



Alliance OF AUTOMOBILE
MANUFACTURERS

216390



FILED
Office Proceedings

MAY 7 2006

Part of
Public Record

STATEMENT

OF

THE ALLIANCE OF AUTOMOBILE MANUFACTURERS

BEFORE THE:

SURFACE TRANSPORTATION BOARD

MAY 11, 2006

PRESENTED BY:

George Telfer
Senior Manager, DaimlerChrysler

My name is George Telfer, Senior Manager for DaimlerChrysler, testifying on behalf of the Alliance of Automobile Manufacturers (Alliance). I am pleased to be afforded the opportunity to offer the views of the Alliance at this important Surface Transportation Board (STB) public hearing. The Alliance is a trade association of nine car and light truck manufacturers including BMW Group, DaimlerChrysler, Ford Motor Company, General Motors, Mazda, Mitsubishi Motors, Porsche, Toyota and Volkswagen. One out of every 10 jobs in the U.S. is dependent on the automotive industry.

The automotive industry depends heavily on efficient and cost-effective rail transportation in order to sustain its manufacturing operations. A vast majority of finished vehicles are shipped by rail to distribution points, as well as a high percentage of materials shipped into the plants. Shipping by any other means would not only be cost prohibitive but would be impossible given the lack of capacity to move such large volumes of bulky freight. Shipping finished vehicles without rail, for example, would require a tenfold increase in specialized truck equipment and drivers. Given the nature of its shipping needs, the automotive industry is in fact captive to this mode of transport.

Over the past several years, the railroads have been able to mandate fuel surcharges covering most of the Alliance Member Company contracts. When first implemented, the surcharges were relatively small and an analysis indicated that they were relatively equitable. Over the past two years, as fuel prices have increased, surcharges have risen dramatically, causing the Alliance to re-examine whether the methodologies used to calculate the surcharges are reasonable.

Before I get into the detail of our concerns, I would like to state that the Alliance is a strong believer in markets and their ability to set a fair price. While we have concerns with how railroads calculate their fuel surcharges, it in no way changes our position on the underlying regulatory structure of the rail industry. We remain opposed to any proposal that would substitute governmentally imposed competition for the market-based approach of current law for the rail industry.

As an industry, we know first hand how rising fuel price impacts costs. Higher fuel prices put pressure on our industry in many areas – through our use of more expensive resins to higher prices for tires. And we recognize that fuel surcharges used by the rail industry are a necessary product of higher fuel prices. What we are asking for is that these fuel surcharges also be subject to the same free market forces and be transparent. We must work cooperatively with the rail industry to share in the burden of higher fuel costs.

To date, the railroads have not provided an analysis to demonstrate that their surcharge practices are reasonable and market driven. Therefore, the Alliance's position on the railroads' surcharges is based on an analysis of the railroads' own financial data, confirmed by similar analyses of prominent, respected industry trade groups and independent consulting firms.

The analysis of the financial reports issued by the railroads indicates that current fuel surcharges do not coincide with the relationship to the railroad's actual fuel expense. As one example of the inequity of the fuel surcharge structures, there have been time periods when fuel

surcharges have risen, but certain railroads have reported to investors that their actual fuel costs have fallen. The analysis indicates that some railroads' surcharges have resulted in their being grossly over-compensated for fuel, well beyond their actual fuel expenses.

The Alliance believes that some of the various surcharge mechanisms are flawed and unbalanced, and work to the financial advantage of the railroads. As a result, we believe the ability to mandate fuel surcharges has become a new profit center for the railroads. The analysis indicates that, in recent quarters, over-recovery of fuel expenses may account for half of the net income being reported to investors. Surcharges have become the latest form of rate increase, avoiding much attention because everyone knows that fuel prices have increased and therefore, the railroads argue, the surcharges must be warranted.

The Alliance has several specific issues with the prevailing practices relative to fuel surcharges:

1. The current revenue-based surcharges (where the surcharge is a percentage of the rate) do not correlate with the actual fuel costs incurred by the railroads. Rail movements with higher rates pay more surcharge than rail movements with lower rates, even if the amount of fuel used for the two moves is the same. Revenue-based surcharges are even more inequitable in today's pricing environment where the fuel surcharge percentage is tacked onto any rate increase the railroad receives, despite the fact that there is no correlation between the rate increase and the amount of fuel used. In recognition of the inequities of revenue-based surcharges, shippers and carriers in other transportation modes are moving to consumption-based surcharges and it is time for the railroads to follow suit.
2. Using West Texas Intermediate (WTI) Crude as the index to establish the surcharge does not correlate with the actual fuel purchases made by the railroads. The railroads do not use WTI Crude to power their locomotives, so changes in the cost of WTI bear no direct relation to changes in the cost of the fuel the railroads are using. Since changes in the price of WTI have increased much more than the price of diesel fuel, the railroads' use of WTI as the basis for their surcharges adds to their being grossly overcompensated. Between the end of 2001 and the first week of April 2006, the price of WTI increased by 239%, where the cost of diesel fuel increased by only 124%. Since the railroads are actually buying diesel fuel and not WTI Crude, the surcharge structure should be based on diesel fuel prices.
3. In their paper entitled "Overview of U.S. Freight Railroads" dated January, 2006 The Association of American Railroads repeated an often-cited statistic that "On average, railroads are three times more fuel efficient than trucks, and railroad fuel efficiency is improving all the time." Our experience however is that, despite using one-third less fuel, on a percent of revenue basis, railroad surcharges have generally exceeded those paid to trucking companies. In addition, while "railroad fuel efficiency is improving all the time," this fact has not been reflected in the railroads' surcharge programs.

The Alliance finds that some of the railroads' unwillingness to justify their surcharge methodologies is frustrating. Our attempts to obtain supporting documentation have been rebuffed. Surcharges have become "non-negotiable," enacted by unilateral decree.

The Alliance believes the STB should press the railroads to fully disclose both cost and revenue data related to fuel and fuel surcharges. This should include the base fuel cost included in all of their rates, the actual fuel cost incurred and the incremental revenue generated by their surcharges.

In summary, the Alliance is requesting STB support for the following:

- Surcharges should cover the incremental cost of fuel and not be a new source of profit.
- Railroads should provide data to their customers demonstrating that the level of surcharge is revenue-neutral.
- Surcharges must be based on the price of locomotive diesel fuel that the railroads actually purchase.

Thank you.

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