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**BEFORE THE
SURFACE TRANSPORTATION BOARD
STB Ex Parte No. 677
COMMON CARRIER OBLIGATION OF RAILROADS**

April 17, 2008

**STATEMENT OF
NATIONAL GRAIN AND FEED ASSOCIATION**

The National Grain and Feed Association is a U.S.-based trade association with 900 member companies that own and operate more than 6,000 facilities throughout the U.S. The NGFA's membership encompasses all sectors of the industry including grain shippers, feed manufacturers, grain and oilseed processors, millers, and exporters.

We appreciate the STB conducting this hearing on the common carrier obligation of rail carriers. U.S. agriculture is dependent on rail service to link customers of grain and grain products with origin shippers and processors. Of all the industries served by rail, agriculture is among the most diffuse and decentralized. Agricultural shippers have concerns about rail service reliability, because the agricultural rail transport network is a collection of many shipping points linked to a wide range of (but fewer than origin points) destinations. This makes the "loss" of any individual shipper's volume less significant to the serving railroad, and railroads have, at times, adopted a number of tactics

to discourage volume in locations where such service is viewed as less significant to the overall business of the carrier, including pricing the service at levels that make the location uncompetitive in rail-delivered markets; degrading reliability of service to discourage rail markets and the switching of some locations to truck only.

Historically, one of the biggest challenges for agriculture and food production is to manage the seasonality of the business. It is common, during the heaviest harvest periods, for the industry to find itself short of needed freight to move product to market. To address this seasonal factor, grain elevators have built additional commercial storage capacity, farmers have built additional on-farm grain storage capacity, and railroads have offered different classes of rail service with some varying degrees of "guarantees" on performance. One such program, the BN's Certificate of Transportation (COT) program, was reviewed by the ICC and the Courts. The Eighth Circuit Court of Appeals ruled that during periods of constrained capacity, a particular railroad cannot shift limitless rail capacity from one class of service to another. The court further concluded that the railroad cannot offer premium-priced "guaranteed" service that is more reliable than standard tariff terms, and simply tell the customer that if they want service, they must purchase the premium service. Thus, the court decision affirmatively stated that the railroad has a common obligation to all classes of customers being served.

While this decision has clear applicability to how railroads may distribute capacity among classes of agricultural rail service during periods of relative shortage, it may also apply to circumstances when railroads have limited capacity and must make service choices across different business lines, such as grain, coal and intermodal. We have observed market circumstances in the past when coal was given priority during periods of

general rail capacity shortage. Also, with the increased volume of intermodal business, which operates at near-just-in-time, as rail capacity becomes more constrained, to what degree must the ag industry suffer service deteriorations to manage the risk of loss in timeliness of service to such other economic sectors?

There is a general view that the ag industries (grain in particular; less so with product sectors, because of limited grain car and tank car storage capacity) have the ability, if necessary, to wait on freight. This is especially true where grain is highly captive, and the only available market is the long haul rail markets. Will grain “wait” on the freight? The truth is that grain will “wait” on the freight, but only to the extent that demand at destination markets can be served by some other source. And then, frequently there is a true economic loss, often for the origin shipper that must pay the market difference for the grain at destination to be “bought in” from some other source to replace the lost delivery. So, the correct response to the question, “will grain wait on freight” is yes, but at a potentially significant economic cost to the shipper and the farmers being served at that loading point. An additional problem is that the market does not provide any reasonable incentive to the carrier to perform in a timely way under such circumstances, so that the economic penalty falls almost completely on the customer of the carrier.

Regarding specific issues related to common carrier service:

1. Car Supply Issues.

Faced with the choice of furnishing their own cars or forgoing rail service, shippers have been forced to replace railroads as the primary suppliers of freight cars. According to AAR data (*Equipment Report*, 2007), shippers supply virtually 100% of all tank cars and 66% of all covered hopper cars, as well as substantial segments of the gon-

dola fleet and equipment necessary to transport automobiles. In some instances, even where carriers operate covered hopper cars, they refuse to make them available for the transportation of certain commodities (most notably, dried distillers grain, a significant byproduct of ethanol production) or do not offer specialized cars necessary to handle flour. Carrier car supplies for soybean meal, a relatively benign commodity, generally are inadequate. With only one-third of the covered hopper car fleet, Class I railroads cannot meet even "average demand" for that type of equipment, which is their common carrier obligation. *See National Grain and Feed Association v. United States*, 5 F.3d 306, 311 (8th Cir. 1993).

