

UNITED STATES OF AMERICA  
SURFACE TRANSPORTATION BOARD

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PETITION FOR RULEMAKING TO ADOPT REVISED  
COMPETITIVE SWITCHING RULES

+ + + + +

DOCKET NO. EP 711

+ + + + +

Wednesday,  
March 26, 2014

Surface Transportation Board  
Suite 120  
395 E Street, S.W.  
Washington, D.C.

The above-entitled matter came on  
for public hearing, pursuant to notice, at  
9:30 a.m.

BEFORE:

DANIEL R. ELLIOTT, III Chairman

ANN D. BEGEMAN Vice Chairman

1 P-R-O-C-E-E-D-I-N-G-S

2 (9:30 a.m.)

3 CHAIRMAN ELLIOTT: Hi, good  
4 morning everyone. Welcome to the second day  
5 of the EP 711 hearing. And I don't know if  
6 everyone was here yesterday for my procedural  
7 comments but, very similar to every other  
8 hearing that we've had.

9 We have lights in front of us.  
10 Those lights, when green, means you start and  
11 the yellow light means you have one minute  
12 left. And the red light means please wrap up.  
13 I won't shut you off when the red light goes  
14 off so feel free to at least continue your  
15 thought.

16 And if you need a little extra  
17 time, if it's running a little long for  
18 whatever reason, I've been pretty generous in  
19 allowing that because this is a very important  
20 hearing. So I definitely want to hear what  
21 you have to say.

22 So I think that's all I have. Do

1     you have anything? Okay, why don't we begin  
2     with Panel Number V, the Railroad panel. And  
3     I believe we are going to start with Ms.  
4     Mulligan from BNSF.

5                   MS. MULLIGAN: Good morning,  
6     Chairman Elliott, Vice Chairman Begeman. My  
7     name is Jill Mulligan. I'm associate General  
8     Counsel Regulatory for BNSF Railway. I  
9     appreciate the opportunity to testify here  
10    before you for the first time.

11                   The Board has initiated this  
12    proceeding to gather information regarding the  
13    potential impacts of NIT League's competitive  
14    access proposal on the national transportation  
15    network and the parties who rely on it.

16                   Leading up to this hearing the  
17    Board has received sizable submissions  
18    detailing the impact of the NIT League  
19    proposal on railroads, on shippers qualifying  
20    for access under the proposal and for the  
21    shippers who would not.

22                   BNSF joins in the comments of the

1     AAR which address in detail the specific  
2     questions raised by the Board as well as the  
3     strengths and shortcomings of the various  
4     methodologies and assumptions used by the  
5     parties to estimate the impact of NIT League's  
6     proposal.

7                 I do not intend to reiterate those  
8     comments here. My comments today are intended  
9     to highlight several general but important  
10    principles that BNSF believes that the Board  
11    should remain focused on during this  
12    proceeding.

13                First, the Board should promote  
14    competition by allowing market forces to  
15    govern. Regulatory intervention should be  
16    limited to circumstances where market forces  
17    have failed to protect shippers from abuses of  
18    market power.

19                The Rail Transportation Policy  
20    directs the Board to minimize regulatory  
21    control over the rail system and allow, to the  
22    maximum extent possible, competition and

1 demand for services to establish reasonable  
2 transportation rates.

3           The Board has been mindful of  
4 implementing rules that generally adhere to  
5 the principle that markets for rail services  
6 should be allowed to operate freely, reserving  
7 regulatory intervention for situations where  
8 it is necessary to protect from abusive market  
9 power.

10           Where shippers believe that line  
11 has been crossed the STB currently provides  
12 direct and meaningful remedies. Most notably,  
13 the Board continues to refine its standards  
14 and procedures to make rate cases more  
15 accessible to shippers who believe they are  
16 entitled to rate reductions.

17           Adoption of NIT League's proposal  
18 would mark a significant departure from those  
19 principles. Under the Board's current regime  
20 access remedies are available to market  
21 participants but are appropriately limited to  
22 instances where serving railroads' actual

1     conduct has required corrective regulatory  
2     intervention.

3             Competitive access remedies, to  
4     date, have been properly focused on addressing  
5     individual instances of competitive harm. In  
6     stark contrast, NIT League's one size fits all  
7     proposal requires no individualized showing  
8     that there is a service issue, that access by  
9     another carrier is appropriate or that a rate  
10    reduction is appropriate before an  
11    extraordinary remedy kicks in.

12            As the AAR and my fellow panelists  
13    point out, that extraordinary remedy can carry  
14    with it significant costs to the rail network  
15    and its users. This leads to my second point.

16            NIT League's reliance on revenue  
17    to variable cost ratios as a measure of market  
18    power is invalid. NIT League's reliance on  
19    R/VC levels as a justification for increased  
20    regulation is also invalid. NIT League  
21    acknowledges that it has eliminated any need  
22    to demonstrate competitive harm before access

1 remedies kick in under its regime.

2                   However, NIT League has argued  
3 that it has incorporated at least some element  
4 of individualized competitive inquiry into its  
5 proposal by relying on R/VCs as a trigger for  
6 mandatory switching access.

7                   Specifically, NIT League asks that  
8 a movement exceeds 240 percent of its variable  
9 costs and is within a prescribed distance from  
10 the interchange be presumed to lack  
11 competitive alternatives and, therefore, be  
12 entitled to mandatory switching.

13                   In doing so, NIT League is making  
14 two assumptions. One, that a rail carrier's  
15 market power can be assessed by reference to  
16 the R/VC for the service. And, two, that  
17 crossing an arbitrary line, here 240 percent  
18 R/VC of a carrier's system average URCS cost,  
19 means that a carrier possesses market power.

20                   These assumptions are simply not  
21 correct. BNSF sets rates based on and  
22 responsive to market conditions. Those market

1 conditions may permit rates that are high or  
2 low relative to BNSF's costs.

3 The R/VC level for a particular  
4 rate does not give the Board meaningful  
5 information about the competitive environment  
6 for that traffic. While R/VCs may be  
7 necessary tools in applying certain rate  
8 reasonableness methodologies they cannot  
9 legitimately be used as determinants of market  
10 power or its abuse.

11 Equally important, when R/VCs are  
12 incorporated directly into regulatory  
13 mechanisms it creates perverse incentives. It  
14 rewards the higher cost, less efficient  
15 railroad and penalizes individual carriers who  
16 make capital investments to improve  
17 efficiencies.

18 Capital investments that reduce  
19 congestion or improve efficiency would  
20 decrease a railroad's operating expenses  
21 which, in turn, reduce our variable costs.  
22 Examples of those investments are lighter rail



1 cars or more efficient locomotives that reduce  
2 fuel consumption.

3 The result is that without any  
4 change in the rate being charged to the  
5 shipper, the carrier's R/VC has increased.  
6 For significant investments that increase in  
7 the R/VC for individual movements would be  
8 material. Such a change in URCS alone may  
9 increase a rate above the arbitrary 240  
10 percent level contained in the NIT League  
11 proposal.

12 While that would trigger an  
13 extraordinary remedy under the NIT League  
14 regime, it certainly doesn't indicate an  
15 abusive market power. To be clear, while the  
16 R/VC has increased, nothing has changed in the  
17 competitive landscape. The shipper's rate has  
18 not increased.

19 The railroad has simply undertaken  
20 the risk of making a very significant  
21 efficiency investment and, as a direct result,  
22 has become subject to adverse regulatory

1 intervention where such regulation was not  
2 previously justified.

3 The result is a regulatory system  
4 that actually incentivizes inefficiencies and  
5 higher costs and disincentivizes the very type  
6 of investment the Board should be encouraging.

7 Third, parties should not use  
8 reciprocal switching rules, revisions to those  
9 rules, to expand the scope of the Board's  
10 jurisdiction to include exempt traffic not  
11 subject to STB regulation.

12 NIT League's petition did not  
13 clearly address whether there are categories  
14 of movements that would be excluded from  
15 switching access and many parties included  
16 certain categories of non-regulated traffic in  
17 their impact studies. The Board should affirm  
18 that no competitive access proposal can be  
19 considered that would apply to exempt or  
20 contract traffic.

21 This is consistent with the  
22 principles of focused and limited intervention

1 captured in the rail transportation policy and  
2 is otherwise required by the jurisdictional  
3 limits of the Board's statutory authority.

4 Finally, the Board could not  
5 ignore the effect of reciprocal switching  
6 remedies in applying market dominance  
7 principles in rate reasonableness cases. In  
8 it's July 2012 decision initiating this  
9 proceeding, the Board assumed that the NIT  
10 League proposal would reduce the agency's role  
11 in regulating rates. That is a logical  
12 assumption.

13 Mandated reciprocal switching's  
14 purpose is to provide access to competitive  
15 alternatives for a shipper that would preclude  
16 a finding of market dominance under the  
17 statute, thereby streamlining the STB's  
18 regulation of rates.

19 Nonetheless, some shipper  
20 interests submitted comments in the  
21 proceeding, asking that the Board allow  
22 shippers to pursue a rate reasonableness case

1 in addition to a competitive access case.  
2 These commentators seek the opportunity to  
3 pursue an access case with the additional  
4 option of bringing a subsequent rate  
5 reasonableness case with a complex market  
6 dominance inquiry that, some parties argue,  
7 should ignore any alternative carrier access  
8 it may have obtained.

9           These parties cannot advocate for  
10 the adoption of the NIT League proposal as an  
11 attractive simplification of STB regulation  
12 when their intent is to expand, with  
13 significant additional complexity, the  
14 regulatory rules available to them.

15           We appreciate the Board's interest  
16 in gathering meaningful information from  
17 multiple viewpoints on the impacts that would  
18 flow from the NIT League proposal. We ask  
19 that the Board keep these four important  
20 principles in mind for the remainder of this  
21 proceeding. I thank you for your time and am  
22 happy to answer any questions that you may

1 have.

2 MS. BROWN: Presentation. Can I  
3 be called for presentation? Thank you. Good  
4 morning, and thank you for the opportunity to  
5 address this board. My name is Cressie Brown  
6 and I am CSX Transportation's Vice President  
7 of Service Design, and I've been with company  
8 for 25 years.

9 Our team leads the creation of  
10 rail transportation services that are aligned  
11 with the needs of our customers. Given the  
12 complexity of rail networks, we use extensive  
13 computer modeling to minimize mileage,  
14 handlings and transit time for over 30,000  
15 customer origin and destination pairs.

16 Our work is focused on achieving  
17 high levels of service reliability and  
18 predictability which are critical elements in  
19 meeting our customers' needs. My purpose  
20 today is to provide CSX's perspective on NIT  
21 League's proposal for a radically new  
22 switching model. The proposal would undermine

1 much of what we have accomplished in the areas  
2 of reliability, efficiency and customer  
3 service.

4 One of CSX's core values is it  
5 starts with the customer. And we are  
6 embracing that in a very real sense. We seek  
7 customer feedback and engagement through many  
8 avenues that we collectively call the Voice of  
9 the Customer. Since 2003 an independent  
10 research firm has been conducting surveys of  
11 more than 2500 CSX customers annually and we  
12 are receiving historically high customer  
13 satisfaction marks.

14 It is a virtuous cycle of pleasing  
15 customers, earning more business and  
16 generating investments in additional resources  
17 and new infrastructure. Customer Advisory  
18 Councils are regular face-to-face meetings of  
19 our senior management team with customers  
20 representing all of our markets.

21 The customers on these councils  
22 rotate so that we gain exposure to the

1 particular needs of all of the markets that we  
2 serve. And for the past three years CSX  
3 employees have visited 4,000 customer  
4 facilities annually to listen to customer  
5 concerns and discuss how we can improve  
6 service.

7 We have formed Service Excellence  
8 teams that include our union-represented  
9 employees who have the most frequent contact  
10 with our customers. These cross-functional  
11 teams work with local customers to gain  
12 insights into their specific business needs.  
13 This engagement reinforces that our customer  
14 success is our success.

15 We borrowed from the success of  
16 our Safety culture to create a culture focused  
17 on customers. We have added service training  
18 for 11,000 Train and Engine employees,  
19 specifically focused on improving customer  
20 service.

21 Through all of these engagements  
22 CSX employees are listening to the Voice of

1 the Customer and acting every day on what they  
2 hear. And what they hear is this, service is  
3 paramount.

4 Turning to Slide 3, we are  
5 responding to what we hear. And these are  
6 actual quotes from our customers, and here's  
7 what they tell us.

8 First, consistency of service is a  
9 top priority. Our operating plan is designed  
10 to minimize mileage and the number of times  
11 individual cars must be handled along their  
12 route. Reducing complexity and variability  
13 are key elements to improving transit time and  
14 service reliability.

15 In the words of another customer,  
16 as cars sit we lose money. We have 200,000  
17 railcars on our lines daily, representing an  
18 estimated replacement cost of \$19 billion with  
19 about half of these assets owned or leased by  
20 our customers. That represents a sizable  
21 investment by our customers and CSX, and those  
22 assets transport a significant inventory of



1 products and commodities critical to our  
2 nation's economy.

3 We are committed to developing an  
4 maintaining the most efficient optimized  
5 networks. Customers also tell us that they  
6 need proactive notification for planning and  
7 better results. We have enhanced our  
8 processes, technology and staffing at our 24/7  
9 customer service center, all to improve the  
10 precision and timeliness of communication and  
11 coordination with our customers.

12 Customers use this information we  
13 provide them to plan their resources,  
14 production schedules and retail deliveries,  
15 enabling them to lower their cost of doing  
16 business. On Slide 4 you can see our service  
17 measures, all of which represent a positive  
18 trend over the past decade.

19 Improvements and performance mean  
20 more consistent, reliable service, increased  
21 asset utilization and lower costs for  
22 customers who manage their privately owned

1 railcar fleets.

2 Customers are telling us, and the  
3 customer satisfaction index validates, that  
4 they are increasingly pleased with our  
5 service. And, most importantly, they tell us  
6 that, as an industry, we must not go  
7 backwards. I am very concerned that the NIT  
8 League proposal will force cars to locations  
9 where we do not have the resources or  
10 infrastructure to handle them.

11 Predictable traffic flows and  
12 effective planning are essential to our  
13 ability to provide a reliable service product.  
14 And shipment visibility is critical to  
15 resource and capacity planning. Unanticipated  
16 pop-up traffic that would occur with the NIT  
17 League proposal threatens all of this.

18 The NIT League proposal would  
19 adversely affect all shipments across the  
20 network. You requested empirical evidence and  
21 today I'd like to focus on two real world  
22 examples that were included in the video we

1 previously submitted. If you haven't already  
2 had an opportunity to review the video we hope  
3 you will take the chance.

4 The first example is going to  
5 focus on our carload network. Like other  
6 Class I railroads, CSX employs a Hub and Spoke  
7 system to handle carload freight. The map  
8 highlights our 12 major hump yards. These  
9 hump yards serve as classification hubs or  
10 sort centers, much like an airline hub for  
11 over 30,000 origin/destination pairs.

12 This Hub and Spoke model enables  
13 cars to move across the CSX network in the  
14 most efficient manner possible. CSX and other  
15 railroad operate other yards where cars are  
16 flat switched by a locomotive and crew. A  
17 flat switch yard, however, does not have the  
18 capacity to accommodate the same level of  
19 switching activity as these hump or hub yards.

20 Important to note is that not all  
21 interchanges are performed in yards. Cars can  
22 be interchanged, and often are, on the

1 mainline, in sidings or on a single track.

2 One of the NIT League proposal's fundamental  
3 flaws is that it assumes that every  
4 interchange can function as a hub, and that's  
5 just wrong.

6 Slide 6 illustrates a specific  
7 example of a customer that ships cars from  
8 Mexico to a facility in Jacksonville, Florida  
9 that is served by CSX. Looking at the picture  
10 labeled Current Route, CSX receives the cars  
11 in New Orleans and moves them to a hub in  
12 Waycross, Georgia capable of classifying and  
13 sorting the cars for connecting train service  
14 to Busch yard in Jacksonville, Florida.

15 Busch yard is the serving yard for  
16 the customer, and this route is highlighted in  
17 gold. The customer is located within 30 miles  
18 of CSX's Moncrief yard which is an active  
19 interchange point with Norfolk Southern.

20 Under NIT League's proposal the shipper could  
21 obtain line haul transportation via NS from  
22 New Orleans and require CSX to receive the

1 traffic at Montcrief yard.

2 Montcrief, however, is not a hub  
3 or a sort center. Rather, it is a local yard  
4 with limited capacity and no connecting train  
5 service to Busch yard. To comply, CSX, as  
6 illustrated in the picture labeled NIT League  
7 Route, would have to take the cars from  
8 Montcrief 147 miles north to Waycross where  
9 they would be sorted and classified for a  
10 train destined to Busch.

11 This routing adds approximately  
12 300 miles and 3 days to the overall movement.  
13 You can clearly see how inefficient this would  
14 be and how it would increase congestion and  
15 readily degrade asset utilization, transit  
16 time and service reliability.

17 A second example involves unit  
18 trains. Unit trains require careful planning  
19 and a high degree of predictability to extract  
20 all of their efficiencies. The routing of  
21 unit trains is over the most direct path and  
22 is tightly coordinated.

1                   Slide 8 illustrates the  
2                   consequences of alternate unit train routing  
3                   in Baltimore. In Baltimore CSX and Norfolk  
4                   Southern have an active interchange at Bayview  
5                   yard. Within 30 miles is a customer that  
6                   receives unit trains of ethanol.

7                   Today CSX delivers the trains  
8                   direct from Chicago to the destination. This  
9                   routing, indicated in gold, is critical in the  
10                  Baltimore area since the ethanol train is just  
11                  one of dozens of trains operating through  
12                  Baltimore each day including other freight and  
13                  MARC commuter traffic. Under the NIT League  
14                  proposal, NS would bring the train from  
15                  Chicago into Baltimore for switching to CSX at  
16                  the Bayview interchange.

17                  From here the train would be  
18                  routed, as indicated by the red line, through  
19                  downtown Baltimore, through the Howard Street  
20                  Tunnel, passed Oriole Park, the Camden  
21                  Passenger Station, the Baltimore Ravens M&T  
22                  Stadium and to the customer's final

1 destination. The difficulties caused by this  
2 move are broad and varied and include  
3 potential disruptions to tightly scheduled  
4 MARC Commuter trains.

5 In summary, railroads have complex  
6 networks which rely on density, efficiency and  
7 predictability. It is not in the broader  
8 public interest to experiment with a forced  
9 switching scheme which would ultimately create  
10 less reliable and less cost-effective service  
11 for our customers.

12 Some of the greatest customer  
13 service and efficiency improvements in  
14 Staggers have been the result of longer,  
15 single-carrier hauls and reduced switching.  
16 The NIT League proposal turns back the clock  
17 on these gains achieved over decades.

18 We urge the Board to reject this  
19 sweeping regulatory restructuring and to  
20 maintain the balanced environment that is a  
21 pillar of our world-class freight system.  
22 Thank you, and I'll be pleased to take any

1 questions.

2 MR. BAILEY: Good morning. It's a  
3 pleasure to be here this morning and be able  
4 to speak on behalf of Norfolk Southern as to  
5 this subject.

6 My name is Rush Bailey and I'm  
7 Assistant Vice President of Service Management  
8 for Norfolk Southern Corporation. I've been  
9 employed by Norfolk Southern or an NS  
10 subsidiary since 1976. And I've worked in  
11 various capacities in both our marketing and  
12 operating divisions.

13 Over the course of those many  
14 years I've come to appreciate the complexity  
15 of railroad operations, and particularly the  
16 nature of network operations, which require  
17 consistent performance in each of its  
18 components in order to consistently deliver a  
19 high level of service to our customers.

20 Norfolk Southern's rail system  
21 includes over 20,000 route miles spanning 22  
22 states on which we essentially run three



1 networks. Each of these share a common set of  
2 assets -- track, terminals, locomotives,  
3 crews, support systems and railcars.

4 The largest part of our unit train  
5 network is dedicated to coal, but we also have  
6 steel, stone, grain, crude oil and other bulk  
7 commodity unit trains. Our premium service  
8 network consists primarily of intermodal and  
9 automotive, and our largest and most complex  
10 network is our general merchandise carload  
11 network.

12 The nature of the NIT League  
13 proposal is such that it's there, the general  
14 merchandise carload network, that I'll focus  
15 my comments today. This network is a good  
16 proxy for our entire system and the potential  
17 impact on network operations.

18 When discussing railroad network  
19 operations I frequently use airlines as an  
20 analogy. While it seems odd at first, the  
21 models are actually very similar. So imagine,  
22 if you will, if airlines were responsible for

1 passengers, not just between terminals but  
2 from their actual point of origin, say from  
3 home, just outside of Atlanta, to the STB  
4 offices here in Washington.

5           The operation would become much  
6 more complex. But the fact is that that's  
7 what Norfolk Southern does every day in its  
8 general carload network, moving thousands of  
9 shipments every day between 8,700 shippers,  
10 receivers and interchange points.

11           Now not every passenger arriving  
12 at the Atlanta airport is headed for the STB's  
13 offices in Washington. And similar to the  
14 airline operations, once at the origin  
15 terminal, rail shipments have to be sorted and  
16 classified into groups or blocks.

17           Norfolk Southern has over 32,000  
18 origin/destination pairs and those shipments  
19 are grouped into over 1,500 road blocks and  
20 5,000 local blocks. These blocks are then  
21 combined into trains in the Terminal 4 in  
22 yard.

1                   This process is repeated at  
2           intermediate terminals as the shipment  
3           progresses across the network and then again,  
4           finally, at the destination terminal where the  
5           shipment will finally be classified for the  
6           customer at the destination or to a connecting  
7           carrier at the interchange.

8                   These classification processes or  
9           handlings at origin, destination and  
10          intermediate terminals make up the bulk of  
11          time that a typical shipment spends in  
12          transit. In fact, a typical general  
13          merchandise shipment will spend only about a  
14          quarter of its total transit time in road  
15          train service.

16                  In a heavy asset-based industry  
17          like ours shipment velocity is a key driver of  
18          cost. The faster a shipment's cycle, the  
19          higher the utilization of railcars,  
20          locomotives, terminals and other assets.  
21          Conversely, the slower a shipment cycles, the  
22          more units are required to move the same

1 amount of traffic.

2 And at some point, adding more  
3 cars and locomotives to the network has a  
4 counterproductive effect of further slowing  
5 shipments, as we have seen by past experience  
6 in our industry. Velocity is also a key  
7 driver of service delivery for rail customers.

8 Here you see our composite service  
9 metric in red. The composite service metric  
10 combines our internal measures of on-time  
11 train performance, connection performance --  
12 that is getting shipments to their scheduled  
13 connections at terminals and plan adherence  
14 which measures the execution of work orders by  
15 our road trains, essentially pick-ups and set-  
16 offs.

17 The blue line is line haul miles  
18 per day. It's a measure of miles that a  
19 shipment would travel in a 24-hour period. It  
20 includes over-the-road time as well as dwell  
21 time at intermediate terminals, passing  
22 sidings and interchanges and also non-handling

1 time at intermediate terminals such as crew  
2 changes or fueling activities.

3 This graph clearly shows the  
4 correlation that better velocity equals better  
5 service. So you might ask about the  
6 divergence in lines in the latter half of 2012  
7 and 2013 when network velocity moved to its  
8 highest sustained levels we had ever seen.

9 Norfolk Southern measures service  
10 as on-time performance and we define that as  
11 neither late nor early. We recognize that  
12 either can disrupt customer operations and  
13 variation in our operation requires additional  
14 asset commitments.

15 As velocity moved into uncharted  
16 levels we found that a number of shipments  
17 arriving more than 24 hours early increased  
18 significantly. And in the time that's  
19 followed we've been reviewing train schedules  
20 and minimum connection times to take time out  
21 of those schedules, which has a very positive  
22 result for both Norfolk Southern and its

1 customers.

2 Understanding this relationship,  
3 Norfolk Southern has successfully focused  
4 efforts on maintaining or improving shipment  
5 velocity, which is shown here in tan, by  
6 minimizing the number of intermediate  
7 handlings, which is shown in blue. The  
8 improvements have both improved service to our  
9 customers and enabled operating efficiencies.

10 This is where the NIT League  
11 proposal because it would result in more  
12 handlings per shipment. The impact of  
13 increased handlings per shipment is even  
14 clearer here where we've plotted our network  
15 philosophy as measured by line haul miles per  
16 day against the average number of intermediate  
17 handlings per shipment trip.

18 And you can see that each  
19 additional handling required by shipment  
20 reduces the average velocity for that  
21 shipment. More handlings mean reduced  
22 velocity and that will result in a reduced

1 service metric, longer transits, more  
2 variation in network operations and service  
3 delivery.

4 Longer transits and increased  
5 variation in operations also means that rail  
6 carriers will have to apply more assets to the  
7 same volume of business. All of these changes  
8 affect more than just the issued shipment  
9 because adding assets to a network to move the  
10 same amount of traffic often has the effect of  
11 further slowing the network and congesting it.

12 While a few customers might be  
13 willing to accept these tradeoffs, slowing and  
14 congesting the network will negatively impact  
15 rail carrier service levels and its underlying  
16 cost structure. And those effects are likely  
17 to be borne by customers.

18 The effect is not limited to those  
19 just directly impacted by this proposal but  
20 also those whose shipments may be moving on  
21 the same trains or through the same terminals  
22 or on or in the same railcars, moving, again,

1 in a network that shares common assets.

2 In the last few months U.S. rail  
3 system has endured shocks from severe winter  
4 weather. The result, as you see on this  
5 slide, has been a decline in the line haul  
6 miles per day compared to 2013. As we all  
7 know, the effects from this decline have been  
8 felt by many customers across our network, and  
9 not just those in the areas affected directly  
10 by the winter weather.

11 Power shortages and railcar  
12 shortages are further symptoms of an  
13 underlying drop in network velocity and a  
14 resulting decrease in cycle times. And  
15 although Norfolk Southern is taking many steps  
16 to reverse this trend, it takes time to turn  
17 the tide. These are exactly the types of  
18 effects one should expect from opposal of  
19 light NIT Leagues that will increase handlings  
20 and therefore decrease network velocity.

21 In conclusion, these relationships  
22 demonstrate that NIT Leagues's proposal and



1 other forced access proposals would be  
2 counterproductive to Norfolk Southern's goal  
3 of minimizing handlings, increasing velocity,  
4 optimizing network operations and service for  
5 our customers. I than you for your time.

6 MR. HALEY: Could we have the  
7 slide clicker, please? Could you bring up my  
8 slides, please? Good morning. Thank you for  
9 the opportunity to speak before you.

10 My name is Tom Haley. I'm  
11 Assistant Vice President, Networking Capital  
12 Planning for Union Pacific, a position I've  
13 held since 1998. I have over 30 years'  
14 experience in the railroad industry. I  
15 started with CSX in 1983 and joined UP in 1989  
16 after earning my MBA.

17 I've worked in Operations, Network  
18 Design and Finance. I'm accompanied this  
19 morning by Louise Rinn, sitting to my left,  
20 Associate General Counsel at Union Pacific.  
21 In my role I share responsibility for the  
22 design and development of UP's rail network,

1 service plans and capital plans.

2 In my time at UP we've learned  
3 important lessons about the causes of service  
4 disruptions and the value to our customers of  
5 consistent, excellent service. We've  
6 substantially improved our service, and this  
7 has translated into increased customer value  
8 and satisfaction.

9 I appreciate the opportunity to  
10 discuss NIT League's proposal with you. This  
11 proposal would seriously disrupt UP's  
12 operations and reduce our ability to provide  
13 reliable service to our customers. The  
14 proposal threatens the exact success story you  
15 see on this slide.

16 I am specifically concerned that,  
17 first, the proposal would increase workload in  
18 terminals that are already capacity  
19 constrained. Second, the increased workload  
20 would degrade service across our network.  
21 Third, the proposal would limit our ability to  
22 plan and manage our network. And, fourth, the

1     proposal would increase the need for capital  
2     investment while reducing our ability to  
3     invest.

4             In short, NIT League's proposal  
5     would create significant problems and, at the  
6     same time, prevent us from fixing them. Our  
7     customers would suffer as a result. Let me  
8     explain these concerns.

9             First, NIT League's proposal would  
10    increase workload in terminals that are  
11    already capacity constrained. The Board heard  
12    Mr. Rennicke's testimony yesterday about the  
13    operational complexity of switching cars and  
14    how reciprocal switching compounds this  
15    complexity.

16            I'd like to further show how this  
17    consumes terminal capacity. Today a typical  
18    operation is for a car to move from a customer  
19    to a terminal on a local train where the car  
20    is switched once for an outbound train. With  
21    reciprocal switching the car is switched for  
22    delivery to the other railroad, then moved to

1 the other railroad, and then switched again in  
2 the other railroad's yard before departing on  
3 an outbound train.

4 The clear result is extra  
5 switches. And the extra switches multiply  
6 quickly. The arrows are double-headed because  
7 switches occur for both loads and empties  
8 moving between the two railroads. The  
9 complexity increases even further if a third  
10 or fourth railroad is involved in the terminal  
11 area.

12 And that's precisely what NIT  
13 League's proposal could force upon UP and the  
14 other railroads. The number of locations on  
15 our network where this could occur will  
16 multiple significantly. UP's terminals are  
17 not equipped to handle such an increased  
18 workload.

19 We plan for our terminals to  
20 operate at fluid capacity levels. This allows  
21 for demand fluctuations, weather events and  
22 other disruptions. Today we are generally

1 meeting this target. However, forecasts show  
2 that transportation demand will increase.

3 This means we face capacity  
4 challenges in many terminals. This isn't just  
5 a matter of railroaders getting the job done.  
6 The capacity does not exist to do what is  
7 being proposed.

8 The additional switches could  
9 force UP well beyond its capacity tipping  
10 point in many terminals. And we know from  
11 experience that consequences would be severe.

12 That brings me to my second point,  
13 NIT League's proposal will have ripple effects  
14 that will harm customers across our network.  
15 As the chart in the upper left shows increased  
16 switching leads to increased freight car  
17 inventory. Every additional switch takes time  
18 and introduces the risk of missing a  
19 connection.

