

SOUTH DAKOTA GRAIN AND FEED ASSOCIATION TESTIMONY

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Thank you Chairman Elliott, Vice Chairman Miller and Board Member Begeman for the opportunity to testify today. My name is Jerry Cope, and I am the President of the South Dakota Grain and Feed Association and am also the Marketing Manager for Dakota Mill & Grain in Rapid City, South Dakota. I am testifying today on behalf of South Dakota Grain and Feed Association, which is an affiliate of the National Grain and Feed Association (NGFA), on whose Rail Shipper / Receiver Committee I also serve.

Agriculture is South Dakota's number one industry and we rank in the top ten in the nation in nearly all crops. The rail service disruption has impacted our state greatly, and we thank you for your efforts to bring this issue to the forefront and to hold railroads accountable for restoring service to acceptable levels.

Our industry group believes that if we are going to voice concerns then we also have a responsibility to present relevant facts on where we were before the service meltdown began last fall, where we are today, and let you know what is wanted, expected and needed, as well as provide suggestions on how to improve rail service.

To begin, I would like to review where we were before we began to experience serious rail service disruptions last fall – well before the harsh winter weather – and before the STB initiated its rail service proceeding (EP 724). I believe my company was typical of others in the state. We were behind by over one thousand cars, leaving farmers and elevators backlogged with over twice the normal grain inventory as we approached spring planting. We had almost no regular communication with the railroads and if there was a plan to solve the backlog, it was not one that we could identify. Secondary freight car costs were roughly equal to the freight rate. Five thousand dollars per car or a \$1.25 per bushel was paid for cars - doubling the freight rate for corn shipped to the Pacific Northwest. These costs had escalated over time and elevators absorbed some along the way but eventually they were reflected in a lower basis and cash price of 50-cents per bushel or more. Wheat costs were 75-cents to a \$1.50 per bushel in lost opportunity to sell for immediate flour mill demand versus selling for delivery two months or more down the road. Ironically, the secondary freight car market rewarded carriers for poor performance - the bigger the delay, the larger premium was for freight. Railroads will argue that day-to-day secondary freight market premiums do not go to them but to the owner of the freight and they are right. However, the urgency to secure adequate freight for this fall's harvest resulted in some BNSF shuttles selling for up to a \$2.5 million to \$3 million dollar premium in the shuttle auctions. To date, total premiums paid to BNSF in auctions for their freight beginning this fall is over \$120 million – all money that DID go the railroad. Through this crisis, there was little or no communication from the railroads. Simply put, we were without a voice.

Now, in the aftermath of this Board's involvement and advocacy, as well as the combined efforts of Senator John Thune, South Dakota Grain and Feed Association, NGFA and the state affiliated grain organizations in Montana, North Dakota and Minnesota, we are being heard when it comes to addressing what is a logistics and operations issue for all the railroads involved, especially the Class I's. As a result of this increased communication, additional reporting of service metrics required by the Board, active monitoring by the Board and actions by some of the major carriers in this region there is some easing of fears as we are able to see the railroads plans for the long term and modifications regarding their day to day operations. It may not always be what we want to hear, but it is a first step. With the required reporting from the BNSF and Canadian Pacific, there is now more transparency to see what the carriers are doing and what they plan to do. There has also been improved communication between these two Western carriers and us, their customers. The CP's specific reporting on their performance providing power and cars to the RCP&E has provided a benchmark for a weekly gauge to measure their progress doing what they committed to do when they sold the western end of the DM&E line.

Today, progress has been made towards cutting the backlog of car orders our region. While this is great news, it is still a very serious situation. Needing a train every five days and getting one every ten days jeopardizes the ability to clean out for this fall's harvest.

In regard to the CP's performance reports, until recently, it had not provided the locomotives it had committed to, which left the RCP&E unable to clear their rail lines of loaded cars. This resulted in loaded cars sitting at RCP&E elevators for a week or longer, causing buyers to shy away from buying more RCP&E origin cars until they see that the ones they have already bought are moving. This situation is made worse at the interchange at Tracy, MN when the CP either hasn't shown up as scheduled or didn't come with as many locomotives as it previously committed; in which case the RCP&E really had no choice but to use their locomotives to help move the loads beyond Tracy –if they were available at all. This throws the RCP&E out of balance. The RCP&E then has crews that were scheduled for RCP&E local work out moving loads on the CP. It requires more locomotive horsepower to move loads than empties which again changes the RCP&E balance of power, crews and cars on its line. While the CP has provided a share of the cars that RCP&E has ordered, they have not until very recently provided the power promised. Without the CP honoring all of its commitments on an on-going basis the problems will only get worse in South Dakota.

