

BEFORE THE
SURFACE TRANSPORTATION BOARD

EX PARTE NO. 665
RAIL TRANSPORTATION OF GRAIN

COMMENTS OF
AG PROCESSING INC

My name is Terry J. Voss. I am Senior Vice President – Transportation for Ag Processing Inc (“AGP”). AGP is a cooperative owned by 211 farmer-owned local cooperatives and six regional cooperatives. It operates 14 facilities that process soybeans and corn, producing crude soybean oil and refined soybean oil, manufacturing methyl esters, for biodiesel and producing soybean meal, ethanol, and various co-products.

AGP also actively buys; stores, sells, and ships feed grains, domestically and for export. AGP also operates 40 grain facilities either through ownership or joint ventures with our members. Our member owners operate hundreds of grain elevators throughout the Midwest and upper Midwest. The success and viability of AGP and its membership are directly impacted by grain transportation and its costs. All have a continuing interest in this proceeding and its outcome.

AGP is a member of National Grain and Feed Association (NGFA) and is aware that NGFA is filing comments today representing the views of its membership, including

those of AGP. AGP will emphasize a limited number of points to minimize duplication of the NGFA statement.

It is often true in the grain industry that, as rail rates increase, there is a decrease in the price a local elevator will bid to buy a farmer's grain. If a local elevator has grain under contract from the farmer for deferred delivery and the rail rate increases subsequent to the purchase, the local elevator normally bears the risk of the increase as between itself and the farmer. Grain and grain products rates as well as accessorial charges can be increased on 20 days' notice. AGP's local cooperatives and their farmer-owners accordingly have a very large stake in grain rate levels, which is a major reason why AGP is participating in this proceeding.

The Board's Notice instituting this proceeding states that the public hearing is intended as "a forum for interested persons to provide views and information about the market conditions that led" the Government Accountability Office ("GAO") to observe that grain rates have diverged from other industry trends (i.e., grain rates have gone up) and that "the amount of grain traffic with comparatively high markups over variable cost increased notably between 1985 and 2004." The Board's Notice also indicated an interest in "grain transportation markets in general" and in "information regarding the interplay between the American and Canadian wheat markets, how the Canadian regulatory system differs from the American system, and what impact those differences might have on grain production in the United States."

AGP is not in a position to shed any light on how the Canadian regulatory system differs from the American system because, although AGP does business in Canada, it has had no occasion to make use of the Canadian regulatory system.

That is not to say, however, there is no interplay between the American and Canadian wheat markets. Wheat, using that term in its broadest sense, is not a fully fungible commodity because there are several sub-species of wheat with different end uses. The southern wheat growing areas – Texas, Oklahoma, and Kansas mainly – produce winter wheat, which is not generally grown in Canada but is grown in other countries. U.S. winter wheat is used for some bakery goods and traditionally has been a large export crop. Increased rail rates may directly impact the ability of the U.S. to compete effectively in those export markets.

Further north in the U.S., and in some parts of Canada, durum wheat is produced, primarily for the pasta market, as well as spring wheat. Spring wheat is utilized in the bakery industry and is another export crop that is impacted by rate increases.

The largest crop in the United States is corn, which is a major ingredient in animal and poultry feed and our leading export crop, although the new profusion of ethanol facilities will detract from corn exports. Behind corn and wheat, soybeans are our nation's third leading grain crop. Like corn, which feeds local ethanol and corn sweetener markets, soybeans enjoy a robust processing market for the production of vegetable oils and soybean meal, an important ingredient in animal and poultry feed. Recently, a bio-diesel market has begun to emerge for soybeans.

Corn and soybeans are grown essentially in an area extending from Ohio, on the east, to South Dakota, Iowa, Nebraska, and Kansas. Unless corn and soybeans are consumed by local producers, it generally requires long haul transportation to export positions or to areas of high population density where dairy cattle, beef cattle, hogs and poultry are raised. Except to the limited extent that barge transportation is available from ori-

gins close to navigable waterways, rail is the primary method of moving these farm commodities. Agricultural products, such as ethanol, distillers dried grains, soybean oil, and meal, similarly require rail transportation for all but the shortest movements.

The grain and agricultural community is heavily reliant on rail transportation not only because of the unavailability or unsuitability of barge and truck for a great many agricultural shipments, but also because of agricultural industry investments in rail-related infrastructure. AGP and our members have invested millions of dollars to upgrade or build new facilities to obtain the most economical rates available. Railroads furnish no tank cars and way less than the number of covered hopper cars that are necessary, although there are exceptions where some railroads have elected to supply covered hopper cars for grain shuttle trains. Additionally, one railroad has implemented a processor car allocation system for soybean meal. Companies such as AGP that process grains must supply some of their own hopper cars, and 100 percent of the tank cars to ship finished products. The ongoing investments we must make in rail equipment, and often in our plant track infrastructure, adds to the degree to which these agricultural facilities are captive to rail service and thus susceptible to rate increases. With a multi, million dollar monthly cost for rail equipment, it is not easy to turn our backs on rail service even when rates increase. Some carriers are now requesting or requiring that additional track be built at facilities.