20 More switching, therefore, means  
21 more dwell time for cars in terminals. And  
22 the longer cars stay in terminals the more

1 cars we have on our system. The chart in the  
2 upper right shows the problem with increased  
3 inventory. The more cars we have on our  
4 system, the slower the cars move.

5 And velocity is the critical  
6 driver behind efficient and reliable service.  
7 The chart on the bottom left demonstrates this  
8 point. Slower velocity harms our service  
9 product. And as you can see in the chart on  
10 the bottom right, poor service creates unhappy  
11 customers.

12 These charts, read together, are a  
13 proof statement of how local changed ripple  
14 through a rail network. I've been in my  
15 current position throughout the time period  
16 reflected in these charts. I've witnessed,  
17 firsthand, the effects that additional  
18 switching has on our system.

19 I can confirm the implication of  
20 the data. NIT League's proposal would degrade  
21 service on our network and harm our customers.  
22 And basically, and my third point, UP will not

1     be able to address these service issues using  
2     our normal planning and management tools.

3             Our ability to plan and manage  
4     depends on having accurate information about  
5     expected traffic flows. We would lose  
6     visibility and the ability to manage our  
7     operation under NIT League's proposal. This  
8     slide shows the problem.

9             For long-term planning we rely on  
10    traffic forecasts that our marketing team  
11    develops with our customers. These forecasts  
12    drive our capital, resource and service plans,  
13    and they're critical because of the long lead  
14    times to put facilities and equipment in  
15    place.

16            Qualifying new train crews takes  
17    six to nine months, and adding rail  
18    infrastructure can take two to three years or  
19    more. We already face many challenges  
20    forecasting traffic two to three years in  
21    advance for our own business. We have no  
22    visibility into our competitors' plans which

1 would add a new dimension of uncertainty to  
2 our planning.

3 We also must do tactical planning  
4 to adjust our train plans and reposition  
5 resources to meet anticipated demand. Again,  
6 advanced information is critical because of  
7 the lead time required. But we don't have  
8 visibility into our competitors' activities  
9 with enough lead time to match resources with  
10 shifting demand. The ultimate result will be  
11 poor service.

12 Finally, on a day-to-day basis, we  
13 make real-time decisions to balance terminal  
14 capacity, control the timing of traffic flows  
15 and assign resources such as crews and  
16 locomotives to handle our line haul traffic.  
17 But we do not know how much traffic will  
18 require reciprocal switching until it appears  
19 on our doorstep.

20 NIT League's proposal means more  
21 traffic would be moving in our blind spots.  
22 That brings me to my fourth point. NIT



1 League's proposal would increase the need to  
2 invest in terminal capacity while reducing  
3 our ability to invest.

4 Terminals are an Achilles' heel  
5 for the rail network. They are extremely  
6 valuable in bundling and unbundling traffic  
7 to efficiently move shipments to and from our  
8 customers, but they are typically located in  
9 congested urban areas and are very expensive  
10 to expand, if it's even possible to expand  
11 them.

12 However, if NIT League's proposal  
13 is adopted, I believe you will see us invest  
14 less in terminals. Terminal investment will  
15 be less attractive because of less revenue,  
16 increased uncertainty about where to put  
17 capacity and whether such capacity will  
18 generate an adequate return.

19 I'd like to make one final point  
20 before I wrap up. One of the NIT League  
21 witnesses claimed the rapid increase in crude  
22 oil traffic proves that railroads can easily

1 handle unpredictable shifts in traffic. In  
2 reality, his example proves the opposite.

3 In UP's largest crude oil lane we  
4 began working with customers more than three  
5 years ago. We spent a year developing  
6 business, operating and capital plans. And  
7 then, as business ramped up, we spent another  
8 two years methodically investing in  
9 facilities and putting resources in place to  
10 make the operation successful.

11 And, I'll point out, this was for  
12 unit train business in one corridor with an  
13 attractive return, not carload traffic  
14 shifting in busy terminal areas.

15 I want to end with my opening  
16 chart. UP has diligently worked to reduce  
17 switching events, reduce car inventory and  
18 simplify transportation plans in order to  
19 provide better service for our customers. As  
20 the chart shows, we've been successful. This  
21 success creates value for our customers.

22 The NIT League proposal adds

1 switching and reduces efficiency. It will  
2 require capacity that does not exist. It  
3 will damage service, perhaps severely. I  
4 believe the long-term adjustment that will  
5 occur from this will be moving less freight.

6 The NIT League proposal would  
7 reverse the progress we made over the last 15  
8 years to the detriment of our customers. I,  
9 therefore, urge you to reject it. Thank you.

10 MR. KONSCHNIK: Good morning,  
11 Chairman Elliott, Vice Chairman Begeman. I'm  
12 David Konschnik, and I'm honored to appear  
13 before you today.

14 In my view, the comments do not  
15 support a change in the Board's approach in  
16 matters of competition and access. The vast  
17 majority of the concerns are about rate  
18 increases and the levels of rates, especially  
19 for coal and chemicals.

20 A fix for customers' rate concerns  
21 is not a fundamental restructure of the rail  
22 industry. Adoption of an unprecedented and

1 far reaching reciprocal switching regime  
2 would have significant unintended  
3 consequences. Rather, the fix is to continue  
4 what the Board has always done -- review,  
5 revise, test, evaluate and change its rate  
6 complaint processes as experience shows is  
7 needed.

8 In my various roles at the ICC and  
9 STB over a 30-year career I've seen firsthand  
10 how the agency has responded to shipper  
11 concerns by making changes to its rate,  
12 service and unreasonable practice complaint  
13 processes.

14 The Board has been open-minded and  
15 flexible in considering concerns and in  
16 trying to improve the processes and make them  
17 more efficient and less costly where possible  
18 without sacrificing fairness to the parties  
19 in individual cases while endeavoring to  
20 remain faithful to the congressional charges  
21 contained in the Staggers Act and the ICC  
22 Termination Act.

1                   Here are a few examples of what  
2                   the Board has done to try to be responsive to  
3                   the concerns that the rate complaint process  
4                   was too long, too expensive and not available  
5                   to smaller shippers.

6                   The Board has eliminated  
7                   consideration of product and geographic  
8                   competition and market dominance  
9                   determinations, adopted mandatory non-binding  
10                  mediation, established a new arbitration  
11                  program for rate and other disputes and  
12                  improved the discovery process, made changes  
13                  to procedures and rules to speed up cases  
14                  including elimination of the ability to  
15                  movement-specific adjustments to URCS,  
16                  adopted simplified standards for rate cases  
17                  including simplified SAC and the Three  
18                  Benchmark methodology.

19                  Just in the past year the Board  
20                  has raised the limits on relief for rate  
21                  reasonableness complaints brought under  
22                  simplified SAC and Three benchmark, sought

1        comments on how to ensure that the Board's  
2        rate complaint procedures are accessible to  
3        grain shippers and opened a proceeding in  
4        response to a request that the Board abolish  
5        the use of the multi-stage DCF model in  
6        determining the railroad industry's cost of  
7        equity capital.

8                    The Board has also improved the  
9        rail customer and public assistance programs.  
10       Now, the Board's reforms may not go as far as  
11       some would like, but there have been  
12       significant reforms and the Board should be  
13       congratulated for its thoughtful and  
14       analytical approach.

15                   Some of the Board's procedural  
16       changes have only recently become effective.  
17       Changes that have been in effect for some  
18       time appear to have provided great relief for  
19       shippers whose rates were too high. These  
20       changes should be given time to prove their  
21       effectiveness. And the Board can adjust the  
22       procedures in the future if it's shown to be

1       necessary.

2                       In the meantime, a case-by-case  
3       approach is the best and most reasonable  
4       approach. Due to these changes several SAC  
5       cases over the past few years have found in  
6       favor of the shipper. More recently there  
7       have been several SAC and simplified SAC  
8       cases that have been settled. And with  
9       respect to those that have proceeded to a  
10      full Board decision, the shippers have  
11      prevailed on most of them.

12                    More broadly, I believe that the  
13      Board's decisions that have clarified and  
14      simplified the rules have helped to encourage  
15      the parties to settle their disputes rather  
16      than litigate them. As such, the Board  
17      should move forward with that approach rather  
18      than moving in the opposite direction in  
19      adopting a complex regulatory scheme that  
20      will take years to figure out and result in  
21      years of litigation and disputes.

22                    Adoption of the NIT League

1     proposal could result in significant  
2     unintended consequences such as some shipper  
3     groups benefitting while others pay higher  
4     prices or get worse service, network  
5     inefficiencies, operational chaos and service  
6     problems discussed in detail by others  
7     testifying at this hearing, extended legal  
8     disputes over the eligibility of a particular  
9     shipper or shipment, the compensation to be  
10    paid and the implementation of the granted  
11    access, potential undermining of the  
12    competitive role played by smaller Class Is,  
13    regional railroads, short lines, all of whom  
14    could have their routes short-hauled and  
15    their most profitable traffic cherry-picked  
16    by the larger Class Is leading, possibly, to  
17    fewer competitive alternatives for shippers.

18               Overall, I think the Board should  
19    be mindful that a little bit of regulation  
20    goes a long way and over-regulation risks  
21    destroying the ability of the railroad  
22    industry to continue to provide the



1 combination of service, efficiency and  
2 reasonable rates this agency is committed to  
3 achieve. Thank you very much for allowing me  
4 to appear here today. I'd be happy to answer  
5 any questions you have.

6 CHAIRMAN ELLIOTT: Thank you very  
7 much for your testimony. Most of the  
8 testimony focused on issues that would arise,  
9 complexities that would arise out of this  
10 proposal and the difficulties.

11 And I think Mr. Rennicke,  
12 yesterday, kind of laid it out very clearly.  
13 And he showed that if you use the proposal  
14 and were involved in the switching that there  
15 would be 24 steps to the move. And then he  
16 said, normally, if the incumbent railroad  
17 handled the traffic it would be six steps.

18 I don't know if that's the way it  
19 occurs all the time, but I think CSX and UP  
20 also presented some complexities that would  
21 arise as a result of applying the proposal.  
22 The question that I have is if it is so much

1 more complicated and the two railroads are  
2 competing how would the incumbent railroad be  
3 able to be underpriced in those situations?

4 It seems as if, that the alternate  
5 railroads would have to spend quite a bit  
6 more money on cost to be involved in these  
7 extra moves, I guess, is what I'm getting at.

8 So, I'm missing some of the logic  
9 on the pricing, that it would seem to me that  
10 the incumbent railroad would generally win in  
11 those situations because of the lack of  
12 complexity in their move compared to the  
13 alternate railroad. Does that make sense?

14 MR. HALEY: I think so. Want me  
15 to start that out or do you, Cressie?

16 MS. BROWN: Sure, go ahead.

17 MR. HALEY: I honestly, I can't  
18 speak to the pricing end of it. I can tell  
19 you that where reciprocal switching does  
20 exist on our railroad to day we see the  
21 phenomena I talked about, which is the  
22 increased complexity, less efficiency, longer

1 dwell times for cars. So on the pricing  
2 side, I really can't comment.

3 MS. BROWN: I mean, I would just  
4 add that in no circumstance where you have  
5 forced switching can you envision that it  
6 would be less complex, right.

7 So there is, by definition, and  
8 Bill Rennicke did a very good job of laying  
9 out a couple of those scenarios, some are  
10 more simplistic than others, but in every  
11 situation there would be additional handling  
12 and additional costs and, by default, more  
13 congestion, a slower railroad.

14 So our concern is not only is that  
15 higher cost to railroads collectively, to the  
16 entire transportation product, but to our  
17 customers because most of the cars that we're  
18 moving are customer-owned equipment, right.  
19 So for them to handle any degradation in  
20 service, any slowing down of our networks,  
21 also has a significant cost to all the other  
22 customers whose shipments we're moving

1       because they own the equipment that we're  
2       moving across our networks.

3                   MS. RINN:   If I may, Chairman?

4                   CHAIRMAN ELLIOTT:   Sure.

5                   MS. RINN:   If you're talking about  
6       the reciprocal switching that is happening  
7       today that's essentially voluntary.

8                   CHAIRMAN ELLIOTT:   Right.

9                   MS. RINN:   It's either been  
10      commercially negotiated or it was part of a  
11      merger condition to protect existing  
12      competition.   And then it's voluntary in the  
13      sense that the merging railroads had the  
14      choice to not proceed with the transaction or  
15      to go forward with the transaction knowing  
16      that they were getting benefits.

17                   And it also is truly reciprocal.  
18      We have many bilateral agreements that  
19      basically set up charges where we say we'll  
20      do the switching for you and you'll do the  
21      switching for us, and we'll charge each other  
22      the same.

1           In those circumstances you're not  
2 worried so much about the control of the cost  
3 and the decision to do it, I guarantee you,  
4 is not coming from the operating department.  
5 It is basically a commercial decision. It's  
6 voluntary, and it's reciprocal.

7           Here you are talking about a  
8 proposal that is going to be forced, and it's  
9 going to be unilateral. And, therefore,  
10 you're not going to be able to have a single  
11 set of fees. You're going to have to take  
12 into account all of the costs of doing the  
13 movement. It's a completely different  
14 approach to the concept of reciprocal  
15 switching.

16           CHAIRMAN ELLIOTT: But if it is  
17 your traffic and however we arrive at the  
18 hypothetical access price, my reading on the  
19 statute was that the parties, the railroads,  
20 would have to enter into an agreement and  
21 then it would come to us if there wasn't one.

22           The way I see it is, no matter

1     what, the alternate railroad would be  
2     required to pay more because at least they'd  
3     have to pay for the switch on top of whatever  
4     rate they're quoting. And then you take into  
5     consideration all these complexities added on  
6     top of that, it would seem like it would be  
7     difficult for them if they were actually  
8     competing for that traffic.

9             It would be difficult for the  
10    alternate railroad to win in that fight for  
11    that traffic.

12            MS. MULLIGAN: If I can add to  
13    what Lou Anne was saying, I think that the  
14    situation where you do actually see that  
15    happening, where alternative carrier service  
16    is being provided, are instances where we  
17    have voluntary switching in place.

18            And those are places where they,  
19    the non-incumbent railroad, the new railroad  
20    that's coming in can actually can offer  
21    superior service. It might be an alternative  
22    rate, sorry, a superior route, some other

1 efficiencies that allow them to compete  
2 despite the presence of a switching fee  
3 there.

4 CHAIRMAN ELLIOTT: I guess in that  
5 instance if that is the case, and they can  
6 offer something that's more efficient, the  
7 alternate carrier, wouldn't that make the  
8 system more efficient rather than less  
9 efficient if they have that ability?

10 MS. MULLIGAN: Yes and no, in  
11 specific instances. I think we would find  
12 that a lot of those situations have already  
13 been dealt with through voluntary  
14 arrangements because every incentive is on  
15 the railroads to make those moves happen  
16 where there is an efficiency there.

17 The issue with the NIT League  
18 proposal is that nothing contained in that  
19 proposal actually leads you to identifying  
20 those situations where you could have a  
21 superior, more efficient service offering.  
22 It's not part of the inquiry.

1                   The switching occurs because the  
2                   R/VC is 240, not because there's anything  
3                   particular about that move that says that  
4                   there's going to be an increased efficiency  
5                   or a superior operational move.

6                   CHAIRMAN ELLIOTT:   Okay.

7                   MR. HALEY:    Could I just add to  
8                   that?

9                   CHAIRMAN ELLIOTT:   Sure, go ahead.

10                  MR. HALEY:    I think it's unlikely  
11                  that a route efficiency or there's some other  
12                  efficiency out there that would overcome the  
13                  inefficiency of the additional switching.

14                  It's the extra switch events,  
15                  extra handlings, it's the time, 24 to 36  
16                  hours each time you add an event, usually  
17                  both ends, in both directions, load and  
18                  empty.  And if you just do the math on the  
19                  miles you would have to save an incredible  
20                  number of miles to overcome that.

21                  VICE CHAIRMAN BEGEMAN:  I'll start  
22                  with BNSF's chart on some of the key



1 principles that I'd like to hear your views  
2 on.

3 It says the Board should promote  
4 competition by allowing market forces to  
5 govern. Now, if I think back on the first  
6 panel yesterday, I think that's actually what  
7 they're seeking. They want to have market  
8 forces, instead of one carrier.

9 So help me understand how the  
10 status quo is allowing for captive shippers  
11 to have market forces govern?

12 MS. MULLIGAN: And I think there's  
13 a little bit of a problem with language  
14 that's being used. I think that one of the  
15 issues was saying that, starting at the high  
16 level of switching is obviously pro-  
17 competitive. Options, access to  
18 alternatives, is competitive.

19 What the shippers are actually  
20 seeking is an artificial insertion of  
21 competition into a market where it would not  
22 otherwise exist. And the proposal is really

1 focused on variable costs, as being the  
2 trigger for that. And that proposal, when it  
3 focuses on variable costs, it's actually not  
4 making any sort of a diagnosis about what the  
5 competitive environment is for that traffic.

6 And so, by referencing variable  
7 costs, you're not getting any sort of  
8 education about, is the move that's actually  
9 occurring inefficient? Is there a superior  
10 competitive alternative?

11 MS. RINN: And, if I may, I found  
12 yesterday very striking because the comments  
13 were all premised on an absence of  
14 competition, when, in fact, we face  
15 tremendous competition for the vast majority  
16 of our business.

17 The Board has decided that for  
18 regulatory administrative purposes it's too  
19 complicated to go into product and geographic  
20 and indirect competition and transload  
21 competition. And I understand, given your  
22 directives and your resources, why you may

1       have made those choices.

2                       But in our world, in the marketing  
3       departments of having to deal with it, we are  
4       always in negotiations with our customers  
5       about whether or not, that the service that  
6       we're delivering and the costs that they're  
7       paying for it allows them to compete in their  
8       market, or whether there are other ways of  
9       doing it.

10                      Coal haulings are down, because of  
11       natural gas competition. Grain changes,  
12       depending on whether or not you have a demand  
13       for ethanol and it's taking a short haul to a  
14       nearby elevator or by truck to be turned into  
15       ethanol, or whether there's a longer  
16       distance, or whether there's an export market  
17       going up.

18                      Lumber competes geographically,  
19       across our business groups. We face intense  
20       competition and we use transloads to  
21       basically try to win market share from  
22       others. And we deal with that all the time

1 in our contract negotiations and in setting  
2 our rates.

3 Sometimes we win the business, and  
4 sometimes we lose the business. So all of  
5 that competition is going on but this NIT  
6 League proposal basically is saying there is  
7 no competition, unless we have direct rail-  
8 to-rail competition. And they don't want to  
9 look at, but are we allowing you to keep, or  
10 win, market share versus your competitors?

11 Likewise, when they're saying that  
12 there are no negative impacts on the  
13 customers who would be outside whatever the  
14 secret radius is going to be. They're  
15 ignoring what the impact would be that if a  
16 favorite customer is able to use a regulatory  
17 regime in order to compel a below market  
18 rate, what that does to its competitors.

19 Now, maybe, the railroad's  
20 response is going to be to make up for the  
21 revenue by raising its prices or maybe it's  
22 going to say I'm going to lose more traffic

1     and more revenue if I don't bring my rates  
2     down on the non-favored customers. And so  
3     you're going to have secondary and tertiary  
4     revenue losses to the railroads.

5             And all of that is going on in a  
6     very complex marketplace. And this proposal  
7     is ignoring that marketplace.

8             MR. BAILEY: If I could add  
9     something, I think that there's no doubt that  
10    if something like the NIT League proposal  
11    went through, there are some customers who  
12    would win.

13            I think what you're hearing from  
14    operating folks is that there's a collateral  
15    impact. You're congesting terminals, you're  
16    adding additional work, extra handlings, and  
17    that's going to have an impact on customers  
18    who don't get the benefit of that lower rate.

19            VICE CHAIRMAN BEGEMAN: I'm going  
20    to come back to this topic, but, I did want  
21    to talk with you and with CSX, and ask if you  
22    could discuss the Conrail shared asset area?

1       How does that work? I'm sure that there were  
2       pockets of pain to begin with but it seems  
3       that it's been quite successful - in terms  
4       that it works operationally.

5                   MS. BROWN: Sure. And I think  
6       there's many market differences, and Rush  
7       will comment as well. But Conrail is a  
8       jointly owned entity by CSX and Norfolk  
9       Southern. And when we purchased Conrail  
10      collectively we never anticipated to have a  
11      residual Conrail, right, it is much more  
12      efficient for us to be the single line haul  
13      carrier to provide direct service. So it was  
14      not envisioned as part of the transaction  
15      that we "aspired" to create this Conrail that  
16      exists today.

17                   And while they do, and the staff  
18      there and Ron Batory and his team (I'm on the  
19      Board of Conrail, so I have a lot of  
20      interactions with them and responsibilities  
21      with Conrail). But they do a phenomenal job  
22      for us. But it operates very differently

1       than this switching proposal.

2                       So it is owned by CSX and Norfolk  
3       Southern, together, and for over many years  
4       and many difficult conversations --

5                       VICE CHAIRMAN BEGEMAN: Can a  
6       shipper randomly switch back and forth?

7                       MS. BROWN: The customers in  
8       Conrail are open. But CSX and Norfolk  
9       Southern are not in there switching those  
10      customers for each other.

11                      VICE CHAIRMAN BEGEMAN: I see.

12                      MS. BROWN: We have a residual  
13      Conrail who behaves and acts a bit like a  
14      terminal company. So entire trains go into  
15      Conrail. We work very hard together to  
16      coordinate those movements, and to design the  
17      operating plan, that works for both owners.  
18      But there is a single party in there  
19      performing the service on behalf of both  
20      owners. And it does behave like a direct  
21      line service. So Conrail has no commercial  
22      presence and, while it works well, it's not

1 ideal. So it is still a handoff, it still  
2 behaves a little bit like a third party, on  
3 the move, and we would not design that  
4 service today.

5 VICE CHAIRMAN BEGEMAN: But the  
6 customers, can they randomly switch back and  
7 forth or is it a known event of what's going  
8 to happen - is it a pop-up, to quote what you  
9 said, or is it actually.

10 MS. BROWN: No, it's very --

11 VICE CHAIRMAN BEGEMAN: -- Or is  
12 it much more managed?

13 MR. BAILEY: Yes.

14 MS. BROWN: Much more stable.

15 MR. BAILEY: Yes, each of the  
16 customers in the shared asset areas is  
17 essentially jointly served by Norfolk  
18 Southern and CSX. And then Conrail acts on  
19 our behalf. Once we take the train into  
20 their terminal, they actually are performing  
21 that destination terminal function for us and  
22 then distributing those cars to the customer.



1                   It's very different than what NIT  
2           League is proposing.

3                   VICE CHAIRMAN BEGEMAN:   I  
4           understand that.

5                   MR. BAILEY:   Yes, so the shared  
6           asset is a very highly concentrated, very  
7           dense area, lots of customers.  So we're not  
8           talking about a few customers, you know, a  
9           few cars to a couple of customers.  We're  
10          talking about taking full trains into that  
11          operation, and they're essentially acting as  
12          our --

13                  VICE CHAIRMAN BEGEMAN:   But are  
14          the customers frequently taking advantage of  
15          their ability to switch?  Or has that all  
16          sort of settled down and you each have your  
17          customers?

18                  MR. BAILEY:   I think it's fairly  
19          settled down.  But they do switch.

20                  MS. BROWN:   I think another  
21          difference that's important, like I said, is  
22          we own this property.  So the investment

1 decisions are made collectively. We went  
2 through a significant negotiation between the  
3 two of us of how costs would be allocated,  
4 how we would make capital investment  
5 decisions, how we would have the  
6 infrastructure to support the business for  
7 both owners.

8 So completely, again, a voluntary  
9 arrangement. We purchased Conrail. We both  
10 have an ownership interest in this property  
11 and we work very tightly together to manage  
12 this entity. So it really is not at all  
13 reflective of what the NIT League is  
14 proposing and does not have all the possible  
15 implications, complexities and effects that  
16 the NIT League proposal would have.

17 There is a collective interest,  
18 because we're owners, to invest in Conrail,  
19 right. There's a collective interest to work  
20 together to make sure we have the facilities  
21 to support the business, as a whole. And the  
22 NIT League proposal is very different, and

1       could be in places where we have absolutely  
2       no capability, no capacity, and where there  
3       is significant complexity to the network,  
4       that we don't have any incentive there,  
5       really.

6                   For our customers, our role is to  
7       really reduce that complexity. For our  
8       customers, our role is to streamline our  
9       operating plans, every shipment, so that it  
10      benefits all of the customers that we serve.

11                  So we work every day to take every  
12      bit of complexity out of this network that we  
13      possibly can, not to introduce, and none of  
14      us would introduce the types of movements,  
15      even the most simple one, that Bill Rennicke  
16      outlined yesterday.

17                  VICE CHAIRMAN BEGEMAN: On one of  
18      your charts you showed the complexity of, the  
19      additional three-day time, the 300-miles, et  
20      cetera. Is that an extreme example? I mean,  
21      why would a shipper want that?

22                  MS. BROWN: It's an absolutely

1 realistic example. I suppose if they're  
2 getting a rate reduction there are some  
3 shippers who would opt for that. I think  
4 we've seen, historically, in the rail  
5 industry that with some of the problems that  
6 we had, we had such complexity and such  
7 inefficiency and routes available to  
8 customers that they could choose. We have  
9 all tried to streamline that. To the point  
10 before, where it made sense and where we had  
11 multiple railroads serving the same location,  
12 we entered into some of those voluntary  
13 arrangements to reduce redundancy.

14 MS. RINN: In fact, I think Ms.  
15 Brown is referring to the fact that many of  
16 the reforms in the Staggers Act we've  
17 forgotten because we've done them, and they  
18 happened first. And that was route  
19 simplification and eliminating inefficient  
20 routes.

21 But there were cases that the  
22 Interstate Commerce Commission was having to

1     decide, where, because there were a multitude  
2     of routes, including some extremely  
3     inefficient routes, if you had railroads that  
4     flagged out of a general rate increase in  
5     order to induce the traffic to move that way,  
6     it happened.

7                 Now, most of those routes got  
8     closed without protest. But there was one  
9     case that went to the ICC to decide where  
10    soda ash from Wyoming, moving to New York and  
11    other eastern locations where the most  
12    efficient route was across Iowa and through  
13    Chicago and then east, was being routed via  
14    Ann Arbor, Michigan to move over a railcar  
15    ferry, because you had some smaller railroads  
16    that, this is back in the days where they had  
17    the 30-plus Class I railroads, that you had  
18    smaller railroads that were flagging out of  
19    this because they were getting the traffic  
20    and they were basically using divisions from  
21    other carriers in order to subsidize what was  
22    happening.

1                   But you had customers who were  
2 willing to accept weeks of delay on getting a  
3 shipment because they were getting a lower  
4 rate, even though it created gross  
5 inefficiency in the railroad network. We  
6 have eliminated those sorts of things.

7                   And then the contracts have also  
8 come in. But frankly, contracts took longer  
9 to take off and get really popular. It was  
10 eliminating that type of routing and  
11 irrational, inefficient routing because some  
12 people want to save money. And if the  
13 inefficiency basically is externalized and  
14 imposed on somebody else, they're going to go  
15 for saving the money.

16                  And I can come up with some even  
17 more current examples of what the SP would do  
18 for pricing for cash flow purposes, in terms  
19 of backhaul traffic. So if, when we say that  
20 we're afraid that there will be participants  
21 in the marketplace who will, if they can come  
22 up with a way of basically saving money,

1 choose an inefficient service option, it is  
2 not talking from theory.

3 We know this from historical  
4 experience. And that is why we are afraid.

5 MR. BAILEY: I think you'd be  
6 surprised at how many of those types of  
7 examples exist. I think of it like Atlanta.  
8 I think, in the NIT League comments they tend  
9 to think of these terminals as one entity.

10 But in fact, our operations in  
11 Atlanta are a series of small yards that  
12 make up the terminal because, over the years  
13 with the mergers, we've ended up with pieces  
14 here and there. So you've got several  
15 different yards that constitute the terminal,  
16 and there have to be movements between those  
17 different yards within the terminal area.

18 And you could likely run into a  
19 case where CSX might interchange something to  
20 us that we could, in fact, carry to a  
21 customer relatively easy if it's served out  
22 of that same particular yard. But another

1 customer in the same terminal area, we would,  
2 in fact, have to move that car to Macon and  
3 then back to Atlanta to get it to that  
4 customer.

5 And I think those are the kinds of  
6 things you're going to be faced with, is all  
7 these individual cases based on the  
8 operations of the railroad.

9 VICE CHAIRMAN BEGEMAN: That's  
10 actually another question I wanted to ask Ms.  
11 Brown. You talked about the hub yards versus  
12 all the other interchanges that can work. If  
13 this proposal, and I know you're here to say  
14 this doesn't work, we have that message, but  
15 if we were to continue to have a dialogue on  
16 this to try to make something work would it  
17 be more operationally workable if this was  
18 focused more on locations within hub systems  
19 rather than a random interchange?

20 Yesterday, one of the maps showed  
21 clearly on the eastern part of the country  
22 that there are a whole lot more areas where



1       there are interchanges -- where the red  
2       circles were - more than there were on the  
3       other half of the country. But is there a  
4       way to balance that?

5                   MS. BROWN: I mean, I would say we  
6       have a couple of concerns. One is, and very  
7       respectfully, we have had a history with this  
8       and we are very concerned about the proposal.  
9       And even segmenting where these things could  
10      occur, we have entered into joint  
11      arrangements where it makes sense.

12                   We often do exercises with the  
13      help of consultants and very talented people  
14      who look at the flows across our networks  
15      collectively and where we can make the most  
16      efficient routing.

17                   Our overall concern here is where  
18      those opportunities exist we try and leverage  
19      those. And we do those voluntarily today.  
20      Our concern with this proposal is you would  
21      have others making those decisions for the  
22      industry, and it's a very complex network.

