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U.S. RAIL CAPACITY CRUNCH

(109–66)

HEARING

BEFORE THE

SUBCOMMITTEE ON

RAILROADS

OF THE

COMMITTEE ON
TRANSPORTATION AND
INFRASTRUCTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED NINTH CONGRESS

SECOND SESSION

APRIL 26, 2006

Printed for the use of the
Committee on Transportation and Infrastructure

U.S. GOVERNMENT PRINTING OFFICE

28–281 PDF WASHINGTON : 2006

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U.S. RAIL CAPACITY CRUNCH

Wednesday, April 26, 2006

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON RAILROADS, COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE, WASHINGTON, D.C.

The subcommittee met, pursuant to call, at 10:04 a.m., in Room 2167, Rayburn House Office Building, Hon. Steven C. LaTourette [chairman of teh committee] presiding.

Mr. LATOURETTE. The Subcommittee will come to order this morning. I want to welcome everybody to our hearing this morning about the U.S. Rail Capacity Crunch.

In 1980, our Nation's rail industry was in dire straits. Twenty percent of our Nation's railroads had gone into bankruptcy in the previous decade, including most of the railroads in the northeast. Many holders of railroad stocks and bonds were left with nothing more than worthless pieces of paper. Competition from trucks had sapped the railroads' traditional traffic base. New investment was needed to meet this competition, but the regulatory regime of the old ICC made this impossible. The ICC forced the railroads to maintain and operate unprofitable branch lines while the busy main lines suffered from years of deferred maintenance and neglect.

Just how bad were the tracks back then? Legend has it that the old Penn Central experience: standing derailments, a situation where a parked train topples onto its side when the tracks give way underneath.

The 1970s were dark days for shippers as well. Labor, fuel, and other costs were rising faster than inflation. But the railroads had little incentive to improve efficiency. Inflative costs were merely passed on to the shippers in the form of higher tariffs blessed by the ICC.

Private investors abandoned the rail system. The remains of the Penn Central system ended up in Government hands under the name of Conrail. Likewise, the burden of operating unprofitable passenger service fell to another Government entity, Amtrak.

Something had to be done or the entire rail system would have ended up bankrupt or nationalized. The answer to this immense problem was the Staggers Rail Act of 1980. Staggers released the railroads from the Government regulatory stranglehold and helped attract billions in new private capital. The rail system underwent a drastic restructuring: the number of employees was drastically reduced; many tracks were torn up and sold for scrap; excess main line capacity was eliminated; unprofitable branch lines were sold to

entrepreneurs; cost cutting became a science; new markets such as premium intermodal service came to the fore.

Rail rates have declined in real terms since the passage of Staggers, while productivity has tripled. At the same time, the industry's safety record has improved immensely, with far fewer injuries or deaths per year than in the 1970s, and we no longer hear of any standing derailments.

But this success has not come without a cost. Twenty-six years after the passage of Staggers, our railroads have become congested, sometimes nearly to the point of gridlock. Shippers are complaining that it takes longer to move a car across the Country now than it did 10 years ago. In some cases, our farmers have been unable to obtain cars to move their products to market. The demand for coal has soared, but utilities have reported difficulty in moving coal from the mines to the power plants.

As incredible as it may seem, railroads are having a difficult time finding qualified workers to meet these new service demands. Much of the older generation is near retirement and it seems that many younger people are put off by the long hours, mental stress, and physical labor required by most railroad jobs. Railroad workers might seem to be well paid, but let me tell you my experience is they earn every penny that they are paid.

The world has changed since 1980. We no longer have the option of diverting rail freight traffic onto our highways, and anybody who has driven the Beltway recently during rush hour knows why. All across the Country motorists are sick of being stuck in traffic every day. People are demanding solutions such as new rail passenger service, but in many cases this is not really new service, we are only trying to restore what was abandoned in the 1950s and the 1960s.

In today's hearing, a quarter century after the passage of Staggers, I hope to learn what it is going to take to build the new rail system of 2050, a system which will carry both freight and passengers with speed, economy, and efficiency.

Before yielding to Ms. Brown, I do want to yield to the chairman of the Highway Subcommittee just for a minute to welcome one of his constituents, Mr. Busalacchi, who is on our now second panel; and I will explain how that happened.

Mr. Petri, is there some Wisconsin word of welcome you would like to—

Mr. PETRI. Yes. Thank you very much. It is my pleasure today to join you in welcoming Frank Busalacchi, someone I have had the opportunity to get to know because we both work on transportation issues, and he has been a strong leader in our State Government and now nationally, and is appearing for a national coalition in the rail area. We work more on highway things, but rail things as well. And I am looking forward—I have been reading his testimony. I am hoping to get back in time for it.

But, again, welcome, Frank.

Mr. LATOURETTE. Thank you very much, Mr. Petri.

I want to ask unanimous consent to allow all members to have 30 days to revise and extend their remarks and to permit the submission of additional statements and materials by the witnesses. Without objection, so ordered.

It is now my pleasure to yield to our distinguished ranking member, Corrine Brown from Florida, for any observations she would choose to make.

Ms. BROWN. Thank you, Mr. Chairman. And thank you for hosting this Committee meeting. It could not come at a more appropriate time, because I believe we are on the verge of a crisis in our Nation railways. Thanks to economic growth and a sharp increase in international trade, the railroad industry has more business than it has capacity to handle.

And while the Nation's freight railroads is in much more financial health today than it was in the 1980s, when we partially deregulated the industry, the railroads still do not earn enough to cover the costs of capital. As a result, railroads have either had to defer maintenance or cut back on the number of miles served. The size of the freight rail network has deteriorated to about half of what it was 26 years ago, but our freight shipments have more than doubled.

We need to find a solution, a permanent solution, to this problem or the situation will only get worse. According to the U.S. Department of Transportation, rail traffic is expected to rise more than 50 percent by the year 2020. A traffic growth, traffic bottleneck will further impede freight and passenger rail operation and adversely impact the business of railroad customers, many of which count on just-in-time delivery. Moreover, as gas prices rise $3.00 and $4.00 a gallon, recovery drivers will turn more and more to commuter rail and Amtrak, putting even more pressure on an already congested system.

I know that there are many ideas out there for helping our Nation's railroads. Railroads are critically important to our Nation's economy, health, and development, and they must have adequate support from the Federal Government, just like we do for aviation, highways, and mass transit, if they are to continue to meet the needs of their customers and if they are to continue to keep truck traffic off of America's highways.

I want to welcome today's distinguished panelists, and I am looking forward to their insight on ensuring the fairest and more effective freight rail service for both the railroad and their customers.

I thank you, Mr. Chairman.

Mr. LATOURETTE. I thank you very much.

Become of some time constraints, we are next going to yield to Mr. Miller of California.

Mr. MILLER. Thank you, Chairman LaTourette.

This is an extremely important issue in my district. I represent Southern California. I appreciate the opportunity of having you here today to hear your testimony, and we are going to try to deal with a real serious issue, and that is how do the railroads invest in infrastructure. Not only new infrastructure, but dealing with the current infrastructure you have to maintain because, in California, moving goods and people are extremely important. And, especially in my district, capacity is something we are having to deal with. I represent an area that the Alameda Corridor runs through, and the Ports of Long Beach and L.A., most of materials come through my district, and it is really scary because if you can't load containers on trains, they have to go on trucks.

And if you have driven the freeways in Southern California and you see the amount of trucks, you realize that we don't have the capacity on freeways to load containers on more trucks. I mean, they are doing a great job. The trucking industry has really stepped up and they are trying to do everything they can to move goods, but there are bulk goods that need to be moved by rail, and it is becoming more and more difficult all the time to do that. And the shipping industry needs to remain competitive, and without timely delivery of shipments in our Country, the economy is going to be impacted overall.

I have been in part of the building industry for about 35 years, and there is a tremendous amount of goods in the industry shipped by rail initially, and then when it gets to retailers, it tends to be shipped by trucks. But if we can't put those goods on rail, we are going to add more and more impact on our roads, and we just don't have the infrastructure to accommodate that. Not only that, but think about the coal that is moved, the energy shipment we are dealing with today, the crisis we are having to deal with and the goods that are moved by rail.

We have to deal with the situation where shippers and the railroads need to work together, and how do we do that. How do we do that in a fair way? I mean, the railroads get beat up a lot of times because of capacity, but then the railroads are required to share their lines to move people. And that was not the initial purpose of building those railroads, it was built to mainly ship goods for profit. And you are allowing your rails to be used for other purposes, and that has to happen in this Country because we need to move people today. But we have got to find a solution where the funds are available to the railroads to invest in infrastructure, and at some point in time Government has to be part of the problem and the solution. We are the problem in many cases, but we have to be part of the solution. And we voluntarily become part of the problem often through regulations and legislation, but we need to voluntarily become part of the solution of this problem also.

And I am looking forward to the testimony.

Chairman, I think this is timely to do this.

I would encourage you to come to my district sometime and see the amount of goods being shipped by rail and the amount of goods being shipped by truck, and you would realize we do not have the capacity in our highways to put more containers on trucks, and that leaves us no alternative but to make sure we do everything we can to make sure the railroads can compete in a timely fashion and that they can produce as they need to delivering those goods and services to our Nation.

Thank you. I yield back the balance of my time.

Mr. LATOURETTE. And I thank you very much, Mr. Miller. And I think you will find that a lot of the testimony deals with your part of the Country today, and I thank you for your participation and your interest.

Ms. Johnson of Texas.

Ms. JOHNSON. Thank you very much, Mr. Chairman. I want to thank you and Ranking Member Brown for holding this important hearing on the issue of rail capacity.

As we all know, our Nation's freight rail system is an integral component of our Nation's robust economy. Each day, freight rail delivers tons of raw materials and consumer goods that support an array of business sectors throughout the Country. According to a recent report by the Congressional Budget Office, rail transportation is responsible for the transport of 70 percent of coal delivered to power plants, 70 percent of domestic manufactured automobiles, and 32 percent of grain shipments.

As manufacturing has become more global and their supply chains have become longer and more complex, freight rail has become a critical component for firms and industries. In the Dallas-Fort Worth region, exploding intermodal growth, coupled with increasing international trade with China, is reshaping the region's economic and freight rail landscapes. In my district, the evidence of this growth is unmistakable. Union Pacific has just completed a $100 million intermodal facility to support the growing intermodal volume and increased trade to the region, and I appreciate Union Pacific's decision to invest in my district as the economic impact on the surrounding area is expected to create 20,000 new jobs and $5 billion in development over the next 15 years.

Cargo bound for the U.S. from China has grown an average of 34 percent annually since 2002. Much of this traffic filters through the Tower 55 corridor in the north Texas region, as China is the world's leading seller of goods to the Dallas-Fort Worth market. Delays at Tower 55 today exceed capacity. Significant future growth in freight rail is expected and addressing this problem remains a top priority. On a busy day, Tower already sees in excess of 120 trails, and on an average day it is occupied 70 percent of the time. Obviously, this type of demand is placing enormous strains on existing rail capacity in our region and has highlighted the need for additional infrastructure.

And while I fully understand this need, I am also aware that, unlike any other mode of transportation, railroads are responsible for paying for and maintaining their own infrastructure. This type of arrangement obviously has implications on infrastructure investment. As a result of this, I think it is imperative that we be proactive in formulating policy that supports, not prohibits, the industry in expanding capacity to avoid a congestion crisis that could endanger or even cripple our Nation's economy.

As I close, I want to thank our witnesses that are coming before us today, particularly Mr. Matt Rose of BNSF Railroad from Fort Worth, Texas. I look forward to that testimony, as I am particularly interested in learning more about their thoughts in how we may all work together in addressing current and future capacity challenges.

Thank you, Mr. Chairman. I yield back.

Mr. LATOURETTE. I thank the gentlelady very much.

Mr. Bachus from Alabama.

Mr. BACCHUS. I thank the Chairman. Mr. Chairman, I will simply say two things. One is that there is a great need for more rail infrastructure and capacity, and I think there is a solution and there is ″not-a-solution.″ I think the ″not-a-solution″ is to re-regulate rail. And I think that is, bottom line, what H.R. 2047 does. I think it would actually have disastrous consequences. On the other

hand, I do believe that we should give the railroad all sorts of incentives, tax incentives, and I actually think that what is being proposed is insufficient and we should go further and be more comprehensive.

It is an economic issue. It is also a safety issue for any of us that have traveled the highways. And we can either turn our highways into rail lines by increasing the size of our trucks, or we can make the investments that we have been making on our highways when we should have been making more of an investment in our rail lines.

But I think that the best solution for the Government is simply to give the incentives to the railroads and let the railroads build the lines with as little regulation as possible.

I yield back the balance of my time.

Mr. LATOURETTE. I thank the gentleman very much, and I think you will be pleased by some of the testimony today. Some of our witnesses will not only talk about some tax structures, but also ways to set rates and do other things that would increase the ability of infrastructure dollars.

Mr. Boswell, from my own—no?

Mr. Sodrel, any opening remarks you want to make?

Mr. SODREL. I don't have any opening statement. Thank you, Mr. Chairman.

Mr. LATOURETTE. I thank the gentleman.

As I indicated before, we are going to go a little bit out of order. We have a request from Congressman Lipinski, Congressman Lipinski from the Chicago area in Illinois. His father, of course, is well known to all of us who serve on this Committee. When I was elected in 1994, Bill Lipinski was the ranking member of the Aviation Subcommittee, I think, and then went on to the Highway Subcommittee; instrumental in drafting a lot of the legislation that this Committee has passed over the years. His successor and his son now has his seat outside or in the Chicago area. So the first panel today will be comprised of the Honorable Dan Lipinski from Illinois.

Thank you, Congressman, for being here, and we look forward to hearing from you.

TESTIMONY OF THE HONORABLE DANIEL LIPINSKI, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS

Mr. LIPINSKI. Good morning. I would like to start off by thanking Chairman LaTourette and Ranking Member Brown and the Committee for giving me this opportunity to come here to speak on this very important issue, something that is certainly critical to our Nation, also to my district, the City of Chicago and the State of Illinois.

While the volume of rail traffic in the U.S. continues to increase, many of our rail systems are antiquated and cannot handle the growing demand. Efficient rail transport is imperative to the economic prosperity of our Nation, so it is critical that we find more ways to improve rail infrastructure and that we support the railroad industry's efforts to improve the movement of goods across our Nation.

As you know, the Chicago area is a perpetual bottleneck for freight rail moving across the Country. I just was looking up at the map there. You can see where all the lines come together very nicely right there in Chicago, producing a very important regional choke point. And choke points such as this impede the efficient flow of commerce, which results in economic losses for businesses and for consumers. And the freight rail congestion also has a negative impact for passenger and commuter rail services.

So with freight traffic expected to double by 2025, our rail infrastructure must be significantly improved or the problems will continue to mount, making congestion more difficult to alleviate and increasing the cost of fixing the situation somewhere down the line. We must continue to provide Federal support to program initiatives that innovatively address the capacity shortage.

One of these initiatives is currently beginning in the Chicago area. While it takes a freight train two days to get from California to Chicago, it takes two days just to get that train through Chicago. To address this growing congestion problem, the Illinois Department of Transportation, the Chicago Department of Transportation, Metro Commuter Rail, and Association of American Railroads, including BNSF, CSX, Norfolk Southern, Canadian National, Union Pacific, and Canadian Pacific, join together to form a unique public-private partnership and developed a plan to ease the bottleneck.

The Chicago Regional Environmental and Transportation Efficiency Project, known as CREATE, is a $1.5 billion 10-year plan that will make significant strides in reducing congestion by modernizing the Northeastern Illinois rail network. CREATE will completely overhaul the system by focusing on 25 new grade separations and 6 rail-to-rail flyovers which will separate freight and passenger lines. By fixing the Chicago bottleneck, this landmark proposal will result in national benefits and set a precedent for streamlining freight and passenger rail lines.

CREATE will also provide additional benefits: traffic delays and grade crossing accidents will be reduced; air pollution from trains and from vehicles on the roads will be lowered; and the consumption of gasoline and diesel fuel will be decreased. And infrastructure investments in CREATE will also create tens of thousands of new good paying jobs.

The National Commission on Intermodal Transportation recognized the regional bottleneck problem and recommended that Congress provide Federal funding incentives for intermodal projects of national and regional significance. The CREATE program is certainly one of these, and was recognized as such by the Committee in last year's SAFETEA-LU bill. I would like to thank the Committee and its leadership for providing the $100 million as we begin this critical program. Also, I would like to thank Mr. Ed Hamberger and the AAR for the continued commitment and support for CREATE throughout this past year.

Study after study has shown us that if we move freight in a more cost-efficient and time-efficient fashion, it means a more dynamic economy, more affordable consumer goods, and ultimately a better quality of life for all Americans. I ask the Committee to continue to provide the support for CREATE and other critical rail projects

that are essential to reducing the congestion on our rails in this Country.

Once again, the efforts and commitments of the railroads to improve the rail infrastructure in this Country are to be applauded, and we must continue to work on important projects such as CREATE that will alleviate the increasing congestion and make rail travel in this Country, both freight and passenger, more efficient modes of transportation and economic engines for our Nation.

I think CREATE provides a good framework, public-private partnership, getting the State, the City of Chicago also to put in funding, the railroads together. It is a good example of what we can do, what we should be doing, and the Federal Government must also continue to fund CREATE and other important programs such as this to ease congestion that we are talking about here today

So I would like to thank the Chairman and the Ranking Member for my time today.

Mr. LATOURETTE. Well, I thank the gentleman for his excellent testimony, and, clearly, the CREATE project is one that both his father and he and Mr. Costello and Speaker Hastert have done an excellent job of bringing to the attention of the Committee, and that work was rewarded somewhat in the passage of SAFETEA-LU. And I thank you for taking your time to come share your thoughts with us today.

And I want to yield just for a few minutes to Mr. Costello, who I think may want to talk on the same subject.

Mr. COSTELLO. Mr. Chairman, thank you. I will be very brief. One, let me say that I do have a formal statement that I would ask unanimous consent that I be allowed to be enter it into the record.

Mr. LATOURETTE. Without objection.

Mr. COSTELLO. And let me commend also the Governor of Illinois, the State of Illinois, the City of Chicago, and the railroads that Mr. Lipinski mentioned for their commitment to the CREATE project. Projects like CREATE, an innovative plan, will be part of the solution to the capacity crunch not only in the Chicago area, but these types of projects, in my judgment, are the solution to the national problem that we face with the capacity crunch.

Let me also commend our colleague, Dan Lipinski. He was very involved, as you mentioned, along with his father and others, in trying to push this project along because of its importance not only to the Chicago area, but to the Nation. And I know that he will continue to be committed to this project and will continue to do everything he can to make certain that the Federal Government steps up to the plate, along with the private sector and the City and the State of Illinois.

And with that, Mr. Chairman, I welcome our witnesses and look forward to hearing their testimony.

Mr. LATOURETTE. I thank the gentleman very much. The Chair is anxious to get to the second and third panels, but I do note—and I don't want to foreclose the opportunity of any member to make some brief remarks.

Mr. Westmoreland, Mr. Graves, and Mr. Cummings, anything you would like to say before we get started?

[No response.]

Mr. LATOURETTE. Okay, that business having been conducted, we will now go to what has become our second panel. I want to welcome the six witnesses on the second panel for today's hearing.

Our first witness will be the Honorable Joseph Boardman, who is the Administrator of the Federal Railroad Administration. Before he began at the FRA in 2005, Mr. Boardman served as the Commissioner of the New York State Department of Transportation. He has been involved in the transportation industry at the local, State, and now Federal level for over 30 years, and, Mr. Boardman, I would note that, with your appearance today, you have now become the most frequent witness of this Subcommittee's hearings, and I congratulate you on that distinction.

Our second witness this morning will be the Honorable Frank J. Busalacchi, the Secretary of the Wisconsin Department of Transportation and the Chairman of the States for Passenger Rail Coalition. The Passenger Rail Coalition is made up of 27 State transportation agencies that support the development and expansion of intercity passenger rail.

Next will be Mr. Matthew K. Rose, who is the President and CEO of the Burlington Northern Santa Fe Corporation. He has been with BNSF since 1993, steadily moving up the executive ranks since his start. Mr. Rose was named President in 1999 and in 2000 also assumed the responsibilities of being the Chief Executive Officer.

Mr. Edward Hamberger, who is also a frequent flier at our hearings, is the President and CEO of Association of American Railroads. Mr. Hamberger began his career in transportation in 1977 as General Counsel of the National Transportation Policy Study Commission. He also served as Assistant Secretary for Governmental Affairs at the Department of Transportation, where he implemented the Reagan Administration's legislative strategy on transportation issues.

Mr. Richard F. Timmons is the President of the American Short Line and Regional Railroad Association. This Association represents a diverse group of regional and short line railroads that make up an important part of the overall rail network in this Country.

And last but not least is Mr. William W. Millar, the President of the American Public Transportation Association. APTA members include public bus, rapid transit and commuter rail systems, and the private organizations responsible for planning, designing, constructing, financing, supplying, and operating transit rail systems. In addition, Government agencies, metropolitan planning organizations, State department of transportations, academic institutions, and trade publications are also part of APTA's membership.

I want to thank each of you for coming. I want to thank each of you for submitting your testimony so that we can review it ahead of time. We do have a rather robust schedule for this hearing today. This panel will be followed by an equally large panel. If you can, I would ask you to be mindful of our newly designed light system here, which has sort of a five minute benchmark for opening statements.

But that having been said, welcome. Thank you for being here. And, Mr. Boardman, we look forward to hearing from you.

TESTIMONY OF THE HONORABLE JOSEPH BOARDMAN, ADMINISTRATOR, FEDERAL RAILROAD ADMINISTRATION; HONORABLE FRANK BUSALACCHI, SECRETARY, WISCONSIN DEPARTMENT OF TRANSPORTATION, CHAIR, STATES FOR PASSENGER RAIL COALITION; EDWARD HAMBERGER, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS; MATTHEW K. ROSE, PRESIDENT AND CEO, BURLINGTON NORTHERN SANTA FE RAILWAY; RICHARD F. TIMMONS, PRESIDENT, AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION; AND WILLIAM W. MILLAR, PRESIDENT, AMERICAN PUBLIC TRANSPORTATION ASSOCIATION

Mr. BOARDMAN. Thank you, Mr. Chairman and Ranking Member Brown, for having me here today to represent Norman Mineta, the Secretary of Transportation. In the spirit of being a frequent flier, I will be very short in my oral remarks and ask that my written testimony be submitted.

As we have heard here today, the economy is strong. It is getting stronger. We have also heard here today that Staggers was a success and made tremendous improvements in efficiency for railroading in this Nation. But the excess capacity that was available is now gone, and what we need is greater investment. It is needed in our physical infrastructure, in our technology that we operate with today, and in the operational aspects of the railroads. And, yet, where we are today is with no agreement on the balance of the investment that is needed either in railroads or in other freight areas of this industry and how we might fund it for the future.

I remain available for any questions you might have.

Mr. LATOURETTE. Well, thank you very much for that concise set of remarks, Mr. Boardman.

Mr. Busalacchi, thank you for being here. Welcome. We look forward to hearing from you.

Mr. BUSALACCHI. Thank you, Mr. Chairman. My name is Frank Busalacchi. I serve as Secretary of the Wisconsin Department of Transportation. I am here today as Chair of States for Passenger Rail Coalition, a group of 27 State transportation agencies that support U.S. intercity passenger rail development. Our Coalition was founded in 2000 driven by a number of factors.

Thirteen States currently provide funding to support intercity corridor services in partnership with Amtrak. You may not be aware of the fact that these State-supported services provide 37 percent of Amtrak's total ridership and about half of Amtrak's daily trains.

Some 35 States have developed transportation plans that call for intercity passenger rail improvements.

Finally, widespread public demand for intercity passenger rail service is reflected in robust increases in intercity passenger rail ridership throughout the Country. For example, the Hiawatha Service between Milwaukee and Chicago supported by the States of Wisconsin and Illinois, set an all-time record in 2005 with more than half a million riders, a 16 percent increase over the prior year. Similar increases in ridership are evident in State-supported services throughout the Country. For example, Pennsylvania's Keystone Service, Illinois' Chicago-St. Louis Service, Maine's

Downeaster, and Oklahoma's Heartland Flyer also had double-digit increases in 2005.

However, while public demand is growing, rail congestion throughout the Country has become a significant threat to States supporting or desiring to implement new passenger rail service. Virtually all current and planned State-supported services operate on corridors owned by freight railroads. Many of these corridors are facing increasing levels of congestion. This rail congestion is driven by increases in freight traffic, as well as bottlenecks caused by aging track and infrastructure.

These rail capacity and congestion problems are reflected in declining trends in passenger rail on-time performance. On-time performance for all State-supported and other short distance trains for fiscal year 2005 was only 70.4 percent.

Some of these statistics disguise even more severe problems in specific corridors. In January of this year, on-time performance for the San Joaquin Service in California was only 35.2 percent. For the same period, on-time performance for the Cascades Service in Washington State was 50.5 percent, and on the Carolinian in North Carolina it was 19.4 percent.

The members of States for Passenger Rail Coalition do not view these capacity problems as insurmountable. We all have extensive passenger rail plans to make improvements in track and signaling infrastructure that also address capacity issues on host railroads.

A national survey documented $10.4 billion in track, signal, and equipment improvements planned by States in freight corridors, which could be programmed over six years, and a total of $47 billion in capital needs over a 20 year period. These corridors are frequently in highly congested urbanized areas where rail capacity issues are most often severe for both passenger and freight operations.

With all of this State interest in intercity passenger rail development, why is on-time performance continuing to decline? The States for Passenger Rail Coalition firmly believes that the missing ingredient is a reliable Federal funding partner. We believe our highly successful Federal programs for highways and airports offer models for long-needed congressional action to address the critical passenger rail corridor improvements. Federal investment in passenger rail improvements can address freight rail capacity needs, while at the same time showing a public transportation benefit.

In the past we have supported tax credit bonding authority for States as one mechanism for ensuring funding continuity for major corridor development projects, which typically take several years to complete. We are on record supporting H.R. 1631, known as Ride 21, which provided $12 billion in tax credit bonding authority to States. We are encouraged by recent bipartisan Senate action on S. 1516. This legislation provides an authorization of $1.4 billion and 80/20 Federal/State funding to States subject to appropriation, which we believe is a good start.

The States for Passenger Rail Coalition stands ready to assist the House Rail Subcommittee in developing intercity passenger rail legislation that can be added yet this year. We believe the public expects such a program. The public needs mobility alternatives to congested highways and airports. As the pump price for fuel contin-

ues to march steadily upward, the public's demand for energy-efficient rail service will continue to increase. The benefits are there, to the general public, to the freight railroads, to the shippers they serve, and to the Nation's economy. What is needed now is congressional resolve to take action.

Thank you very much.

Mr. LATOURETTE. I thank you very much, Mr. Busalacchi.

Mr. Rose, welcome to you, and we look forward to hearing from you.

Mr. ROSE. Thank you, Mr. Chairman, Ranking Member Brown. I appreciate the opportunity to testify before you today. What you are doing here, quite frankly, is of national significance for our Country. You are going to hear my views about what I think are the solutions to the capacity issues, and you are going to hear some other views that, quite frankly, are in direct conflict.

The regulatory model has served our Country well. Tremendous value has been passed to the consumer by deregulating parts of the pricing model and allowing railroads to improve efficiency. We now find ourselves in a supply-demand equilibrium that is causing some capacity shortages. This is exactly the intent of the Staggers Act. It is actually very nice to see public policy working out very, very well.

At BNSF, we have experienced unbelievable growth. In 1995, when we merged our two railroads, we hauled 7 million loads. In the year 2005, we have hauled 10 million loads. That is 3 million loads that otherwise would have had to have gone on the highway system. Over the last three years we have added the volume of an equivalent of a new Class I railroad each year. That is an average of about 650,000 units, which is really unprecedented demand for any growth of any railroad.

Well, what is driving this growth? The combined growth of Transpacific trade specifically fueled by China, highway congestion, growth in agricultural trade, increased coal demand due to higher natural gas prices have come together in ways that, quite frankly, have been foreshadowed five years ago and never could have been fully comprehended. We have seen almost a complete reversal in the U.S. supply chain over this period as we have moved from a production economy to a consumption economy. In addition, much of what we used to manufacture in the United States is now returning via containers as imports through Transpacific trade.

The good news that I share today is that this model can respond to this ever-required amount of new capacity. In the next few minutes I would like to outline some public policies that can assist the private sector in adding the right capacity at the right time.

Obviously, handling annual increases in volume can be only done by reinvesting adequately to both maintain the quality of the infrastructure that we have, as well as to expand infrastructure to handle more freight at the right time. This requires that railroads reach a level of return on invested capital that is greater than our costed capital, and then continue to improve our returns throughout the business cycle. Put another way, a railroad that does not earn its costed capital loses money by reinvesting in itself.

The biggest obstacle to achieving sustained investment in rail infrastructure has been the fundamental undervaluing of freight rail

transportation in the supply chain. The prices the industry charged for transportation services fell more than 50 percent between the years 1980 and 2003. Only since the second half of 2003 have the railroads began to receive more value for the services provided. This should be viewed very positively for sustained economic viability of the industry. As you will see in my written testimony, there is a direct relationship at BNSF between the rate of return on invested capital and the amount of capital that is required for reinvestment in the expansion of our network.

Shippers want more capacity and so do we. Increased capacity will provide the network with more reliability, as well as reduce time for recovery for outages, which reduces operating costs and improved service. Most importantly, increased capacity will allow us to meet our customers' demand. BNSF can handle the projected growth if the network can be expanded in the right ways at the right time,

Further regulatory stability allows us to plan for future improved returns and for this strong demand. In 2005 and 2006, about 20 percent of our capital program, or more than $400 million a year, is targeted for network expansion. The key is not just adding capacity, but the right capacity. BNSF, like all private businesses, will only add capacity where it is needed and where we can earn adequate returns from it. I believe our investments in the coal transportation network are an example of a prudent approach to capital investment.

I would like to now turn to my final point, which is steps policymakers such as members of this Committee can take to induce private freight railroads to invest in the right capacity enhancements and to do it faster. There are really three options. The first one is to do nothing and rely on the current market structure. Certainly, as railroads improve their returns, they will invest more capital to expand their networks.

Public policymakers should continue to vigorously defend any attempts to change the regulatory scheme in a way that will not allow the railroads the means, the stability, and the predictability to earn sufficient returns. Passage of legislation such as H.R. 2047 would fundamentally alter that regulatory model and have the effect of significantly reducing private capital investment. But even with no change, capital expansion may be below what our economy needs.

A second option is for direct Government investment into the freight railroad system. This can be done through outright grants or through loan guarantees that will induce investments that will not be made by private investors alone. BNSF supports public-private partnerships, but believes that direct Government investments must be carefully scrutinized so that it does not compete with private investment.

Direct Government investments which may seem attractive at first blush could have a significant unintended consequence for overall rail capacity: rather than increase it, it would reduce it. Why, you ask? When making investment decisions, private companies like BNSF will have to consider whether its privately financed investments will compete against Government subsidized carriers. The result will be that companies like BNSF will not invest pre-

cious privately raised expansion capital in competition with non-market-driven Government investments, and there will be overall disinvestment and not increased investment by the rail industry.

I respectfully submit that the role for public policy is a new third option to supplement the current model with a stimulus such as the investment tax credit recently proposed in the Senate. This kind of tax credit is not enough to make a bad investment occur, but enough to induce companies like BNSF to make investments sooner, rather than they otherwise would. Such an outcome would benefit rail shippers and the public at whole. This would give real impetus to increasing expansion capital of the rail industry from around $2 billion to perhaps $3 billion or maybe even $4 billion a year. That could have a true impact on the rail industry's fluidity and performance.

