybody can answer that question.

11 MR. BUTLER: Yes, Commissioner
12 Mulvey, I'll take a shot, and let me just give
13 my appreciation to those nice comments made by
14 the Vice Chair. I have enjoyed my last five
15 years working with the STB and RSTAC. This is
16 my last year, and I will miss the meetings,
17 but I certainly have enjoyed the great
18 dialogue that we've had in the meeting.

19 Commissioner, you asked several
20 questions. One question, I believe your first
21 question, was dealing with the flex -- or
22 which commodities would we believe, and I

1 would just say, speaking for my industrial
2 products business, I am not aware of any
3 commodity that I am responsible for that does
4 not have significant fierce competition,
5 whether it's rail, whether it's truck, whether
6 it's barge, whether it's source product,
7 geographic competition.

8 Sitting here today, I can't think
9 of one that does not have significant
10 competitive factors. The reason why I quoted
11 some of the statistics that I quoted was it is
12 interesting to me how many requests for
13 transportation proposals and services we get,
14 and we work competitively to go after them.

15 I have a great team that works
16 every day, and still there's a very small
17 percent, less than ten percent -- the number
18 is actually closer to five than it is ten --
19 of those requests that I win, so to me that
20 suggests that there is significant
21 competition.

22 When you asked the question about

1 the exemption and how I believe that will
2 impact, I believe, looking at the regulatory
3 regime in the past, that when you look at the
4 publication requirements and the notification
5 requirements --

6 I have many customers that want us
7 to do quick -- for lack of a better term, I'll
8 call it spot deals, quick-hit deals that they
9 want it to be quick and deal with the project,
10 deal with an issue, and my understanding of
11 the previous construct, I'm not sure we'd be
12 able to deal with those very effectively.

13 COMMISSIONER MULVEY: Anybody
14 else? You talk about the way things were
15 before the exemption process, and I think that
16 that's something that people seem to think
17 that we're talking about some sort of
18 revocation of all the exemptions.

19 I think what the Board was looking
20 to see whether or not the exemptions were
21 equally valid as they were before for all
22 commodities and all traffic types, rather than

1 a blanket revocation, going back to the pre-
2 Staggers case where every commodity was
3 regulated and, I think, as the railroads and
4 most economists have rightfully pointed out,
5 we over-regulated to the detriment of our
6 nation's transportation system.

7 The question really is are there
8 some commodity exemptions that should be
9 examined. We did have one testimony, which
10 I'm sorry he is not here today, and I don't
11 want you to go back and look for yourself,
12 that made a good case. But it has to be on a
13 case-by-case basis, and it needs to be
14 factually driven.

15 Of all the pleadings that we got,
16 only one of them really had the kind of facts
17 and the kind of analysis that we would be
18 looking for, and we were going to consider
19 whether or not an exemption should continue.

20 Clearly, there are many, many
21 products where either they were moving under
22 contract or the ratio was such that it's clear

1 that there is very, very intense intermodal
2 and intramodal competition.

3 The other point I wanted to raise
4 was we had these shares of traffic, shares of
5 revenue, and shares of tons, and we all know
6 that truck dominates tons and certainly
7 dominates revenues, and pipelines also are
8 very big on tons.

9 When it comes to ton miles, the
10 railroad's market share is even greater than
11 the trucks, suggesting that when you talk
12 about long-haul movements, especially long-
13 haul movements of bulk commodities, rails do
14 have a large share of the market.

15 I asked this question before, and
16 that is what would you think about looking at
17 the exemptions and perhaps removing the
18 exemptions for certain distance movements, as
19 opposed to the removal of an exemption for any
20 particular commodity? For a commodity at a
21 certain distance, where there really isn't
22 effective competition. Would anybody want to

1 care to comment on that?

2 MR. BRANSCUM: I'll address that.
3 I think there is a misconception out in the
4 marketplace about market share in intermodal,
5 anyway, on long haul. To put it in
6 perspective for you, let me give you some
7 numbers.

8 In the western two-thirds of the
9 U.S., you know, the BNSF and the UP territory,
10 BNSF moves about four and a half million
11 intermodal shipments a year, and the UP number
12 I think is about four, maybe a little less
13 than four million, but yet you have to dissect
14 those numbers to really understand share.

15 About half of that, actually, a
16 little more than half of that, maybe 60
17 percent of it, is international freight coming
18 into the West Coast, and I think we
19 demonstrated that that's all subject to
20 competition going to the East Coast, and that
21 could even get greater after 2014, when the
22 Panama Canal is widened.

1 So you set that aside, and then
2 you have roughly 40, 45 percent of those
3 volumes left, which is domestic transportation
4 that's probably going to exist in the western
5 two-thirds of the U.S.

6 So that would mean BNSF handles
7 about two million shipments a year, UP about
8 one and a half. I'm sorry. I don't know what
9 number I threw out for BNSF. It's about two
10 million a year and UP about one and a half or
11 maybe a little more than that.

12 There's been some studies recently
13 looking at truck share in existing long-haul
14 intermodal lanes that are offered by BN and
15 UP, and the number is somewhere between seven
16 and ten million truckloads that are still on
17 the highway.

18 So we have -- looking at it from
19 that perspective, the share could be as low as
20 20 percent, so I think there is still extreme
21 competition from the trucking industry in the
22 long-haul markets.

1 COMMISSIONER MULVEY: Is it true
2 that most of those truck movements consist of
3 a single container, whereas a lot of what
4 you're taking and UP is taking are multiple
5 cars that are going to large distribution
6 centers, Wal-Mart for example.

7 So it really depends upon the
8 nature of the shipment, and if it's a multiple
9 car shipment, it's more likely to go by rail,
10 but if it's a single car shipment, it's more
11 likely to go by truck? Would that be fair?

12 MR. BRANSCUM: I'm not sure what
13 you're referring to when you say multiple car.
14 Are you talking about multiple stops?

15 COMMISSIONER MULVEY: Multiple
16 containers. In other words, if you have a
17 ship coming from China and it's got 100
18 containers on it that are bound to a Wal-Mart
19 distribution center in Arkansas, those would
20 very likely go on a single unit train, whereas
21 if you have one or two containers going to a
22 single warehouse someplace, say, in Nebraska,

1 it's more likely to go by truck?

2 MR. BRANSCUM: No. You recall I
3 disregarded the international, saying it's
4 competitive to all water service, so I wasn't
5 counting that, so if you count --

6 A lot of that would move on unit
7 trains out of the ports either in California
8 or the Pacific Northwest to destinations
9 across the U.S., but in the domestic markets,
10 which is represented by the seven to ten
11 million loads that I believe are still on the
12 highway in our existing lanes, that, a lot of
13 that is single truck movements.

14 COMMISSIONER MULVEY: Of those
15 seven to ten million trucks that are still on
16 those highways, are they averaging the same
17 distance for those hauls?

18 MR. BRANSCUM: Yes, they're in the
19 same exact lanes that would offer service
20 today.

21 COMMISSIONER MULVEY: The same
22 market. Okay. Thank you.

1 CHAIRMAN ELLIOTT: Just to follow
2 up on Commissioner Mulvey's question regarding
3 flexibility, the way I understand it is some
4 of the problems with flexibility were
5 eliminated during ICTA, eliminating the
6 requirement to file the contracts and tariffs.
7 But maybe one of the reasons that people can't
8 be as flexible without the exemptions is the
9 ability to raise the rates at a moment's
10 notice.

11 I was wondering with -- and I'm
12 not aware of any other hindrances, so if there
13 are any other hindrances, I'd like to hear
14 them, but I was wondering if the Board looked
15 at it in that way, if instead of making it a
16 full revocation -- this is obviously a
17 hypothetical -- and just kept that exemption
18 with respect to whether you can raise or lower
19 a price on the spot, you know, quickly without
20 notice, if that would eliminate some of the
21 concerns that you have regarding flexibility.

22 MR. BUTLER: I think if you look

1 at some of the respondents and some of the
2 customer respondents, they gave some other
3 factors in the filings, the written filings,
4 including the concern where customers desire
5 to have very special, unique deals that
6 perhaps the perspective is we were not able to
7 construct some of those deals in the previous
8 environment, as we can when you have
9 exemptions, and I think some of -- at least,
10 one notable customer response gave some
11 examples of those types of things.

12 CHAIRMAN ELLIOTT: That's all I
13 have. Do you have anything else?

14 VICE CHAIRMAN NOTTINGHAM: Thanks.
15 I just wanted to follow up on a question I
16 believe I asked Mr. Hamberger earlier, and he
17 kind of referred me to this panel, so I'll ask
18 it here.

19 What type of contractual or
20 contract-like terms do you offer customers
21 when they explain that time is important to
22 them, that they're in the just-in-time

1 delivery or inventory business, and they'd
2 like to do business with the railroad, but
3 they've got to have some dispute resolution
4 process if the train doesn't show up or if a
5 surcharge surprisingly appears on a bill?
6 What, for any of you, what types of dispute
7 resolution mechanisms or terms are you able to
8 offer, to the extent you can talk about that?

9 MS. KREHBIEL: It's certainly an
10 automotive, you know, both from a vehicle
11 perspective, as well as production, parts.
12 Service is very important and our ability to
13 hit their service windows.

14 So although, you know, we can't
15 talk about specific terms and conditions, we
16 certainly have service commitments within the
17 contracts, and, actually, the business is at
18 risk if we don't meet those service
19 commitments. Then there's a process for
20 remedy within the contracts.

21 VICE CHAIRMAN NOTTINGHAM: I mean,
22 is it fair to say that -- I don't want to use

1 specifics, but I'll throw an example out, a
2 UPS, probably the biggest rail shipper in the
3 country.

4 If they need some type of dispute
5 resolution mechanism in a contract, you're
6 going to come up with something to get that
7 business. Is that a fair --

8 MR. BRANSCUM: Absolutely.

9 VICE CHAIRMAN NOTTINGHAM: -- fair
10 statement to make? What about a smaller
11 customer? I mean, is it only for the super-
12 mega customers that get that kind of
13 attention?

14 MS. KREHBIEL: No, I mean,
15 certainly from our perspective it's not really
16 the size of the customer. It's the
17 requirements of the business.

18 Production parts, no matter how
19 big a manufacturer you are, you have to have
20 them there to hit production. Otherwise, it's
21 very costly to you, so it's not really the
22 size of the customer as much as the

1 requirements of the business.

2 MR. BUTLER: Our focus is really
3 on customer service, so one example is we have
4 what we call a shutdown report, and regardless
5 of whether or not a customer has a contractual
6 service provision with us or not, any customer
7 that is at risk because of our transportation
8 service shows up on that report, which gets
9 widely disseminated, including up to our
10 Chairman.

11 We figure out what we need to do
12 to address that so that it doesn't happen, and
13 so our focus is really customer service,
14 because we want the long-haul customer
15 relationship and the long-term customer
16 business relationship.

17 MR. BRANSCUM: I might add to
18 that. In the intermodal world, you know, most
19 of the products that are handled in an
20 intermodal means are retail-related, so it's
21 fast-paced. The products have to get to
22 market.

1 So, given that, you know, there's
2 a whole range of remedies that are negotiated
3 in contracts, and it's very difficult in this
4 setting to talk about the specifics, but I can
5 tell you that there is always some form of
6 remedy, and, you know, the most extreme is
7 just simply to get off rail and go back to the
8 highway.

9 You know, within a given contract,
10 we might attempt to limit how much of that
11 could happen, but there is always that
12 solution, at least for some portion of the
13 traffic. The contracts in general are not
14 that long in term, so the ultimate solution is
15 always to go to the competitive options, which
16 is highway.

17 MR. BUTLER: Yes, and I would like
18 to make one more comment about the focus on
19 service and the remedies, and I would echo
20 what the Vice Chair said earlier this morning.
21 The STB's Office of Consumer Support is, I
22 think, a tremendous resource for the rail

1 shipping community.

2 I've been the recipient of a
3 number of inquiries from the STB, and I think
4 -- not I think, but I know according to my
5 understanding, every single one of those we've
6 resolved to the satisfaction of the customer,
7 the rail shipper, and the STB.

8 So, certainly, even if the
9 customer did not have a contractual remedy,
10 that is an option that's available, and I
11 believe, at least speaking for Union Pacific,
12 we've been very responsive to that.

13 VICE CHAIRMAN NOTTINGHAM: Thank
14 you. That's all I had, Mr. Chairman.

15 COMMISSIONER MULVEY: I just have
16 one other question. We talked about sole-
17 served shippers before or singularly served
18 shipper, whatever you want to call them.

19 One of the pleadings mentioned
20 that it's not so much that there was two
21 railroads serving us and now there's only one,
22 but rather that a railroad that was nearby

1 that wasn't competitive was taken over by
2 another railroad, and so you could still go to
3 the other station, but it's now owned by the
4 single railroad, and it's much, much more
5 difficult for the shipper to get to a
6 competitive railroad.

7 Where you might have had one 50
8 miles away, perhaps now the nearest one is 300
9 miles way and so not really accessible. So
10 would you accept that there has been a decline
11 in competition from that standpoint?

12 MS. KREHBIEL: You know, speaking
13 just to the automotive business, especially in
14 the finished vehicle side, I wouldn't. You
15 know, if you look at every major geographic
16 market, we have got competing rail heads with
17 the Burlington and Santa Fe for sure and
18 mostly also the case, yes, in some cases.

19 And even in markets that we're not
20 in like San Diego and the BN is, we compete
21 with a truck from our Los Angeles facility and
22 do very well, so, you know, I think, speaking

1 to finished vehicles, we compete head-to-head
2 across the board in the western U.S.

3 COMMISSIONER MULVEY: Thank you.
4 That's all I have.

5 CHAIRMAN ELLIOTT: I want to thank
6 the panel. We appreciate your presentations,
7 very informative, and we will move on to the
8 next panel, Panel V. That's the Shipper
9 Panel. Welcome, everyone. We'll begin with
10 Holcim, Inc. Is that correct? And you have
11 ten minutes.

12 MR. GIOVINAZZI: Thank you. Good
13 afternoon, Chairman Elliott, Vice Chairman
14 Nottingham, and Commissioner Mulvey. My name
15 is Tom Giovinazzi, and I am the Manager of
16 Rail Services at Holcim US, Inc., which I will
17 refer to today as Holcim.

18 I am here to speak about Holcim's
19 experiences as a captive shipper of an
20 exempted commodity. I commend the Surface
21 Transportation Board for undertaking this
22 much-needed review of categorical exemptions

1 from regulation.

2 I sincerely appreciate the
3 opportunity to express my concern over a
4 fundamental flaw in the current system, the
5 failure to protect all shippers from potential
6 market abuses. To be clear, Holcim does not
7 support returning to a time of expansive
8 government oversight of the rail industry.

9 Holcim acknowledges that
10 deregulation has benefitted rail carriers and
11 shippers alike and that efforts to reregulate
12 will ultimately prove detrimental to both
13 parties. Nevertheless, the current system is
14 inequitable and needs to be modified.

15 In particular, Holcim supports the
16 removal of commodity exemptions to allow for
17 a redress of the grievances encountered by
18 cement manufacturers, a right already afforded
19 to many other shippers under existing federal
20 law. Before I continue, I would like to
21 familiarize the Board with my company's
22 operations and its product.