1 It's a very difficult modeling problem to  
2 solve, right.

3 And we all spend inordinate  
4 amounts of time, either individually within  
5 our own networks or for opportunities of  
6 shipments that are handled between us, to  
7 make that the most efficient possible. And  
8 any introduction of new complexity, by  
9 definition, requires more workload, more  
10 time, more handling, more congestion.

11 You're doing things that are  
12 unnatural. And it would not be the people  
13 who sit down and try and optimize these  
14 networks making those decisions. It would be  
15 somebody else forcing those decisions on us.  
16 And it has, absolutely has, cascading ripple  
17 effects.

18 You take isolated incidents. You  
19 know, Chicago is a great example. It just  
20 cascades and those effects start spreading  
21 across our networks because it is an  
22 integrated network. And any issue anywhere

1 on the network can impact the whole and  
2 impact all the customers.

3 And we like to call it, it's like  
4 the perfect or perpetual storm where you  
5 constantly have things that we're trying to  
6 do that are completely unnatural that don't  
7 fit within our service plans. That could  
8 happen every day. We don't have the  
9 resources, we don't have the infrastructure.

10 It takes a long -- Tom had a great  
11 slide on the lead time. We spend a lot of  
12 time preparing for new business development.  
13 We don't have, don't typically, have pop-up  
14 traffic. We spend a lot of time preparing  
15 for business shifts. It takes a lot of time  
16 to make sure you have the adequate  
17 infrastructure and resources to handle that.

18 MR. HALEY: Just to follow up and  
19 to add to that, my map was up there just for  
20 a short time about a future projection on our  
21 network. But the red dots which are  
22 terminals that are over-committed in the

1 future based on the capacity today, on Union  
2 Pacific, are both local yards and hubs.  
3 There are both of those there.

4 And one of the ways that we try to  
5 balance is to shift work between the two. So  
6 I don't think a hub only or a local yard only  
7 approach solves the problem at all.

8 And the second thing, if I may  
9 just follow up, Cressie made a great point  
10 about how we all work to take events out,  
11 switching events out, to make the service  
12 more streamlined and more efficient. And I  
13 think that's the great frustration because  
14 this is such a big step in the opposite  
15 direction.

16 Part of how we're going to grow in  
17 the future is by taking steps out, to live  
18 within our infrastructure and to move more  
19 freight. And why on earth would we spend our  
20 scarce capacity re-switching, re-handling  
21 traffic that we already move? It just  
22 doesn't make good sense.

1 MS. BROWN: If I could add one  
2 more point on that from a customer  
3 perspective. We went through the slide that  
4 showed how much time we spend with customers  
5 trying to listen to what's important to them.  
6 And they have indicated to us that they love  
7 the value proposition of rail.

8 But what is going to be required  
9 for them to give us more of their business is  
10 service reliability and that that is  
11 paramount to them. So we work very hard to  
12 take these complexities out. We have every  
13 incentive to make our service product more  
14 streamlined, provide faster transit and  
15 better service to our customers. That's  
16 really what we're focused on.

17 And this goes in absolutely the  
18 opposite direction by adding complexity. By  
19 definition, it adds complexity. It adds  
20 time. And it degrades our service  
21 reliability, and that's our primary concern.

22 VICE CHAIRMAN BEGEMAN: May I keep

1       going?

2                       CHAIRMAN ELLIOTT:   Keep going.

3                       VICE CHAIRMAN BEGEMAN:   All right,  
4       so back to market power.   We have conflicting  
5       policies.   I think no one would disagree with  
6       that, but the Board may require rail carriers  
7       to enter into reciprocal switching where it  
8       finds such agreements to be practicable and  
9       in the public interest, or where such  
10      agreements are necessary to provide  
11      competitive rail service.

12                      Not to put words into your mouth,  
13      but it seems that the comment earlier was NIT  
14      League's proposal is "artificial" market  
15      forces.   So what is not artificial that the  
16      Board could do to promote competitive rail  
17      service options that doesn't turn us back to  
18      1979?

19                      Yesterday I asked the second panel  
20      because there is a disagreement, a legitimate  
21      disagreement, on what the impact of how much  
22      traffic would move.   You know, the crystal

1 balls are not real clear on either side. Is  
2 there some level of competitive switching  
3 that the rail industry could live with?

4 If you just look at the Board's  
5 record we know that there are various  
6 railroads that are working to assist  
7 shippers, to sort of do what some people are  
8 wanting to do, more broadly. They're -- I'll  
9 just leave it at that, so I --

10 MS. RINN: I understand where  
11 you're coming from. In our world we,  
12 likewise, have to balance competing, not  
13 always congruent, interests. But I'll make  
14 one observation. Successful regulation isn't  
15 necessarily measured only by the number of  
16 disputes that are officially resolved by an  
17 administrative agency in favor of one side or  
18 the other.

19 In fact, you have, the more  
20 successful your governance or regulatory  
21 scheme, the fewer disputes you have because  
22 the parties understand what the rules are and

1     either they're going to comply because it's  
2     already aligned with their economic self  
3     interest, or they're in a compliance mode.

4             And if you know what the rules are  
5     and you know how you're going to comply with  
6     it, then you're going to avoid creating  
7     unnecessary or avoidable disputes. And, in  
8     fact, that's why the vast majority of your  
9     rate cases end up getting settled and even  
10    more rate disagreements between customers and  
11    railroads get resolved before even getting to  
12    the Board.

13            I would submit that there's  
14    already a great deal of competition between  
15    the railroads. And we're doing it in other  
16    effective ways. One way is we like taking  
17    market share from BNSF using transloads. We  
18    do that with a lot of traffic. Now that may  
19    not work for everything.

20            But the other thing we have done,  
21    and in fact we went from a zero percent  
22    market share to more than 50 percent market



1 share on the Powder River Basin is that we  
2 had a marketing strategy that we were going  
3 to make our customers the low-cost generators  
4 in their territory. So they were burning  
5 coal that used to be delivered to a power  
6 plant that might have been local to the BNSF,  
7 but we had the low-cost producer.

8                   So there are all sorts of ways of  
9 competition that we're engaged in because  
10 it's in our economic self interest. And  
11 there are other forms where maybe the  
12 marketing department doesn't want to do it  
13 that way, but when we say well, here are the  
14 results in the regulatory scheme, and you  
15 don't want to go there, so I'm suggesting  
16 that, to a certain extent, the current  
17 standard basically says you need to prove  
18 that there's a competitive abuse. We  
19 recommend against competitive abuses because  
20 we don't want to end up here before the STB.  
21 So I'm saying that there are ways of getting  
22 success that don't necessarily show up on

1     your radar screen, and it is a successful  
2     regulatory scheme.

3                   MS. MULLIGAN:  And I think that's  
4     exactly right.  I would just add to Lou  
5     Anne's comments as well that you have, well,  
6     she was focusing on the competitive access  
7     remedies and remedies that are focused on  
8     instances of competitive harm, commercial  
9     abuse, market power abuse.

10                   There's also the rate  
11     reasonableness standards as well that step in  
12     when market power has resulted in an  
13     unreasonable rate.  And there's a lot of  
14     active disputes at the Board about that.  But  
15     then that's also something that we have, that  
16     we take into consideration when we're having  
17     negotiations with customers.

18                   Just because it doesn't rise to  
19     the level of being an active proceeding  
20     before the Board doesn't mean that these  
21     rules have real impacts in how shippers and  
22     railroads engage with each other.

1                   VICE CHAIRMAN BEGEMAN: You don't  
2                   have to talk if you don't want to.

3                   MS. BROWN: Sorry. I would just  
4                   add, from a pure operational perspective, our  
5                   concern is that you will make transportation  
6                   less competitive for all of our customers,  
7                   right. That's part of their cost of doing  
8                   business. And by implementing this proposal  
9                   in particular, does nothing to improve the  
10                  efficiency of freight transportation in the  
11                  U.S.

12                  VICE CHAIRMAN BEGEMAN: I will now  
13                  trade off with you.

14                  CHAIRMAN ELLIOTT: Do you have  
15                  more?

16                  VICE CHAIRMAN BEGEMAN: I might  
17                  later.

18                  CHAIRMAN ELLIOTT: Okay. And just  
19                  two more questions. The first question, I  
20                  guess, is more for the lawyers. And some of  
21                  the railroads, in their comments, raised the  
22                  issue that we don't really have the authority

1 to do what NIT League is proposing today.

2 And as a result of past  
3 regulations that we have put in place  
4 regarding competitive access and as a result  
5 of the 1996 Interstate Commerce Commission  
6 Termination Act those policies were  
7 essentially ratified, can the panel speak to  
8 that? Do we actually, or is it the  
9 railroads' belief that we do not have the  
10 power to put in place what is suggested by  
11 NIT League?

12 MS. MULLIGAN: I think that,  
13 speaking for BNSF, we've taken the position  
14 that, regardless of the authority of the  
15 Board, the STB's, sorry, the NIT League  
16 proposal is not an appropriate step under the  
17 Rail Transportation Policy.

18 I think it's inconsistent with the  
19 direction that has clearly been given by  
20 Congress there, in terms of focusing  
21 regulation on instances where there's  
22 actually an activity that needs to be

1       governed and otherwise allowing market forces  
2       to operate.

3                   MS. RINN: We didn't repeat but we  
4       agree with the legal analysis in the AAR. I  
5       would say we certainly do not question that  
6       the Board has statutory authority, in a  
7       particular instance, to impose reciprocal  
8       switching.

9                   The key difference we have with  
10      what the NIT League is proposing is they're  
11      basically saying we're going to come up with  
12      these conclusive presumptions for a large  
13      number of stations and a large number of  
14      carloads where you get a pass in basically  
15      the high passenger lane when statute written  
16      by Congress envisioned doing this on a case-  
17      by-case basis.

18                  And we think that there is a  
19      fundamental disconnect there which is, in  
20      fact, contrary to the law and the  
21      congressional policies that are out there as  
22      well as your prior decisions.

1                   CHAIRMAN ELLIOTT:  And, following  
2                   up on that, would it be your position that  
3                   the way this works, and I think the term  
4                   winners and losers, us choosing winners and  
5                   losers, was used by the railroads, would you  
6                   consider that to be an arbitrary use of our  
7                   powers?  Is that more or less what you were  
8                   getting at?

9                   MS. MULLIGAN:  I think it would  
10                  certainly be a troubling use of your powers.  
11                  I think that, the question came up  
12                  previously, aren't there winners and losers  
13                  already?  I think if, by that, people are  
14                  talking about the fact that, yes, there are  
15                  carriers, there are, sorry, shippers who have  
16                  access to two carriers and access to one  
17                  carrier.

18                  That has been the result of where  
19                  they've located.  This would be something  
20                  that's very different, I think, than what the  
21                  Board has previously done which is creating a  
22                  new category of winners and losers by virtue

1 of implementing a remedy that really doesn't  
2 have reference to any actual individualized  
3 or issues, competitive service otherwise that  
4 a shipper is experiencing.

5 And I think the panels yesterday  
6 identified there are some real impacts to  
7 that in terms of shippers.

8 MS. RINN: I would like to  
9 actually go back to some of the points that  
10 Jill made during her presentation. The 240  
11 percent as a, you've got market power and if  
12 it's under 240 you may not have market power.  
13 And that, as a threshold, that's absolutely  
14 arbitrary.

15 I've not seen any evidence in this  
16 record that basically says, based on a  
17 revenue to variable cost ration which, by the  
18 way, can change based on system-wide costs,  
19 tells you anything about the particular  
20 market circumstances of that individual  
21 customer. To my mind, it's a very clear  
22 example of something that is arbitrary.

1                   CHAIRMAN ELLIOTT: Okay, putting  
2     aside what I just asked about whether or not  
3     the 240's arbitrary or if the mechanism  
4     itself is arbitrary, yesterday I mentioned,  
5     with respect to service, I know that's a  
6     serious concern of yours and for good reason.

7                   What if, and I mentioned this  
8     yesterday, if we put in place some type of  
9     safe harbor for the railroads so if the  
10    incumbent has a rate above 240 and someone  
11    brings a case of this nature seeking access  
12    that the railroad could lower their rate, I  
13    assume by tariff, and put it below 240.

14                  And as a result they're  
15    automatically in a safe harbor and not  
16    covered. Would that eliminate our service  
17    concerns that the Panel has presented today?

18                  MS. RINN: No.

19                  MS. MULLIGAN: Yes, I was going to  
20    say the same thing. I think one of the  
21    issues that's been highlighted with this  
22    panel is that it's not so much the volume of



1 switching. It's where it actually occurs.

2 And so while that proposal might  
3 limit the place, the number of places where  
4 switching would occur, you could still have  
5 switching taking place in some pretty  
6 critical places on the network that would  
7 have potential service impacts.

8 But I also think, too, the issue  
9 with the safe harbor is that it doesn't  
10 really fix the sort of arbitrary nature of  
11 the starting point of the proposal which is  
12 the 240. You've maybe put a couple  
13 protections against that being widespread in  
14 terms of the safe harbor.

15 But you still have the issue that  
16 you are putting in place a regulatory remedy  
17 where it's really not connected to showing  
18 that there's some sort of issue that needs to  
19 be addressed.

20 MS. RINN: And if I could offer,  
21 like two practical examples of why 240 would  
22 be arbitrary and not make a lot of sense.

1 One example would be do you really want to  
2 have a rule like that that basically says you  
3 could be forced to a reciprocal switching  
4 opening on TIH.

5 The fact is that URCS, as you're  
6 applying it and for purposes of the market  
7 dominance test I understand why you're doing  
8 it, you do an unadjusted URCS. But it does  
9 not reflect the extra handling that is  
10 associated with TIH or other hazardous  
11 materials. And it certainly does not weigh  
12 the risk that we face in handling TIH.

13 Those commodities have  
14 historically carried a higher margin because  
15 of the costs, because of the risks that are  
16 associated with handling it. And so it  
17 doesn't make a lot of sense to use a system  
18 average costing system to set that kind of a  
19 basically informal rate cap. It's basically  
20 a backdoor way of doing rate regulation.

21 Another example would be when  
22 you're making a lot of investments that are

1 going to benefit a particular community of  
2 shippers, so, for example, taking our  
3 southern region where a lot of those capacity  
4 constrained terminals are, that is where we  
5 have a lot of inbound traffic that is  
6 associated with the fracking boom.

7           So to create the natural gas and  
8 to create the crude oil at a low cost that  
9 then the chemical industry is using to create  
10 more domestic production, we're making  
11 massive investments. And we need to get a  
12 margin on the traffic that's going to be able  
13 to pay for those investments.

14           While I submit to you that they  
15 may not like necessarily seeing it, nobody  
16 likes to see the price they're paying for  
17 something going up, but those are customers  
18 who should be paying margins that are going  
19 to allow us to make this investment in order  
20 to meet their transportation needs now and  
21 into the future.

22           And that's what I've got, is a

1 concern with having an R/VC ration that  
2 you're talking about applying across  
3 commodities and across our system.

4 MS. MULLIGAN: And I would just  
5 also add, too, this goes back to my  
6 testimony, but when you do incorporate the  
7 R/VC at the system level you do have this  
8 issue where you are essentially creating a  
9 incentive.

10 Whether it's to stay below the 239  
11 that you're talking about, you remove the  
12 incentive for carriers to make efficiency  
13 investments because, as a result of making an  
14 investment that reduces your variable cost,  
15 you could actually tip back up over that  
16 level. And you haven't changed your rate,  
17 it's just because you've made an investment  
18 that does reduce your costs.

19 VICE CHAIRMAN BEGEMAN: May I ask  
20 a question? I'm having trouble, it seems  
21 like you're all looking at it from the  
22 perspective of not wanting to lose your

1 current shipper, perhaps, or your current  
2 revenue.

3 But why not look at it as a way to  
4 get more revenue from more shippers, the  
5 people that switch to you? How is that not a  
6 potential benefit, long term?

7 MR. HALEY: I can't get past the  
8 issues that I talked about, which is more  
9 work and less efficiency in a capacity  
10 constrained environment.

11 And it seems to me, and I truly am  
12 not one to speak to all the ins and outs of  
13 revenue and the legal issues, but it seems to  
14 me something that has a net effect of being  
15 less efficient at a higher cost, and at that  
16 same time reducing revenue, just can't be a  
17 win/win.

18 VICE CHAIRMAN BEGEMAN: But in the  
19 rest of system, where there's competitive  
20 service you figured out how to make that work  
21 successfully, at least looking at your  
22 spreadsheets and what I read.

1                   MR. HALEY:   So I think --

2                   VICE CHAIRMAN BEGEMAN:

3                   Collectively, I should say.

4                   MR. HALEY:   Yes, so I think the  
5                   issue here is though, again, we're doing  
6                   something that's less efficient.  I mean, it  
7                   just doesn't make good sense.

8                   MS. BROWN:   I mean, I would offer  
9                   to that as well.  I mean, this proposal would  
10                  absolutely add cost to the rail industry as a  
11                  whole.  It absolutely would make us less  
12                  efficient because we are adding workload to  
13                  the system for the same amount of cars.

14                  So you can't add significant  
15                  amount of work and not add the cost of  
16                  handling those cars -- the time, the  
17                  complexity, the congestion.  And our  
18                  customers are very clear to us that what is  
19                  going to enable us to grow our business is  
20                  better transit, better service, better  
21                  reliability.

22                  And until we get there they can't,

1       they are tightly managing inventories in  
2       their own systems, right. So they need to be  
3       able to depend on if a shipment is scheduled  
4       to be there Wednesday they're production  
5       schedule requires us to show up on Wednesday.

6               And every time that you add  
7       complexity in the system our opportunity to  
8       be there on Wednesday is diminished. And we  
9       don't see a scenario where we can effectively  
10      grow our business when we are degrading our  
11      service product.

12             And most of the markets and  
13      sectors of our business that are growing,  
14      going forward, are very service sensitive  
15      markets that are requiring very high levels  
16      of predictability, reliability, on-time  
17      performance in transit. It's a network. You  
18      can't impact pockets of the system without  
19      affecting the system.

20             MS. RINN: Again, just to be  
21      concrete about it, we are already growing our  
22      business. We're going after folks who have

1       traditionally used trucks and barges. And so  
2       we're going after that business.

3               We go after folks who may be  
4       located on a different railroad by transload.  
5       And we have built in or we have provided  
6       inducements to customers to build-in to us or  
7       to expand their capacities on our railroad  
8       lines as opposed to expanding their capacity  
9       at a plant on another railroad line.

10              So we are interested in growing  
11      our business and we are, in fact, doing it.  
12      But we do it with our money or money that  
13      basically is paying for that competition  
14      where we're sure that we can provide a  
15      competitive transportation service.

16              The model of trying to do it in a  
17      way that is inefficient and where, if you  
18      come up with the wrong pricing scheme, can  
19      have us subsidizing our competition and while  
20      making us less competitive is not a way, to  
21      us, to basically advance competition. It is  
22      basically taking a step back on competition



1 on several fronts.

2 CHAIRMAN ELLIOTT: Thank you very  
3 much for your testimony today. We greatly  
4 appreciate you coming out here today and  
5 helping us with this important matter. And  
6 we will bring up the next panel.

7 (Off microphone comments)

8 CHAIRMAN ELLIOTT: Okay, why don't  
9 we start with our Panel Number VI, and I  
10 believe we'll hear from the American  
11 Chemistry Council first.

12 MR. MORENO: Good morning. I'm  
13 appearing today on behalf of the American  
14 Chemistry Council because this proceeding is  
15 tremendously important to the chemical  
16 industry. Three decades of consolidation of  
17 the rail industry has produced rail duopolies  
18 in the eastern and the western United States.

19 And perhaps more importantly it  
20 has extended the distance over which many  
21 chemical production facilities are captive to  
22 a single railroad. As a result of this

1       increased captivity the rail industry has  
2       been able to impose significant rate  
3       increases over just a very short period of  
4       time.

5                       These rate increases reduce the  
6       ability of U.S. chemical producers to  
7       increase economic output and to create new  
8       jobs. The NIT League's competitive switching  
9       proposal has the potential to restore some of  
10      the rail competition that has been lost  
11      through past mergers.

12                     This, in turn, would establish a  
13      fair and reasonable balance between the often  
14      conflicting goals of revenue adequacy and  
15      effective competition in the Staggers Act.  
16      First slide, please.

17                     Since the Conrail acquisition,  
18      which was the last major merger that  
19      completed the current eastern and western  
20      duopolies, rail rates have increased at an  
21      unprecedented pace. You saw this slide  
22      yesterday with the NIT League presentation.

1                   And I think it's significant to  
2                   understand, in looking at this slide, the  
3                   Conrail acquisition was basically completed  
4                   in 2000. But there were a few years of  
5                   basically digesting service disruptions, et  
6                   cetera. And also there were several years of  
7                   Board oversight.

8                   As Legacy contracts began to  
9                   expire you start to see the rail rates  
10                  deviate from the pace of trucking increases  
11                  and the pace of inflation, which is strongly  
12                  suggesting that the railroads are exercising  
13                  significant newfound leverage over captive  
14                  shippers as a result of their extended  
15                  bottlenecks from theses mergers.

16                  A recent study commissioned by the  
17                  ACC which was included in our opening  
18                  comments estimated that the chemical industry  
19                  paid \$3.9 billion in charges above the 180  
20                  percent R/VC jurisdictional threshold in  
21                  2010. Recently ACC released an updated  
22                  version of this study for 2011 which showed

1       that that premium had increased to \$4.5  
2       billion.

3                   The jurisdictional threshold is a  
4       significant benchmark for this analysis  
5       because it shows how much and how fast rates  
6       have increased in the years following the  
7       Conrail merger. In just five years, between  
8       2005 and 2010, the amount or the rate paid  
9       above the 180 percent threshold increased  
10      from \$2.2 billion to \$3.9 billion, a 78  
11      percent increase.

12                  If you benchmark that against the  
13      \$4.5 billion in ACC's updated analysis for  
14      2011 that figure jumps to 145 percent over  
15      just six years. The analysis also shows that  
16      more than one-third of chemical shippers have  
17      rates that are above the 300 percent R/VC  
18      ratio.

19                  This high fraction of rates above  
20      300 percent confirms the trends that were  
21      identified in the GAO and the Christensen  
22      Associates reports that have continued and

1       likely have become more pronounced, at least  
2       for the chemical industry.

3               This increase cannot be attributed  
4       to higher demand because overall carload  
5       volume over 2011 was virtually unchanged from  
6       2005 levels. Yet we can see, for all traffic  
7       on the system, the rail premium above the 180  
8       percent had increased by over 90 percent.

9               Comparisons to Canada illustrate  
10       the consequences of reduced rail competition  
11       for the competitiveness of U.S. chemical  
12       producers. Canada has long had  
13       interswitching. And interswitching is a far  
14       more liberal form of competitive switching  
15       than what the NIT League has proposed.

16              Within this study that was  
17       commissioned by ACC it compared 2010 rail  
18       rates to U.S. destinations from Canada  
19       origins and from U.S. origins and found that  
20       40 percent of the Canadian origin chemical  
21       traffic had R/VC ratios below 180 percent,  
22       whereas only 23 percent of the U.S. origin

1 chemical traffic had R/VCs below 180 percent.

2 The competition that  
3 interswitching creates at Canadian origins  
4 clearly gives Canadian chemical production  
5 facilities an advantage over U.S. locations.  
6 And competitive switching would do much to  
7 level that playing field for domestic  
8 chemical producers.

9 Restoring competitive balance to  
10 the rail industry would reduce the rate  
11 premium paid by chemical shippers and would  
12 allow the U.S. chemical industry to increase  
13 economic output and create more jobs.

14 The NIT League proposal would  
15 restore lost competition from 30 years of  
16 rail consolidation by breaking some of the  
17 bottlenecks, just some of the bottlenecks,  
18 that have grown increasingly longer with each  
19 merger.

20 As a general rule the ICC  
21 Termination Act permits the rail carrier, the  
22 origin rail carrier, its long haul. That

1 long haul, however, has increased for most  
2 shippers after many years of end-to-end rail  
3 mergers.

4 As a result, facilities where the  
5 origin carrier's long haul may have been over  
6 relatively short distance now find themselves  
7 captive to an origin carrier's long haul that  
8 extends several hundred miles or, in some  
9 cases, even the full distance of the entire  
10 route.

11 This extended long haul created by  
12 mergers precludes shippers from using  
13 competitors that may be available for the  
14 majority of the distance. This is a very  
15 simple and basic illustration of that  
16 example. We have a pre-merger and a post-  
17 merger scenario.

18 Pre-merger, the origin was still  
19 captive to a single railroad, but that  
20 railroad had a fairly short distance to  
21 travel before it had been handed off to  
22 Railroad 2 or Railroad 3 for delivery to the

1 destination. So there was competition  
2 between Railroads 2 and 3.

3 Post-merger between Railroad 1 and  
4 Railroad 2, Railroad 1 now has a long haul  
5 all the way to the destination that  
6 completely precludes the participation of  
7 Railroad 3 in any of its transportation  
8 options.

9 The NIT League proposal, if the  
10 intersection and the interchange between the  
11 new merged railroad and Railroad 3 would  
12 occur within this 30-mile radius, it would  
13 reverse that effect and, therefore, restore  
14 that level of competition.

15 I would like to address a few of  
16 the comments that we heard about service  
17 issues and, particularly, some of the stuff  
18 we've heard this morning. It's easy for the  
19 rail industry to cherry-pick and create  
20 doomsday scenarios for this. They have no  
21 incentive to acknowledge or even identify  
22 those scenarios within their systems where



1        efficiencies might be improved.

2                        But I think, and they've also left  
3        off the question of at what levels do these  
4        doomsday scenarios kick in. And maybe  
5        because that question is a bit of a red  
6        herring. As I heard one of the panelists  
7        just immediately before me say, it's not the  
8        volume of switching, it's where the switching  
9        occurs.

10                      Well, what I haven't heard any  
11        railroad participant say today is they  
12        haven't addressed why NIT League's \*\*\*  
13        11:11:36 fore-factored dealing with service  
14        concerns wouldn't protect against those  
15        scenarios. Where those doomsday scenarios  
16        are likely to occur, that would be a defense  
17        against reciprocal switching under the NIT  
18        League scenario.

19                      In this proceeding the rail  
20        industry had described the NIT League  
21        proposals as a wealth transfer that is  
22        motivated solely by rate reductions. Well,

1     there can be no denying that rapidly rising  
2     rail rates have been an important factor in  
3     developing this competitive switching.

4                 But the attainment of reasonable  
5     rate levels is a central objective of  
6     competition. So to the extent that the  
7     railroads have been exercising undue market  
8     power to charge excessive rates, competitive  
9     switching has the potential to introduce  
10    competition to keep that power in check.

11                In other words, what the railroads  
12    are calling a wealth transfer is simply  
13    competition at work. Furthermore, ACC  
14    support for competitive switching is driven  
15    by far more than just rates. Providing  
16    access to nearby rail alternatives promotes  
17    use of the most efficient carriers and routes  
18    for each movement and permits manufacturers  
19    to design more flexible supply chains.

20                These are options that are often  
21    foreclosed today by the examples that are on  
22    the screen where monopoly carrier origin

1 carriers are seeking to preserve their long  
2 haul. In contrast, if the incumbent  
3 carrier's route is more efficient, based on  
4 both price and service, a shipper will  
5 continue to use it even after the  
6 implementation of the competitive switching.

7 Competitive switching also is not  
8 the death nail for differential pricing. NIT  
9 League has demonstrated that the universal  
10 traffic potentially eligible for competitive  
11 switching is limited and revenue

12 Furthermore, today's industry does  
13 not need to engage in the magnitude of  
14 differential pricing that may have been  
15 required in the past. The industry is more  
16 than financially sound and is thriving by  
17 setting records for operating ratios, income  
18 earnings per share and railroad stock prices  
19 have outpaced the broader market for many  
20 years.

21 Much of the money from the current  
22 level of differential pricing is being

1 returned to shareholders through higher  
2 dividends and stock buy-backs. Ironically,  
3 this is a wealth transfer from captive  
4 shippers to railroads that has been  
5 facilitated by a lack of rail competition.

6 Competitive switching is not a  
7 panacea, however. For every captive shipper  
8 and every captive movement that would be a  
9 substantial improvement over the status quo,  
10 I'll wrap up quickly here, AC members still  
11 harbor substantial concerns that even with  
12 competitive switching railroads will not  
13 compete.

14 And the Board's public hearing at  
15 Ex Parte 705 revealed broad shipper support  
16 for greater rail to rail competition.  
17 However, a number of shippers in that  
18 proceeding expressed deep concern about  
19 railroads willingness to compete.

20 The Board need not focus on just  
21 one issue. It can focus on both regulatory  
22 remedies and enhancement of competition. But

1 the Board needs to be cognizant of the fact  
2 that two railroads will not always compete.  
3 And they must be prepared to address those  
4 situations through other regulatory remedies  
5 even when competitive switching might  
6 otherwise be available.

7 Therefore, in conclusion, ACC  
8 strongly supports competitive switching and  
9 urges the Board to proceed promptly to a  
10 notice of proposed rulemaking based upon the  
11 NIT League's proposal. No further purpose  
12 would be served by requiring additional steps  
13 before offering specific rules for public  
14 comment other than to further delay this very  
15 important proceeding for the shipping  
16 community. Thank you.

17 MR. JOHNSTON: Good morning,  
18 Chairman Elliott, Vice Chairman Begeman. My  
19 name is Eddie Johnston. I've worked for the  
20 Dupont Company for 33 years.

21 I'm here today representing  
22 Dupont, a leading science company, and the

1 Chlorine Institute where I serve as Chair of  
2 the Board Committee on Rail Issues. I  
3 appreciate the opportunity to address you  
4 this morning.

5 I'm pleased that the Board is open  
6 to considering proposals that would improve  
7 rail competition. Today our nation's  
8 railroads are healthy, profitable and  
9 actively reinvesting. Their improved  
10 profitability results from improved  
11 productivity on one hand and virtually  
12 unrivaled pricing power on the other.

