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BEFORE THE

SURFACE TRANSPORTATION BOARD

STB EX PARTE NO. 677

COMMON CARRIER OBLIGATION OF RAILROADS

COMMENTS OF THE

U.S. DEPARTMENT OF AGRICULTURE

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AUTHORITY AND INTEREST

The Secretary of Agriculture is charged with the responsibility under the Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 to represent the interests of agricultural producers and shippers in improving transportation services and facilities by, among other things, initiating and participating in Surface Transportation Board (Board) proceedings involving rates, charges, tariffs, practices, and services.

INTRODUCTION

The Department of Agriculture (USDA) commends the Board for holding this hearing to allow interested parties to present their views concerning the Common Carrier Obligation (CCO). USDA appreciates the willingness of the Board to take into consideration the views of interested parties in its efforts to better understand, monitor and enforce the CCO.

Since 1980, economic deregulation of the railroad industry has resulted in extensive benefits to both shippers and railroads. Inflation adjusted rail rates per ton-mile have decreased while the financial health of the rail industry has become much stronger. Shippers, however, have expressed concerns that the increased market power of major railroads—because of rail consolidation since 1980—may be a contributing factor in major railroads giving shippers less effective rail service and being less receptive to shipper needs.[1]

[1] See USDA and various shipper comments, Surface Transportation Board Ex Parte No 658, The 25th Anniversary of the Staggers Rail Act of 1980, October 19, 2005, for a fuller discussion.

Although deregulation has given railroads more freedom to make management decisions, it has challenged the ability of regulators to enforce the CCO. For instance, deregulation allows railroads to enter into contracts for rail service and fulfill its reasonable commitments under contracts before responding to reasonable requests for common carrier service.[2] In addition the *Interstate Commerce Commission Termination* Act (ICCTA) permits the Board to exempt commodities when there is sufficient transportation competition to protect shippers from the abuse of market power and when the exemption would not inhibit the Board from carrying out the transportation policy of §10101.[3] Another factor contributing to the challenge of enforcing the CCO is the introduction of car allocation programs, such as auctions for the guaranteed delivery of railcars. Finally, the unforeseen extent of major U.S. railroad consolidation may have also increased the ability of railroads to de-market rail service to some shippers or commodities because of the loss of rail-to-rail and geographic competition.

Frustrated with what they see as inadequate and discriminatory rail service, many agricultural shippers have voiced concerns to the Board and USDA regarding enforcement of the CCO and the lack of effective rail-to-rail competition. The Board acknowledges that it has seen an increasing number of questions arising in recent years regarding the extent of a railroad's CCO, resulting in this proceeding.[4]

One of the main problems with the CCO, due in part to its history and statutory construct, is that it is not straightforward and clear to all concerned. While easier said than done, a desirable policy objective would be for the Board to provide clearer rules,

[2] Commitments, which deprive a carrier of its ability to respond to reasonable requests for common carrier service, are not reasonable. See ICCTA §11101(a)
[3] See ICCTA §10502. The Board has no authority to require any specific level of rates or services for exempt commodities See ICCTA §10502 (e).
[4] Surface Transportation Board Notice of Public Hearing, STB Ex Parte No 677, February 22, 2008

definitions, and/or guidelines on when and how CCO applies. USDA believes that in calling this hearing, the Board should be commended in attempting to seriously address CCO concerns. USDA believes this is important work to undertake, but recognizes it will not be easy. USDA recognizes that in developing clearer CCO rules, definitions, and/or guidelines, the Board will be required to strike a delicate balance between the competing requirements of the concepts of:

1. Public convenience and necessity;
2. Needs of agricultural and other shippers;
3. Interests of rail firms; and
4. Goals of rail deregulation, including preserving the benefits of deregulation.

THE COMMON CARRIER OBLIGATION

Even after economic deregulation, under current law railroads are expected to fulfill their CCO obligation as public for-hire transportation providers, but that obligation has become less clear. In addition, even though railroads are privately owned and operated, many shippers believe that railroads have a responsibility to the public due to the initial governmental investment in the rail network.

