

SURFACE TRANSPORTATION BOARD**Ex Parte 711 (Sub. No. 1)****Reciprocal Switching****Summary of Ex Parte Meeting Between CSX Transportation, Inc.,
and Surface Transportation Board Member Michelle Schultz****March 24, 2022**ENTERED
Office of Proceedings
March 31, 2022
Part of
Public RecordCSX Attendees:

- Sean Pelkey, Executive Vice President and Chief Financial Officer
- Nathan Goldman, Executive Vice President, Chief Legal Officer and Corporate Secretary
- John Patelli, Head of Regulatory & Federal Affairs, Associate General Counsel
- Jason Marques, Senior Counsel, Corporate & Transportation Law
- Raymond Atkins, Sidley Austin LLP

STB Attendees:

- Michelle Schultz, Board Member
- Michael Small, Attorney Advisor

Meeting Summary:

CSX thanked Member Schultz for the opportunity to meet. Because of the time constraints associated with CSX's hearing testimony, which was presented on the last panel of the last day of the hearing, CSX explained that it hoped to elaborate on its testimony and offer Member Schultz an opportunity to ask questions about its presentation.

CSX began by revisiting slides 9 and 10 of its hearing presentation, which address how the mandatory reciprocal switching proposal would influence its capital budgeting process. Moving from sole access to dual access at customer locations creates substantial uncertainty over customer retention. Mr. Pelkey explained an illustrative example of how this would cause a reduction in expected returns of many new projects below CSX's cost of capital, thereby reducing CSX's incentives to invest.

Member Schultz asked what it would mean for CSX's investment model if reciprocal switching were expanded in terminal areas where it currently takes place, a concept that Chairman Oberman raised at the hearing. She also asked whether it is fair to assume every railroad handles investment decisions in a similar way.

CSX responded that yes, the numbers and models may differ slightly, but the general budgeting approach and need to justify investment projects with returns above the cost of capital would be a natural financial expectation for railroads and corporations in general. CSX then provided maps to illustrate the limited difference to CSX between the rule as originally proposed, based on a 30-mile radius around Class I interchanges, and the proposal to expand existing reciprocal switch

locations. CSX also provided a map to contrast the small amount of reciprocal switching that took place in 2021, fewer than 20,000 carloads, with the roughly 1 million carloads that originate or terminate within 30 miles of a junction where reciprocal switching has been occurring.

Member Schultz asked about how often shippers currently open to reciprocal switch exercise that option. CSX responded that there had not been enough time for that factual inquiry, but that there was reciprocal switching occurring at the majority of the switching locations. Member Schultz asked about railroad capacity to handle volume growth if reciprocal switching were expanded. CSX explained that resulting dramatic changes to demand flow would require significant resource reallocation and would introduce a level of uncertainty and complexity that would be destabilizing to operating plans.

Member Schultz inquired about the common carrier obligation and service on reasonable request. CSX explained that, if switching were ordered, the railroad would be obligated to switch the traffic. CSX explained its concern that any customer could request a switch at any time and the impact that would have on terminals.

Member Schultz asked about the proposed rule's impact on low-volume shippers. CSX replied that investment disincentives flowing from the rule could be detrimental to small shippers most because they are more likely than larger customers to rely on railroad investments to grow.

Member Schultz inquired about the impact on differential pricing if the rule were limited to terminal areas. CSX replied that such a limitation would be insufficient, and noted that, in the East, terminals are located in major metropolitan areas that generate large amounts of traffic. CSX explained that in addition to operational complexity and investment disincentives, all such traffic would be expected to see rate compression.

Finally, CSX and Member Schultz discussed the merits of the current fault-based reciprocal switching standard. They also discussed existing measures at 49 C.F.R. pt. 1147, that allow relief to address service inadequacies on a temporary basis—key for preserving railroad investment incentives because the railroad can always win the business back. CSX explained that the permanent nature of switching orders under the proposal produces uncertainty and negatively impacts investment decisions. CSX views existing remedies as adequate to address shippers' concerns and sees open access as a back door to rate regulation, which carries enormous, known risks that outweigh any benefits.

Concluding the meeting, CSX and Member Schultz thanked each other for their time and for continuing the discussion on this topic.

Copies of the slides used in the meeting are attached.

CSX's improved profitability enables new investments

- A shipper has asked CSX to invest **\$10 Million** in rail capacity upgrades at the customer's facility
- With the investment, CSX adds **\$7.5 Million** in annual revenue and 3,000 incremental carload

	Scenario 1: Pre-Scheduled Railroading		Scenario 2: Post-Scheduled Railroading	
	Years 1-3 Business Locked	Years 4-10 75% Retention Probability	Years 1-3 Business Locked	Years 4-10 75% Retention Probability
Revenue per Carload	\$2,500	\$2,500	\$2,500	\$2,500
Annual Revenue	\$7.5M	\$7.5M	\$7.5M	\$7.5M
OR on the Business	75%	75%	60%	60%
Annual Operating Income	\$1.9M	\$1.9M	\$3.0M	\$3.0M
Probability	100%	75%	100%	75%
Weighted Annual Cash Flow ¹	\$1.4M	\$1.1M	\$2.3M	\$1.7M
Rate of Return	3%		14%	
Will CSX Invest	NO		YES	

Reciprocal switching uncertainty will prevent growth investments

- The probability of retaining business after the 3-year contract is another major consideration in CSX's analysis
- **Reciprocal switching makes our projections much less certain...**

Revenue per Carload
Incremental Annual Revenue
OR on the Business
Annual Operating Income
Probability
Weighted Annual Cash Flow ¹
Rate of Return
Will CSX Invest

Scenario 3: Reciprocal Switching

	Years 4-10 Business Scenarios		
Years 1-3 Business Locked	Keep business at lower rate	Lose to other RR; receive switch fee	Lose to Truck
\$2,500	\$2,140	\$500	
\$7.5M	\$6.4M	\$1.5M	
60%	70%	75%	
\$3.0M	\$1.9M	\$0.4M	\$0.0M
100%	50%	25%	25%
\$2.3M	\$0.8M		
5%			
NO			