At one time, railroads paid either mileage allowances or freight rate differentials to compensate shippers for private cars. *LO-Shippers Action Comm. v. Aberdeen & Rockfish Ry.*, 4 I.C.C. 2d 1 (1987), *aff'd.*, *LO-Shippers Action Committee v. ICC*, 857 F.2d 802 (D.C. Cir. 1988) and *Ex Parte 328 Investigation of Tank Car Allowance System*, 3 I.C.C. 2d 196 (1986). When rail transportation contracts were widely used for agricultural commodities, beginning in the mid 1980s, it was not uncommon for a negotiated rate to exclude payment of mileage allowances for tank cars. However, as railroads began to discontinue the use of rail transportation contracts, especially in the past two or three years, the common carrier rates that they offered were devoid of mileage allowance compensation, although the railroads argued that their rates would be even higher were they to make actual mileage allowance payments. As a result, there is a growing segment of tank car rates for agricultural commodities that apply by definition in private cars (because railroads have no tank cars) and yet pay no mileage allowance.

In *LOSAC*, the ICC determined that compensation for private covered hopper cars should not be on a prescriptive basis similar to the Ex Parte No. 328 system, and that “market conditions” should determine covered hopper car allowances. Unfortunately, however, where carriers provide covered hopper car compensation, either through mileage allowance payments or freight rate differentials, allowance payments to shippers do not reflect the marketplace. Allowances and freight rate differentials remain static even though the value of covered hopper cars has increased dramatically.

Where the railroads’ common carrier car supply obligation is concerned for agricultural commodities, it appears that the railroad industry is neither supplying an adequate number of cars nor compensating shippers to do so in their place.

NGFA is not seeking to establish a statutory violation by railroads of any particular aspect of their common carrier obligation in this proceeding, as that does not seem to be the Board’s purpose. In keeping with the Board’s stated goal of acquiring more information regarding various aspects of the common carrier obligation, NGFA brings these conditions to the Board’s attention. Hopefully, the Board will consider whether a railroad that does not supply cars and does not compensate shippers for doing so is fulfilling its common carrier car supply obligation.

2. Carriers setting conditions to receive common carrier service

Although the agricultural shipping community copes with historical car supply problems by relying on private cars to a great extent, other aspects of common carrier service are becoming increasingly problematic.

One such aspect consists of conditions set by railroads for the institution or maintenance of service. The burgeoning production of ethanol and biofuels have led to the

construction and expansion of renewable liquid fuel facilities that rely heavily on rail service. Companies attempting to construct or expand such facilities are encountering a range of obstacles and conditions that may conflict with the Section 11101(a) common carrier obligation or other related statutory provisions.

NGFA recognizes that railroads have a legitimate interest in protecting the integrity of their operations from unsafe or impractical conditions and that there will in many cases be sound reasons for railroads to resist providing service at points preferred by shippers.

Nevertheless, NGFA does not believe that railroads have the right to unilaterally fix the terms and conditions on which they will provide common carrier service, free of any standard except their own self interest. Members of the agricultural community have encountered numerous instances where railroads impose unilateral or virtually non-negotiable conditions highly favorable to their own interests before they will agree to install or upgrade service to a shipper facility. These practices include long delays in furnishing actual facilities, such as switches, for installation or withholding written agreements until shippers have essentially completed their construction or upgrades, placing shippers in a position where their investments conflict with their ability to negotiate terms; requirements for infrastructure within the shipper's facility; total absorption by shippers of switch installation costs even where traffic will be sufficient to warrant a switch installation investment by a carrier; long-term prepayment of maintenance costs; service cancellation clauses; and liability assumption provisions that are decidedly carrier friendly.

A Plant Infrastructure.