In recent years, some agricultural shippers that were dependent upon rail or intermodal transportation have lost reliable access to those services. It is critically important for all agricultural producers—small as well as large—to be able to move their crops to market. Access to rail and intermodal transportation is important to agricultural shippers because:

- Rail and intermodal transportation connect agricultural shippers to distant international and domestic markets.

- For those agricultural shippers who are distant from barge transportation, railroads provide the only cost-effective transportation choice and the only efficient means of transporting bulk grain and other agricultural products to distant markets.

- Rail access may affect the ability of rural businesses to remain in business or new businesses to locate in rural regions, affecting rural employment, wage levels, and economic vitality.

- A shift from rail to truck transportation significantly increases road maintenance costs for local and state governments due to increased road damage from large trucks transporting agricultural and manufactured products as well as natural resources.

- Railroad transportation, which is 3 times as fuel efficient as truck transportation, becomes increasingly important during periods of high fuel costs, which reduce the cost-effectiveness of truck competition.

Agricultural producers commit significant resources, which cannot be shifted to another crop, once that crop is planted. The harvest of these crops usually occurs several months after planting for grains, oilseeds, and vegetables, but the harvest of fruits, nuts, lumber, and horticultural crops may occur years after planting. At the time of planting, agricultural producers are not assured of a price for the crop that will cover the costs of the inputs or even be assured of normal yields. When the crop is sold, producers usually receive a price net of transportation. Transportation costs, especially during times of historically typical grain prices and costs, may determine whether an agricultural producer receives enough from a crop to remain solvent or to access the markets in which they normally sell.

A clearer interpretation and enforcement of the CCO could help agricultural producers and shippers obtain or improve their access to cost-effective and efficient rail transportation in the movement of agricultural products. In today's highly competitive world markets, access to cost-effective and efficient transportation is needed to preserve the competitiveness of the Nation's agricultural producers. Improved access to rail transportation could also help agricultural producers preserve the benefits of economies of scale—which can only be obtained through large scale production and specialization—through the preservation of efficient, effective, and cost-effective transportation options.

COMMENTS

In these comments USDA will highlight shipper concerns when the concerns expressed: (1) appear to indicate a clear violation of the CCO, (2) are of major importance to agricultural shippers, and (3) the benefits of addressing the concerns are expected to exceed the negative effects upon railroad efficiency or operations. In highlighting shippers' concerns, USDA will also suggest relevant questions for the Board to consider. USDA asks that the Board carefully consider, study, evaluate, and address – where it can – the concerns expressed by agricultural shippers in relation to the competing requirements listed on page 4

Service Limitations Resulting From Capacity Constraints

Since late 2003, capacity constraints have developed as the number of railroad route miles operated has decreased substantially, even as the volume of railroad traffic has increased markedly As a result, on average, each railroad route mile today carries more than 2.6 times as much traffic volume as it did in 1980.

As capacity constraints began to reduce system operational fluidity, railroads rapidly increased rail tariff rates to regain operational fluidity and to ration traffic to those shippers willing to pay the most for rail service. To the extent that capacity constraints exist and appropriate investments in additional rail capacity are made, this may be a rational economic response on the part of the railroad industry.

USDA notes, however, that rail rates on agricultural traffic have risen much faster than the rates for all commodities (including grain); and that the carload rates are higher than those for other similar commodities. USDA recognizes that the Board has limited authority to set rail prices, and that authority is present only when a shipper has filed a rate appeal. The Board, however, has broad discretion regarding business practices

- USDA asks the Board to study the issue of whether railroads are meeting the intent of the CCO when agricultural shippers are assessed disproportionate price increases that eliminate reasonable access to rail transportation.
- USDA requests the Board consider whether the reliance upon rail transportation by agricultural shippers located in some geographic regions should merit special consideration and Board action.
- USDA also asks the Board why current capacity constraints should now exempt railroads from their CCO obligations.

