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BEFORE THE
SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 705
COMPETITION IN THE RAILROAD INDUSTRY

WRITTEN TESTIMONY
ON BEHALF OF OLIN CORPORATION
BY JOHN L. MCINTOSH, SENIOR VICE PRESIDENT, OPERATIONS

Chairman Elliot, Vice Chairman Begeman and Commissioner Mulvey, I am pleased to be here today on behalf of Olin Corporation as you examine issues relating to competition in the railroad industry. I have served as a corporate officer of Olin Corporation for 12 years, and have 34 years of experience in the chemical manufacturing industry. Olin Corporation's view of competition in the railroad industry is that there is no competition for captive shippers. Consequently, captive shippers are often forced to pay rates that far exceed what is necessary for railroads to earn a reasonable profit. In addition to excessive rates, captive shippers are also faced with increasingly onerous terms and conditions, such as the indemnity obligations contained in a recently published tariff that could essentially force Olin to become an insurer of the railroads against the negligence of third parties. Olin Corporation appreciates the Board's effort to address these issues in this hearing today and hopes that meaningful changes will be made to ensure that a vibrant and competitive rail system is available to all shippers who depend on rail transportation.

I. Olin Corporation and the importance of the chlor alkali industry.

Olin Corporation has its headquarters in Clayton, Missouri. As way of background, Olin consists of two businesses: Winchester Ammunition, a leader in small caliber ammunition production and a supplier to U.S. law enforcement and military; and Chlor Alkali Products, a leading producer of bulk chlorine, caustic soda, bleach and other chemicals in North America. Today, I am testifying on behalf of Olin's Chlor Alkali Products business, which is headquartered in Cleveland, Tennessee and includes manufacturing sites in New York, Georgia, Tennessee, Alabama, Nevada, Louisiana, California, Washington state and Quebec, Canada.

We have been involved in the U.S. chlor alkali industry for over one hundred years, and we were the first commercial supplier of chlorine in the United States. Olin is a publicly traded company that has been listed on the NYSE since 1917. We continue to grow and service the public and expect to be in business for another hundred years.

As one of the nation's leading producers of chlorine, Olin produces an essential chemical that has played a key role in dramatically reducing infant mortality rates and eliminating water-borne diseases around the world. Chlorine chemistry is essential to everyday life. The products of chlorine chemistry make possible clean water and safe foods, pharmaceuticals, medical equipment, construction materials, computers, electronics, automobiles, clothing, sports equipment, agriculture and much more. For the majority of these applications, there are no reasonable substitutes for chlorine.

Chlorine products and their derivatives also have a significant impact on the U.S. economy, contributing more than $46 billion each year. The chlor alkali industry alone contributes over $7 billion directly to the U.S. economy each year.

In addition to its importance to our Nation's health and economy, chlorine is vital to U.S.

security. The Department of Homeland Security has deemed chlorine to be an essential asset to the "critical infrastructure." Moreover, chlorine is used in materials that promote the national defense, including bullet-proof vests, helmets, and parachutes. In sum, chlorine plays an essential role in our Nation's health, economy and security.

II. The importance of rail transportation to Olin Corporation.

Rail transportation is essential to Olin Corporation and to the chlor alkali industry. Olin has shipped chlorine by rail for more than 100 years. Each year, Olin ships more chlorine by rail than any other producer in the world. The importance of reasonable rail transportation to Olin, the chlorine industry and the public cannot be overstated. Due to the nature of chlorine and the volume of chlorine that is produced, there is no reasonable economic alternative to shipping chlorine by rail. Rail transportation is also critical to the safe shipment of chlorine as it keeps large volumes of chlorine off of our Nation's highways and roads.

Railroad executives have indicated that railroads would not carry TIH products, like chlorine, if they were not required to do so under the federal common carrier obligation. If the wishes of these railroad executives were met, the chlorine industry could not survive in the United States as there is no reasonable alternative to rail transportation for chlorine. Class I railroads should not be permitted to decide what industries succeed in the United States.

Because there is no reasonable alternative to shipping chlorine by rail, rail rates are of critical concern to chlorine manufacturers such as Olin. The cost of shipping makes up a substantial percentage of the price of chlorine. Thus, an increase in rail rates has a direct effect on the prices that consumers pay for goods that are made with chlorine. Furthermore, in some instances where manufacturers have existing supply contracts at set prices, the cost of unreasonably high rail rates are borne directly by the manufacturer. Although a manufacturer can take steps to protect itself from some risks—such as acts of God, natural disasters, etc.—through insurance or other means, the risk of unreasonably high rail rates cannot be adequately protected against or avoided.

III. Olin Corporation as a captive shipper.

The risk of unreasonably high rail rates is most damaging in situations where shippers are captive to a single railroad. Such is the case with Olin's chlor alkali facilities. Under current regulations, our facilities can only be accessed by a single railroad; therefore, there is no competition to regulate rail rates. Due to the lack of competition, Olin is subject to whatever rates or terms the monopoly railroad chooses to impose.