Most often, large railroads are unwilling to serve new agricultural facilities unless those facilities are equipped internally to ship and receive large train units on terms that are acceptable to the carrier. If a new ethanol plant is constructed, most carriers require that their approval be given in advance of installing a switch connection to the plant to a plan for the construction of internal plant trackage acceptable to the carrier. These requirements normally are in addition to shipper payment for the installation of high speed switches between the carrier's line and the plant trackage.

For example, if a shipper wishes to construct an ethanol production facility, there are likely to be 100-car shipments (although that is not always feasible) of both ethanol and its byproduct, dried distillers grain (DDG). Some carriers thus require that the plant have a track capable of holding 100 to 110 loaded ethanol tank cars. In addition, the carrier will demand that the plant construct a second, nearly identical, track to hold 100 or more empty tank cars, the idea being that the carrier can use one set of engines and one crew to place empty cars on one track and then remove loaded cars from the next track. Since the plant also produces DDG, the carrier will want two similar tracks for DDG. And, if the plant receives corn by rail, the carrier will insist on a third set of tracks to handle empty and loaded corn cars.

Each separate track will cost the shipper well over a million dollars to install, yet two sets of tracks for each commodity are not operationally necessary. The carrier could make two trips with its engine and crew, one to remove loads and a second to place empties, all on the same track. Admittedly, that would be a more costly method of operation for the carrier. But shippers who are required by carrier conditions to the institution of service to build duplicate tracks receive no compensation for doing so, while the carrier

experiences a cost savings that it is under no compulsion to share with the shipper and does not do so through reduced rates. Carriers construe the implementation of their common carrier obligation as allowing them to impose costs on the shipper that are of primary benefit to the carrier.

B. Delays in Making Switch Connections

Normally, prior to the construction of a new synthetic fuel facility, discussions are instituted between shipper and carrier with respect to site selection. Carriers have ample notice of when service will be required and will have approved engineering plans well before the shipper facility construction begins. Nevertheless, as the commencement date for service approaches, shippers seem to face long delays in the completion of switch connections by carriers, in some cases delays of a year or more. These delays in the institution of service are incongruous with the Board's rules requiring that carriers respond to requests for rates and service terms within 10 days, a requirement that apparently evinces the Board's view that service unduly delayed is service unduly denied.

C. Withholding Essential Agreements

The institution of common carrier service normally entails certain types of agreements between shipper and carrier. Even though carriers are aware long before service actually is commenced that a shipper is relying on receiving rail service, carriers normally neglect to provide their proposed written agreements to shippers for discussion or negotiations until the shipper is well into the process of constructing a new facility and probably well beyond the point where it can bargain meaningfully over conditions imposed by the carrier for common carrier service to be provided to the shipper. These

conditions assist the carrier in extracting one-sided terms and conditions to provide requested rail service.

D. Risk Shifting

The availability of common carrier rail service increasingly has become subject to various methods by which railroads shift the risks of rail service to their customers, either entirely or on a one-sided basis.

The three most common areas where risk-shifting occurs are with respect to the installation and maintenance of switch connections; grade crossing agreements that make it possible for trucks to deliver or remove materials from an agricultural facility; and so-called industry track agreements which generally pertain to the track on which cars are interchanged between shippers and carriers.

The necessity of a switch connection and an interchange track for the provision of rail service are both obvious. Without a switch connection, the shipper has no access to the rail network. Without an industry interchange agreement, carriers refuse to allow their engines to enter upon shipper track to either pick up or drop off cars. And, so long as carriers take the position that they will not pick up or drop off cars without an industry track agreement, there likewise is no common carrier service.

Grade crossing agreements present a slightly more tangential aspect of common carrier service. They often apply to private roads that cross rail track in order to reach a facility that is served by the common carrier railroad. Normally, these grade crossings are the only means of ingress or egress to the shipper facility. A grain elevator, for instance, requires vehicular access so that corn or other commodities can be delivered for movement by rail. A soybean processing plant requires vehicular access to receive soy-

beans and to provide delivery of feed ingredients, such as soybean meal, to nearby customers who can be served by truck. Where new facilities are constructed, the practice of carriers more often than not is to tie the execution of a grade crossing agreement to the carrier's willingness to install a switch connection. Switch connections, industry track interchange agreements, and grade crossing agreements thus have all become essential components of common carrier service.

