

Now, TAX, do you all have some rebuttal that you want to offer?

MR. MEYER: We do.

CHAIRMAN NOBER: Okay. Please come on up.

How much time do they have left? Twenty minutes, okay.

(Pause.)

MR. REARDON: Mr. Chairman, Vice Chairman Mulvey, and Commissioner Buttrey, we will make efficient use of our rebuttal time.

There are a couple of things that I think absolutely must be corrected that were said by our opponents. In particular, Commissioner Buttrey, in response to the question which you asked Mr. Mayo saying, "What about rail labor, rail locomotives," and Mr. Mayo responded that TAX does not have that either. That is not the case.

We are members of the Brotherhood of Railway Carmen at all of our 37 field maintenance operations throughout the United States. That contract covers approximately 500 employees. All of our employees, starting with myself down through the entire organization are subject to the railway tax -- railway retirement taxes, which are substantially higher than Social Security. I think as several of you perhaps have had some experience with them, they are dramatically higher.

We do not have locomotives. However, our cost structure far more resembles and is higher on an employee individual basis -- far more resembles the railroads.

I might also comment with respect to the maintenance. The statement was made that, well, everybody has the same maintenance facilities. That is simply not accurate. First of all, we have 1,500 -- almost 1,600 employees throughout the United States. With the exception of our clerical staff in Chicago, almost 100 percent of those employees are devoted to TAX maintenance.

At our three division shops which are on both coasts -- the west coast as well as the east coast -- and our 37 field maintenance operations which are spread about -- around the United States, and those spaces are leased or purchased as the case may be, immediately adjacent to or part of the property of the railroads, but they are leased on an arm's-length basis.

That maintenance network is highly unique to this industry, and it in fact dramatically contributes to what we constantly refer to as the efficiency of the TAX equipment because that means we do not have to take that equipment out of service for any appreciable length of time to repair or modify it, which in turn would run up the cost. That is one of the very unique features of TAX and a unique feature of pooling.

With respect to car supply, Mr. Mayo indicated that in response to a question I believe by Vice Chairman Mulvey that because TAX is such a large player in that market, in the intermodal market, then they have the ability to raise rates and, in effect, to the detriment of the shipper. That could not happen for this reason: a) we are owned by the railroads, we are owned by that customer to whom we charge that rate.

If in fact we were to take some albeit artificial advantage in that type of market and raise our rates, the railroads wouldn't hear of it. That is in fact one of the beauties of the cooperative system, the beauty of the pool, is we keep those rates down.

Another statement was made with respect to R&D. TAX has tremendous effort and money poured into R&D. You heard about the TTUX car earlier, and, in fact, Mr. Goode was commenting on it. That is only the tip of the iceberg. That is, in fact, one car we're working on now, yes, and that will soon go into production. It's included in our capital spending plans, and that is to carry Class 8 highway rigs to their first point of sale. It's done in a more

expensive fashion at the present time.

Over the past 12 years, we have invested \$425 million in research, development, and ride control equipment for auto rack cars. We did so at the behest of the automobile industry that at that time was complaining about rough rides.

We, in fact, did research ourselves at the test track in Pueblo, invested that money, and we have really only recouped about \$40 million of that through anti-rate adjustments. The balance of that we have swallowed. That is a huge R&D commitment to this industry, and it has continued over time.

Mr. Thomas made the statement that TAX has guaranteed income. If cars go into storage, the rates in the rest of the fleet increase. I can assure you that does not happen. We've had a lot of cars in storage, and we have not had a rate increase but for a minor increase on some change items here recently. Hasn't even gone into effect yet -- will July 1.

We have not had a rate increase, and so I can assure that when some part of our fleet goes into storage we do not recouple that on the rest of this fleet. Those cars are at risk. The leasing companies made the statement that, yes, they can lease as short as three months I believe the statement was made, and, in fact, I'm sure that's true.

Bear in mind, however, that we in fact lease it for five days, because these cars are turned back cars, both intermodal and non-intermodal. Consequently, our risk is inordinantly higher. The utilization occurs only because the equipment is reliable and the rate is low.