The difficulties faced by captive shippers are well documented in Exhibit A to Olin's comments, which provide Olin's experience in managing the operations and logistics of the SunBelt chlor akali facility in McIntosh, Alabama. SunBelt is a perfect example of how the lack of competition for captive shippers allows railroads to impose onerous rates and terms. The original rate provided by the NS for the SunBelt movement in 1997 was $1,440/car. The current tariff rate is $11,763/car, an increase of 817% over the original contract rate. For comparison, the consumer price index has increased only 40% over this same time period. The greatest rate increases did not begin until approximately 2002. Since December, 2002, the chlorine line-haul rate for this lane has increased approximately 600%. Furthermore, as documented in Exhibit A to Olin's comments, the NS has systematically denied competition for the SunBelt movement despite the existence of an interchange in Mobile that is only 40 miles from the SunBelt facility.

Olin believes that the dramatic increase in rail rates is a direct result of the current system of regulation that does little to prevent abuse of captive shippers by railroads and places unrealistic burdens on shippers who seek relief. The principal tool available to shippers, an SAC rate case, is widely considered to be ineffective for several reasons. Foremost among these reasons is the high costs associated with a rate case. For example, the cost of an SAC rate case for the SunBelt movement has been calculated to be approximately $12 million dollars, which includes legal and consultant fees and the increased tariff freight rate that would need to be paid during the pendency of the action.

In addition to the high cost, shippers are also discouraged from pursuing rate cases because of the long periods of time necessary to prosecute a case. Furthermore, even if relief is eventually obtained through an SAC rate case, the results may be short lived if the shipping lane changes due to a change in customer demand. For these reasons, shippers often are forced to choose the "lesser of two evils," i.e., a contract rate that is lower than the published tariff, but that is higher than what a reasonable rate should be. Although private contracts for rail transportation often contain unreasonable terms and rates, they avoid public scrutiny because they are not reviewable by the STB and because they contain confidentiality provisions. This abuse is exemplified by one Class I carrier continuing to demand a rate-based fuel surcharge in its contracts despite the STB ruling this is an unreasonable practice.

Shippers are also deterred from pursuing rate cases because they are aware that rate cases do little to change railroad behavior towards captive shippers. For example, it is public knowledge that DuPont has brought 5 rate cases, yet the railroads apparently continue to impose unreasonable rates on DuPont. Shippers are also aware that railroads have little incentive to provide a reasonable tariff rate to captive shippers. Even if a shipper succeeds with a rate case, the "penalty" to the railroad is that it only can charge what it should have charged in the first instance, a reasonable rate. Although a railroad incurs costs in defending against a rate case, those costs are easily made up by the many shippers that simply sign a contract and endure unreasonable rates and terms.

Olin's experience with SunBelt provides a pointed illustration of the way that captive shippers are cornered into paying unreasonable rates without any avenue of relief. Although SunBelt has recently begun shipping under tariff and is bringing a rate case against the NS, there is no recovery for the years spent overpaying for the SunBelt movement under private contract.

The difficulties faced by Olin are similar to the difficulties faced by many other captive shippers. Although railroads attempt to justify their treatment of Olin and other chemical shippers on the basis that chlorine is a TIH product, the experiences of other captive shippers, such as the coal and wheat producers that have commented in this proceeding, establishes that this is not a TIH issue. Rather, this is an issue of railroads charging what they can because they can. For these reasons, Olin joins with many other captive shippers to encourage meaningful change in rail policy and regulations.

As indicated in Olin's initial and reply comments, Olin believes that an R/VC ceiling may be the simplest solution to the unreasonable rates imposed by railroads on captive shippers. Adopting an R/VC ceiling would allow railroads to earn a reasonable profit while protecting shippers from excessive rates without the need of an expensive, time consuming and complicated rate case. As noted by the U.S. Department of Agriculture in its reply comments, "A corresponding R/VC ratio adopted as a ceiling (or a rebuttable presumption of a maximum reasonable rate) would seem to be just as straightforward to calculate and not require the devotion of significant resources by all parties that has been the characteristic of rate cases under the SAC tests." In addition to its simplicity, the U.S. Department of Agriculture correctly recognizes additional benefits to an R/VC ceiling:

> Moreover, an R/VC ceiling has at least one advantage over the types of competitive access options discussed above: a relatively high level of certainty about its effects. It is relatively easy to estimate what the effect of such ceiling would be on the revenues of the railroad industry, and the level of the ceiling can be calibrated to achieve whatever balance between rate relief and revenue adequacy is considered desirable from a rail competition policy standpoint. By contrast, new regulatory polices with uncertain effects tend to discourage investment, both by investors in railroads and by railroads in capital projects. An R/VC ceiling has the additional benefit of focusing a remedy on the most egregious cases of high rates caused by lack of competition, and does not depend on the competitive response of a second carrier (which, as already noted, some parties have alleged to be less than might be expected).

Olin is grateful to the Board for initiating this proceeding and hopes that the Board will consider the many proposals submitted in this proceeding and choose the best way to respond to the changes in the rail industry and the challenges facing shippers and railroads. Olin, and other captive shippers, would appreciate any changes to encourage competition as the current state of competition in the rail industry for captive shippers is that there is no competition. Thank you for your time and for the opportunity to present this testimony.

Respectfully submitted on behalf of the Olin Corporation by:

/s/ John L. McIntosh
John L. McIntosh, Senior Vice President, Operations