13 During the recent economic  
14 recession rail rates escalated three times  
15 the rate of inflation. Railroading is once  
16 again a great business. America's farmers  
17 and manufacturers like Dupont, who pay these  
18 increasing prices, are too often faced with  
19 no choice for rail service.

20 Rail-to-rail competition has  
21 disappeared for most of us. Dramatic  
22 consolidation, the emergence of dominant

1 regional carriers has left three-quarters of  
2 all ship points captive to a single railroad.  
3 Captive shippers enjoy neither competition  
4 nor the dynamics of free market forces for  
5 transportation.

6 At the same time rail is the  
7 safest or only practical mode of  
8 transportation for many shippers. These  
9 shippers and their customers need greater  
10 competition. Competitive switching in this  
11 proceeding aims at increasing competitive  
12 access over existing infrastructure. It is a  
13 step in the right direction.

14 As the Board considers this  
15 proposal I urge you to recognize that  
16 competitive switching rules stop short of  
17 actually creating competition. They make  
18 competition possible. Unless the invitation  
19 to compete is met with a willingness to  
20 compete shippers will not benefit by rates  
21 that are set by market forces. And so the  
22 Board must not interpret competitive

1 switching rules as creating competition per  
2 se.

3 The three important implications  
4 that flow from recognizing the distinction  
5 between competitive switching rules and  
6 actual competition -- first, the Board cannot  
7 rely on competitive switching rules to  
8 discipline railroad pricing or limit  
9 oversight to the first or last 30 miles  
10 without evidence that pricing from origin to  
11 destination is indeed being set by  
12 competitive market forces.

13 This is particularly true for  
14 products like ammonia and chlorine that  
15 railroads have publicly stated they would not  
16 carry if they were not required to do so by  
17 law. Second, the Board should make clear  
18 that the mere existence of competitive  
19 switching rules does not disprove market  
20 dominance in a rate case.

21 If railroads able to compete  
22 choose not to compete under competitive



1 switching rules, just as they are doing  
2 today, shippers are exposed to market  
3 dominance and its attendant rates. The  
4 opportunity to bring a rate case challenging  
5 unfair rates must be preserved with or  
6 without revised competitive switching rules.

7 Finally, I urge the Board to  
8 require all railroads falling under the  
9 conditions of these rules, both the incumbent  
10 railroad and all competing railroads, to  
11 provide tariff rates when shippers are faced  
12 with no acceptable contract offers.

13 Although this provision may not  
14 stimulate competition, shippers would retain  
15 the remedy of bringing a rate case before the  
16 Board. You've heard extensive testimony on  
17 rail competition through Ex Parte 705, 714,  
18 715 and now this proceeding.

19 I encourage you to examine that  
20 whole record for opportunities that create  
21 greater rail-to-rail competition. In  
22 conclusion, I urge the Board to proceed to

1 rulemaking on competitive switching with the  
2 following recommendations.

3 Recognizing that competitive  
4 switching cannot be interpreted as creating  
5 competition per se, the Board should not  
6 lessen its oversight over end-to-end rail  
7 rates. The Board should unambiguously  
8 disallow the use of competitive switching  
9 rules alone as a defense against market  
10 dominance in a rate case.

11 And the Board should require  
12 railroads subject to competitive switching  
13 rules to provide tariff rates when a shipper  
14 is not able to obtain a reasonable contract  
15 offer. These measures will help preserve the  
16 rights of shippers to challenge unreasonable  
17 rail rates while creating additional  
18 competition for some.

19 Thank you again for the  
20 opportunity to appear today.

21 MS. DEARDEN: Good morning. I'm  
22 here on behalf of Diversified CPC

1 International because rail-to-rail  
2 competition is very important to small and  
3 mid-sized customers like Diversified.

4 Highroad Consulting filed opening  
5 comments in this proceeding with supporting  
6 analysis in a report prepared by our  
7 consultant, Neil Thurston, assessing Canada's  
8 regulated interswitching impact on our  
9 operations and service to customers. And  
10 that has been referenced by numerous parties  
11 in the reply comments.

12 Diversified support the NIT League  
13 competitive switching proposal, CSP, with  
14 some modifications. Diversified and other  
15 shipper representatives have produced  
16 adequate evidence to justify opening of the  
17 rulemaking proceeding.

18 Rationalization of the rail  
19 network from 26 Class I railroads to 7 had a  
20 dramatic impact on competition. Further, in  
21 the Board's decision dated July 25, 2012 you  
22 commented that the NIT League proposal has

1 the potential to establish discipline and to  
2 reduce the number of regulatory proceedings.

3 This would benefit all parties  
4 including the agency, the shippers and the  
5 railroads who are currently required to  
6 commit time and resources to those  
7 proceedings. The railroads contend forced  
8 switching will shift traffic flows and put  
9 capital investments in infrastructure at  
10 risk.

11 We submit the railroads will have  
12 no choice but to continue to invest in their  
13 systems simply to keep up with the dramatic  
14 growth forecasted by the United States  
15 Department of Transportation. Diversified is  
16 a relatively small shipper. Yet they have  
17 invested more than \$2.2 million for  
18 infrastructure improvements required to  
19 maintain and increase rail shipments.

20 The railroads seem to have a one-  
21 sided view of the need to earn return on  
22 investments. In 2004 one of Diversified's

1 customers asked them to develop a new product  
2 for the customer's foam packaging operations.  
3 Diversified developed the new product which  
4 was accepted by the customer.

5           Diversified acquired additional  
6 tank cars and they invested more than  
7 \$500,000 for the construction of a storage  
8 tank farm, blending system, associated pumps  
9 and piping for the new commodity. During the  
10 three-year period when we had the business  
11 the rail rate for this move increased more  
12 than 41 percent.

13           The railroads disregarded our  
14 warnings and ultimately priced Diversified  
15 out of the business. It is extremely unfair  
16 for railroads to encourage customers to  
17 develop business that will require capital  
18 investments and to subsequently chase the  
19 business away with irresponsible pricing  
20 practices.

21           This is only one example of  
22 inadequate competition in the railroad

1 industry. One hundred percent of  
2 Diversified's rail links have bottlenecks at  
3 origin and/or destination. For this  
4 particular lane both origin and destination  
5 are classic bottlenecks.

6 While we have not developed a plan  
7 to request competitive access we believe it  
8 is possible that simply having an option to  
9 open industries to reciprocal switching will  
10 create a competitive environment that will  
11 serve the public interests.

12 My railroad career started in  
13 1969. As a railroad marketing officer, I had  
14 the privilege to learn while working in a  
15 regulated industry and to subsequently  
16 compete aggressively in a deregulated  
17 environment.

18 We competed in a number of ways,  
19 developing marketing and pricing strategies  
20 and we implemented strategies to improve the  
21 efficiency of the railroad's locomotive and  
22 railcar fleets. And there's no question that

1 competition was a motivator to drive  
2 efficiency into the railroad's networks.

3 Based on my experience, I submit  
4 that one of the many benefits of CSP will be  
5 the continuing development of productivity  
6 initiatives that will result in more  
7 efficient operations and quality service.  
8 The railroad party's allegations that service  
9 will decline and costs will increase if CSP  
10 is approved is without foundation.

11 First of all, a single line route  
12 is not always the most efficient route. If  
13 time permitted I could relate a number of  
14 instances where more direct routes were  
15 developed by routing a portion of the move  
16 over a second carrier.

17 Further, when selecting carriers  
18 and routes shippers consider service and  
19 total costs which includes rates, the  
20 difference in fuel surcharges, car costs for  
21 private equipment and inventory costs.  
22 Competitive switching will be optional.

1                   The railroads will have the option  
2                   to compete and the shippers will have the  
3                   option to select a preferred carrier and the  
4                   routes. As a result the competitive market  
5                   forces will improve the efficiency of  
6                   operations.

7                   AAR contends that competitive  
8                   switching will not work in the U.S. because  
9                   the U.S. rail system is more complex than the  
10                  Canadian system. Further, AAR witnesses,  
11                  Phil Ireland and Rodney Case, stated  
12                  regulated interswitching has been part of  
13                  their regulatory system for 100 years.

14                  As a result the Canadian  
15                  interswitching does not lend any support to  
16                  the proponents of mandated switching in the  
17                  U.S. which has never had a history of  
18                  mandated switching. There's no reason to  
19                  believe that CSP will not work in the U.S.  
20                  Also, I fail to see the point that regulated  
21                  interswitching has been part of the Canadian  
22                  regulatory system for 100 years.



1                   While the rules may have been in  
2 place, the first industry to actually access  
3 interswitching in Canada was Cominco  
4 Fertilizer Company in 1993. Some of the  
5 railroads, in their reply statements'  
6 reference to the Thurston report, would  
7 suggest that Canadian interswitching has had  
8 a negative impact on railroad operations.

9                   However, those statements were  
10 taken out of context. The remainder of this  
11 section of Thurston's report reads, Such  
12 switching activities are part of the everyday  
13 life of railway operations. For without such  
14 operations, mainline functions would not  
15 occur in an efficient manner. One might  
16 consider such demands on the railway system  
17 would lead to inefficiencies and significant  
18 negative impacts on railway operations.

19                  As such, outcomes do not appear to  
20 be apparent. Over the past 10 to 15 years  
21 both CN and CP have driven forward and  
22 achieved significant productivity and

1 efficiency gains. Union Pacific's railroad  
2 stated they would not have proceeded with the  
3 series of consolidations that created the  
4 current UP system had they been conditioned  
5 at the time by the NIT League proposal.

6 UP consolidated six railroads into  
7 a single system. UP's statement appears to  
8 support the theory that the consolidation of  
9 the rail industry and the creation of  
10 monopolies was strategic and intentional and  
11 underscores the need for the Board to take  
12 corrective action.

13 AAR stated it is impossible to  
14 know in advance how much switching would  
15 occur if the NIT League proposal were  
16 adopted. AAR is correct from the standpoint  
17 we will be forging new ground. Also, the  
18 incumbent railroads would influence the  
19 number of shippers that will actually access  
20 competitive switching.

21 However, we have learned from  
22 experience that we can predict behavior based

1 on history. Canadian interswitching has been  
2 successful. It has established discipline in  
3 the industry without any apparent negative  
4 impact on railroad efficiency and it has not  
5 decreased customer satisfaction.

6 The report attached to Highroad  
7 Consulting's opening comments authored by  
8 Thurston and NIT League's witness, Tom  
9 Maville, presented a history of the  
10 development of interswitching in Canada and  
11 evidence that the Canadian railroads have  
12 thrived since interswitching was established.

13 We submit the Board should modify  
14 the proposal before issuing proposed  
15 competitive switching rules. The process  
16 should be simplified, the same or similar to  
17 the Canadian model. Shippers should not be  
18 required to pass a test to access competitive  
19 switching.

20 A process that would require  
21 shippers to assume the cost to retain  
22 transportation attorneys and consultants to

1     initiate proceedings that will require proof  
2     of market dominance and prove that rates  
3     exceeded designated R/VC threshold would not  
4     be a practical alternative for small to mid-  
5     size customers like Diversified.

6                 This should not be a privilege  
7     reserved for very large industries that have  
8     significant financial resources to take on  
9     such an initiative. Instead, the process  
10    should be simple and automatic as it is in  
11    Canada. I'm nearly done.

12                However, if the Board elects to  
13    include in the new rules procedures that  
14    include calculation of a regulatory  
15    benchmark, the benchmark should be fair to  
16    all parties. We contend the regulatory  
17    threshold should be consistent with that in  
18    place for other STB proceedings and that is  
19    180 percent.

20                However, the problem with URCS  
21    continues to exist. URCS needs to be updated  
22    or replaced as it produces costs that are not

1 accurate and the costs are grossly  
2 overstated. The Canadian Board of Railway  
3 Commissioners in 1918 ruled that  
4 interswitching is a right, not a privilege.

5 We encourage the Board to initiate  
6 a rulemaking proceeding and to amend the NIT  
7 League proposal to simplify the process with  
8 the objective to increase competition in the  
9 rail industry for all shippers, not just a  
10 privileged few.

11 MR. KEPLER: Good morning,  
12 Chairman Elliott and Vice Chairman Begeman.  
13 I'm Dave Kepler, an Executive Vice President  
14 with the Dow Chemical Company. And I really  
15 appreciate the opportunity to testify today  
16 on competitive switching.

17 I think it's one of the important  
18 steps towards achieving a competitive rail  
19 transportation system, one that we all feel  
20 is worth continuing to invest in. Dow is an  
21 American manufacturing company that is making  
22 investments that will create higher quality

1 jobs for our country.

2 Nearly 800,000 Americans rely on  
3 the chemical industry for employment. And  
4 for every one of these jobs there's another  
5 six jobs that are created in the U.S.  
6 economy. And so Dow, with others in our  
7 industry, are working hard to ensure that we  
8 have the right competitiveness through the  
9 right policy in energy, education, regulatory  
10 and infrastructure policy.

11 The U.S. needs sound policy and a  
12 comprehensive strategy for the transportation  
13 sector and investment in its infrastructure  
14 if we are to improve the global  
15 competitiveness of the U.S. manufacturing  
16 sector. It's in our interest to make sure  
17 the policy continues to have and encourage  
18 investment in the rail sector.

19 The rail industry has undergone  
20 multiple rounds of consolidation that has  
21 been mentioned earlier, down to seven  
22 railroads today. This has resulted in fewer

1 choices for shippers and much longer  
2 bottleneck segments that really limit and  
3 close down options for shippers.

4 Regulatory policy has accepted  
5 this reduction in competition in favor of  
6 promoting railroad revenue adequacy. But  
7 with the level of railroad consolidation that  
8 has been allowed it is overdue to establish a  
9 greater balance for supplier options.

10 The U.S. rail system enables the  
11 American manufacturer to move product at  
12 scale. Therefore, U.S. rail policy should  
13 not put a captive manufacturer at a  
14 disadvantage versus, say, importers that have  
15 a choice of competitive entry points. The  
16 chemical industry, for example, pays on  
17 average 20 to 30 percent higher than it pays  
18 at competitive locations with less service  
19 options.

20 Importers can choose their points  
21 of entry based upon competitive rail rates  
22 that reap the benefits of this differential.

1 It also limits other carriers from taking  
2 that differential on reinvesting and other  
3 options and services. The magnitude of this  
4 is hardly justified that the revenue  
5 performance that the rail industry has today.

6 So we believe that there is a  
7 responsibility today, along with the tools we  
8 have, to address the current competitive  
9 imbalance between shippers and railroads.  
10 Those include promoting this switching to  
11 address captivity over short distances,  
12 establishing bottleneck rates and making sure  
13 the rate case process becomes more accessible  
14 by reducing the cost, time and effort of  
15 these cases.

16 The Board developed its current  
17 standards for reciprocal switching back when  
18 the rail industry was struggling financially.  
19 And frankly, the market power was more  
20 dispersed. But after 30 years that situation  
21 has changed dramatically.

22 As I noted at the outset, there



1 was significant rail consolidation since the  
2 1980s which means even more market power and  
3 scale for the railroads. And that actually  
4 should mean more service options for the  
5 shippers, not less. And we don't have that  
6 today.

7           According to the recent Staff  
8 Report from the Senate Committee on Commerce,  
9 Science and Transportation the rail industry  
10 regularly and consistently has been setting  
11 records for operating ratios, operating  
12 income and shareholder earnings. This  
13 evidence demonstrates that a major goal of  
14 the Staggers Act to rehabilitate railroad  
15 financing has been achieved.

16           The fact now enables the Board to  
17 give greater attention to the other major  
18 goal, the promotion of effective competition  
19 among railroads which has yet to have been  
20 realized.

21           The League's competitive switching  
22 proposal contains long overdue revisions to

1 the Board's competitive access rules. The  
2 present rules are onerous. The shippers have  
3 not then, to my knowledge, even attempted to  
4 use them in order to obtain competitive  
5 switching for more than 20 years.

6 The League's proposal presents a  
7 less onerous yet modest standard for  
8 switching and is predicated upon a reasonable  
9 distance to a working interchange. This type  
10 of rule could extend competitive options to a  
11 meaningful amount of rail traffic without  
12 destroying the rail industry's ability or  
13 incentives to make capital investments.

14 Our perspective, Dow's perspective  
15 on the importance of adopting an accessible  
16 and meaningful form of competitive switching  
17 is based on our experience both in the U.S.  
18 and in Canada where a form of competitive  
19 switching known as interswitching has existed  
20 for many decades.

21 Dow's U.S. facilities are  
22 competitively handicapped by the lack of rail

1 competition which competitive switching would  
2 alleviate. In North America we operate a  
3 fleet of over 20,000 railcars and carry over  
4 110,000 rail shipments to over 2,100 of our  
5 customers from multiple North American  
6 production facilities, some of which are open  
7 and others closed to the competitive rail  
8 service.

9 On the whole, Dow and its  
10 customers are impacted since we are one of  
11 the largest chemical shippers in the country.  
12 Dow's largest plants in Freeport, Texas,  
13 Plaquemine and Taft, Louisiana represent over  
14 58 percent of Dow's U.S. origin rail  
15 shipments. All are captive to the same  
16 railroad and 80 percent of Dow's U.S.  
17 destination shipment are captive to one  
18 railroad.

19 Thus, even if the Board were to  
20 adopt the League's proposal, a significant  
21 part of our traffic would continue to be  
22 captive, yet we still support the League's

1     proposal for the portion of the traffic that  
2     it would benefit.

3                 We support this competitive  
4     switching. It's based on our experience in  
5     Canada which has been a more constructive and  
6     balanced approach. We operate major  
7     facilities in western Canada and really have  
8     benefitted through Canada's interswitching  
9     regulations.

10                As a result, Dow sees a fair  
11     system with the ability to foster rail  
12     competition that improves service, routing  
13     options and actually has increased investing  
14     by the railroads and the shippers with that  
15     type of system.

16                As I noted on the outset of my  
17     remarks, there will be renaissance in  
18     American manufacturing that can create new  
19     investment and job opportunities, that a  
20     competitive transportation system is key to  
21     continuing that trend.

22                Competitive switching is one step

1     that will help bring us closer to promoting  
2     competition for shippers and rail  
3     transportation and promises to improve rail  
4     service, provide better routing options and  
5     establish competitive rates, all of which are  
6     important for American manufacturers to be  
7     competitive in the global marketplace.

8                 Just as railroads are doing, Dow  
9     is making significant investments in capital  
10    improvements and expansions. We have  
11    announced a \$4 billion investment to expand  
12    our largest integrative sites in the U.S.  
13    Gulf coast.

14                Because those locations are held  
15    captive to a single rail carrier, our captive  
16    rail volumes will increase. Because everyone  
17    benefits from this investment, our country  
18    could have higher paying jobs in both the  
19    rail and manufacturing sector. We need to  
20    support these significant investments by Dow  
21    and others to ensure our products are moved  
22    to customers in the most effective, efficient

1 and fair manner.

2 In fact, the existence of  
3 competition, Dow believes, will result in the  
4 development of new and more efficient  
5 routing. So our premise is that this  
6 actually will simplify and improvement  
7 services and encourage investments.

8 And I don't have a slide with me  
9 but one example in our Louisiana rail supply  
10 chain, Dow estimates that competitive  
11 switching would remove 1 million miles from  
12 its supply chain for an average reduction of  
13 200 miles per shipment.

14 So in reality, when we use the  
15 airport analogy, it's not just the complexity  
16 to the interchange. The reality is we can  
17 take, in the long haul, a lot more  
18 simplification and actually reduce complexity  
19 in shipment which results in more efficiency  
20 in our supply chain and the railroad's.

21 For this reason, Dow is asking the  
22 Board to act upon the League's competitive

1 switching proposal by initiating a notice of  
2 proposed rulemaking. Thank you.

3 MR. RINE: Chairman Elliott, Vice  
4 Chairman Begeman, my name is Phillip Rine.  
5 I'm Director of Logistics for Auriga Polymers  
6 Charlotte, North Carolina.

7 I hold Commercial Logistics  
8 responsibilities for Indorama Ventures Oxide  
9 & Glycols in Bayport, Texas, Starpet Inc. in  
10 Ashburn, North Carolina, AlphaPet Inc.  
11 Decatur, Alabama, Auriga Polymers, Inc.  
12 Spartanburg and Greer, South Carolina. All  
13 four Indorama companies are captive shippers.

14 I have over 35 years' logistics  
15 experience in general and chemical and  
16 plastics transportation experience, in  
17 particular. Previous employers include  
18 Allied Chemical, City Service, AE Staley,  
19 Ashland Chemical, Degussa Corporation,  
20 Aristech Chemical, Kerr McGee Chemical and  
21 Vista Koch Industries.

22 I've served two 3-year commissions

1 as a member of the Pennsylvania Governor's  
2 Rail Freight Advisory Committee under Thomas  
3 Ridge representing the chemical industry for  
4 the state of Pennsylvania. I appeared before  
5 the Service Transportation Board before the  
6 Conrail merger, representing the chemical and  
7 plastics industries and served on the Conrail  
8 Transaction Council after the CSX and NS  
9 acquisition of Conrail was completed.

10 My experience predates Staggers  
11 Act, shipper railroad contract negotiations  
12 and railroad mergers that followed. I have  
13 direct experience in two rate reasonableness  
14 cases. I'm accompanied today by Mr. Tom  
15 O'Connor of the Tom O'Connor Group, who has  
16 assisted in the preparation of the testimony  
17 being provided today and is available also to  
18 respond to questions.

19 It is a pleasure and a privilege  
20 to appear before the Board today representing  
21 Indorama Venture's companies. Thank you for  
22 the opportunity.



1           The need for revised competitive  
2       switching rules is widely recognized. NIT  
3       League filed its petition over two years ago  
4       following hearings at the conclusion of the  
5       EP 705 docket on competition in the industry.  
6       In its January 2011 STB decision instituting  
7       EP 705 the Board stated it is time for the  
8       Board to consider the issues of competition  
9       and access further.

10           The record in EP 705 amply shows  
11       that existing regulatory rules have only  
12       partially achieved the purpose of the  
13       Staggers Act. For many shippers in a wide  
14       range of industries, some of whom are captive  
15       shippers, access to competition has been  
16       reduced or eliminated.

17           Indorama intends to show that  
18       competitive switching is advisable. It meets  
19       a need and can be accomplished with minimal  
20       adverse affects. Many parties have noted,  
21       and Indorama strongly supports the position,  
22       that the revised competitive switching rules

1     should not block access to rate  
2     reasonableness remedies.

3                 When the competitive switching  
4     rules are revised they must clearly provide  
5     that where an otherwise captive shipper  
6     utilizes the revised rules to obtain  
7     additional rates from a competing railroad  
8     the existence of those rates should not be  
9     considered as effective competition, and  
10    there should be no exemption of rates that  
11    are in a contract.

12                By doing that you will further  
13    provide a barrier for shippers to access the  
14    benefits of competitive switching. Railroads  
15    sometimes have shown tendencies to serve  
16    their own interests to the diminishment of  
17    captive shipper interests and the public  
18    interest.

19                Examples of favoring railroad  
20    interests over captive shipper interest and  
21    the public interest include excessive rates  
22    and charges, paper barriers, over-recovering

1 fuel surcharges, restricted routing and other  
2 techniques that impede access to more  
3 reasonable rates.

4 Indorama management's experience  
5 spans the time period including the passage  
6 and implementation of the Staggers Act. We  
7 have observed often that as competitive  
8 alternatives decrease rates increase. The  
9 proposed revised competitive switching rules  
10 can serve to mitigate some of the adverse  
11 effects of this loss of access to competitive  
12 alternatives.

13 Indorama operates extensively in  
14 both the U.S. and Canada. In our experience  
15 and observation the Canadian competitive  
16 switching process operates effectively. It  
17 provides major benefits and does not result  
18 in adverse affects.

19 The record in Ex Parte 711 shows  
20 that potential impact on railroad revenues  
21 and traffic volumes would be relatively  
22 small. USDA and US DOT each independently

1 found that the impact on railroad revenues  
2 and traffic volumes would be relatively  
3 small.

4 Analysis entered in evidence  
5 indicate that while 37 percent of CN and CP  
6 traffic was eligible for interswitching in  
7 2011 less than 4 percent of the Canadian  
8 traffic is interswitched annually. This also  
9 indicates that the proposed competitive  
10 switching will have a minor impact on  
11 railroad revenues and volume.

12 Indorama expects that the costs  
13 related to interswitching will be offset by  
14 additional revenues. The remaining net cost,  
15 if any, can be shared with the shippers  
16 involved. Indorama is open to the idea of  
17 sharing the cost, of gaining access to  
18 competitive rail switching.

19 Indorama supports the NIT League  
20 proposal which will help remedy several  
21 issues centering on access to competition  
22 while recognizing and accommodating the

1 ongoing need for railroads to maintain  
2 adequate financial strength and continue to  
3 build efficiency and productivity.

4 A reasonable access price can be  
5 developed for use in competitive switching.  
6 Indorama supports the use of a mutually  
7 agreed trackage rights fee or a haulage  
8 rights fee for covering the costs associated  
9 with reaching the competitive switching  
10 carrier.

11 Both trackage rights fees and  
12 haulage rights fees are well established  
13 concepts in the rail industry. If the  
14 parties in a given switching access situation  
15 do not agree to such fees we recommend that  
16 the Board prescribe a reasonable access fee.

17 My testimony today focuses on two  
18 principle commodities transported for  
19 Indorama. These commodities are PET and MEG.  
20 Tom O'Connor Group has analyzed the 2011  
21 Board's confidential Waybill file made  
22 available for us in this proceeding.

1                   Moreover, the Tom O'Connor Group  
2                   has analyzed and will also rely on analysis  
3                   of Indorama data. Indorama will present  
4                   charts showing aggregate summaries of PET and  
5                   MEG, the two major Indorama commodities, as  
6                   well as other Indorama products moving along  
7                   similar routes of movement.

8                   The data will be drawn in part  
9                   from the Board's 2011 Waybill data. These  
10                  data are germane to determining the  
11                  reasonableness of the rates charged or  
12                  proposed by rail carriers serving Indorama.

13                  Indorama previously requested Tom  
14                  O'Connor Group to review the benchmark and  
15                  benchmark the level of Indorama rail rates.  
16                  Analysis for Indorama included rail rates for  
17                  inbound and outbound movements of MEG and  
18                  outbound shipments of PET.

19                  The methodology we used to  
20                  calculate variable cost follows the  
21                  procedures used in the Board's rate  
22                  reasonableness proceedings. We find that the

1 proposed 240 R/VC is a reasonable first-step  
2 guideline. However, our preference would be  
3 180 percent R/VC as presented by other  
4 interested parties in this proceeding.

5 In conclusion, analysis of  
6 Indorama data found that many of the Indorama  
7 lanes produced an R/VC greater than or equal  
8 to the 240 percent. These results support  
9 the need for the pro-competitive benefits of  
10 the NIT League proposal.

11 Our analysis allayed concerns  
12 which may be voiced by some parties that the  
13 NIT League proposal could cause dislocations  
14 in markets. The relatively high R/VC results  
15 indicate that with competitive switching a  
16 competing railroad may secure some additional  
17 rail business at rates which are still highly  
18 profitable.

19 Practical experience suggests that  
20 the endemic railroad would likely retain the  
21 business in many, if not most, cases. This  
22 indicates that while shippers may achieve

1 modest gains, there would be little adverse  
2 impact on other shippers.

3 Our conclusion is that the NIT  
4 League proposal will have beneficial effects  
5 in PET and MEG markets without leading to  
6 significant adverse effects on other shippers  
7 or the rail system as a whole. The points  
8 outlined in this summary support  
9 implementation of the NIT League proposal.

10 And Indorama recommends that the  
11 Board do so by granting the NIT League  
12 petition and instituting a rulemaking to  
13 adopt the revised competitive switching  
14 rules. Thank you for your attention. We'll  
15 be glad to answer any of your questions.

16 VICE CHAIRMAN BEGEMAN: Thank you.  
17 I think, for the most part, I really have  
18 just one question for all of you. And a  
19 couple of you certainly touched on it. You  
20 specifically did, Jeff.

21 But given what the prior panel,  
22 and what the rail panel said yesterday about



1 the impact of this proposal if it goes  
2 forward, what it would do to rail operations,  
3 systems - three times the length of time to  
4 deliver a product.

5 Clearly, that would give one pause  
6 if it turned out to happen across the  
7 network. Obviously, you represent either  
8 various shippers, or you are shippers  
9 yourselves, who really want service. That's  
10 what this is all about, affordable, efficient  
11 service. If you can just comment on their  
12 concerns, and why that isn't giving you  
13 pause.

14 MR. MORENO: If I can just start  
15 off by saying a lot of these are red herrings  
16 because the question is why would a shipper,  
17 I think you yourself asked that question of  
18 the last panel, why would a shipper choose  
19 one of these far more complicated  
20 alternatives.

21 Well, the important factor, if  
22 service is the ultimate objective, they may

1 not choose that more complicated factor.  
2 They probably won't. But the point here is  
3 they have the choice. And for some shippers  
4 it may be they may be willing to pay a  
5 premium for better service.

6 Other shippers, the service isn't  
7 as, the timeliness or the predictability of  
8 the service is not as important for them.  
9 We've heard a lot of analogies drawn to the  
10 airline industry here. And the airline, and  
11 I think someone yesterday compared a direct  
12 flight to a flight that goes through a hub  
13 and spoke.

14 Well, yes, all other factors  
15 equal, anyone would choose the direct flight.  
16 But we still have a lot of passengers out  
17 there who choose to fly through connections  
18 because they get a better rate that way. And  
19 for them it's not as important to get the  
20 direct flight and to pay for the direct  
21 flight.

22 And anyone who's flown today

1 typically knows that you will pay more for  
2 that direct flight versus the cheaper  
3 options. I'll leave it to the individual  
4 shippers on the panel to talk about their  
5 specific circumstances.

6 MS. DEARDEN: Well, first of all,  
7 I would like to think that we could work with  
8 the incumbent railroads as opposed to having  
9 to go through this process. However, I don't  
10 believe that this is going to have a negative  
11 impact on service because, like Jeff said,  
12 people are going to make the right decisions  
13 for their company and that's going to be  
14 based on efficient operations.