If we were to raise rates, which occasionally in the future we're going to have to do, if we were to raise rates in order to recoup more income for its own sake, then the railroads with increasing frequency I'm sure would turn to some of our competitors, as they do today.

I also hasten to add that our risk over the long term is virtually identical -- or excuse me, our costs over the long term per unit of equipment is virtually identical to the leasing company's, but our risk is substantially higher because of the very short nature, i.e. five days, that the railroads actually commit to take these cars when they do take them.

And, in fact, at other times they do go into storage. Last year alone our monthly storage costs were at about \$300,000 a month. That was in a light year, a very light level of storage for that year.

With that, I'll turn to my colleague, David Meyer.

MR. MEYER: Just a few. I think the papers pretty well deal with the issues in this case. A few responses to some of the specific points that Mr. Mayo and others made in support of the leasing opponents positions here.

First, they were asked a question that for them I think it really is -- it goes to the crux of the issue, and that is, what is their theory by which anyone is harmed by their alleged anti-competitive attributes of the pool? And what Mr. Mayo said, if I was hearing him correctly, is essentially there is a conspiracy theory here that in the short run TAX is offering wonderful benefits in terms of efficiencies and low cost equipment supply, is allowing the railroads a mechanism for supplying their equipment, you know, at the lowest cost and most efficient way.

But over the long run, these leasing companies are going to be forced out of the market, forced out of business, so that when the time comes for some shipper down the line who wants -- who needs a car that the railroads choose not to supply, he'll have no alternative and the car supply costs will be higher.

That's a classic predatory pricing theory. Price low today, drive someone out of

business so that later on there can be some anti-competitive harm because prices come up and there is no recourse to alternatives.

Well, such a theory hasn't really even been asserted -- well, they really haven't asserted such a theory, and one would be impossible to assert on the facts of this case. First of all, leasing companies aren't being driven out of any marketplaces. But I think the evidence really is quite clear that they have been growing their investment, growing their presence in flatcar types, and in every car type. They're not going anywhere.

Second, TAX hasn't been pricing in a predatory fashion below its cost. To the contrary, it has been pricing at a level that reflects its efficiencies as any good supplier of cars should be allowed to do, and to support reinvestment, billions of dollars of reinvestment, which wouldn't come if there were predatory pricing at issue here.

And then, finally, even if you were to weave the theory through to its end-game consequences, that somehow the leasing companies are no longer leasing a particular type of flatcars because they have chosen -- they have concluded it is not in their financial interest to do so today, if the railroads or if TAX sought to extract a premium from -- if TAX sought to extract a premium from the railroads, first of all, as Mr. Goode told you earlier today, it wouldn't have it.

The leasing companies would still be there. They'd be out there as an available alternative for anyone who wanted, including a shipper or a railroad, to go acquire some cars on a short-term or a long-term basis. Again, there is just absolutely nothing to the anti-competitive theory presented in this case.

The second conundrum that the leasing companies have -- reflected in their comments is they acknowledge wholeheartedly the wonderful benefit that the TAX pool has achieved in the intermodal arena.

Well, you know, that -- we certainly accept that support. We think that there are tremendous benefits in the intermodal arena. But then they turn around and argue that there is no appropriate need for TAX to be able to price its cars, that TAX shouldn't be able to set the price of its cars, and they point to really nothing in the record establishing any basis for that assertion.

They ignore completely the points we have made about the essence of what the pool is all about as a jointly shared investment in capacity on the part of the railroads, and they point to examples that really are contrary examples to their own case.

The multilevel reload pool, for example, the racks that go on the multilevel cars are set in accord -- are priced pursuant to a pricing schedule that has antitrust immunity. That kind of pricing schedule is essential if there's going to be a free-running and highly efficient pool of the sort they acknowledge that the multilevel pool is.

The record is quite filled with examples of other pools that have not been able to achieve the tremendous benefits of, at least as leasing companies acknowledge, the intermodal pool that TAX has. None of them had the attributes that the TAX pool has in their full measure.

So by supporting the fact that the intermodal pool generates tremendous efficiencies, I think the leasing companies have demonstrated that there is no case whatsoever for imposing any restrictions or any alterations in the way that pool operates. To do so would, we think, cripple and/or destroy the pool and its benefits.