1 Holcim is a leader in the domestic
2 cement industry capable of producing more than
3 13.5 million tons of cement and cementitious
4 products annually. Holcim has more than 1,800
5 employees and, in 2010, approximately \$1
6 billion in annual revenue.

7 Over the last decade, we have
8 invested in excess of \$2 billion to upgrade
9 and expand our U.S. facilities, including a
10 significant investment in our new Greenfield
11 plant in St. Genevieve County near St. Louis,
12 Missouri.

13 Our parent company, Holcim
14 Limited, is a global leader in the building
15 materials sector, present in around 70
16 countries. In 2009, the group supplied over
17 130 million tons of cement and almost 150
18 million tons of aggregates and generated \$19.4
19 billion in annual revenue.

20 Occupational health and safety is
21 a top priority for Holcim. As such, the
22 utilization of safe and eco-efficient

1 transportation options is central to our
2 business success and to ensuring the safety of
3 our employees, contractors, and visitors to
4 our operations.

5 Holcim serves customers in 44
6 states through network of 15 production
7 facilities and 59 distribution terminals. In
8 2010, roughly six and a half million tons of
9 cement moved from our manufacturing facilities
10 to these terminals for final distribution to
11 customers. Forty percent of that volume moved
12 by rail.

13 Additionally, Holcim relies
14 extensively on rail for the delivery of
15 critical raw materials and energy feed stocks
16 to our facilities to feed their continuous
17 operation.

18 Cement is a strategic building
19 material. It is the key component of
20 concrete, which is an environmentally
21 responsible building product used to construct
22 and repair a country's vital infrastructure,

1 the backbone of economic growth.

2 Nearly 50 percent of our product
3 has an end use in the public sector, in roads,
4 airports, bridges, and schools.

5 Unfortunately, our nation's cement
6 manufacturers are often confronted with the
7 high transportation rates and inconsistent
8 service that add to the cost of cement and
9 therefore to the cost of infrastructure, which
10 is ultimately shouldered by taxpayers.

11 This is largely attributed to the
12 fact that transportation by rail of cement and
13 several other important commodities used in
14 the manufacture of cement have been exempted
15 from protections under federal law since the
16 early 1990s.

17 In these exemption decisions, the
18 Interstate Commerce Commission noted that the
19 transportation of these materials was
20 competitive with intermodal, intramodal, and
21 geographic competition existing in many
22 markets. However, in the two decades since

1 these exemptions were imposed, much has
2 changed.

3 America's manufacturers
4 undoubtedly benefit from a robust
5 transportation network. However, given the
6 regional nature of the cement industry, there
7 are, unfortunately, limited competitive
8 transport options available to cement
9 manufacturers.

10 Average cement shipments are in
11 the range of 350 to 400 miles. However, truck
12 transportation is not economical much beyond
13 175 miles, and only three of Holcim's 15
14 production facilities have access to water
15 transportation for domestic shipments and then
16 only to select markets.

17 As a result, the cement industry
18 relies on rail transportation to move
19 approximately 50 percent of all shipments
20 between cement plants and distribution
21 terminals, according to 2006 U.S. Geological
22 Survey data. Not surprisingly, the railroads

1 are the only viable option for Holcim to
2 maintain a meaningful presence in many North
3 American markets.

4 It is therefore highly important
5 to our industry that the railroads provide
6 reliable, efficient, and cost-effective
7 service to enable manufacturers to meet demand
8 for their product, but more than 80 percent of
9 the country's cement plants are captive to a
10 single railroad.

11 Due to the absence of competition,
12 cement manufacturers may encounter
13 unreasonably high rail rates and may not
14 receive adequate service. Holcim is not
15 immune to these unfavorable market conditions,
16 as only three of our 15 production facilities
17 are serviced by more than one Class I
18 railroad, and the potential for competition at
19 these three facilities is negated by the fact
20 that all of our receiving terminals are
21 single-served.

22 With no competitive options and no

1 federal protection, captive shippers of
2 exempted commodities such as cement
3 manufacturers may face unrestrained shipping
4 costs and unreliable service and are
5 ultimately put at a competitive disadvantage.

6 Substantial changes in the
7 competitive landscape and the railroad
8 industry have occurred that call into question
9 the relevance and/or necessity of some of the
10 existing commodity exemptions. Unless these
11 exemptions are revoked so that manufacturers,
12 unlike shippers of non-exempted products,
13 cannot seek Agency protection for the
14 imposition of unreasonably high rail rates.

15 Such exemptions also prohibit
16 these manufacturers from raising concerns
17 about a rail carrier's refusal to provide
18 service on reasonable request or from
19 contesting various unreasonable practices in
20 which a rail carrier might engage.

21 As a shipper of a strategic
22 building material, Holcim needs a robust rail

1 industry to support the nation's economic
2 growth. Holcim must have access to a
3 competitive rail transportation system to
4 ensure timely and cost-effective delivery of
5 cement to those who construct and repair our
6 nation's infrastructure.

7 Revocation of cement-related
8 exemptions would permit Holcim, if needed, to
9 protect itself from abuses of market power by
10 rail carriers. The Agency must address the
11 plight of captive shippers of exempted
12 commodities, for the Staggers Act not only
13 directed the Agency to pursue exemptions
14 aggressively, but also instructed it to
15 correct any problems arising as a result of
16 such exemptions through its revocation
17 authority.

18 In conclusion, Holcim respectfully
19 requests that the commodity exemptions on
20 hydraulic cement and materials used in the
21 manufacture of cement be revoked. I sincerely
22 thank you for this opportunity and will answer

1 questions at the end if needed.

2 CHAIRMAN ELLIOTT: Thank you, Mr.
3 Giovinazzi. Next we will hear from Packaging
4 Corporation of America. Mr. Ridley and Ms.
5 Calabro, you'll have ten minutes.

6 MS. CALABRO: I'd like to thank
7 the Board for listening to this subject matter
8 today. My name is Dina Calabro. I am the
9 Transportation Manager for Packaging
10 Corporation of America. Next to me is Mr.
11 Bruce Ridley, PCA Mill Manager from our
12 Tomahawk, Wisconsin, mill.

13 Packaging Corporation corporate
14 office is located in Lake Forrest, Illinois.
15 Our industry is corrugated boxes and container
16 board cells. Annually, sales are \$2 billion
17 yearly. Our four paper mills and 68
18 corrugated box plants, approximately we
19 produce two million tons of container board
20 per year, equivalent to 20,000 rail cars and
21 45,000 trucks.

22 Our liner mills are located in

1 Jackson, Tennessee, and Valdosta, Georgia.

2 Our median mills are located in Tomahawk,
3 Wisconsin, and Filer City, Michigan.

4 PCA integrates 80 percent of their
5 paper manufactured and is consumed by the PCA
6 box plants. Thirty-nine of our plants are
7 rail served.

8 PCA's product background. Roll
9 stock is our commodity. Increasing
10 competition in container board industry,
11 service, and quality is what we sell.

12 Rail is essential to PCA
13 transportation plan. The industry is going
14 towards larger rolls, 110-inch rolls, 130-inch
15 rolls. This can only be shipped by rail.

16 Our shipping dynamics have changed
17 within the last ten to 15 years. Rail used to
18 be our main mode. Overall, currently we are
19 shipping 50 percentage tonnage moving rail and
20 50 percent tonnage moving truck. It was 75
21 percent rail and 25 percent truck.

22 As an example, one rail car equals

1 two to three trucks. By shifting to truck,
2 there is more stress on the national
3 transportation infrastructure and gridlock on
4 our highways.

5 PCA's goals and reasons for
6 attending today's hearing. Ask the STB to
7 investigate the effectiveness of boxcar and
8 commodity exemption.

9 PCA is not a advocate of either
10 side but rather asks the Commission to study
11 whether or not the exemption is still
12 practical. We want to correct unreasonable
13 practices that impede competition with other
14 modes.

15 PCA rail transportation concerns.
16 Number one, diminishing competition from
17 railroad service. Consistency and timeliness
18 is not as good as truck.

19 Pricing. Boxcar supply, we are
20 constantly being -- we have shortage of our
21 boxcar orders on a weekly basis at some of our
22 mills.

1 Our boxcar quality has moving
2 upward as far as a percentage of rail cars
3 that we have to reject. The number of cars,
4 we have taken a survey over the last year, and
5 the percentage at our mills are just going up,
6 the cars that we cannot accept to put our
7 product in.

8 Number two item we would like to
9 talk about today is boxcar utilization and
10 boxcar reload effectiveness. An average
11 boxcar turns 12 times per year or one to two
12 per month. We would like to reduce our rail
13 operation cost, and we could also reduce the
14 railroad's rail operation cost.

15 To date, we are not able to
16 accomplish that. We have cars that we load
17 our roll stock into a facility, and we'd like
18 to reload that car back with scrap to our
19 mills.

20 There are restrictions on rail
21 cars that belong to other lines that we were
22 not able to use, so the car goes back empty.

1 Not all railroads are participating in the
2 national boxcar pool.

3 Accountability of railroads as
4 partners. Sometimes it's, in my experience,
5 it's been a one-way relationship. Annual rate
6 increases are norm. Railroad dictates their
7 intentions without requesting customer
8 feedback, like reducing switching days.

9 No consequences for service
10 interruption. Railroad causes mis-switches,
11 misrouted cars, and transit delays that can
12 put our facilities in a shut-down mode, and
13 we're always occurring demerge, whether we're
14 guilty until proven innocent to prove that we
15 have caused the emerges.

16 Also, the role of the short line
17 has diminished. Three out of our four mills
18 are served by short lines. They are
19 leveraging service over volume of cars that we
20 need to ship per day.

21 In closing, PCA is interested in
22 continuing success partnership with railroads.

1 Railroads are integrated to PCA's
2 transportation strategy. Competitive service
3 and competitive rates are most important.

4 PCA is interested in the STB to
5 investigate the past and current effectiveness
6 of boxcar exemption policy. Thank you. Would
7 you like to say anything, Bruce?

8 CHAIRMAN ELLIOTT: Thank you very
9 much. Now we'll hear from Mr. Weaver from the
10 Weaver Popcorn Company. You have ten minutes.

11 MR. WEAVER: Thank you. Thank
12 you, members of the Board, for holding this
13 valuable hearing today. It was suggested by
14 our short line partner, the Wabash & Central
15 Railroad in northeast Indiana, that I come
16 today and share some of my concerns with you
17 all, and, again, we are a very happy customer
18 of Packaging Corporation of America, actually,
19 as well, so thank you for the good supply.

20 What I'd like to try and to today
21 is you all have received a lot of information
22 today that's very broad in scope, and I'd like

1 to try and offer up a little bit of a granular
2 perspective.

3 We are a -- Weaver Popcorn is a
4 smaller company. Our only business is
5 popcorn. Popcorn is a market that is heavily
6 and increasingly export-oriented, so we have
7 a very heavy reliance on the intermodal system
8 of this country.

9 I spend a lot of my time overseas
10 selling popcorn, and I will tell you a lot of
11 the commentary that you received today is very
12 true. I often run into foreigners who marvel
13 at how efficient the American railroad has
14 become, so I really think, quite frankly, the
15 standard that Staggers set has really paid
16 off.

17 Having said that, I don't think
18 you ever sit on your laurels, and, you know,
19 you always need to address how you can improve
20 further. I think that's probably why you all
21 called this meeting today and are considering
22 various discussions.

1 The key for the export market in
2 the popcorn commodity is that we're a very
3 weight-sensitive, very freight-sensitive
4 commodity, and right now the way this
5 country's intermodal service is structured,
6 it's an absolute mandate that companies such
7 as mine have to truck their product before it
8 can achieve -- before it can hit the rail or
9 the ship.

10 What that obligates people like me
11 who are trying to export products to is our
12 weights per container are set by the first leg
13 of the journey to Shanghai, Mumbai, or
14 Alexandria, so my dray to Chicago really
15 determines my weight all the way to Shanghai.

16 For a small company such as mine,
17 one product, all popcorn, that's a big
18 competitive disadvantage, and so, you know,
19 when I export a container here in the United
20 States, I ship about 21 tons per container at
21 the most.

22 Most of the competition in my

1 industry is from Argentina. They have
2 different restrictions on weight there. They
3 can ship 25, 26 tons per container.

4 Now, my job is not to complain
5 about the terrible Argentine, you know, those
6 evil Argentine guys. My job is to grow
7 volume, so, you know, we came up with a
8 proposal working with our short line to load
9 export containers directly onto cars that we
10 would lease.

11 We would use equipment to load the
12 cars that we would pay for ourselves as a
13 company. All we needed was for our short line
14 to take it up to Fort Wayne and for it to be
15 picked up by the Norfolk Southern and taken to
16 the various export ports.

17 That would, for our company, a
18 small company, much smaller than all the other
19 companies here today, that would yield by my
20 estimate almost an immediate 30 percent
21 increase in export volume because of that
22 elimination of the freight disadvantage.

1 Now, again, we're just one
2 company, but, again, I think that provides an
3 example of although many things are going very
4 well in the last 25, 30 years in the rail
5 industry, a lot of productivity improvements,
6 very impressive charts and graphs today, I do
7 think there are some things you should look at
8 in terms of these exemptions, particularly
9 around the intermodal, where I think a lot of
10 the intermodal, just the inherent productivity
11 of that transportation medium, you're almost
12 inherently going to grow that over boxcars in
13 a two or three decade as boxcars became -- or
14 as containers became more available.

15 So what I kind of would like in
16 closing to say to you is just, quite frankly,
17 consider whether or not increasing the reach
18 of the intermodal network, allowing companies
19 like my own, Weaver Popcorn, to load
20 containers at the railroad would make sense,
21 and thank you for your time.

22 CHAIRMAN ELLIOTT: Thank you, Mr.

1 Weaver. I only had one question. It was
2 directed towards Holcim.

3 Your -- I took a look at hydraulic
4 cement, the STCC for that and the R/VC ratios,
5 the traffic that runs, the percentage of
6 traffic that runs over 180, and from '93 it
7 was 21 percent. In '98, it went up to 26.
8 2003, it went up to 41 percent, and 2008 was
9 44 percent.

10 So I'd say that is one of the
11 extreme examples of the percentage of traffic
12 running over 180 for revenue over variable
13 cost, making kind of a significant economic
14 statement as far as indicating some possible
15 market power use.

16 Can you -- I know you talked about
17 captive plants and things of that nature in
18 your testimony, but can you tell me, if
19 anything, what's changed since 1993 to 2008 as
20 far as the competition that you see with
21 respect to railroads?

22 MR. GIOVINAZZI: Well, I've only

1 been in the cement industry a short time, so
2 from a cement standpoint I couldn't answer
3 that question, but I've been in the rail
4 industry since 1970.

5 I think that Commissioner Mulvey
6 is hitting close to the point of what we're
7 all trying to say here. I don't think -- I
8 can tell you for a fact Holcim doesn't
9 consider the railroads the enemy or a bully,
10 even.

11 You know, I don't think that our
12 experiences are bad with the railroads, but we
13 have a piece of our business that I think
14 anyone who has a business and has to negotiate
15 rates, if you have no alternative and then you
16 have no voice, what ultimately can you do, and
17 the person you're negotiating with for that
18 rate or for that service realizes you have no
19 voice? I mean, I think that's the piece of
20 this that we're focused on.

21 I would stand with the railroads
22 before I would ever want to see the railroads

1 reregulated. I think all the charts we've
2 seen today prove out, and I'm not saying
3 anything that anybody here doesn't already
4 know, the railroads are far better at
5 railroading than the government is and really
6 any of the shippers are.