15 Currently, we have numerous  
16 situations where the railroads have developed  
17 routing protocols that produce very  
18 circuitous routes. And it seems like the  
19 intent of the routing protocol is to get the  
20 origin carrier a longer haul. But it's not  
21 the most efficient route. It actually  
22 increases the miles on the route

1 significantly.

2           If there are situations where you  
3 could change the interchange. We have pushed  
4 back on some of those routing protocols and  
5 we have succeeded at getting the interchange  
6 points changed, giving so that we did have a  
7 more efficient route.

8           But it takes a lot of effort to do  
9 business with the railroads. And to try to  
10 come up with something that's good not only  
11 for the shipper but also for the railroads,  
12 because you have to understand it from the  
13 railroads put of view. But I just don't see  
14 that this is going to have a tremendous  
15 impact on the railroads.

16           If you look at the number at the  
17 estimate in the NIT League proposal it's not  
18 going to impact on a huge amount of carloads.  
19 But I do think it will add, put discipline  
20 into the system. And just having the option  
21 to request for reciprocal switching will  
22 establish competition, and I think that

1       should be our goal.

2                   Our goal should actually to be  
3       able to work with railroads as opposed to  
4       running to the STB every time we have a  
5       complaint.

6                   MR. JOHNSTON: I think in the  
7       argument here there's a premise that the  
8       existing state of affairs for captive  
9       shippers gives them, in fact, the best  
10      service under the best terms. And that's  
11      simply an assertion. There hasn't been any  
12      evidence presented here that, in fact, that  
13      is always the case or most of the time the  
14      case.

15                  So I suggest you test that  
16      premise, first of all. It might very well be  
17      that with, in certain cases with competitive  
18      switching there might, in fact, be  
19      improvements in service. There might. And  
20      furthermore, I would say, as a shipper, we  
21      look at the whole package.

22                  We want reliable service. We want

1       efficient transportation. We want cost-  
2       effective transportation, and we want safe  
3       transportation. It's that whole package that  
4       we're always going to look at and make the  
5       choices.

6                       MR. KEPLER: Okay. In our  
7       situation, you know, I mentioned we have  
8       20,000 railcars, we have 110,000 shipments.  
9       So it's, we don't turn them around a lot in a  
10      year for the amount of shipments. There's a  
11      lot of capital investment there. So service  
12      is a huge deal to us.

13                     And I think when we work with, and  
14      we have a good relationship with our sites in  
15      working with the railroads on safety, service  
16      and routing is a key issue in terms of how we  
17      manage that. If I look at the example in  
18      Canada we always, it's not that we pick one  
19      or the other and use it just about  
20      negotiations.

21                     They've invested in our site to  
22      make sure they have flexibility at the

1 interchange. We always have had two  
2 suppliers there in my decade of working with  
3 that and we've had it, as far as I know,  
4 almost always. Having two, having multiple  
5 choices, especially in times like winter or  
6 hurricanes or whatever provides a huge safety  
7 net for us in managing, to have options.

8 And I think just the ability to  
9 look at not only the interface of this 30  
10 miles but how you really route across this  
11 network give you better options with that.  
12 So our view is that this will encourage  
13 investments and actually optimize the  
14 networks better, and you'll do it more on a  
15 commercial basis rather than trying to deal  
16 with all the rules set.

17 MR. RINE: I think, first of all,  
18 we're talking about competition. There's  
19 absolutely no incentive for a shipper to  
20 sacrifice service when he's trying to  
21 negotiate between two or three carriers. The  
22 shipper also is not interested in adding to

1 congestion which would increase transit time.

2 We have heavy investments in  
3 railcars. We have heavy investments in  
4 assets for manufacturing plants. We're  
5 interested in those assets, railcars, moving  
6 expeditiously through the supply chain to get  
7 back to reload, to ship more product.

8 We size our railcar fleets to meet  
9 our production and sales needs. We don't  
10 have excess cars just to, you know, you just  
11 keep loading them thinking well, this car's  
12 going to get back in two or three or six  
13 months. That's not reality in this industry.

14 And I think to focus on the  
15 service side in the rail system is something  
16 you need to do. But also I can cite many  
17 examples where we've worked with the  
18 operation people in the railroads. And we've  
19 had some good local success.

20 And we've had some projects we've  
21 worked on operationally that the rail  
22 operations people would agree to, even went



1 through the unions and got the approval to do  
2 it, moving back and forth between individual  
3 railroad yards to bypass interchange tracks  
4 that were not adequate to handle the volume  
5 only to be not approved by the commercial  
6 side because they cut a deal somewhere in  
7 some other state.

8           There's been a lot of work, as  
9 been previously mentioned, with the railroad  
10 to try to do business. It shouldn't be that  
11 hard. And I'm appalled at some of the  
12 examples that are used. I've been in this  
13 business a long time, worked with a number of  
14 different companies.

15           I've never seen any of what I  
16 heard yesterday and today. That must be  
17 something in a boardroom somewhere or  
18 something. That's foreign to me.

19           MS. DEARDEN: All right, one  
20 comment on I'd like to make is when I was at  
21 the Railroad I attended the more daily  
22 morning operating meetings because I had a

1 lot of unit train traffic. And in those  
2 meetings, I attended over probably a 12-year  
3 period, I cannot once remember any discussion  
4 relative to inefficient operations as a  
5 result of reciprocal switching.

6 Number two, they do have daily  
7 reports of the car inventory on the system.  
8 But the purpose of that, of monitoring the  
9 number of cars online is to control the per  
10 diem cost that they have to pay to the  
11 connecting railroads. There was, it had  
12 nothing to do with the impact on operations.  
13 It was strictly to control the per diem  
14 costs.

15 So I think a lot of the examples  
16 that the railroads presented today and  
17 yesterday have been like the sky is falling,  
18 you know, the world's going to come to an  
19 end. I just believe the railroads, it's not  
20 that the railroads don't want reciprocal  
21 switching per se. I think it's that the  
22 railroads don't want any change at all.

1                   MR. O'CONNOR: I'd like to offer a  
2                   comment as well. I have looked at dozens of  
3                   companies in detail. And what I find is that  
4                   when I'm dealing with a captive situation,  
5                   almost invariably, the rates are  
6                   significantly higher, holding all else equal.

7                   And that goes across companies.  
8                   It goes across railroads. It is almost  
9                   axiomatic, that as the captivity of the  
10                  traffic increases the rates go up. As the  
11                  absence of competition increases the rates go  
12                  up.

13                  And it's important to be clear  
14                  about what we're recommending here and what  
15                  we're evaluating here. As Jeff stated at the  
16                  outset of this panel, this is a voluntary  
17                  operation. The NIT League proposal would  
18                  have a couple of pre-conditions which, if you  
19                  met them, you would be allowed to ask the  
20                  competing carrier to offer the service.

21                  If asked, the competing carrier  
22                  might decline to offer. The incumbent

1 carrier might respond with a better deal.  
 2 You would be allowing the creation of  
 3 competition and with it you would be solving  
 4 all sorts of issues that just would never  
 5 arise.

6 We'd be allowing the market to  
 7 operate just by dropping that barrier and  
 8 asking a lot of the questions we ask. Would  
 9 somebody else like to handle this traffic?  
 10 That's all we're saying here. That's all  
 11 we're saying. It's voluntary.

12 VICE CHAIRMAN BEGEMAN: No, I  
 13 think they're saying you have to handle it,  
 14 aren't they?

15 MR. O'CONNOR: I'm sorry?

16 VICE CHAIRMAN BEGEMAN: Or, is it  
 17 you're saying, you have to handle it?

18 MR. O'CONNOR: No. No, the  
 19 proposal, as proposed, would not compel a  
 20 competing carrier to come in. It would allow  
 21 the competing carrier to offer its services,  
 22 which might either be -- well, first of all,

1       they might not be offered.

2                       Secondly, if offered, they might  
3       not be adequate to the task and they might  
4       not be accepted.

5                       VICE CHAIRMAN BEGEMAN:   Don't you  
6       have a common carrier obligation to provide  
7       service?

8                       MR. O'CONNOR:   Well, I'm sure  
9       there's a common carrier obligation to  
10      provide service.   But what we have here is a  
11      situation where you're preventing that  
12      competing common carrier from stepping  
13      forward to ask can I provide this service.  
14      That's what we're talking about here in  
15      practical effect.

16                      And if you have two people  
17      competing you're going to get a better deal.  
18      There's almost no question about it.

19                      MR. RINE:   One other comment,  
20      please.   There was comments made about chaos  
21      and not knowing where cars were at.   We have  
22      systems where we track our cars.   In fact, we

1     have some fleets we have two tracking systems  
2     on cars.

3                   So we know where our cars are at  
4     all the time and if there's a question we  
5     have people that follow those cars daily.  
6     That's their job. They interact with the  
7     railroads. But we have systems where we know  
8     the temperature of a car inside and outside.  
9     We know where that car is at, we know what  
10    time it was there, date and time.

11                  So I'm not sure, now we've lost  
12    cars too. And then we've had to go out to  
13    rail yards and find them for our self. But  
14    the idea that you don't know where your cars  
15    are at, those are exceptions. Those are not  
16    what goes on every day in our business.

17                  MR. O'CONNOR: I want to reinforce  
18    that also. When you think about, and I think  
19    you raised this question earlier, you posited  
20    a merger. We've had discussions of mergers  
21    in the course of these two days.

22                  Now I've appeared as a witness in

1 merger cases for railroads and for shippers,  
2 both, generally analyzing a proposed merger  
3 and asking for conditions that would meet  
4 specific defects that we found on the merger.

5 Now what we're talking here is  
6 vastly simpler than a merger. And UP has  
7 consolidated down from a half a dozen or so  
8 to the current UP. And I participated in a  
9 couple of the merger proceedings that  
10 resulted in the four that we know have.

11 The complexity of that kind of an  
12 operation is vast and it's been mastered.  
13 They rose to the challenge. They did it.  
14 And in that particular one, as a matter of  
15 fact, I was representing a series of clients,  
16 most of whom were opposed to that merger.

17 But it got resolved. UP bore  
18 down, solved the problem, gave it some, came  
19 back. They got it done. They get it done.

20 If you look at the data that's  
21 presented to you on a quality basis and the  
22 rail cost adjustment factor, and you just

1       compare the rail cost adjustment factor  
2       unadjusted for productivity and adjusted for  
3       productivity, no matter what the period, and  
4       we're talking 20, 30 years here now, no  
5       matter what the period, no matter what the  
6       challenge, no matter who's running the  
7       railroad, the productivity line, the  
8       productivity keeps getting better and better.

9               They keep rising to the challenge,  
10       rising to the challenge.

11              MR. KEPLER: I think in the last  
12       panel there was a little discussion around  
13       this which is my experience and our  
14       experience at Dow is when you're in a  
15       position where you have the competition, if  
16       another entrant's going to come in, they're  
17       going to factor the service in.

18              So the questions that were being  
19       asked about well, if this is going to  
20       actually, if this interchange costs more  
21       service, that is going to be factored in.  
22       That cost will be factored into the



1 competitive rate.

2 And then the carrier will  
3 determine well, do I make a capital  
4 investment to improve that service or do I  
5 find that that's an expense I can build,  
6 still be competitive because of my long haul  
7 or whatever.

8 So I think the fact is the choice  
9 and the price will come, that's where the  
10 choice comes. And what we've seen in other,  
11 in Canada, was the competition is there to  
12 make the choices, and it's balanced not just  
13 on that one point of service but how I invest  
14 to improve that service or how I manage my  
15 long haul network to get better optimization  
16 out of that.

17 CHAIRMAN ELLIOTT: Just a few  
18 questions. Some of these things are just to  
19 kind of nail down what the proposal is  
20 specifically. There still seems to be some  
21 confusion with respect to whether exempt  
22 traffic would apply.

1                   And I probably should have asked  
2                   the panel yesterday this question when NIT  
3                   League presented. But maybe Mr. Moreno can  
4                   speak to that, whether or not that is part of  
5                   the proposal.

6                   MR. MORENO: I think that's an  
7                   issue for specific notice of proposed  
8                   rulemaking. Obviously, the NIT League  
9                   proposal is predicated on some determination  
10                  of market dominance. And exempt traffic  
11                  always has the option to seek a removal of  
12                  that exemption, either the class exemption or  
13                  on a movement specific basis.

14                 There is at least language in the  
15                 current CFR under the Exempt Traffic section  
16                 that does suggest that showing a market  
17                 dominance would basically remove the  
18                 exemption in these situations.

19                 And so that may already be  
20                 addressed, although the question is, well, is  
21                 this market dominance or is it the market  
22                 dominance showing that the NIT League's

1     proposing or is it the market dominance  
2     showing that you require in a rate case, for  
3     example.

4                 But those are issues that I think  
5     are appropriate to be addressed in a  
6     rulemaking proceeding.

7                 CHAIRMAN ELLIOTT:   Okay, second  
8     question, with respect to the 75 percent  
9     presumption, there was some concern raised in  
10    some of the rail testimony and comments, that  
11    that number could possibly be manipulated and  
12    by pushing more traffic onto one carrier in  
13    these situations, in trying to meet that  
14    number.

15                I can see, common sense wise that  
16    makes sense.   But in the real world is that  
17    going to happen or can it happen?

18                MS. DEARDEN:   I'd like to comment  
19    on that.

20                CHAIRMAN ELLIOTT:   Sure.

21                MS. DEARDEN:   Diversified has a  
22    plant in Mississippi that's single-served by

1 a carrier. And that carrier's been very  
2 difficult to work with in terms of  
3 establishing competitive rates.

4 And so, as a result, that plant  
5 has not performed at the level that it was  
6 intended when they built that plant in, I  
7 think it was the early 90s that they built  
8 it. And so, as a result, they are doing some  
9 local truck moves.

10 But they're not reaching  
11 destination markets they had initially  
12 planned to meet to access by rail. So, for  
13 example, they have a distribution plant in  
14 Miami for, it's a distribution tank for  
15 shipments to the Carribean.

16 We were thinking, or they were  
17 thinking, we weren't working for them at the  
18 time. They were thinking that they would be  
19 able to ship from Mississippi to Miami  
20 cheaper than going from the Illinois plant.  
21 Well, instead, we're still shipping from  
22 Illinois because it's more cost-efficient.

1                   Bottom line is we're not going to  
2                   be able to demonstrate at that plant, even  
3                   though the rates are unreasonable with the  
4                   incumbent carrier, we're not going to be able  
5                   to prove that, meet that 75 percent test  
6                   because a good portion of the shipments are  
7                   going truck instead of rail. And we're not  
8                   going to be able to prove market dominance.

9                   But in fact, unless things change,  
10                  that plant is at jeopardy and the people that  
11                  are employed down there, they're jobs are in  
12                  jeopardy because unless that situation  
13                  changes and unless we get competitive rail  
14                  rates it's very possible they'll close the  
15                  plant.

16                  CHAIRMAN ELLIOTT: Another  
17                  question, a couple of you raised the  
18                  consolidation of the rail industry as one of  
19                  the reasons for some of the higher rates and  
20                  this upswing in the rates by the Class Is,  
21                  and then in Mr. Moreno's final exhibit he  
22                  provided an example.

1                   And I haven't been involved in a  
2 merger. I think the last one was '96. But  
3 wouldn't, in that situation that was laid out  
4 here, wouldn't the Board have remedied that  
5 situation of a two to one going to, in this  
6 situation, by allowing trackage rights out to  
7 Railroad 3 in that situation?

8                   It's just, it's been a while so I  
9 don't remember exactly.

10                  MR. MORENO: Yes, if we can put up  
11 my slides, up again, this example. This is  
12 not a 2-to-1 example. It was a captive  
13 shipper pre-merger. It was a captive shipper  
14 post-merger.

15                  CHAIRMAN ELLIOTT: I see. Okay.

16                  MR. MORENO: So the Board does not  
17 consider that a loss of competition. But the  
18 fact of the matter is, in this example, the  
19 shipper lost competition over the vast  
20 majority of the distance of its route, but  
21 the Board has never recognized that as a  
22 loss.

1                   CHAIRMAN ELLIOTT:   Okay.   Now that  
2   makes sense.

3                   MR. O'CONNOR:   There is also a  
4   simple way to evaluate the loss of  
5   competition.   In the BNSF merger we were  
6   addressing loss of competing service in the  
7   category called 4-to-3.

8                   By the time we got to the UP  
9   merger a few years later the 4-to-3s were  
10   gone.   The 3-to-2s were pretty much gone, and  
11   it was 2-to-1 and there weren't that many of  
12   those.   So you can see, in having 4-to-3 be  
13   an issue, as that merger process really got  
14   underway and then they disappeared.

15                  And what we're talking about here  
16   is a remedy for some of that loss of  
17   competition.   Staggers was extremely  
18   successful.   I was at AAR when Staggers was  
19   proposed and I was more or less a briefcase  
20   carrier at that part of the deal but I can  
21   claim some credit for it.   And it worked  
22   very, very well.

1 All we're asking for here is a  
2 little attention to the loss of competition.  
3 The 4-to-3s are gone.

4 MR. KEPLER: The other point, I  
5 think, is it's 30 years, so it's dynamic. So  
6 what you had examined at that transaction,  
7 the traffic patterns on the rails  
8 significantly changed.

9 So while you're looking at what  
10 the market is at the time, the market's  
11 significantly different in terms of the  
12 commodities that are shipped and where  
13 they're shipped. And that's part of the  
14 dynamics of how we, you know, how things get  
15 manufactured and shipped here. So it  
16 changes.

17 The fact that you've consolidated  
18 to seven carriers creates a different  
19 structure. And you put this rate structure  
20 in place when there was 20. And now our view  
21 is you've got scale in these companies,  
22 investment capability, that flexibility would



1 actually encourage more investment.

2 CHAIRMAN: And -- go ahead.

3 MR. RINE: Excuse me. Yesterday  
4 there was a lot of discussion about, you  
5 know, it would cost more money and there was,  
6 I think, an example about a balloon and you  
7 push in on one side of it. And I think the  
8 explanation about how they were going to  
9 recover that money, they would get it from  
10 another shipper, you know, it wouldn't be  
11 fair, and so forth.

12 When I appeared in the Conrail  
13 merger the Chairman of Service Transportation  
14 Board asked me a question, last all of the  
15 panel. Said if we do what you shippers would  
16 like us to do the railroads tell us they're  
17 going to go bankrupt. And I said well, the  
18 only thing I can tell you, what's in the  
19 public record.

20 Conrail testified that when they  
21 had two railroads competing, them being one  
22 of them, the rates were about 30 percent

1 less. If they had three railroads competing  
2 the rates were lower than that. And what  
3 really caught my attention was Conrail also  
4 said the last two years that Conrail existed  
5 was the most profitable years in Conrail's  
6 history.

7 And they were competing with one  
8 or two other railroads. They were profitable  
9 and they weren't going bankrupt.

10 CHAIRMAN ELLIOTT: To that point,  
11 with respect to those of you who have either  
12 facilities or clients that, where this would  
13 not be applicable, does that cause you any  
14 concern with respect to their balloon analogy  
15 that the rate increases will be pushed onto  
16 those shippers who do not have the reciprocal  
17 switching option available?

18 MR. JOHNSTON: So this is the so-  
19 called winners and losers argument, right?

20 CHAIRMAN ELLIOTT: Right.

21 MR. JOHNSTON: First of all, I  
22 think we need to recognize that in today's

1 environment there are already winners and  
2 losers. Mr. Kepler made reference in his  
3 remarks to foreign competition who are  
4 bringing goods to the United States and have  
5 choices that American manufacturers do not.

6 And I would suggest that to some  
7 degree the current regime is creating winners  
8 and losers, and in some cases those winners  
9 are foreign companies and foreign governments  
10 and foreign workers to the detriment of U.S.  
11 manufacturers and U.S. workers and the  
12 benefit to the U.S. economy.

13 The other observation that I would  
14 have is that some improvement in competition  
15 is better than no improvement in competition.  
16 And so while some will benefit and others  
17 will not, it's time to begin walking down  
18 this road and this is a way to start.

19 MR. KEPLER: Yes, I would say it's  
20 not too clear to us that we're going to be  
21 competitively advantaged. And as I  
22 mentioned, a lot of our stuff will still be

1 captive. But I think the idea that we're  
2 working towards a system that has flexibility  
3 is very important.

4 I think the other thing to  
5 recognize is that shipments aren't static.  
6 So, I mean, we have 30 percent rail turnover  
7 a year in terms of where we ship to based on  
8 the customer. So what may be competitively  
9 advantaged today may be disadvantaged  
10 tomorrow. And that's the dynamics of just  
11 how the value change work here.

12 So I think what we're looking for  
13 is something that kind of makes things  
14 flexible and clear and transparent, and that  
15 can be done on a transaction basis from a  
16 shipper to a carrier. And ultimately that  
17 puts a better environment for everybody to  
18 compete in.

19 MR. MORENO: I think it's also  
20 important to understand that the advantage  
21 that foreign producers obtain occurs even if  
22 those foreign producers still have to use our

1 U.S. rail system once they come into the  
2 country because they have a choice of which  
3 port of entry they come into and, therefore,  
4 which railroad they use.

5 And therefore, they have that  
6 competition that competitive switching would  
7 provide to domestic producers.

8 CHAIRMAN ELLIOTT: One final  
9 question. Mr. Kepler, you raised, I thought,  
10 and interesting point. And I haven't really  
11 heard it discussed a lot in the proceeding  
12 but you mentioned that there are other  
13 routes.

14 You mentioned, the carriers  
15 mentioned the inefficiency from the  
16 switching, but you mentioned that there were  
17 inefficiencies on the longer haul portions  
18 where you use more inefficient routes. And I  
19 believe Ms. Dearden also mentioned that.

20 Is that a common occurrence or is  
21 that just anecdotal?

22 MR. KEPLER: I think it's, you

1 know, back to the point on where, with the  
2 airline. I'm not always sure that's a good  
3 metaphor but, I mean, a carrier will, an  
4 airline will try to keep you on the same  
5 plane regardless of how, or same system  
6 regardless of how efficient that is.

7 And that's what happens here. So  
8 when you look at the boundary issues of where  
9 we ship, especially if you do it nationally,  
10 and you look at what the best route is, it's  
11 the long haul can get optimized if you look  
12 at it from a holistic point of view.

13 So now when we did the value chain  
14 around Louisiana those are the two or three  
15 manufacturing facilities that go all around  
16 the country. And we would have similar  
17 models, I think, in other aspects.

18 I think also, from the safety  
19 point of view, both, everybody should be  
20 trying on the hazardous side which is a small  
21 percentage of what we ship to minimize the  
22 route miles. This system doesn't encourage

1       that because you end up going with a carrier  
2       that optimizes around themselves.

3               So, no, I think it is a very  
4       predominant thing that we need to look at.

5               CHAIRMAN ELLIOTT: I know that Dow  
6       did not submit lengthy comments, more of a  
7       supportive letter, but was there any data put  
8       in the record with respect to the longer  
9       routes being used in these situations? I  
10      cannot recall that.

11              MR. KEPLER: We can --

12              CHAIRMAN ELLIOTT: I'm not --

13              MR. KEPLER: -- speak with the  
14      ACC. We can, yes.

15              CHAIRMAN ELLIOTT: No, I'm not  
16      asking for additional data. I'm just saying  
17      is there any in the record I could look at  
18      now. I do not want to reopen this record.

19              MR. KEPLER: Yes, we'll go, I  
20      think we did so I'll go back and try to get a  
21      reference for you.

22              CHAIRMAN ELLIOTT: Okay, thank you

1 very much. Okay, thank you very much for  
2 your testimony. We greatly appreciate it.  
3 And I believe we have our final panel, which  
4 I believe has been cut down to one party.

5 Okay, Mr. MacDougall, I believe  
6 you are our last party.

7 MR. MACDOUGALL: Perhaps  
8 everything's been said. Who knows. I'm here  
9 on behalf of Samuel J. Nasca who is the New  
10 York State Director, Legislative Director for  
11 the UTU.

12 As we stated in our comments that  
13 UTU has merged with the sheet metal workers  
14 but it's in the process of a fender bender,  
15 that merger. And so there may be further  
16 name changes and so on at the conventions  
17 this June and August.

18 One thing I'd like to concentrate  
19 on, if you'll excuse me, with is the absence  
20 of any information in this record as to the  
21 effect on employees. We raised that. So did  
22 KCS, Norfolk Southern and CSX.



1                   And taking a legalistic  
2                   standpoint, that's very difficult for me to  
3                   see how you can go forward with the specific  
4                   employee protection and the issue in the  
5                   statute, section in the separate subsection  
6                   C2 when the NIT League says well, we'll just  
7                   wait until you have your notice of proposal  
8                   with NIT League.

9                   And it seems to me that where the  
10                  statute specifically says things they have  
11                  not met their burden of proof. And they have  
12                  all kinds of experts and they can have  
13                  consultants and they can make some estimates  
14                  as to what the impact will be or likely to be  
15                  on rail employees.

16                  And that defect, I think, is just,  
17                  this is monumental, how anybody can prepare a  
18                  case when the statute says certain things. I  
19                  might add that in the C1 there's the  
20                  reference to the public interest.

21                  You can prescribe these things on  
22                  the public interest or it can be competition.

1 And the impact on rail employees is a factor  
2 of the public interest. That's been in a  
3 number of Supreme Court decisions. It's not,  
4 I mean, it's a separate thing but that the  
5 failure of proof come with anything on an  
6 employee impact, I think, defeats the  
7 petition for rulemaking.

8           You may want to defer certain  
9 things like the 75 percent rule, something  
10 like that, for rulemaking. But you cannot  
11 afford a specific statutory requirement.

12           And one other thing, another thing  
13 that I'll conclude with, that's come to my  
14 mind watching this for the last two days, I  
15 want to point out that I think the Board  
16 lacks expertise in dealing with yards. And  
17 why is that?

18           The reason for it is that by  
19 Section 109.06, you are not to consider the  
20 construction, operation, abandonment or  
21 discontinuance of switching tracks. And as  
22 the result of that, the past, that's been

1       given to the state commissions.

2                       Now nobody has it. You were  
3       trying to set up a consumer advocate thing,  
4       people can enquire about problems they have  
5       in the yards. But over the years you have  
6       not become involved very much in yard works,  
7       in yard operations.

8                       And therefore, there's a lot of  
9       questions, a lot of discussions and a lack of  
10      knowledge, really, on your ability to  
11      administer such a rulemaking. And this has  
12      happened ever since 1920. You never had  
13      jurisdiction over the yards.

14                      And therefore there's a lot of  
15      questions, how does it work. Well, it's  
16      complicated. It's, you know, if you have  
17      worked on a railroad you know what yards are.  
18      It's a complicated thing.

19                      And about 25 percent of all the  
20      Train and Engine wages paid is in four switch  
21      groups. And that doesn't even include trains  
22      that are operating in and out of yards or

1       away trains.

2                       So yards are an important thing.  
3       And when you wanted to find out about yards  
4       in the Powder River Basin you sent some of  
5       your staff out there, at the invitation of  
6       the rest of us, to look at yard operations  
7       out there in Montana.

8                       So there's this lack of  
9       experience. Now you do, you have had some,  
10      read cases and other cases involving yards.  
11      I've been a practitioner for over 50 years.  
12      There's been a certain number of them, but  
13      it's not the basic work that you've done in  
14      the railroad industry because it's been  
15      excepted from your jurisdiction. Thank you.

16                      CHAIRMAN ELLIOTT: Just one  
17      question. With respect to the labor  
18      protection that is mentioned in the statute,  
19      is there any type of labor protection that  
20      you would propose or recommend?

21                      MR. MACDOUGALL: Well, I've  
22      thought about that and it came to my mind

1     that, of course, the Legislative Department  
2     of the organization doesn't get into those  
3     protectionist issues. And so the answer has  
4     to come if they assign a Vice President, if  
5     it goes forward.

6             But it would appear that in the  
7     terminal situation there would be problems of  
8     New York Dock and N&W, conditions that would  
9     be the things which you might pattern things  
10    after. As for the line haul, which is very  
11    serious, like if you have an operation from  
12    Powder River Basin, yet at that the  
13    destination power plant there's a terminal 30  
14    miles away with another carrier you're going  
15    to have a big employee protection bill,  
16    something like that.

17            And that would be more like the  
18    Oregon Short Line or that I say this is out  
19    of my expertise, out of my authority actually  
20    and it may be that they have to fashion some  
21    special rules like they did at the Wisconsin  
22    Central rulemaking for Class II acquisitions

1 of certain short lines.

2 CHAIRMAN ELLIOTT: Thank you, Mr.  
3 MacDougall. I'm glad that the fire alarm  
4 didn't go off this time in the middle of your  
5 testimony. Do you have anything there?

6 Well, I have about two and a half  
7 hours of closing remarks so -- no, thank you  
8 very much everyone for coming to a two-day  
9 hearing. I know that's a large commitment  
10 and we greatly appreciate it.

11 We also appreciate what our staff  
12 has done by bringing this together today.  
13 It's been quite an undertaking. And we will  
14 take the testimony and comments under  
15 advisement.

16 And the hearing is hereby  
17 adjourned. Thank you.

18 (Whereupon, the hearing in the  
19 above-entitled matter was concluded at  
20 12:29:18 p.m.)

21  
22

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C E R T I F I C A T E

This is to certify that the foregoing transcript

In the matter of: PETITION FOR RULEMAKING TO ADOPT  
REVISED COMPETITIVE SWITCHING RULES

Before: STB

Date: 03-26-14

Place: Washington, DC

was duly recorded and accurately transcribed under  
my direction; further, that said transcript is a  
true and accurate record of the proceedings.