In conclusion, I am very, very bullish on the future of freight railroads, but I want to encourage public policy initiatives that induce the right investments and recognize the importance of regulatory stability and creating the right incentives for continued investment in the rail capacity. Public policy will play a large role determining whether we will gain the right amount of capacity and at the right time. As you have heard and you are going to hear from customers testifying here today, the number one concern is sufficient capacity. As I said, the Staggers Act has served this Country extremely well. America's freight railroads are the standard for efficiency and excellence, and, quite frankly, the envy of all the countries around the continent. We need to preserve our ability to serve our customers and the economy.

Thank you for this opportunity to testify.

Mr. LATOURETTE. I thank you, Mr. Rose.

Mr. Hamberger, welcome to you, and we look forward to hearing from you.

Mr. HAMBERGER. Thank you, Mr. Chairman. On behalf of the members of the Association of American Railroads, I want to thank you and Congresswoman Brown for the opportunity to appear here today. I can't tell you how happy it makes my heart to see a standing room only crowd and the number of members who are here today for a hearing on freight rail. I can remember a few years ago a similar hearing, to put it mildly, was just not quite as robustly attended. So I think it underscores the importance of freight rail capacity and freight rail in today's economy.

In the past few years, numerous major studies have concluded that our Nation's transportation network is being stretched to capacity and requires additional investment if we are to sustain the growth of the economy. "Every aspect of the supply chain is stretched," noted a West Coast port terminal operator. "It is not a question of whether a congestion crisis is going to happen, it is a question of when." Another quote: "Our highways, waterways, railroad and aviation networks are simply not keeping up with ordinary demands," says Michael Eskew, CEO of UPS.

To be sure, record levels of freight are still being delivered. But as these statements make clear, all freight mode in the United States are facing capacity challenges today. For U.S. freight railroads, year-over-year quarterly carload traffic has increased in nine out of the past ten years, and intermodal traffic has increased in

each of the past 16 quarters. As a result, U.S. railroads today are hauling more freight than ever before.

These traffic increases have resulted in capacity constraints and service issues at certain junctures and corridors within the network. In fact, excess capacity has disappeared from many critical segments of the national rail system. And as we have heard, demand will continue to increase by perhaps as much as 70 percent through the year 2020.

To help meet this challenge, railroads must be able to both maintain their existing extensive infrastructure and build a substantial new capacity that will be required to transport the significant new traffic our economy will generate. Where will that money come from? The Congressional Budget Office recently noted, "As demand increases, the railroads' ability to generate profits from which to finance new investments will be critical. Profits are key to increasing capacity because they provide both the incentive and the means to make these new investments." The Committee must understand that two-thirds of all investments in the freight railroads come from internally generated dollars, and a strong balance sheet is necessary to justify going into the capital markets to borrow the additional third of investment.

Last year was the twenty-fifth anniversary of the Staggers Act. Since then, rail safety has improved by 66 percent. Productivity has increased by 168 percent. And as those productivity increases were passed along to our customers, average rail rates have dropped 60 percent on an inflation-adjusted basis. And now, in 2005, railroads themselves are finally beginning to show tangible signs that financial sustainability might be within reach. Without question, 2005 was a very good year for railroads. Revenue and net income were up substantially. But I would point out that the return on equity for the Class I railroads is still beneath the median for the Fortune 500 companies in 2005. Improved rail earnings should be viewed as a welcome development, because it means railroads are better able to afford the massive investments in new capacity that need to be made.

Railroads are among the Nation's most capital-intensive industries, as you know, and even when returns were not where they were in 2005, from 1995 to 2004 railroads invested an average of 17.8 percent of all of their revenues back into cap ex. This compares to 3.5 percent of manufacturers across the board. And in 2006 a step level increase to $8.2 billion is planned to be spent on track, locomotive cars, signaling systems, yards, intermodal facilities, new technology to increase and maintain our capacity, and we will be spending millions more to hire and train thousands of new employees.

To maintain and increase that level of investment so that our Nation's freight transportation can be met, I respectfully suggest that Congress should consider three policies with respect to freight railroads. One, do no harm; do not re-regulate. The primary objective of those seeking re-regulation is to reduce rail rates. Lower rail rates will mean lower earnings, and as the CBO report emphasized, lower earnings mean less investment in rail infrastructure, exactly the opposite of what the Nation and our customers need.

Two, continue to encourage public-private partnerships for freight rail infrastructure projects. Public participation in freight rail infrastructure projects is justified because of the extensive public benefits that would accrue to the general public by increasing the use of freight rail. These include reduced highway congestion, greater fuel efficiency, less pollution, and improved safety.

I would like to thank this Committee, and especially Congressman Weller and Congressman Lipinski, for their support of what Secretary Mineta has called the model public-private partnership in the Country, the CREATE project in Chicago.

Three, support investment tax credits to bridge the funding gap between what should be invested in rail infrastructure and what railroads are likely to be able to invest on their own. Under the Rail Infrastructure Tax Incentive Program, soon to be introduced in the Senate, the projects to expand freight rail capacity—I emphasize only projects and investments that will expand freight rail capacity—would be eligible for a 25 percent tax credit. The Nation's economic health requires additional transportation capacity, and we look forward to working with the Committee and Congress as you develop policies to meet that need.

Thank you, Mr. Chairman.

Mr. LATOURETTE. I thank you very much for your testimony, Mr. Hamberger. I like to think that the size of the crowd is a direct reflection on the quality and the breadth and depth of the knowledge of the witnesses testifying today, as well as the wonderful bipartisan leadership of the Subcommittee.

General Timmons, thank you for coming, and we look forward to hearing from you.

Mr. TIMMONS. Thank you, Mr. Chairman and members of the Committee. I appreciate the opportunity to be here this morning to talk about the short line railroad industry. As I think you all know there are some 500 short line railroads operating nearly 50,000 miles of track across the Country. We serve shippers that aren't on the Class I main line system, preserving rail line that otherwise would be abandoned, saving rail jobs that otherwise be lost, and providing customers with competitive service that is almost always less costly than comparable truck transportation.

Just to put our role in the context of the national transportation system, 23 of the 24 members of this Subcommittee have a short line in their district. Now, I might add that we are taking up a collection from those 23 to purchase a short line in that last remaining district, which is Congressman Porter's of Nevada.

In the short time I have this morning, let me touch briefly on three topics that relate to the issue of capacity. First, the short line industry strongly supports the Class I tax credit initiative. Ed Hamberger has briefly laid out the facts and figures, and we think they are compelling. As I will discuss in a moment, short line infrastructure needs are different from the Class Is; yet, the capacity improvements they are addressing are important to us as well. Nearly 90 percent of our traffic originates or terminates on a Class I railroad. Short lines handle an origination or termination one out of every four railcars moving on the national rail system. When the Class I system experiences capacity problems, our customers can't get cars, can't move their product, and ultimately can't market

their product. This is a particularly critical condition in rural America, where truck transportation is more expensive than short line rail and where local roads certainly cannot accommodate substantial increases in heavy truck traffic.

Our strong support for the Class I initiative also results from our own experience with a recently enacted short line rehabilitation tax credit. 2005 was the first year of the tax credit, and already it is demonstrating its worth. Our railroad in Congressman LaTourette's district, the Wheeling and Lake Erie, is using the tax credit to replace light jointed rail with heavier welded rail on a line where traffic has increased some 35 percent in the last five years. The steel, coal, and utility customers on the line are making major capital improvements partly due to the competitiveness and improvements in rail service.

The Kansas & Oklahoma Railroad in Congressman Moran's district is using the tax credit for an $8 million rehab project on a line that has 100-year-old rail. Speeds will increase from 10 to 25 miles per hour and the line will be able to handle the new heavier 286,000 pound cars which are the industry standard. It is likely this line would have been abandoned without the credit.

The Florida Northern and Florida Central Railroads in Congressman Mica's district are using the credit to support a $14 million track upgrade which will increase speeds from 25 to 40 miles per hour and allow the short line to handle the heavier, longer trains that are so important to shippers. The railroad believes the upgrade will result in a significant increase in the amount of coal that can be shipped over the line.

We are collecting dozens of such stories from around the Country, and they all share a common theme. The tax credit is allowing light density lines to take on or accelerate projects that would otherwise fall by the wayside. These projects are allowing us to handle more traffic, pick up and deliver heavier, longer trains from the Class I system, and help our customers reduce their transportation costs.

This obviously is a good news story for many reasons, but one that is worth highlighting here is the reaction of our shippers. One such is from the owner of Delta Trading Company, which ships hazardous materials on the San Joaquin Valley Railroad in Bakersfield, California, and which operates over a line that received a $2.7 million upgrade made possible by the recently passed tax credit.

His comments: "The track rehabilitation made possible by the tax credit is directly responsible for my company's decision to invest nearly $3 million in our facility and almost triple our number of employees. We now have a short line railroad partner that can provide the volume and level of service that allows us to significantly grow our business. The tax credit was a very smart decision by the Federal Government, and I suspect it will more than pay for itself as our experience is repeated on short lines across the Country."

Mr. Chairman, you and members of this Subcommittee were strong supporters of this tax credit, and the capacity enhancement is already abundantly clear. However, as a final thought, as successful as we believe it has been and will continue to be, there is

one hitch we did not contemplate, and that is the impact of the Alternative Minimum Tax on the credit itself. In many cases the AMT is taking up to half the credit, and in some cases is eliminating it altogether. I would hope that this Subcommittee would consider this and support some type of AMT relief for the period of the credit.

I appreciate the opportunity to be here today and will be happy to answer any and all of your questions that you may have at the appropriate moment. Mr. Chairman, thank you very much.

Mr. LATOURETTE. Thank you very much, General Timmons.

Last, Mr. Millar. Thank you for being here, and we look forward to hearing from you.

Mr. MILLAR. Thank you, Mr. Chairman and Ranking Member Brown and all the members of the Committee. I am very pleased to return before the Committee. And let me congratulate you on holding this hearing about our rail capacity, both passenger and freight capacity.

We need only look at today's headlines to see that Americans' travel patterns are changing due to the price and availability of gasoline. Public transit in America has had an unprecedented growth, some 25 percent increase in usage over the last 10 years; and that was well before gas prices reached the $3.00 a gallon level.

Now, America has long enjoyed the most extensive and efficient transportation system in the world, but other countries are catching up. The critical capacity issues affecting railroads are a part of an overall capacity crisis in the whole transportation system that affects airports, roadways, port facilities, public transportation infrastructure, and the list goes on. Such congestion is putting severe stress on America's transportation logistics network, which has historically given America its economic edge as globalization increases and the competition of people and goods around the world increases as well, and maintaining our edge is critically important to maintaining our lead in the future.

Railroads, both passenger and freight, must play a greater role in our transportation network. Earlier this year the Census Bureau tells us that we are more than 300 million Americans for the first time. They expect that within 30 years an additional 100 million people will be in our Country. They aren't making any more land, so this means we are going to face an unprecedented challenge, and how do we serve those 100 million additional people, maintain the service to the people we have, and growth the economy so that all have the proper opportunities to do what they want in their lives? Most of this population growth will occur in our metropolitan areas, making urban transportation corridors more important than ever.

As we examine the options for expanding our transportation infrastructure, the need for greater reliance on rail becomes clear. Rail is much more efficient in terms of land use, energy, and adding rail capacity is imperative. I strongly agree with the statements we heard just a few minutes ago of Administrator Boardman, that we need to make more investment in rail infrastructure. There simply isn't another good choice.

In urban and suburban areas, roads are hopelessly congested, but most of those roads have already been expanded to their maximum practical capacity. Adding additional highway capacity in urban areas is enormously expensive and for just a fraction of that cost we could expand the availability of railroads for both freight and passenger purposes.

Now, not surprisingly, many Americans faced with the choices of higher gas are turning more and more to commuter rail. Last year, 423 million trips were made on the Nation's commuter rail network. This is up some 2.8 percent from the year before. Every one of the almost 20 commuter railroads in America experienced increased ridership last year.

And thanks to the work of this Committee and others in the Congress with the SAFETEA-LU legislation last year, there are opportunities to expand commuter rail. This year we will see new systems opening in Nashville and Albuquerque. We are in the advanced planning stages in Minneapolis, Salt Lake, Portland, Charlotte, Raleigh, and Denver, just to name a few cities that we expect to see projects come online in the very near future. Use of public transit, and particularly commuter rail, which tends to service long distance trips, is the quickest way that most Americans can beat the high cost of gasoline.

Now, my colleagues on the panel here today have spoken eloquently of the capacity crunch, and we certainly agree that it is there. And while all of us are working hard together to do things about better scheduling, on-time performance becomes a real challenge, and all passenger and freight interests involved here are doing what they can to improve on-time performance, but, as I said, we are going to need additional capacity. There are some really good success stories, though. The Baby Bullet South of the San Francisco Bay, for example, for the same amount of labor input, have succeeded in growing their ridership by over 20 percent by making better use of the capacity that they already have.

Now, there are many ideas, and, again, my colleagues have spoken about some of these ideas, and generally APTA is favorable towards many of these ideas. Now, about 90 percent of all the commuter rail trips take place on rail that is owned by APTA members; however, it is apparent that many of the new commuter rail systems will need to use rail freight rights of way. We are prepared to pay our share of that. We agree that public-private partnerships are a good way to go.

We think, though, that there need to be a series of principles that guide some of those partnerships. Four that APTA firmly believes in is that, one, more capacity is needed in strategic rail corridors; two, these rail corridors must be available for both passenger and freight purposes; three, that a cooperative framework must be put in place for negotiating fair access terms to both the public interests and the private interests involved; and, finally, that we must come to grips with the liability issue and that reasonable liability limits be established. We certainly agree with earlier testimony that describe that many projects will have public benefit, and certainly the public needs to be prepared to contribute financially to that.

Finally, let me say, Mr. Chairman, that I believe America is also ready for high speed passenger rail transportation. All other industrialized countries in the world have or are developing high speed rail networks, and many developing countries as well. I returned from my first visit to China last week and, as the phrase goes, had my mind blown away by the investments that they are making in all forms of their infrastructure. Their high speed passenger rail system under construction envisions tying all their provinces and all 30 of their largest cities together in a national grid. They are proposing shared use corridors with freight operations, but then publicly funded dedicated tracks for high speed rail in those corridors. The Chinese have plans to invest $16 billion to $20 billion per year on improvements in their rail network. We certainly need to look there and elsewhere as examples.

Finally finally, the Subcommittee's proposal for a dedicated fund for high speed rail projects through tax-exempt and tax credit bonds, such as was proposed in Ride-21, would create the favorable policy environment for which high speed systems could evolved and thus providing increasing opportunities for Americans to travel.

In conclusion, thank you, Mr. Chairman, for including us in this important hearing. We stand ready to work with you and to answer any questions that we might. Thank you.

Mr. LATOURETTE. Thank you very much, Mr. Millar.

And thank all of you for your excellent testimony.

Mr. Boardman, I want to start with you. In your statement you note, I think correctly, that the Class I railroads have made a number of investments and expanded capacity to a number of rail lines and yards. I want to focus my question on the yards. On the second panel today, Mr. Martland will testify, and he makes the observation that the railroads have put the vast majority of their improvement dollars in certain high return sectors of traffic and have, in effect, written off the general merchandise traffic, which we know is a major source of highway congestion.

Of the yard improvements that you mentioned in your statements, are you aware of any that have been oriented towards general velocity or dwell time improvement, as opposed to improvements that are specifically targeted at a specific sector like intermodal traffic?

Mr. BOARDMAN. Well, I think, as a general response, all of them would improve the dwell time and improve the velocity of the railroad. But I do not know the specifics of that, and I would be happy to investigate that and get back to you.

Mr. LATOURETTE. Okay. If you would, I would appreciate it. And I think you correctly point out that in order to devote specific—it is not a surprise to me that the railroads make a business decision that those lines where they can make money are those lines that they are going to make the biggest improvements in, but it does, I think, then speak to our discussion of—I think Mr. Bacchus, in his opening remarks, and others talk about—General Timmons—tax credits and things of that nature, and it becomes incumbent upon us to figure out a way how to make additional dollars available, and we've tried to do that with the RIF loan and the TIFFIA program.

But let me ask you this—and I would like others on the panel to comment about it. We have talked about RIF, we have talked about tax credits, we have talked about Section 45(g). What do you think about the option of having the shippers and the carriers negotiate contract rates that include a requirement that a certain portion of the rate be dedicated to improving the infrastructure that benefits them, not only the shipper, but also the rail carrier?

Mr. BOARDMAN. Is this the UPS trust fund concept?

Mr. LATOURETTE. No, it is not. We are going to hear from UPS on a trust fund. My question, I think, is, in addition to that testimony that we will hear late, what if we suggested to the Class I railroads and others that, when they are negotiating a rate with a shipper, that a portion of that rate be set aside, dedicated to infrastructure improvements, as opposed to just the cost of carrying the goods.

Mr. BOARDMAN. I think—I don't have a studied position, obviously, on that, it is something that those kind of innovative ideas are hopefully something that the secretary's new commission is looking at all sorts of ideas on how they might be able to finance in the future would perhaps give us a better idea of what that looks like, and we have got two of those members here on the panel with us today. So while we could look at that, and will, for you on a more specific answer, generally I think that would really have to be looked into and see what it would do to the competition.

Mr. LATOURETTE. Okay.

Mr. Rose, what do you think about that, as a CEO of a major railroad?

Mr. ROSE. Mr. Chairman, I think, practically speaking, that that is what the market does, a portion of the profitability of a certain movement does go to infrastructure. I think if you got very specific and target it and said that a certain rate has to put so much infrastructure back in a line, it would be very difficult. We operate—we own 26,000 miles of track and operate 33,000 miles of track, and these are long-lived investments. When you put a new tie in, it is for 30 years. So I think it is very hard for a piece of that rate to go in and say, well, we are going to dedicate it to upgrading these ties on this line segment.

But I think generally that is what the overall economic theory will do, and where higher returns are in the industry, that is where reinvestment is going back into the industry. If you think about our network, we probably generate 40 percent—we probably generate 70 percent of our net income over about 40 percent of our lines. So to say it the other way, you have got about 60 percent of our lines are underperforming. You want—the economic theory will want to drive back those reinvestments into those lines that are long-term sustainable, and the Staggers Act—I don't want to sound like a broken record. If you go back to the 1970s, when it was enacted, railroads were in chaos and the Government was spending billions of dollars bailing out Penn Central, Old Milwaukee Road. And the last thing I think that the industry economy wants to do is to get back to that time. So I will always come back to let the market sort this out, and it will and it has done it exactly right so far.

Mr. LATOURETTE. Part of the purpose of today's hearing is what can Congress do, and I have heard the observations about tax policy and other things and not re-regulating, but I read someplace the other day that when they built the Transcontinental Railroad, that they were able to build a mile of track a day using hand tools. It seems to me—and this is a question I guess to both Mr. Hamberger and Mr. Rose—it seems to me that, as BNSF and all the railroads are making infrastructure across the network at a stepped up rate, that there are particular challenges when it comes to permitting with State and Federal agencies and coordination among them. And I guess my question is is there anything that the Congress can do in your mind that would better facilitate the construction of these must-needed projects to expand the infrastructure which we all agree needs to be expanded?

Mr. ROSE. I think that is a great question. When the transcontinental rail network was built, obviously, we didn't have the sensitivity to the environment, which is fine, we ought to be, because we stand on that record as well, that more rail infrastructure helps the environment very much. The problem we are finding out, even on our own right-of-way, where we are running into permitting issues that are taking a year or 18 months to resolve, so these are issues where we are not able to add capacity on our own right-of-way with our own private capital to provide needed congestion relief for our customers because of some of the environmental issues that are out there now and, quite frankly, in terms of the complexity of the number of agencies that we have to deal with. We have a very good relationship with the Corps of Engineers and we feel like we can work through that group. Yet, sometimes we will get local people, local authorities who want to get involved, State authorities, and what it does, it ends up holding back investment that we are not asking anybody else to make on our behalf in terms of preventing us from being able to expand capacity and improve service.

Mr. LATOURETTE. Maybe as a service, because my time is short and I do want to ask General Timmons one question, maybe if you and the other railroads and short lines could provide us with a list of those Federal regulations that you find to be most impeding the ability.

Mr. Hamberger?

Mr. HAMBERGER. I would just like to add one sentence of praise for Administrator Boardman and Secretary Mineta, who have assigned a full-time person to work with the CREATE management Committee to try to cut through the various environmental regulations that have to be dealt with to take advantage of the Federal dollars. And there are things that can b done on the administrative side as well as taking a look at legislation.

[The information received follows:]

Ed Hamberger's answer for the record:

Railroads have faced, and continue to face, numerous efforts by state and localities to stymie rail infrastructure improvements through the application of federal and state environmental, zoning, and other requirements. In some cases, railroads have been forced to engage in time-consuming and expensive litigation to overcome alleged regulatory obstacles. Following are examples of efforts by state and local governments to prevent infrastructure improvements.

Fueling Facility in Hauser, Idaho

BNSF's effort to construct a fueling facility in Hauser, Idaho, was challenged by the local water district, environmental groups and others. Although BNSF believed it was not required to obtain local permits, BNSF applied to Kootenai County for land use permits. The County Board of Commissioners voted to approve BNSF's plans, with conditions to which BNSF agreed.

Nevertheless, the complaining parties filed suit, alleging that the facility threatened local drinking water supplies. The plaintiffs further alleged that the proposed fueling facility amounted to an extension of a rail line requiring STB licensing authority and NEPA review. In *Flynn v. Burlington Northern Santa Fe Corp.*, 98 F.Supp.2d 1186 (E.D.Wash. 2000), the district court held that the issue was within the exclusive jurisdiction of the STB. The matter then went to the Board, which held that it lacked jurisdiction and that its decision did not require an environmental review. *Friends of the Aquifer, City of Hauser, ID,* STB Fin. Dkt. No. 339966 (served Aug. 15, 2001).

While BNSF ultimately obtained favorable resolution, four years passed between the time it filed for local permits (1997) and the time of the STB decision (2001).

Automobile Unloading Facility in Ayer, Massachusetts

Guilford Transportation's efforts to construct an automobile unloading facility was challenged by Ayer, Massachusetts, which attempted to impose permitting and other requirements. Guilford had operated an automobile unloading facility since 1974 in a section of Ayer classified as a "heavy industry district." Guilford sought to open a second automobile unloading facility across the street from the existing facility on land also within a "heavy industry district."

In 1998 Guilford filed an application with the Ayer Planning Board requesting site plan approval. Ayer hired a consultant to review the plan, which recommended changes to protect a local aquifer. Guilford incorporated almost all of the requested changes. In 1999, the Planning Board issued a certificate of approval with thirty-six conditions. However, the Ayer Board of Health determined that automobile unloading facilities are a "noisesome" trade that could be prohibited within Ayer.

Consequently, Guilford filed suit, asserting that the town's actions were preempted. The district court referred the matter to the STB. The STB issued a decision in Guilford's favor, which was subsequently upheld by the district court. While Ayer based its actions, in part, on the Clean WaterAct and the Safe Drinking Water Act, both the district court and the STB held that the Acts were being used as a "pretext" to obstruct the construction of the facility. Consequently, Ayer was preempted by the ICC Termination Act (ICCTA). *Boston and Maine Corp. v. Town of Ayer,* 191 F.Supp.2d 257 (D.Mass. 2002), *citing, Joint Petition for Declaratory Order– Boston and Maine Corp. and Town of Ayer, MA,* STB Fin. Dkt. No. 33971 (served May 1, 2001).

Four years passed between the time Guilford requested townapproval (1998) and the time the district court issued its final decision (2002).

Reopening of the Stampede Pass Rail Line

In 1996, BNSF sought approval of the STB to reacquire the Stampede Pass Line in western Washington and make various improvements. King County, Washington, and the city of Auburn sought an STB opinion as to whether ICCTA preempted environmental review by the county. The STB found that King County was preempted. Furthermore, the STB found that BNSF's proposed acquisition of the Stampede Pass Line and the planned improvements would not have a significant environmental impact if certain mitigation measures were implemented. Consequently, the STB approved BNSF's proposal.

Auburn challenged the STB's decision in the Ninth Circuit, aguing that ICCTA does not prevent the application of local environmental permitting requirements. The Ninth Circuit held that the environmental permitting requirements were preempted and upheld the STB's environmental review of Stampede Pass project. The Supreme Court denied review. *City of Auburn v. United States,* 154 F.3d 1025(9th Cir. 1998), *cert. denied,* 527 U.S. 1022 (1999).

Three years passed between the time BNSF first sought approval (1996) and the denial of the certiorari petition by the Supreme Court (1999).

Construction of Passing Track in Encinitas, California

To improve both passenger and freight service, the North San Diego County Transit Development Board (NCTD) sought to construct a 1.7 milelong passing track. The California Coast Act required that NCTD obtain a permit from the city of Encinitas. In 1996, NCTD applied for the permit. The city planning commission decided that an environmental report would be necessary before a decision could be made. In 2001, fearing the loss of funding, the NCTD decided to proceed with construction without the permit and at the same time asked the STB to declare that the permit requirement was preempted. Meanwhile, the city challenged the NCTD's decision in state court, but after removal to federaldistrict court, the suit was dismissed. The court held the city's permitting process was preempted by ICCTA and that it lacked jurisdiction. *City of Encinitas v. North San Diego County Transit Development Board et al.,* No. 01-CV-1734-J (AJB) (Jan. 14, 2002). Subsequently, the STB also held the city was preempted under ICCTA. *North San Diego County Transit Development Board– Petition for Declaratory Order,* STB Fin. Dkt. No. 314111 (served Aug. 21, 2002).

Six years passed between the time NCTD filedfor a permit (1996) and the decisions by the district court and the STB (2002).

Construction of Intermodal Facilities in Vermont and Georgia

Green Mountain Railroad proposed to build an intermodal facility in Rockingham, Vermont, to handle the unloadingof bulk salt for distribution by truck, the unloading of bulk cement for distribution by truck, and the unloading of nonbulk goods such as steel pipe. Vermont asserted that Green Mountain needed a preconstruction permit under a state environmental land use statute.

Prior permits and permit amendments had been issued for activities at the site, including the construction of a salt storage shed. In 1999, Green Mountain applied for a permit to modify the location, size, and color of the shed. That same year, Green Mountain started construction of the shed. In 2000, Vermont issued notices of violation and commenced hearings on Green Mountain's application to modify its permit for the salt shed.

Faced with enforcement action, Green Mountain filed suit in 2001, seeking a declaration that Vermont was preempted from enforcing its permit requirement. Subsequently, Vermont issued the permit, but the case continued over the permit conditions mandated by the state. In 2005, the Second Circuit concluded that Vermont was, in fact, preempted by ICCTA. *Green Mountain RR. v. Vermont,* 404 F.3d 638 (2d Cir. 2005).

Six years passed between the time Green Mountain applied for a permit to modify the location, size, and color of the salt shed (1999) and the time the Second Circuit concluded that Vermont could not require Green Mountain to obtain a permit (2005).

NS sought to construct an intermodal facility in Austell, Georgia, to handle containers and trailers. Austell took the position that rezoning was necessary and in 1996 denied NS's request to rezone the property. Believing that rezoning was unnecessary, NS applied for a land use permit, but the locality continued to insist that rezoning would be required and that even if the property were rezoned, a special land-use permit was required. NS filed suit, asserting that Austell's zoning and permit requirements were preempted. The district court concluded the locality's requirements were preempted by ICCTA. *Norfolk Southern Ry. v. City of Austell,* 1997 WL 1113647 (N.D.Ga. 1997).

Interference with Railroad Operations

The South Coast Air Quality Management District is attempting to impose operational restrictions on the freight railroads operating in the L.A. region. Specifically, the District is attempting to impose idling restrictions that would interfere with railroad operations and burdensome recordkeeping requirements of "idling events." The District also is attempting to require the railroads to conduct risk assessments of rail yards in the L.A. region and has indicated it intends to impose additional requirements based on the risk assessments. The District's actions are inconsistent with a voluntary memorandum of understanding between BNSF, UP, and California's Air Resources Board, which addresses idling restrictions and risk assessments on a statewide basis. The railroads believe the SCAQMD is preempted and are currently litigating the issue in federal district court.

Dismantling of a Bridge

UP owns a bridge over the Missouri River at Boonville, Missouri, that had not been used for twenty years. UP seeks to use four of the bridge's spans to construct a second bridge crossing the Osage River, where currently there is bottleneck stemming from a single track bridge connected to double-track right-of-way; the bridge's lift span would be used for scrap. The Missouri Department of Natural Resources is attempting to stop demolition. The matter is currently being litigated.

Expansion of Passenger Service

Lake County, Illinois, has delayed the expansion of Metra service by twice changing requirements for protection from flooding.

Mr. LATOURETTE. Okay. I appreciate that very much.

General Timmons, before I yield to Ms. Brown, I was, I think, shocked by your testimony that the Alternative Minimum Tax has reared its ugly head relative to this tax credit, and it seems to me that what the short line tax credit was designed to give us the AMT is taking away. Are there some hard numbers that you can give us relative to the impact that it is having on the industry?

Mr. TIMMONS. Mr. Chairman, the taxes were filed generally just several weeks ago, as you know, and we are just starting to get a feel for what the implications of that are, but prior to the actual filings we had a number of members come forward and say they had taken advantage of the tax credit but the actual returns, as a consequence of the AMT, were severely degrading what they thought they were going to get.

Now, I understand that the AMT is an enormously complicated problem and has broad, broad implications across the Country. However, in the context of the tax credit, the three year tax credit, we think that would be enormously valuable for this Committee and the Congress to consider some kind of relief so that the intent of the Congress and the point of the tax credit itself is carried through so that we can actually make the enhancements and improve the system that needs that attention.

Mr. LATOURETTE. Sure. I think a lot of us understand where AMT came from, but a lot of us, given the fact that there has been no index for inflation, a lot of our constituents are shocked to wake up and find that they are rich when they fill out their tax forms, and I imagine you are experiencing the same thing. When the dust settles, the request I would make of you is could you poll your members and get some information as to what the impact is so that we can evaluate that with our friends in the Ways and Means Committee?

Mr. TIMMONS. We would be more than happy to do that. And it begs the—because of the degradation, it begs the issue of should we extend the tax credit; and obviously we think for that reason and the obvious success that we are having, that clearly that is an initiative that we should strongly pursue and would ask you to consider that.

Mr. LATOURETTE. I thank you very much.

Ms. BROWN. Thank you.

Mr. Boardman, I want to point out that this hearing is not just about freight rail congestion, it is also about how freight congestion impacts the passenger and commuter railroads. The Administration has, time and time again, criticized Amtrak for poor on-time performance, when it is the freight railroad and congestion that are causing these delays. What sort of assistance is available for Amtrak and commuter railroads to deal with the freight railroads that are delaying passenger trains? And, secondly, the first proposal, the FRA proposed using RIF loans to improve railroad infrastructure. Yet, the Administration zeroed out RIF in the budget. And, lastly, when you all sent your proposal over, you did not indicate where you stood on the 25 percent tax credit. Can you perhaps go on the record here today as to whether or not the Bush Administration supports the 25 percent tax credit that I keep hearing people

talk about? You know, when I hear that America is hooked on oil, policies have something to do with this hook on oil.

Mr. BOARDMAN. Let me address, Congresswoman, each one of your questions. First of all, the question of whether Amtrak on-time performance and commuter rail in terms of freight congestion is a difficult question. Certainly, on a line that is a lightly used freight line, we don't have any difficulties, generally, with commuter services operating on that line. But when there is today the growth that there has been in the economy, the intermodal traffic, the unit train traffic that is on an Amtrak line, it becomes much more difficult for the freight railroads to make the kinds of improvements that they need to to allow Amtrak to get through on an on-time basis.