7 I also realize that there's --
8 pick a number -- 5,000 shippers and seven
9 railroads, and so there is always going to be
10 a complaint. There is always going to be
11 someone dissatisfied.

12 Someone's rates are always going
13 to be too high, but I think those numbers also
14 proved out that there are a number of
15 industries that are already removed from the
16 exemption, and the numbers were still good.

17 I mean, the railroads are able to,
18 I think, work in that environment, and I think
19 that what we're looking for is just a process
20 that doesn't overburden the railroads, doesn't
21 overburden this Board, but that just gives us
22 a voice for those lanes where we have no

1 competition.

2 Again, Commissioner Mulvey, when
3 you were talking about mileage, maybe that's
4 a starting point for that. Where you can't
5 truck it effectively, you don't have any
6 access to barge, you don't have any access to
7 additional railroads, maybe it's a starting
8 point where you say, "Okay, these lanes, at
9 least, when you come together, if there is no
10 agreement between railroad and shipper, then
11 maybe we have a voice." That's it.

12 CHAIRMAN ELLIOTT: Thank you.

13 Vice Chairman?

14 VICE CHAIRMAN NOTTINGHAM: Thank
15 you, Mr. Chairman. I also wanted to recognize
16 Bruce Ridley as another outstanding member of
17 our Rail Shipper Transportation Advisory
18 Committee. You've been a member for a long
19 time and a real valuable addition to that
20 group, along with Eric Butler, whom I
21 mentioned earlier.

22 I just wanted to recognize you,

1 Bruce. Thank you for being here. Thank you
2 for what you do for the Agency and for the
3 shipper community on the RSTAC Committee.

4 Mr. Giovinazzi, it occurs to me
5 that freight railroads are actually pretty big
6 consumers of concrete, aren't they? They
7 often like to show us their new concrete rail
8 ties on some of their high-density lines. Are
9 they buying some of that, I hope, from Holcim?

10 MR. GIOVINAZZI: I'm hoping so.

11 VICE CHAIRMAN NOTTINGHAM: Maybe
12 you can get some leverage that way. They --
13 you've got something they need, and they've
14 got something you need, but far be it for me
15 to give you advice. I just throw that out
16 there.

17 Mr. Weaver, I've got lots of
18 questions for you, but they really relate to
19 the consumption and proper preparation of
20 popcorn, and we'll have to wait for another
21 proceeding.

22 MR. WEAVER: I'll stay after.

1 VICE CHAIRMAN NOTTINGHAM: But I'd
2 love to improve my ratio of popped kernels to
3 unpopped kernels.

4 MR. WEAVER: We're working on it.

5 VICE CHAIRMAN NOTTINGHAM: I'm
6 sure you could help me with that, but I won't
7 take up everyone's time on that today. But,
8 seriously, you mentioned a situation you were
9 trying to achieve some efficiencies working
10 with one of the Class I railroads.

11 Did I hear it correctly? Did that
12 -- what's sort of preventing from happening?
13 It sounds like you had a good idea that would
14 save some money, increase efficiency, make
15 your company more competitive, but the --

16 MR. WEAVER: We've -- it's
17 actually our Class III, the Wabash Central,
18 and we have not received any response from the
19 Norfolk Southern, and we've been asking for a
20 number of years, which is, again, just one of
21 our concerns. Again, it's a capital-neutral,
22 you know, equipment-neutral, we feel, approach

1 for the Norfolk Southern.

2 VICE CHAIRMAN NOTTINGHAM: Well,
3 if I could, Mr. Chairman, ask that our Rail
4 Consumer Assistance Office get in touch with
5 Mr. Weaver if you'd be willing to --

6 That's exactly the kind of problem
7 I think we might be able to help with
8 sometimes just bridging communication gaps and
9 problems between shippers and railroads where
10 a shipper wants to try a new approach or do
11 something innovative and it doesn't at first
12 glance sound convenient or interesting to the
13 railroad, but with a little bit of extra
14 communication often we can see success there,
15 so let's try to give that a chance. I'm sure
16 the staff can track you down, given your
17 presence here today.

18 Let's see. On the container
19 weight limits, Mr. Weaver, if you could just
20 elaborate on that. Argentina and other
21 countries have higher weight limits is your
22 understanding?

1 MR. WEAVER: That's correct. I
2 think in Europe they're 25 tons, and Argentina
3 I'm not entirely sure, but 26 is what my
4 competitors are shipping. I'm not sure if
5 they're maximum or not.

6 VICE CHAIRMAN NOTTINGHAM: I'm
7 real familiar with truck size and weight
8 limits from my highway work in the past, but
9 is it the trucking leg of your move that
10 really constrains that, or is it also the rail
11 leg?

12 MR. WEAVER: The rail leg will
13 constrain me below 26 tons because of the
14 weight limits on my Class III, but we can do
15 25.4 tons, I believe, is the number I've been
16 given.

17 VICE CHAIRMAN NOTTINGHAM: Thank
18 you. That's all I had, Mr. Chairman.

19 CHAIRMAN ELLIOTT: Commissioner?

20 COMMISSIONER MULVEY: In line with
21 Vice-Chairman Nottingham's point about the
22 Railroad Consumer Protection Program, I'll

1 have someone from there talk to you, and
2 hopefully they can help you out. Also, have
3 you considered filing a case-specific
4 revocation request?

5 MR. WEAVER: After we filed our
6 paperwork, I got a number of solicitations
7 from third-party consultants saying, "For a
8 fee, we'd love to help you fill that out,"
9 which, you know, is definitely something we
10 might approach. Typically, we don't like to -
11 - we're a low overhead operation.

12 COMMISSIONER MULVEY: Okay. Mr.
13 Giovinazzi, you were saying that more and more
14 you need modification. Something like 50
15 percent of your outgoing movements are by
16 rail. That changes by distance, though? The
17 further you're going out, the more it is rail-
18 related, rail-oriented?

19 MR. GIOVINAZZI: As a general
20 statement, that's correct, right.

21 COMMISSIONER MULVEY: So you would
22 think that there is some possibility, some

1 usefulness of looking at distance, a distance-
2 based approach to the exemptions and seeing
3 whether or not certain commodity times
4 distances might be more appropriate for
5 revoking the exemption than doing so on a
6 general basis.

7 MR. GIOVINAZZI: Well, again, to
8 that point, as a general statement, within 175
9 miles or so you can usually get some truck
10 competition. When you're single served,
11 either at origin or destination, you're pretty
12 much locked into that railroad, and if it's
13 much over 175 miles, then again you really
14 have very limited negotiating ability if the
15 rate is a rate that just doesn't work for you
16 in that lane.

17 COMMISSIONER MULVEY: It's my
18 understanding that, and I could be wrong on
19 this, but has there been a decline in the
20 number of manufacturers in the cement industry
21 over the last few years so that the distances
22 are getting longer from origin to destination?

1 MR. GIOVINAZZI: Again, I'm new to
2 the industry, so I'm not positive what the
3 answer to that is, but I can tell you that as
4 a general statement, cement is a regional
5 business, and that's because the demand is
6 sort of just-on-time type of demand. If the
7 weather turns against somebody, that might
8 delay a job for three or four days, and then
9 all of a sudden you need five more, six more
10 cars of cement.

11 COMMISSIONER MULVEY: To PCA,
12 hello, Bruce. It's nice to see you again.
13 You're saying that you're making larger and
14 larger rolls, and bigger rolls have to be
15 moved by rail rather than by truck.

16 On the other hand, you say that it
17 used to be 50/50, and now it's 75 percent
18 truck, 25 percent rail. That doesn't seem to
19 jive with the larger rolls. You should be
20 moving more by rail if the rolls are getting
21 larger.

22 MS. CALABRO: Well, the mills that

1 produce the larger rolls, we're just basically
2 producing the larger rolls heavier at the two
3 liner mills.

4 MR. RIDLEY: And just to make sure
5 you get your numbers right, they're 50/50 now.
6 It was 75 percent truck. Excuse me, 75
7 percent rail and 25 percent truck.

8 COMMISSIONER MULVEY: Right.

9 MR. RIDLEY: Now it's 50/50.

10 COMMISSIONER MULVEY: Now it's
11 50/50. That's what I meant, but you switched
12 more towards truck, even though the rolls are
13 getting larger. That's what I was wondering
14 about.

15 MS. CALABRO: Well, those larger
16 rolls are shipping by rail. We pay premium
17 just to ship them by rail.

18 COMMISSIONER MULVEY: Okay.

19 MS. CALABRO: We have no
20 alternative. We have to ship them by rail.

21 MR. RIDLEY: The point being we do
22 have some captive product.

1 COMMISSIONER MULVEY: Okay. Thank
2 you. That's all I have.

3 CHAIRMAN ELLIOTT: Thank you very
4 much for your informative presentations, and
5 I think we're off to the next panel, so you
6 may be seated. The next panel is Panel VI,
7 and that is the Intermodal Interests Panel.

8 I think there is only one person,
9 our second panel of one, and our panel
10 speaking today from the Intermodal Association
11 of North America is Joanne Casey, and you have
12 ten minutes.

13 MS. CASEY: Thank you very much.
14 Good afternoon, Chairman Elliott, Vice
15 Chairman Nottingham, and Commissioner Mulvey.
16 My name is Joanne Casey, and I'm the President
17 and CEO of the Intermodal Association of North
18 America, otherwise known as IANA.

19 Accompanying me today is our
20 general counsel, Mr. John Bagillio, and I
21 appreciate the opportunity to appear before
22 the Board today to elaborate on the written

1 comments that IANA did provide to you and to
2 encourage you to maintain the current
3 exemption for trailer on flat car and
4 container on flat car transportation service.

5 I apologize in advance for
6 repeating some of the information that you
7 already heard today. I think it's an
8 occupational hazard and the time of day, so
9 I'll try to be brief.

10 I've been employed with the
11 freight transportation industry for more than
12 25 years. I started my career in the early
13 eighties, about the same time that the Motor
14 Carrier and Staggers Act, as well as the
15 subsequent intermodal exemption were being
16 debated and made into law. I focused
17 exclusively on the intermodal industry since
18 assuming my position at IANA in 1997.

19 Our Association's members consist
20 of hundreds of transportation service
21 providers from all of the intermodal modes,
22 including railroads, ocean carriers, motor

1 carriers, and third-party logistics companies
2 and intermodal marketing companies. They
3 handle approximately 90 percent of the
4 intermodal shipments moving through the global
5 supply chain.

6 Railroads are an essential link to
7 the integrated multi-modal services needed to
8 meet freight transportation demands both today
9 and in the future, and it was the recognition
10 of the railroad's importance by Congress and
11 the ICC 30 years ago that led to the exemption
12 of TOFC/COFC rail service from regulatory
13 oversight.

14 The initiatives that flowed from
15 that decision have contributed directly to the
16 growth of intermodal service, both
17 domestically and internationally, which in
18 turn has been a key component to the
19 revitalization of the railroad industry.

20 The ICC's decision in ex parte 230
21 sub number 5 was based on the conclusion that
22 TOFC/COFC service was very competitive with

1 comparable motor carrier service, that
2 sufficient intra-rail competition existed, and
3 that regulation was not needed to protect
4 shippers against abuses of market power.

5 Those same relative conditions exist today and
6 justify the continuation of the intermodal
7 exemption, and I think that several metrics
8 support this view.

9 In the most recent Commodity Flow
10 Survey, CFS, that was released by the Bureau
11 of Transportation statistics at the end of
12 last year -- it had data through 2007, by the
13 way -- it shows that motor carriers transport
14 approximately 70 percent of the goods both by
15 value of and by weight in tons.

16 The corresponding shares for
17 multi-modal transport, and they define multi-
18 modal as parcel, truck and rail, truck and
19 water, and rail and water, are 16 percent for
20 value and 4.4 percent, respectively, and I
21 don't believe we've heard that number today.

22 The National Rail Plan Progress

1 Report issued by the Federal Railroad
2 Administration last September documented the
3 level of competition among the modes by length
4 of haul and commodities transported, and I
5 know we've discussed that earlier.

6 For retail goods, consumer
7 durables, and other manufactured commodities,
8 rail, intermodal, and truck transportation are
9 considered competitive alternatives for hauls
10 ranging from 500 to 2,000 miles.

11 The final example comes from the
12 American Trucking Association's publication,
13 U.S. Freight Transportation Forecast. That
14 analysis includes a comparison of revenues
15 earned and tons transported by truck and
16 specifically rail intermodal service. Some of
17 the other numbers were larger aggregates.

18 2010 motor carrier revenues were
19 estimated at 87.9 percent of the nation's
20 total freight bill versus 1.3 percent for rail
21 intermodal. Motor carrier tonnage was
22 estimated at 68.6 percent and rail intermodal

1 tonnage, 1.6 percent.

2 Regardless of the unit of measure,
3 the relative market shares of truck versus
4 rail intermodal have not changed significantly
5 over the last decade. Freight volumes have
6 grown in total, and so to use an analogy that
7 was used earlier today, the pie itself is
8 bigger, but the rail intermodal piece is still
9 small compared to that of the trucking
10 industry.

11 The numbers show that shippers,
12 including a large portion of the nation's top
13 motor carriers, including UPS, are exercising
14 their ability to determine how much cargo to
15 transport solely over the road or via
16 intermodal services, and it's based on
17 prevailing commercial conditions absent any
18 kind of market dominance or market abuse of
19 power.

20 Maintenance of the TOFC/COFC
21 exemption I think is also supported by some
22 recent programs and decisions that the current

1 administration and federal regulatory agencies
2 have made.

3 The President's National Export
4 Initiative, with a goal of doubling exports by
5 2015, cites a reliance on continued
6 improvement of rail intermodal market share
7 and intermodal connections, that last mile
8 between the terminals.

9 Another White House directive that
10 was mentioned earlier was the Executive Order
11 issued by the President in January that called
12 for review of all regulations that place
13 unreasonable burdens on business, stifle
14 innovation, impact growth and jobs, and create
15 unnecessary paperwork requirements.

16 Most recently, the Federal
17 Maritime Commission, last week on the 16th,
18 made a decision to exempt non-vessel operating
19 common carriers from the requirement to use
20 published tariffs as the basis for their
21 pricing, thus allowing this intermodal
22 transportation intermediary to negotiate rates

1 directly with their customers.

2 The success of intermodal
3 transportation service is reliant on an
4 equilibrium among the modes. I don't think I
5 have to tell anyone that.

6 Economic regulation of one segment
7 such as the removal of rails, intermodal
8 exemption could have adverse impacts on the
9 other modal partners, causing a disruption in
10 pricing and service offerings currently
11 afforded to shippers.

12 It could also impact the
13 competitive balance between the modes if
14 regulatory scenarios differed among the
15 transportation providers, and delays that may
16 be associated with regulatory oversight of the
17 rail's intermodal services and pricing of
18 those services could render their actions
19 untimely and non-responsive to customers'
20 needs, and I believe we've heard that, as
21 well.

22 In conclusion, I'd like to look

1 back on some legislative history, if you'd
2 allow me. When the Staggers Act was being
3 crafted, Section 10505F, now number 10502, of
4 the Act was introduced as a floor amendment by
5 Pennsylvania Congressman Alan Ertle.