  
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Court Reporter

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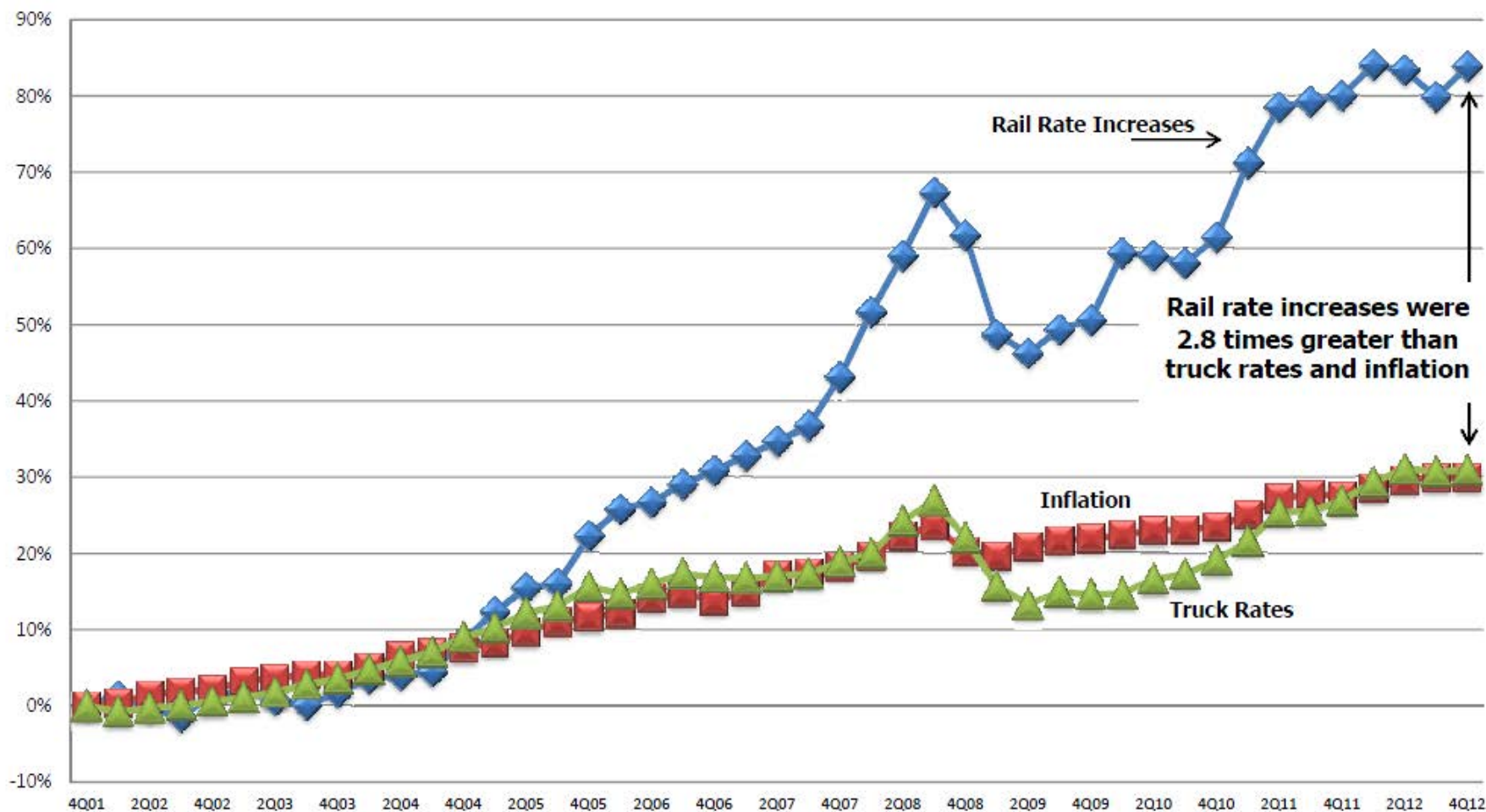
(202) 234-4433

[www.nealrgross.com](http://www.nealrgross.com)

Ex Parte No. 711  
Petition for Rulemaking to Adopt  
Revised Competitive Switching Rules

Testimony of the  
American Chemistry Council  
March 26, 2014

## Rail Industry Consolidation has Allowed Railroads to Increase Rates Dramatically More than Inflation and Trucking



The number of large railroads in the US have reduced from 26 in 1980 to only 7 by 2001. Following 2001 the percent increase in Rail Rates on the Big Four U.S. railroads has been 2.8 times greater than Inflation and Long Haul Trucking

# Analysis of Freight Rail Rates for Chemical Shippers

The premium paid by chemical shippers for rates above 180% RVC totaled more than \$3.9 billion in 2010

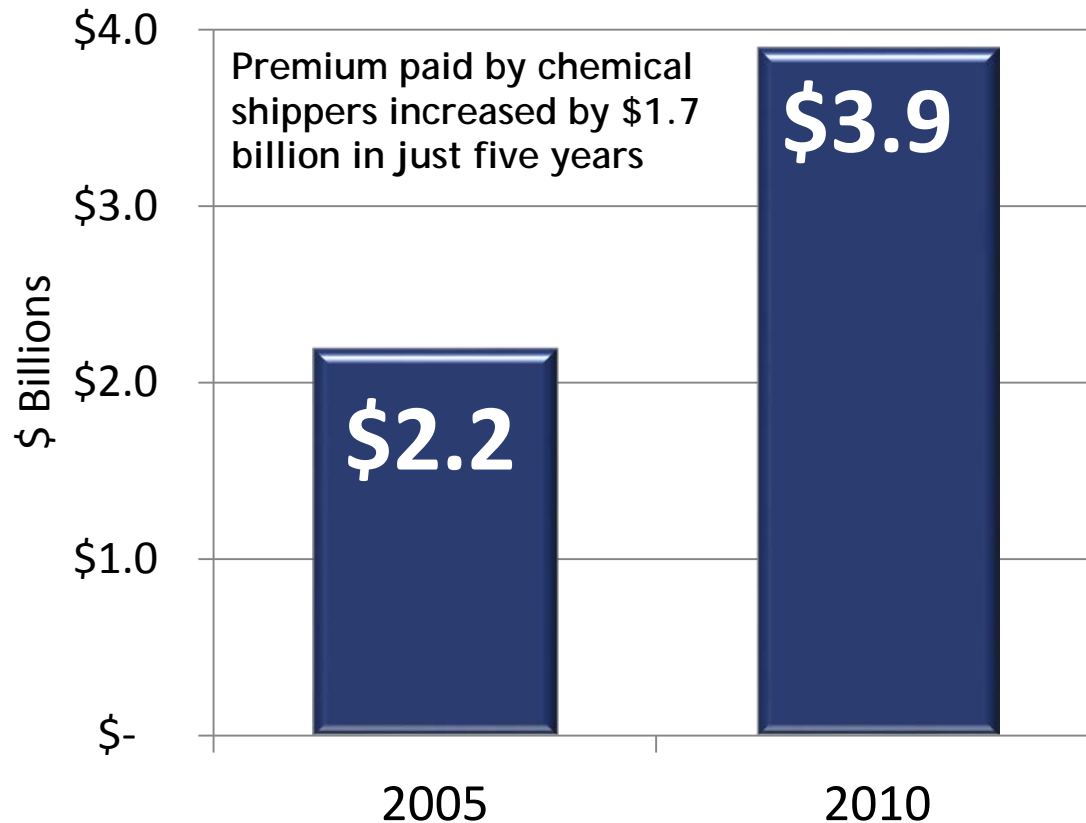


## \$3.9 Billion Cost to Chemical Shippers

RVC Range	% Total Carloads	Premium for Rates above 180% RVC
<180	24.7%	--
180-240	23.0%	\$402,945,412
241-299	16.7%	\$665,473,520
>300	35.6%	\$2,880,710,533
Total	100.0%	\$3,949,129,465

# Analysis of Freight Rail Rates for Chemical Shippers

From 2005 to 2010, the cost premium for chemical shipments increased substantially

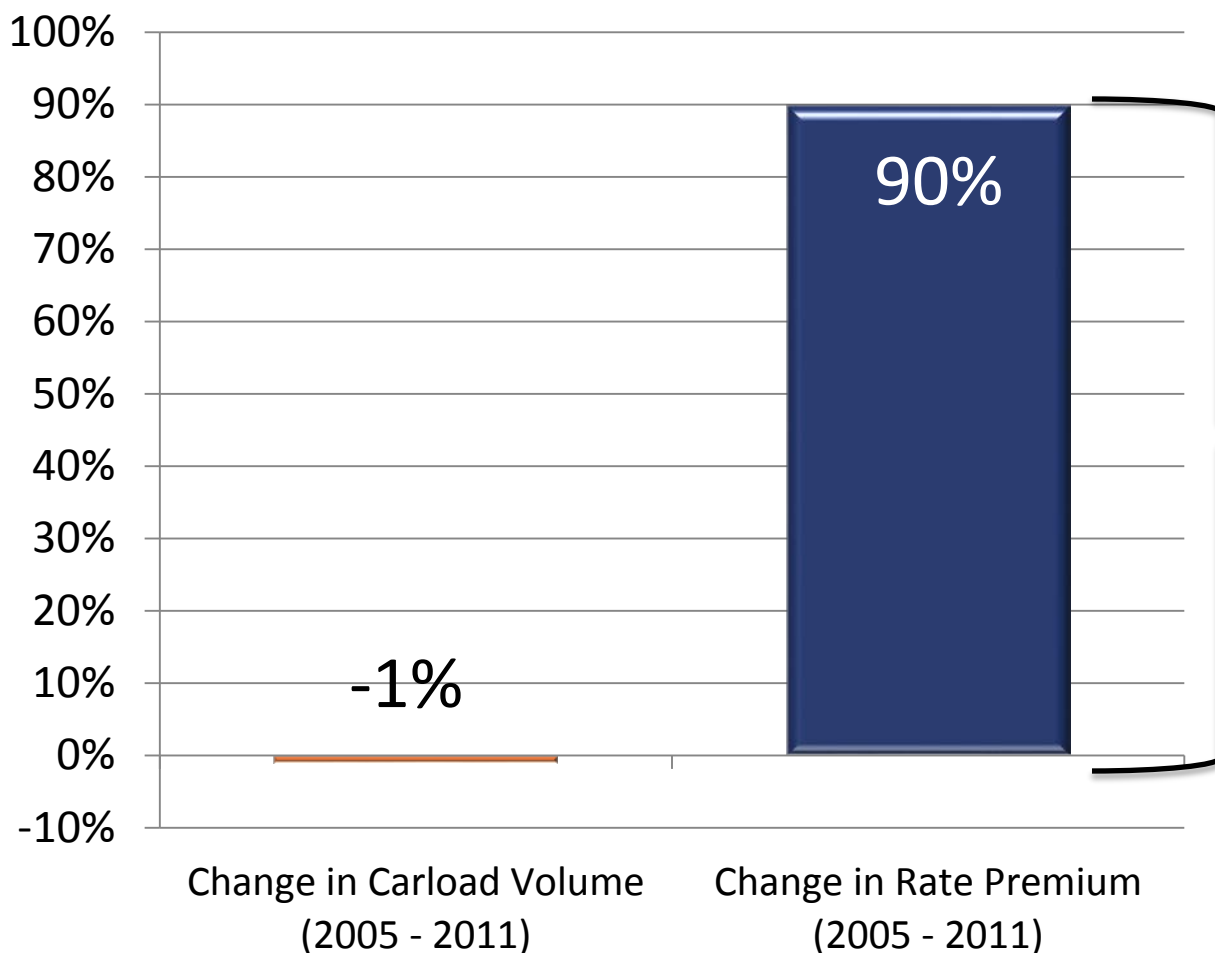


## From 2005 to 2010:

- The number of carloads that moved at rates below 180% RVC dropped from 40% to only 25%.
- The number of carloads above 300% RVC increased from 25% to over 35%

# Railroad Pricing Power - Not Demand or Costs - Is Driving Rates Higher

What other industry can get away with charging much higher prices even as demand drops?

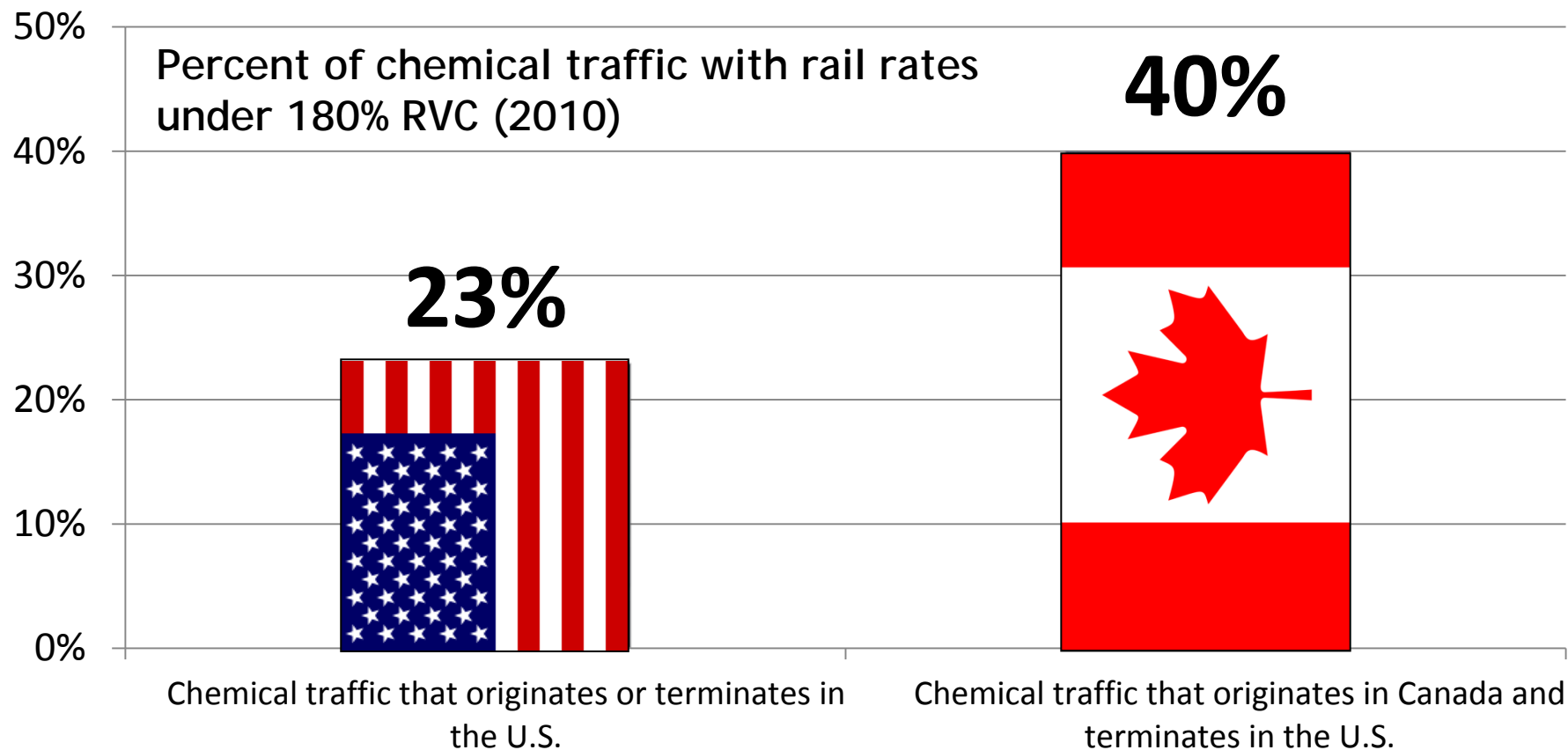


**The Common**  
**Sense Gap**  
Competitive  
markets simply do  
not work like this



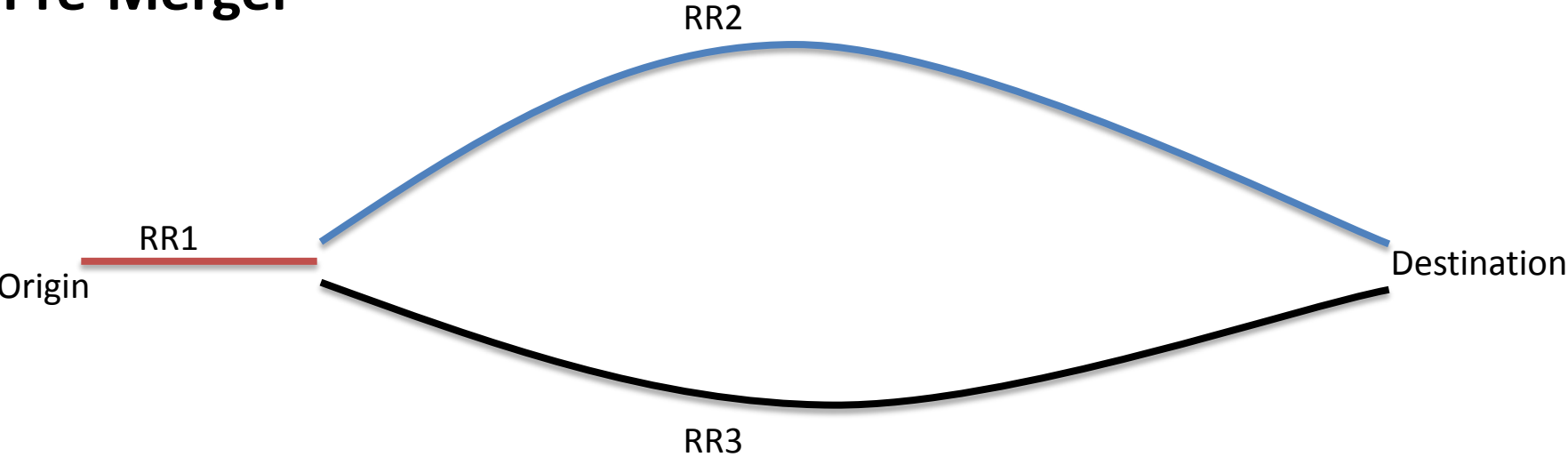
# Analysis of Freight Rail Rates for Chemical Shippers

Canada's policies allow for more rail competition – enabling chemical producers to ship at lower rates and providing Canada with a substantial competitive advantage

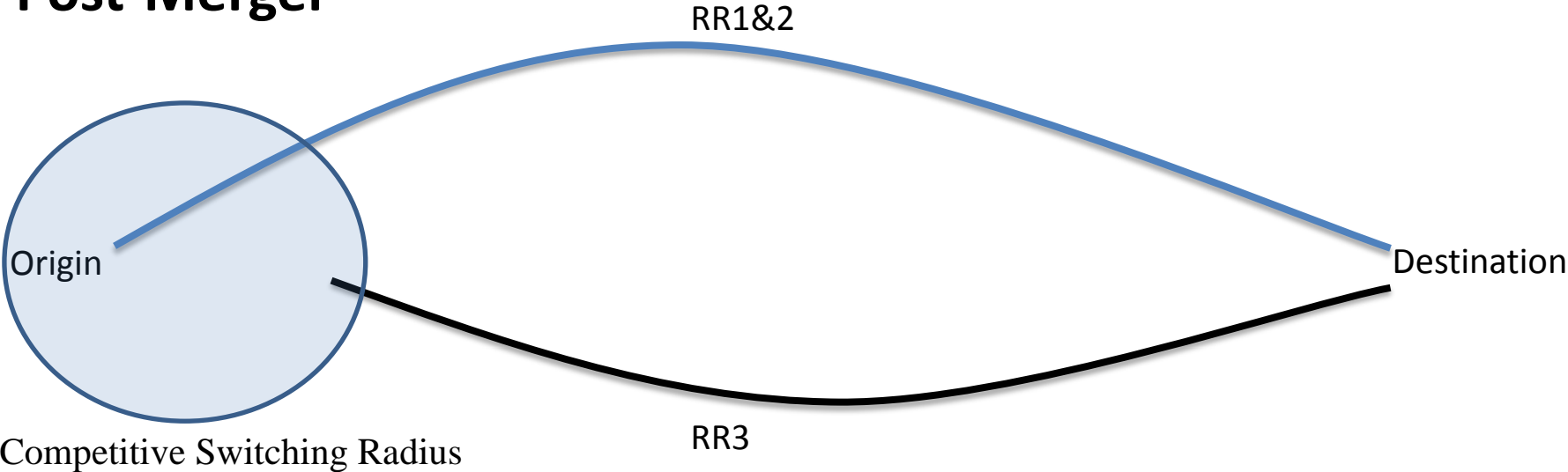


# Pre-Merger

218



# Post-Merger



# STB Hearing: Ex Parte No. 711

## Testimony of BNSF Railway Company

Jill Mulligan, Associate General Counsel

March 26, 2014

# Key Principles

---

- **The Board should promote competition by allowing market forces to govern. Regulatory intervention should be limited to addressing actual abuses of market power.**
- **Reliance on R/VCs to measure market power—much less market abuse—is invalid and disincentivizes efficiency investments.**
- **Movements not subject to STB regulation could not be subject to the NITL switching regime.**
- **The Board cannot ignore the effect of reciprocal switching remedies on market dominance in rate reasonableness cases.**





## ***NS Line Haul Mile Per Day (LHMpD) Study***

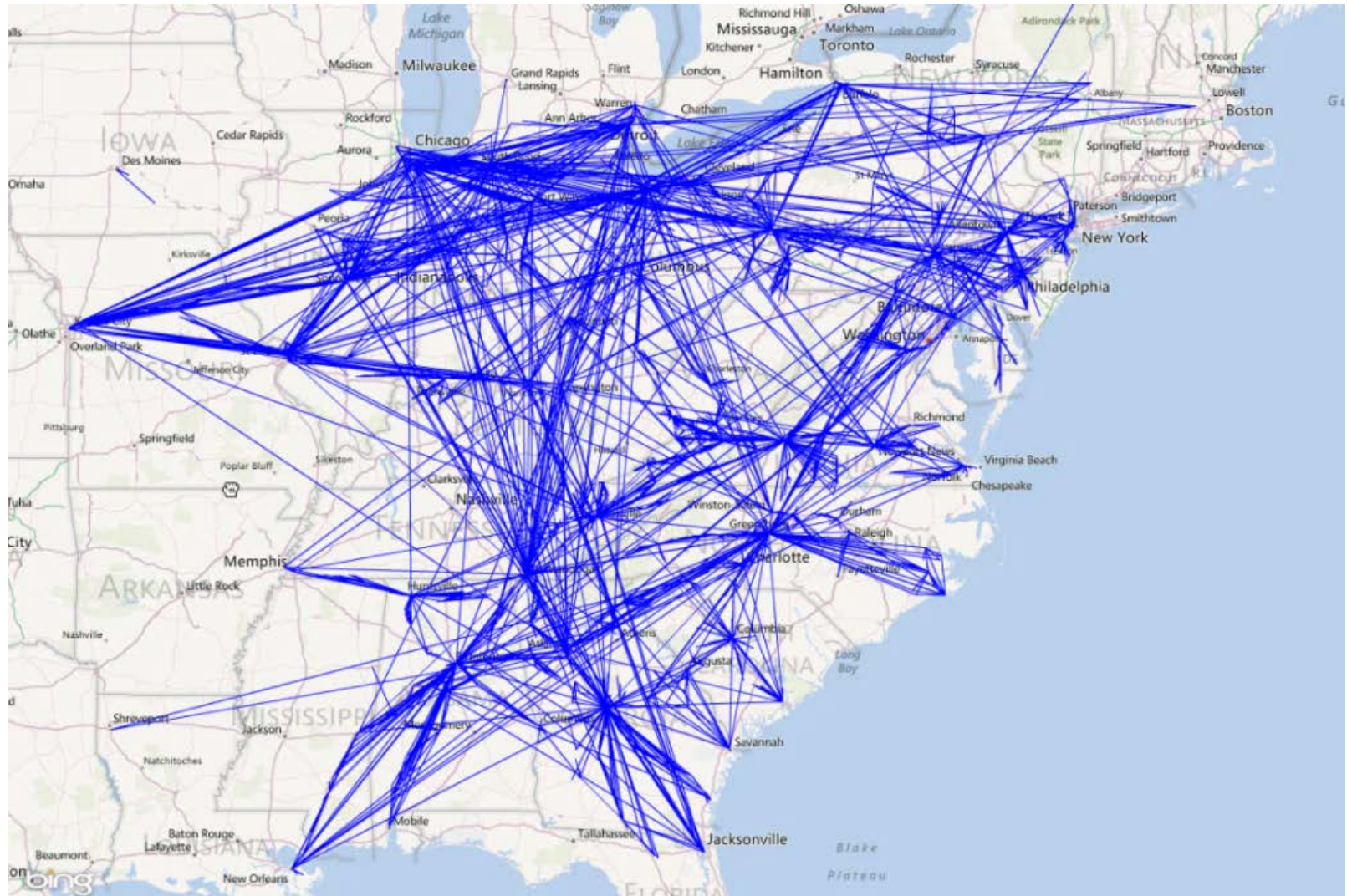
*Rush Bailey, Assistant Vice President Service Management*