We assist as we can in terms of looking at how the dispatching services go on with the freight railroads and how we might be able to make sure that they are giving the priority and checking to make sure that they are giving priority to passenger services. So we assist in that way.

And your second question was—let us see, your third question—second question was on the RIF program, which we had a hearing, one of my frequent flier hearings here that we had fairly recently here. The Administration believes that under the RIF program that the kinds of funding that would be available are available in the private sector and the private sector would be the way to finance the kinds of improvements that the RIF program would do. We will, however, carry out the law, which is what you passed, to make sure that for the time that the RIF program is available, we will move it as quickly as we can.

And on the third point, which was the—excuse me, help me.

Ms. BROWN. Twenty-five percent tax credit that they keep talking about.

Mr. BOARDMAN. Right.

Ms. BROWN. That I am supportive of but I want to know where is the Administration on this issue today, on record.

Mr. BOARDMAN. I don't think the Administration at this time has taken a position on it. Certainly, the sensitivities of a tax credit really belong in the Treasury Department, as opposed to the Transportation Department. We know that it is an important issue for the railroad industry, but the position is not taken by the Administration at this time.

Ms. BROWN. I guess I am confused. What do you mean? The Congress makes that decision, recommendations from the Administration. And my question is where is the Administration on this 25 percent tax credit today.

Mr. BOARDMAN. I understand. But the FRA is not the appropriate agency to make that recommendation; it is a larger issue in terms of tax policy, which really belongs with Treasury.

Ms. BROWN. Okay. So the Secretary of Transportation would not make a recommendation to the Congress on this issue?

Mr. BOARDMAN. Not without the Treasury folks involved in the process and having a recommendation from Treasury.

Ms. BROWN. And the Secretary is a former railroad person. I would think that he would at least have some knowledge of the needs of the industry.

Mr. BOARDMAN. I know that I do not speak for Secretary Snow.

Ms. BROWN. Okay. I guess I wanted to ask someone else.

Mr. Secretary, there seemed to be a high degree of urgency in your testimony. Am I reading that correctly?

Mr. BUSALACCHI. Yes, Representative, you are. You are reading the testimony correctly because we believe that it is urgent that we move forward. You know, we know the capacity clock is ticking; demand is up; supply is static. Time is of the essence. New signal systems have to be hand built, all the improvements have to be built while the system is in operation. New train sets would take three years to bring online. We must act now if we are to address these pressing national needs.

Ms. BROWN. Mr. Hamberger, my time is running out, but I do want to ask you about the tax credit. Will it go for infrastructure expansion to provide benefits to the public or the rail customer, or will it go to tax credit to use for infrastructure improvements which yield the highest return? I guess that is kind of a business decision, but is this business overall helping the crunch that we are experiencing?

Mr. HAMBERGER. Yes, it would support only expansion capital. And you make a very important point, that it is only to expand our capacity to move more freight that would qualify for this investment tax credit. And it would also be applied if a customer wanted to expand capacity at a receiving dock or wanted to—if a trucking company wanted to build an intermodal yard, that would also qualify for this expansion of rail capacity. So I think it would have, because of the public benefits that increased freight has, as pointed out by the AASHTO report, it certainly would have public benefits as well.

Ms. BROWN. Have you gotten any reading as to whether or not the Bush Administration supports the 25 percent tax credit?

Mr. HAMBERGER. We have met with various people within the Administration. I think it is under consideration, but they have not told us—made any final decision. In fairness, the bill has not yet been introduced, so I guess the action, force and event, where they have to actually issue a statement of Administration policy, hasn't occurred. But at some point we will continue to make our case to them and hope that we will be successful.

Ms. BROWN. Mr. Chairman, we will have another round, won't we? Thank you, sir.

Mr. LATOURETTE. I thank you very much.

Mr. Oberstar.

Mr. OBERSTAR. Mr. Chairman, it is a very good idea to hold these hearings. I appreciate the work that you and Ms. Brown have undertaken to bring to the fore in this public forum the needs of rail transportation, the importance of railroading to our national economy; the significance of railroads in our ever-increasing congestion in moving goods, as well as people. And it has afforded the Association of Railroads, Mr. Rose and others an opportunity to spread upon the public record, as quaintly say in the legislative process, the investments made with the new-found revenues that railroads are enjoying.

As we go through this—and for that I certainly commend the railroads. But as we go through this exercise, I can't help but think

back on 1980 and the intensity of debate—Mr. Hamberger, you were on the staff at the time, I believe—of debate not in this Committee, because we didn't have jurisdiction over railroads, though we should have, at that time—we probably would have done a better job of deregulation—and I rubbed my worry beads about whether this was a good thing to do.

Our committee had already done trucking deregulation, intercity bus deregulation, aviation deregulation, and what tilted the scale for me was that we were beginning to see the benefits of taking the Government out of deciding market entry and rates in aviation. And I thought that that might apply as well to railroads. So I voted for it, against many objections from constituents, from user groups, from railroad brotherhoods who were divided on the subject.

We had 61, roughly, Class I railroads in 1980. No one envisioned that we would have four today, five; some of you will say seven. But that is where we went, consolidation. Aviation went in the other direction for a very long time. Aviation, at the time, 1980, we already had 10 new entrants into air competition; in five years we had 22 new entrants. But then aviation took the same direction that railroading took. Consolidation, acquisitions and mergers reduced the number of new entrants to today we have only one of that original 22. I usually ask people—offer frequent flier miles if they can tell me which one that was. Almost everybody says Southwest. It was America West. And they too have merged.

Aviation is going in the other direction: it is losing money, while railroads now, for the first time in a very long period of their history, are making money. The Surface Transportation Board has rarely found that railroads are making adequate return on revenue, revenue adequacy, but in the 1970s, when your return on equity was in the one to two percent range, it is now—Norfolk Southern just recently reported 11.6 percent. On balance, they are running in the 8 to 9 percent range. And we are seeing those capital investments that BNSF particularly has worked hard, on course with a very major $2 billion or $3 billion plus investments plan in the late 1980s, early 1990s, and then had to shelve it because Wall Street said your return on equity isn't sufficient.

Well, we have not stood by with our finger in our ear in this Committee. We supported the railroad retirement recapitulation that was supposed to generate equal benefits for the Railroad Retirement Fund for the health insurance and for capital investments. I want you to briefly comment on what you have done with those revenues.

We also supported 4.3 cent repeal of the fuel tax that in AAR's own economic policy paper fuel tax, energy policy, deficit reduction said repeal of the deficit reduction fuel tax would restore to freight railroads—and, uncharacteristically, in your paper you mention barges—$200 million a year for equipment and infrastructure investments. But the FRA has said that railroads have generated 85 percent of their capital investments—or directed 85 percent of the capital investments to maintenance. So what has happened to the money generated from the Railroad Retirement Fund recapitulation and the 4.3 cent repeal?

Mr. ROSE. Congressman, in my testimony there is a chart that I was hoping we could get up here, but it shows return on vested

capital and then it shows level capital investments, and it follows economic theory perfectly. As our returns came down, capital was withdrawn from our railroad. And then as our return started going back up, capital was infused back into the railroad.

Mr. OBERSTAR. Are you attributing that directly to the Railroad Retirement Fund and the 4.3?

Mr. ROSE. Okay, let me give you a perspective on that. We will generate close to $3 billion in operating income at our company. Four point three was worth about $60 million. Railroad retirement was worth about $70 million.

Mr. OBERSTAR. A year.

Mr. ROSE. A year. So $120 million to $130 million of the $3 billion of operating income. So, yes, that relief for diesel fuel tax went right to our bottom line, which helped our operating income, helped our return on invested capital, helped us to where, last year, we had record capital spending. Last week, at my board meeting, my board agreed to increase our capital this year by another $100 million. So I think the model did exactly what you were hoping for, and it has worked exactly as intended.

I would just—I have got to make this one illustration that I think you understand more than most because of your understanding of the airline business. The difference between the airline business and the railroad business is that the airlines do not own the airports, and you have basically publicly supported airports that are off on one track; whereas, the railroads, we own our own airports. And what was happening in the—

Mr. OBERSTAR. Do you own your own locomotives?

Mr. ROSE. We own our own locomotives.

Mr. OBERSTAR. Do you lease any like the airlines do?

Mr. ROSE. Or a lease structure. Both.

Mr. OBERSTAR. A lease structure. I gave a talk some years ago in which I said why spend $150 million to buy a 747 when you can buy a whole fleet for $50 million? When Mr. Chechi and Mr. Wilson pooled their $25 million apiece, bought Northwest Airlines for $50 million and then leveraged everything else in the company and turned Northwest from a corporation that had $3 billion in equity and $1 billion in debt to a company with $3 billion in debt and $1 billion in equity. That is what leasing did for them.

Mr. HAMBERGER. Could I piggy-back on Mr. Rose's answer on behalf of—

Mr. OBERSTAR. That is a good term for a railroader to use.

Mr. HAMBERGER. Yes, sir. I knew you would pick up on that.

It is difficult to identify specifically where the cash flow comes from. Obviously, it comes from increased rates, it comes from improved operating ratio, it comes from not paying as much taxes. But the fact is, between 1980 and 2004, the industry put in $360 billion in capital expenditures. Now, not all of that is expansion capital; there is maintenance capital. We wear out, you know, several miles of railroad every day, each one of these companies. But the capital expenditure has gone up—and I believe it is in my testimony—dramatically over the last several years, from the $5.4 billion to $6.4 billion, this year to $8.2 billion, now, new news, $8.3 billion, now that Matt is in for another $100 million.

So that as the revenue is there, as the returns are there, the industry makes the commitment to reinvest it and to provide not just the maintenance capital, but also the expansion capital.

Mr. OBERSTAR. Well, I know that we are trying to stick with a five minute time limit here, Mr. Chairman, but—and many questions I would like to ask do not admit 30-second responses.

But since money is fungible, it is very difficult to track where the 4.3 repeal actually went, how much it was distributed in which categories, and the Railroad Retirement Fund recapitulation, and that raises questions for the tax credit proposal and how that can be structured so that we can track exactly where it goes and what it is used for.

I will conclude, Mr. Chairman, by simply observing that I feel very privileged that the Association has chosen to dedicate an entire portion of its testimony to an attack upon my rail fairness legislation. I know you have had a mobilizing effort here, you have made a great outreach to Committee staff and member staff, and you have made quite an assault upon it. But it is not re-regulation. It is not re-regulation. That is a very catchy term to use to discredit a piece of legislation. But just as I have resisted re-regulation outright in aviation, we are not about to decide market entry and rate determinations for railroads with this legislation.

But the fairness of filing with the Surface Transportation Board and the cost of the paperwork to do this, and the right of access to lines are matters that deserve better treatment than they are getting now in the railroad industry. And to understand that, all of you need to listen to your shippers, because if you are not listening to them, they are telling us their story, and their stories range from the cement industry and the grain people who are buying their own cars or trying to lease them from the rail sector, and then the railroads say we won't move your cars because you own them and that is a liability for us.

And there are numerous instances of those evidences of unfairness in the service, and the reduction from 252,000 miles of rail line in 1980 to 141,000 or so today may have been good practice business at the time, but go and ask any one of the small towns that lost their LCL service, any one of the grain centers who have been told we won't move grain from your elevator unless you can fill 1500 ton hopper cars, and ask them whether that was a good thing. Those are the inequities in the marketplace that we as members of Congress hear about, that I hear from my colleagues and that I hear directly from my constituents.

So while I am an admirer of the rail sector, an advocate for what you contribute to the national economy, I want to see you carry more cargo because it is more environmentally friendly. I want to see more passenger rail moved on commuter lines that share those lines with the rails, and to that you have to have double lining. To take cars off the road and pollution out of the air. Every car we take off the road takes five tons of CO2 out of the atmosphere a year.

So, on the other hand, there are inequities that, if you don't address them, we think that the legislative process must address them. So we will have a continuing dialog on that subject. Thank you.

Thank you, Mr. Chairman.

Mr. LATOURETTE. I thank the distinguished Ranking Member. And, as he knows, the second panel is made up of a number of the shippers that I think will echo some of his observations.

I think—we are waiting for Mr. Bachus to come back, and I did promise Ms. Brown we would do a second round, so we will have a second round. We may not all take the full five minutes, but I have—

Mr. HAMBERGER. Mr. Chairman, before Mr. Oberstar leaves—

Mr. OBERSTAR. I am not going forever.

Mr. HAMBERGER. Okay. I was just going to say that I certainly understand and appreciate his view, and really understand and appreciate the time you have given us to continue to discuss these issues that we have over the past several years, and we will continue to take you up on that offer. Thank you.

Mr. OBERSTAR. Thank you. I will be back.

Mr. LATOURETTE. I appreciate that. Just a couple of things.

Mr. Boardman, on the plasma screen—we have now gone to plasma screens here—is a map of the United States, and I think this map may have shown up in an edition of Trains magazine, and it basically highlights the lines that are illuminated in color, it is my understanding that those are the only lines in the United States that have at least double track, and, in some instances, more than that. I would think when you deal with—I don't see any in big States like—well, very little in Florida or Texas.

Doesn't this map I think pretty much indicate the difficulty that faces us as a rail system when we are talking about the capacity problems either from the railroads' standpoint or from the shippers' standpoint and really cry out for some kind of increased investment? The railroads have indicated and testified to the amount of money that they plow back into infrastructure improvements.

But doesn't this map really—a little bit like in Florida, I guess, where the gentlelady is from, I think it is a little bit like having an interstate highway that only goes one direction at a time. And I think, to me, at least, would you agree with me that this map sort of cries out for some sort of investment in rail capacity in this Country?

Mr. BOARDMAN. Mr. Chairman, I would just make the comment that all through the 1970s and the 1980s and the early part of 1990s the industry was literally taking up double track, and the reason is, again, very financially understandable: the returns were not there and it was all about taking expense dollars out. So the model worked exactly what it should have, what the deregulation model said it should have.

And I guess I would tell you the good news is that there is an awful lot of right-of-way that is still owned by the railroads that double track can go back into, and on our railroad, if you look—and that green line, that heavy green line is our transcontinental main line between Chicago and Los Angeles. At the end of this year we will be down to 50 miles of single track railroad on that 1800 mile haul. And we have been spending—we have spent about $800 million to complete that double track, and we are continuing to do that. I was just out on the railroad a couple weeks ago, and as we have that double track, it really does change the railroad.

But I want to go back to what drove the decline was the decline in the railroad profitability. And what will drive, under current regulatory access, what will drive the increase in capital will be that same financial model.

Mr. LATOURETTE. And not to beat a dead horse, but I would go back to the question about permitting that I asked you before. Take a line where you ripped out the double track. If you want to put in the same track that you used to have in the 1980s on the same right-of-way that you own, now you have permitting requirements that you didn't have.

Mr. BOARDMAN. Correct.

Mr. LATOURETTE. To restore these lines.

Mr. Boardman, is there an observation you would like to make about this map?

Mr. BOARDMAN. I certainly think that, Mr. Chairman, when you look at that, it certainly builds a graphic example of what we need to do to add capacity. I think there is another interesting thing you can look at here. There are several of them, I think. Mr. Lipinski is no longer here, but certainly when you look back at the history of how railroads really came together, you see where everything did come together at the Great Lakes in Chicago and why there is such an important need on that gateway to make sure that we make new investments in that particular area.

The other thing that I think is interesting that we found on other studies that we have done in the past is the lack of north-south movements. You see it here—you identified it in terms of double track, but you would see it even looking at all railroads. After the Civil War, it was somewhat difficult from a communication and improving the trade between the north and the south. A lot of the growth that would have been there under other circumstances wasn't there, and now we have 70 percent of the U.S. population lives east of the Mississippi River, and you see a lot of that could be improved by additional improvements along that alignment.

Mr. LATOURETTE. Sure. I think Ms. Brown or somebody else mentioned the RIF program, and Mr. Boardman knows that we had a hearing on that a little earlier, so I don't have any more questions for you on the RIF program. I think the Subcommittee made its feelings pretty well known.

But, Mr. Busalacchi, I did want to ask you. In your testimony I didn't see any reference to the utilization of the RIF program. It is my understanding that not only State departments of transportation, but other entities can either independently apply for the $35 billion that we have set aside—we hope the Administration will let us set aside in the SAFETEA-LU program, and I am wondering if you and your organization has considered the utilization of these highly favorable 25 year financing provisions as you move forward with your plans.

Mr. BUSALACCHI. Yes, we have, Mr. Chairman. Certainly, how we get to the finish line on this is what we are looking at. We are looking at somehow getting an investment back into the system so we can take care of these capacity problems. Obviously, what we are seeing or what I said here today is that we have got issues with on-time performance. It is going to be very difficult to get people that want to use intercity passenger rail if we can't make these

trains on time. And we need to have that Federal investment; we need to have investment of some kind for the freight railroad so that we can decrease the problems that we are having with capacity.

So certainly any vehicle that we can get our hands on that would help us get to the finish line is certainly something that we are going to consider. But keep this in mind, Mr. Chairman. I am a DOT Secretary. I deal with transportation problems, not just rail problems, every day. And what our State is experiencing is what all the States are experiencing nationwide. The needs are astronomical. We don't have the revenue and we are running into these congestions in our major metropolitan centers. And that is where we come in and what is where intercity passenger rail comes in. . You know, we need to have this Federal partner so that we can decrease this congestion, get people—some people, not all of them—out of their cars, using rail.

Mr. LATOURETTE. I appreciate that. I often think that—not to highlight one railroad, but we should ask Norfolk Southern where they got the seats for that tree that takes the containers off the trucks and puts them onto the railcars.

Mr. Rose, I just want to ask you one question about the RIF program. I have heard your testimony and I have read your testimony, and the Subcommittee did have a hearing on the RIF loan program earlier this year, and, specifically, many of us expressed our disappointment with the Administration, at least we thought putting additional impediments into the application process. We have addressed that with Mr. Boardman and hopefully we will have some relief from the Administration soon.

But it has been brought to my attention that recently BNSF circulated to a number of offices at least on the Senate side, at least, a document that strenuously opposes the application that has been made by the Dakota, Minnesota, and Eastern Railroad for a RIF loan. And I assume you have looked at that question, and my questions would be two. Does that document accurately state the position of your railroad, and, two, could you share with us the logic behind, as I read the document, asking the Executive Branch to ignore a provision basically that as in SAFETEA-LU, and that is removing this obstacle of lender of last resort?

I understand your argument why—I believe it is your feeling that the granting of loans like this would create an unlevel playing field, but relative to the specific document, maybe if you could give us your comment.

Mr. ROSE. Mr. Chairman, unfortunately, I am not sure exactly which document you are talking about, but I can speak specifically, and I want you to clearly understand my position on RIF loan. First off, we have supported RIF loans. We think that it is a great way and we think that the short line industry is a poster child of how we can continue to build out the short line industry applying market base financing to help them with the lower financing cost. What I am saying, though, and I think you pretty much answered your question to me, we are very concerned that—and so would any economist.

And I think if you ask any economist to look at this issue, where private market base capital all of a sudden now has to compete

with Government money, I think it has compelling issues, and it will have unintended consequences that this Country will not like. You are asking us to compete on an unfair battleground. And we believe fully that—and I will speak on the DM&E piece briefly. We supported the DM&E through an amicus brief for their railroad to be built on the environmental permitting issue. That was when they were privately financing it. We welcome all competition that has the same playing field in which we operate.

When Government money wants to come in on a very specific target, it is going to send unintended consequences, as we have to approve, like our board did, billions and billions of dollars of capital investment.

Mr. LATOURETTE. I thank you very much.

Ms. Brown.

Ms. BROWN. Yes, sir.

Mr. Hamberger, the auto train comes into my district; it has a 17 percent delay rate. I get a lot of complaints. What is the freight rail industry doing to address the growing concern voiced by both freight shippers and Amtrak about service performance?

And then my question for everyone is how do you feel about a trust fund like we have for highways and aviation that have been very, very successful? And I think you and I have had some discussion on that.

Mr. HAMBERGER. Yes, ma'am.

Ms. BROWN. So will you answer that question? Then I would like the comments from the rest of the panel on the trust fund.

Mr. HAMBERGER. Could I answer the one on the trust fund too?

Ms. BROWN. Yes, sir.

Mr. HAMBERGER. Thank you.

Ms. BROWN. You are part of the team.

Mr. HAMBERGER. With respect to Amtrak and customer service, of course, one of the main impediments to on-time performance is capacity, and that is why, led by Class Is and the Class IIs and Class IIIs, $8.3 billion is being spent in 2006, and that includes signalization, it includes a new track, new cars, new locomotives. So that is the first thing.

The second thing, there was a major meeting, it happened earlier this week, with Amtrak and representatives of the Class Is, where a reaffirmation was made that, indeed, the Class I railroads are abiding by the statutory mandate to give Amtrak the preferred service in dispatching and running over the Class I railroad lines. So we are trying to address that. We are trying to improve operating procedures to improve service across the board.

With respect to the trust fund, I appreciate your giving me the opportunity to address that, because those people who support a trust fund are very well meaning, they want to figure out a way to help us help ourselves help us expand capacity. In fact, Congressman Lipinski, Bill Lipinski and I had this same discussion many times when he was on this Committee. We believe, as an industry, that while it is well meaning, it is not the answer. Number one, of course, is where does the money come from. If it comes from a fuel tax, as some have suggested should have been done, that is money that we, as we just discussed with Mr. Oberstar, have put back into capital already. So taking money from us to give back to

us didn't seem to really be any additional revenue there, it is money that we are already investing.

Alternatively, we could increase the rates of our customers. I don't think the second panel is going to have a lot of people saying that they think they are paying rates too low. I don't think many of them are going to come in and say they want higher rates. And, in fact, what would happen if there were higher rates, we would probably have to absorb that increase or else there would be diversion from rail to truck or to barge. So, again, we would be impeding the ability of the industry to earn internal capital to invest.

But assuming that the money somehow occurs, would it get spent? Mr. Oberstar mentioned that I referred to AWO in my statement, American Waterway Operators, has a trust fund. They were paying 4.3 cent deficit reduction fuel tax, and they testified before this Committee, and anybody who would listen, they didn't want it go to the trust fund because it never got spent. And this Committee, above all else, knows the fight that you have to go through to restore the trust to the trust fund. So AWO has a trust fund, had the tax, said no, we don't want it to go into the trust fund.

Third, of course, if it does get spent, if OMB says, all right, go ahead and spend it, who is going to make that decision? Isn't it better to have the individual railroads talking with their customers, taking a look at what traffic patterns are, what are the projections for more coal coming out of the Powder River Basin, what are the projections for more intermodal traffic coming into Charleston, South Carolina? That is how we determine where the investments need to be made; more grain going to the Pacific Northwest; working with our customers, having the ability to put that money where it belongs, and not having it decided on a political basis either, with all due respect to Mr. Boardman, at the Department of Transportation FRA or, with all due respect to members of Congress, earmarked in appropriations legislation.

And I mention that because, fourth, if it were made on a political basis, I am afraid that most of that investment would be targeted toward commuter rail operations. Now, that is a very important aspect, that there is enough capacity, as Bill Millar pointed out, there needs to be enough capacity for both freight and passenger. But I don't think that a tax on freight rail would be the way to fund passenger rail.

And, finally, this is not an overall argument against it, but I do find it mildly ironic that it is UPS that is pushing this idea of a trust fund, when it was their CEO who rated all of the modes recently, and he didn't give any of us a very good grade. But I will point out that freight rail got the highest grade. The lowest grades went to highways, inland waterways, and aviation, all of which have a trust fund. This is a different model. We are privately owned, we make the private sector investments. As I have testified before, we get the dubious distinction and pleasure of paying taxes on our real estate. So I think as well meaning and as well intentioned as a trust fund is, it is not the answer for this industry at this time.

Ms. BROWN. I would like to hear the response from the other participants. Mr. Hamberger, you are very elegant, but I want you to

understand that we have got a problem and I need you to get ahead of it.

Mr. HAMBERGER. And that is why we are hoping that the idea of public-private partnerships will continue to catch on, why the idea of investment tax credit will gain support, and why we hope that you will continue to refrain from allowing us to continue to try to earn our costed capital. So by doing those three things, I believe, working together, we can stay ahead of the curve.

Ms. BROWN. Mr. Rose?

Mr. ROSE. I would just agree with what Ed said and just give you one illustration. Again, we operate 33,000 miles of track, 230,000 cars, 6,000 locomotives. If I had my laptop here today, I could draw up and show you where every bottleneck from yesterday's traffic that occurred on our railroad, every delay that we had.

When I think about trust fund, the question I have is who is going to be the master planner of where that money is going to go? I know we have five year plans out in terms of what the energy sector says. They want to grow. This year we are going to do 350 million tons. They want to grow to about 410 million tons next year. We know by milepost, track segment, switch, interlocker, signal, mask, we know exactly where that capacity needs to be put in. And for somebody else to have the insight into our railroad, which we live with 24 hours a day, 7 days a week, it is just impossible. And I think what would happen, with all respect, that money that desperately needs to go into these railroads would be moved into nonmarket-based investments and it would cripple this industry.

Ms. BROWN. Mr. Rose, do you not believe in dedicated sources of revenue, knowing that we are going to invest X amount into the railroad industry every year for safety or what will benefit the overall system?

Mr. ROSE. Well, I guess when I think about it, that is what making a profit does, it allows—if you just allow the free market model to work—if you go back to Staggers, there were two parts of Staggers, and one of them was to assure the financial health of the industry. And that is why, when these cases come before the STB, that is one of their fundamental responsibilities they have. And as long as they will do that—and they always haven't done that, but as long as they will continue to do that, then the railroads will have financial help, they will make those investments in infrastructure and more value will be put into the economy so more people can utilize the railroad network.

Ms. BROWN. Mr. Secretary?

Mr. BUSALACCHI. Thank you, Representative Brown. A few months ago we had this conversation with Secretary Mineta, and the Secretary agreed with our assessment on the 80/20 funding transportation, rail transportation like we fund highways and airports. We think, the Coalition thinks that this is really the way to do it. It is transportation. I know I am kind of in conflict with my friends over here as to how they feel it should be done, but certainly we think that once we put this model together, wherever it arrives at, if we have a long-term solution, this is where we need to head. Right now we have this yearly bloodletting over Amtrak, and we go through this wrangling of whether we are going to fund them, whether we are not, and everything else, and if we have this

six-year plan, or whatever it ends up being, like we do on highways, I think we can accomplish a lot and we can get to the capacity problem that we have.

Obviously, where we want to get to is we want to get to the intercity passenger rail. As I said earlier, and I will say it again, the highways are getting congested. I am a DOT Secretary. Seventy-five, 80 percent of my budget is spent on highways, and I don't think we need to do that anymore. Once a highway gets full, it can't get any fuller, it just gets fuller longer; and that is what is happening. That is what is happening in the Country and that is why we need to come up with a program, a plan, because the people want it. The numbers show that the passengers, people are riding the trains; they want to ride the trains. We need to provide this for them.

Mr. HAMBERGER. Can I make a distinction so as not to leave a misimpression? My response to you, Congresswoman Brown, was with respect to a trust fund for freight rail and freight rail investment with a tax on freight rail operations. I am not intimately familiar with Secretary Busalacchi's idea for high-speed passenger rail. To the extent that there is an appropriate Federal role to fund high-speed passenger rail, that wasn't what I was addressing in my response to you, which was a trust fund which would, as Mr. Rose pointed out, supplant the investment decisions of the individual railroads. I was looking just at the freight side, not at the high-speed passenger side.

Ms. BROWN. And let me be clear. I did not say anything about tax. We are talking about revenue enhancement and dedicated sources. And, of course, that is another committee that decides where the funds would come from.

Mr. HAMBERGER. Yes, ma'am.

Mr. ROSE. I want to say I was not speaking on behalf of commuter or passenger rail as well. I am only focused on our little freight railroad.

Ms. BROWN. Mr. Millar, we are coming to you.

Mr. MILLAR. Yes, I will speak on behalf of passenger and commuter rail, and generally we have been supportive of the notion of a trust fund. I think particularly in the way the discussion has gone today, it is very clear all of us see there are private benefits and there are public benefits, and certainly a trust fund from some type of dedicated reliable source to fund the public benefits, I don't think there should be much disagreement on at all.

I think the magnitude of the problem is likely to be, though, that it is going to take a trust fund and it is going to take tax credits, and it is going to take all kinds of other ideas to make sure we get the kind of investment we can have in the railroads both for the purpose of carrying freight and serving passengers. Both are essential to the Country. A trust fund is something, you know, we would want to know the details, as they say, but generally we are favorably disposed to it for the public benefits of passenger transportation.

Ms. BROWN. Mr. Boardman, do you have any comments that you want to make?

Mr. BOARDMAN. Do I want to make? No.

[Laughter.]

Ms. BROWN. Speaking for the Administration.

Mr. BOARDMAN. I think just the comments we have had thus far—and I was kind of waiting for Rich to jump on there to see what the short lines had to say, but this is a very complex issue, and I think Ed is right in terms of it is a very different model here than with the other modes. And, yet,—and they went back, both Ed and Matt went back and talked a little bit more specifically about the fact that we in fact do use some trust fund dollars right now to make investments in railroads in certain areas, and largely it is as a result of where the commuters operate and largely within the northeast corridor. And part of the difficulty and complexity of looking at the northeast corridor is you have capital plans that come out of the commuter railroads which may or not be attached to a larger transit authority in the northeast that has to have approval about how they spend those dollars from their MPO locally, and those dollars then generally come out of the trust fund, although in the transit side of the world that even, in itself, is a little bit different than what the highway side is, because the transit piece isn't fully funded through the trust fund, it also has general fund revenues that come into its particular funding mechanisms.

And then you have Amtrak in the northeast corridor, which is funded through direct appropriation from Congress on its capital projects, and it mixes with, in many cases, the projects that are on the corridor, for example, the East Side Access Project and the Access to the Region's Core Project, which are a New York and New Jersey project that are going to add additional commuter trains to the line. And there is also the freight operating on the corridor that has a capital program, which is a private investment in their capital program. So it truly is a different model, as most of the modes do have different models. The passenger facility charges for airports is operated differently than what the trust funds are.

I think that one of the things that Secretary Mineta wants to have happen in the commission that he is putting forward on how we finance for the future is to have some discussion and dialog, and two of the members up here of this panel are on that commission, but have that discussion and dialog about the different mechanisms and the complexities of those to get financed.

Mr. TIMMONS. Congresswoman, let me comment about the free short line and regional railroad concerns on this thing. Ed has mentioned at least one or two of them previously. The source of the funds, of course, is of great interest to us, and I won't dwell on that. Probably more significantly is the distribution or adjudication of those funds. State by State—for example, in Pennsylvania you have got 59 small railroads; in Texas you have got probably 41; in Illinois you have got 39 or 40. As you go State by State, the density and concentration of these small railroads and the commodities that they carry is extremely divergent. So how would you or how you would formulize some solution to get money to the right place at the right point in time to really enhance the system would be a real challenge. So there are some clear difficulties associated with that.

And, finally, the dilemma of what happens to other funding sources that we currently have. In other words, is there an impact on the RIF process? Is there an impact on the tax credits? Clearly,

if the Class I tax credit, the 25 percent, went through—which, under the current rules, we are eligible for that also—what are the consequences if we are going to get involved in some kind of a trust fund proposition? The study and review of all this, I think, is very, very important as we consider it for the future.

Mr. LATOURETTE. Okay, I thank you very much.