6 His justification for the
7 amendment was that greater use of TOFC/COFC
8 service would conserve fuel, would reduce
9 highway maintenance and railway operating
10 costs, increase productivity, and help
11 maintain American competitiveness in the world
12 economy and that regulatory structure had
13 heretofore inhibited intermodal growth by
14 isolating modes from one another, the silo
15 theory.

16 The past is often a predictor of
17 the future, and I would submit that Congress
18 and Ertle's rationale in introducing the
19 amendment that led to the creation of rail
20 intermodal exemptions is still applicable
21 today, 30 years later. I thank you for
22 allowing me to make these comments this

1 afternoon, and I'd be happy to respond to any
2 questions that you might have for me.

3 CHAIRMAN ELLIOTT: Thank you, Ms.
4 Casey. Commissioner?

5 COMMISSIONER MULVEY: Thank you
6 for your testimony, Joanne. We talked a lot
7 today about the railroad industry and the
8 changes that have occurred in the railroad
9 industry but not so much about trucking, and
10 it's my understanding there have been
11 substantial changes in the trucking industry
12 over the last couple of decades.

13 One, of course, the fuel costs
14 have increased, and fuel is a more important
15 component for trucks than for rail. There is
16 also a driver shortage, which I think
17 continues to persist, and there are other
18 restrictions, more congestion, et cetera.

19 All of these should lead to a
20 switch in the rail-truck market share, but you
21 suggest that the market shares have remained
22 fairly stable and the pie as a whole just

1 growing. How do you reconcile that, or is
2 there a change in the distribution?

3 When you say market shares are the
4 same, how are you measuring that? Is that
5 tons, or is that number of movements, or is
6 that ton miles or what?

7 MS. CASEY: Really, all of the
8 above, the value of the goods, the tonnage,
9 and the percentage within any of the markets.
10 I think certainly trucking is going to be
11 faced with a lot of challenges, as we all are
12 and have been.

13 The contention that these
14 challenges for the motor carrier industry are
15 going to make them less competitive and then
16 have a heavier reliance, whether it's the
17 compliant safety analysis, whether it's the
18 hours of service or electronic onboard
19 recorders, I think it harkens back to the
20 relative percentage of rail intermodal.

21 I hate to keep harping on that,
22 but I don't think, regardless of the challenge

1 that the motor carrier industry are faced,
2 that the rail component, which is small by
3 nature, is going to be significantly impacted
4 by any kind of shifting in motor carrier
5 regulatory requirements.

6 If you go back and look at the
7 relative shares, whether it's tons or value,
8 they really have been consistent, and rail
9 intermodal service in general has never been
10 any higher than ten percent. It's usually
11 less, so you're talking about ten percent
12 versus relative 70, 80 percent of the market.

13 COMMISSIONER MULVEY: It's
14 interesting, because the railroads say
15 intermodal is sort of where the growth is
16 going to be for the railroad sector, and the
17 purpose or the desire is to increase the
18 railroad's profit share over time, but exactly
19 how much that will be true is still in
20 question.

21 MS. CASEY: I think absolutely.
22 It's market-driven.

1 VICE CHAIRMAN NOTTINGHAM: Ms.
2 Casey, thank you for your very helpful
3 testimony, very data rich, exactly the kind of
4 information we need to review these types of
5 issues, and, Mr. Mulvey, I don't know if this
6 answers your last question, but if I
7 understood the previous testimony and Ms.
8 Casey's testimony, yes, railroads have
9 experienced an uptick in earnings attributed
10 to intermodal business, but part of that I
11 believe is related to the growing pie, right,
12 Ms. Casey? The total amount of traffic is
13 growing?

14 MS. CASEY: Right.

15 VICE CHAIRMAN NOTTINGHAM: The
16 overall modal split has not changed that much
17 if I understand your testimony correctly.

18 MS. CASEY: That's correct. If you
19 look at some of the studies, you have
20 projections of freight either doubling, or I
21 think that's been cut back a little bit
22 recently. The U.S. Chamber has done some

1 studies that have projections, but I feel
2 strongly that there is going to be more than
3 enough freight to go around.

4 It will be distributed according
5 to how it has been in the past, and the
6 intermodal piece of that service is very
7 competitive, and it'll have to continue to
8 have the flexibility in service and pricing in
9 order to remain competitive, vis-a-vis some of
10 the other components of intermodal, whether it
11 be water or a third party or motor carrier,
12 which is a component itself.

13 VICE CHAIRMAN NOTTINGHAM: Thank
14 you. That's all I have.

15 COMMISSIONER MULVEY: I guess the
16 other point is since this is so competitive
17 and since it's known that historically the
18 intermodal revenue-to-variable-cost ratio has
19 been much below 180 percent, it strikes me
20 that this would not be one of the cases where
21 we would be talking about a revocation of the
22 exemptions. Intermodal almost by definition

1 would not be an area where this Board would be
2 looking to revoke the exemption, simply
3 because the evidence is so overwhelming that
4 it is a competitive market.

5 On the other hand, that is not
6 true for all the commodities. For some of the
7 commodities, those revenue to reasonable cost
8 ratios are much higher, and it's not as clear
9 that it's as competitive as the intermodal
10 market.

11 Would you -- I know you represent
12 the Intermodal Association of North America,
13 but you're also a transportation expert, so
14 would you care to comment on the broader issue
15 of the exemptions?

16 MS. CASEY: In terms of the R/VC,
17 I don't have any direct knowledge of the
18 various exempted commodities on that, and
19 unlike Mr. Hamberger, who deferred to me on
20 the R/VC for intermodal, I would defer back to
21 him, and his 130 I think is a reasonable
22 number. IANA deals primarily in operations.

1 We do not get involved in rates and pricing.

2 CHAIRMAN ELLIOTT: Thank you very
3 much, Ms. Casey, for coming today and sharing
4 you're thoughts with us.

5 MS. CASEY: You're quite welcome.
6 Thank you.

7 CHAIRMAN ELLIOTT: Now we will
8 hear from the final panel, Other Interests,
9 Panel VII. First we'll hear from CNJ Rail
10 Corporation. Mr. Strohmeier, you have five
11 minutes.

12 MR. STROHMEYER: Thank you,
13 Chairman Elliott. Good afternoon, members of
14 the Board. My name is Eric Strohmeier, and I
15 would just like to briefly add one brief
16 comment to the Board's hearing today that I
17 feel might have some advantage to the Board's
18 deliberation in this proceeding.

19 We've heard a lot about revoking
20 exemptions and whether or not it would be
21 prudent or not prudent or whether it should or
22 should not be revisited. I would simply offer

1 in respect to intermodal, in particular, TOFC
2 and COFC exemptions, that the Board also
3 consider one additional reason for not
4 revisiting the TOFC and COFC revisions.

5 Insomuch as I believe that while
6 the other economic reasons are also
7 justification, I also believe it also serves
8 as a proverbial wax seal to the Pandora's that
9 might be opened if you decided to lift the
10 TOFC/COFC exemption, and I'd like to just
11 briefly give you a two-minute oversight here
12 in the post-Staggers Act of 1980.

13 From 1980 to 2000, the intermodal
14 market itself has matured over the years.
15 Services that were contemplated in the 1980s
16 grew into the 1990s.

17 Vice Chairman Nottingham had
18 mentioned the use of the term "stack train,"
19 which first originated in 1983 with Sealand
20 and Maersk service off the East Coast and
21 eventually grew into the 1990s. We saw many
22 of the market develop stack train operators.

1 In fact, that became a term that we've come to
2 readily expect in the marketplace today is a
3 stack train operator.

4 That didn't exist pre-Staggers,
5 and so you might ask, "Well, what's the
6 Pandora's box? What's the reference to stack
7 train operators and the potential for an
8 adverse impact?"

9 I point the Board to a case that I
10 think even Commissioner Mulvey might have been
11 involved with many moons ago, well, not too
12 long ago, about 2005, where the Board did a
13 careful analysis of a tour train operator, and
14 you're probably saying, "What in the world
15 does this have to do with it?"

16 But after looking at the
17 relationship between the operator of that
18 train and how their customers interacted with
19 the person, how the service was developed, how
20 the contracts were written between the rail
21 carrier, and how that service was ultimately
22 marketed to the end consumer, it was

1 determined that that entity was a carrier by
2 the Board. It was the American Orient Express
3 case.

4 Now, if you take that same basic
5 scenario and apply it to a stack train
6 operator, an independent entity set up by
7 either steamship companies or rail companies,
8 they act independent of the national rail
9 system, but they offer door-to-door or ramp-
10 to-ramp services just like a CSX or a BNSF
11 would.

12 As such, they in essence provide a
13 market -- market this service to the shipping
14 public, and one of the reasons why the Board
15 has never had to ever ask the question is a
16 stack train operator a carrier subject to the
17 Board's regulation has been under the
18 intermodal exemptions. It's an unrelated
19 commodity. There is no need to address the
20 issue.

21 However, if you decide to address
22 the issue and say, "Well, we want to consider

1 revoking the exemption," then comes the
2 question of, "Are these potential stack train
3 operators" --

4 I'm using stack train operators
5 simply because they're the most obvious, but
6 it then raises the possibility of how do you
7 regulate a carrier that isn't a railroad, even
8 though they might be a common carrier subject
9 to the Board's jurisdiction.

10 And I won't go into great detail
11 over how that would potentially adversely
12 impact a rate scenario. It's just a
13 situation that the Board hasn't had to look
14 at, and these various types of services have
15 matured and grown and evolved in the 20 years
16 since the Staggers Act was created, and you
17 have lots of new different elements in the
18 marketplace today that the Board just simply
19 hasn't looked at extensively.

20 That would be simply my closing
21 comment that I would simply done is I don't
22 know if I -- I've looked myself to see if the

1 Board from 1996 to the current term has ever
2 done anything where they made a formal public
3 inquiry, anyway, into the various
4 relationships between shippers and shippers'
5 agents and the railroads and made a
6 determination as to, you know, all of these
7 various little nuances.

8 But I would simply suggest that
9 before the Board consider revoking an
10 intermodal exemption it might just simply want
11 to ask the question how would this affect many
12 of the relationships that have evolved over
13 the time? -- how I would prefer to end my
14 brief comment here and thank the Board for
15 giving me five minutes to make that comment.

16 CHAIRMAN ELLIOTT: Thank you, Mr.
17 Strohmeier. Next we'll hear from the Mercury
18 Group. Mr. Dickman, you have five minutes.

19 MR. DICKMAN: Chairman Elliott,
20 Vice Chairman Nottingham, Commissioner Mulvey,
21 STB staff, and interested parties, thank you
22 for the opportunity to appear before you

1 today.

2 I am Craig Dickman, the CEO of
3 Breakthrough Fuel, a company focused on
4 bringing transparency of fuel consumption,
5 fuel cost, and emissions to freight movements.
6 I am also here on behalf of the Mercury Group,
7 a shipper energy study group working to use
8 this transparency to better manage the fuel
9 costs that result from shipping products to
10 market.

11 The question we submit today is
12 does a consolidation of the Class Is combined
13 with the exemptions impeded adoption of
14 marketplace alternatives to industry-wide use
15 of fuel surcharges?

16 Today you've invited comments on
17 whether to investigate and attempt to resolve
18 a conflict, a conflict between shippers and
19 the railroads arising not only from their
20 unique respective economic interest but also
21 from an apparent lack of trust on some key
22 business terms.

1 Fuel and fuel surcharges are one
2 of the main areas of conflict. The conflict
3 and the underlying lack of trust will neither
4 be resolved by revoking the exemptions in
5 question today nor by leaving them intact, but
6 it will -- but the opportunity that is created
7 is to advance marketplace transparency.

8 It's easy to understand why
9 today's surcharge environment creates
10 conflict. Shippers are being asked to pay for
11 fuel costs that have virtually no relationship
12 to the freight being moved.

13 Fuel surcharges based on
14 percentage of revenue models have been called
15 unreasonable except or only for non-exempt
16 freight, and even mileage-based surcharges
17 using the Department of Energy's EIA Index do
18 not accurately capture the fuel costs
19 associated with freight movement.

20 I found it particularly
21 interesting and illustrative today when
22 Professor Willig, as he was walking through

1 the data, highlighted a couple of occasions
2 where fuel moves too fast for the data to
3 allow precise understanding, and that's the
4 same challenge that shippers, rail, and other
5 interested parties run into.

6 The economic distortion included
7 within fuel surcharges, whether it's the
8 timing is not correct, the geography, the
9 pricing, all creates a situation where
10 virtually every freight transaction has
11 economic distortion built in.

12 Now, it's easy to understand how
13 we got here. When fuel costs first spiked and
14 fuel surcharges were introduced, transparency
15 was impossible. Information and technology
16 was not available, and the ability to manage
17 fuel cost was neither important nor possible.

18 Well, that's not today's
19 marketplace. Fuel prices are high and getting
20 higher and greatly impact the competitiveness
21 of a shipper's product.

22 Technology now exists to make

1 transactions routine and inexpensive, and
2 transparency available today creates the
3 opportunity for a far more effective
4 competitive marketplace, but the key is that
5 the payment for fuel cost between the shipper
6 and the carrier be based on actual fuel market
7 conditions and not an artificial index.

8 When shippers are able to see,
9 understand, and pay the railroads for the real
10 price of fuel, they can make informed
11 decisions and improve the competitiveness of
12 their product.

13 In a transparent market, a shipper
14 will see the benefits and the differences
15 between different transportation modes. For
16 the first time, shippers will be able to
17 understand the gallons, the emissions, and the
18 market fuel cost of their transportation
19 decisions.

20 They will see the impact of using
21 more efficient carriers, shipping from
22 different locations, and including alternative

1 fuels into their process, and they will
2 understand the impact of decisions on their
3 carbon footprint. Today, reducing emissions
4 can be a competitive advantage.

5 In total, shippers will have the
6 necessary information to make decisions that
7 make their products more competitive, but the
8 benefits of transparency are not exclusive to
9 shippers. When the railroads are paid
10 accurately for fuel costs they incur to move
11 freight, it will support a more efficient
12 competitive market.

13 Simply, what's the benefit of
14 being a more fuel-efficient mode if it's not
15 visible to those that are choosing which mode
16 to ship, and what's the benefit of better fuel
17 economy and lower emissions if it cannot be
18 accurately calculated by those using the
19 service?

20 Transparency will connect the
21 benefits with the decisions and the most
22 efficient mode and carrier relationship.

1 Further, transparency creates the opportunity
2 for shippers and their transportation
3 providers to move from being adversaries on
4 this issue, which is almost inevitable, to
5 collaborators focused on how to best manage
6 fuel, the most volatile of all transportation
7 costs.

8 As a path forward, we respectfully
9 ask the Board to formally review questions
10 regarding the exemptions and the implications
11 on index-based surcharges, which have been
12 highlighted in our verified testimony, and
13 move toward a more transparent pro-competitive
14 marketplace that we've discussed today. Thank
15 you.

16 CHAIRMAN ELLIOTT: Thank you, Mr.
17 Dickman. Now we'll hear from the United
18 Transportation Union, New York State
19 Legislative Board. Mr. McDougall, you have
20 five minutes.

21 MR. MACDOUGALL: Thank you. I'm
22 here on behalf of Samuel J. Nasca, who has

1 been the New York State Director of the UTU
2 for 27 years, and I believe he has the
3 distinction of being the longest-serving full-
4 time State Director in that Union, and he has
5 participated in many ICC and STB proceedings
6 over the years.

