



**ASSOCIATION OF
AMERICAN RAILROADS**

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May 8, 2009

The Honorable Anne K. Quinlan
Acting Secretary
Surface Transportation Board
395 E Street, S.W.
Washington, DC 20423-0001

Re: STB Ex Parte No. 680 (Sub-No. 1), Supplemental Report on Capacity and
Infrastructure Investment

Dear Secretary Quinlan:

Pursuant to the order of the Board served April 8, 2009, attached are the
Comments of the Association of American Railroads for filing in the above proceeding.

Respectfully submitted,

Louis P. Warchot
Attorney for the Association of
American Railroads

BEFORE THE
SURFACE TRANSPORTATION BOARD

Ex Parte No. 680 (Sub-No. 1)

SUPPLEMENTAL REPORT ON CAPACITY AND INFRASTRUCTURE INVESTMENT

COMMENTS OF THE
ASSOCIATION OF AMERICAN RAILROADS

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Introduction and Overview

In a Notice served April 8, 2009, the Surface Transportation Board (“Board”) sought comments on an independent study prepared by Christensen Associates, Inc. entitled, *Supplemental Report to the U.S. Surface Transportation Board on Capacity and Infrastructure Investment*, released on April 8, 2009 (“*Christensen Capacity Report*” or “*Report*”). The *Christensen Capacity Report* supplements an earlier report prepared by Christensen Associates, *A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals That Might Enhance Competition* (released in November 2008).¹

The Association of American Railroads (“AAR”) hereby submits these comments on behalf of its member freight railroads. The AAR’s members account for 75 percent of U.S. freight rail mileage, 92 percent of employees, and 95 percent of revenues.

¹ The earlier Christensen report provided qualitative and quantitative research on the U.S. freight railroad industry on issues relating to competition, rates, capacity and service. The report was the subject of a public meeting held by the Board on November 6, 2008 in Ex Parte No. 680, Study of Competition in the Freight Rail Industry and public comment solicited at the Board’s November 6, 2008 hearing. The AAR’s December 22, 2008 comments in Ex Parte No. 680 are incorporated herein by reference.

The *Christensen Capacity Report* was prepared in response to the Board's August 2008 request to provide an "analysis of long-term forecasts of freight rail demand, particularly the U.S. Department of Transportation's Freight Analysis Framework...." (Notice at p. 1). These Freight Analysis Framework ("FAF") forecasts of freight rail demand are the basis of railroad investment projections found in "*National Rail Freight Infrastructure Capacity and Investment Study*," a September 2007 report prepared by Cambridge Systematics ("*Cambridge Study*" or "*Study*"). As the *Christensen Capacity Report* notes (*Report* at pp. 3-1, 3-2), the *Cambridge Study* was commissioned by the AAR at the request of the National Surface Transportation Policy and Revenue Study Commission.²

The AAR believes that the *Christensen Capacity Report* provides insight regarding potential future infrastructure needs of the U.S. freight rail industry. That said, nothing in it negates the critical point that the AAR originally made in its April 4, 2007 comments to the Board in Ex Parte No. 671, Rail Capacity and Infrastructure Requirements, that: (1) the United States cannot prosper in an increasingly—competitive global marketplace if its freight railroads are unable to meet the nation's growing transportation needs; and (2) having adequate railroad capacity is critical to meeting those needs. Railroads must be able to both maintain their extensive existing infrastructure and equipment and build the substantial new capacity that will be required (the current economic slowdown notwithstanding) to transport the additional traffic the nation's economy will generate.

² The Commission was authorized by Section 1909 of The Safe, Accountable, Flexible, Efficient Transportation Equity Act—A Legacy for Users (SAFETEA-LU) (Pub. L. 109-59, 109th Congress, 1st Session.) It was charged with completing a comprehensive study of the U.S. surface transportation system and the Highway Trust Fund, then developing a conceptual plan, with alternative approaches, to ensure that this system continues to serve the needs of the United States.

At its most basic level, the *Christensen Capacity Report* reflects the undeniable fact that all long-term economic projections, by definition, rely on a set of assumptions regarding economic conditions, legislative and regulatory issues, and other factors that may or may not be realized. As the *Report* notes, “one must recognize that there is considerable uncertainty surrounding all forecasts that extend thirty years into the future” (*Report* at p. 4-14).

Accordingly, a key question that results from the *Report* is whether policymakers should gamble by making policy decisions based on the lowest possible growth forecast for rail transportation demand and risk being wrong.