Now, a new member of the full Committee, and counsel tells me that we may not have met as a full Committee to ratify his addition to our Subcommittee, but we are happy to have him on the case. Just for the bookkeepers, I ask unanimous consent that Mr. Barrow be a member of the Subcommittee for today's purposes if he is not.

And we welcome you very much, Mr. Barrow from Georgia.

Mr. BARROW. Thank you, Mr. Chairman. And thank you, Mr. Chairman and Ranking Member Brown, for scheduling this hearing.

Gentlemen, I can't add much to what has been said so far, but I do want to kind of give a preview of coming attractions on a subject that Mr. Hamberger has put on the table and I think is sort of implicit in what we are talking about, and that is the subject of rail safety. I agree with the premise that investing in basic infrastructure is going to have safety payoffs, but there are some things we could do that are less reliant on infrastructure and more reliant on systems and ways of doing things.

For example, I represent the City of Augusta, Richmond County, Georgia, which, as you know, was right near by Graniteville, where we had a most unfortunate incident in the dead of night early last year, and the lion's share of the first responders to that tragedy came from Augusta, Richmond County as a result of their participation in a mutual aid agreement which is a common feature of local Government. Little communities enter into compacts with their big neighbors. If we have got something we can't handle, we send out the warning, you come, you respond, you come help us out. Neighbors helping neighbors is a fact of life all around the Country.

One of the concerns I have got is that we still, today, are relying on such incredibly ineffective technology. Let first responders know what the hell they are up against when they are responding. The idea of relying on placards on the side of a container car warning you about what is inside, which I guess is effective to prevent somebody from causing a puncture, you know, that they can prevent is one thing, but it doesn't do anything for the first responder who is coming in the middle of the night, charging into an area that has been contaminated with a chlorine cloud. First responders need to know at least as much as the railroads know about what they are going to encounter when they charge in the middle of the night. We had people seriously injured because they did not have as much information as the railroads had about what they were going up against that night.

Now, I know that folks in my former walk of life, as county commissioners and city councilmen, are all pushing rules and regs that would basically create what may well be criticized as a system of information overload, telling local governments everything that is going on, everything that is moving through while it is moving

through, which is not what you need to know when you need to know it.

What I want to know is what plans are being made, either by the industry, Mr. Hamberger, or by the Government, Mr. Boardman, either to do it on your own or to make sure that it gets done, that we create a system of notification of all of the parties to mutual aid agreements and all of the folks who are likely to be affected by a spill when it happens.

I note and I commend you all for the fact that the number of hazmat releases in trains is much lower than trucks. I think that is, frankly, to be expected when you consider the relatively small number of huge combination vehicles that are closely regulated, closely maintained that is the railroad freight industry, versus the infinitely large number of articulated vehicles being driven by everybody and his brother all over the Country.

I would expect fewer hazmat releases. I would expect a higher safety record from the railroad industry. At the same time, though, your vehicles are so big, and the stuff that can get loose when you have an accident that, despite our best efforts, can't be prevented, is much larger than many governments and first responders are capable of dealing with.

So what I want to do is I want you all to tell me what is the industry doing on its own or what is the regulatory community going to do to try and make sure that first responders know what they are up against, they know at least as much as the railroads know when the railroads know it. Who can answer that?

Mr. HAMBERGER. Well, let me try first, Congressman. First of all, I think you have to know that the industry and the Government are together in trying to make those kinds of improvements, absolutely and positively. And in the Government, my sister agency, which is the FMSA, which actually does the rulemaking for hazardous materials within DOT—and we enforce that rulemaking—is working with us, along with the Transportation Security Administration, especially now that Robert Jamison, who used to sit in this seat, is over at Transportation Security. We are making improvements on how we are communicating and the kinds of information that we would need on hazardous material, especially TIH, which is the toxic inhalant, one of them, at least, in the unfortunate situation at Graniteville.

Mr. BARROW. What kind of improvements are we getting and when can we expect real-time notice?

Mr. HAMBERGER. We individually and collectively are making those improvements to especially first responders, not only in terms of when the actual event may occur, but also telling the local communities the types of products that would be moving through their communities, so that they're prepared for the kinds of things that they may face.

But we haven't stopped there. We are looking at how do we, and to use a word that I guess Traffic World told me wasn't a word, how do we operationalize the FRA so that we know much sooner what hazardous material is in the train, where it is in the train, and protect the communities that we are operating through and protect the national security to make sure that that information doesn't get out into the wrong locations.

We are actively making improvements on an incremental basis, and we are hoping that we are trying out some additional programs, like CSX's NOW program and some of the additional ones that Ed and Matt may want to talk about that are coordinated and that work appropriately for the community and the Nation.

Mr. BARROW. Well, I don't want to trespass on the Committee's time. But it sounds like what I am hearing is, we are working on it. What I am looking for is an answer to the question, what can I tell my fire department chiefs and my chiefs of police when they can expect to know just what they are up against when these things happen?

Mr. HAMBERGER. There is a system in place, Mr. Barrow, working with our chemical customers, called ChemTrek, which is a 24/7, been around for many years, and it is supposed to be a real-time notification for the local responders. We go out, we work with them, we train them, the industry trains 20,000 local responders a year, so that they can go to ChemTrek, get experts on the phone from the chemical companies, the people who know what this stuff is, how it moves, how it reacts, what is the atmospherics in the area where the spill has occurred and get real time expertise and advice. I guess what you're telling me is that perhaps it wasn't quite as real time as—

Mr. BARROW. Well, Mr. Hamberger, training folks to have the equipment to deal with the kind of stuff that moves through routinely, giving them a number to call so they can figure out what to do with the spill when they find it is not the same thing as taking affirmative action to contact them and telling them, in the communities, this is what you're up against. We have this on this train, this train is derailed in Graniteville, it's got X number of cars in the consist, they've got this kind of stuff on it. Govern yourself accordingly. We are here to help any way we can.

Telling the chief of police in Graniteville who send in the call to the rest of Richmond County, that giving him an 800 number to call is not really making it, is what I am getting at. Because these guys are going to get there sooner than that. And they need to know what the railroad knows when the railroad knows it. I don't think anything is going to be adequate until we get that. And I think that's the goal we ought to strive for.

Mr. LATOURETTE. I thank the gentleman very much, and I would indicate to the gentleman that we had a previous hearing that dealt with some of those issues. But you're going to love the next hearing that we're going to have, which is going to focus specifically on tank car safety. I invite the gentleman to come to that hearing.

Mr. BARROW. That's why I refer to it as a preview of coming attractions, Mr. Chairman.

[Laughter.]

Mr. LATOURETTE. In just a second, Ms. Brown. That hearing will explore a number of important issues that affect not only communities, the safety of people that live around the rails, people who work on the rails, but address again the concerns that shippers of hazardous materials have as well as the railroads' legitimate concerns relative to their common carrier obligations to carry materials that create great liability for their systems with little rewards.

So I thank you for those questions, thank you for being here today, and I look forward to seeing you at the next hearing.

Ms. Brown?

Ms. BROWN. Mr. Chairman, I ask unanimous consent for members to submit additional questions to witnesses for the record.

Mr. LATOURETTE. Without objection.

Mr. Bachus?

Mr. BACHUS. Thank you.

Mr. Rose, you discussed increased efficiency and asset utilization as a way to increase capacity and network velocity. Could you give us some examples of what Burlington Northern has done?

Mr. ROSE. You bet, Congressman. The industry has made a lot of progress in terms of creating more electronics on the railroad, from looking at the locomotive health of the locomotive to car health to hot box detection. A number of things on physical track to provide a more reliable infrastructure.

The next step level of improvements though really comes when we integrate a GPS type of planning system onto the railroad industry. And we're still a ways from that. We believe that there's an interim stage that will go a lot to the Congressman's concern on hazardous material that can help prevent a number of the things that cause derailments and train wrecks to where we basically give the locomotive engineer a much better view of the railroad and understanding what else is on that track and whether or not that switch is properly aligned, all these various things.

The railroad, from that standpoint, really has not had a lot of investment in technology at that level. These are very, very expensive investments. We call it PTC, positive train control. It's kind of at the end of the spectrum. We think that that number could be in the five, six, seven, $8 billion range.

Mr. BACHUS. Just for Burlington Northern, or the industry?

Mr. ROSE. No, to fully implement on the entire Class I railroad industry. So these are major dollars. And again, the returns that we will work towards of implementation of this we think can give us both a much safer railroad as well as a step-level capacity. Right now the ruling distance, if you will, of a railroad is confined by its signal system. And long term we believe that we will remove the signal poles and that we will be getting train instructions into the cab of that locomotive through differential GPS, which is what the military of course uses.

Mr. BACHUS. How about intermodal facilities? You mentioned that. You have constructed several, and you have several under consideration. What do those cost?

Mr. ROSE. We are building, most of our intermodal facilities now are in the hundred million dollar range. And we are putting a lot of technology in those, from retina scan to thumbprint scan for drivers to come in and go through the gate. We have GPS monitoring of containers, lot containers. We have GPS cranes that literally take the container and take it to the spot on the location.

So the intermodal side has really modernized quite nicely.

Mr. BACHUS. I have read it has quite an economic impact on the area where you build one of those.

Mr. ROSE. We have built several, we call them logistics parks. Our last one was in Joliet, Illinois. And what we are finding is, be-

cause of the capacity issues that have been described here is that customers and then supply side, the whole transportation chain, wants to locate very close to these intermodal yards. So we've seen literally growth that's been doubling in a period of two or three years outside of our facility in Chicago. Wal-Mart just announced a 5 million square foot warehouse right on that plant.

And you say, well, what does that matter? Well, the reason it matters is that, if they didn't have their distribution center right there, these intermodal trains would come in and then they would have to dray to a different location. And UPS, one of our most important customers, has a couple of facilities co-located with us to where the train comes in and literally the hosteling tractor doesn't even go on the highway, it goes through the gate, from the railroad gate to the UPS property.

And so where we can tie the supply chain, what it does, it eliminates highway congestion, eliminates highway miles and improves environmental air quality.

Mr. BACHUS. If I could have one more question, Mr. Chairman?

Mr. LATOURETTE. Go ahead.

Mr. BACHUS. Administrator Boardman, the proposal on the DM&E, the new rail line to the Powder River Basin, that's to create a third rail line competition into Powder River. Is that the reason that the Government would be making that expenditure? Because I know you have two right now.

Mr. BOARDMAN. Mr. Bachus, in terms of any RIF loan that we deal with, it's a loan. If a railroad comes in and makes a business case for the amount of money that it wants to borrow, if it meets the conditions of the loan, then it meets the conditions of the loan and they are granted the loan.

Mr. BACHUS. Yes, I guess I am trying to figure out why there is a lot of discussion about that particular rail line. There are two rail lines in there, and I just heard Mr. Rose describe all these things that Burlington Northern could use money for. And I'm sort of wondering, when you have a rail line in there, does the Government decide to set up a third competition or would you—

Mr. BOARDMAN. I think what you have to look at is that the STB made that decision when they set up the—

Mr. BACHUS. Yes. But you understand what I am saying. I am sort of troubled why they'd say, okay, we have got two rail lines that could use, that are there, and private—

Mr. BOARDMAN. I am still happy with the question you asked Mr. Rose about using positive train control to improve capacity. I mean, it was not that long ago that there was a question about whether it really would improve capacity. And I think it is eligible, is it not, in the tax credit?

Mr. BACHUS. Of course, you have been on the railroad lots like I have, and they are spending every dime they can get. I think that is the bottom line. And I guess they have to prioritize. And I am just going to say, if we build a third line into the Powder River and part of the reason we give that preference is competition, what would prevent one of the existing railroads from buying that line?

Mr. BOARDMAN. Is that a question to me?

Mr. BACHUS. Yes.

Mr. BOARDMAN. I don't know that there is anything.

Mr. BACHUS. Yes. So I mean, you could build it in there and then the Burlington Northern could buy it, or the UP. Right? There wouldn't be anything to prevent that?

Mr. BOARDMAN. As far as I know, that is not the case. I would have to, I think STB would be the ones to—

Mr. BACHUS. I agree. I guess you would acknowledge, though, at FRA, that there are rail lines all over this Country that could use millions of dollars to upgrade the capacity. And a lot of rail lines where there is, that is the only, the shipper has to depend on that rail line and that rail line is clogged. You would almost think you would spend money on that rail line as far as creating, spending money on that rail line out to the Powder River Basin.

Do you all have discussions like this between you and the Surface Transportation Board? Do you all kick these things around?

Mr. BOARDMAN. Well, I think there is discussions on specific items at the Surface Transportation Board. I think your question is really maybe directed more toward General Timmons or somebody that is looking at whether there are appropriate expansions that some of the smaller railroads would like to do using the RIF program.

Mr. BACHUS. Sure. There have been almost no RIF loans approved though, is that right? Or I would ask Mr. Timmons. How many have been approved?

Mr. TIMMONS. To date, sir, 12. A total of $517 million and there are six additional loans that are being considered at the present time. That is over a space of about eight years.

Mr. BACHUS. The one that the DM&E, how much is that proposal?

Mr. TIMMONS. I think it is about $2.5 million, maybe $2.8 million, something.

Mr. BACHUS. Billion?

Mr. TIMMONS. Billion, yes, sir.

Mr. BACHUS. The RIF loans that have been granted so far, what is the total for those?

Mr. TIMMONS. Five hundred and seventeen million.

Mr. BACHUS. Okay.

Mr. LATOURETTE. Thank you, Mr. Bachus.

I want to thank this panel. Obviously I think we could spend the rest of the afternoon with this panel because of the quality of the answers you've given us. I want to thank you all for not only your testimony but also for responding to our lengthy questions.

Then if you were asked to supply some additional information, General, for instance, when your members are finished filing their taxes and all that other business, if you could give us some information on the AMT.

Mr. TIMMONS. We certainly will, sir.

Mr. LATOURETTE. You all go with our thanks, and thank you very much for being with us today.

It is my pleasure to welcome our third panel of witnesses today. We are fortunate to be joined by Mr. Carl D. Martland, who is a Senior Research Associate in the MIT Department of Civil and Environmental Engineering, where he's been engaged in rail and freight research since 1971. Mr. Martland has participated in freight rail research studies both at the State and Federal level

here in the United States and also studies the freight operations in more than ten foreign countries.

Next will be Mr. Burt Wallace, who is the Vice President of Transportation for the United Parcel Service. United Parcel Service is one of the largest customers of Class I railroads, as we heard in our last panel. Moving trailers and packages through the Country, UPS delivers over 14 million packages a day to over 200 countries around the world.

Mr. John White is here today on behalf of the Portland Cement Association. This trade association's members account for 98 percent of the cement making capacity in the United States and have manufacturing plants in 36 States. Mr. White, I would just mention that I was advised earlier that Congressman Dent of Pennsylvania very much wanted to be here to introduce you, but his other duties have taken him away. I am sure that he would have appreciated the opportunity to welcome you here today. But I will have to do it on his behalf.

Mr. Kendell W. Keith comes to us from the National Grain and Feed Association, where he serves as the President. He earned his B.S. and M.S. and Ph.D degrees in agriculture economics at Oklahoma State University, before joining the staff at the National Feed and Grain Association in 1980.

And finally, Mr. Glenn English, from the National Rural Electric Cooperative Association. Before beginning with the NRECA in 1994, Mr. English was a member of the U.S. House of Representatives, where he proudly represented the Sixth District of Oklahoma for 20 years. I want to thank all of you gentlemen for coming. You may have noticed from the first panel that we have this five minute rule. We kind of ignore it sometimes, but again, because of the number of folks in this panel, we have read the statements you have been kind enough to give us and if you could summarize your remarks, we look forward to hearing from you.

Mr. Martland, welcome, and you are first.

TESTIMONY OF CARL D. MARTLAND, SENIOR RESEARCH ASSOCIATE AND LECTURER, DEPARTMENT OF CIVIL AND ENVIRONMENTAL ENGINEERING, MASSACHUSETTS INSTITUTE OF TECHNOLOGY; BURT WALLACE, VICE PRESIDENT, TRANSPORTATION, UNITED PARCEL SERVICE; JOHN WHITE, VICE PRESIDENT, LOGISTICS, BUZZI UNICEM USA INC.; KENDELL KEITH, PRESIDENT, NATIONAL GRAIN AND FEED ASSOCIATION; AND GLENN ENGLISH, CEAO, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION

Mr. MARTLAND. Thank you very much for the opportunity to speak before a Committee that is truly interested in all aspects of rail transportation. I am speaking I guess on my own behalf at the invitation of the Committee, and I am speaking from the perspective of someone who has been involved in railroad research, capacity, service and systems issues for more than 35 years.

I obviously believe that the railroads play an important role for the system, a role that should be growing, if it could be growing, but that it's not clear that the railroads will be able to grow enough to play the role in relieving congestion, reducing fuel, reducing

emissions, providing space for commuter and Amtrak that the public I think really would like to see.

The capacity crunch. I think that it is real, it is serious and it can and should be overcome. I see four key symptoms of the problem. First of course is poor service. Average train speeds are well under 25 miles per hour. Yard times are frequently above 30 hours, whereas the benchmarks that I looked at in the 1970s and 1980s and early 1990s were 16 to 18 hours. Trip times are commonly 10 days or longer today. When I did studies in the early 1970s and the early 1990s, the average trip times for general merchandise freight was six to eight days. So service clearly has deteriorated and capacity clearly is the culprit.

Rising rates. For the first time since just after deregulation, average revenue per ton mile is increasing. This is a reversal of a 20 year trend, and it is not caused by the changes in service, obviously. It is caused by the fact that capacity is limited and basic economics say that's when prices will go up.

Third, longer hauls is nothing new. It has been going on for a long time. But it is again evidence that the industry will focus on the most profitable traffic, which is the long haul, especially the bulk and intermodal.

Fourth is that the public really is interested. This hearing is one bit of that evidence, and we have many examples of public investment.

The causes, I think the causes go beyond the basic financial ones that we have heard many times. One, we have a nineteenth century system in many places that is trying to serve twenty-first century needs. We have most rail managers growing up in an era when downsizing was the requirement, not growth. We don't know how to manage well for growth.

Starting about ten years ago, the increases in tonnage and traffic was no longer masked by the improvements in productivity. Bigger, heavier trains worked for a while, but now we just need more space.

Deregulation created intense competition that has reduced prices. The customers and the public are benefiting to the tune of about $25 billion per year. The railroads, despite the claims that things are better, things are a little bit better, but not much better than they were in say, even the mid-1980s or even the mid-1960s. The problem is that technology is not the solution to this, it is a systems problem—systems and institutions, financing, management, legislation.

The question, can the private sector solve the problem? The private sector could, but the experience of the last ten years sets doubt, because we are in a situation where every year or two for some reason there is a tremendous crisis in terms of gridlock and service. The public interest calls for more capacity for commuters. The public interest calls for moving trucks off the road, shorter haul intermodal, support for general merchandise. So I think the public wants more than the private sector is likely to put in on their own.

There's a strong history of public participation. I don't have an Power Points, I do have a required tie showing the Union Pacific Railroad constructed as a great public service project more than

100 years ago, with public funds and a private participation. We have had many examples of land grants and innovative financing since then.

And I guess my main recommendations, yes, we should be exploring and analyzing ways that the public can help the rail industry to increase capacity. I think any public programs that provide megabucks for infrastructure should provide something for planning and research. If the dollars are to be spent, let's spend some time and money to figure out how best to spend those dollars.

I think in general there is a greater need for policy analysis. FRA needs more money and more people to answer the questions that the Committee is asking. In my paper, I talk about the freight car utilization program of the 1970s as a good example of a program that involved the railroads, Government, customers, and I think even some public agencies in looking at in that case equipment utilization issues. But that was a systems problem, much like capacity.

In summary, I think we need a vision for the rail system. We started today with the Chairman's statement of a vision for 2050. I think we need to define what is an interstate rail system. I am not talking about a public system, but what is the rail system for 2050, what would it look like? And I think it would have 50 mile per hour freight trains. I think it would have six to eight day service for general merchandise freight, capacity for coal, capacity for commuters and a smattering of high speed rail.

And I think that this Committee could do a great service in providing some of the resources to help the planning, for the planning and eventual implementation of such a system. Thank you very much.

Mr. LATOURETTE. I thank you, Mr. Martland.

Mr. Wallace, welcome. We look forward to hearing from you.

Mr. WALLACE. Thank you, Mr. Chairman. At UPS, we believe the future of the Nation's rail system is at the very heart of our Nation's ability to compete globally. Right now, from our experience, there is much that needs to be done to ensure that future ability.

There is a collective need and there must be a collective remedy. As a Nation, we recognize the importance of first class highway and aviation infrastructure. Our rail network must be placed in that same category. Today commerce and the demand for efficient transport is global. U.S. companies remain leaders in innovation and our workers are as capable as any.

Our Nation's infrastructure, however, has failed to keep pace with the demands of this century. Railroad infrastructure is an integral and necessary part of a system that increasingly must be viewed as a single, all-encompassing network. If any part of that network fails to keep pace, the entire system suffers along with our ability to compete.

UPS remains among the largest corporate customers of Class I railroads in the United States. We and our customers, businesses large and small, homeowners and families all across America have a vital interest in the efficient operation and future direction of the North American railroad industry.

In 2005, we spent more than $750 million on freight rail transportation. And through our supply chain solution subsidiary, we

controlled another $800 million in customers' railroad transportation spend. On an average day last year, we moved 3,000 trailers filled with packages on flat cars. We have been incorporating rail transportation into our network since the 1960s. It is important to us to understand that every trailer we put on the railroad represents one less trailer moving on the highways.

UPS and our customers depend on rail service as a vital part of our worldwide intermodal transportation network, which on a daily basis delivers more than 14.8 million packages to 7.9 million customers worldwide. It is estimated UPS delivers more than 6 percent of the U.S. gross domestic product and 2 percent of the global EDP each and every day.

Allow me to give you an example of how our system interacts with that of the railroads. A national hair products manufacturer uses UPS for its nationwide shipping needs. Their Southern California distribution location supplies products to much of their West Coast retail beauty salon customers. UPS uses the rail network to feed these packages to UPS hub locations in the Pacific Northwest.

This customer has had repeated service problems and delays in this region and recently stated, taking a week into Oregon and Washington from California simply does not work. Other carriers get to these locations in two days via truck. At this rate, we might be forced to make changes.

Unfortunately, this scenario is all too common on today's rail network. When our customers confront us with this feedback, we are left with few alternatives. UPS wants the railroads to succeed and to continue our mutually rewarding transportation partnership. But the bleak current service picture forces us to be responsive to our customers' needs and find an alternative transportation mode.

Our marketplace dictates a quick and appropriate response. Along that same vein, we wish the railroads had the ability to respond to our needs. Whether as a result of the 1990 rail mergers or other reasons, there has been little new rail capacity. Given the current state of the industry, UPS remains opposed to additional Class I rail mergers.

Regrettably, the railroads have been unable to make adequate capital investments, technological enhancements and innovative solutions in responding to the new market conditions. I stress the word adequate. It is not as if the industry has not been investing, as you have heard today.

Rail performance clearly underscores, however, that it simply has not been enough. An aside, the proposed railroad infrastructure investment tax credit legislation is not sufficient. We need to devise a more comprehensive solution. Nothing illustrates the current challenges we face more than time in transit, which remains a significant issue for UPS customers. Since the passage of the Staggers Act, the efficiency and speed of our Nation's transportation system generally has increased. The lone exception, however, is the railroad velocity, and demands on an already overburdened rail network are increasing.

In recent years, UPS has invested billions of dollars on technology, much of which is directly related to embedding information on each individual package. Today we can provide our customers a wealth of information regarding the status and time and transit

of a $6 package or an ocean-bound cargo container. In contrast, the railroads lack the capacity to give their customers information about trainloads of freight.

As noted earlier, however, this is not only an issue for the Nation's railroads. UPS strongly believes this is an issue critical to an array of constituency beyond the railroads themselves: the major users, such as the Nation's farmers, retailers, the mining industry and chemical manufacturers. Looking forward, one concept that should be explored is the notion of establishing a public-private partnership to help fund a railroad infrastructure improvement projects.

I would ask the Committee to consider the following. The Nation's highway system has a highway trust fund to support and maintain a safe and efficient Federal highway system. The Nation's airports have a aviation trust fund to support, maintain and enhance airport infrastructure and provide necessary capacity. If the existence of these two transportation trust funds are deemed to be in the public interest, why not a railroad trust fund or a similar, user-funded mechanism?

We need a private-public investment plan to address the serious challenges facing the industry. Wouldn't improving railroad capacity, safety, infrastructure and technology be in the best public interest? Yet the user-funded trust fund has not gained traction, while service levels diminish and rates continue to rise.

The railroad industry should be challenged to find a mechanism that does meet its approval, because doing nothing is not a viable option. Thank you.

Mr. LATOURETTE. Thank you very much, Mr. Wallace.

Mr. White, welcome. We look forward to hearing from you.

Mr. WALLACE. Thank you, Mr. Chairman.

Mr. Chairman and members of the Subcommittee, my name is John White. I am Vice President of Logistics for Buzzi Unicem USA. We are a leading manufacturer of Portland cement in the United States.

I appear today on behalf of the Portland Cement Association, where I serve as Chairman of the Logistics Committee. I appreciate the opportunity to testify and look forward to a constructive dialogue addressing the need for additional rail capacity and reasonable steps we believe are necessary to improve—

Mr. LATOURETTE. Mr. White, could I ask you to move your microphone a little closer to your mouth? Thank you very much.

Mr. WHITE. Current rail policy and capacity constraints impede cement manufacturers from effectively and efficiently delivering an essential commodity needed to build our Nation's infrastructure. With more than 80 percent of cement manufacturing plants captive to a single railroad, the current railroad policy is unnecessarily contributing to higher construction costs.

The PCA is a trade association representing 31 cement companies operating 102 manufacturing plants located in 36 States, accounting for 98 percent of the domestic cement-making capacity. Portland cement is the powder that acts as a glue in forming concrete. Nearly every construction project requires Portland cement. In 2005, the U.S. consumed 127 million metric tons of Portland cement.

Average cement shipments range between 250 and 300 miles. However, truck transportation is not practical beyond 125 miles. As such, the cement industry is reliant on railroads to deliver our product beyond the economical range of trucks, which accounts for at least 50 percent of all shipments by volume.

Several member companies report that they are charged substantially higher rates at their captive locations versus their dual rail serve facilities. Some of the cement industry's inbound coal and raw materials are also captive, which results in higher rail rates that add to the cost of cement and ultimately the cost of construction.

Mr. Chairman, inconsistent service from the Class I railroads is a serious problem the cement industry confronts in bringing an affordable and essential product to market. The rail cars supplied by the railroad are typically old and frequently a safety concern. They are asking industry to provide private or company-owned rail cars but cannot guarantee a minimum level of service to help justify the cost of buying and operating these cars.

The cement industry has no recourse regarding rates, since cement is classified as an exempt product from rate regulation by the STB. Since the STB has done little to address service issues, we believe Congress should enact legislation expanding the STB's authority in this area. The modest provisions included in H.R. 2047 do not constitute re-regulation, a term used by our friends in the railroad industry to overstate the perceived negative impact of this legislation.

Mr. Chairman, the PCA believes that the intent of Congress and the Staggers Act was only to regulate the railroads where competition existed. Unfortunately, the implementation of the Act has often resulted in deregulation where there is no transportation competition.

One example of unintended consequences of the Staggers Act involves a captive East Coast cement company that must transport cement 300 miles by rail to its distribution terminal. The applicable rail rate is so outrageously high, the cement company concluded that importing cement all the way from China to the East Coast was less expensive than shipping it 300 miles by rail. Additional examples are provided in our written statements.

Cement consumption is expected to grow from 127 million metric tons to 200 million metric tons by 2030. To meet this demand, our industry currently is engaged in its most aggressive capacity expansion in the history of the industry. Despite our concern about captivity, market forces require we expand existing facilities.

While the industry is committed to providing reliable and adequate supplies of cement, these efforts are partially offset by existing rail constraints. As the economy grows and more cement capacity is put in place, it is likely that existing rail constraints will be exaggerated, potentially leading to the repeat of the large rate hikes we experienced in 2005.

PCA obviously supports increasing investment in the Nation's rail infrastructure. As the Class I railroads report profit increases, now is the time for them to bolster investment, to expand capacity and improve their service, especially to the captive shippers. PCA does not yet have a position on the 25 percent tax credit proposal,

but would be inclined to support it if Class I railroads are required to invest in capacity projects providing relief to the captive shipper. This would be the most prudent use of taxpayer dollars.

We also urge Congress to further examine the concept of the railroad trust fund, similar to the highway trust fund, to finance rail capacity.

Mr. Chairman, contractors utilizing cement in large scale concrete paving projects, such as those authorized under the SAFETEA-LU, need a reliable supply of cement to meet construction timetables. Just as contractors expect timely shipments of concrete from the cement company, it's the obligation of the railroad, we believe, to deliver timely shipments to us.

In conclusion, it is essential that the Portland cement industry have access to a competitive rail transportation system to ensure that our product is delivered in a timely and efficient manner to our customers who are building the Nation's critical infrastructure, fostering economic expansion. With more than 80 percent of the cement manufacturing plants, and a similar ratio to the industry's 400 distribution terminals, they are held captive with a combined declining service. This only adds to our Nation's construction costs.

Thank you for the opportunity to testify today, and I look froward to questions.

Mr. LATOURETTE. Thank you very much, Mr. White.

Mr. Keith, welcome to you, and we look forward to hearing your remarks.

Mr. KEITH. Mr. Chairman and members of the Committee, rail transportation is very important to the grain and feed industry, as about 35 percent of all commercial grain movements go by rail. The U.S. transportation system in the past has been a competitive strength for U.S. agriculture in both domestic and export markets. But it is turning into a competitive weakness, as globally we are falling behind in infrastructure investment, compared to our competitors, in particular, in water and rail.

The current rail capacity shortage has all the signs of a growing and chronic problem. We believe it is becoming a serious issue, both for the private and public sectors, as limitations on transportation capacity could well become an impediment to growth in the overall U.S. economy.

The railroads of course have acknowledged the capacity shortage and have announced higher levels of infrastructure investment. But will it bring new capacity quickly enough?

In the past, Wall Street has punished railroads for investing in infrastructure. We think, though, that this current situation is different, as all the transportation systems, water, rail and highway, are at or near capacity. But will railroad management and Wall Street analysts correctly perceive this as an opportunity for railroads to grow their business with new investments, while still maintaining profitability? We have our doubts.

The capacity crunch in rail has become most severe in the last three years, and the various carriers have responded in different ways, some more successful than others in serving this new demand. Some carriers are up by as much as 20 percent in car loads, some are as low as 5 percent gain in the last three year period.

Clearly, and overall to solve the capacity crunch, railroads need to invest in more engines, crews, build passing lanes and double track some areas. These investments are going to take some time.

We think the railroads might also want to review what they might do operationally. The Canadian National, for example, has done, has improved train velocity partly through a balanced system of incentives and penalties for both the railroad and the customers. This has resulted in an improved railroad-customer cooperation and better operational performance.

One concern that we have from an agricultural perspective is how much new investments will really benefit agricultural shippers. In the latest capacity crunch, agriculture and food shipments have not proven to be a high priority for rail carriers. Intermodal and coal have both received higher priority than agriculture in general

Also, grain in the past has been viewed as a commodity that will wait on transportation in a freight shortage situation, despite the need for grain to be delivered in a timely way to obtain optimal value.

We are also concerned about how well shippers that are less than unit train and shuttle size will be treated if the rail capacity crunch continues or becomes worse. Clearly the unit trains and shuttles are the most efficient way to move high volumes. But there are some markets out there that simply cannot justify those movements and that still need reasonable rail service. We think there is a common carrier obligation still under the law.