7 I'm not going to read you the
8 statement and the little argument that I put
9 in for it. I'd like to give a little
10 background and explain the interest of UTU
11 people that have participated in the various
12 exemption proceedings. I checked over the
13 weekend, and since 1976 there have been 18 of
14 them.

15 Eighteen of those commodity
16 proceedings that you have listed have been --
17 there's been UTU representation generally in
18 opposition to it. There was one in which they
19 participated and they were successful, and
20 that was the export coal exemption case, which
21 the ICC turned down some years ago.

22 The general interest of employees

1 are that they see the exemption process not as
2 a way to compete for traffic but to get rid of
3 traffic, and there is some basis of experience
4 on that under the surcharge cases which
5 occurred, the branch line surcharges which
6 were in effect for about five years or more.

7 The carrier railroad rate changes
8 were based to get rid of traffic, not to
9 charge more and have the shippers be happy and
10 ship more. It was to discourage the traffic
11 preparatory to abandonment or if they just
12 didn't want to handle that particular
13 commodity, and there have been over six of
14 those cases actually went into the federal
15 courts during the late 1970s, early 1980s.

16 So there's a feeling that to be
17 exempt, which really the railroad don't want
18 to handle boxcar traffic. They don't want to
19 handle vegetables, and so therefore we
20 generally support regulation or the
21 possibility for a federal agency such as the
22 ICC or the STB to give relief to protect

1 traffic.

2 Now, what's been the change in the
3 last five or ten years? The big change has
4 been the great recession of the last five
5 years where the economists and a lot of
6 politicians look down on marketplace
7 economics.

8 The market is often irrational.
9 We don't always get the best result from the
10 marketplace. The word "competition" does not
11 appear in Section 10502. This Agency looks to
12 competition, and if they say, "If there's a
13 lot of competition, we don't need regulation."
14 Exact opposite is the case.

15 If there's a lot of competition,
16 you've got to have regulation so that it's
17 fair. That's why we had the 04 section. In
18 other words, you could have lower rates
19 between two points and higher rates
20 intermediate.

21 The fact of competition is not a
22 ground for exempting traffic. It's the

1 opposite. If traffic -- if the traffic is
2 moving okay, the shipper has relief under the
3 rate relief.

4 You know, Congress has set up a
5 rate schedule where the market dominance,
6 there's a regular formula, RV ratios and so
7 forth, but to say that if an industry -- a
8 commodity is competitive; therefore, we
9 deregulate it, it's just the opposite.

10 That's when you want regulation.
11 That's why we have a Federal Trade Commission.
12 It's why we have an anti-trust division of the
13 Department of Justice, to regulate
14 competition, because competition is often
15 irrational.

16 It gives us recessions. It causes
17 all sorts of diseconomies in our country, and
18 therefore we have to regulate competition.

19 That's the generally the position that
20 organized labor has had and the UTU Directors
21 feel that the exemption process --

22 It's a warning signal, see.

1 That's what you get for being the last person.

2 This is a test.

3 CHAIRMAN ELLIOT: The hearing is
4 over. We don't have any further questions, so
5 thank you for coming today. Please, everyone,
6 exit in an orderly manner, and the hearing is
7 adjourned. Thank you.

8 (Whereupon, the above-entitled
9 matter was adjourned at 3:17 p.m.)

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C E R T I F I C A T E

This is to certify that the foregoing transcript

In the matter of: Review of Commodity, Boxcar, and
TOFC/COFC Exemptions

Before: Surface Transportation Board

Date: 02-24-11

Place: Washington, DC

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NEAL R. GROSS

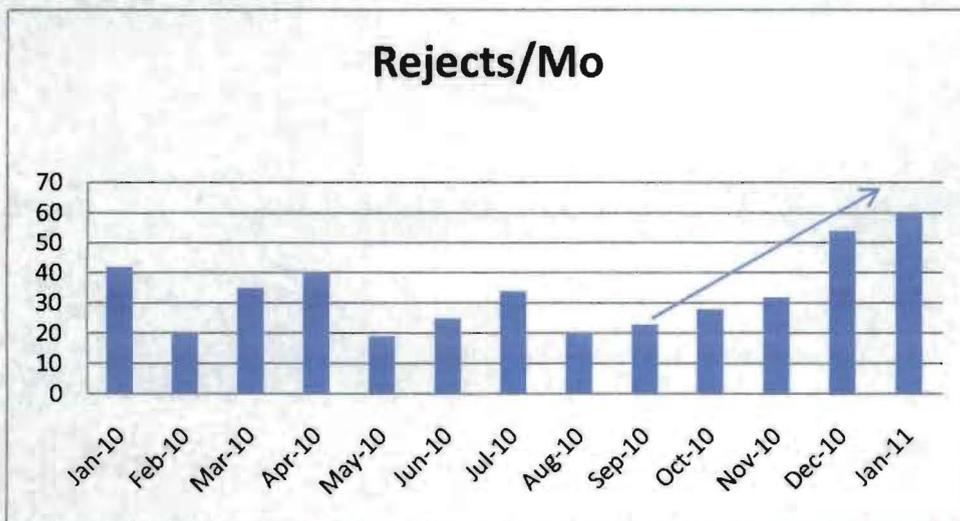
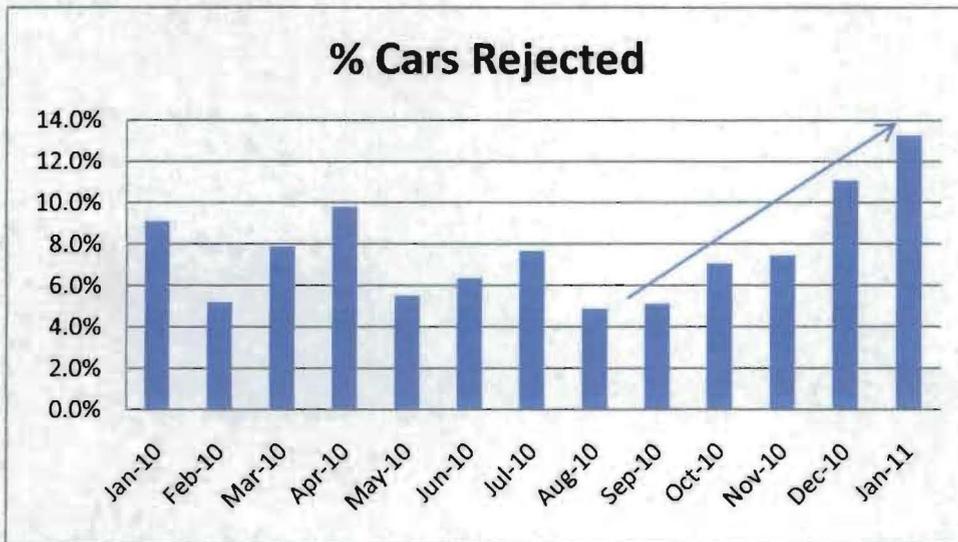
COURT REPORTERS AND TRANSCRIBERS

1323 RHODE ISLAND AVE., N.W.

WASHINGTON, D.C. 20005-3701

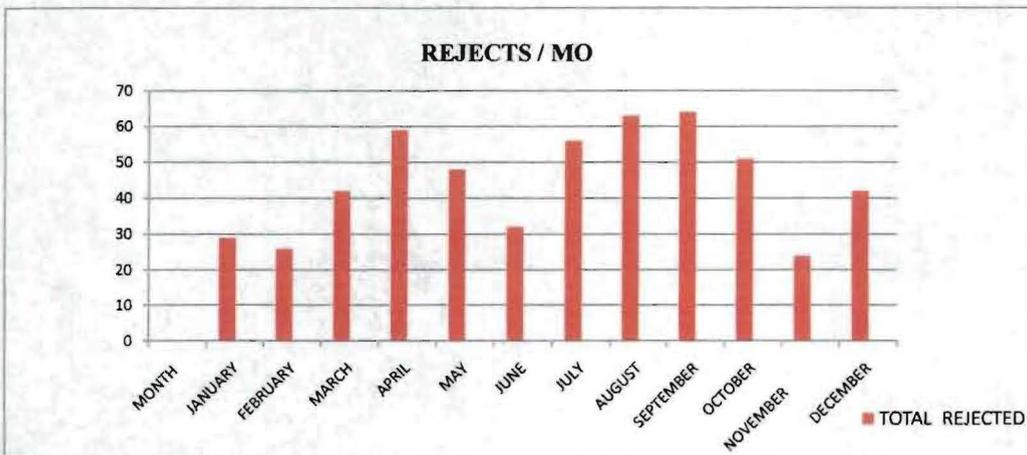
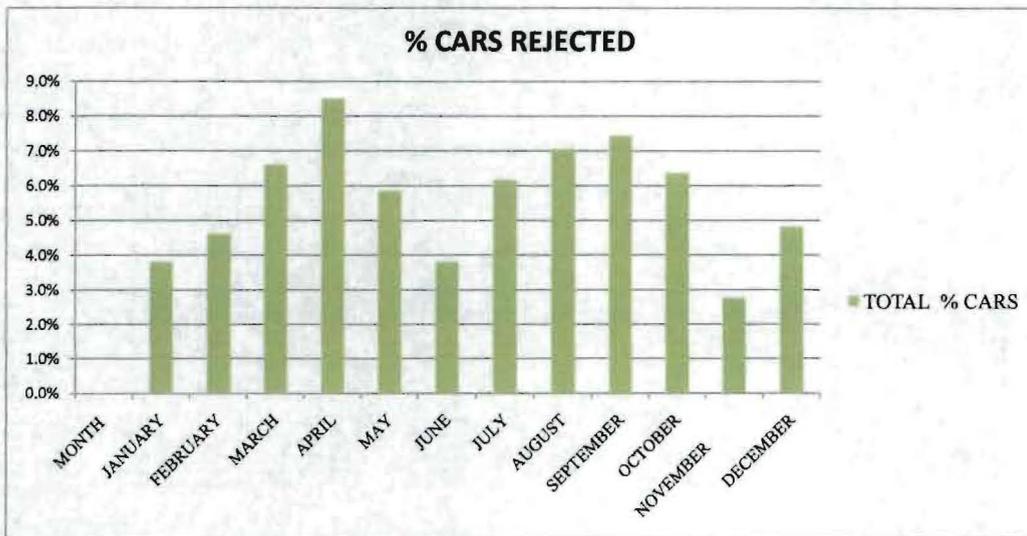
Data From Tomahawk Railway 2010. 2011

	#Loads	#Rejected	%
Jan-10	461	42	9.1%
Feb-10	384	20	5.2%
Mar-10	444	35	7.9%
Apr-10	408	40	9.8%
May-10	344	19	5.5%
Jun-10	393	25	6.4%
Jul-10	443	34	7.7%
Aug-10	410	20	4.9%
Sep-10	448	23	5.1%
Oct-10	396	28	7.1%
Nov-10	429	32	7.5%
Dec-10	487	54	11.1%
Jan-11	452	60	13.3%
Total:	5499	432	
Avg:	423	33.2	7.7%



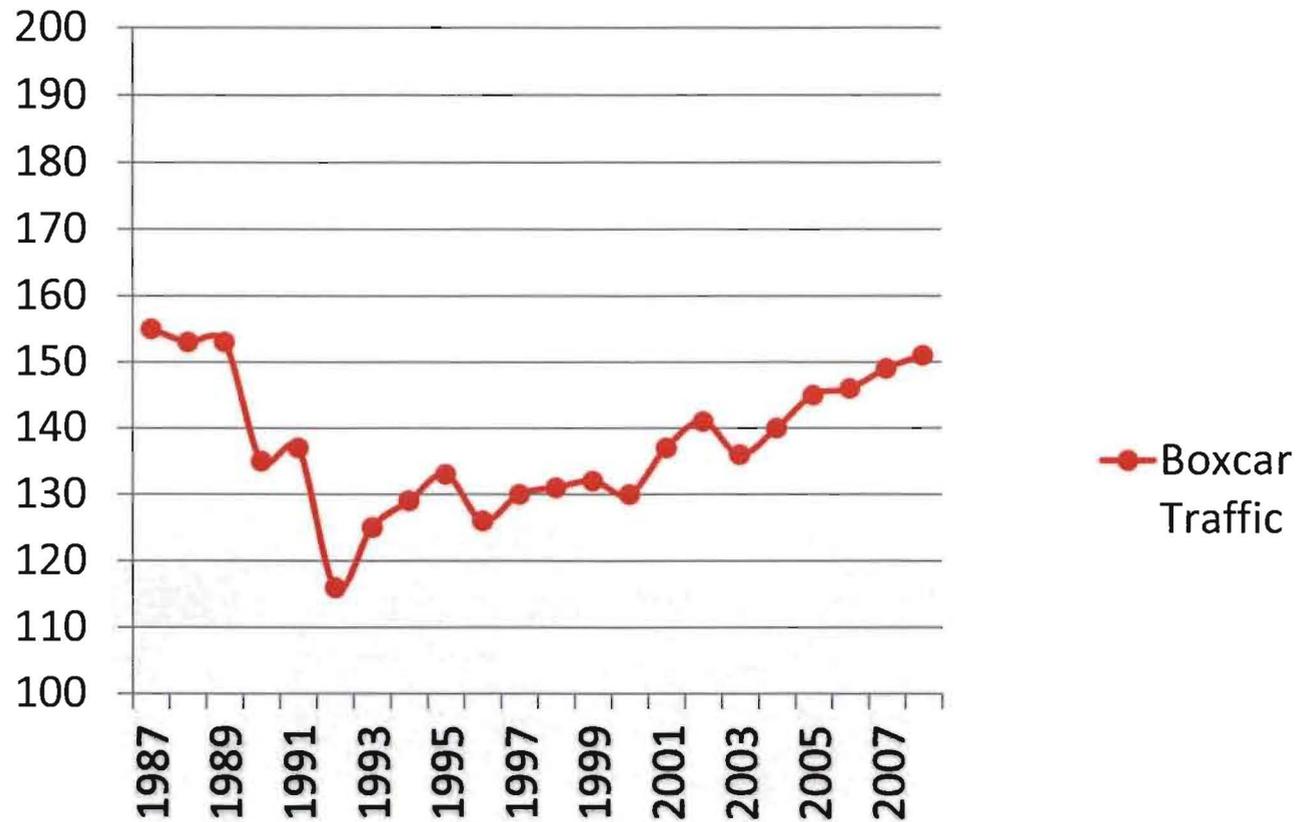
PCA COUNCE RAILROAD PERFORMANCE 2010 (% OF REJECTED BOXCARS)

<u>TOTAL</u>			
	<u>CARS</u>	<u>REJECT</u>	<u>% CARS</u>
<u>MONTH</u>	<u>SHIPPE</u>	<u>BOXCA</u>	<u>REJECTED</u>
JANUA	761	29	3.8%
FEBRU	563	26	4.6%
MARCH	635	42	6.6%
APRIL	694	59	8.5%
MAY	820	48	5.9%
JUNE	841	32	3.8%
JULY	908	56	6.2%
AUGUS	892	63	7.1%
SEPTEN	860	64	7.4%
OCTOB	802	51	6.4%
NOVEM	869	24	2.8%
DECEM	871	42	4.8%
TOTAL	9516	44.7	5.7%



