MR. SMITH: Thank you, Mr. Chairman.

CHAIRMAN NOBER: Okay. I’d like to remind all of the witnesses that we have all of your written testimony, and we’ve had a chance to read it all. So please feel free to summarize any of your comments as you go forward. Mr. Smith?

MR. SMITH: Mr. Chairman and members of the Board, good morning. My name is Paul Samuel Smith, and once again it is my privilege to represent the United States Department of Transportation.
The Department has two main points that we’d like to make today, and the first is to ask the Board to consider seriously the suggestions offered last year in this docket.

Many of those suggestions were drawn from the Board’s then-recent refinement of procedures in major rail rate cases, such as non-binding mediation and accelerated discovery, staff conferences and so forth.

The initial review is all pretty favorable on those, and we think they might well prove helpful in these kind of cases as well.

The second point is to bring to the Board’s attention something the Chairman already alluded to and which we’re well aware of in other contexts, and that is the possibility that large portions of the country’s rail network are approaching the limits of capacity.

There is at least some evidence that points in this direction, and we therefore think that the Board should explore whether and to what extent this is true, for if it is, there are clear
implications for railroad pricing.

To illustrate, as a matter of economics, a railroad at capacity would tend to treat incremental demand than a carrier with excess capacity.

A railroad without capacity would be less willing to accept traffic that simply made some contribution to fixed costs, whereas such a railroad would have to incur such significant fixed costs in order to expand capacity to accommodate more business. Alternatively, such a carrier might be inclined to restrict service.

It is important to keep in mind, of course, that these choices would be made in an industry that overall fails to earn an adequate return on capital.

As a matter of law, of course, continuing requirements to charge reasonable rates and to maintain common carrier obligations are most relevant.

We therefore recommend that the Board not only consider the past suggestions made in this
proceeding already, but to expand its scope to take
into account the prospect of constrained capacity,
and its implications for railroad pricing. Thank
you very much, and I know I’ll try to answer any
questions you might have.

CHAIRMAN NOBER: Yes. Well, thank you.

Commissioner Buttrey?

COMMISSIONER BUTTREY: I have no
questions.

CHAIRMAN NOBER: Commissioner Mulvey?

VICE CHAIRMAN MULVEY: Your testimony
does focus on the capacity crisis facing the
American railroads, and their inability to meet the
forecasted demand for rail transportation over the
next ten to 20 years.

This is a very, very complicated
situation. You would normally think in most
industries that an industry that’s facing this
tremendous surge in demand for its services would be
eager to try to make the investments necessary to
meet it.

But railroads think they cannot earn the
return on that investment to justify making those expenditures.

That’s due to a lot of reasons, including the fact that the railroads face higher costs for certain of their inputs than other firms do, and they also face competition from truckers, who don’t pay the total cost of their use of the infrastructure. Many argue they don’t pay the full costs of their infrastructure, but that’s what the real world is like.

Therefore, if the railroads are going to meet this demand, is there anything the Board can do, to help the railroads meet their need to expand capacity?

Secondly, what do you think is the role for the Federal government? Is there a role of the Federal government to assist the railroads in making that infrastructure investment, to get that capacity to meet that expected demand?

MR. SMITH: I think there is a role for the Federal government. The rail industry is vital to this country’s economy and security. It’s --
probably the most beneficial steps the government
could take would be, would require legislation, that
of course would be beyond the ability of this Board
to implement.

In terms of this Board’s authorities,
much more limited, of course. You have your
requirements to continue to monitor the financial
healthiness. You’ve done that, so there’s that
information that Congress can use and that you can
use.

There’s a proceeding like this to
streamline, in a very admittedly complicated and
difficult situation, the cases that do arise because
since there are no cases that have been brought
under the current procedures and standards for the
small cases.

Clearly, those are not adequate. Those
are not appropriate to meet the needs of all
shippers. It cannot be that every shipper, other
than major shippers that bring the major cases, are
satisfied with their rates and service.

I think it would be very helpful, as we
said 15 months ago, to try and get a better understanding on the dimensions of that problem. Of course, the eligibility standards, for whatever shippers and cases might be appropriate for these new procedures and standards, whatever they might be, are an immediate matter of controversy.

Some would make them open only to shippers of no more than a certain size. Some would make them open to shipments of no more than a certain size.

So I wish I could be more creative myself in offering to you the kinds of things that would be helpful in putting some concrete regulations, procedures and standards in place. I’m afraid I really cannot.

CHAIRMAN NOBER: Mr. Smith, I mean, you mentioned something that I had mentioned as well, which is the impact of the needs of capacity on how we would look at this. How would you have us do that? What suggestion do you have? How would we take that into account?

MR. SMITH: Well, I think the capacity
is a factor that, of course, relates to more than just this proceeding, and it has very broad impact upon the industry and upon the economy beyond that. That might take more time.

I don’t know that I would recommend doing nothing while you determine the existence of the problem where it might be, whether it’s just seasonal, as it has been in the past, and so on and so forth.

I would recommend moving forward on more finite, more narrowly-focused procedures and standards that might apply in these cases, but by all means moving forward simultaneously with an exploration of the capacity and how economically and legally that would impact upon, in some cases, even the major rate cases and not just these.

CHAIRMAN NOBER: Is it the Department’s position that there should be some changes to our current standards?

MR. SMITH: I think there has to be, because these have just simply proven not attractive to any kind of shipper.
CHAIRMAN NOBER: So the status quo is unacceptable in the Department’s view?

MR. SMITH: I think that’s right.

CHAIRMAN NOBER: Okay. Well, thank you.

Anybody else have any questions?

VICE CHAIRMAN MULVEY: No.