Some other points that we would like to make toward possibly improving rail service in addition to infrastructure investments, we would urge the railroads to reconsider some of their policies toward shipper owned cars. A number of these policies are one-sided and distort the incentives for investment in equipment by rail customers that currently supply over half the rail cars being used in our marketplace today.

Railroads also need to review their current fuel surcharge programs to ensure they are fair. Some are clearly excessive. Many accessorial charges now being imposed by carriers are simply a drain on manpower in both the railroads' and customers' business. Both of these issues, frankly, we believe, are distractions, distractions that take away from the focus needed by both carriers and their customers to improve rail service and performance.

In conclusion, our industry remains very dependent on rail service. We need a market responsive rail system. With the era of cheap fuel appearing to be forever behind us, fuel efficient carriers like railroads stand to reap long term benefits if the necessary investments are made to serve the growing demand base.

Thank you.

Mr. LATOURETTE. Thank you very much, Mr. Keith.

My neighbor to the east in Erie, Pennsylvania, is Congressman English. It is a pleasure to meet another one. Thank you for coming here today and we look forward to hearing from you.

Mr. ENGLISH. Thank you very much, Mr. Chairman. I appreciate that, and it is certainly a pleasure to be here and have an opportunity to visit with you a little bit about this issue.

Last month I visited with some of the folks over at Homeland Security, talking about the lessons we had learned from responding to Rita and Katrina and how things might be done better. One of the officials there made the point to me that one lesson that they had learned is that the critical element in the response was electricity. And until you got the power turned on, a lot of other things didn't work. And I am afraid far too often, that is something that is not recognized and I think in the future, that is going to be a priority as far as homeland security and the way that we respond to some of these challenges.

As far as that electric power is concerned, roughly half of all the power in this Country, whether it is electric cooperatives or the municipals or investor owned utilities, is generated through the use of coal. Coal is the fuel, and it is the cheapest fuel. And in fact today, we know that coal is cheaper to buy than it is to ship to the destinations where it is used to generate electric power.

Now, 25 years ago, when Mr. Oberstar and I were here, and the Staggers Act was being passed, we had a far different situation than we do today. At that time, as Mr. Oberstar pointed out, we had roughly 60 railroads around this Country who were delivering that coal to those generating plants. Today we only have four Class I railroads left, and I think three others that operate on a regional basis, as I understand it.

That is a far different world than it was 25 years ago. Twenty-five years ago, Chairman Staggers had it in mind that the Interstate Commerce Commission was going to be able to deal with the problem that he understood would come out of the Staggers Act; namely, that you were going to have a portion of the shippers in this Country who were in fact not going to have access to competition. And for that reason, he provided that authority to the Interstate Commerce Commission, and of course that has been passed on now to the Surface Transportation Board.

Twenty-five years ago, Chairman Staggers assumed there would be competition among all these railroads. And with only four Class I railroads, there virtually is no competition. What in fact we are dealing with today are monopolies. And I think that it is important for the Congress to recognize and to deal with that.

Now, we have complained for some time about the problems of shipping, those of us who are captive shippers, shipping where there is no competition and what that has done to the rates. We have in some cases rates 300 and 400 percent profits being made off of captive shippers. And that is abuse.

But today we have an additional problem, and that is raising the question as to whether or not railroads are going to be able to meet the demand of moving coal to these plants. The Vice President has just pointed out about three years ago in order for electricity to meet the needs of the Country's rising demand, to meet our growth, that we are going to have a power plant a week come online in order to meet those needs for the next 20 years.

Now, the decision for us is this question: should in fact those plants be coal-fired? Can they be coal-fired? And if they are not coal-fired, what happens to the rates that the American consumer is going to have to pay? And we have a serious question in our mind today, Mr. Chairman, whether there is in fact going to, those

needs are going to be met by America's railroads, whether they can meet those needs. Because quite frankly, they are not doing it in a timely manner today.

I would also point out, in the electric utility industry, we have an obligation to serve. And I would suggest to you with only four Class I railroads left in this Country, and given the fact that this has become such a vital ingredient, this is the only way we can move coal to those generating plants, that if they do meet the same kind of importance to the economy to this Nation that the electric utilities do, and that they should have the same requirement, namely, an obligation to serve.

If the Congress is going to move forward, if the Congress is going to provide assistance to the railroads to in fact improve the structure, and there needs to be improvement, I wholeheartedly agree with that, then I would also suggest to you, Mr. Chairman, that there is no free lunch and there shouldn't be a free lunch handed out by the Congress. And in fact, there should be this obligation to serve as a part of the understanding.

And that obligation to serve should begin with providing relief, and I am talking about in the form of transportation, to those who are captive shippers, as well as to those in the rest of this Country, the rest of this Nation's economy, before we give preference to those overseas, namely those cargo containers that are coming in from foreign countries.

Mr. Chairman, this is becoming a very important thing, and I think your hearing is very timely. I would also suggest that this is probably an item on the agenda that is going to reach a priority that we have not yet seen.

So I commend you for the hearing, and we are ready to help this Subcommittee in taking care of this problem.

Mr. LATOURETTE. I thank you very much for your excellent statement and observation.

I thank all of you for your observations today. I want to focus on this notion of a trust fund first, that Mr. White and Mr. Wallace talked about. I assume you were in the room when we had the first panel, and I not only serve on this Subcommittee, but also on the Water Resources Subcommittee. There is some discussion in this Country about whether or not we need to have a water infrastructure trust fund at this moment in time.

And then you always get to the $64 question: where does the money come from? I don't know if it is easy or not, but we have relied in the Highway Trust Fund on the Federal excise tax since the formation of the system, at 18 and some cents. When you talk about water trust fund, does it come from the people that manufacturer flushables? The bottled water people are scared to death it is going to come from them.

And so when you talk about a rail trust fund, I am wondering if, and let me throw it open to Mr. Wallace and Mr. White, and then ask you, Mr. Martland, if you have thought of this as one of the ways that we could address this problem. Have you given any thought as to how we are going to raise the money to go into the trust fund?

And in line with, Mr. Hamberger was here, he talked about the fact that, and I think that it is right—he is still here—that if you

say, okay, well, let's put an excise tax on fuel, I don't know how that is putting new money into the system. But Mr. Wallace, have you given any thought as to how we would fund a freight rail or a rail trust fund?

Mr. WALLACE. Yes, Mr. Chairman. Our thought is that shippers, like UPS, would contribute via some type of a user fee. And while we can't give you the specifics at this time, and certainly that would need to be worked out, this would be in an effort to create a public-private arrangement to ensure that we are investing in railroad infrastructure improvement projects.

Our position at UPS is that we don't have the specifics at this time, but we would certainly be willing in working with this Committee to helping to develop that process.

Mr. LATOURETTE. So Mr. Hamberger, at least in the case of UPS, is wrong, you would be willing to pay higher rates as long as some of the higher rates went to infrastructure improvements, is that right?

Mr. WALLACE. We need to improve the fluidity of the network. We need a solution. So if it came to that, then we would be willing to pay more fees towards infrastructure improvement.

Mr. LATOURETTE. Mr. White, how about you and the cement folks? How do you feel about that?

Mr. WHITE. I think you will find that the cement industry is also a heavy user of the inland waterways. Most of the cement companies belong to the American Waterways Association. I think like UPS, we don't have a specific funding methodology. Our idea on the trust fund relies more on the fact that it would target where that type of funding would be applied. It would be trackable and it would be discernable to Congress.

And it would allow us to, as an industry on the user side and as an operator from the railroad side, to target areas where we think as a group these investments need to be made. Because some of them are regional, but many of them are on a very national basis, much like the infrastructure on the locks and dams. They benefit a large variety of people that don't even know they touch, that type of improvement.

So whether it is a user fee like we have on the waterways, some type of tax or even something in the rate. I am getting higher rates anyway. If I could put some tangible benefit to that rate, it would certainly be more palatable to sell to my board of directors than telling them I am paying higher rates but I don't have a definitive plan on what that is going to get me.

Mr. LATOURETTE. Let me ask you both this before I turn to Mr. Martland for his observations as to whether this is sort of the public participation he was thinking about. There are two things that I think haven't been discussed. One is, I think I asked Mr. Rose about it but the other one I didn't. But the RIF infrastructure loan program allows currently joint venture loan applications by a railroad and just about anybody else. And so have either of your organizations considered partnering with one of the railroads for a RIF loan application that would specifically be designed to create improvements that benefit that carrier and the major shipper?

And secondly, the question I did ask Mr. Rose, is why can't, in the long term contracts that were first authorized in the Staggers

Act, be used creatively to include a contribution by the shipper to be dedicated to specific infrastructure improvements on the lines that you use? Have either of you given that any thought? Mr. Wallace?

Mr. WALLACE. Well, unfortunately in the case of both of those points, I have not been involved in discussion on either one of those. Although on your second point in regards to putting into the rate additional dollars that would go directly toward infrastructure improvement, I think that would be something that we would be willing to explore and understand exactly how that would work, particularly if we were sure it was going to bring benefit to improving the overall performance of the network.

Mr. LATOURETTE. Mr. White?

Mr. WHITE. Our industry has looked at that. We continue to fall back to the point that where we have the capacity constraints are not in areas specifically served in the first 60 to 80 miles coming out of our plants. We have 10 plants in the United States, 5 of them are served by short lines for the first 15 to 25 miles, until they reach the Class Is. So for us, we weren't really sure if that type of creative investment did anything for us. Because what we are seeing, the congestions are in the major areas, Kansas City, the southern part of the United States, over toward the East Coast. So it did not initially look like a mechanism for us that would work.

Mr. LATOURETTE. Let me ask you this, because you also raised the issue of captive shippers. My understanding is that one of the new options by the RIF program that was created permits captive shippers that are only served by one railroad to also access the RIF loan program. Have any members of your association who may have a close proximity to a second railroad explored that opportunity that you are aware of?

Mr. WHITE. We are only aware of one member company that is currently trying to do something similar. Since I don't have the specifics, I think their problem isn't a funding problem. I think their problem is a right of way problem. They have another railroad that is within some distance of them, but the only right of way available without buying private right of way and creating a new corridor is to put it next to one of the existing Class Is. I think there is some legal entanglement in that right now.

Mr. LATOURETTE. If you would be so kind, after this hearing, could you may supply this Subcommittee with the specifics of that example that you are talking about?

Mr. WHITE. I would be happy to.

Mr. LATOURETTE. And then my last question, Mr. Martland, when you talk about where we are today versus where we were before and the increase in wait times and yard times and everything else, I thought I understood you to say that this is a legitimate public interest, public sector interest to be involved in now. What do you envision, how do you envision the public getting involved? Is it the trust fund? Is it the RIF loan program? Is it the contract rates? Or is it something else that you see, a tax?

Mr. MARTLAND. I think I would agree with Administrator Boardman, who said that there are many possible ways to finance the improvements. I think that the different ways should be stud-

ied, we should have some analysis with all the different perspectives included.

The point I would make is that since deregulation in the last 25 years, there has been a tremendous, tremendous benefit to the public through the reductions in rates passed on to the customers. I keep listening carefully, and what I hear are concerns with equity, inequitable increases in rates, more than the rate level. The rate levels are much lower than they were, and the amount of money, $20 billion to $25 billion a year, according to my studies, is more than enough to fund the grandest of vision that anybody is talking about.

So I think that it is worthwhile to consider the tax credits. I think it is worthwhile to consider direct investment, whatever. But I think the private sector makes a very strong case that they are the ones who can identify the bottlenecks and work on the freight and work with the customers and that why make it more complicated than it is.

What is really lacking is a way to get the public dollars into the rail system. We have heard people talk for the commuter rail and the clarification of the urban networks, as in Chicago. And I think that that is an area where some mechanism to get general public dollars into the sections of the rail system that would not necessarily be upgraded by the freight railroads themselves. And probably the best way to do that is to have some mechanism for coordination.

Mr. LATOURETTE. I tend to agree with you on that last point. I happen to be a huge fan of the Highway Trust Fund. I think that most members of this Committee would think that members of Congress are in a better position to identify high priority highway projects in their districts than perhaps the Secretary of Transportation or the head of their department of transportation.

But the one concern that I think I do have about this freight rail or rail trust fund is that I don't think I am in a better position to figure out or would be able to say that all the money for choke points should come to Cleveland, Ohio, because I happen to be there. I think that the private sector may be better able to assess that.

But thank you very much. Ms. Brown.

Ms. BROWN. Thank you, Mr. Chairman.

I think I am going to yield my time to Mr. Oberstar, but I do have a question for Mr. Wallace. Mr. Wallace, I understand recently that UPS has taken some of their business off of the railroads. Can you talk about that? And briefly, can you all tell me what you think about the 25 percent tax incentive? Is it enough, or do you agree with it? Starting with you, Mr. Wallace.

Mr. WALLACE. Yes. We recently rolled out an initiative that we referred to as fast lane. And basically that is to improve time and transit from point to point for ground packages. And in doing so, in order for us to achieve that objective, we did remove about 300,000 packages per day from the rail network, simply because the rail network doesn't currently have the capability to move as fast as we would need them to. So therefore, we had to go to the ground transportation for that.

Ms. BROWN. How many additional trucks did that put on the road?

Mr. WALLACE. That added, on a daily basis, over 600 trucks per day.

Ms. BROWN. That's a problem.

Mr. WALLACE. In regard to the tax credit, conceptually it sounds good. However, the problem is we are not sure what type of impact it would really make. And financially, the railroads have had some very good years recently. We think that additional investment, additional capital investment is where we need to start in lieu of a tax credit.

Ms. BROWN. I thought the 25 percent tax credit would be to increase the, to expand that investment, it had to go for that.

Mr. WALLACE. Well, I have to tell you that I am not familiar enough with exactly how that would be applied to acknowledge that.

Ms. BROWN. Well, I just want you to know that I am concerned about this 600 additional trucks that was put on the road. That is something that I guess the Committee is talking about how we can resolve some of these issues.

Mr. White?

Mr. WHITE. The PCA has not taken a final position on the tax credit. It looks like a method that could work. One of the things again that we are most interested in is, are these monies going to be applied to relieve some of the congested areas and give some of the captive shippers some relief. If you can make a tie to that, I think you would find our organization could get behind that proposal.

Ms. BROWN. I am coming to you, Mr. English. Nice meeting you, sir.

Mr. ENGLISH. Thank you very much.

I think there is a little bit of a political problem here that the Congress may have to wrestle with on this. I think it is a good idea as has been pointed out, if we are going to deal with the problems, if in fact we are going to deal with the infrastructure, if in fact we are going to deal with the whole question of captive shippers, if we are going to look at making sure that we are able to make the deliveries on time and meet capacity needs for the future.

However, I think the railroads have to invest something too. And I think they have not demonstrated at this particular point that they are willing to do that. I notice here Business Week on April 3rd, the top performers, the S&P 500, number 12 was Burlington Northern Santa Fe. One year return of 58.5 percent and a three year return of 230.3 percent. We have the same thing with Norfolk Southern at number 46, one year return at 44.5 percent, and a three year return of 179.7 percent.

Well, are they investing this money in infrastructure? Are they in fact trying to relieve the captive shipper problem? And is the Surface Transportation Board doing its job when in fact it takes $4 million with one of our members, spent $4 million just to get before the Surface Transportation Board and got dismissed. We had another member that wrote in, complaining with regard to one of the railroads, to the Surface Transportation Board, and the people that

responded was the president of the railroad, not the Surface Transportation Board members.

Now, something is amiss here, and I think these kinds of issues have to be addressed if in fact the taxpayers are going to be putting money up. I think that the Congress is going to have to be able to go to the American people and say, yes, we are going to clean up these problems and take care of these problems. And it means that the railroads are going to invest as well as the American people. It has to be a Wall Street and Main Street type of effort here.

Ms. BROWN. Yes, sir.

I yield back the balance of my time.

Mr. LATOURETTE. I thank the gentlelady very much. Congressman English, I just want to insert in the record, we were obviously, in your testimony, concerned about the letter going to the STB. I think that the president of BNSF responded. I am told by Mr. Nober, who is a former associate of all of us, worked here on the Committee, that his belief is that the letter was copied to the Surface Transportation Board and did not go directly to them. But if you have a different set of facts, if you could get that to the Subcommittee, I know we would be happy to take it up with Mr. Nober.

Mr. ENGLISH. I was shocked about this, Mr. Chairman, and we will be happy to provide that for the record for you.

Mr. LATOURETTE. Okay. I thank you very much.

Mr. Bachus, did you have some questions?

Mr. BACHUS. Thank you.

Mr. Martland, reading your testimony, I notice you highlighted the delay time in rail yards as being very significant, and has actually increased since the 1980s and is now up to 20 or 30 hours.

Mr. MARTLAND. Yes, sir.

Mr. BACHUS. You might think that the merger of railroads would actually have quickened that time. But I mean, it has not. Is that sort of a surprise? You would think with less railroads, you would get more efficiency.

Mr. MARTLAND. As you try to consolidate the system, you get more and more lines going into the same junctions. And you have, the railroad lines of 1980 were capable of handling maybe 40 or 50 million gross tons per year. And the ones we have today can handle 100, 150 or more. So the you have even bigger arteries going into the same heart. I think that's the basic problem.

Mr. BACHUS. Now, just in the last year or two, the railroads have started spending a lot of money on expanding their yard capacities, is that correct?

Mr. MARTLAND. I know that they continue to invest very heavily in intermodal. I don't have specifics about recent investments.

Mr. BACHUS. Let me read for all of you, we have talked about profits, and Congressman English, you were talking about the railroads are making record profits recently. I would agree with you in the last year or two. But on page four of Mr. Martland's testimony, he actually says, the average revenue per ton mile declined every year from 1983 to 2001. In constant dollar terms, average revenue per ton mile began to rise only in 2004.

So you have actually had declining rates with deregulation every year from 1983 through 2001.

Mr. ENGLISH. The 20 percent of us who are customers of the railroads that are stranded shippers have not seen anything like that. What we are negotiating now with regard to our coal contracts, we are seeing huge escalations. That is the issue, the part of the problem here that we see is, you go back to the Staggers Act and what was intended, this kind of abuse was never intended. And we are just not seeing any kind of response or addressing of that problem, and we are seeing these huge escalations come once again.

And now we have an energy problem facing this Country. We have electric rates, you probably heard up here at Baltimore Gas and Electric, they put caps on that State, and I think maybe it is the State doing it. But they are going to have a 50 percent increase in rates.

We are going to have cases right now in which deliveries are not arriving at the generating plants. We have several of our folks that are in single digits as far as the number of days supply they have left. And they have to use natural gas or buy on the open market.

Now, natural gas will run anywhere from 7 to 9 percent, or 7 to 9 times higher in price. So all this stuff I think comes in and—

Mr. BACHUS. Well, now, I agree, obviously there is a capacity restraint, there is a velocity restraint.

Mr. ENGLISH. We need to address that.

Mr. BACHUS. I guess what I am sort of puzzled by, the shippers not saying tax incentives would be a great thing.

Mr. ENGLISH. If you read my testimony, I said that we would be willing to go along with tax incentives if in fact we are going to address the problem. We would be supportive of doing that if the railroads are going to invest their money in this thing. I think they ought to put something up.

And also, I think we get back to the same issue here, and Mr. Chairman, I would say that this industry is vital. It is vital to this Country's economic health and I think that we have to recognize that and we have to come to grips with it. I think that is what makes it worth the American people investing in it.

But along with that, the railroads have an obligation to help this Country meet its needs, its energy needs and other needs. And it is vital to us, and we have to come to grips with that.

So there needs to be an adjustment made. It has been 25 years since Staggers. I hope that this Committee will come to grips with that. I hope we can get some investment tax credit. I am hopeful that we are going to see the inequities eliminated and we see some new structure. And I hope also that we get the Surface Transportation Board to make some interpretation of the Staggers Act that allows stranded shippers, when they get to the point where they can compete, to be given that opportunity. And they are not given that today.

Mr. BACHUS. Seeing Mr. Martland's testimony, he says the rail industry is investing heavily in capacity, but individual railroads will concentrate their limited funds on what they perceive to be the most profitable market segments.

Mr. ENGLISH. And I think that is a key issue. Because we get into this question, if this is a vital industry, if we are down to four

Class I carriers in this Country, and this Country's economic health depends on that, and if the United States Government is going to assist the railroads in fixing this infrastructure because it is in the best interest of the Country, there has to be reckoning that comes to be bear here. And I think that it is not just in the areas where you can make the most money, and because of the fact we squeeze this thing down to where, the heck with those folks that we can't make the most money, there is an obligation to take care of the—

Mr. BACHUS. I understand what you are saying. But you do get into problems when you start telling industries you will invest in this as opposed to that. Any time, and I think you will agree, any time you add regulations or control, you usually diminish profits.

Mr. ENGLISH. Well, then, there shouldn't be any assistance from the United States Government. There is no free lunch. And if we are getting to the point that the United States Government is going to take taxpayer money and going to fork out taxpayer money to help the railroad, but the railroads don't have to do anything, hey, we want a little of that over in the electric utility industry. We have obligations. There is an understanding that is reached.

If this is a vital national interest, if in fact the taxpayer is going to help out, and if we are going to get this thing straightened out, then we have an obligation or the railroads have an obligation then to serve this Country and to help meet the needs of this Country. Whether it is national defense, you ought to bring some folks over from the Department of Defense and see what kinds of difficulties they are running into in getting their equipment to the shores where they can ship it overseas. I understand there are great difficulties over that.

But all this is a national—

Mr. BACHUS. I think we all agree that—

Mr. ENGLISH. Well, let's fix it.

Mr. BACHUS.—it is a problem, and we ought to fix it. But I am just saying that tax incentives, the Congressional Budget Office has studied this. Now, I just say maybe do you agree or disagree with this? Because I think this kind of debate is very helpful. Let me read their statement to you.

"As demand increases, the railroad's ability to generate profits from which to finance new investments will be critical. Profits are key to increasing capacity, because they provide both the incentives and the means to make new investments."

And I believe in competition. But if there is no competition, and there is a monopoly, then the question comes in, a question of abuse. And there is a difference between making a profit and abusing people who are held captive and they are held hostage and they are under a monopoly. And we have a monopoly situation developing here, and that is not in the best interest of this Country.

Is the main problem—

Mr. LATOURETTE. Mr. Bachus, could I ask you to make this your last question?

Mr. BACHUS. Yes. Is the problem the rates, the shipping rates, or is the problem capacity? Those are two different problems.

Mr. ENGLISH. I think we have several issues that are coming together.

Mr. BACHUS. And if you are talking about shipping rates, that would be where they are making a profit. If you are talking about capacity or velocity—

Mr. ENGLISH. Right.

Mr. BACHUS. That is not because you are a captive shipper.

Mr. ENGLISH. That is right. Where you have competition, it is my understanding that the rate return is about 6 to 8 percent. And goodness knows, that is fair. Where yo have captive shippers, those 20 percent of us that are captive shippers, with the new contracts that are being negotiated, it is my understanding you are up to a 400 percent return. Now, that is abusing folks.

You have a problem with regard to being able to make deliveries on time, and that is killing us. And that may be more important than the profits at this point.

So yes, I think we need to respond to that, and that is the reason we say hey, if we can get this thing straightened out and take care of the infrastructure of the railroads and the railroads are willing to invest some money and help us take care of the economy of this Country, let's do it. Let's help them.

Mr. BACHUS. The rates have declined every year until 2004.

Mr. ENGLISH. Where there is competition.

Mr. BACHUS. They didn't for captive shippers.

Mr. ENGLISH. And we have had long term contracts with regard to coal. And those contracts are expiring. That is where we are really seeing the big jumps.

Mr. BACHUS. And could you give us some of those figures?

Mr. ENGLISH. Be happy to do it. Appreciate your interest.

Mr. BACHUS. And you are Jan English's husband, right?

Mr. ENGLISH. That is who I am known about in this town, yes, I am known as Jan English's husband.

Mr. BACHUS. She is chairman of the First Lady's luncheon this week, so I would say you are having a very difficult week.

[Laughter.]

Mr. ENGLISH. Under tremendous stress and strain, you understand.

Mr. LATOURETTE. Thank you, Mr. Bachus. Our last questions today will be asked by Mr. Oberstar.

Mr. OBERSTAR. Thank you, Mr. Chairman.

I think this last exchange was one of the most productive all day. I enjoyed listening to the discussion. And again, I compliment you and Ms. Brown on scheduling these hearings and the preparation that has gone into their development.

Congressman English, you raised the issue that has been lurking in the background here for this whole hearing, and that is, the obligation to serve. The common carrier responsibility.

When in the nineteenth century the Federal Government created, in effect, the rail industry in America, it was for public interest service and necessity. Railroads got every other section of rail, some cases more than that, of land, in which to run their rail lines. And the mineral rights. And the wood fiber rights, to log the woodlands to make the railroad ties. They extracted ballast from gravel pits along the way to build the trackage.

And they did that out of the public interest, convenience and necessity, to serve. But what we heard from the railroad sector testi-

mony was this clash of Wall Street investments, profitability, return on equity, return on investment, and very little in the testimony, you have to take a microscope to find our obligation to serve the public.

Now, each of you witnesses has raised a different aspect of the service responsibility. In the law, the Surface Transportation Board, successor to the Interstate Commerce Commission, provides that rail carriers shall provide any person on request, carrier's rates and other service terms in writing, electronically. The transportation of agricultural products, carriers shall publish, make available, retain for public inspection the common carrier rate, schedule of service and other service terms.

There is really very little in the law that says what quality of service. That was left to the Interstate Commerce Commission.

Now, further on, in use of terminal facilities, the board may establish conditions and compensation for use of facilities. The board has done very little in the obligation to serve. And in your testimony, Mr. English, Congressman, there is "effectively no Government agency to which rail customers can turn for redress, even when severe rail service problems are being experienced."

Now, the bill that I introduced with a number of other co-sponsors, and that was rather roundly attacked in the rail testimony earlier today, is not re-regulation. It is just an attempt to restore the public service content of the responsibly the railroads have to the public. They have a responsibility to the public, and not only to the shareholders. Not only to Wall Street. Wall Street doesn't receive product from the railroads, but our power companies do. Concrete ready mix association does. The producers of agricultural products do.

And when, as the PCA, Portland Cement Association, testimony says, Class I railroads have refused to add cement rail cars to their fleets. Isn't that a service obligation? Isn't that a public responsibility on the part of the railroads? It is not only profit driving this. Profit is vital to their operation. But so is public service.

Your members report as much as 15 percent of empty rail cards delivered to manufacturing plants are being rejected. And that railroads add tariff provisions, charging for storage, that is demurrage, of private rail cars and then they refuse to carry them and move them.

I think we need to further explore, Mr. Chairman, this common carrier obligation of the railroads, which they don't like to talk about, but which is their core responsibility.

Mr. English?

Mr. ENGLISH. Congressman Oberstar, I think there is a balance to be struck here between Wall Street and Main Street. And this is a vital industry, just as the electric utility industry is a vital industry. And I think it is up to the Congress to deal with the realities of today as opposed to the way things were 25 years ago.

I have been around this town long enough that, and certainly on this issue have seen enough of it, I remember how it was in 1980. And there is no question the railroads needed help. And it was recognized, they play such a vital role in this Country that we have to do something.

Deregulation, the district that I represented at that time was very rural. We lost our airline service with airline deregulation. We lost our bus services as a result of bus deregulation. We lost our trucking service because of trucking deregulation. And I was scared to death when it came up with regard to this issue what was going to happen to us.

But certainly we all recognized and understood, we desperately need rail service and we need the railroads and we need them just as much today as we did back then. And I think there was a recognition of that throughout the entire Government—Democrats, Republicans, Congress, the Administration. And we put in process here a way of rescuing the railroads. And I think it has been very successful, over 25 years, you look at these returns and you look at Wall Street. Railroad is on the cover of FOrbes Magazine in February talking about, this is the best investment going. We hit the promised land.

If you go back to 1980 and what Chairman Staggers saw and he was trying to do, not all of it has worked as well as that. Those of us who are stranded shippers, it hasn't worked the way he intended. But I think we have reached a new plateau. And I think we have to understand that our infrastructure is vital for the railroads. And we have to understand that we need a very healthy rail system in this Country. And we have vital industries that are heavily dependent on the railroads, and they are only going to be able to do their job if in fact the railroads are healthy and profitable and being successful.

Mr. OBERSTAR. I agree with that, and you have stated the case very well. But maximization of profit to the exclusion of public service is contrary to the concept upon which the railroad sector was created in the public interest by the Federal Government.

And one of, what we are trying to address in this legislation that I have introduced to reinstate competition and rephrase competition, one of the obstacles is the bottleneck rule that I am sure each of you in the grain and cement sector has unfortunately encountered. Mr. Wallace, Mr. White, Mr. Keith, do you have some examples that you would like to share with us?

Mr. KEITH. Bottleneck issues are an issue at some locations for agricultural shippers. They are not so severe as in some other industries, though. We have switching issues that are competition issues and some other things. But the bottleneck per se is not as big an issue for ag. But I know it is for some other sectors.

Mr. OBERSTAR. What about rail car availability?

Mr. KEITH. Rail car service in particular, where there are captive shippers, has proven to be a difficult situation, in particular, last year with Katrina and so forth. And really, to the extent we can't get timely service, it tends to run up Government costs to farm programs because of our loan deficiency payments. So we do need to solve that problem.

Mr. OBERSTAR. Mr. White?

Mr. WHITE. I can speak for my company. What we have done is we have simply purchased an entire private fleet of rail cars. We don't rely on the railroad to provide any cars. We currently own about 1,250 cars. Most of the rest of our industry does that.

We have determined that that part of the capital investment in the overall delivery of our products is going to have to be made by our company. The railroads are investing in rail cars, just not in cars that haul cement. And we came to a meeting of minds with that with the railroads. What we need now is, and part of what we have asked for and the legislation provides is, if we are going to make this capital investment as a partner with them, give us some level of service that we can depend on for the movement of those cars.

You have asked me to make a substantial investment. Guarantee me that you will move them in a predictable, reliable and efficient manner. And you won't hear me complain about my investment in the cars. But don't do that and then I have a major problem.

Mr. OBERSTAR. Do you know whether the barge lines partner with their customers to have a customer acquire a barge?

Mr. WHITE. Yes, sir. Our company also owns about 60 barges. And it is a very similar relationship. We go to the barge lines and we come to an agreement on how we are going to move a product. I do, oddly enough, agree with the railroad on one side. The river is there for anybody who wants to use it. There is no barrier of entry. The highways are there, there is no barrier of entry.

It is expensive to build a piece of railroad. And I know that, as an industry, we build it. And that is why some of the creative alternatives, tax credit, the trust fund, I think are really good ideas. I just want to make sure they are coupled with some type of service and opportunities to go before the STB when there is a problem, so that the railroad and the industry can resolve them together. We don't hate the railroads. We like the railroads. We need them to be profitable and we need to have good infrastructure.

On a larger basis, as a Nation, I think the Federal Government is going to have to help the railroads get to some level of development that supports the Amtrak and the public transportation that we are all going to need if we are going to pay $3.50 a gallon for gas. We are going to need to ride on trains.

Mr. OBERSTAR. That is a good, thoughtful, balanced approach and one that I embrace. Because you equate service and investment and the need for profitability. The Surface Transportation Board, along with the railroads, have justified higher costs and higher rate of return for railroads from bulk shippers, grain and coal and chemicals. That helps them to profitability, to be able to provide other service to less, lower profit centers in their service network.