Clearly, conditions have changed markedly since the *Cambridge Study* was released. Most obvious, of course, has been the onset of the most severe global economic downturn since the 1930s. The current economic conditions, which have negatively affected every major U.S. industry that utilizes rail transportation, have led to an 18 percent reduction in U.S. rail carload traffic and a 16 percent reduction in U.S. rail intermodal traffic.³ However, the *Report* does not dispute the fact that freight transportation needs will grow — which is a point that has been reinforced by numerous studies in addition to the *Report*, including the *Freight Rail Bottom Line Report* of the American Association of State Highway and Transportation Officials in January 2003.

Even if the economic downturn delays previously projected growth by a few years, there can be no doubt that if the nation is to have the rail capacity it needs in the years ahead, the issue needs to be addressed at this time. The *Report* does not dispute the need for capital investment to sustain the current rail infrastructure or to grow it (*Report* at p. 3-24). The

³ U.S. rail traffic in the first 17 weeks of 2009 compared with the first 17 weeks of 2008, based on *AAR Weekly Railroad Traffic* data.

nation needs public policies that will encourage investment in the capacity that will be needed.

In that regard, the role of public policy in considering future railroad infrastructure needs should not — and cannot because it is unrealistic — strive for certainty as to future scenarios. Instead, the role should be to evaluate network capacity constraints in the context of a range of traffic growth scenarios, and to use conservative approaches to minimize any risks to the transportation network in case the projections are substantially lower than the actual outcomes.

Specific Findings of the *Christensen Capacity Report*

While the AAR does not take issue in general with the findings of the *Christensen Capacity Report*, several aspects of it warrant comment.

First, the *Report* takes issue with some of the assumptions and methodologies of the *Cambridge Study*. It's important to note, though, that the *Cambridge Study* was prepared under strict guidelines from the U.S. Department of Transportation ("DOT") as to forecasts, market share, and timing. For example, the *Study* had to take as given the DOT's earlier forecast, in the FAF, of an 88 percent increase in freight rail demand (measured in tons) in 2035 from 2002 levels, and the *Study* had to be developed so it could be easily compared to an analysis of highway capacity that was already well underway. Moreover, only two months were available to complete the work, making interim estimates impossible to produce. Thus, Cambridge Systematics had only limited discretion regarding the assumptions inherent in its *Study*.

Indeed, the AAR has long recognized that there were limitations on what could be done in the time allowed and with the external constraints placed on the work. For this

reason, in October 2008 the AAR commissioned Cambridge Systematics to undertake a follow-up study that is more comprehensive than the original effort and, in fact, addresses many of the issues raised by the *Christensen Capacity Report*. This follow-up study will be completed later this year.

Second, the *Christensen Capacity Report* notes (*Report* at p. 3-7) that much of the detailed information behind the *Study* is proprietary and cannot be directly analyzed. This is true, but the information is of a competitive nature and therefore confidentiality is necessary. The AAR and Cambridge Systematics collected and analyzed data submitted by individual railroads. Much of this railroad specific data — including detailed line characteristics and traffic routing decisions — is highly sensitive commercial information and thus was not shared with or among the other railroads or specifically revealed in the *Cambridge Study* itself.

Third, the *Christensen Capacity Report* notes (*Report* at p. 6-10) that “given the positive externalities or reductions in negative externalities associated with rail transportation (both freight and passenger), public commitments to railroad infrastructure investment can prove to be socially beneficial.” In cases where public funding is to be involved, the *Christensen Capacity Report* also urges a transparent cost-benefit assessment. The AAR agrees that public funds should be spent wisely, and cost-benefit analyses are extremely helpful in facilitating this outcome.

However, it should be noted that the *Cambridge Study* was only designed to estimate the total requirements for funding given the DOT economic assumptions. The *Study* was not designed to specify a plan, or alternative plans, for rail infrastructure development.

The rail infrastructure development process is an individual railroad activity based upon the specific markets the railroad serves and the business within those markets that would dictate the need for new or expanded capacity. It is a case-by-case effort in which public funding may, or may not, be involved; and the railroads themselves should determine the scope, timing, and location of their investments in infrastructure and equipment. In cases where the potential for public funding is involved, the individual railroad would have to assess in each circumstance whether the level or conditions of such public funding warrants the release of railroad internal information.