USDA also notes that agricultural shippers bear a disproportionate decrease in rail service relative to shippers of other commodities during periods when railroads are experiencing operational fluidity difficulties, changing to new operating systems, lacking sufficient equipment or locomotive supply, implementing mergers, or adjusting to new retirement rules for train crew members.

- USDA asks the Board to clarify the CCO requirements to assure that agricultural shippers receive a fair proportion of available rail service.
- In addition, USDA asks the Board to define railroad obligations to distribute railcars and service among shippers of different commodities when rail capacity is constrained.

Economically Motivated Service Reductions and Metering of Demand

USDA is concerned that many of the major railroads appear to have de-marketed rail service to many agricultural shippers for at least 15 years—long before the current capacity constraints—through reductions in car allocation, poor service, and excessive tariff rate increases. Even during the early-1990s, smaller agricultural shippers located on a major railroad complained that railroad car allocations were limited to no more cars than the shipper used the prior year, even though a drought, late frost, or disease had reduced demand the prior year.

- USDA asks the Board whether railcar allocation systems that reduce the allocation of railcars to a shipper over time should be considered a violation of the CCO and an unfair business practice.

Another USDA concern is the possibility that Class I railroads may have limited the interchange of traffic with connecting carriers, in an effort to force traffic from markets located on the connecting carrier to longer hauls on their own lines. To our knowledge, the annual Waybill Samples have not been analyzed to determine whether the proportion of traffic interchanged with connecting railroads (adjusting for mergers since 1985) has decreased. If this proportion has decreased measurably, it could indicate devolution into a rail network contrary to the public interest rather than a freely interchanging national rail network. USDA supports the ability of agricultural shippers to sell in the market of their choice rather than those chosen by the railroads.

- USDA requests that the Board analyze the annual proportion of traffic the 7 major U.S. railroads have interchanged to connecting railroads (using the current rail firm configuration) since 1985.

- For those railroads in which the proportion has decreased, USDA requests that the Board determine whether it was due to physical closure of the interchange locations, disproportionate increases in rates to offline markets, decreased rates to online markets, or some other reason.

- USDA asks the Board to determine whether the CCO requirements allow railroads to eliminate shipper access to markets located on connecting carriers.

USDA is also concerned that railroads may be refusing to quote tariff rates to some off-line locations in an effort to force traffic to destinations located on their own lines. For instance, shippers located in southern Texas report that a railroad refused to provide service or quote a price on grain destined for Mexico because the railroad's portion of the haul is less than 500 miles. USDA interprets the CCO as giving a shipper the right to a rate even when the railroad currently has no rate for that particular movement.[5] In addition, when fuel prices are at or near record highs, rail becomes competitive with truck transportation on shorter hauls than would normally be the case.

- USDA requests that the Board clarify the CCO requirements as they apply in cases of this type.

Cost and Safety Issues in the Transportation of Hazardous Materials

The major U.S. railroads have expressed concerns regarding their liability exposure in the event of an accident while hauling hazardous materials, particularly products classified as toxic inhalation hazards (TIH). The railroad industry is actively discouraging the movement of hazardous materials and encouraging shippers to use safer substitutes. However, USDA believes the CCO and concept of public convenience and necessity must be fully considered in addressing cost and safety issues in the transportation of hazardous materials by rail.

The railroad industry's effort to encourage shippers to use safer alternative materials is certainly an option that should be explored. However, it may not be a suitable solution for all hazardous materials and it is not the only option that should be under consideration. Shifting the transport of hazardous materials away from rail to trucks should be considered only after careful study of all options, including careful

[5] Interstate Commerce Commission Termination Act, §11101(b).

consideration of whether the current non-rail infrastructure would support such a change, the anticipated costs of building infrastructure that could accommodate such a change, and the speed at which the needed infrastructure could be built.

