

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

Ex Parte No. 646 (Sub-No. 1)

SIMPLIFIED STANDARDS FOR RAIL RATE CASES

COMMENTS OF THE

**NORTH DAKOTA PUBLIC SERVICE COMMISSION
NORTH DAKOTA GRAIN DEALERS ASSOCIATION
NORTH DAKOTA WHEAT COMMISSION
NORTH DAKOTA GRAIN GROWERS ASSOCIATION
NORTH DAKOTA FARMERS UNION
NORTH DAKOTA FARM BUREAU**

Due Date: October 24, 2006

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Identification

This statement is submitted jointly by the North Dakota Public Service Commission, North Dakota Grain Dealers Association, North Dakota Wheat Commission, North Dakota Grain Growers Association, North Dakota Farmers Union, and North Dakota Farm Bureau (North Dakota).

The North Dakota Public Service Commission (NDPSC) is a three-member elected constitutional body that is charged with representing North Dakota's shipping interests in proceedings such as this. NDPSC and its predecessor, the North Dakota Board of Railroad Commissioners, have been active in Interstate Commerce Commission and Surface Transportation Board cases for well over one hundred years. This level of involvement is indicative of the state's ongoing need for reliable, reasonably priced transportation services and of its lack of transportation alternatives.

The North Dakota Grain Dealers Association (NDGDA) is a 95 year-old voluntary trade association of grain elevators in North Dakota. More than 90% of North Dakota's 400 grain elevators are members of NDGDA.

The North Dakota Wheat Commission (NDWC) was created by the state legislature and exists to promote the use of wheat (flour) and durum (pasta) that is grown in North Dakota. The NDWC is financed through voluntary per bushel payments that are made by North Dakota farmers when they sell the wheat that they produce each year.

The North Dakota Grain Growers Association (NDGGA) is a farmer association that was organized in 1967 and exists to provide a voice for wheat and barley producers on domestic policy issues and to provide education, leadership, information and representation to increase profitability and enhance value added opportunities. The NDGGA is governed by a 12 member board of directors, and is funded by producer memberships and contract proceeds from commodity groups.

The North Dakota Farmers Union (NDFU) is the largest general farm organization in the state, founded in 1927. The organization is a grassroots, producer-controlled organization dedicated to 35,000 North Dakota families. NDFU provides a voice for family farm agriculture, cooperatives and rural communities on a state and federal level through the legislative process. The NDFU actively promotes and develops member-owned cooperatives and provides youth and adult education on agricultural issues and cooperatives.

The North Dakota Farm Bureau (NDFB) is an independent, non-governmental, voluntary organization comprised of over 27,000 farm and ranch families. Its mission is to be an advocate and catalyst for policies and programs that will improve the financial well-being and quality of life for its members. NDFB is county, state, national and international in scope and influence. It is non-partisan, non-sectarian and non-secret in charter. NDFB represents agricultural producers at all levels. Funding is provided by membership dues to the organization.

Summary

North Dakota commends the Surface Transportation Board (STB) or (Board) for initiating this rulemaking proceeding. Fair and equitable rail transportation rates are vital to North Dakota's grain industry and to the state's economy as a whole. It is essential that all shippers, large and small, are provided with a reasonable and cost effective way to

challenge excessively high rail rates. The proposed rules, while providing some positive changes, do not provide a viable solution to the problems. The rules are still much too complex, and the eligibility criteria preclude all but a few very large shippers from any form of rate relief. North Dakota urges the Board to take the necessary steps to ensure that all shippers are afforded the opportunity to challenge unreasonable and unfair rail rates.

Background

Agriculture is North Dakota's number one business. Without the ability to move its agricultural production to distant markets at reasonable and competitive rates, North Dakota's vast production capabilities lose all or part of their value. This proceeding is extremely important to North Dakota, its grain elevator industry, its economy, and individual farmers throughout the state.

North Dakota has 640,000 residents and over 70,000 square miles of land. Agriculture is the single largest industry segment within the state's economy. The state has approximately 30,000 farms and typically leads the nation in the production of spring wheat, durum wheat, barley, sunflower, dry edible beans, and canola. Other major grain crops include corn and soybeans.