*STB Hearing on Ex Parte 711*

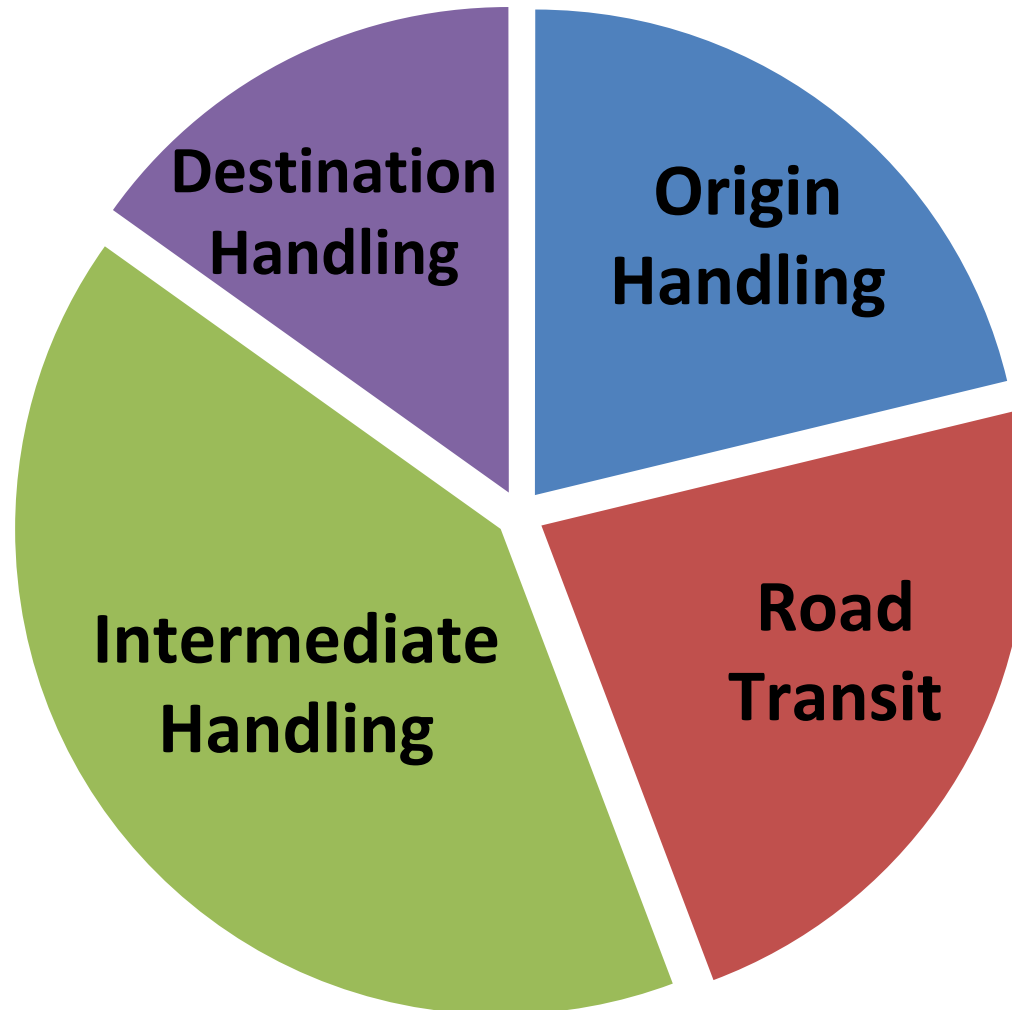
*March 26, 2014*



# NS ROAD HAUL AND LOCAL BLOCKING NETWORK

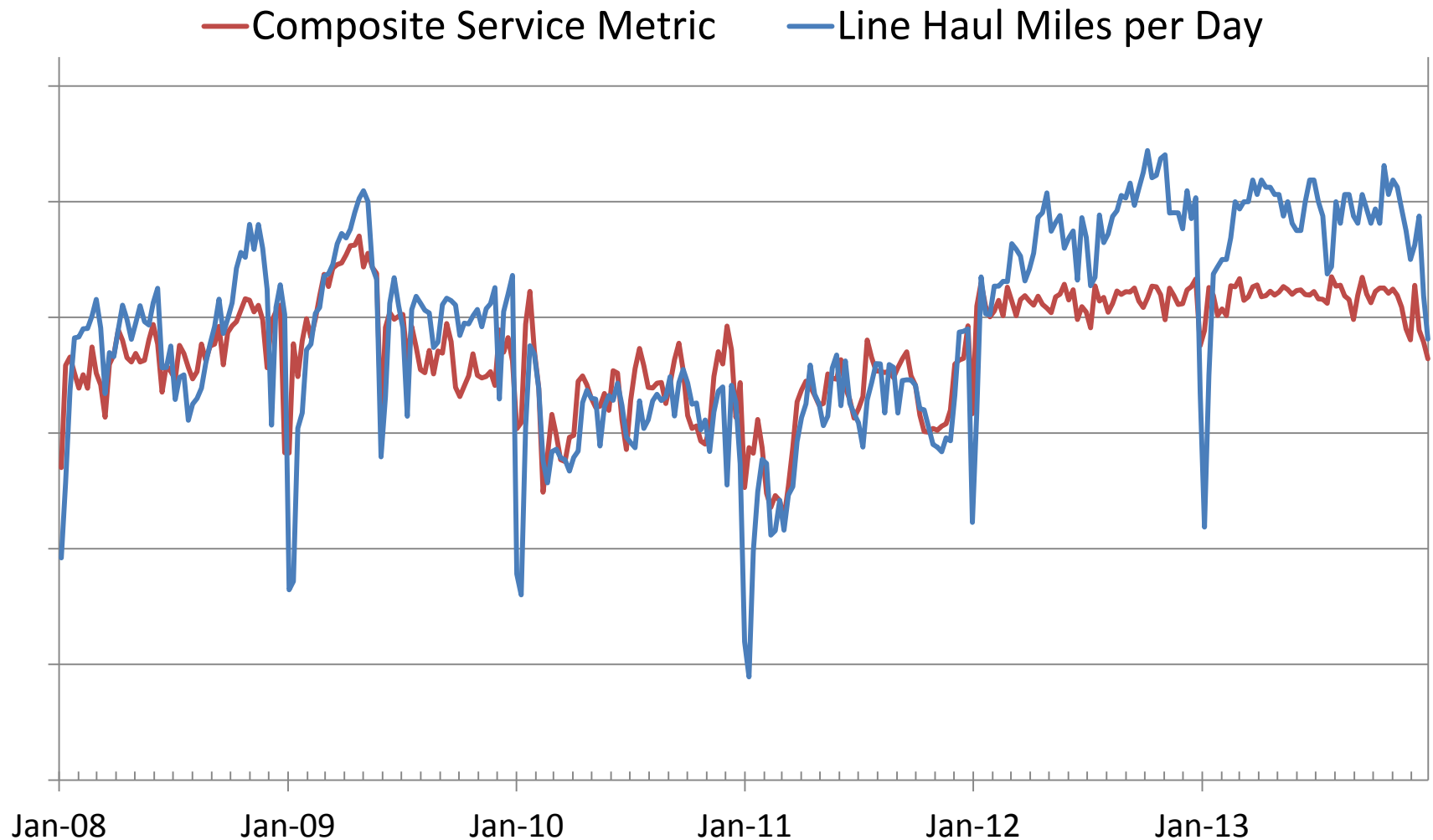


# ***MERCHANDISE TRANSIT CYCLE TIME ALLOCATION***

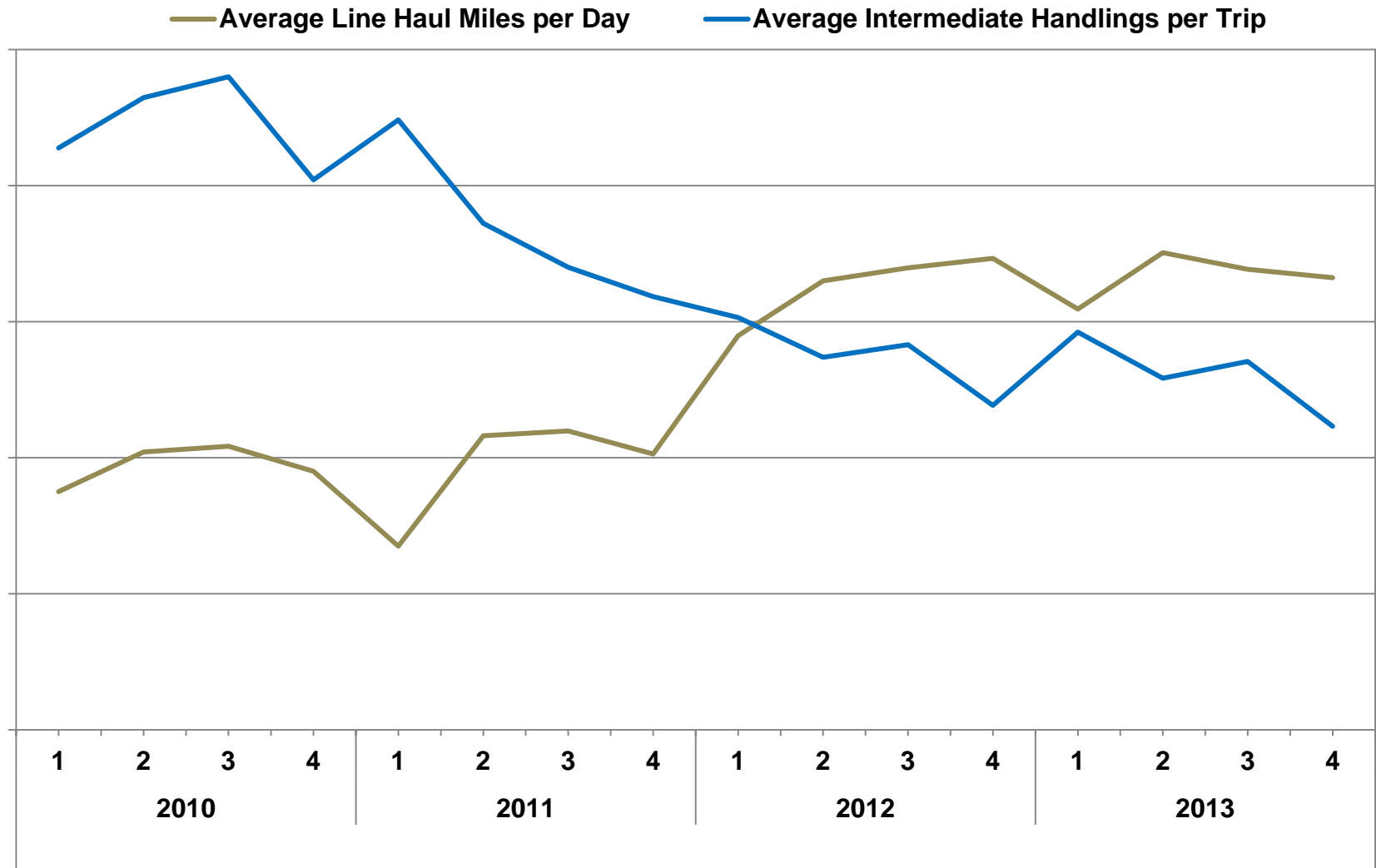




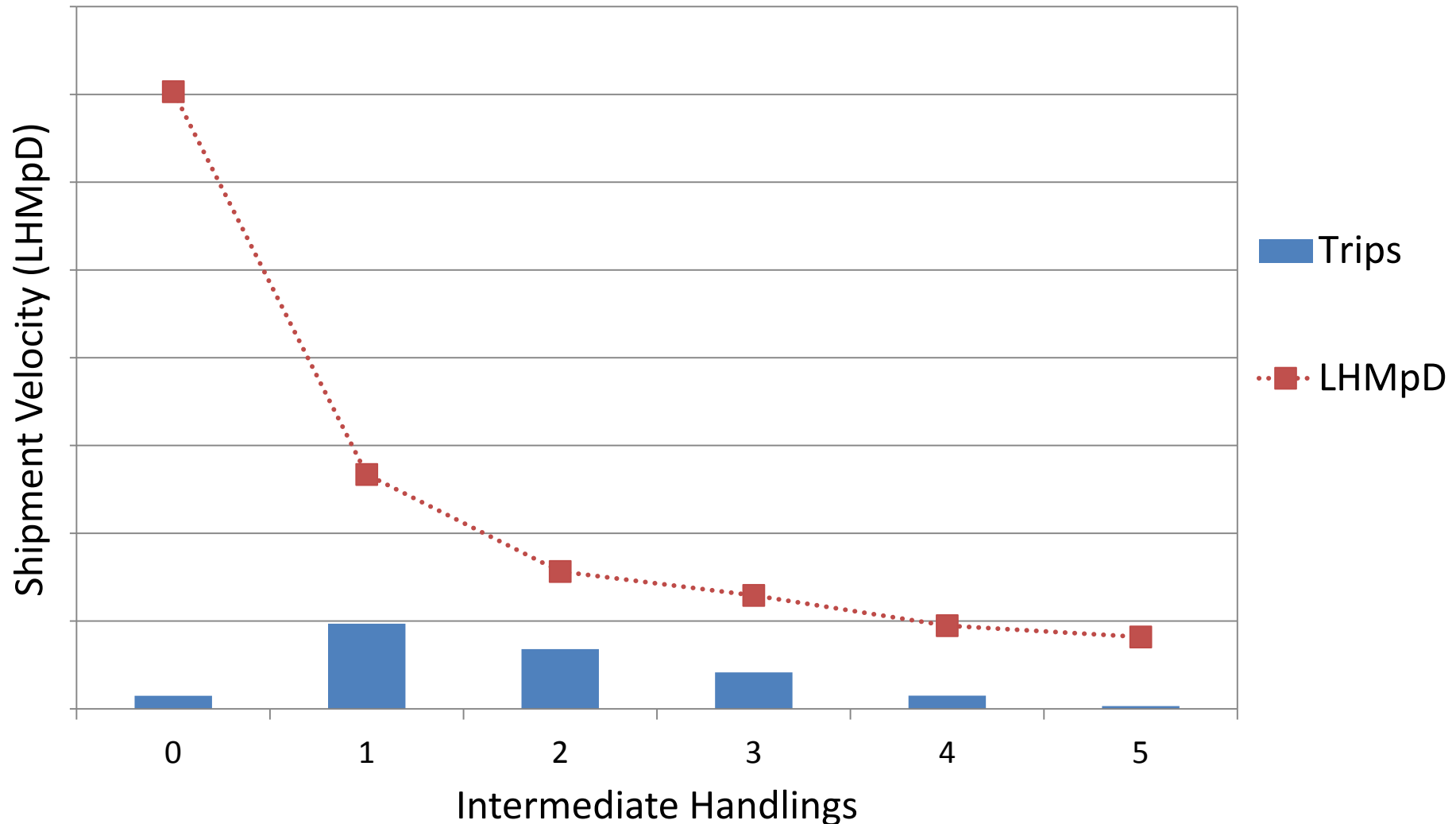
# COMPOSITE SERVICE AND LHMPD – 2008-2013



# SHIPMENT VELOCITY V. INTERMEDIATE HANDLINGS

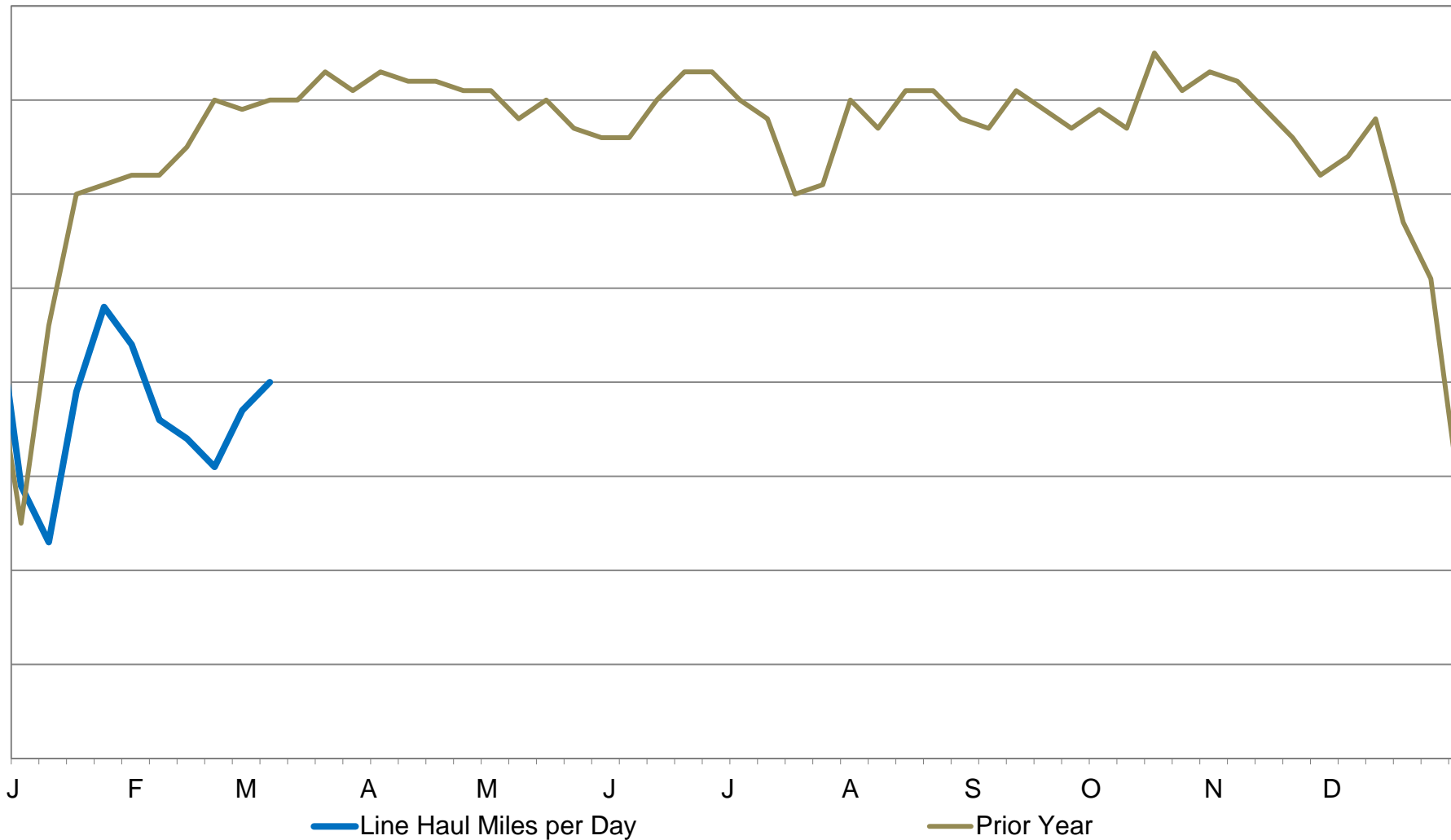


# SHIPMENT VELOCITY AND NUMBER OF INTERMEDIATE HANDLINGS



# Line Haul Miles Per Day (Network Velocity)

2014\* vs. 2013



\* Through week ending March 7



# CSX Transportation Ex Parte 711 Comments

Cressie Brown, VP Service Design



# *It starts with the customer and CSX is listening*

Over 2,500  
third-party  
independent  
**customer surveys**  
annually



**Customer  
Advisory  
Councils** for  
all markets



Over 4,000  
annual **customer  
site visits**



Frequent  
cross-functional  
**Service  
Excellence**  
meetings across  
the network



**Customer  
Focused  
Culture:**  
All employees,  
every day



Customers tell us: "Service is paramount"

# *CSX is responding to the voice of the customer*

## Service Predictability

- ***“Consistency of service is a top priority”***
- Improving transit times and service reliability

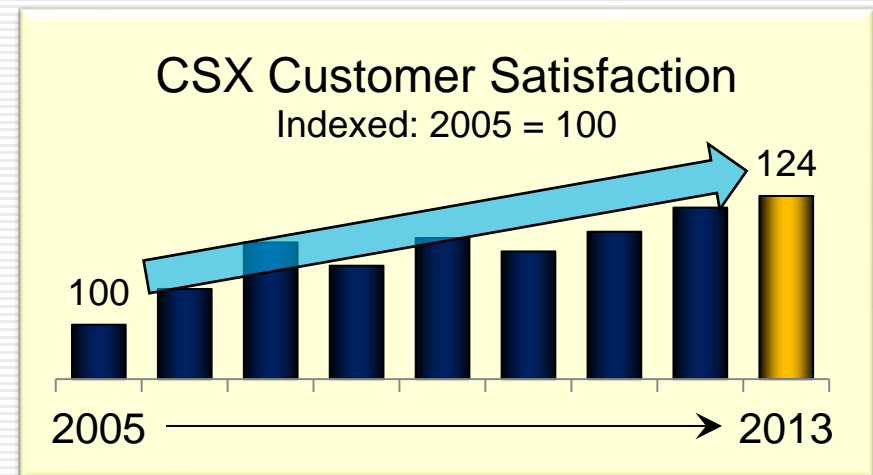
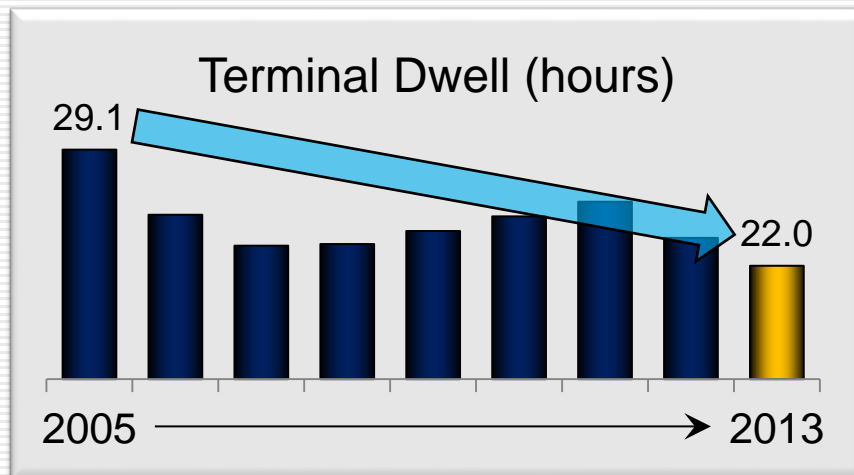
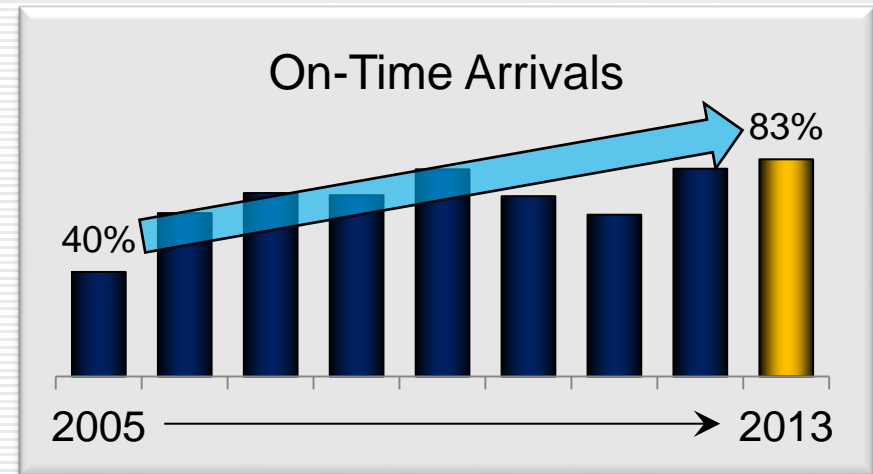
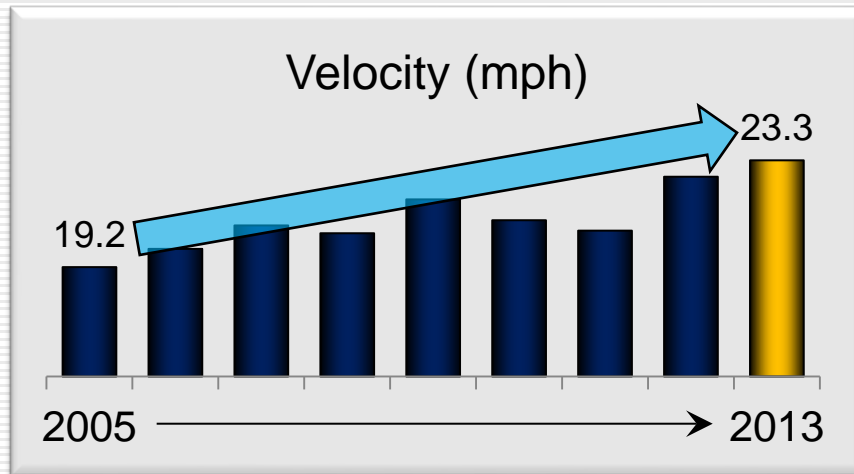
## Enhanced Efficiency and Asset Utilization

- ***“As cars sit, we lose money”***
- Driving improved railcar utilization for customers & CSX

## Improved Communication and Coordination

- ***“Proactive notification for planning and results”***
- Providing information for customers to plan resources

# Service gains demonstrate customer commitment





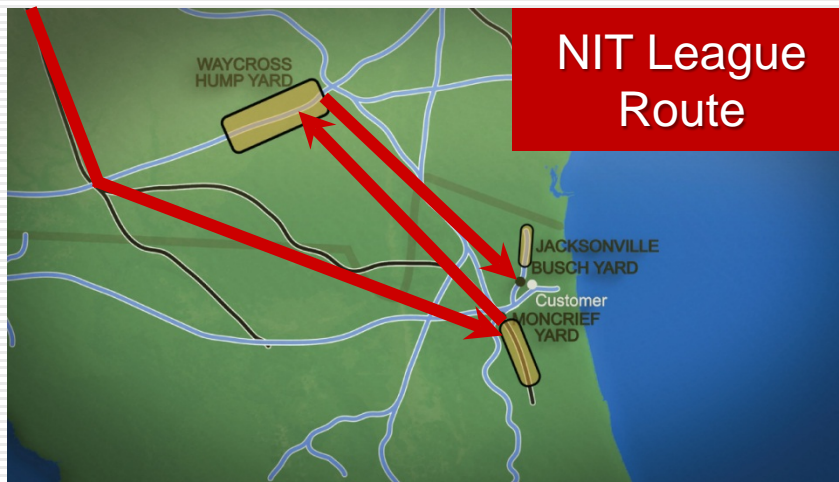
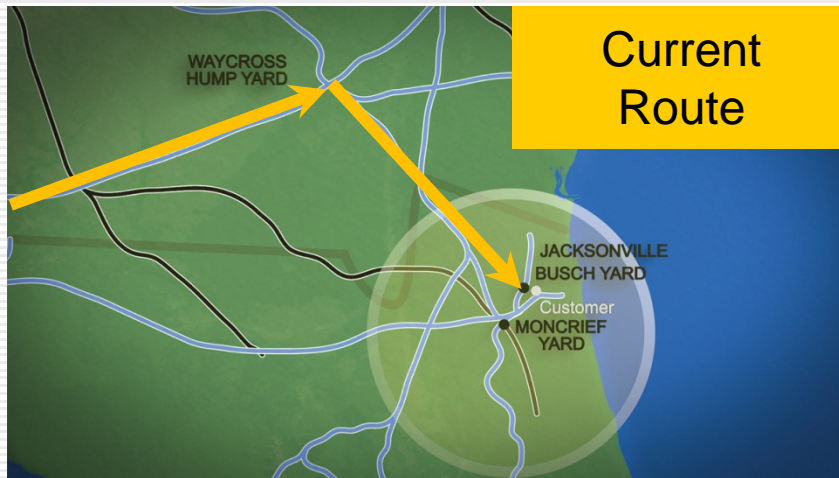
# *NITL proposal threatens to disrupt hump efficiency*

## CSX Hump Yards



- Carload traffic flows rely on hump yards for processing
- Hump yard “hubs” are safe, efficient and reliable
- NITL assumes all interchange locations can act as hubs
  - *Smaller yards rely on less efficient flat switching*
  - *Often, capacity doesn’t exist*

# Potential outcomes: Jacksonville carload example



- Reduced efficiency of hump yard processing
  - *Forces traffic to small interchange location, out of route to hump and back to local yard*
- Increases transit by three days and nearly 300 miles
  - *Creates inefficiency and uncertainty*
- Disrupts critical first mile - last mile service
  - *Cars already spend 50% of time in local service*

# *Proposal also threatens unit train predictability*

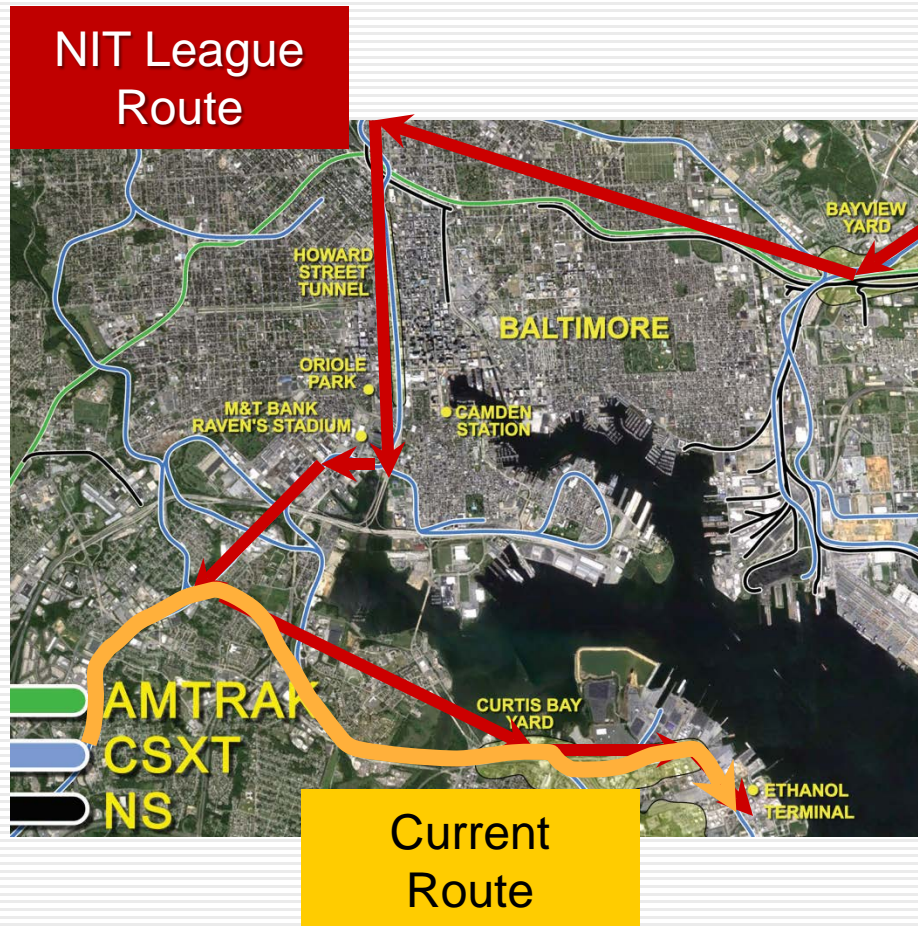
## Unit Train Business



- Unit train service requires planning, predictability
- Routing depends on most direct path, current traffic mix
- Proposal brings disruption to tightly coordinated network



# Potential outcomes: Baltimore unit train example



- Proposal could force traffic over indirect, congested routes
  - *CSX wouldn't be able to regulate traffic flow from other rails*
- Creates congestion with far-reaching consequences:
  - *Baltimore effect is likely to extend beyond the local area*
  - *Passenger traffic impacted*



# Summary

## Service Predictability

- Railroading is a network operation that relies on density, efficiency and predictability

## Enhanced Efficiency and Asset Utilization

- Forced switching would create less reliable, less efficient service for customers

## Improved Communication and Coordination

- Proposal introduces uncertainty and unpredictability, driving costs up

NITL proposal risks turning back the clock on decades of customer service gains



# Ex Parte 711 Hearing

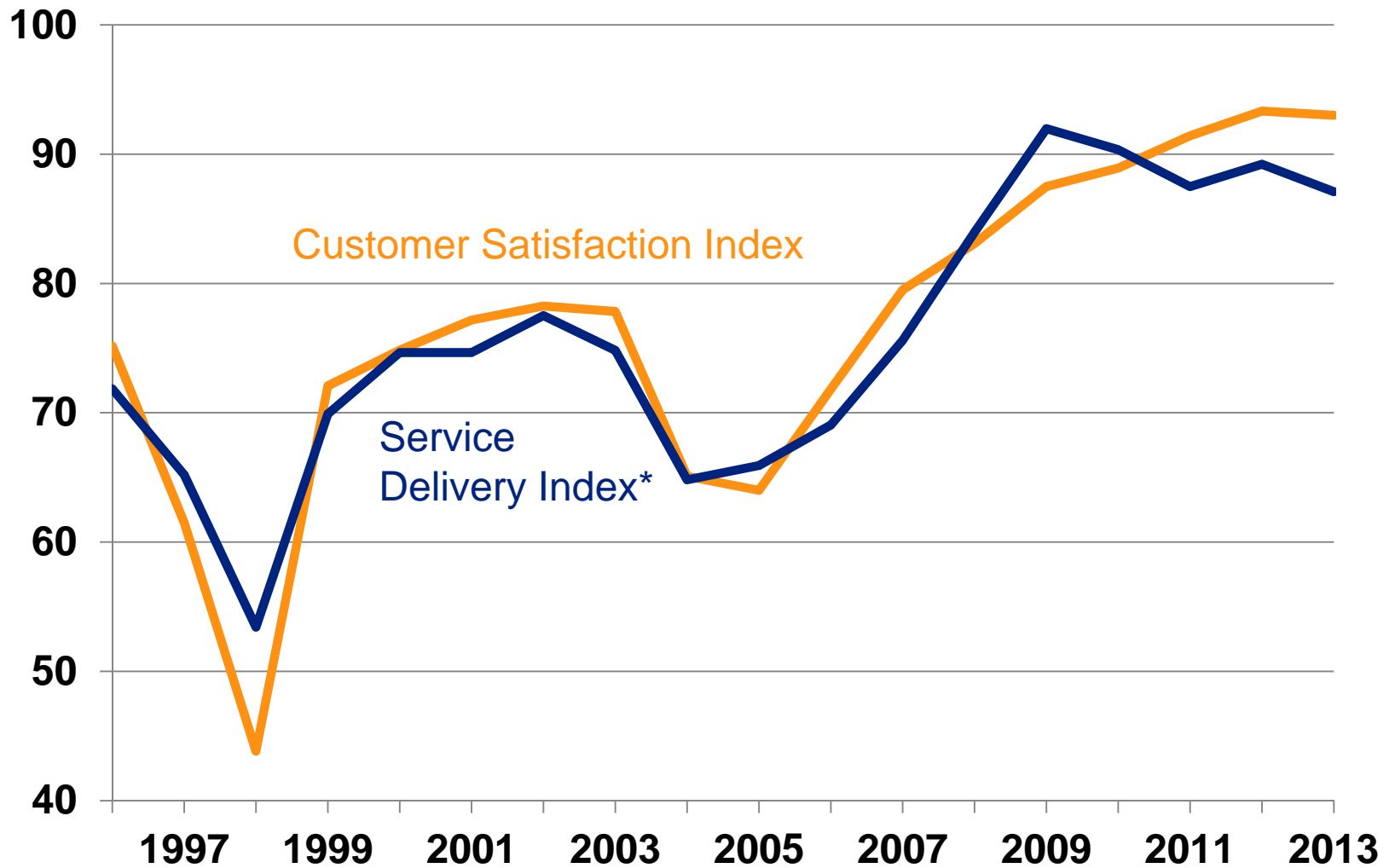
**Tom Haley, Assistant Vice President -  
Network and Capital Planning**