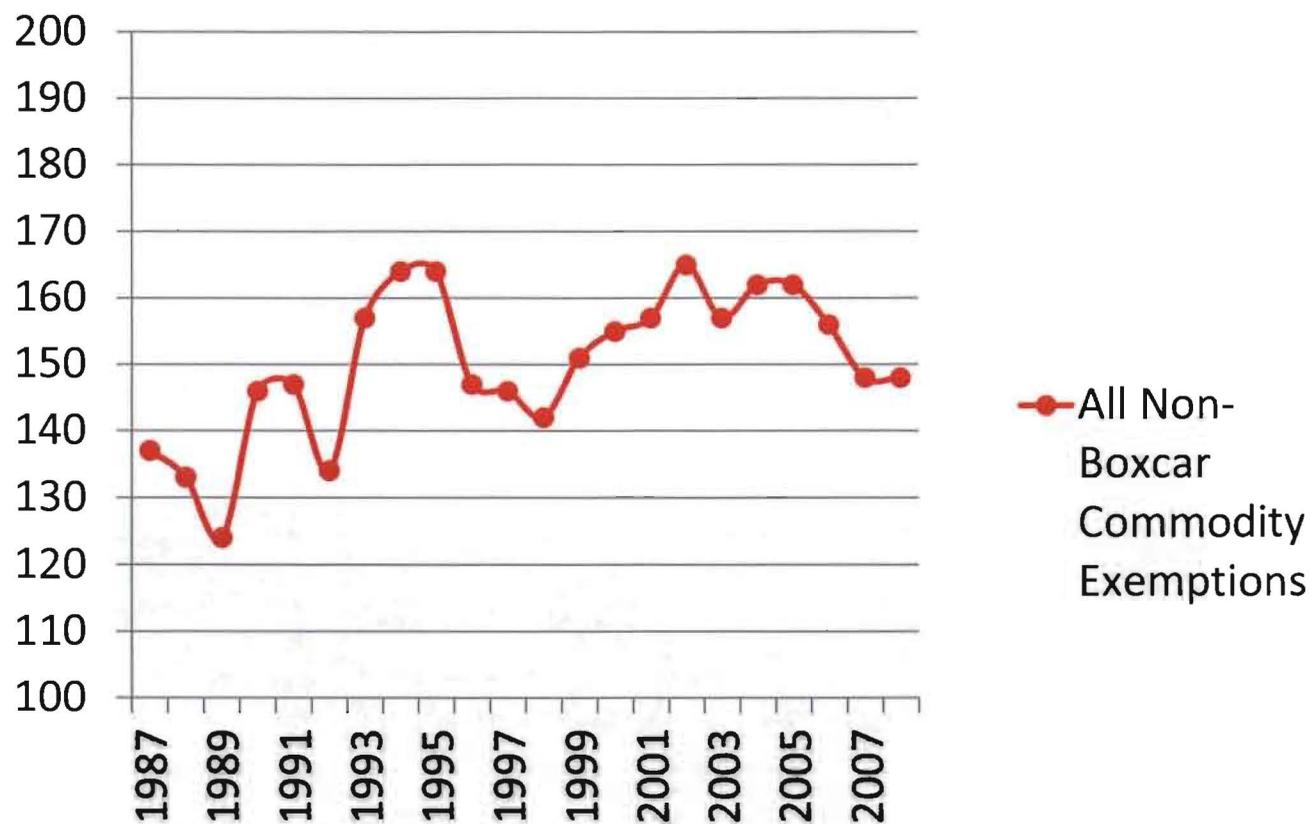
All Boxcar Traffic - R/VC Since 1987

URCS Costed STB Waybill Sample – Masked Revenue



All Non-Boxcar Commodity Exemptions - R/VC Since 1987

URCS Costed STB Waybill Sample – Masked Revenue



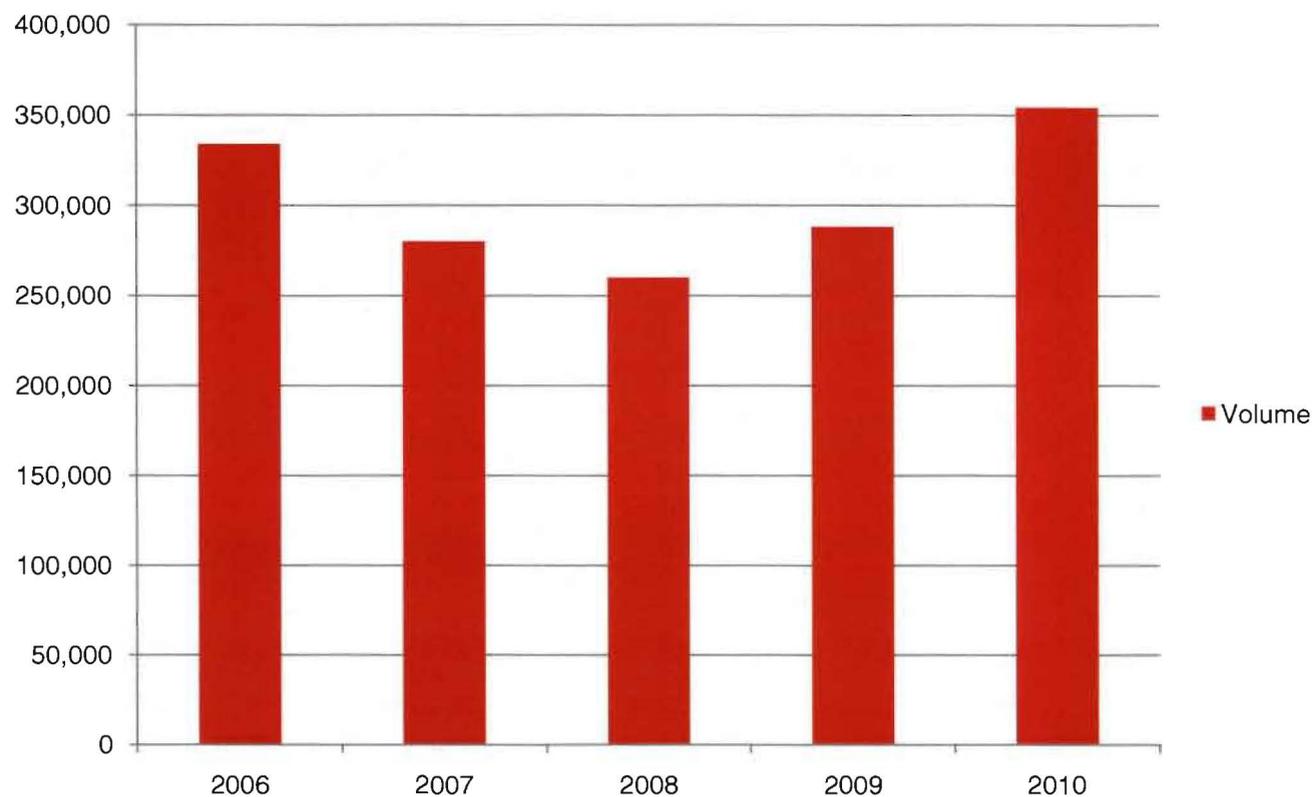


SURFACE TRANSPORTATION BOARD

PATRICK J. OTTENSMEYER
EXECUTIVE VP OF SALES & MARKETING



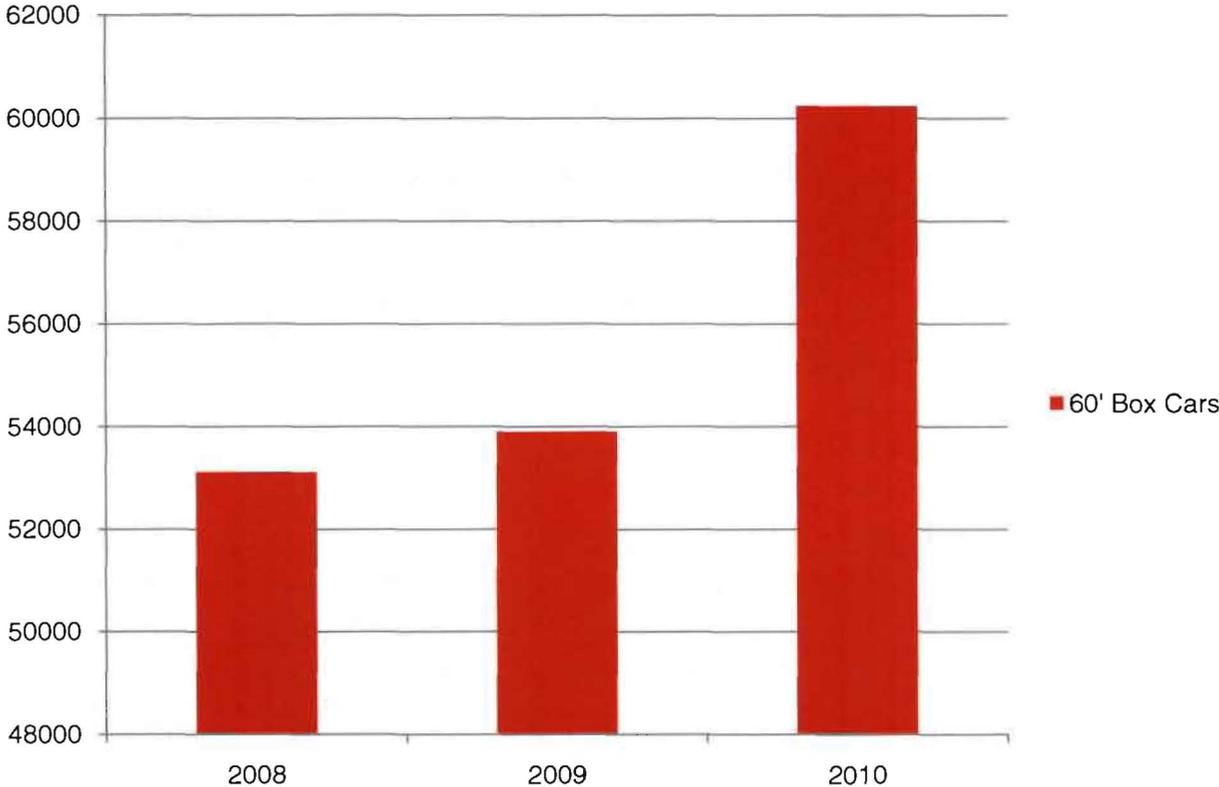
INTERMODAL GROWTH (VOLUME)



SOURCE: KCS Waybill Data



BOX CAR TRAFFIC (UNITS)