And we do have to, because of the structure we have created, the Federal Government does not own the rail beds, but in creating the railroads, they get an enormous benefit, mineral rights, land rights, timber rights, over many, many decades. They have and uniquely shoulder the obligation to serve. It is a balancing act.

Mr. Wallace?

Mr. WALLACE. In terms of bottlenecks, if you are describing that as the same as congestion, then clearly that is a significant problem that we have experienced as users of the railroad. There is a very significant number of service failures that we experience that are associated with congestion and bottleneck problems. Certainly that is what we are interested in seeing improvement in, is increas-

ing the fluidity of the network, so that we can get back to the service levels we were achieving and had achieved for 25 years. We are very dependent upon the railroads and have good working relationships. We are looking for solutions to help them solve that issue.

In terms of availability of equipment, such as flat cars, that is not a problem for us. Although rail trailers has been more challenging, getting rail trailers, which we use heavily, has been more challenging. The railroads have a different strategy as it comes to managing rail trailers. That has changed how we have to operate and put a little bit of a burden on us.

Mr. OBERSTAR. Mr. Martland, do you have any summary observations on these issues?

Mr. MARTLAND. One thought that has occurred to me is that as we go back to 1980, or 1970, we had the problem of the light density lines. There were tremendous battles in the Congress and the ICC about how to deal with that problem. And the way it was solved is, Congress said in the 3R4R Act somewhere, okay, if somebody wants that line to remain in service, put some money in up. If you don't put the money up, then no line.

And the Federal Government said, well, we will put up some money that will last for a few years, where the States can buy the lines or subsidize the lines, and then that money would come to an end.

Commuter rail, many cases now that the States just, or the MPOs contract with the railroads or with Amtrak to provide the service. They are not trying to make a profit out of the fare box. And I think we, in the discussion of public benefits, I think the public agencies, at the State, local and Federal level, have to figure out what are these public benefits worth and then pay enough to get sufficient benefits to justify the public investment.

And in that way, the railroads are still doing what they do best. They would get revenue for certain services, they would identify the bottlenecks and they would deal with the bottlenecks.

Mr. OBERSTAR. Thank you. Mr. Chairman, this has been a very, very productive session. The written testimony is very much in-depth, unlike much of what we see over the course of a hearing here, in not only this but other Subcommittees as well, and very useful documentation.

And the response has been very substantial. You have been generous with the time so that we can explore issues at length.

We need to continue this dialogue, and we need to explore further and dig deeper into how we can unlock this grid that is choking America. The trucking sector doesn't have enough capacity to move the goods that are foisted upon it. They are trying to ship trailers on the rails. The rails don't have enough capacity to haul the trailers. They want the trucking sector to take more of its responsibility. The barges can't go everywhere, because waterways are limited by their pathways.

And more goods are coming into our ports every year. The Chinese now have launched the Chinese Shipping Company, COSCO, its 9,000 container vessel, 1,000 footer, that is going to add to our congestion on the West Coast ports. They can't put in on the East Coast ports.

The railroads are now in a period of profitability. Clearly they need some help in making the capital investments that are required. The public needs help too, with the service issues that have surfaced. I thank you very much.

Mr. LATOURETTE. I thank you very much.

One of the reasons that I enjoy serving on this Committee so much is because you happen to be the Ranking Member of the full Committee, and there isn't a hearing that goes by that I don't learn something from your participation. So I thank you very much.

This was an important hearing, and I want to thank the Ranking Member of the Subcommittee for making it possible. And it does add, if it was easy I guess we would have solved the problem.

At our next hearing, we are going to be dealing tangentially with the railroads' common carrier responsibility, and on that subject we are going to be dealing with hazardous materials and the movements and the economies of scale with that as well. So I look forward to the gentleman's participation there, too.

Ms. Brown?

Ms. BROWN. I just wanted to say thank you, Mr. Chairman, and Mr. Oberstar and other members that have come and participated. And of course, to all the panelists.

In closing let me just say, recently I had a hearing in Jacksonville, where a lot of the citizens came to see me about the port, very excited that we are getting a new Asian carrier that is going to be working out of the Port of Jacksonville. It is less than a half mile from my house. That will bring about 1,600 huge tractor trailer trucks. And I said, well, what is wrong with the railroads, which is there, the facilities? They said, well, it will take them two days to do something that is 15 minutes away.

That is unacceptable. All of those players have to come to the table and sit down and talk and figure out how we can work this out. So if we know issues beforehand, how we are going to best serve the public, then this is one of the reasons why this Committee may be coming up with some additional funding. But we certainly have to work to the needs of the community and provide the—we are all excited about these jobs, it is going to provide 5,000 new jobs and X amount of income. But 1,600 tractor trailers, trucks, every day, that is unacceptable.

Mr. LATOURETTE. I thank the gentlelady very much.

I want to thank all the members for participating today. I want to thank this third panel for your testimony and adding to our body of knowledge.

Not to single anybody out, but I have been at this only for 12 years, not the number of years Mr. Oberstar has, but Mr. Martland, I found your testimony to be some of the most informative I have read in those 12 years. I thank you for your body of work. I thank you all for coming today, and you go with our thanks.

[Whereupon, at 1:45 p.m., the subcommittee was adjourned.]

Statement of

The Honorable Joseph H. Boardman

Federal Railroad Administrator

Before the
Subcommittee on Railroads
Committee on Transportation and Infrastructure
U.S. House of Representatives
April 26, 2006

Chairman LaTourette, ranking member Brown, and other members of the Subcommittee, it is my pleasure today to represent Secretary of Transportation Norman Y. Mineta to discuss the critical issue of capacity of our freight transportation system and the ability of the nation's freight railroads to contribute solutions.

Today, I will talk about the economic cost of insufficient capacity and resulting congestion, how the problem only worsens if freight and transportation demand forecasts are accurate, how railroads have up until now been meeting demand growth with strategic investments, and how more will be needed to meet capacity requirements.

But first, I want to highlight the success of railroad deregulation as a backdrop to where we are today. The Staggers Act was the most important in a series of major railroad reform and deregulatory legislation. Now, twenty-five years later, it is clear to the Department that this legislation has been an unqualified success. The major railroads are financially healthy, the industry infrastructure has been modernized, productivity is high, and shippers have enjoyed the benefits of lower average rates. Prior to Staggers, nine major railroads were in bankruptcy or receivership, rail market share was declining in the face of steadily rising rates and poor service, and the rail plant was in a sorry state.

While the challenges following deregulation were met, the railroad industry, indeed the entire transportation sector, faces new challenges not dreamt of in 1980. These are the challenges of success; demand for freight transportation, reflecting the growing economy, strains the existing infrastructure overall. Increased highway congestion, higher fuel prices, and concern about the environment all indicate that the rail industry will be asked to do more in the future. The Staggers Act was meant to make the industry viable. It has

INTRODUCTION

Transportation efficiency, long a strategic U.S. asset, is decreasing.

The capacity of our freight highway and rail network has not kept pace with the growing demand for freight transportation. These inefficiencies add additional and unnecessary cost to every sector of our economy through delays in goods movement and unreliable delivery times.

The data bear this out. The Federal Highway Administration reports that, since 1990, vehicle miles traveled (VMT) has grown over 38 percent while lane miles increased by little over three percent. Hours of delay on our nation's highways increased by over 117 percent. For rail, since 1990, the network measured in miles-of-road owned has not expanded -- indeed, it has decreased by almost 19 percent -- but revenue ton-miles increased by 60 percent. While much of the system needed paring back due to redundancy and unused and light density lines, traffic on the remaining portion is moving over heavily traveled corridors. This has resulted in a reduction in system average train speed by nearly 20 percent, accompanied by network congestion and deterioration in service reliability.

Generations have been accustomed to a resilient transportation system. But those days are over. Rob Ritchie, CEO of Canadian Pacific Railway, characterized the situation: "The North American railroads' network holiday is over -- the rail industry is **finally** [emphasis added] running enough freight trains to consume the capacity of the network."

Insufficient capacity is expensive.

Constrained transportation capacity is a cost we all pay, whether or not we drive. Every motorist has experienced the frustration of sitting in traffic backed up because of insufficient peak period highway capacity -- and the peaks have been getting longer and longer. In its 2004 Conditions and Performance Report, the Federal Highway Administration reported that cities with populations between 500,000 and 1 million saw an increase of nearly 180 percent in the average annual delay experienced by drivers, from 5.9 hours in 1987 to 16.5 hours in 2002. For the same period, drivers in cities with populations between 1 million and 3 million experienced average annual delays of 29.5 hours, up from 9.3 hours. And drivers in cities with populations over 3 million experienced 35.6 hours of delay, up from 30.6 hours. The Texas Transportation Institute's 2005 Urban Mobility Study estimates that the aggregate cost of highway congestion is $63 billion, just for wasted fuel and extra hours of travel time, and there are other significant costs more difficult to quantify. These include lost productivity of those waiting in traffic, and increased levels of harmful emissions, with their associated health disorders. All these costs are borne by society in one way or another.

Everyone bears the burden of freight-related congestion as well. Constrained capacity adds extra cost to virtually all goods and services produced in the economy. The resulting congestion adds to direct transportation cost and also forces companies to carry larger inventories and invest in increased warehouse space -- making U.S. businesses less

FREIGHT DEMAND

Until recently, freight growth and surge demand were met by improved productivity and excess capacity.

Up to now, the cushion of excess capacity, combined with significant productivity gains over the past 20 years, has allowed the rail system to handle growing demand, even the recent surges.

Like the nation's highway system, the rail industry had excess capacity for decades. For the highways, traffic grew onto a defined system that has been in place since the completion of the Interstate system in the early 1980s. The rail system, measured in miles-of-road, was largely complete in the 19th century, reaching its peak in the 1920s. Even though competition from trucking soared with the growth of the Interstate system, significantly reducing rail market share, rigid regulation kept carriers from streamlining and restructuring until passage of the Staggers Act in 1980. The Act provided railroads the flexibility they needed to compete in an ever more dynamic transportation environment, by allowing the use of differential pricing and contracts in setting rates. To the surprise of many, rate flexibility led to sustained declines in real (inflation adjusted) rail rates. Freight rates declined by an average of 1.3 percent per year between 1990 and 2003. And, from its passage in 1980 through the 1990s, the Staggers Act allowed the rail industry to concentrate on paring its system to accommodate relatively stagnant traffic; new capacity was added only where there was proven growth.

Even though the physical system was shrinking, record productivity gains allowed the railroads to carry much more traffic. From 1987 to 1999, railroad productivity grew by nearly 48 percent, while traffic measured in ton-miles grew by nearly 52 percent. (In comparison, the US manufacturing sector as a whole increased productivity by only 16.1 percent during the same period.) Tons originated grew by over 25 percent with coal, chemicals, metal products, and motor vehicles and equipment leading the way. Rail intermodal shipments, measured in units shipped, grew by 73 percent. The locomotive fleet grew by only one percent, but new units are now able to haul more trailing tons; lighter and larger freight cars now carry heavier payloads. The mergers over the past decade also added efficiencies to the system, bringing large networks under more central control and reducing duplicate facilities. Overall, the industry has been able to improve productivity on every part of the system. Investments to enhance productivity ultimately reduce transportation costs and benefit consumers.

All freight demand forecasts predict increasingly limited capacity.

At its root, congestion is a byproduct of a vibrant economy and the demands it imposes on transportation infrastructure. In 2005 alone, the Nation's real Gross Domestic Product grew 3.5 percent, above the historical average. The Department's Bureau of Transportation Statistics' Transportation Services Index shows that freight transportation demand is at record levels. Since the economy began its recovery in 2001, the Freight Service Index has grown by over 14 percent, and the overall trend is expected to continue. Global Insight, Inc., an economic forecasting firm, projects growth in tons for

rail for this year at 2.5 percent, while trucking is expected to grow by 3.3 percent. Similarly, the Federal Highway Administration's Office of Freight Operations forecasts that overall demand for freight transportation will grow 43 percent[1] by the year 2020. The rail freight system's traffic growth is forecast at 35 percent to maintain its present share of the freight market, and substantially more if highway congestion or public policy drives more freight from roads to rail.

Congestion on our highways, at our seaports, and at major border gateways with Canada and Mexico already imposes costly delays on the movement of freight. Current global trade, particularly with Asia, is straining our seaports and shifting truck and rail patterns and routes to inland consumption areas. The freight forecasts that I've just cited carry with them the prospect of more frequent disruptions if solutions are not implemented.

Even now, events that once would have had little effect now cause major disruptions throughout the rail network, because there is no reserve capacity. Last year is a good example. West Coast storms interrupted shipments from California ports to the east, and forced eastern carriers to hold traffic moving west; the result was filled yards and a clogged rail system. In the Powder River Basin, necessary track work and severe winter weather slowed delivery of coal to utilities.

Increased demand for rail freight transportation also affects efforts to provide commuter rail services in urban areas. Commuter rail operations that operate over lightly used track may be relatively easy to implement. However, on main railroad lines, where traffic is steadily increasing, new or expanded commuter operations may require additional investment in capacity, to accommodate both passenger and freight needs.

The era of inexpensive transportation is over. Providing new capacity to meet needs will be costly; the private sector is the best judge of where that capacity is most needed.

Providing new transportation capacity is costly. In addition to rapidly rising fuel costs, construction materials -- primarily steel, concrete and wood products -- are outpacing inflation. Land for new or expanded rights-of-way, terminals and other infrastructure is expensive to acquire. Nonetheless, railroads are making these investments.

But too much, or too little, capacity is even more costly. If the system has excess capacity, then economic theory tells us that resources are not being used efficiently. On the other hand, a shortage of capacity also proves costly through congestion, service [illegible] the transportation system with the optimum allocation of resources. Attaining this balance is extremely challenging because significant rail projects are expensive and require significant lead times.

[1] Freight Analysis Framework growth rates from 2005 to 2020

MEETING DEMAND – INFRASTRUCTURE, TECHNOLOGY, AND OPERATIONS

Railroads are investing in additional capacity.
Freight railroading is among the most capital-intensive of industries. The railroad industry's capital expenditures from 1990 through 2005 totaled nearly $90 billion. The industry reports that as a general rule, 15 to 20 percent of that investment for any given year goes to capacity expansion. This includes investments to double- and triple-track strategic sections, improvements to yards, new locomotives, rolling stock, and investment in new technologies, all designed to improve operations and respond to customer demands. The remaining 85 percent goes to maintaining the system in its current condition. Additionally, during this same period, another $175 billion was expensed for maintenance-of-way and maintenance-of-equipment.

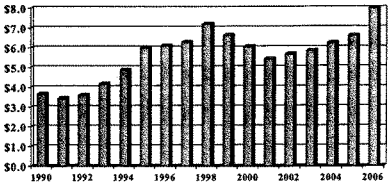
The following charts give an indication of railroad spending, how spending has kept up with growth, and how much is available for investment.

Chart 1 shows railroad capital expenditures between 1990 and today. In the early part of the decade, when the rail industry was shedding capacity, spending levels were $3.5 to $4 billion. With the mergers from 1995 through 2000, spending levels grew to the $6-7 billion range. As the economy began its growth in 2001, capital expenditures steadily increased from their low point of $5.4 billion to a projected $8 billion this year.

As Chart 2 shows, growth in capital expenditures generally outpaced growth in revenue ton-miles until 2001, when it began to fall behind the surge in traffic [illegible]

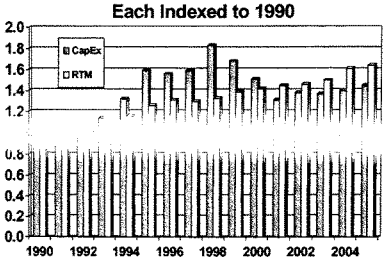
Chart 3 compares capital expenditures to operating revenue, showing the percentage of revenue that railroads have invested in maintaining and expanding their systems. The spike from 1995 to 2000 reflects merger activity, but overall the chart shows that

Chart 1
Class I Railroads
Capital Expenditures
(Dollars in Billions)



Source: Assn. Of American Railroads, "Railroad Facts," various for historic results
2006 investment level from AAR press release

Chart 2
Index of Capital Expenditures* and Index of Revenue Ton-Miles
Each Indexed to 1990

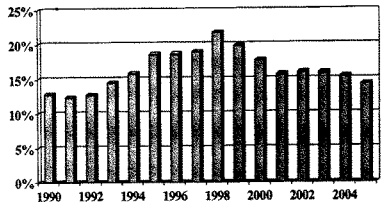


Source: Assn. Of American Railroads, "Railroad Facts."
* Capital Expenditures are in constant 1990 dollars

railroads can consistently invest at least 15 percent of their operating revenues.

In addition to annual growth in capital spending from increasing revenues, the industry appears to have the financial resources to raise additional capital for capacity expansion. According to industrial sector data compiled by New York University's Leonard Stern School of Business, the U.S. railroads[2] debt ratio [defined as (long term debt)/(long term debt + shareholders equity)] has improved by a little over 25 percent in recent years, moving from 41 percent in 2000 to 30 percent in 2004. (Out of 100 industry sectors in this database, ranked from most to least debt, railroads consistently ranked 23, meaning that only 22 other sectors had worse ratios.) Using AAR data, if the analysis is confined to the seven Class I railroads, it appears the industry has the capability of assuming up to $4 billion in additional debt.

Chart 3
Class I Railroads
Ratio of Capital Expenditures to Operating Revenues



Source: Assn. Of American Railroads, "Railroad Facts."

Railroad investments must meet the test of the marketplace.
As the discussion above makes clear, the industry's capital expense budget, while large compared to other sectors, is not unlimited. Railroads judge a project by testing its expected internal rate of return against a pre-set hurdle rate. Projects with the highest return are funded first, followed in order by others until available investment capital is exhausted. Carriers must be confident that the investment will be justified by traffic levels or cost-saving operational improvements. Even projects with high rates of return may not be funded if there are other, better, uses for the money.

This review process has produced many significant projects that expand rail capacity. For example, The Burlington Northern Santa Fe has nearly completed double-tracking its transcontinental route from California to Chicago. Union Pacific is double-tracking its Sunset Route, which serves the same markets. Both carriers are continuing to triple-track their Powder River Basin joint line, to improve the movement of low sulfur coal to the nation's utilities. Similarly, other Class I's are expanding yards, double and triple-[illegible] increase capacity.

This month, Norfolk Southern Railway (NS) and Kansas City Southern Railway (KCS) received regulatory approval for their joint venture to improve capacity along KCS's Meridian Speedway, a 320-mile line between Meridian, MS and Shreveport, LA. NS is investing $300 million in this project. In addition, CSX is adding capacity on its rail lines between Chicago and Florida, and between Albany, New York and New York City. Overall CSX plans to spend $255 million on capital expansion projects. The industry is also expected to add over 800 locomotives this year and hire over 12,000 new employees.

[2] Analysis was comprised of 18 selected U.S. railroads, which includes more than the Class I's.

New rolling stock is also being added to handle the increase in business.

New technology will improve capacity.
New terminals and expanded rights-of-way are not the only means to increase rail freight capacity. Investment in new technology also holds significant promise. Two of the most important opportunities available today are Positive Train Control (PTC) and Electronically Controlled Pneumatic (ECP) brakes. The industry and FRA have researched each extensively.

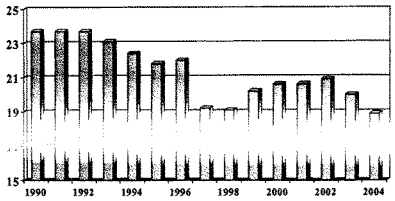
Under PTC, enhanced communications and real-time information reduce headways and improve train speeds and safety. The information provided by PTC will permit more effective management of train movements over the affected infrastructure. These improvements will eventually allow the carriers to move more freight over the system without adding track or equipment. Better train speeds improve a carrier's asset utilization. Consider that a 1 mph increase in average train speed can save large railroads an estimated $200 million a year. By moving freight a littler quicker over long distances with the same number of trains and crews, the effective number of workers and locomotives per mile falls, generating large efficiencies. PTC is not yet a reality across the general rail system. However, very substantial technical progress has been achieved, and now momentum appears to be increasing toward wide-scale implementation

Research and actual implementation has shown that ECP brakes offer major benefits to the rail industry. In addition to improved train handling, car maintenance, and fuel savings, ECP brakes also offer increases in network capacity.

Each system requires substantial investment on the part of the railroads. Investment in either of these technologies offers additional choices to improve capacity. But as with any expenditures, railroads will require these investments to meet the rate-of-return test, based on real-world assumptions.

The bottom line on any rail expansion is the requirement by investors for an adequate return on that investment. The industry appears to be making capacity-enhancing investments at a responsible pace, but is unlikely to [illegible] surge demand. But even at this pace, there is still some question whether the industry can keep up with the growing levels of traffic. Chart 4 shows the decline in train speed since 1990 as an indicator of service levels and asset utilization.

Chart 4
Class I Railroads
Freight Train Speed



Source: Assn. Of American Railroads, "Analysis of Class I Railroads."
Measure of Freight Train-Miles per Freight Train-Hour

PUBLIC BENEFITS OF ADDITIONAL CAPACITY

There are often public benefits to expanding rail.
Rail transportation can provide significant public benefits. For example, a single intermodal train leaving the Ports of LA/Long Beach represents 280 fewer trucks on the highways between Los Angeles and Chicago. In one day, 50 intermodal trains, the equivalent of 14,000 trucks, leave Los Angeles. Various studies show that rail is anywhere from three to ten times more energy-efficient than intercity trucking, an important consideration in times of rising fuel prices. Rail is also the safest way to transport freight over land. Substituting rail for long distance trucks reduces highway congestion, road maintenance costs and truck VMT. Reductions in VMT reduce highway exposure and deaths.

Many individual rail and rail-related projects provide specific significant public benefits along with private benefits. The $2.43 billion Alameda Corridor project separated local streets and a heavily used rail line, eliminating grade crossings and reducing vehicular congestion. In addition to providing local benefits, the Corridor has eased congestion at the Ports of LA/Long Beach by facilitating faster intermodal service between the Southern California ports and receivers in the Midwest and East.

Brownsville, Texas recently completed a project begun in 1973 to relocate in-city rail yards and deactivate 79 of the city's 93 grade crossings. The project, which cost $52 million, provided smoother rail operations and took the majority of traffic from the Port of Brownsville out of the downtown business district.

Another successful project is the Norfolk Southern's Shellpot Bridge rebuilding in Wilmington, Delaware. The bridge's poor condition caused the previous owner, Conrail, to take the bridge, and consequently the line serving the east side of Wilmington, out of service. Freight moved through the city and rail service to industries on Wilmington's east side was degraded. The parties realized that rebuilding the bridge and reopening the line would improve efficiency and capacity for north/south freight traffic, lessening freight on a passenger route and providing economic benefits to Wilmington and Delaware. NS had limited capital to finance the $13 million project; however, the state used a combination of grants and loans to rehabilitate the bridge, with the loans to be repaid through a per-car user fee. The project has been a success; NS reports that the line has attracted new business, car counts are up, and available capacity at the Edgemoor Yard in Wilmington is now being used.

In none of these projects, nor in many others underway or on the drawing boards of transportation planners, were the returns to the rail carriers involved sufficient to justify funding the entire cost of the endeavor. Nor could the public bodies accomplish the projects by themselves. However, through successful collaboration and innovative uses of funds, both the public and private sectors benefited.

TODAY'S SOLUTIONS

Expanding rail capacity will require investment from several partners.

The rail industry has been clear that it is committed to expanding capacity -- at a pace and a level justified by available capital and project-by-project rates of returns. But that investment, reasonable from a railroad perspective, may not be sufficient to respond to nationwide capacity and congestion issues. One view of this, from a state DOT perspective, can be found in the American Association of State Highway and Transportation Officials' 2003 *Freight-Rail Bottom Line Report.* That study estimated that the rail system would need to invest between $9 and $10 billion per year to maintain current traffic and accommodate a "fair share" of forecast growth. The study noted that the rail industry could be expected to cover $6 to $7 billion; the remainder had to come from other sources. Public/private partnerships, such as the Alameda Corridor project, Delaware's rehabilitation of Norfolk Southern's Shellpot Bridge, and the Brownsville rail relocation provide one approach to increasing capacity.

State and local public-private partnerships provide a logical, market-based approach to address the returns demanded by private capital and the public benefits needed by communities and governments. Each party to the partnership accepts the risks it can manage and the returns it must receive. It competes for use of capital to assure an efficient allocation process. In addition to the three noted above, examples of successful public-private partnerships, financed through a variety of mechanisms, include:

The Alameda Corridor-East

This project is being undertaken in anticipation of the growth in train traffic into and out of the ports of LA/Long Beach. The project is designed to mitigate the effects of the growth of this traffic on urban streets and thoroughfares. Estimated to cost $950 million, the project to be completed in two phases will improve at grade crossing along a 35-mile corridor. Overall, the project will improve 39 crossings, making them safer and reducing the amount of time that motorist must wait. Railroad and public funding (including local contributions) has been secured through the completion of Phase 1.

Kansas City Flyovers

Kansas City has completed two projects that improve the flow of rail traffic [illegible] million project opened in 2000, and the Argentine Connection, a [illegible] million flyover opened in 2004. The Sheffield Project helped reduce delays of as many as 250 trains by eliminating at-grade intersections of several railroads. Similarly, the Argentine Project reduced delays for 80 trains through the Kansas City Terminal area. Each project was financed through special bonding authority, to be paid off through user fees. The projects improve rail flows and eliminate significant congestion on area roads and highways.

Public-private partnerships are not a panacea, however. The rail industry's willingness, and ability, to enter into them is constrained by available funds, the level of private benefits that would accrue, and competing projects with better internal rates of return.

There is a mix of programs available at the federal level to fund rail projects. There are two loan programs that could fund rail capacity expansion -- the Railroad Rehabilitation and Infrastructure Financing (RRIF) and Transportation Infrastructure Finance and Innovation Act (TIFIA) programs; both require a guaranteed revenue stream to secure the loan. Some rail-oriented projects received funding under the new Projects of National Significance program initiated in SAFETEA-LU. Other opportunities include private activity bonds for intermodal terminals, and federal highway funds (the Section 130 program) available to improve the safety of rail-highway grade crossings. On the state and local level, the public share of some projects has been provided through taxes, transportation and/or economic development funds and other financing mechanisms.

This mix of programs, and constrained private resources, may be why many of the more ambitious public/private projects developed in recent years to expand capacity and eliminate congestion have not yet gotten underway.

One notable example is the Chicago Regional Environmental and Transportation Efficiency Project (CREATE). CREATE is an agreement between six railroads, the City of Chicago and the state of Illinois to develop five rail corridors, including one primarily for passenger trains, construct 25 new grade separations, build six rail-to-rail "flyovers" to separate freight and passenger trains and convert the St. Charles Air Line elevated railroad tracks to public use. This is an ambitious $1.5 billion project that would improve the flow of rail freight and passenger traffic through one of the most important -- and congested -- rail hubs in the country, and mitigate the adverse effects of increased traffic on the local community. The freight railroads agreed to commit $212 million, covering what they believe to be the operational benefits they would receive from the project. SAFETEA-LU provided another $100 million.

A plan developed in Houston is aimed at rationalizing the maze of rail lines and terminals that serve the city's port and its extensive chemical industry. A major objective of the plan is to eliminate at-grade rail highway crossings and the congestion associated with them. It is my understanding that at this point no project financing commitments have been make by public agencies, or railroads.

The Mid-Atlantic Rail Operations Study (MARO) was a joint study by NS, CSX Railroad, and AMTRAK. The study identified infrastructure constraints in five Mid-Atlantic States (New Jersey, Pennsylvania, Delaware, Maryland, and Virginia). Removing these rail constraints could attract more freight to this corridor, lessening truck congestion on I-95 and parallel routes. It delineated improvements in three time periods: near term, mid-term and long term. The total cost is estimated to be $6.2 billion. No funds have been committed.

Alternative Financing Options

On the highway side, private ownership and operation of toll roads is generating considerable interest -- the recent acquisition of the Chicago Skyway and the Indiana Tollway by private firms is a case in point. For rail, an alternative approach may be the development of "third party" projects, where non-railroad private sector interests build and operate specific pieces of infrastructure, funding it through tolls or other user fees.

This approach is being explored in the Trans Texas Corridor, a proposed 600-mile transportation corridor from the Mexican border to Dallas, paralleling I-35. Recently a partnership of two construction firms, Cintra of Spain and Zachry from San Antonio, won a bid to develop plans for the corridor segment paralleling I-35. The company is offering to build a toll road from San Antonio to Dallas and pay $1.2 billion to collect fees from it for up to 50 years. In addition to this project, Cintra-Zachry is offering to develop a high-speed freight rail line. The firm states that the project cost could be up to $6 billion. It would be financed through charges to shippers, but might also look to funding from the Texas Rail Relocation Fund or other federal and state programs.

This project, as well as the two recent highway acquisitions, demonstrates that third party investors are clearly interested in supplementing transportation investment in the U.S. Similar third party ownership and funding is worth exploring for rail projects, particularly in congested urban areas. Rail terminals, in particular, offer a good prospect for capitalizing user fees.

Potential Barriers to Additional Investment

In today's environment, the economic regulatory framework must ensure that needed capacity investments are not discouraged. Already, high levels of demand from shippers for rail services are exacerbating tensions between carriers and shippers, with some calling for more constraints on rail rates and revenues. Since 1980, the Surface Transportation Board has administered the Staggers Act to ensure a favorable climate for rail infrastructure investment. It is important that the regulatory framework contributes to solving capacity problems rather than compounding them.

Additionally, we must find a way to address community and environmental issues associated with rail capacity expansion. The current high level of railroad operations has led to numerous complaints about noise, blocked grade crossings and reduced safety. With many communities already sensitive to changes in railroad operations, major capacity expansion may face delays unless community issues are addressed.

Communities often do not realize that railroads are not required to provide noise barriers and other environmental mitigation measures as they increase train traffic. Unlike highway expansions, there are usually no public funds available to mitigate rail impacts.

CONCLUSION

Transportation congestion of both rail and highways is a significant national concern, constraining our economy and wasting resources. Demand for rail transportation is growing faster than additional capacity can be provided, leading to service problems as

traffic increases. As private firms, railroads must choose expansion projects that best fit their business plans and available capital, limiting their ability to add capacity quickly. State and local public-private partnerships are a well-tested mechanism for funding rail projects with significant public benefits, but the public sector, like the rail industry, has limited available funds. We need to add other models, such as third-party investments, where appropriate. Finally, the Federal government needs to be wary of actions that would skew the market. We should not support mechanisms that foster speculative projects based on wishful thinking. Nor should we discourage needed investment or encourage disinvestment through an unbalanced regulatory policy.

STATEMENT OF
THE HONORABLE CORRINE BROWN
SUBCOMMITTEE ON RAILROADS
HEARING ON
"THE U.S. RAIL CAPACITY CRUNCH"
APRIL 26, 2006

Thank you Mr. Chairman for holding this important hearing. It could not have come at a more appropriate time because I believe we are on the verge of a crisis on our Nation's railways.

Thanks to economic growth and a sharp increase in international trade, the railroad industry has more business than it has the capacity to handle. And while the nation's freight railroads are in much better financial health today than they were in 1980 when we partially deregulated the industry, the railroads still do not earn enough to cover their cost of

capital. As a result, railroads have either had to defer maintenance or cut back on the number of miles served. The size of the freight rail network has literally deteriorated to about half of what it was 26 years ago while freight shipments have more than doubled.

We need to find a solution – a permanent solution – to this problem or the situation will only get worse. According to the U.S. Department of Transportation, rail traffic is expected to rise more than 50 percent by the Year 2020. As traffic grows, traffic bottlenecks will further impede freight and passenger rail operations and adversely impact the businesses

of railroad customers, many of which count on just-in-time deliveries. Moreover, as gas prices soar to $3 or $4 a gallon, recovering drivers will turn more and more to commuter rail and Amtrak, putting even more pressure on an already congested system.