As mentioned earlier, railroads all too frequently make it a practice to withhold presentation of these agreements until a shipper facility has been nearly completed and the shipper is in a position of needing to commence rail service as quickly as possible. Under these conditions, the shipper has little or no bargaining position.¹

Whether an agreement is one for a switch connection, interchange track, or grade crossing, it will invariably have risk assumption provisions that favor the carrier. These provisions may have certain mutual negligence clauses, but most often they require a shipper assumption of liability, accompanied by an indemnity commitment, for certain activities that take place on the switch connection, interchange track, or grade crossing regardless of carrier negligence or with the exception of only gross or willful carrier negligence. Shippers who attempt to seek relief from these provisions normally are told by the carriers that the agreements are non-negotiable.

NGFA questions whether risk-shifting provisions, especially those that do not arise from genuine arms-length negotiations, are an appropriate premise for common carrier service to commence or continue.

3. Service Priorities

¹ The Board has jurisdiction over switch connections pursuant to 49 U.S.C. § 11103

Shippers of agricultural commodities increasingly are confronted with various forms of carrier action that evince the assignment of carrier service priorities. The most common type of service priority observed by members of NGFA's Rail Shipper-Receiver Committee, who were surveyed for the purpose of preparing this statement, is a carrier's election to give preference to certain types of shipments, such as 100-car unit trains versus 25 car units. Carriers find it more convenient to handle larger units, and simply defer service for smaller units whenever one element or another of their capacity is in short supply. The deferred units do not necessarily service the same markets as those the carriers choose to handle, and so the impact of this type of service prioritizing falls unevenly on those who have requested rail service.

A matter of growing concern to NGFA is how the railroads plan to prioritize their services if capacity increasingly becomes in short supply across the board, a state of events that the railroad industry believes will be upon us shortly and that the Board seems to believe will occur.

The agricultural community already has seen examples of selective rail rate increases intended to "demarket" specific movements deemed undesirable by a carrier through quoting rates that are increased by many multiples of the existing rate and that are intended by the carrier to make use of rail service impossible. These tactics presently are used when a railroad believes it can replace traffic from one origin with traffic that can be handled more efficiently from another origin. If capacity constraints become as widespread as the railroads are encouraging the public to believe, we can expect a greater use of these types of rate increases as a method of rationing capacity.

Freight rate increases designed to discourage traffic movements are not a legitimate form of differential pricing or, in the opinion of NGFA, a legitimate response to a reasonable request for transportation service from a railroad. The President of a major Class I railroad told an electronic conference of rail industry analysts on March 6, 2008, that his railroad is open for business, but only if that business will result in improving returns. Rate quotations, aimed not at the transportation of traffic but at putting an end to the transportation of traffic, are just as deceptive as the "fuel surcharges" that were recognized by the Board as unreasonable because they did not, in fact, have as their primary purpose the recovery of fuel costs. *See Ex Parte No. 661, Rail Fuel Surcharges*, April 26, 2007.

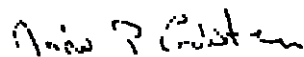
If rail capacity truly is in short supply, the allocation of scarce railroad resources will be challenging. Members of NGFA have heard many different railroads and railroad investors say that the railroad industry should have the unfettered prerogative to determine how railroad assets should be used by their private owners. NGFA is not unsympathetic to the point of view that the owner of an asset normally should determine how the asset is utilized. But railroads are not altogether like other businesses. As this proceeding underscores, railroads are common carriers, and common carriers have certain prerogatives, such as the right of eminent domain, not enjoyed by private enterprise generally, and that are available precisely because there is a "public interest" aspect of common carriage.

NGFA would hope that if conditions truly demand capacity rationing, railroads take a common sense approach to the public interest, and not shun essential commodities,

such as, for example, feed for animals or energy-generating commodities, merely because railroads or their investors see greater profits in transporting other types of goods.

NGFA concludes its statement by again thanking the Board for instituting this significant proceeding and by expressing our hope that the comments submitted by the parties will make a contribution toward a needed definition of the "common carrier obligation."

Respectfully submitted,



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