Farmers typically use their own trucks to haul grain from their farms to a nearby grain elevator / warehouse. Typical haul distances are 10 to 20 miles. Farm truck capacities range from 350 to about 850 bushels – between 1/10th and 1/4th of a single rail car.

Grain elevators serve as the primary market for farmers' grain. The state's 400 grain elevators purchase between 500 and 550 million bushels of grain per year. Elevators clean the grain and blend it with different qualities of grain to meet the exact specifications of domestic users and export markets. Many of the state's grain elevators are cooperatives that are owned by the farmers that they serve.

Over 80 percent of the grain sold by North Dakota's grain elevators each year is sent to out-of-state markets. North Dakota does not have direct access to any navigable waterways and almost all of its out-of-state markets are too distant to be effectively reached by truck. Trucks typically are not an effective way to move lower value bulk commodities like grain over distances of more than 250 miles.

The distance to North Dakota's nearest major out-of-state market (Minneapolis) is up to 700 miles depending on location in the state. Many markets, including the Pacific

Northwest export market, are 1200-1500 miles away. This level of captivity explains why nearly 81 percent of the grain that was shipped to out-of-state destinations during the last crop year was shipped by rail. North Dakota shippers simply have no other viable options. This also explains why many of the rates charged to move grain out of North Dakota generate revenue-to-variable cost ratios of 220%, 300%, or even 400%.

North Dakota's grain elevator industry is heavily dependent on rail service. Without rail, the industry would have no feasible means of transporting North Dakota grain to market. This near total reliance has a direct impact on farmers since grain is the main commodity grown by the majority of North Dakota farmers and local grain elevators are the only major local market for this grain. North Dakota and its farmers and grain elevators are clearly dependent on railroads.

North Dakota is served by two Class I railroads and four affiliated short lines. The Burlington Northern Santa Fe (BNSF) operates about 1855 miles of track in the state, including two east-west (Chicago to Seattle) main lines. Its two affiliated short lines, the Red River Valley & Western (RRVW) and Dakota Northern Railroad (DNR) operate about 428 and 71 miles of track respectively. Collectively, these three carriers serve about 66 percent of the North Dakota grain elevators that have direct access to rail service.

The Canadian Pacific (CP) is North Dakota's other Class I carrier. CP operates about 445 miles of track in the state, including its Chicago to Vancouver main line. Its two affiliated short lines, the Dakota, Missouri Valley & Western (DMVW) and the Northern Plains (NP) operate about 399 and 434 miles of track, respectively. Collectively, these three carriers serve about 34 percent of the North Dakota grain elevators that have direct access to rail service.

The four shortline railroads do not provide competition to the two Class I systems because the rates and service offerings of the shortlines are controlled by the Class I railroads.

Only about three percent of the state's grain elevator locations are directly served by more than one rail carrier.

It is vitally important that the STB understand North Dakota's dependence on railroads. Like any commodity, farmers' grain is virtually worthless unless it can be delivered to buyers. Unfortunately, North Dakota farmers and grain elevators have very limited means of transporting their grain to distant markets. Barge transportation is not

available. Because of distances to market, truck transportation does not provide a viable alternative. One major grain shipper in the state would have to put 23,000 truckloads of grain on the highway to handle its volume. Given this lack of options, rail rates have a direct and immediate impact on shipper profitability and farmer income.

The price that farmers receive for their grain is based on destination market prices minus transportation charges and grain elevator margins. Elevators typically hope to achieve a margin of ten cents per bushel. This amount is used to pay operating costs and to hopefully provide a profit at the end of the year. The following example illustrates how an elevator arrives at the price that it offers farmers for their grain:

Grain Elevator Offering Price on Wheat

Minneapolis Grain Exchange Price (Delivered to Mpls.)	\$4.00 / bushel
Minus Typical Rail Delivery Charge (\$2,129 / car)	- \$.63 / bushel
Minus Grain Elevator Margin	<u>- \$.10 / bushel</u>
Offering Price to Farmers	\$3.27 / bushel

Competition in the local grain market prevents elevators from taking a larger margin and low profit levels make it impossible for them to operate on a smaller margin. Therefore, there is a direct correlation between grain prices and rail rates. As rail rates increase, elevator offering prices decline and so does farmer income.

