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COMPETITION IN THE RAIL INDUSTRY

Reply Comments of the National Grain and Feed Association

The National Grain and Feed Association (NGFA) is a voluntary trade association of grain, feed and processed product shippers that have approximately 7,000 locations throughout the United States. Grain, oilseeds (soybeans primarily), feed ingredients, and processed products (ethanol, soymeal, soy oil, corn processing by-products and wheat milling by-products).

Dominant themes in Railroad Initial Filings

The carriers' dominant themes in initial comments in this proceeding were that, in general, there was ample competition in most markets to discipline behavior by the railroads; and, where less than adequate competition might exist, there were readily accessible remedies for shipper or receiver customers. Also, an underlying theme from the carriers was that since the Staggers Rail Act and subsequent regulations had worked to help revive the financial health of railroads, nothing should be changed in current law or regulation.

The NGFA does not dispute that there are some marketplace situations where there is adequate competition to discipline behavior. In some cases the competition comes from other railroads; in other situations the competition comes from a competitive transport mode, either trucks or barges.

But where there is a lack of overall competition in a particular market, the NGFA disputes the notion that there are cost-effective and practical remedies available to rail customers to address the situation. Without criticizing the current STB, which is trying to streamline the regulatory process and make it more affordable and accessible, the agricultural shipping industry has confronted some very difficult processes at the ICC and STB in the past that discouraged the pursuit of regulatory relief where inadequate competition existed. Examples include everything from the regulatory process taking more than five years to complete a case to the agency being unresponsive to requests for an injunction on railroad rules and practices that had not yet become effective.

The Agricultural Industry and Rail Rates

The grain- and oilseed-based agricultural industry in the United States is extremely price sensitive. It is largely commodity-based, so the least-expensive product delivered to a market generally obtains the business volume in that market. As demonstrated in the NGFA's *(et. al.)* original comments in this proceeding, average rail rates for agricultural shipments increased 30 percent in four years (between 2006 and 2010). While the U.S. agricultural industry does not necessarily seek to be the "cheapest" freight compared to other industries – if it is, it may lose service at some stage – if rates continue to spiral upward (even in recession periods like 2007 and 2008) some agricultural production regions will lose business volume. U.S. agriculture consists of geographically fixed physical assets serving agricultural producers – farmland cannot be moved like factories theoretically could to address transportation cost structures. If certain sections of the United States lose markets because of excessive transportation costs, then the U.S. agriculture sector as a whole will lose its competitive edge in global markets. And the nation will lose jobs and the extremely positive contribution U.S. agriculture makes to the U.S. economy.

The NGFA's advice on addressing rail rates is for the STB to reconsider its decision in the 3-B small rate case. The benefits that potentially could be achieved from rate challenges need to be a minimum of $3 million over five years, not the current level of $1 million. Otherwise the benefit-cost ratio, when coupled with the probability of success in a case for the shipper, simply does not make business sense. At the same time, we continue to believe that even with this change, few rate cases would be brought before the STB. Such a change, though, could be helpful in modifying rail carrier behavior to at least sit down and have a dialogue with the customer to keep the customer competitive in markets, and keep both the shipment volume and overall rail volume at a high level.

Railroads' market share of grains and oilseeds has declined from 50 percent in 1980 to about 35 percent currently. Pricing of rail services and strong competition from other modes have contributed to that decline. Our industry wants rail volumes to stabilize or increase. But to do that, carriers must calculate the impact of their own pricing on the eventual business volumes from the agricultural industry.

Switch Charges and Terminal Access

One of the Class I carriers in this proceeding offered the following argument on switch charges (which in many cases have been elevated to $500 to $700 per car, or roughly five-to-seven times the variable cost of conducting the switch): "For several decades, under the cloak of seeking "competition," certain shippers have asked Congress, the Interstate Commerce Commission ("ICC") and the Board for a regulatory regime that would allow shippers served by a single railroad to have government-mandated access to service by other railroads. Some have sought a change in the law to allow shippers to obtain forced interchange, such as 'reciprocal switching'....Others have demanded forced access, such as terminal trackage rights...."

Carriers should not have a free hand to cut off existing access to markets through absolute closures of intersection points or by economically pricing the switch beyond any reasonable availability for market access. Because switch charges are a major conduit to maintaining a national network of rail freight, railroads should not have the degree of pricing freedom on switches that they currently are given on long-haul rail rates (which can vary from 100 percent of variable cost to 400+ percent of variable cost). To allow such autonomy on switch charges will have a negative impact on the competitive fabric of the nation's economy.

Several policy options exist to ensure that switch rates do not become barriers to access to markets. In its original comments, the NGFA suggested that the STB consider establishing a revenue-to-variable cost threshold for switches, and if the railroad charges for such switches exceeded the threshold (e.g., 180 percent), the burden of proof that the switch cost is reasonable should shift to the carrier.

One additional issue regarding switch rates that can be shown is that the intention is often the de-marketing of rail traffic such that switch rates should be treated as an unreasonable business practice, rather than a rate case. Rate cases are extremely expensive to pursue, and improved regulatory access where there is an absence of viable competition is a necessary element to improving competition and the regulatory balance.

Alternative Mechanisms to Resolving Disputes

The NGFA has an arbitration system that can be used to address disputes between carriers and shipper/receiver members of the NGFA. Within the agricultural sector, this system is available only to NGFA members, so many shippers cannot take advantage of it.

We believe the STB could establish a similar government-based dispute-resolution system for a broader range of shippers, or other industries could initiate something similar on a private basis. Either way, creating better access to dispute-resolution, in the NGFA's view, does not encourage litigation. To the contrary, the NGFA's experience has been that it actually discourages litigation and its many downsides, such as excessive costs and lengthy time periods for resolution. But effective dispute-resolution does encourage business-to-business dialogue that quickly and efficiently can eliminate challenges to remaining competitive.

The NGFA holds the view that an arbitration system could be used for a number of types of disputes between carriers and their customers, such as unreasonable practice complaints. There may be practical limitations for certain types of disputes, but the concept is sound if well-managed. And, it could be helpful in managing the utilization of scarce government resources from the STB in addressing market challenges.

The NGFA appreciates the opportunity to submit these reply comments, and thanks the STB for initiating this proceeding.

Respectfully submitted,

National Grain and Feed Association

Dated: May 27, 2011