USDA contends that one of the key issues to consider regarding the proposed shift of hazardous materials from rail to truck transportation is the relative safety of the modes. Rail unquestionably provides the safest movement of these materials as the Association of American Railroads has stated for many years. Shifting hazardous materials from rail to trucks will require 4 trucks for every railcar, which may compromise public safety. In addition, rather than solving the problem of transporting these materials, it shifts the liability burden to the trucking industry, which also would be devastated by a catastrophic accident. Thus, with the lack of safer alternative materials, public convenience and necessity could require railroads to continue to move these hazardous materials for basic public safety.

Anhydrous ammonia is a good example of a necessary hazardous material that should be hauled by rail for public convenience and necessity. Anhydrous ammonia, a product often used for agricultural purposes, is the second largest user of railroad transportation for TIH products. However, anhydrous ammonia is a product where, in most cases, there is no suitable substitute. Anhydrous ammonia is the base material for all other nitrogen fertilizers and some phosphate fertilizers. Anhydrous ammonia fertilizer is essential to the growing of food for millions of Americans and in helping meet the nation's energy needs.

- USDA recommends that the Board, in determining the CCO requirements for hazardous materials such as anhydrous ammonia, consider: (1) the lack of substitutability, (2) the relative safety of rail movement compared to truck movement, and (3) the concept of public convenience and necessity.

A possible market-based solution to the railroad liability issue could be the use of different liability insurance pricing mechanisms in combination with a Board requirement that railroads not profit from liability insurance costs. Under this scenario, liability insurance companies would need to price liability for railroads and other transportation modes either by the ton or by carload for hazardous materials. The price of the liability insurance should be set based upon the type of hazardous material hauled and the relative safety of the railcar used in the haul. Liability for non-hazardous materials could continue to be priced as a lump sum if desired. Under this scenario, the liability insurance rates for hazardous materials should be: (1) filed with the Board, (2) made available to shippers and the public, and (3) railroads should be limited to passing through to the shipper only an amount equal to the cost of the liability insurance. This could have enough transparency to satisfy shippers that railroads are not making liability insurance costs a profit center.

- USDA recommends that the Board, as it did in its fuel surcharge ruling, rule it an unreasonable business practice for railroads to profit from liability insurance costs incurred in the movement of hazardous materials.

<u>Carrier Imposed Requirements for Infrastructure Investments by Shippers</u>

Agricultural shippers have raised concerns that railroads may be using siding upgrades as a means to push freight off the rail line. Agricultural shippers report that railroads are mandating extensive upgrades of rail sidings that often are not economically justifiable to the shipper. These upgrades often mandate power switches that can be controlled by the engineer in the cab, heated switches, and heavier rail. In some cases, the siding, after these upgrades, would be in better condition than the rail lines serving the siding. Typically the shipper has no access to rail service until these siding upgrades are completed and approved by the railroad. The new service contract often transfers all liability risks to the shipper regardless of railroad activity or involvement.

In addition, these shippers report that it may take as long as 18 months for railroads to approve siding specifications for new service. After these delays and the siding is in place, the shipper is often given a take-it-or-leave-it service contract that shifts all liability to the shipper regardless of railroad activity or involvement.

- USDA requests that the Board investigate railroad requirements for siding upgrades in relation to the CCO requirement and reasonable business practices.
- USDA requests that the Board monitor railroad service agreements in regards to possible unreasonable shifting of liability in relation to the CCO requirement and reasonable business practices.

Impact of Volume Requirements or Incentives

Exports of U.S. agricultural products are projected to reduce the U.S. balance of trade deficit by $24.5 billion during 2008. The ability to obtain cost-effective transportation for agricultural products is important for rural economies and supports domestic prices for agricultural products.

For several years, USDA has become increasingly concerned regarding the closure of rural intermodal facilities in favor of larger facilities located in urban areas. Although the location of intermodal yards in urban areas supports the import of goods into the United States, urban locations usually increase the difficulty of exporting agricultural products, which are produced in more remote rural locations.