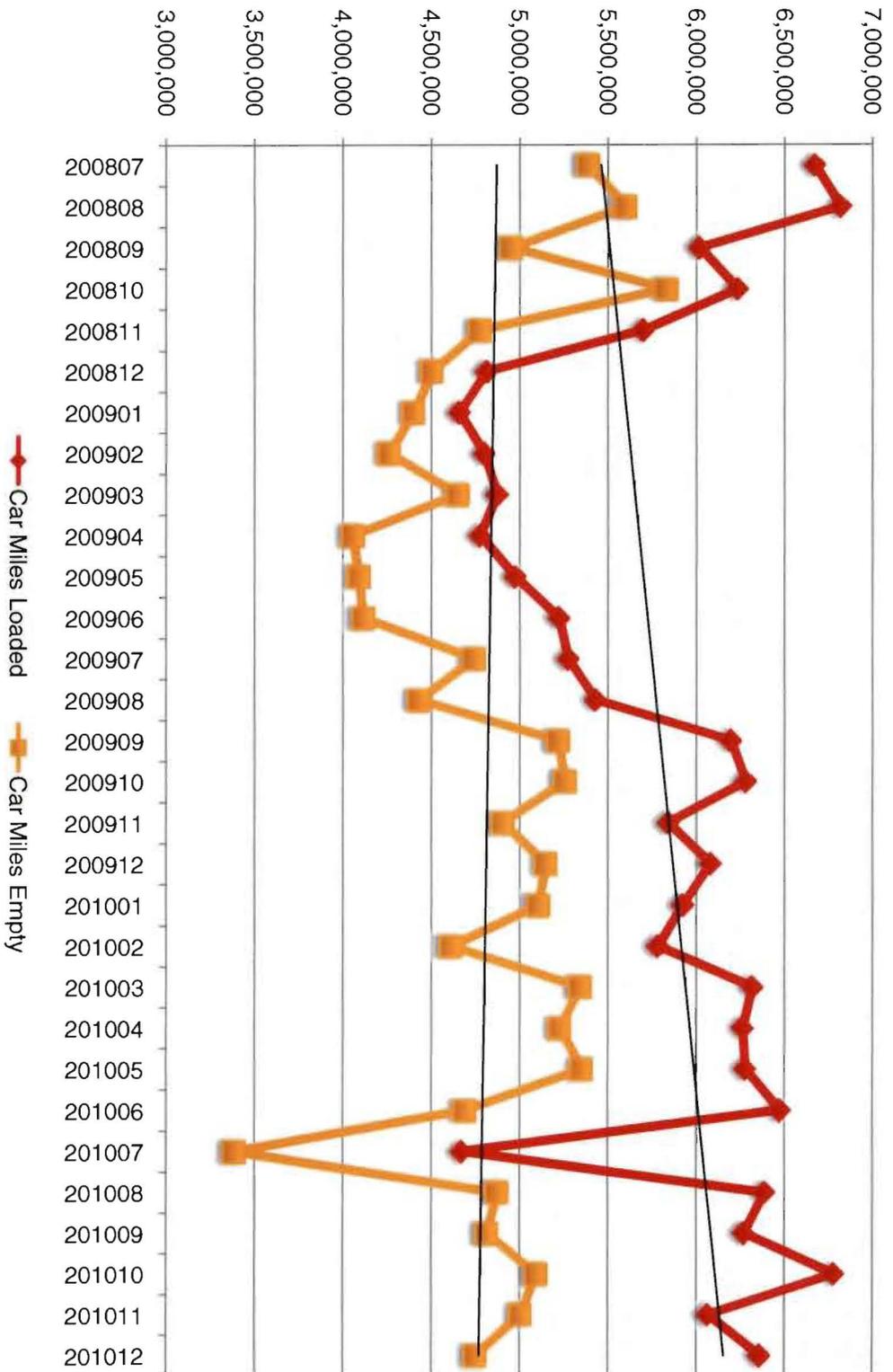


SOURCE: KCS Waybill Data



KCS Box Cars Total Car Miles Load vs Empty

July 2008 through December 2010

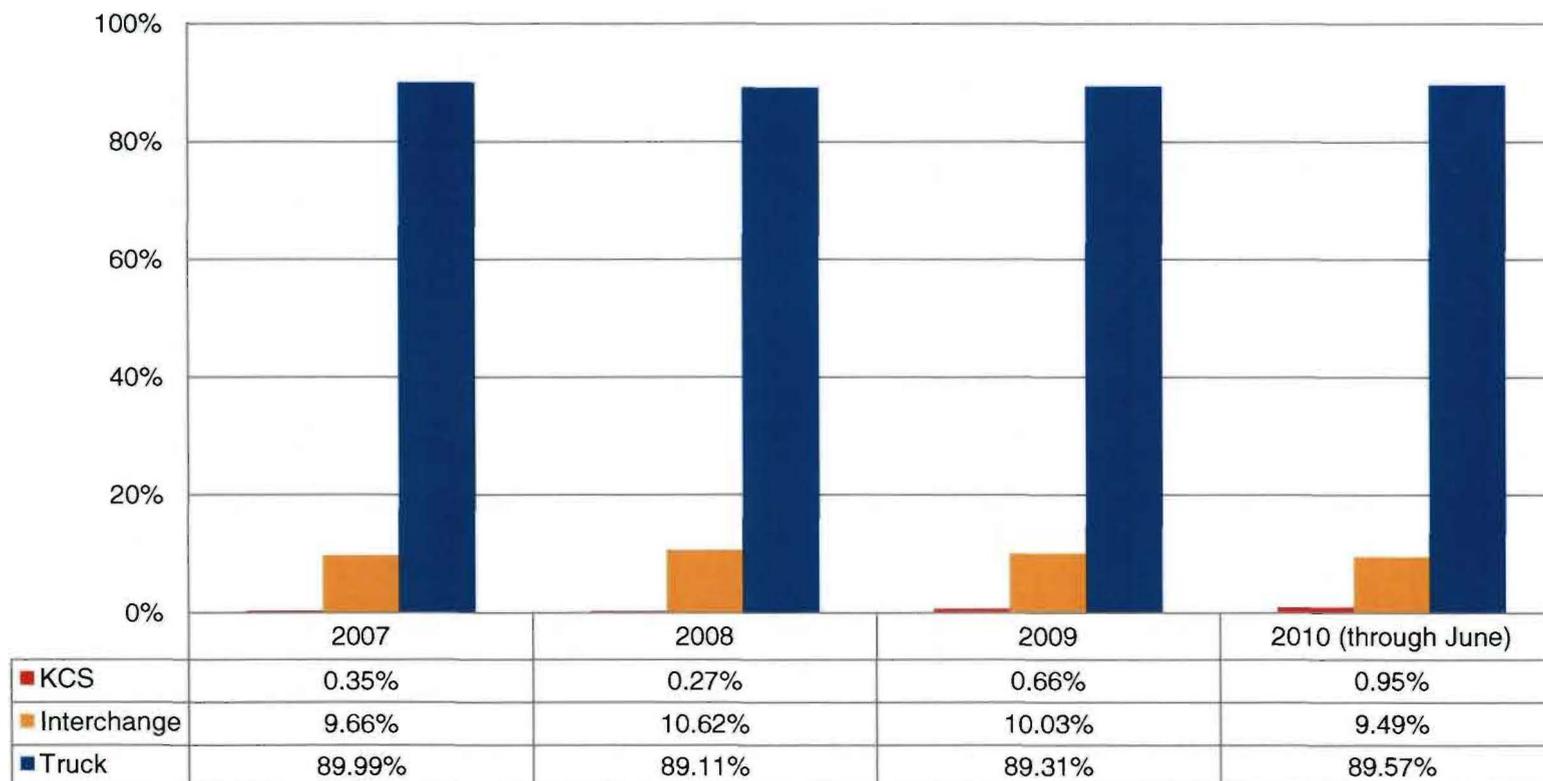


SOURCE: KCS Waybill Data



LAREDO: BORDER CROSSINGS/ENTRIES

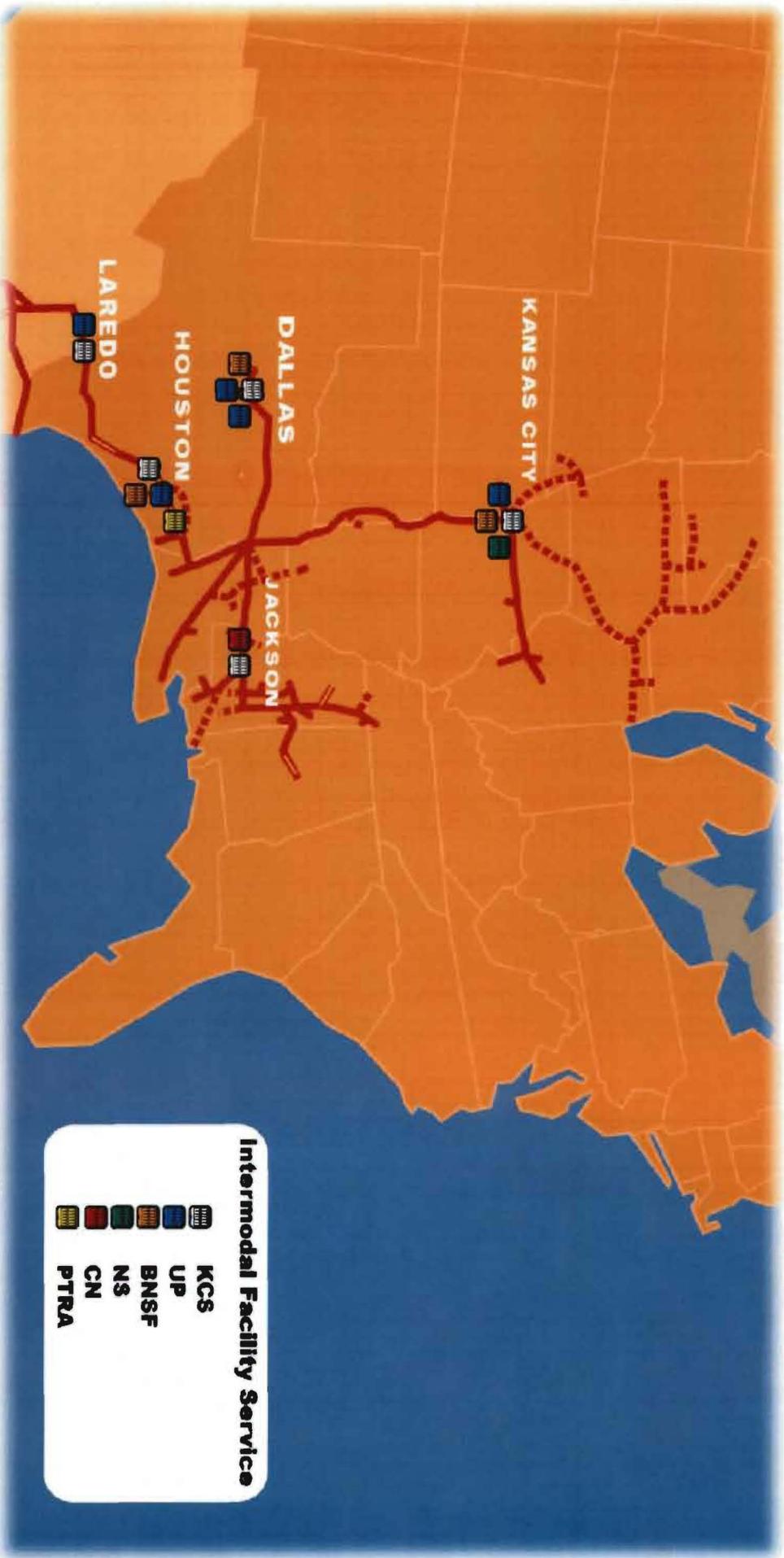
Intermodal Cross-Border Market Shares



SOURCE: KCS, U.S. Department of Transportation – Research and Innovative Technology Administration



INTERMODAL FACILITIES

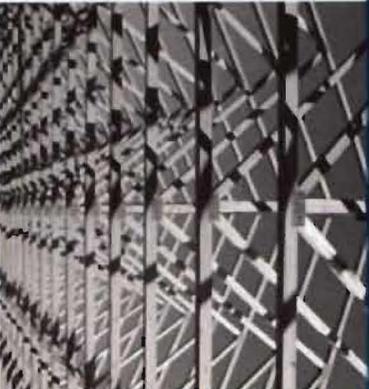


WWW.KCSOUTHERN.COM

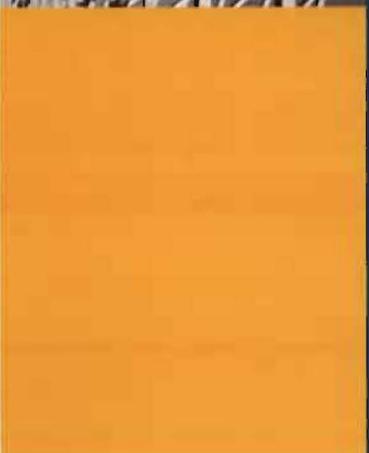




**STB Exemption Hearing, EP 704
February 24, 2011**



[CSX]
How tomorrow moves™



Executive Summary

- Congressional and Economic Preference for Market-Driven Rates and Services
- Experience Shows that the Current Regulatory Scheme is Working
- Competition Has Been and Remains Pervasive
- Continued and Increased Reinvestment is Required to Meet Present and Future Expectations

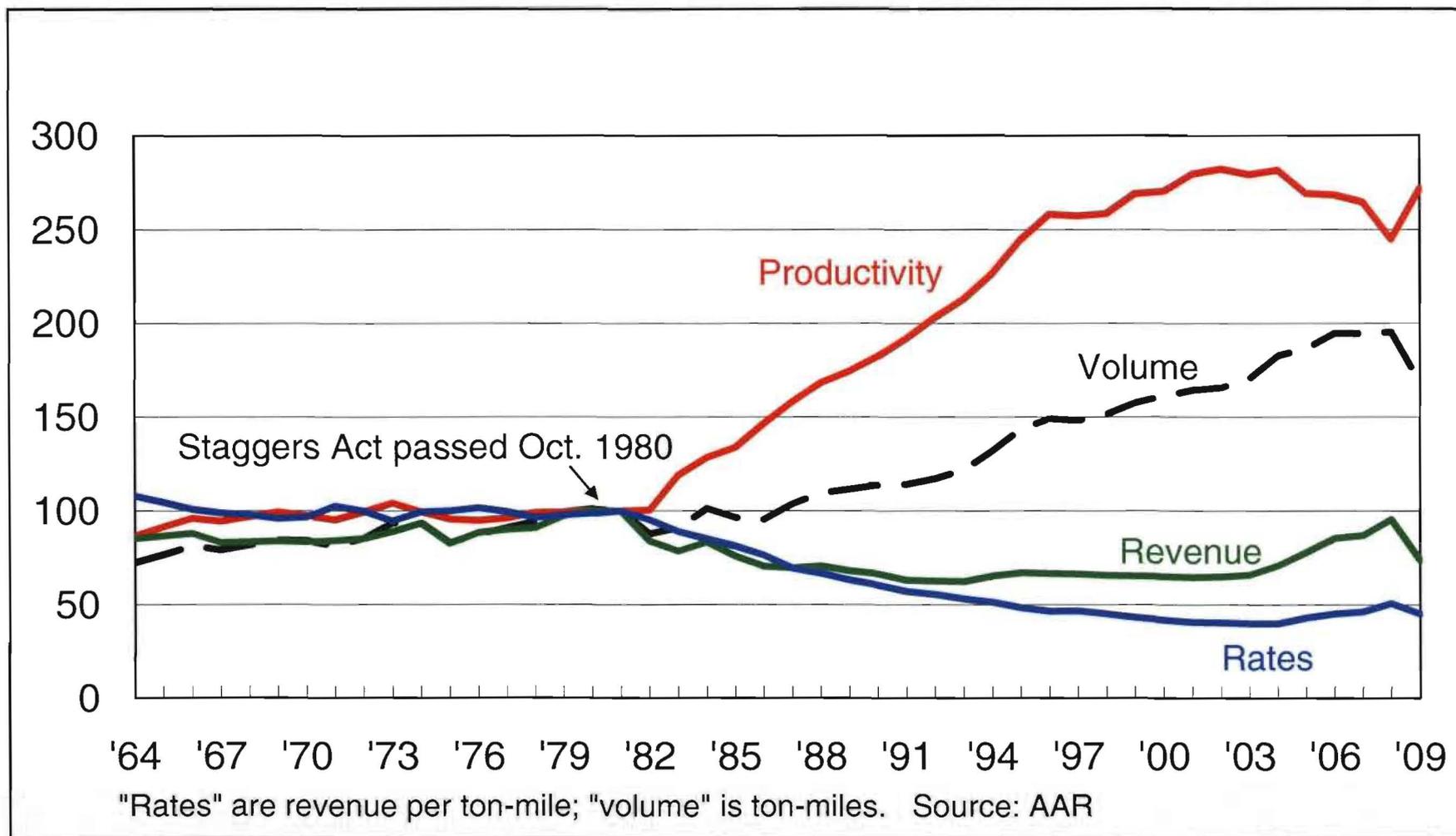
Market-Driven Solutions

- Primary Principle of Rail Transportation Policy:
 - Competition and demand should establish reasonable rates, to maximum extent possible

- Markets Guide Every Aspect of our Business:
 - What capacity to increase
 - What services to offer
 - What equipment to buy
 - What rates to charge

- Ultimate beneficiaries are the customers and consumers

Performance and Rates Since Staggers



Post-Staggers Cultural Transformation

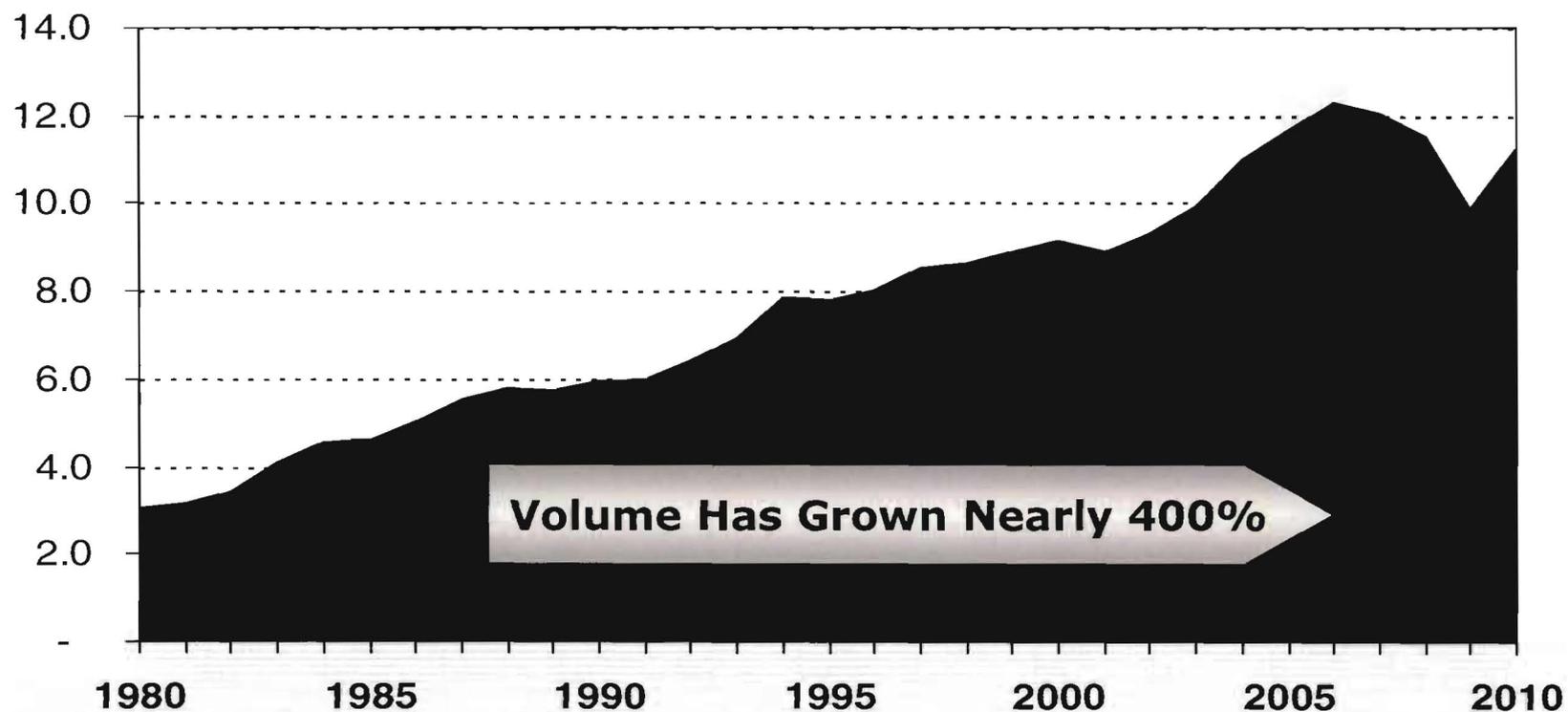
- Pre-Staggers Mentality:
 - Shippers accustomed to relying on public rates and traditional service
 - Railroad initiatives on rate adjustments and service experiments were delayed by internal regulatory review processes, and threat of being challenged
 - Result: disincentive for shippers and railroads to try anything new