But at the same time, the non-intermodal flatcars benefit in all the same ways that the intermodal cars do from pooling, from the sharing of risk, from the joint investment, from the network-wide approach to maintenance. And it's -- you know, the evidence is I think fairly clear on that subject.

Now, it's true that those cars don't -- unlike intermodal cars, are unable to go literally anywhere for the next load. But there are efficiencies TAX is able to achieve. The thousands of swaps that occur occur because of TTX's presence. They don't occur with respect to non-TAX cars, and we submit as a practical matter they couldn't because of the transactional costs, because of the frictions, because of the need for some negotiation, the appointment of some trustee or, you know, some mechanism that no one has yet invented.

As Mr. Goode pointed out, you know, if TAX didn't exist, the railroads would yearn to invent something that came close to approaching TTX's level of efficiency and benefit. What they might invent that wasn't pooling I can't even imagine. Leasing companies certainly haven't pointed to it, and we submit in this case that, really, the only sensible outcome here is an authorization -- a reauthorization of TAX to the full extent of its current authority.

Now, Mr. Mayo tried to paint a picture, which the supporters for that outcome really are a narrower group, and that the opponents are a broad group of -- a broad constituency. In fact, I invite the Board -- I don't want to do that here, but I invite the Board to look one by one at the comments in this case.

The only parties that in any respect want TTX's authority to be restricted relative to the full measure of what it does today are the leasing opponents.

Now, it is true that some other parties -- for example Greenbrier, for example Pacer, have suggested some desire for a shorter term of authorization than the 15 years. We think as a matter of good policy, really fundamentally good policy, there is no advantage to a shorter term, and all of the aims of a shorter term can be accomplished through the Board's ongoing oversight, and, if the Board desires it, an invitation for comments at some defined time in the future.

But having a drop-dead date after which TAX will cease to exist unless reauthorized inevitably creates a kind of uncertainty in the financial community that while not necessarily devastating to TTX's role and ability is just not advantageous to anyone. That is, to anyone except those who would want to impose extra costs on this option for railroads to supply their cars, so that they might earn greater profits on their own from car supply.

Finally, I just want to clarify the record on this issue of Rule 16 assignments. I think that our response to the leasing opponents motion to supplement spells it out quite clearly, but Mr. Mayo seems not to have read that. We don't assign cars anywhere. We make pool cars available to railroads. Railroads use those cars because it is in their interest to use them to meet shipper needs, and they use them in ways that are the most effective for the type of car, the type of commodity, etcetera.

In some cases, that means the railroads will choose not to turn those cars back every five days. That's absolutely their right. The 1994 decision addressed this point specifically. And to imagine that the only way in which a pool can operate efficiently is if there is turn back every five days, rather than the placement by a railroad, its option of a car in a particular corridor, service, or with a particular shipper, is to imagine a pool that is less efficient than it could be.

At the same time, as the record shows, TAX is able to work -- because it can manage its fungible fleet of cars, it can work to maximize the way those railroads' use of cars is optimized within the network, the entire nationwide network that is the rail industry, by engaging in swaps, engaging in redirected car moves, in order to, again, optimize. No bilateral contracting approach could ever reach the level of benefit that TAX is able to accomplish.

At this point, I think I'll stop. I think the other points the leasing companies have

made are all addressed in detail in our papers, and I'll respond -- or we'll respond to any questions you may have.

MR. REARDON: I'd like to make one additional comment if I might.

CHAIRMAN NOBER: Please.

MR. REARDON: And it does pertain to this matter of the antitrust immunity. You know, on the surface of it, antitrust immunity sounds almost like a dirty word, indicating some gambling away in some dark room. The truth in fact is that antitrust immunity is inextricably intertwined with pooling in the statute.

It was created in the Interstate Commerce Act of 1920. It was done so at the urging of William Gibbs McAdoo, who ran the nation's railroads in World War I and was shocked at the fact that they were unable, under the antitrust laws at the time, to get together and set joint rates and pool equipment instead of going out and duplicating each other's investment, much to the economic detriment of the industry. So that predated the existence of TAX by many decades.