I know there are many ideas out there for helping our nation's railroads. Railroads are critically important to our nation's economic health and development and they must have adequate support from the Federal Government – just like we do for aviation, highways, and mass transit – if they are to continue meeting the needs of their customers and if they are to

continue to help keep truck traffic off America's highways.

I want to welcome today's distinguished panelists, and I look forward to their insight on ensuring the fairest and most efficient freight rail service for both the railroads and their customers.

Thank you, Mr. Chairman.

TESTIMONY OF SECRETARY FRANK J. BUSALACCHI
WISCONSIN DEPARTMENT OF TRANSPORTATION

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To the U.S. House of Representatives Subcommittee in Railroads
Hearing on "The U.S. Rail Capacity Crunch"
April 26, 2006

Mr. Chairman, my name is Frank Busalacchi. I serve as Secretary of the Wisconsin Department of Transportation and Chairman of the States for Passenger Rail Coalition. I also was recently appointed to the National Surface Transportation Policy and Revenue Study Commission, which will address the current condition and future needs of the nation's transportation system.

The States for Passenger Rail Coalition is a group of 27 state transportation agencies that support U.S. intercity passenger rail development. The coalition's mission is to promote the development, implementation and expansion of intercity passenger rail services with involvement and support from state governments. Our primary goal is the enactment of a comprehensive federal intercity passenger rail program that provides sufficient capital funding to the states to implement planned corridor improvements throughout the country. A map of our member states is attached.

While I am here today representing the States for Passenger Rail Coalition, virtually all of our state members have various kinds of freight rail support programs, and we are also vitally interested maintaining the competitiveness and efficiency of our nation's freight railroads.

Our coalition was founded in 2000 during a period of emerging state interest in US intercity passenger rail development. This interest is driven by a number of factors:

Thirteen states currently provide funding to support intercity corridor services in partnership with Amtrak. These state-supported services provide 37 percent of Amtrak ridership and about half of Amtrak's daily trains.

Some 35 states in the country have developed transportation plans that call for intercity passenger rail improvements as one way to provide additional mobility choices for their citizens and to address increasing congestion on our highways and at our airports.

Finally, widespread public demand for intercity passenger rail service is reflected in robust increases in intercity passenger rail ridership throughout the country. For example, the Hiawatha Service between Milwaukee and Chicago supported by the states

of Wisconsin and Illinois set an all time record in 2005 with 544,000 riders – a 15.8 percent increase over the prior year, which was also a record. Similar increases in ridership are evident in state-supported services throughout the country. For example Pennsylvania's Keystone Service, Illinois' Chicago-St. Louis Service, Maine's Downeaster and Oklahoma's Heartland Flyer also had double digit increases in 2005.

However, while public demand is growing, rail congestion throughout the country has become a significant threat to states supporting or desiring to implement new passenger rail service. Virtually all current and planned state-supported services operate on corridors owned by freight railroads; many of these corridors are facing increasing levels of congestion. This rail congestion is driven by increases in freight traffic, as well as by bottlenecks caused by aging track and signal infrastructure.

As a state transportation secretary, I am concerned about the impacts rail congestion will have on our highway system. As our rail system becomes congested and less reliable, traffic will shift to our already congested highways. Additional heavy truck traffic can take a terrible toll on our bridges and pavements. This will translate into additional costs for our already under-funded highway program.

I am also very concerned about the impacts of rail congestion on our passenger rail service. Rail capacity and congestion problems are reflected in declining trends in passenger rail on-time performance. On-time performance for all state-supported and other short distance trains for the fiscal year ending in September 2005 was 70.4 percent, a decline of 3.1 percent from fiscal year 2004. On-time performance dropped to 67.5 percent during the next four months ending in January of this year, a decline of 7.8 percent from the same time period in the prior year.

These summary numbers disguise severe problems in specific corridors. In January of this year, on-time performance for the San Joaquin Service in California was only 35.2 percent, a fall of 33.3 percent from January 2005. For the same period, on-time performance for the Cascades Service in Washington State was 50.5 percent, a drop of 27.2 percent and on the Carolinian in North Carolina it was 19.4 percent, a decline of 21.6 percent.

The members of the States for Passenger Rail Coalition do not view these capacity problems as insurmountable. We all have extensive plans to make improvements in track and signal infrastructure to allow for enhancements in passenger rail service. These improvements are designed to also address capacity issues associated with the underlying freight service provided by our host railroads.

The investments proposed by states are substantial. The American Association of State Highway and Transportation Officials' 2002 "Intercity Passenger Rail Transportation Report" documents the findings of these plans in some 35 states. The report identifies $10.4 billion in track, signal and equipment improvements planned by states in freight corridors, which could be programmed over the next six years. The report identifies $47 billion in state capital needs over a 20-year period. The report also recommends

substantial funding to bring the Northeast Corridor owned by Amtrak up to a state of good repair.

State plans generally focus on corridor improvements between major city pairs. These corridors are frequently in highly congested urbanized areas where rail capacity issues are most often severe for both passenger and freight operations. For example the nine -state Midwest Regional Rail Initiative Plan calls for a total of $6.6 billion in infrastructure investment across its recommended 3,000 mile Chicago-hubbed passenger rail system. Of that total, over $1.2 billion in investment is targeted on the highly congested area within 40 miles of Chicago. State plans identify a number of other such corridors of national significance in the Southeast, the Pacific Northwest, California, the Southwest, the Northeast and the Gulf Coast in addition to the Midwest.

Many of these plans can be implemented in the near future if fully funded. In Wisconsin, we are proposing to extend the Hiawatha Service from Milwaukee to Madison with track and signal improvements estimated at $227 million in 2002 dollars. The project has been developed cooperatively with the Canadian Pacific Railway. We have already completed preliminary engineering and environmental work for this project and the Federal Railroad Administration has issued environmental clearance in the form of a "Finding of No Significant Impact."

Many other states have also worked cooperatively with freight railroads on similar planning and project implementation activities:

- California, Washington State and Oregon in partnership with Burlington Northern Santa Fe
- New York in partnership with the Canadian Pacific Railway
- New York, Florida, Virginia and North Carolina in partnership with CSX Transportation
- Delaware, Ohio and North Carolina in partnership with Norfolk Southern
- Oregon and Illinois in partnership with Union Pacific
- Pennsylvania in partnership with Norfolk Southern

With all of the interest on the part of the states and the general public in intercity passenger rail development -- why are we continuing to witness declining on-time performance? The States for Passenger Rail Coalition firmly believes that the missing ingredient is a reliable federal funding partner.

We believe our highly successful federal programs for highways and airports offer models for long-needed congressional action to address the critical passenger rail corridor improvement needs that have been identified by the states. Federal investment in passenger rail improvements can address freight rail capacity needs in these corridors, while at the same time showing a public transportation benefit. Action is needed now on a comprehensive federal program that provides adequate capital funding for states to address these needs.

The States for Passenger Rail Coalition is on record supporting a dedicated, multi-year federal funding program for state-supported passenger rail projects. In the past we have supported tax credit bonding authority for the states as one mechanism for insuring funding continuity for major corridor development projects, which typically take several years to complete. We are on record supporting HR-1631 The Railroad Infrastructure Development and Expansion Act for the 21st Century (RIDE 21) which provided $12 billion in tax credit bonding authority to states.

We are encouraged by recent bipartisan Senate action on S.1516 The Passenger Rail Investment and Improvement Act of 2005. This legislation provides an authorization of $1.4 billion in 80/20 federal/state funding to states subject to appropriation, which we believe is a good start. But more funding is required to address the national project needs that have been identified by the states and a mechanism needs to be provided to allow for the development of multi-year projects.

The States for Passenger Rail Coalition stands ready to assist the House Rail Subcommittee in developing intercity passenger rail legislation that can be acted on yet this year. Action on such a program can be a first step in addressing the national rail capacity problems that exist throughout the country.

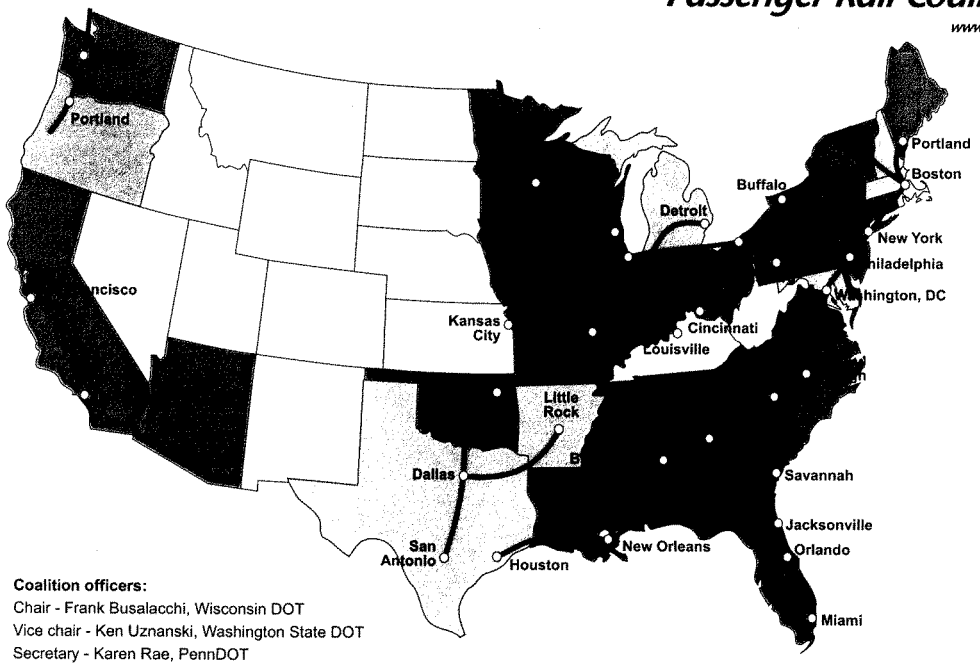
We need to remedy the lack of balance in our federal transportation funding programs. In the 25 years before the watershed September 11 tragedy, $782 billion was spent on transportation at the federal level: 48% for highways, 22% on aviation, 12% for ports and waterways, 12% for public transit and only 4% for rail. The need to adjust our transportation priorities is obvious.

We believe the public supports such a program. The public needs mobility alternatives to congested highways and airports. As the pump price for fuel continues to march steadily upward towards $4 and $5 dollars per gallon, the public's demand for energy-efficient rail service will continue to increase. From an environmental standpoint, an argument can be made that for every passenger or two who boards a train, a vehicle is taken off the road, along with that vehicle's contribution in emissions to the global warming mix.

The benefits are there -- to the general public, to the freight railroads, to the shippers they serve and to the nation's economy. What is needed now is the congressional resolve to take action.

States for Passenger Rail Coalition

www.s4prc.org



Coalition officers:
Chair - Frank Busalacchi, Wisconsin DOT
Vice chair - Ken Uznanski, Washington State DOT
Secretary - Karen Rae, PennDOT

Member states (27) **Other high-speed rail corridor states** **Federally designated high-speed rail corridors**

Statement by Congressman Jerry F. Costello
Committee on Transportation and Infrastructure
Subcommittee on Railroads
Hearing on the US Rail Capacity Crunch
April 26, 2006

Thank you, Mr. Chairman. I am pleased to be here today as we discuss the US rail capacity crunch. I would like to welcome today's witnesses.

Freight railroads operating in the US move more freight more efficiently and cheaply than any other freight rail system in the world. Our system moves vast amounts of everything, connecting businesses all over this country and with markets globally over a rail network spanning approximately 143,000 route miles. And with rising fuel prices, more companies are turning to railroads as a cheaper way to transport goods. This surge in freight is so pronounced that it threatens to create a capacity crunch.

This demand for freight transportation is predicted to continue to grow over the next 20 years, relieving highway congestion, conserving fuel, and promoting safety. With this increased demand comes a continued need for additional investments in infrastructure projects to enhance service, promote efficiency, and reduce prices.

The city of Chicago, the busiest hub in the U.S. with more than 1,200 trains passing through it every day, put forward a plan to invest $1.5 billion in public and private funds for railroad upgrades. Six major rail companies pledged $212 million, and Congress has put forth $100 million for the project.

Innovative plans and initiatives, like the CREATE project, must be part of the solution to this capacity crunch. With demand continuing to exceed supply, the rail system is extremely strained overall and I look forward to hearing from our witnesses on other proposed solutions.

Again, thank you Mr. Chairman for calling today's hearing.

COMMITTEE ON TRANSPORTATION & INFRASTRUCTURE
Subcommittee on Railroads

"U.S. Rail Capacity Crunch"

April 26, 2006
10:00 a.m.
Room 2167, Rayburn House Office Building

Opening Statement of Congressman Elijah E. Cummings

Mr. Chairman:

I thank you for calling today's hearing to enable us to examine the growing capacity crunch on our nation's rail network.

In 1980, Congress passed the Staggers Act in an effort to revive the American railroad industry by reducing regulatory control and giving railroads more freedom to establish rates and routes, and to make other business decisions.

After passage of the Act, the railroad industry began to consolidate dramatically. There were more than 60 Class I railroads in 1976; today, there are 7.

Much as the authors of the Staggers Act had hoped, these remaining railroads have slowly regained their financial footing and their position as the dominant carriers of freight in this nation.

Thus, while the share of freight traffic carried on railroads in the United States had been declining prior to deregulation, today, railroads carry more than 40% of intercity freight ton-miles in the United States – which exceeds the percentage of freight carried by any other mode of transportation in our nation.

As a result of this growth, many of the Class I railroads are experiencing annual increases in both net income and rates of return-on-investment.

However, because railroads sold or abandoned significant stretches of track as the industry consolidated, we have now reached a point where railroads are carrying twice the total number of ton-miles that they carried a quarter century ago on a network that is approximately half the size it was then.

While this consolidation has surely contributed to the railroads' return to profitability, as demand has increased, the railroads have not begun to restore network capacity fast enough to keep pace with that demand.

Today's hearing gives us an opportunity to explore in more detail the causes of this growing mismatch between demand and capacity and the impact that it is having on the movement of rail freight in our nation and on the service provided to shippers.

Mr. Chairman, I am particularly eager to know whether investments are being constrained by the amount of capital available to railroads or whether railroads are constraining their investment to continue to grow their profitability.

Whatever its cause, it is clear that the consequences of the service crunch that currently exists are very serious for all shippers but particularly for our nation's public utilities, which rely on the railroads to bring them the coal they use to generate electricity.

At this critical time, when consumers are increasingly squeezed by rising gas prices, we cannot afford to have already high electricity prices increased by unreliable rail service that forces utilities to buy electricity on the spot market or increase their use of natural gas for generation.

We must ensure that the nation's rail network – which is a vital part of our nation's transportation system – is providing the most effective and efficient possible service to shippers to keep our economy moving forward. We must also prepare for what the U.S. Department of Transportation has projected may be a 50% increase in total freight tonnage on our rail network by 2020.

I am confident that today's hearing will help us assess whether our current business and regulatory structures are

helping us meet these goals and I look forward to hearing from today's witnesses.

Thank you and I yield back.

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BEFORE THE

House Committee on Transportation & Infrastructure

Subcommittee on Railroads

The U.S. Rail Capacity Crunch

TESTIMONY OF

Glenn English, C.E.O.
National Rural Electric Cooperative Association

4301 Wilson Boulevard
Arlington, Virginia 22203

Wednesday, April 26, 2006
10:00 a.m.
2167 Rayburn House Office Building

Mr. Chairman, my name is Glenn English. I am the Chief Executive Officer of the National Rural Electric Cooperative Association. I also serve as Chairman of Consumers United for Rail Equity (C.U.R.E.), a captive rail customer advocacy group representing a broad array of vital industries – chemical manufacturers and processors; paper, pulp and forest products; agricultural commodities producers and processors; cement and building materials suppliers; and many more.

I appreciate the invitation to appear before you today to discuss an issue that has rapidly risen to the top of the policy agenda for members of NRECA, a trade association consisting of nearly 1,000 cooperatives providing electricity to more than 39 million consumers living in 47 states. As member-owned, not-for-profit organizations the obligation of cooperatives is to provide a reliable supply of electricity to all consumers in our service areas at the lowest possible price. We take our obligation to serve very seriously – the personal and economic health of our members, our communities and our nation depends on it. Co-ops serve primarily the more sparsely populated parts of our nation, but cover roughly 74 percent of the land mass of the nation.

The Captive Shipper/Railroad Monopoly Problem

Mr. Chairman, about 50% of the nation's electricity is generated from coal. In the electric cooperative community, about 80% of the electricity generated by our plants is from coal. Very few of our generating facilities are located at coal mine sites, so most of the coal consumed by our plants is delivered by rail.

Co-ops buy the coal at the mine site and arrange for its transportation, so the shipping agreements are between the railroad companies and the cooperative. Generally, our co-ops provide and maintain the "train sets" – the unit trains that today normally number from 120 to 130 cars. We also provide unloading facilities and make other capital investments related to rail transportation of coal to our plants. In the movement of coal to our plants, the railroads provide the locomotives, the tracks, the crews and the fuel.

Increasingly, our members are must deal with poorer service and higher costs for their coal transportation than ever before. Horror stories abound. Consolidation of the rail industry has resulted in many of our generators being held "captive" to one single railroad for coal transportation. As a result, a great many of our electric generators are subject to railroad monopoly power over price and service with no access to competition. The railroads have extensive exemptions from the nation's antitrust laws. Under the Staggers Rail Act, the ICC (now Surface Transportation Board) was to deregulate competitive rail traffic, while also preventing railroad monopoly abuse of "single served" or "captive" traffic. That protection is not being provided.

The STB has interpreted Staggers in a manner that allows railroads to deny shippers access to competing railroads, and has a rate challenge process so complex, costly and time consuming as to provide virtually no protection to rail customers. Recently captive rail rates have increased steeply for Dairyland Generation and

Transmission Co-op in Wisconsin, where freight rates doubled this year, resulting in 45% higher consumer electric bills. We recognize that rail traffic is growing and there is a need for investment in rail infrastructure. That need for investment, however, is not an excuse for the unfair practices that are now standard operating procedures for the railroads.

I want to recognize the Ranking Member of the full committee, Mr. Oberstar, for his keen interest in resolving both of the issue areas before us today – the U.S. railway "capacity crunch," and the need to mandate reforms in the industry at the same time we seek to provide mechanisms to encourage adequate infrastructure investment.

Along with Congressman Baker of Louisiana and 13 others, Mr. Oberstar introduced H.R.2047, the Railroad Competition Improvement and Reauthorization Act, on May 4th last year. He clearly articulated "the rest of the railroad story" in his introductory statement, citing the anti-competitive stranglehold of the remaining four major Class I railroads over captive shippers in "entire States, regions, and industries." Today there are 30 cosponsors for that legislation.

The situation facing us today goes far beyond just the very high prices being charged captive shippers. Currently, the nation faces a situation wherein the railroads are either unable or unwilling to deliver reliable supplies of coal to our generators in a timely fashion. So, in a very real sense, our members are paying much more and receiving far less when it comes to rail transportation. Policies must be changed to address a rapidly worsening situation that is harming critical industries.

Current Coal Delivery Problems Adversely Impact Electricity

April 17th, we were reminded what happens if there is a shortage of electric generating capacity. Hundred degree temperatures in Texas sent folks scurrying for air conditioners, overwhelming the available electricity generating capacity. According to the Electric Reliability Council of Texas (ERCOT), significant generating capacity on the system was down for maintenance prior to the summer air conditioning season. Thus, the transmission system was short of electricity resulting in forced 15-minute rolling blackouts. This incident illustrates what happens when – for any reason – there is not enough generation, and it serves as a warning. The fact is that electric generation is now threatened by the railroads' poor performance and their lack of reliability.

The delivery system for half the nation's electricity consists of coal mines, rail transportation, generators, and transmission and distribution systems. Due to rail transportation problems, many of the electric cooperative generators are extremely low on coal supply as we enter the summer cooling season. Some generating facilities are dangerously close to the point where continued operation cannot be sustained. If these units are forced to reduce their production of electricity, our co-ops would either have to use natural gas generators – at fuel costs as much as 5 to 7 times as high as the cost of coal – or buy excess electricity on the grid, if there is any. If the gas or excess electricity is not available, certain areas of the nation could be short of generating capacity and brown outs or rolling black outs just like those experienced last week in Texas could occur.

In a world suffering from shortages of energy supplies, our nation is blessed with enormous reserves of coal that can provide for electricity and other uses for many decades in the future. Our coal resources are sufficient to meet our energy needs for more than 250 years. Some have referred to the United States as the Saudi Arabia of coal. In a 2001 speech, Vice-President Dick Cheney pointed out that the overall demand for electric power is expected to rise by 43-percent over the next 20 years, and that just meeting the demand would require between 1,300 and 1,900 new power plants. That averages to more than one new power plant per week, every week, for the next 20 years. "We all speak of the new economy and its marvels," he said, "sometimes forgetting that it all runs on electric power."

Coal is still the most plentiful source of affordable energy in the country, and by far the primary source of electric power generation. What the Vice-President might not have recognized at the time of his speech was that the railroads responsible for moving this strategically important fuel supply were already in the process of making America's most abundant and affordable energy supply scarce and expensive. When electric co-ops are looking to South America and other foreign coal sources because the railroads cannot make timely domestic deliveries, we know the *status quo* cannot stand.

Let me focus on the coal delivery problem confronting just one very large coal-fired electric generator in Wyoming – the Laramie River Station. In the spring of 2005, there were two derailments on tracks coming from the Powder River Basin (PRB), the source of the nation's largest supply of low sulfur coal. This reduced rail deliveries of coal by 80 to 85 percent, and deliveries have not yet recovered.

The three unit (1650 MW) Laramie River Station in Wheatland, Wyoming, located only 170 miles from the coal source, is down to a 6 day supply of coal, even with its coal conservation plan. This plant is operated by Basin Electric Power Cooperative for 6 not-for-profit utilities. Other co-ops are experiencing similar problems securing sufficient coal to run the generators and have had to cut production at those plants that are normally the least expensive to operate. Electricity generators have resorted to burning more expensive natural gas, purchasing higher cost electricity from the grid, or purchasing more expensive and higher sulfur local coal. Arkansas Electric Cooperative has estimated that alternate-fuel power generation costs for its customers have increased by $100-million because of the shortage of coal deliveries over the past 12 months to its power plants.

The shortfall in rail coal deliveries has many far-reaching consequences. In order to replace an expected 20-million ton shortfall of PRB coal deliveries in 2006, it will require the use of about 340-billion cubic feet of natural gas costing about $2.6-billion more than the coal. The additional use of natural gas to generate instead of coal has also significantly driven up the price of gas across the country, and – again illustrating the adverse impacts on many of our other industrial sectors – has increased the costs to those using natural gas as a feed-stock for manufacture of their products. Restriction in the supply of PRB coal has also resulted in a tripling of the coal spot market price, increasing those prices from roughly $6.00 per ton to more than $20 per ton.

Railroad Obligation to Serve – Wall Street vs. Main Street

Mr. Chairman, we believe that an overriding national public interest applies to the railroad industry. Clearly, as with our electric utility industry, there is a national interest in the operation of the rail system. No electric utility – whether a rural electric cooperative, a municipal power system or an investor owned utility – is free to conduct business in any manner it likes, including "maximizing" profits. City officials overseeing municipal utilities are subject to the vote of the people; rural electric co-op boards must earn election by their member-owners; and investor owned utilities are subject to the oversight of both state public service commissions and the Federal Energy Regulatory Commission.

Railroad companies want to tell the Congress only one side of the story, emphasizing the status and effects of freight railroad traffic "constraints" – the "capacity crunch – while alleging there is a crying need for financial incentives to lure the level of investments needed to provide additional capital necessary to modernize and expand America's rail infrastructure and capacity.

There is no question that the infrastructure and the capacity of our railroads needs significant expansion and capacity improvement if we as a nation are going to continue to grow our economy, provide new and better jobs, and compete for business in a global marketplace. However, Mr. Chairman, there is a dark side to the story about how America's railroads are operating. There is an honest question of how really sincere they are about reducing "constraints" in capacity when those very same constraints – coupled with their exercise of monopoly power over captive customers – have led to ever growing profit levels for the major rail corporations. The railroads and Wall Street have been focused on making large profits while Main Street Americans are focused on the "big picture" of growing and expanding our overall economy – not just one sector.

We contend that the railroad industry should – like electric utilities – also have an obligation to serve the national public interest. This obligation may sometimes be called a "common carrier" obligation, but in the end it is an obligation to serve. Further, this obligation to serve means the obligation to provide reliable transportation service to all customers at fair and reasonable prices. Without mandating an obligation to serve by the railroads, the economy of this nation cannot move forward. Adequate, dependable, and reasonably priced rail service is almost as critical to our national and economic security interests as electricity, and the public interest cries out for the imposition of an "obligation to serve" in order to correct the current abusive tendencies of the railroads.

The Surface Transportation Board asserts little jurisdiction over railroad service issues and has been completely passive during the current coal delivery problems. When the CEO of Arkansas Electric Cooperative sent a letter on this subject to the STB last August, not only did he never receive a response from the STB, his letter was answered by a Vice President of the Burlington Northern Railroad – the railroad about whom he was complaining! Today, there is effectively no government agency to which rail customers can turn for redress even when severe railroad service problems are being experienced.

Some tell us that the economic self-interest of the railroads will solve the railroad service and capacity problems over time. That certainly was the premise of the Staggers Rail Act – deregulate the railroads and they will become healthy and provide the rail service needed by the nation at fair and reasonable prices. Railroad customers have good reason to doubt that assertion.

In the absence of strong signals from the government about service and capacity to meet the needs of "Main Street" America, the railroads will take their signals only from "Wall Street." Financial analysts today rate railroad stocks high because the railroads possess "pricing power" based on the fact that demand for rail transportation exceeds capacity. Moreover, Wall Street tends to grade railroad stocks down when the railroads make heavy investments in their systems. So, Mr. Chairman, there is significant concern among the rail customer community that actually providing sufficient capacity and reliable service for them will be perceived by Wall Street as adverse to the economic interests of the rail industry.

Questions about future reliable rail service at fair prices is a significant concern to the electricity industry as it attempts to provide the additional coal-fired power plants the nation will need in the future. Can we depend on reliable rail transportation of coal in the future at a fair and reasonable price?

Assistance Helps Ensure Profits – Requires an Obligation to Serve

Finally, Mr. Chairman, we understand that legislation may be introduced to provide a 25% investment tax credit for investments in railroad infrastructure. We may very well support such a federal incentive, so long as it was part of a package of legislation that also addressed the concerns of rail customers that find themselves subject to railroad monopoly power, and so long as the tax credit is also available to rail customers when they make similar investments in infrastructure to improve overall rail capacity.

Moreover, there should be certain conditions imposed on the investments eligible for the tax credit. For example, the investments that qualify for this tax credit should be limited to first improving the infrastructure that currently provides insufficient service to captive or single-served rail customers. Investments eligible for the tax credit should be focused first on infrastructure that benefits the movement of domestic products and commodities as opposed to infrastructure that benefits imported container traffic. Finally, any infrastructure that benefits from the tax credit should be deployed in a pro-competitive manner as suggested in H.R.2047, as opposed to further expanding the monopoly power of the railroads.

But I remind the subcommittee again that the rationale for providing any level of assistance to the railroads is because of the important role they play in our nation's overall economy. Electric utilities are viewed as absolutely critical not only to the economy, but also indispensable in helping to ensure our homeland security. Railroads obviously

occupy a similar role, and thus Congress and the American people are willing to provide all reasonable assistance to ensure the rail transportation system is robust and efficient, but with those benefits to help ensure the profitability of the rail industry also should come an obligation to serve the best interests of Main Street America – not just Wall Street.

Conclusion

Mr. Chairman, thank you for conducting this hearing today. We support a strong and viable rail industry that will provide reliable service to its customers at fair and reasonable prices. The status quo in the industry will not result in this type of rail system for the nation. Those kinds of reforms and changes from current law as suggested in H.R.2047 must be adopted as federal policy, and the public benefits that result from competition in the marketplace must be applied to the rail transportation system by removing the rail industry's exemptions from the nation's antitrust laws.

I can assure the subcommittee that the 39-million consumer-owners of the NRECA electric cooperative family look forward to working with you, and with all of the other stakeholders involved, in resolving these critical rail transportation issues in an objective and constructive manner.

--- END ---

STATEMENT OF

EDWARD R. HAMBERGER

PRESIDENT & CHIEF EXECUTIVE OFFICER

ASSOCIATION OF AMERICAN RAILROADS

BEFORE THE

U.S. HOUSE OF REPRESENTATIVES

COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

SUBCOMMITTEE ON RAILROADS

HEARING ON

RAILROAD CAPACITY

APRIL 26, 2006

On behalf of the members of the Association of American Railroads (AAR), thank you for the opportunity to discuss freight railroad capacity. AAR members account for the vast majority of freight railroad mileage, employees, and revenue in Canada, Mexico, and the United States.

Over the years, comprehensive, reliable, and cost-effective freight railroad service has been critical to our nation's economic prosperity. Freight railroads serve nearly every industrial, wholesale, retail, agricultural, and mineral-based sector of our economy. North America's freight railroads are the most efficient and cost effective in the world.

Looking ahead, the United States cannot prosper in an increasingly competitive global marketplace if our freight railroads are unable to meet our growing transportation needs, and having adequate railroad capacity is critical in meeting these needs. Railroads must be able to both maintain their extensive *existing* infrastructure and equipment and build the substantial *new capacity* that will be required to transport the significant additional traffic our economy will generate.

If they are to be able to handle this traffic, though, railroads must earn profits consistent with long-term financial sustainability. As the Congressional Budget Office (CBO) recently noted, "As demand increases, the railroads' ability to generate profits from which to finance new investments will be critical. Profits are key to increasing capacity because they provide both the incentives and the means to make new investments."[1]

Today, some 25 years after the Staggers Act was passed, freight railroads are finally beginning to show tangible signs that financial sustainability might be within reach. Rail earnings over the past year, while below average within the universe of all industries,

[1] Congressional Budget Office, *Freight Rail Transportation: Long-Term Issues* (January 2006), p. 11.

have been significantly higher than their historical norm. This welcome development means that railroads can more easily justify and afford the massive investments and capacity enhancements that will be required if railroads are to continue to play their proper role in meeting our freight transportation needs.

I respectfully suggest that members of this committee, your colleagues in Congress, and other policymakers also have critical roles to play. Indeed, a primary obligation of policymakers is to take steps that assist — and, just as importantly, not take steps that hinder — railroads in making the investments needed to provide the current and future freight transportation capacity our nation requires.

Any policy that unreasonably restricts future rail earnings and capital cost recovery — and especially a swing in the regulatory or legislative environment back to heavy-handed government interference in rail operations — will take railroads away from the sustainability they need. Such an outcome would be harmful at any time, but it would be especially harmful today, given that as a nation we are in dire need of *more* railroad investments and *more* railroad capacity, not less.

Capacity is a Challenge Everywhere in Transportation Today

"Every aspect of the supply chain is stretched. It's not a question of whether [a congestion crisis] is going to happen. It's a question of when," notes a West Coast port terminal operator."[2] "In 23 years, I have never seen a situation where the supply chain is at capacity. It's busting at the seams," an executive with a major chemicals firm notes.[3]

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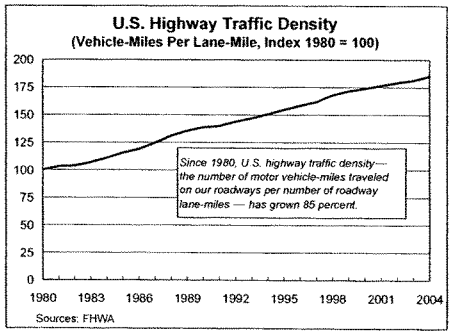
[2] Doug Tilden, CEO, Marine Terminals, quoted in *The Financial Times*, March 14, 2006.