- Post-Staggers Cultural Change:
 - Railroads shifted to a market-based environment
 - Normal market incentives drove new sense of energy and creativity
 - Result: improved service, increased efficiencies, and unprecedented reinvestment

Intermodal Success Story

Intermodal Loadings Growth

(millions of units)



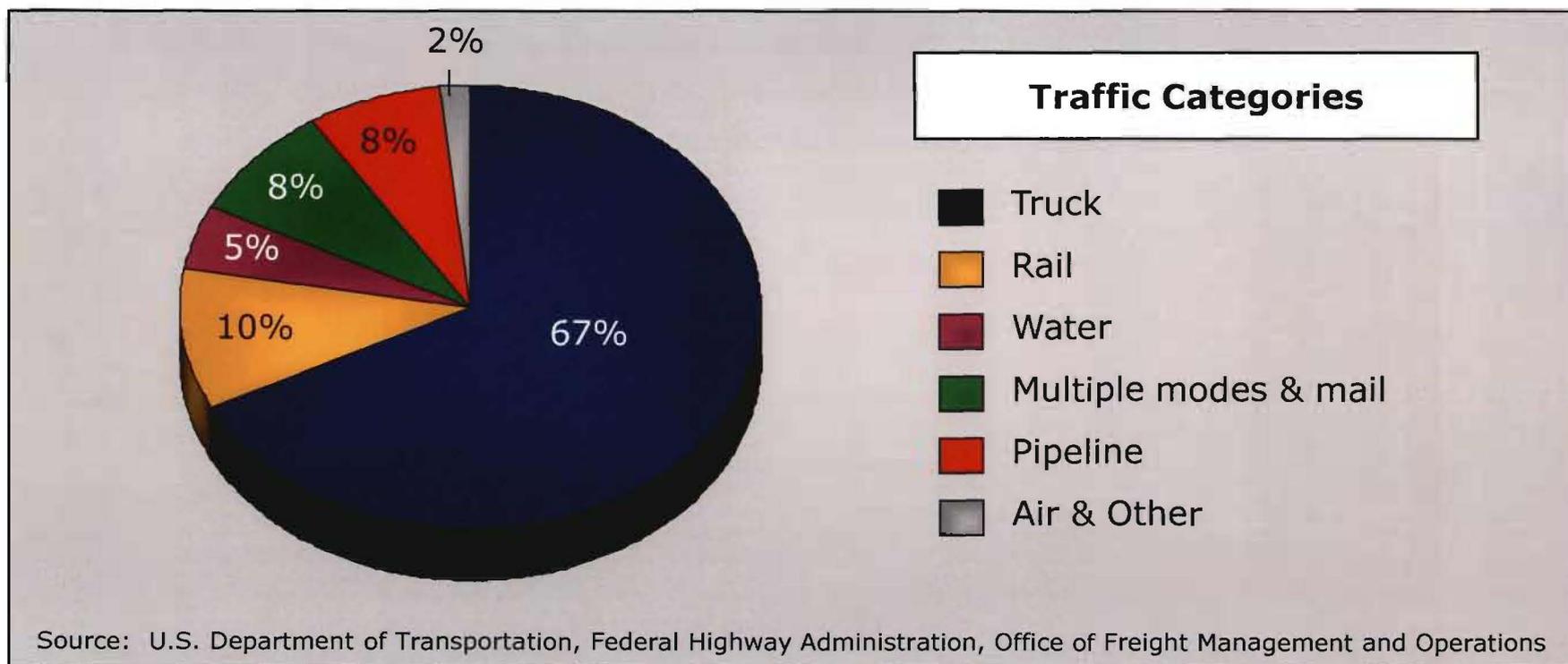
Source: AAR Weekly Railroad Traffic, AAR Fact Book

Northwest Ohio Intermodal Terminal



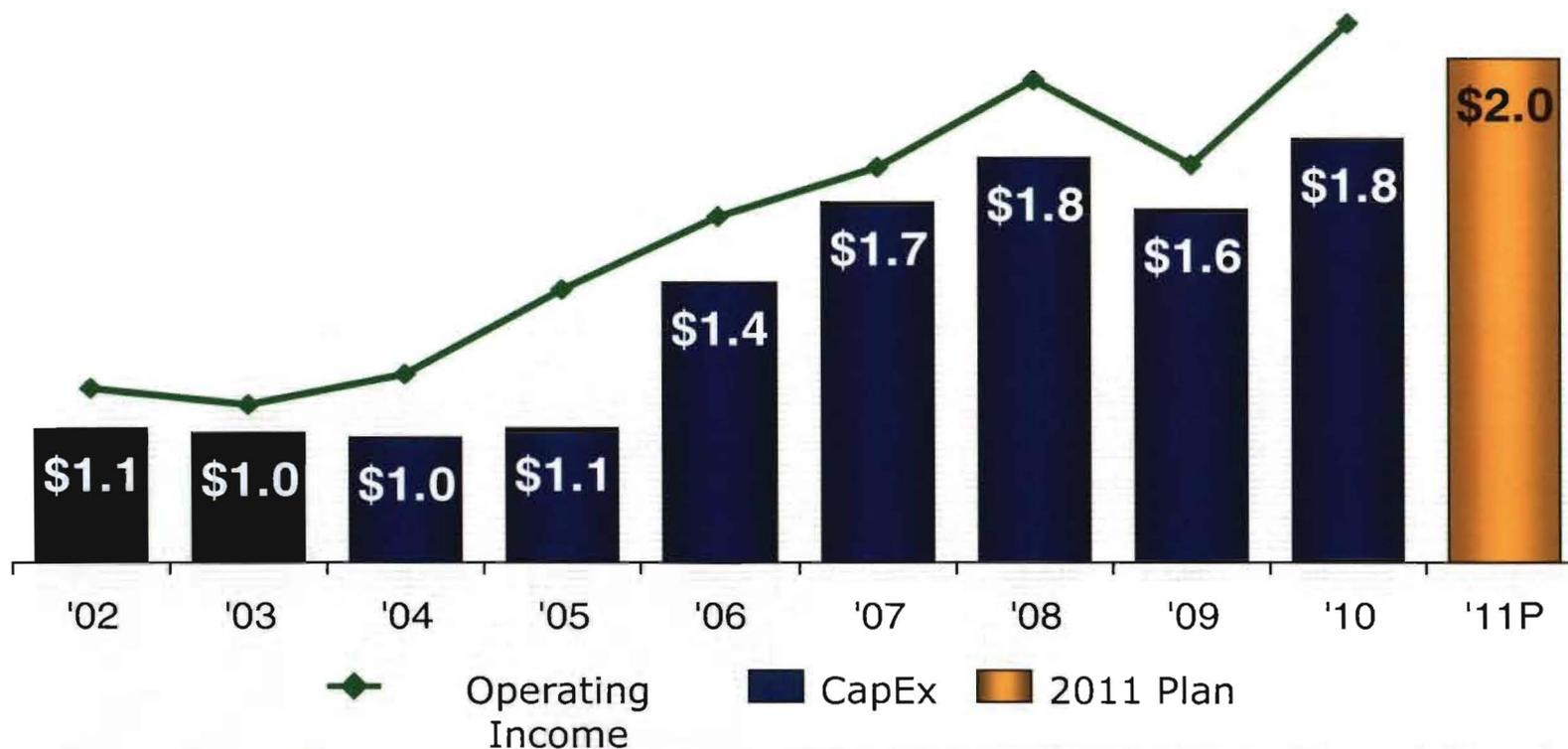
Competition Is Pervasive

Shipments by Transportation Mode 2009 (millions of tons)



Financial Progress Allows for Reinvestment

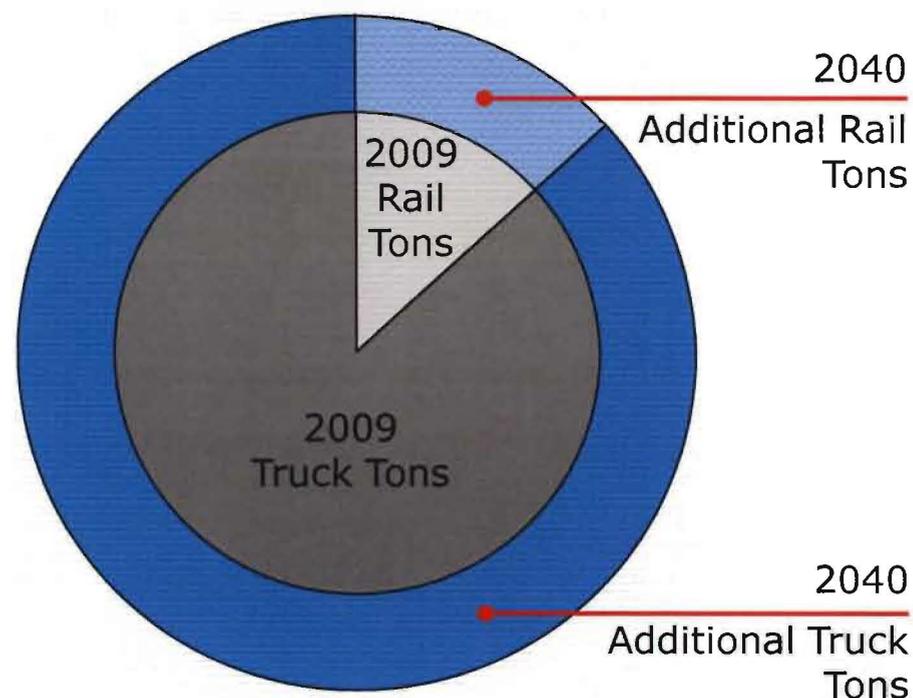
CSX Operating Income and Capital Expenditures
(Dollars in Billions)



The Need for Reinvestment Has Never Been Greater

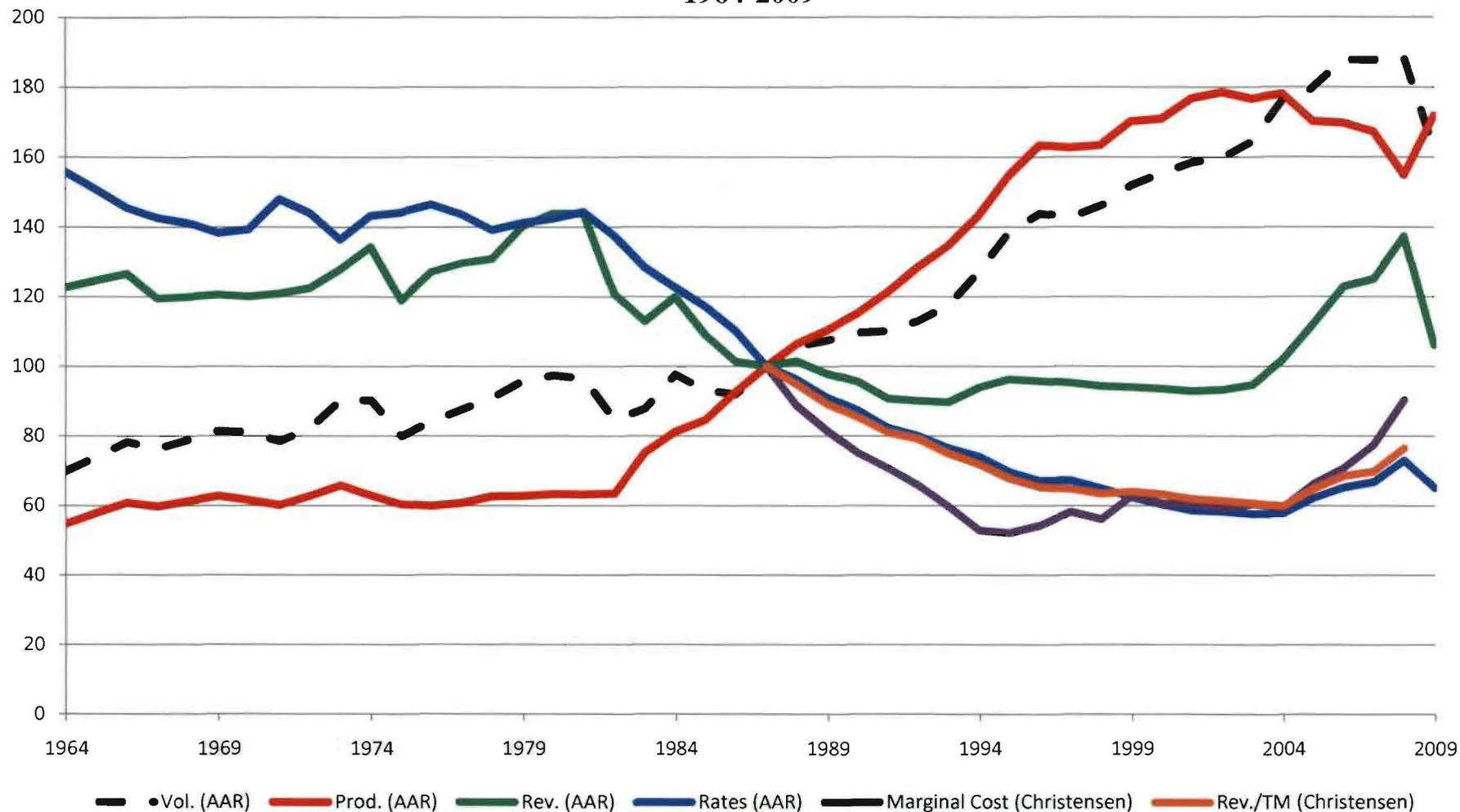
- Freight demand projected to increase 68% by 2040
— 16.1B → 27.1B Tons
- At current market share, Rail is expected to handle 1.3B increase in tons by 2040
- Due to Rail's efficiency and environmentally friendly nature, America expects rail to increase market share

Freight Demand: 2009 and 2040



Source: U.S. Department of Transportation, Freight Analysis Framework 2010

Figure 1
RAIL RATES, REVENUES, PRODUCTIVITY, TRAFFIC VOLUMES, AND MARGINAL COSTS
1964-2009



Source: AAR (Vol. (in ton-miles), Prod., Rev., and Rates (in RPTM)) and Laurits A. Christensen Associates, Inc. (Marginal Cost and Rev./TM) using data from *A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals that Might Enhance Competition* (Madison, WI, November 2008).