Ultimately, farmer income translates into the land's ability to produce income. If farmer income declines, so does the value of his land. This occurrence then influences lenders' willingness to provide operating loans that are necessary to finance farm operations – farmers borrow money in the spring to buy seed and fuel, plant crops, apply fertilizer and herbicides, and eventually to harvest. When grain is sold, loans are repaid.

The railroads' influence on North Dakota's economy is enormous.

Proposed Rules

On July 28, 2006, the STB announced that it had instituted this rulemaking proceeding to revise and clarify its existing simplified guidelines. The STB proposes to: (1) create a simplified stand-alone cost (Simplified-SAC) procedure to use in medium-size rate disputes; (2) retain the current "Three-Benchmark" method of the existing simplified guidelines, with some modifications and refinements, for small rate disputes; and (3) establish eligibility presumptions based on the maximum value of the case to distinguish between large, medium-size, and small rate disputes.

Simplified-SAC

The STB states that constrained market pricing (CMP) with its stand-alone cost (SAC) constraint, (Full-SAC) continues to be its preferred and most accurate procedure available for determining reasonableness of rail rates where there is an absence of effective competition. Under the proposed rules, the STB proposes to create a Simplified-SAC method to be used in medium-size rate disputes for which a full stand-alone cost (Full-SAC) presentation would be too costly, given the value of the case. The Simplified-SAC would provide a streamline methodology that uses the framework of the Full-SAC methodology, but eliminates or restricts evidentiary submissions on certain issues.

The inquiry under the Simplified-SAC method would be limited to a determination whether the captive shipper is being forced to cross-subsidize other parts of the railroad's rail network. The STB would assume that all of the existing infrastructure along the route selected by the complainant would be needed to serve the traffic moving over that route.

Eligibility criteria would be based on the maximum value of the case (MVC) which is the maximum rate relief the shipper could attain over five years if the challenged rates were reduced to the jurisdictional floor (the level at which the R/V ratio equals 180%). The Simplified-SAC methodology would generally apply if the MVC is between \$200,000 and \$3.5 million.

The proposed Simplified-SAC methodology is an inadequate attempt to provide a more reasonable and equitable approach for smaller shippers to utilize the STB's rate complaint process, but the cost will still be prohibitive for most shippers who would be required to use this method. The STB states that the Simplified-SAC process would be the methodology available for medium-size shippers, but in reality very few shippers with MVC between \$200,000 and \$3.5 million could afford to utilize the Simplified-SAC process.

Under the proposed rules, the Simplified-SAC methodology would likely become the primary methodology for use in small rate complaint proceedings. While the Simplified-SAC process would be less time consuming and less costly than a Full-SAC proceeding, it will still be a complex procedure and will be cost-prohibitive for most small shippers. The STB's proposed a three-phase procedural schedule would provide for an STB decision within 18 months. The STB proposes a \$200,000 estimate of the cost to make a Simplified-SAC presentation.

North Dakota commends the STB on its proposal to shorten the procedural timelines, but believes that while the STB's suggested procedural timeframes for completing a Simplified-SAC presentation represent some improvement over the existing rules, we question whether the timeframes are achievable given the fact that the parties would have the opportunity to present evidence and argument in each phase of the case, and that there would be a decision by the STB at each of the three separate stages of a case. The STB does state that it would consider deviations from the procedural schedule only upon a good cause showing by a party.

North Dakota also questions the STB's \$200,000 cost estimate for a Simplified SAC presentation. That estimate appears to be overly optimistic given that the STB estimate for a Full-SAC presentation is \$3.5 million.