Agricultural producers often incur substantial additional costs because of hauling their produce longer distances in order to obtain intermodal service. Because agricultural markets typically have small margins, the increased costs of accessing intermodal service often results in the loss of domestic and international markets.

For example, when the intermodal yard in Lubbock, TX, was closed, cotton shippers had to pick up empty containers from Dallas, haul them by truck to Lubbock and load them, and then haul the loaded containers by truck back to Dallas. This added more than $1,000 in transport costs.

Another example is the loss of intermodal facilities in Wisconsin Since rail no longer loads in Wausau and Eau Claire, WI, dairies must now truck to either Milwaukee or Chicago at a cost of approximately $600 per truckload. In 2006, rail transportation to the West Coast ports cost $760 compared to only $300 only 3 years earlier. Since dairies on the West Coast can truck their product to the ports for only $200, Wisconsin dairy exporters faced a $1,160 cost disadvantage—rather than a $100 disadvantage—versus West Coast dairies. Service has also been suspended to other rural loading points serving producers of other agricultural commodities in Washington State, Idaho, North Dakota, and Minnesota.[6]

In some instances, local investors would like to invest in an intermodal facility but have been unable to obtain adequate assurance from the railroad that it would be able to supply sufficient empty containers in a timely manner and provide adequate service hauling filled containers. The location of empty containers in urban population centers and the fact that shipping companies owning the containers control their availability for reloading are factors contributing to the inability of railroads to guarantee a timely supply

[6] Testimony of Peter Friedmann, Executive Director of the Agriculture Transportation Coalition before the Wisconsin Department of Agriculture, Trade, and Consumer Protection, Public Service Commission at the Rail Service hearings in Milwaukee, WI, September 26, 2006.

of empty intermodal containers. Shippers contend, however, that major railroads are not interested in serving smaller intermodal facilities.

- USDA requests that the Board study this situation and clarify the CCO requirements of railroads to serve smaller intermodal facilities.
- USDA also inquires whether the Board has the authority to direct another railroad to serve a smaller intermodal facility and under what conditions such a directive would be issued. To what degree would the willingness of shippers to invest in a smaller intermodal facility affect the Board's decision?

Captive and smaller agricultural shippers have also expressed concern regarding railcar allocation rules that could unreasonably limit the amount and timing of rail service available to them. Smaller shippers have expressed concern regarding the fair allocation of rail cars between small and unit-train shippers. Captive agricultural shippers have expressed concern that railroads may serve non-captive shippers before captive shippers during periods of increased demand for rail service because non-captive shippers have other shipping options. Finally, shippers of minor agricultural crops have expressed concern regarding their timely access to railcars.

- USDA requests that the Board clarify the CCO requirements of railroads to distribute railcars among similar shippers in regards to captivity and size of the shipper.
- USDA also requests that the Board determine whether the car supply programs used by the major U.S. railroads allow adequate participation of smaller shippers and an appropriate allocation of railcars.
- USDA further requests that the Board clarify the CCO requirements of railroads serving shippers of sugar beets, dry beans, and other agricultural products having smaller volume requirements.

Proper Use of Rail Embargoes

Agricultural shippers have raised concerns about some railroads using embargoes as a way to stop serving a line that is not as economically viable as other lines. The embargo tends to be long term and will likely remain until abandonment proceedings are started. USDA notes that in the case of branch lines, railroads may have an incentive to abandon the distal portions of the line in the absence of nearby competition from another railroad.

- USDA requests that the Board investigate and clarify the CCO requirements as they apply to these situations.

CONCLUSION

The CCO is important to agricultural shippers, but is not straightforward and clear to all concerned. In these comments USDA has presented shippers concerns with regard to CCO and raised relevant concerns for the Board's consideration. USDA asks that the Board carefully consider, study, evaluate, and address – where it can – the concerns expressed by agricultural shippers.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Bruce Blanton, certify that on this 17th day of April, 2008, I caused a copy of the foregoing document to be served by first-class mail, postage prepaid, on all parties of record in STB Ex Parte No. 677.

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