The marketing system for feed grains is, perhaps, less complex than for grain products. The value of a feed grain to its producer is determined largely by the value of the commodity at its point of consumption minus the transportation costs of reaching that point of consumption. From that price, the local grain elevator deducts its own margin to

the extent the market permits, and the balance is essentially the price received by the farmer. Depending on the distance between the origination point and consumption point, rail transportation costs can represent up to one-third of the delivered value of field grains. Grain processing involves a somewhat more complex pricing structure, but transportation costs nevertheless play a significant role in the grain product marketplace.

Rail rates are influential in the marketing of grain and agricultural products not simply as an element of delivered price, but also as a competitive factor. Indeed, comparative rail rates may well have a greater market impact than absolute rail rates. Rail rates that provide one origin with even a small relative advantage to another origin can determine which shipping facility will survive in the marketplace and which will not. This sensitivity to rate disadvantages may well be more acute in the grain industry than in other industries that use rail service because grain trades are known to turn on fractions of a cent per bushel.

Increasingly, AGP and its members are seeing and experiencing steep and frequent increases in its rates for both grain and grain products, and sometimes highly selective increases. We can illustrate these trends with both statistical and anecdotal information.

The following charts, with data derived from carrier financial reports, compare agricultural rate changes for the two major western railroads between 1998 and 2006 with rate changes for commodity groups as reported by those railroads.

TABLE 1

Average Rates Per Unit

BNSF

	<u>1998</u>	<u>3rd Quarter 2006</u>	<u>% Change</u>
Agriculture	\$1854	\$2524	36.1%
Automotive	\$1717	\$2800	63.1%
Energy	\$1077	\$1191	10.6%
Intermodal Units	\$790	\$973	23.2%

TABLE 2

Average Rates Per Unit

Union Pacific

	<u>1998</u>	<u>3rd Quarter 2006</u>	<u>% Change</u>
Agriculture	\$1552	\$2635	69.8%
Automotive	\$1461	\$1715	17.4%
Chemicals	\$1708	\$2366	38.5%
Energy	\$1130	\$1308	15.8%
Industrial Products	\$1352	\$2237	65.5%
Intermodal Units	\$599	\$819	36.7%

Further, so far as I am aware, the rates shown in the above in tables do not include fuel surcharge revenue. Nor do they include the costs of private equipment in the processing industry which are often supplied by shippers in lieu of carriers. All tank cars are supplied by the shipper. If the costs of shipper car and infrastructure investments necessary to make rail service more efficient could somehow be included in a statement of real world transportation costs, these tables would have markedly different results. For example, the cost of leasing a tank car is approximately \$700.00 per month. When used for agricultural products, the car usually realizes approximately one round trip per month, and adds \$700.00 to the shipper's per unit cost of transportation for that shipment above the rates and fuel surcharges paid to the carrier. Put another way, if carriers supplied all equipment, their rates presumably would be much higher than those shown as they are highly unlikely to absorb a unit cost of \$700.00, or even of just a few hundred dollars, without a rate adjustment.

Now, let me offer some anecdotal examples of what we face from the railroad industry and why we are here today representing our members' interests.

1. One carrier's corn shuttle rates from an Iowa origin have gone up by \$1,275 per car since September 2000, an increase of 85 percent, or an average of about 15 percent per year.

2. A railroad has grain rates to Texas from two different points in Iowa, exactly the same railroad miles from the destination. The rates from one of the origins are \$240 per car higher than from the other. Both origins and the destination are served by the same railroad. I use this example to illustrate how difficult it is to plan for transporta-

tion expenditures because only the railroad knows why his views one of those origins as entitled to a better rate. The high rate origin in this example is unable to compete effectively for this traffic.

3. Soybean meal rates have been impacted particularly hard by increases. From one of AGP's origins, the rates on 100-car units moving to the Pacific Northwest for export went from \$2,945 per car in October 2005 to \$3,695 per car today, an increase of 26 percent. Another carrier's 100-car train rates for meal increased by \$800 per car, or 37 percent, from January 2005 to October 1, 2006, plus fuel surcharges which add over \$800 per car, or nearly 27 percent of the rate. AGP is losing export soybean meal business to South America in large part as a result of these railroad rate increases. We expect that our volume of those exports will be less than one-third of what they were in 2005. The railroads are impervious to this result.

One of the most serious flaws in all of the discussions I have seen of grain markets and railroad grain rates is that only rates actually used are captured in the waybill samples and show up in studies like the one issued by GAO. AGP has on several occasions been quoted rates by railroads that are so high that they cannot be used at all. We have been told in some cases that our rates are going to be increased by amounts that equal a 50 percent to 250 percent raise at a single time. When we complain that these increases will preclude the use of rail service, there is no reaction from the carrier except to say that this is what the new rate will be.

To my way of thinking, this is an instance where railroads are using their freedom from effective rate regulation (we still have no practical way to challenge rates other than through a full stand-alone cost case) to avoid their common carrier obligation to provide

transportation or service on reasonable request. In any event, however, there are a growing number of instances where the waybill sample simply does not fully or accurately measure the extent to which railroad rates have been increased where the increases are so high as to deter the use of those rates.

As rate continue to increase, the American farmer and consumers suffers most in the end.

Respectfully submitted,

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