Three-Benchmark Method

For small shippers with MVC less than \$200,000, the Three-Benchmark method would be retained under the proposed rules but with refinements to lessen the uncertainties of the existing method. This is what the STB refers to as the methodology for small rail rate disputes. The basic problem with this approach is that only a very few of very small shippers would be eligible for this method. An example of this problem is presented in the Eligibility Criteria comments below.

The STB proposes a two-phase procedural schedule under the Three-Benchmark method. The procedural schedule envisions an STB decision at two separate stages of a case. The parties would have opportunity to make arguments and present evidence in each phase. The first phase would determine eligibility, and that threshold issue would be decided within 50 days. A final decision by the STB on the merits would be made within one year of the date of the complaint. There is no STB cost estimate for a Three-Benchmark presentation.

Eligibility Criteria

Under the propose rules if the MVC exceeds \$3.5 million, the STB would presume that complaint would fall under the Full-SAC methodology. If the MVC is between \$200,000 and \$3.5 million, the STB would presume that the complaint would fall under the Simplified-SAC methodology. If the complaint is less than \$200,000, the complaint could be filed under the Three-Benchmark methodology.

The first obvious problem is that the MVC is probably not a realistic number, because it is unlikely that any complaint proceeding would result in rates being reduced to the 180% R/VC level.

The second obvious problem is that even if rates were reduced to the 180% R/VC level, the potential relief would likely be insufficient to encourage any of the eligible shippers for the Three-Benchmark method to pursue a rate complaint, and only the largest shippers eligible for the Simplified-SAC method would likely be encouraged to pursue a complaint.

The following example illustrates the problem. Let's assume, for instance, that a grain elevator ships 36 cars per year or 3 cars per month at a rate of \$3,000 per car, and the 180% R/VC is \$2,000 per car. The difference is \$1,000 per car per year. The MVC in that hypothetical case is \$180,000 ($\$1,000 \times 36 \times 5 = \$180,000$) and as a result this very small 36 car per year shipper would be eligible for the Three Benchmark method because the MVC is below \$200,000. If that shipper increases shipments to 4 cars per month (48 cars per year) the MVC would be \$240,000 ($\$1,000 \times 48 \times 5 = \$240,000$). This very small 4 car per month shipper would not be eligible for the Three-Benchmark method and would have to use the Simplified-SAC method to seek relief because the MVC is no longer less than \$200,000.

The eligibility criteria must be modified substantially if shippers are to have any realistic hope of being able to seek rate relief in any proceeding before the STB.

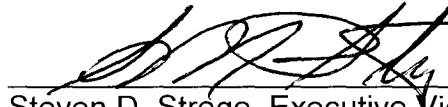
Conclusion

North Dakota commends the STB on taking positive steps to address the problems associated with the existing simplified guidelines available for smaller rate complaint proceedings. However, the eligibility criteria proposed by the STB will force nearly all of the small cases to be filed under the Simplified-SAC process. The end result is that the shippers that could possibly qualify for the Three-Benchmark process are not likely to pursue the limited relief available to them under that process when they apply a cost/benefit analysis to their situation. All of the remaining small shippers would fall under the Simplified-SAC methodology, and even using the STB's cost estimate of \$200,000 as the cost, only the largest of those shippers meeting the eligibility requirements would likely be able to justify using the Simplified-SAC process.

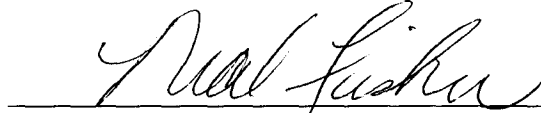
Respectfully submitted,



Tony Clark, President
North Dakota Public Service Commission



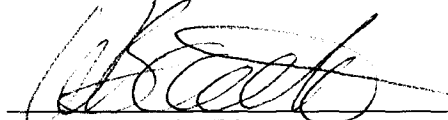
Steven D. Strege, Executive Vice President
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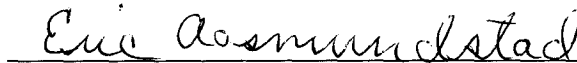
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