There are also seven other instances of which I am personally aware in the transportation industries and communication industries, including the airline industries, motor carrier industries, where antitrust immunity is given in just such a case, and that's the sharing of commonly employed assets. This is not something unique to the railroad industry, nor is it unique to TAX. And I think that in this type of instance it's certainly a worthy attribute.

Our worthy opponents are well aware of the fact that if in fact we were to attempt to resort to bilateral arrangements and keep the fleet homogeneous, the minute we try to impose a universal circumstance condition, universal rate, the industry would be subjected to a lawsuit. And as a practical matter, that would make operation of the pool totally untenable, which, of course, then opens it up to our competitors. So I think that has to be borne in mind by this Board.

Last but not least is the matter of our opposition. Yes, there is some opposition there. The four car builders of the nation do support us. There are two leasing companies related to two of the car builders which express some degree of reservation. We have not attempted to hide that in any way.

I should also point out the matter of General Electric. General Electric is a multi-faceted company. General Electric Capital chose not to participate in this case. General Electric Power Systems chose to participate and strongly supports TAX because of its non-intermodal flatcar fleet, which it provides to that industry in providing very rare equipment, I might add, for the transportation of heavier componentry throughout our nation.

With that, I will close my comments, and, again, thank each of you for your time and consideration today of our application.

CHAIRMAN NOBER: Frank, do you have anything further?

VICE CHAIRMAN MULVEY: Two brief questions. One, the commenters said that in terms of setting pricing for the fleet that when times are slack you raise prices in order to maintain your return. And prices -- when demand is low, you lower the prices, which is sort of counterintuitive to what a market would do. Is that an accurate depiction?

MR. REARDON: No, Mr. Vice Chairman, it's not. We have not increased our rates, with one minor exception in the auto rack fleet a number of years ago to start to recoup some of that investment I told you about a moment ago. That was since repealed.

We recently had a small rate increase on some chain tie-downs to accommodate some capital improvements we made. We do not fluctuate our rates with the market at all, or

with utilization with respect to the flatcar fleet. If utilization of that flatcar fleet is high, which it is today, that rate is as it was in 2001 when we had tens of thousands of those cars in storage.

VICE CHAIRMAN MULVEY: The economist would say, well, if the demand is high, those rates probably should go up.

MR. REARDON: In an ordinary market, that's probably true, sir.

VICE CHAIRMAN MULVEY: Secondly, there --

MR. REARDON: And can I add one item? There is a discount program in the intermodal program, but it does not fluctuate with usage. It's simply to encourage high usage, but it is a fixed rate discount.

VICE CHAIRMAN MULVEY: There has been some suggestions about having an open pool, like a TAX pool be open to some of the lessors so they could also contribute to it and get some of the same benefits of the TAX pool. Do you want to comment on the problems or the benefits that might be associated with --

MR. REARDON: I'll defer to Mr. Meyer. But I'll tell you that under the current statute and physical operation I don't think it would work, but I'll defer to my legal counsel.

MR. MEYER: In some sense -- I mean, I think we mentioned earlier in some sense there is a degree of contribution by leasing companies. TAX does obtain some of the cars that it owns from the leasing companies. It leases them. Those are long-term financial leases rather than short-term operational leases.

I don't think anyone is really -- at least at this side of the table is really seriously requesting, you know, inclusion somehow in the TAX pool, because in order for the pool to continue to function what that would necessarily mean is that TAX -- that the pool would determine the price and it would determine the obligation to keep the cars in the pool and determine -- you know, kind of impose restrictions if you will on the leasing company's freedom to remove the cars when they saw fit or to establish whatever pricing they saw fit.

Now, one could imagine a situation I suppose in theory where if they ceded that control and those cars then got painted yellow so they were fungible and homogenous, you know, pool cars recognized by all the participants as the same in terms of all of the, you know, usage restrictions, usage terms, freedom to move wherever desired, etcetera, perhaps theoretically possible, I don't think at all workable in the real world, and there may be issues -- frankly, I haven't even begun to think about the statutory authority and whether that could be paired with the pool authority that is provided for in the statute. But that's probably the third or fourth issue down the string before -- you know, after which the idea is already foundered.

VICE CHAIRMAN MULVEY: Thank you very much.