**March 26, 2014**



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# Service Drives Customer Satisfaction



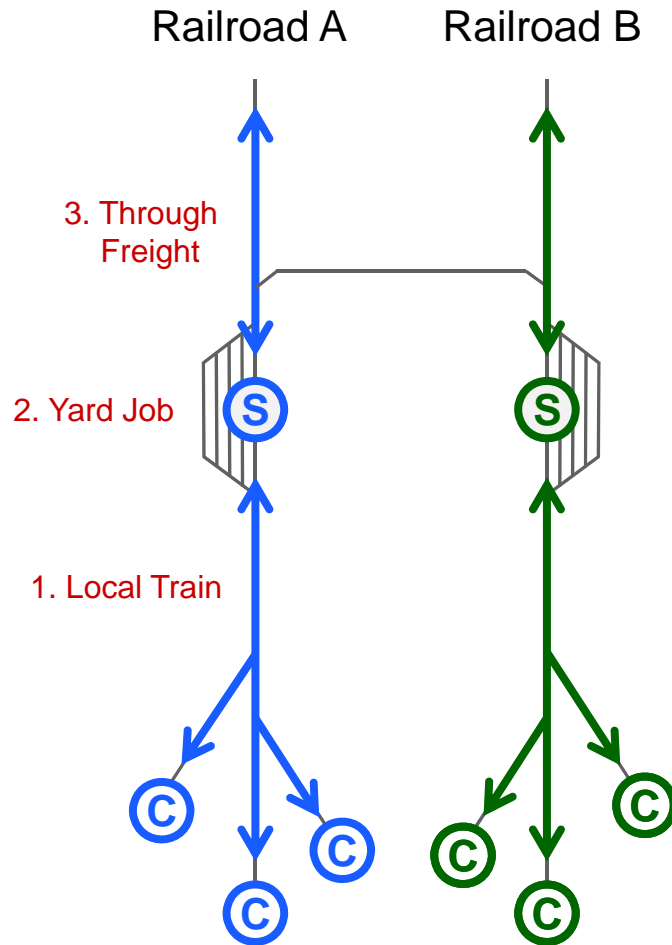
# NIT League Proposal Threatens Progress

- **Increases workload in constrained terminal areas**
- **Degrades service across the network**
- **Limits ability to plan and manage the network**
- **Increases need for capital investment while reducing ability to invest**

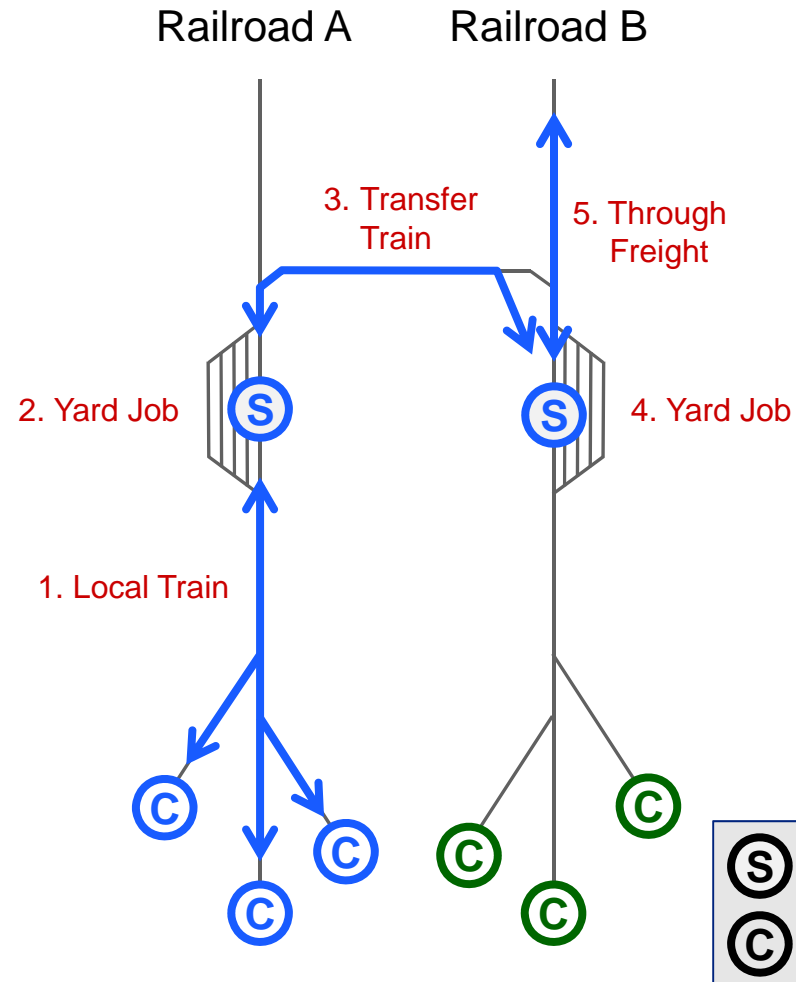


# Direct Service is Clean and Efficient

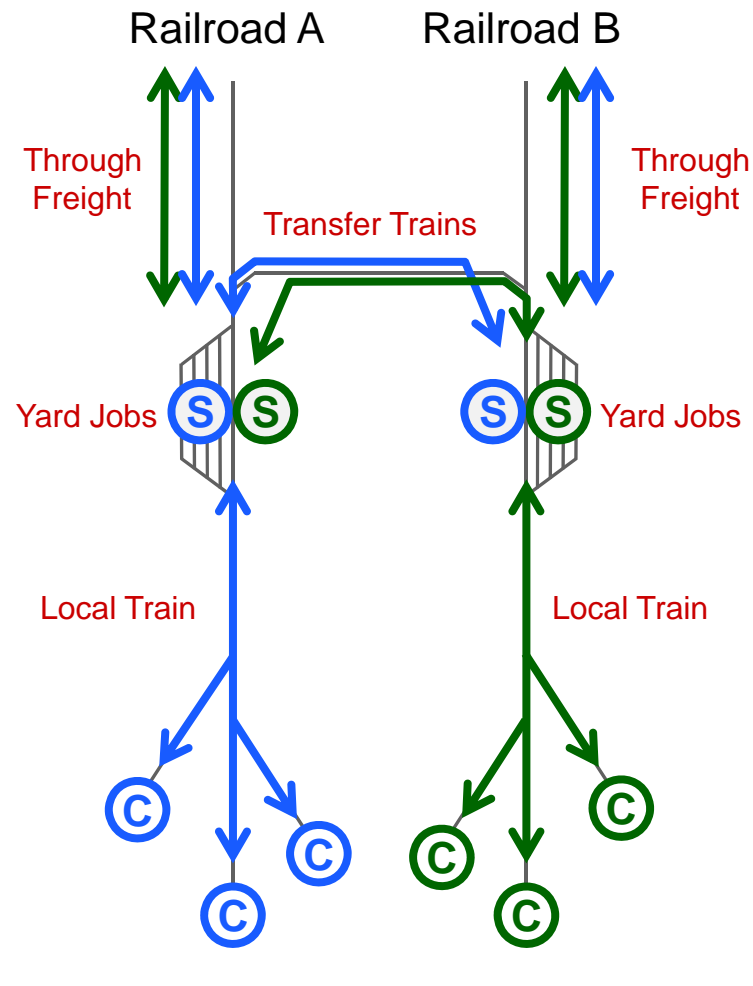
## Direct Service



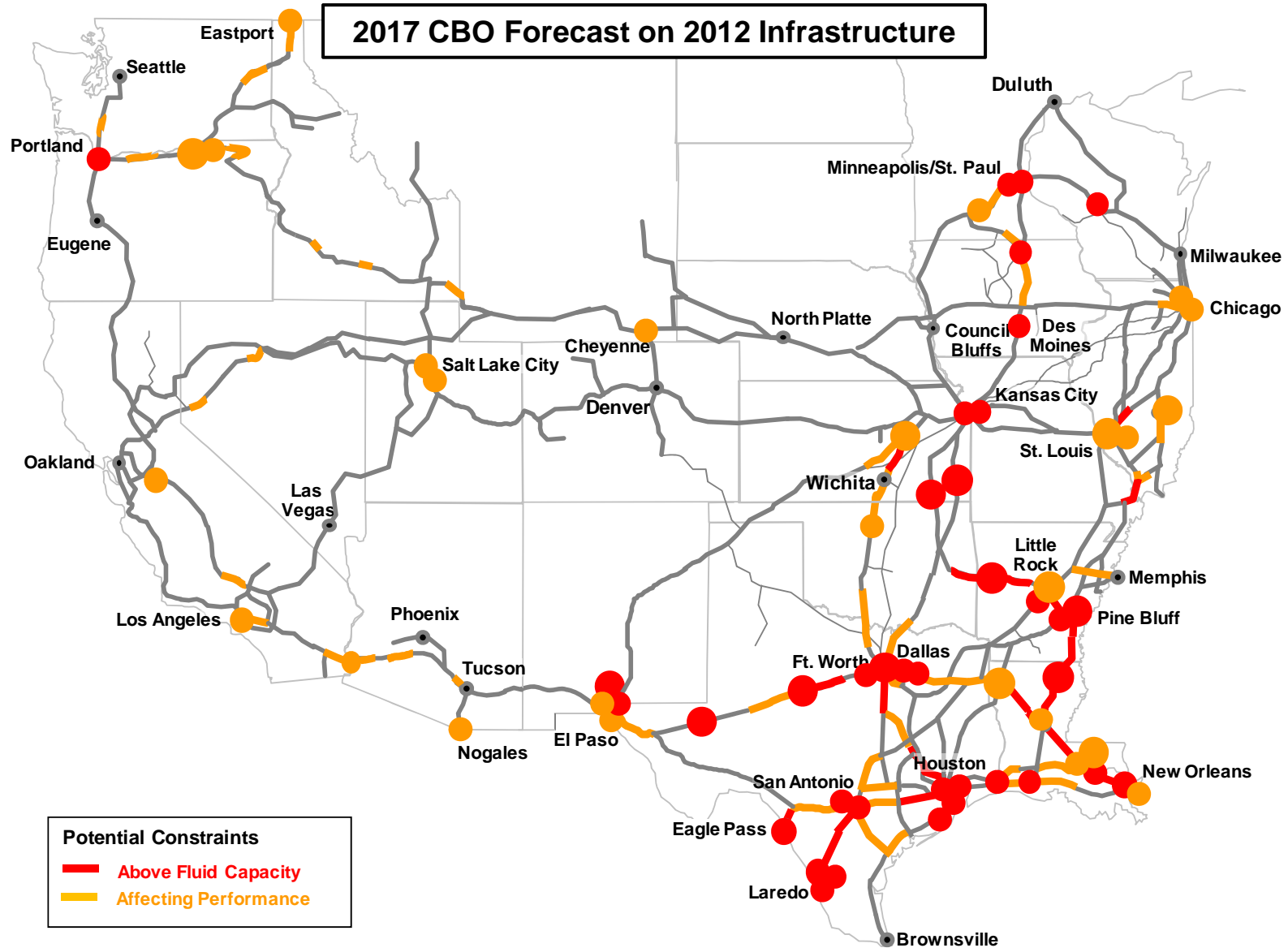
## Reciprocal Switch



# Reciprocal Switch Adds Work and Complexity

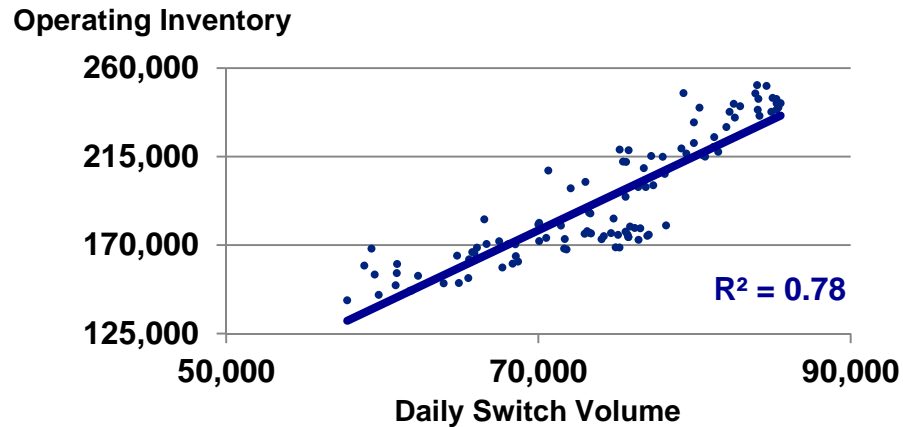


# Network Capacity



# Additional Switching Degrades Service

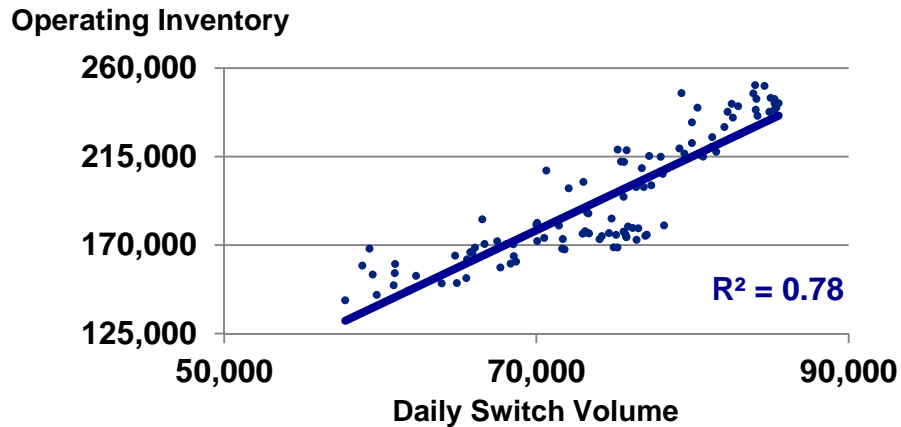
## Switch Events Increase Operating Inventory



*Operating Inventory = All cars on trains and in yards*

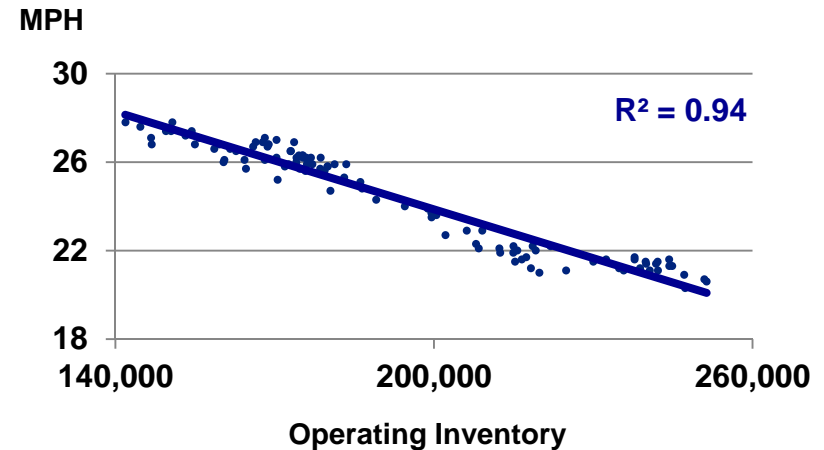
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## Switch Events Increase Operating Inventory



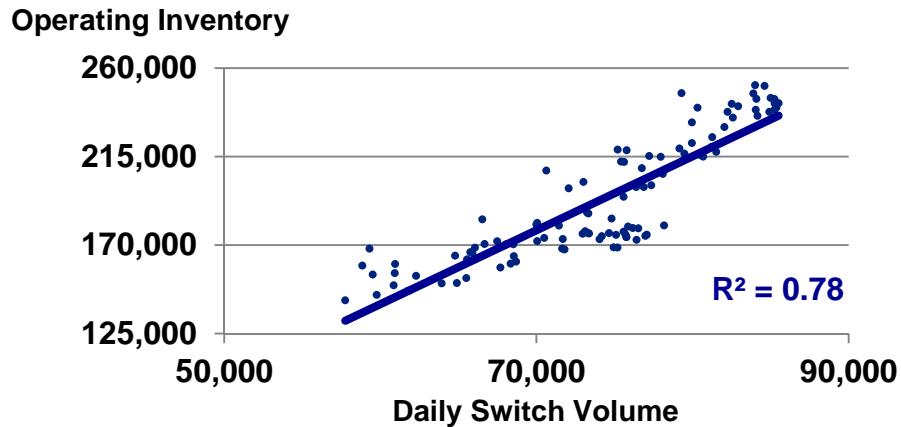
*Operating Inventory = All cars on trains and in yards*

## Operating Inventory Decreases Velocity



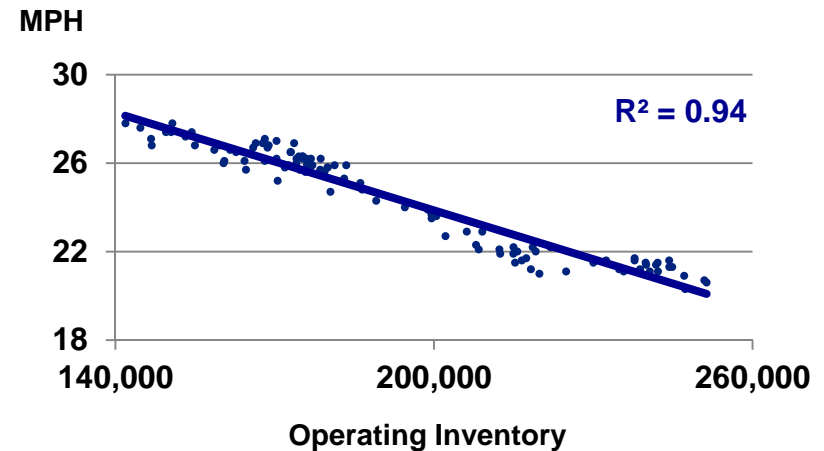
# Additional Switching Degrades Service

## Switch Events Increase Operating Inventory

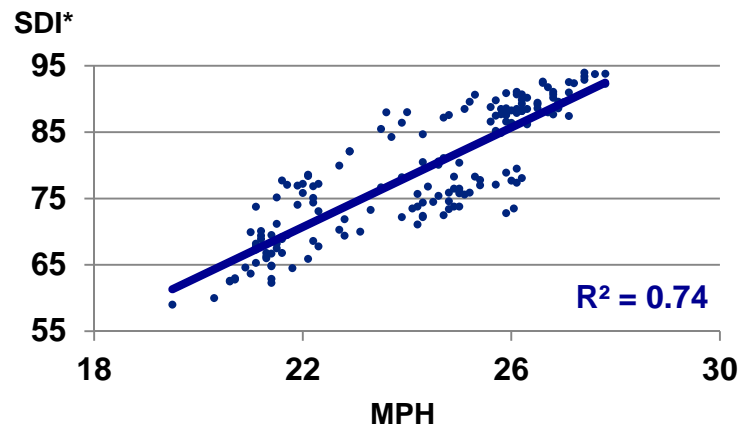


*Operating Inventory = All cars on trains and in yards*

## Operating Inventory Decreases Velocity

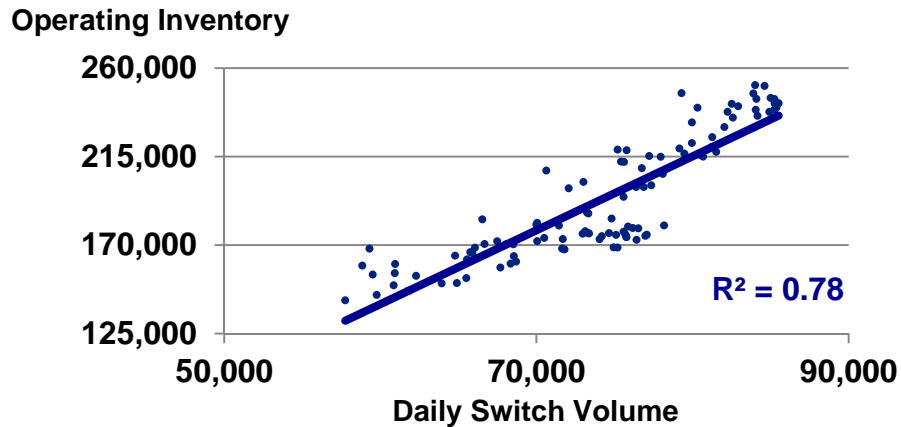


## Slower Velocity Hurts Service



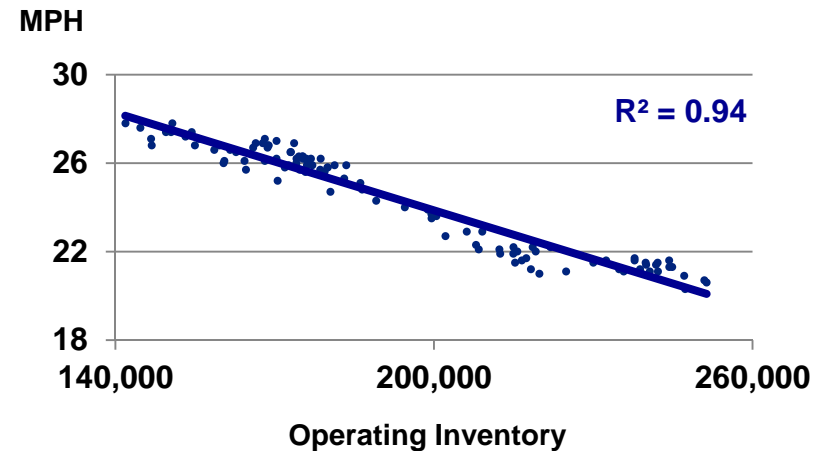
# Additional Switching Degrades Service

## Switch Events Increase Operating Inventory

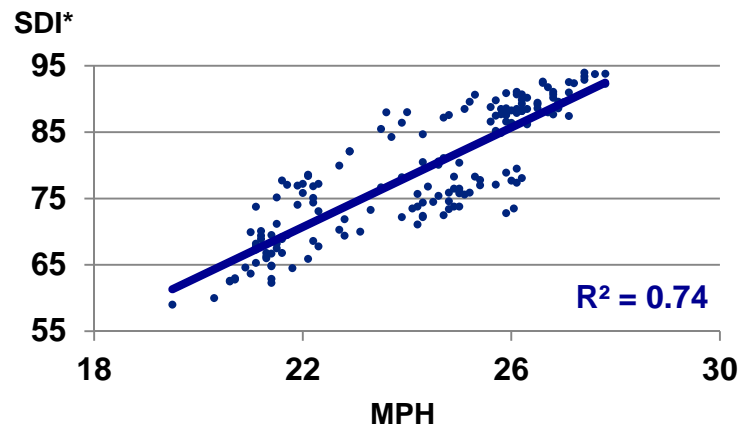


*Operating Inventory = All cars on trains and in yards*

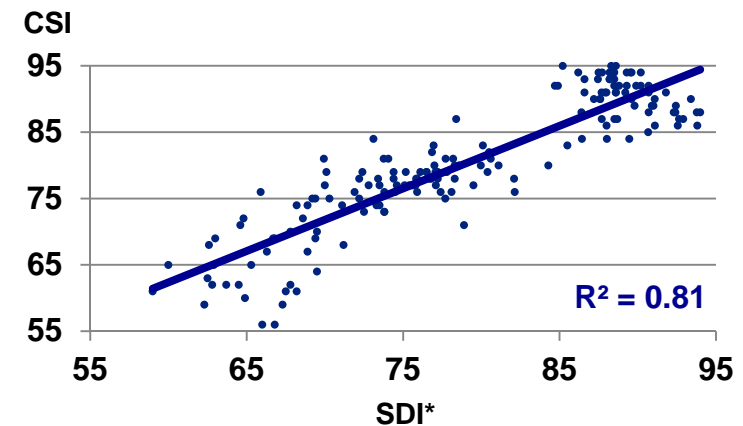
## Operating Inventory Decreases Velocity



## Slower Velocity Hurts Service



## Poor Service Hurts Customer Satisfaction



# NIT League Proposal Decreases Ability to Plan and Manage Resources

## Timeframe

### 1. Long-term Facility & Resource Planning

- Capital
- Crews / Equipment

## Objective

### Acquire

## Issues

- Uncertainty in longer-term traffic forecasting --
  - What
  - Where
  - How much / how far



# 5 Critical Resources

## *Lead Times in Italics*

- ✓ Right Amount
- ✓ Right Place
- ✓ Right Time



**Workforce**  
*6 – 9 months*



**Main Lines**  
*18 – 36 months*



**Locomotives**  
*12 months*



**Terminals**  
*18 – 36 months*



**Freight Cars**  
*12 months*

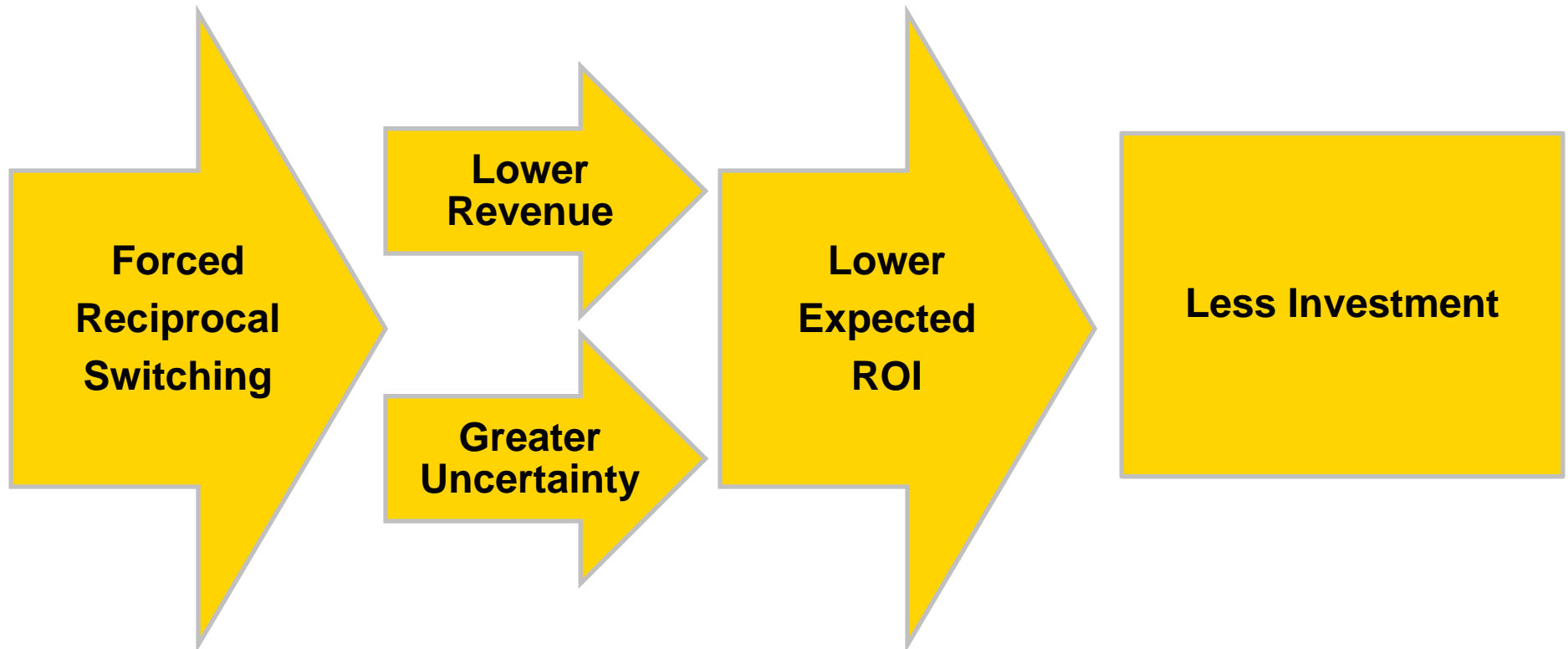
# NIT League Proposal Decreases Ability to Plan and Manage Resources

<u>Timeframe</u>	<u>Objective</u>	<u>Issues</u>
<b>1. Long-term Facility &amp; Resource Planning</b> <ul style="list-style-type: none"> <li>• Capital</li> <li>• Crews / Equipment</li> </ul>	<b>Acquire</b>	<ul style="list-style-type: none"> <li>• Uncertainty in longer-term traffic forecasting --               <ul style="list-style-type: none"> <li>- What</li> <li>- Where</li> <li>- How much / how far</li> </ul> </li> </ul>
<b>2. Tactical Planning</b> <ul style="list-style-type: none"> <li>• 2-10 day horizon</li> <li>• Train plan</li> <li>• Position resources</li> </ul>	<b>Position</b>	<ul style="list-style-type: none"> <li>• Uncertainty in short-term demand forecasts</li> <li>• Lack of time to relocate resources</li> </ul>

# NIT League Proposal Decreases Ability to Plan and Manage Resources

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<b>3. Real-time Network Management</b> <ul style="list-style-type: none"> <li>• Balance terminals</li> <li>• Control the flow</li> <li>• Assign resources</li> </ul>	<b>Assign</b>	<ul style="list-style-type: none"> <li>• Blind spots in managing daily traffic flows</li> <li>• Resources won't match demand</li> </ul>

# NIT League Proposal Will Reduce Investment



# NIT League Proposal Threatens Progress

- **Increases workload in constrained terminal areas**
- **Degrades service across the network**
- **Limits ability to plan and manage the network**
- **Increases need for capital investment while reducing ability to invest**