On top of that, crop yields are expected to be at record highs this year. This year's wheat yield in South Dakota is running approximately double of normal. Even though our state's total wheat acres are down from the five-year average and the final yield is yet to be determined, total production will, at worst, be slightly above the five-year average but more likely 10 to 20 percent above. The USDA forecast for South Dakota corn production is the same

as 2013; however, another well respected private firm forecasts corn to be a record 10 percent above last year's production. Production of other crops such as soybeans, sorghum, sunflowers, oats and millet look just as promising. Given these projections, and at the BNSF's and CP's current pace of service recovery, the backlog will continue and possibly even increase through next summer. There is no room for even a minor hiccup in rail service this fall and winter—including weather, competing demand or anything else.

If there is no change in the pace of rail service, the storage of this abundance of wheat and other crops will create challenges. In my travels through western South Dakota, there are farmer piles ranging from 20,000 bushels to over 200,000 bushels. Elevators have open ground piles of grain waiting to be shipped. In some cases quality issues will require blending and cleaning of wheat to make it marketable. Unfortunately with elevator storage capacity full and waiting for cars, space to segregate and blend does not exist, leaving open the risk that less than ideal quality wheat may not be marketable – which negatively impacts local producers who have taken the risk of planting those very crops. While secondary freight costs have relaxed from their peak levels, the bids elevators are offering now more accurately reflect the crop-quality risks they are taking and the freight costs they are incurring. Basis cost for freight is 25 to 30-cents per bushel now and 40 to 50-cents for harvest delivery. The CP railroad, RCP&E and the processing industry may not experience direct secondary market costs but they are part of the market pricing for all buyers because high freight costs are inversely proportional to freight availability – the higher the extra cost of rail freight, the less freight there is to go around which in turn impacts the elevator industry's ability to handle grain.

Is it an option for companies to expand storage? Over the past 15 years hundreds of millions of dollars have been invested in South Dakota grain and fertilizer facilities based on expectations of reasonable and predictable rail service. Investments in rail facilities at grain elevators can easily run from over \$3 million dollars for a minimal amount of bins and a 25 car track upgrade to over \$30 million for a state of the art shuttle shipper and fertilizer receiver. As an industry we have to ask ourselves when does the risk outweigh the reward given the unpredictability of transportation services.

Moving forward, it is hoped that this Board will continue your stringent oversight of the agricultural rail service crisis as the recovery in service hopefully continues and ultimately returns to more normal levels. In the long term, your continued vigilance and the spotlight on this crucial issue will facilitate needed communication between the railroads and the state, where one did not exist before. Hopefully, this same communication can come into play when railroads are making investment decisions to increase capacity. The BNSF has responded to the heightened awareness with announcements to add locomotives and double track around North Dakota's oil fields. We hope that the CP will follow through with their commitments also.

While oversight from the STB, efforts by agricultural producer and shipper organization, and the leadership efforts of Senator John Thune, the ranking member of the Senate Committee on Commerce, Science and Transportation, has helped and will be needed moving forward, ease of doing business and safeguards against overregulation also are important. Certainly, the rail business environment can be improved by implementing reasonable processes and rules to make it easier to bring justifiable grievances regarding rail service, as well as rates and charges to a timely conclusion. Direct government intervention in railroad operations is not our goal. But this this can be accomplished while still not encumbering railroads with regulatory constraints that make it uneconomic for them to invest in their systems to more efficiently handle grain and to enable our industry to continue to serve our farmer customers as their link to domestic and foreign markets.

In addition to your oversight, continued reporting of service metrics are important and necessary. We have a saying in our company that the problem with communication is the illusion that it actually took place. While seemingly tongue in cheek, it speaks to a real problem. Communication has to be open, honest and real. Action plans, progress reports and relevant scorecards from railroads on a real time basis are needed. Real time is defined as weekly or at least bi-weekly. In this region we would like to see the BNSF continue publicizing its plans and following up with the STB, affected states and customers. The CP needs to continue its reporting especially regarding the RCP&E commitments so that all stakeholders are aware and the RCP&E can make real progress addressing the backlog on their line. The recent addition for BNSF and CP to report shuttles by region (specifically the three states of ND, MN and SD) is a helpful metric and we're pleased that you followed through with the request made by Senator Thune in July, which mirrors a recommendation from NGFA. Further, NGFA is in ongoing discussion with rail carriers on how to determine additional service metrics to show that agricultural shipments are not being disadvantages at the expense of other, higher-value products hauled by rail.

In addition to reporting, there needs to be one-on-one discussions between railroads and their customers to comprehensively outline what is needed and expected. Customers have the responsibility to honor commitments but the end goal is a team effort. We also believe additional manpower is needed to operate along the rail. Rail workers hours of service regulations are more stringent than those of trucks. Could hours of service regulations be relaxed during this period of service recovery so that while still operating in a safe and responsible manner, additional hours would help improve car movement?

Again, let me stress, we are not asking for direct government intervention and we are not asking for preferential treatment for grain. We just want to ensure that we are not disadvantaged or that grain is marginalized in the rail freight picture. Thank you for your time today entertaining input from us. The members of the SD Grain & Feed Association appreciate your proactive stance and efforts to improve the dire situation of rail freight service for grain in SD.