CHAIRMAN NOBER: Okay. Well, I just have two very quick ones, and then we'll wrap up. The first is in your submittal, you have asked for the authority to clarify and make unilateral changes to your -- I guess to the terms and provisions of your contract. What do you have in mind with this? Why do you want this?

MR. MEYER: Let me just clarify our request clarification.

CHAIRMAN NOBER: Please.

MR. MEYER: And then I think I can point to a few --

MR. REARDON: I've never known a lawyer to be able to do that before.

(Laughter.)

MR. MEYER: I mean, this has sort of been presented as a Pandora's Box by our opponents. It's not at all. All we're asking for is there is a TAX pooling agreement. The

pooling agreement has some very detailed principles that TAX is to adhere to. Obviously, it limits the pool to flatcars. It adopts principles for establishment of the lowest cost of base prices to the members who have contributed their capital to the pool, and so forth.

But within that framework of the pooling agreement, which we know we cannot alter without coming back to the Board for approval in advance, what we're asking for is the clarification that we may do what the pooling agreement allows us to do.

And rather than facing the chilling effect of -- presented, really, by language in the 1974 decision, that a distribution change or a change in the way in which TAX is involved in the distribution of TAX cars, for example, might be regarded as a -- somehow a "substantive change" in our operations, or a substantive change in the underlying car contracts, and that in order to accomplish it we would have to file a -- you know, an application, have a proceeding, have some significant delay in order to make a change which would be motivated by desire for more efficient distribution.

Now, one example -- one concrete example --

MR. REARDON: Let me give you a 30-second example of that, if I could, because it's about to come up here in the fall. Let's say we're operating at very tight capacity, which we will in the fall, and that really occurs pre-Christmas rush.

And TAX wants to make some change to the distribution formula that will facilitate a transfer of equipment, let's say, in the west from Union Pacific to Burlington Northern, or vice versa. If we wanted to make a change in that agreement, we would actually have to come back to the Board, get prior approval, and then go make the change.

Well, by that time, peak is over and the problem is over. Those are the types of -- and the example of the exigencies. We're not seeking to do something cute, and in all events we would disclose it. We're simply saying we'd like to be able to do it in an expeditious fashion.

CHAIRMAN NOBER: I mean, I'm not for having to do extra regulatory filings on the one hand. On the other hand, I get a lot of complaints from shippers and private car owners about unilateral changes in car terms, and so I'm sensitive to that. And so one question I would have is: can you spell out exactly what kind of -- rather than open-ended authority to make changes, can you spell out exactly what you would want to make changes in, you know, to avoid duplicative filings?

MR. MEYER: Certainly. The changes -- I mean, the changes would be to the Form A car contract, which is between TAX and its owners. There wouldn't be -- we're not talking about unilateral changes in any contracts or other terms that TAX has with respect to third parties. This is the way in which the railroads, through TAX, decide how it is best to distribute the cars that are part of the pool.

It was talked about -- the desirability of TAX having the freedom to, you know, as a constructive force for efficiency --

CHAIRMAN NOBER: Well, that was my next question, which is, how would you respond to the military's -- the issues that they've raised?

MR. MEYER: Well, from TTX's perspective, you know, I think what Mr. Gounley has recognized is that we are a force for efficiency and finding better ways, more efficient ways to have the TAX cars distributed, moved around the rail network. And TAX will continue to do that, and we are -- as we said in our rebuttal comments, and I think Mr. Reardon can echo here, you know, we are more than eager to participate in a dialogue with shippers, any shipper not just DOD, about, you know, are there better ways to have cars distributed?

And if a better idea does come about and the railroads are -- you know, recognize it and TAX recognizes it, and it's in everyone's interest, what we're asking for basically is to be allowed to do it, provided two critical things, provided that it is consistent; and, second, provided that it's consistent with the restrictions which we're not asking to change at all in this case on assignment and allocation as set forth in '89 and '94.

But if it is consistent with those things, we'll do it, we'll notify the Board as we have consistently of changes in the Form A car contract. There is opportunity for anyone who has an objection to come before the Board at any time on any issue.

But the delay and the burdens associated with a formal application for essentially a new pooling authority is -- really imposes a chilling effect on that kind of creativity.