Fourth, the *Christensen Capacity Report* notes that railroad investment in infrastructure capacity usually comes only after there is a clear need for the capacity, not in anticipation of new business. As the *Report* notes, “Lumpy and irreversible investments in markets with uncertain demand will mean that those investments will have significant option values. Thus, one would expect to see that such investments would be undertaken only if they are clearly expected to be profitable.” (*Report* at p. ES-3) This parallels what the AAR noted in its Comments in Ex Parte No. 671: “[B]efore investments in...capacity enhancements are made, railroads must be confident that traffic and revenue levels will remain sufficiently high to justify the enhancements for the long term. In this regard, railroads are no different than the vast majority of their customers.”⁴

Railroads work diligently to have the appropriate assets in place to handle the traffic they are called upon to haul. From time to time, though, demand for rail service exceeds expectations and, in these circumstances, the rail infrastructure cannot always support the transport of all the business offered to the railroads. In this regard, the *Christensen Capacity*

⁴ See AAR Comments of April 4, 2007 in Ex Parte No. 671, Rail Capacity and Infrastructure Requirements at p. 5.

Report makes the important point that “Observed short-run capacity shortages (which need to be handled through capacity rationing) may be the economically rational response in the short-run to demand fluctuations.” (*Report* at p. 2-19) Thus, the *Report* directly rebuts shipper groups that have wrongly alleged that railroads should always have on hand whatever assets might possibly be needed at any time by rail customers, even if those assets would sit idle most of the time.

Moreover, even if railroads were required to have such excess assets, the STB’s rate regulation involving the stand alone cost (“SAC”) methodology (as well as the simplified stand alone cost methodology) would not permit railroads to earn a return on such assets. SAC permits recovery on only the smallest amount of assets needed to move only a subset of the railroad’s actual traffic.

Fifth, the *Christensen Capacity Report* notes (*Report* at p. 2-9) that “[o]ther factors affecting the capacity of a rail network are the traffic mix on the network and the prioritization of certain types of traffic over other types of traffic (e.g., passenger/commuter vs. freight)...” The *Report* found that the “prioritization of trains is likely an important factor when a mix of train types share services on a corridor or network.” (*Report* at p. 2-9) The *Report* further noted that such shared usage has an inordinate effect on capacity, *i.e.*, where passenger/commuter trains are given preferential treatment over freight trains, the result is increased delays and reduced capacity on the corridor or network. (*Report* at p. 2-9)

The AAR concurs in this finding and emphasizes its significance given the simultaneous efforts to dramatically expand rail passenger service and place service requirements on host railroads. There is no doubt that where the traffic mix on a corridor or network is comprised of both freight and passenger/commuter trains, the prioritization of

passenger/commuter trains over freight trains will adversely affect the fluidity of the traffic flow and will result in an inordinate lessening of network capacity unless public bodies compensate for this loss by investing adequately in additional rail capacity. And as passenger/commuter trains form a larger part of the traffic mix, the larger will be the adverse capacity effects because priority “fast” trains consume more capacity than slower trains, especially in a mixed use environment. The AAR’s freight railroad members strongly support the growth of passenger rail in the United States, but that growth should complement, not conflict with, freight rail growth.

Finally, the *Christensen Capacity Report* notes that “A feature common to most network industries is that congestion at nodes and other specific network locations can often become a binding constraint on the utilization of network route capacity (*Report* at pp. 2-9 to 2-10). Railroads recognize the deleterious role individual chokepoints can have on overall network performance. However, the focus of the *Cambridge Study* was, by design the performance of the network as whole, not specific individual locations.

Conclusion

The current economic downturn means that future rail traffic levels, at least in the near term, will be lower than the projections of even six months ago. No one can know for sure what traffic levels will be next year, much less 30 years from now. Still, it is clear that rail capacity will have to increase as the economy expands — a point that holds true whether traffic increases 40 percent, 55 percent, or any other number by some specific date. The railroads are committed to meeting these increased capacity needs primarily through private capital.

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Policymakers at the Board, in Congress, and elsewhere have critical roles to play in helping to ensure that rail capacity is adequate for whatever the level of demand actually occurs. Indeed, the AAR would urge that policy decisions should support an environment that allows for and supports the investment in infrastructure needed to provide the current and future freight transportation capacity the nation requires. In that regard, policy decisions should be based upon realistic — and not the lowest possible — growth forecasts in order to minimize the risk of severe adverse consequences on the national rail network.

Respectfully submitted,



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