[3] Randy Schaeffer, Manager of Rail Fleet Procurement, Air Products and Chemicals, quoted in *Traffic World*, May 16, 2005.

"Our highways, waterways, railroads and aviation networks are simply not keeping up with ordinary demands," says the head of UPS.[4]

To be sure, freight is still being delivered, and there is a tremendous amount of strength and flexibility in our nation's transportation systems. But as these statements make clear, all freight modes in the United States are facing capacity challenges today.

For example, the number of motor vehicle-miles traveled on our roadways has grown some 95 percent since 1980, while the number of roadway lane-miles rose just 5 percent during this time. The result is an 85 percent increase in vehicle-miles per mile of roadway — a major reason why many highways that were not routinely seeing traffic jams 20 years ago are routinely seeing traffic jams today. Building our way out of highway gridlock will be extremely difficult: as the American Association of State Highway and Transportation Officials (AASHTO) notes, "[T]he social, economic, and environmental costs of adding new highway capacity are prohibitively high in many areas."[5] Hours of service regulations and a huge perennial driver shortage create additional motor carrier capacity limitations.



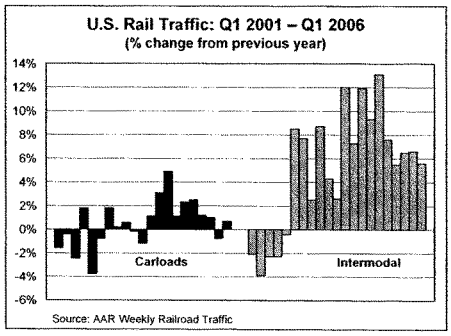
Ports too are increasingly congested due to the explosion in international trade. For example, at the Ports of Long Beach and Los Angeles, the two largest U.S. container ports,

[4] Michael L. Eskew, Chairman and CEO, UPS, in a speech to the World Affairs Council of Philadelphia, April 6, 2006.

[5] AASHTO *Freight Rail Bottom Line Report* (January 2003), p. 2.

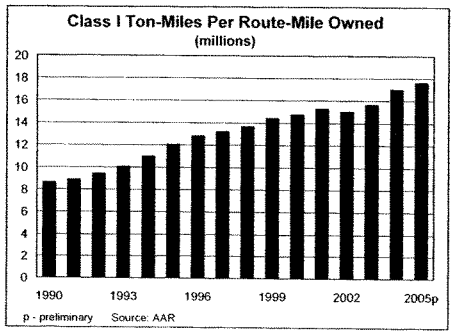
the combined number of containers handled in aggregate (in TEUs) rose from 3.7 million in 1990 to some 14.2 million in 2005, a 280 percent increase. Other ports registered huge intermodal traffic gains over this period as well, including 78 percent for the Port of Seattle, 147 percent for the Port of Charleston, and 354 percent for the Port of Savannah.

For U.S. freight railroads, year-over-year quarterly carload traffic has risen in nine of the past ten full quarters, and intermodal traffic has increased in each of the past 16 full quarters, year-over-year. As a result, U.S. railroads today are hauling more freight that ever before.



These traffic increases have resulted in capacity constraints and service issues at certain junctions and corridors within the rail network. In fact, excess capacity has disappeared from many critical segments of the national rail system.

The reality that rail assets are being used more intensively is reflected in rail traffic density figures. From 1990 to 2005, traffic density for Class I railroads — defined as ton-miles per route-mile owned — more than doubled. (Other measures of traffic density, such as car-miles per mile of track, have also shown substantial increases.) Of course,



different rail corridors differ in their traffic density and their change in density over time, and individual railroads differ in the degree to which their capacity is constrained overall. Still, there is no question that there is significantly less room to spare on the U.S. rail network today than there was even a couple of years ago.

In light of current capacity and service issues, some shippers and others have inappropriately blamed railroads for not having enough infrastructure, workers, or equipment in place to handle the surge in traffic. Perhaps railroads and their customers could have done a better job of forecasting and preparing for the sharply higher traffic volumes of recent years. But to contend that railroads can afford to have significant amounts of spare capacity on hand 'just in case' — or that shippers would be willing to pay for it, or capital providers willing to finance it — is completely unrealistic. Like other companies, railroads try to build and staff for the business at hand or expected to soon be at hand. "Build it and they will come" has rarely been a winning strategy for freight railroads.

Over the past couple of decades, Class I railroads have shed tens of thousands of miles of marginal trackage. They had no choice, because they could not afford to keep it, and it freed resources for use on higher priority core routes. Most of the miles that were shed were transferred to short-line operators, and most of these remain part of our rail network. Even if railroads could have afforded to retain this mileage — and again, they could not — most of it was in locations that would not be useful in ameliorating today's capacity constraints.

In part, this is because long-lived rail infrastructure installed many decades ago was often designed for types and quantities of traffic, and origin and destination locations, that are dramatically different than those that exist today. For example, only within the last two

decades has Powder River Basin coal taken on the enormous importance it currently enjoys. Similarly, the explosive growth of intermodal traffic is mainly a phenomenon of the past 20 years.

When business is unexpectedly strong, railroads are unable to expand capacity as quickly as they might like. Locomotives, for example, can take a year or more to be delivered following their order; new entry-level employees take six months or more to become hired, trained, and qualified; and it can take a year or more to plan and build, say, a new siding.[6] And, of course, before investments in these types of capacity enhancements are made, railroads must be confident that traffic and revenue levels will remain sufficiently high to justify the enhancements for the long term. Again, in this regard railroads are no different than the vast majority of their customers.

Freight Transportation Demand Will Increase Sharply in the Years Ahead

No matter the mode, capacity constraints exert a substantial economic toll. As Secretary of Transportation Norman Mineta has noted, "Congestion and inefficiency in transportation are, in effect, hidden taxes that burden every business and every individual, and we must find ways to lighten that load." That "load" could become much worse over the next 15 years if demand for freight transportation grows as quickly as expected.

The U.S. Department of Transportation (DOT) has projected that overall demand for freight rail service (measured in tons) will increase 55 percent (1.3 billion tons) by 2020 from 1998 levels, equal to 2.0 percent per year. The DOT projects a 69 percent increase (10.6 billion tons) in total freight transportation demand.[7]

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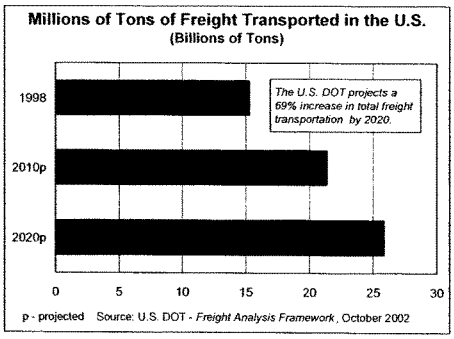
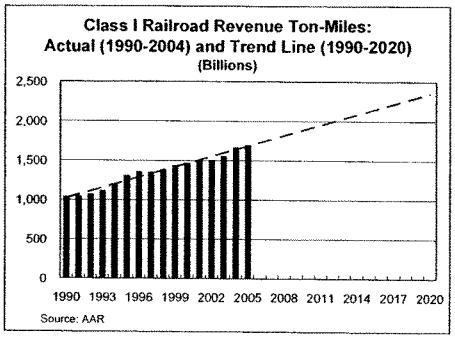
[6] This may seem like a long period of time, but it compares favorably with the decade (or more) it can take to build a typical stretch of highway.

[7] U.S. Department of Transportation- *Freight Analysis Framework*, October 2002.

In a 2005 forecast, economic consultants Global Insight predicted that rail carload and intermodal tonnage will increase by 29 percent (650 million tons) from 2004 to 2016, or 2.1 percent per year. Global Insight expects total freight transportation demand to rise 31 percent by 2016.[8]



If Class I ton-mile growth from 2005 through 2020 does nothing more than match the rate of growth from 1990 through 2005, rail ton-miles in 2020 will total 2.35 trillion, up 38 percent (or 2.2 percent per year, on average) from the 1.70 trillion in 2005.



These projections for increases in freight transportation demand should give all of us pause. At full or near-full capacity, transport systems become more fragile. With inadequate redundancy, there are fewer alternative routes and facilities, breakdowns and back-ups proliferate faster and further, and recovery from disruptions takes longer. Ameliorating capacity constraints across modes will entail significant costs, but in the long run the cost is likely to be far less than if we do not adequately address the issue now.

[8] *U.S. Freight Transportation Forecast to 2016*, produced for the American Trucking Associations.

Railroads Are Working Hard on a Variety of Fronts to Increase Capacity

For their part, U.S. freight railroads are well aware that capacity constraints have led to service-related problems on parts of their networks, and they are committed to solving these problems by addressing the host of factors that influence the fluidity and resiliency of freight rail operations.

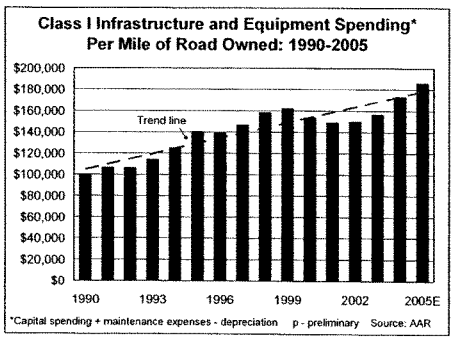
Spending on Infrastructure and Equipment

Of the many different factors that affect how well a rail network functions, the basic amount and quality of infrastructure and equipment is probably the most important. That is why U.S. freight railroads have been expending, and will continue to expend, enormous resources to improve their asset base. As traffic grows, railroads will have to concentrate increasingly on building new capacity to accommodate that growth — while continuing to maintain existing capacity. But if a railroad is not financially sustainable over the long term, it will not be able to attract the capital necessary to maintain its existing network in top condition, or make additional investments in the replacement or expansion of infrastructure required by growing demand.

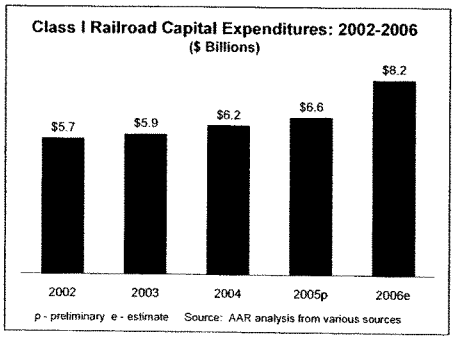
This point is especially relevant for railroads relative to other modes. In contrast to the extensive government funding for truck, barge, and airline infrastructure over the past 25 years, freight railroads have historically received little government financial assistance for infrastructure construction or maintenance. Instead, freight railroads have financed infrastructure improvements (and equipment investments, such as locomotives) almost exclusively through their own earnings and by borrowing.[9]

[9] As discussed beginning on page 25, railroads favor more pronounced use of public-private partnerships for rail infrastructure improvement projects where the fundamental purpose of the project is to provide public benefits or meet public needs, and support tax incentives for rail investments that enhance capacity.

From 1980 through 2005, Class I freight railroads alone invested some $174 billion in capital and maintenance expenses related to infrastructure, and another $183 billion in capital and maintenance expenses related to equipment. (Non-Class I railroads have invested additional billions of dollars.[10]) Class I railroads typically devote approximately 45 percent of their operating revenue, or $15 billion to $17 billion per year, toward these purposes, which have been trending higher since 1990 on a per-mile basis.



Moreover, rail spending, which is already substantial, is expected to rise sharply. Based on an analysis of recent railroad financial presentations, press releases, and other sources, it appears that Class I capital expenditures on infrastructure and equipment are set to rise in 2006 to around $8.2 billion, up sharply from around $5.7 billion just four years earlier. This huge increase demonstrates the diligence with which railroads are responding to the capacity issue.



The following is just a sampling of the diverse types of capacity-enhancing investments individual railroads have recently made or will soon make:

[10] For non-Class I railroads, improving infrastructure to handle 286,000 pound cars is a major issue. The AAR urges Congress to extend the three-year short line infrastructure tax credit, which expires in 2007.

- BNSF Railway double-tracked 76 miles of main line between Chicago and Los Angeles in 2005, and another 56 miles will be double- or triple-tracked this year. Within a couple of years, the entire 2,200-mile route will be double-tracked. In 2005, BNSF also took delivery of some 400 centerbeam cars (for hauling lumber); 3,700 high-capacity covered hoppers for carrying grain and other commodities; 1,300 rapid-discharge coal cars; and 650 intermodal flatcars with capacity to carry 6,500 intermodal double-stack containers. BNSF also took delivery of 288 new locomotives in 2005 and will add more than 300 more in 2006.
- In 2006, Canadian National will spend $1.2 billion to $1.3 billion on capital programs in the United States and Canada. Included are the reconfiguration of the key Johnston Yard in Memphis, a gateway for CN's rail operations in the Gulf of Mexico region; siding extensions in Western Canada; and investments in CN's Prince Rupert, British Columbia, corridor to capitalize on the Port of Prince Rupert's potential as an important traffic gateway between Asia and the North American heartland.
- In 2005, Canadian Pacific finished its biggest capacity enhancement project in more than 20 years by expanding its network from Canada's Prairie region to the Port of Vancouver. The project increased the capacity of CP's western network by 12 percent and improved the route structure from Canada's Pacific coast to the United States. Like other carriers, CP has added new sidings on congested corridors; taken delivery of dozens of new locomotives and newer, higher-capacity freight cars; and hired and trained hundreds of new employees, many of whom will be in the United States.
- CSX recently announced plans to spend $1.3 billion to $1.4 billion per year on capital expenditures in 2006 and 2007, up from approximately $1 billion over the previous few years. In addition to improvements elsewhere, installation of sidings, signals, and other infrastructure on lines between Chicago and Florida and between New York City and Albany will expand

capacity and improve service reliability. CSX will also add several hundred new locomotives over the next few years.

- Kansas City Southern is busy integrating its Kansas City Southern dé Mexico subsidiary fully into the railroad's other operations. KCS plans to spend some $120 million in the United States and another $96 million in Mexico in 2006. Particular attention will be given to the construction of new tracks and other improvements at the railroad's Shreveport, Louisiana hub; improvements on the "Meridian Speedway" between Shreveport and Meridian, Mississippi to augment the new rails, new sidings, and new drainage system installed in 2005; and the expansion of rail yards, track upgrades, and new sidings on its "Tex-Mex" subsidiary.
- Norfolk Southern (NS) will purchase more than 220 new locomotives from late 2005 through mid-2006 to augment the hundreds purchased over the past few years. NS is also in the midst of its largest-ever locomotive rehabilitation program — in 2005, 491 locomotives were overhauled and 29 were rebuilt; another 420 will be overhauled and 52 rebuilt in 2006. NS is also beginning its "Heartland Corridor" project, which, among other things, will entail raising clearances at 28 tunnels in Virginia, West Virginia, and Kentucky to allow double-stack intermodal service over the entire route from the Port of Norfolk to Columbus, Ohio and Chicago.
- Since 2004, Union Pacific has purchased 713 new locomotives and will purchase an additional 200 in 2006. One of UP's main capacity expansion programs for 2006 is its 760-mile Sunset Route between Los Angeles and El Paso. Today, more than 42 percent of the Sunset Route is double tracked, including 69 miles that were completed in 2005 at a cost of some $100 million. UP plans to double track another 50 miles this year and most of the remainder within a few years. In addition, UP will also be adding siding capacity improvements along its corridor from Los Angeles to Salt Lake City to facilitate bi-directional running and provide further surge capacity for the Sunset Route; the North Platte, Nebraska to Chicago

corridor; the Kansas City to St. Louis corridor; and the Dallas-San Antonio-Houston areas in Texas.

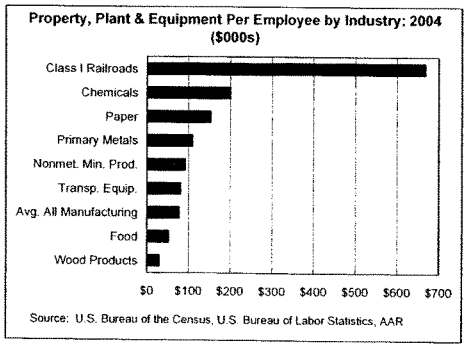
The massive investments railroads must make in their systems are a reflection of the extreme capital intensity of railroads. By any of a variety of measures, railroads are at or near the top among all U.S. industries in terms of capital intensity.

For example, from 1995 to 2004, the average U.S. manufacturer spent 3.5 percent of revenue on capital expenditures. The comparable figure for U.S. freight railroads was 17.8 percent, or more than five times higher. Likewise, in 2004 railroad net investment in plant and equipment per employee was $667,000 — more than eight times the average for all U.S. manufacturing ($78,000).

Capital Expenditures as a % of Revenue for Various U.S. Industries: Avg. 1995-2004

Average all manufacturing	**3.5%**
Food manufacturing	2.6%
Transportation equip. mfg.	2.8%
Machinery manufacturing	3.0%
Wood product mfg.	3.0%
Petroleum & coal products mfg.	3.0%
Fabricated metal product mfg.	3.5%
Chemicals manufacturing	4.4%
Plastics & rubber products mfg.	4.5%
Paper manufacturing	4.7%
Computer & electr. product mfg.	5.0%
Nonmetallic mineral product mfg.	5.4%
Electric utilities	11.6%
Class I Railroads	**17.8%**

Note: Utilities are 1999-2004
Source: U.S. Bureau of the Census, AAR, EEI



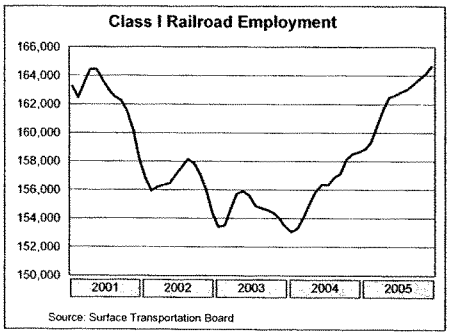
The bottom line is that railroading is extraordinarily expensive, and simply cannot be done "on the cheap." At the same time, adding capacity is risky, which is why railroads, as noted earlier, need to be sure that the market will support additions to capacity over the long-term (which in railroading can be 30 years or more). As a former NS official remarked in comments to the Transportation Research Board, "Any capacity enhancing

project (be it fixed plant or locomotives or cars) has to be compared to all of the other demands on corporate capital and the returns must be attractive. Further, all investments must be consistent with a company's ability to raise capital. However "worthy" a capacity project might be, it must, in the end, lead to improved financial returns."[11]

Aggressive Hiring

In addition to infrastructure and equipment, rail capacity is a function of personnel, and railroads have been aggressively hiring and training crews to expand capacity.

In fact, over the past two years, Class I freight railroad employment has risen after 60 years of general decline. According to STB data, the number of Class I train and engine employees (essentially, engineers and conductors) rose from 61,113 in December 2003 to 69,658 in December 2005, an increase of 14 percent in just two years. The number of maintenance of way and structures employees rose from 32,925 in December 2003 to 34,227 in December 2005, an increase of 4 percent. Total Class I employment rose 8 percent from December 2003 to December 2005.



Infusion of Technology

Technology has always played a key role in expanding rail capacity. Control systems have become more sophisticated; trains have become longer and heavier;

[11] James McClellan, "Railroad Capacity Issues," background paper for Research to Enhance Rail Network Performance: A Workshop, Transportation Research Board, April 5-6, 2006.

locomotives have become more powerful and more reliable; and track structures have become more robust and thus less prone to outages for maintenance or because of failure.

Many of the dramatic technological advancements that have increased railroad efficiency (and safety) by helping to protect freight cars, locomotives, track, and cargo before damage, costly repairs, traffic holdups, and derailments occur have been developed and/or refined at the Transportation Technology Center Inc. (TTCI) in Pueblo, Colorado, a wholly-owned subsidiary of the AAR that is generally considered to be the finest rail research facility in the world. Just a few of these technological advancements include:

- *Wayside detectors* that identify defects on passing rail cars — including overheated bearings and wheels, dragging hoses, deteriorating bearings, cracked axles and wheels, and excessively high and wide loads — before structural failure or other damage occurs. Some of the newest wayside detectors being developed use *machine vision* to perform higher-accuracy inspections through the use of digitized images, which are then analyzed using computer algorithms
- Trackside *acoustic detector systems* use "acoustic signatures" to evaluate the sound of internal bearings to identify those likely to fail in the near term. These systems supplement or replace existing systems that identify bearings already in the process of failing by measuring the heat they generate.
- Advanced *track geometry cars* use sophisticated electronic and optical instruments to inspect track conditions, including alignment, gauge, and curvature. TTCI is developing an on-board computer system that provides an even more sophisticated analysis capability of track geometry, predicting the response of freight cars to track geometry deviations. This information will better enable railroads to determine track maintenance needs and help improve the safety of day-to-day rail operations.

- One of the most straightforward ways to add capacity to a rail network is to pack more freight on each train, and railroads have been doing that ever more aggressively. In 1995, for example, the average coal car carried on a Class I railroad held just under 103 tons of coal. By 2005 that figure had risen to nearly 112 tons, a 9 percent increase. But heavier loads are far more damaging to track structures than lighter loads. Researchers at TTCI and elsewhere are engaged in efforts related to this *heavy-axle load* (HAL) service. HAL-related work is underway on rail steels, insulated joints, bridges, welding, maintenance practices, and more.

Freight railroads have always been at the forefront in the use of computers and information technology, and today railroads are rapidly expanding their use of these technologies to improve overall efficiency and the fluidity of their operations, thereby adding capacity without adding infrastructure.

For example, advanced computer modeling software is used in a wide variety of rail applications, from automating rail grinding schedules[12] and improving customer demand forecasting to optimizing yard operations. CN, for example, is implementing what it calls "SmartYard," complex computer software that identifies and analyzes every possible combination and outcome for sequencing cars in a large classification yard and simultaneously updates and communicates the car processing plan. The result is more efficient, faster yard operations. Other railroads are engaged in similar efforts.

Recognizing that another way to add capacity is to move more trains faster over the same length of track, railroads are also working with their suppliers to design, implement, and improve innovative computerized "trip planning" systems. These highly-complex

[12] Rail grinding is a maintenance procedure for removing rail corrugations and surface defects, and for restoring the shape of rail to improve wheel and rail interaction and extend rail life.

systems automatically incorporate and analyze a mix of ever-changing variables (*e.g.*, crew and locomotive availability, terminal congestion, the different priority status of loads of freight, track conditions, maintenance plans, weather, etc.) to optimize how and when cars are assembled to form trains and when those trains depart.

Trip-planning systems are just one way that railroads are trying to improve equipment "cycle time" — *i.e.*, the total time it takes for a freight car to be loaded, hauled to destination, unloaded, returned to the same or a different shipper, and loaded again.

The benefits of increased efficiency explain rail efforts to "supersize," automate, and increase the velocity of traffic flows where practical. For example, railroads and their grain customers collaborate to consolidate grain loading at high-speed "shuttle loader" elevators. Railroads gain by improving the efficiency of their operations; shippers gain because the efficiencies produce railroad cost savings that are passed through in the form of lower rates. The efficiencies of shuttle operations can be striking. At BNSF, for example, a typical grain car in shuttle service hauls approximately three times more grain over the course of a year than a typical grain car in non-shuttle service.

Expanded over a network, operational efficiency can free up substantial capacity for other uses. At one major railroad, for example, a one mile-per-hour increase in system-wide velocity could mean that 250 locomotives, 5,000 freight cars, and 180 train and engine employees would be freed up to move additional traffic.

Cooperative Alliances and Collaborations

Railroads are also entering into operational alliances with each other which often rely on non-standard techniques to achieve desired results. These innovative collaborations lead to improved capacity utilization, lower costs, and better service. For example:

- A recent BNSF and CN track-sharing agreement will improve network fluidity and infrastructure capacity, principally in Vancouver, Chicago, and between Memphis and southern Illinois. Under the agreement, the railroads will exchange track and rail infrastructure, and CN will grant trackage, haulage, and other access rights to BNSF.
- CSX and UP are now operating their "Express Lane" service to haul fruits and vegetables by refrigerated rail car from California and the Pacific Northwest to population centers on the East Coast. UP and CSX also offer a similar "Wine Connection" service for wine movements. These joint ventures improve the utilization of rail assets and enhance the efficiency of coast-to-coast transportation.
- A KCS-NS joint venture will increase capacity and improve service on the "Meridian Speedway," a rail line between Meridian, Mississippi and Shreveport, Louisiana, that is crucial for transporting freight between the Southeast and the Southwest. KCS will contribute a 320-mile rail line between the cities, while NS will invest $300 million in cash, substantially all of which will be used for capital improvements to increase capacity over a four-year period. The capital improvements will include signal systems, extended sidings and stretches of double track.
- UP and CN have reached a routing protocol agreement to streamline their exchange of rail traffic at major gateways and reduce rail congestion in the Chicago area. Under the protocol, CN and UP are directing rail traffic flows through the most efficient interchange locations, thereby improving transit times and asset utilization.
- NS and CP recently began a partnership under which NS runs trains on CP trackage in New York state and then hands off the trains to CP, which hauls them across the border for further interchange or final delivery in Canada. The agreement allows NS to replace the inefficient and circuitous route it previously had to use for trans-border operations. In addition, NS hauls CP

trains between other points in New York, thereby allowing CP to improve the efficiency of its own operations.

- UP and CP recently strengthened their alliance at Eastport, Idaho, where CP hands off grain trains to UP for delivery to Pacific Coast ports. Working with customs authorities, the railroads have improved the customs clearance process, eliminating a major bottleneck that had been backing up trains at the border. The result has been a significant decrease in dwell time and a sharp increase in daily train count at the interchange.

Collaborations Between Railroads and Their Customers

Railroads, of course, recognize the importance of working closely with their customers to improve rail responsiveness to shipper needs, and in fact, collaborations between railroads and their customers are on the rise.

This fact was borne out by a recent survey of hundreds of shippers, carriers, third-party logistics providers, and government agencies by the Massachusetts Institute of Technology Center for Transportation and Logistics (CTL). Among other things, the CTL survey found that private sector collaboration — such as more frequent meetings between carriers and shippers, joint forecasting, establishing contingency plans, and other forms of interaction — are being used to find creative ways to prevent future problems and resolve current ones.

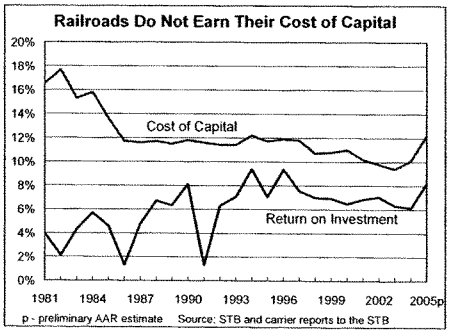
Railroads Must Be Financially Healthy to Expand Capacity

Since Congress passed the Staggers Act, railroads have only slowly made progress toward the goal of long-term financial sustainability. Financial sustainability is essential if railroads are to have any hope of meeting future rail capacity needs.

This slow progress is documented in the STB's annual revenue adequacy determinations. A railroad is "revenue adequate" — *i.e.*, it is earning enough to cover all

costs of efficient operation, including a competitive return on invested capital — when its rate of return on net investment (ROI) equals or exceeds the industry's current cost of capital (COC). This standard is widely accepted, approved by the courts, and similar to that used by public utility regulators throughout the country. It is also consistent with the unassailable point that, in our economy, firms and industries must produce sufficient earnings over the long term or capital will not flow to them. As a prominent Wall Street rail analyst recently noted, "Earning the cost of invested capital is not the end goal, but the entry ticket to the race, a credit without which Wall Street will squeeze investment."[13]

During the more than 25 years in which railroad revenue adequacy determinations have been made, railroads have significantly narrowed the COC vs. ROI gap, but a gap still remains.



Rail customers certainly understand the importance of earning the cost of capital over the long term. A spokesman for a major Florida electric utility noted, "If we can't make an attractive investment for the shareholder, then we are going to have a very difficult time going in the marketplace and competing for dollars."[14] The CFO of a major U.S. chemical company stated, "We want to create spread above the cost of capital through the cycle."[15] And the

[13] Anthony Hatch, "Six for 06: Trends To Watch in Rail," *The Journal of Commerce*, January 2006.

[14] Spokesman for Florida Power & Light, quoted in *The Palm Beach Post*, January 16, 2005.

[15] Rich Lorraine, SVP and CFO, Eastman Chemical Co., at the Morgan Stanley Basic Materials Conference, February 21, 2006.

CEO of a major U.S. forest products company recently stated "Each of our businesses continues to assess the ability of their individual facilities and product lines to earn the cost of capital. Those that cannot make the grade do not belong in our portfolio."[16]

Railroads agree with this sentiment, which is echoed by firms in every sector of the economy. Without the ability to cover total costs and earn adequate returns, railroads — like electric utilities, chemical companies, forest products firms, or any other firm — would be unable to maintain (much less increase investment in) their networks and could not sustain themselves over the long term.

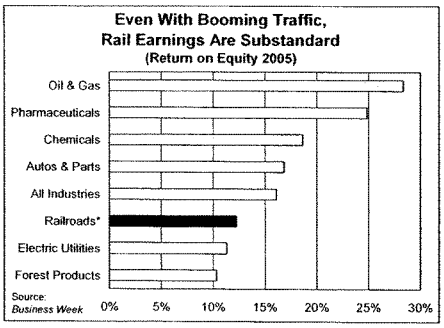
Without question, 2005 was a good year for railroads financially — revenue and net income were both up substantially. Frankly, it's about time the rail industry had a year like 2005, and they require them going forward. Improved rail earnings should be viewed as a welcome development because it means that railroads are better able to justify and afford the massive investments in new capacity and upkeep of their existing systems that need to be made.

That said, no one should get carried away regarding railroads' *relative* profitability in 2005, because the fact is, in 2005 — when railroads were hauling record levels of traffic and had sharply higher-than-historical profitability — rail industry earnings were *still* substandard compared with other industries.

Return on equity (ROE) is commonly used as an indicator of short-term profitability. According to *Business Week* data covering the S&P 500, in 2005 the average ROE for the four largest U.S. railroads was 12.3 percent — a substantial improvement over the 7.8 percent recorded in 2004, but still well below the 16.1 percent average for all firms

[16] Steve Rogel, Chairman, President & CEO, Weyerhaeuser Co., Q4 2005 Weyerhaeuser Co. Earnings Conference Call, February 3, 2006.

in the S&P 500 for 2005. The railroad REO was well below the median for chemical companies in the S&P 500 (18.7 percent) and only moderately higher than the median for electric utilities (10.8 percent) in the S&P 500.



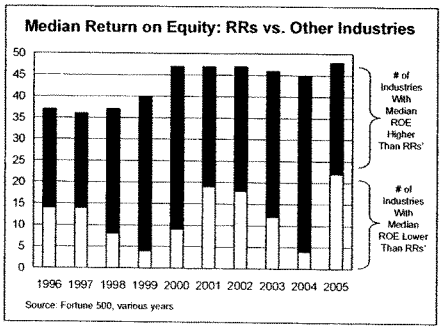
Data from the *Fortune 500* tell a similar story. In 2005, the median ROE for the railroads in the *Fortune 500* was 14.1 percent, less than the *Fortune 500* median of 14.9 percent and well below the ROE of numerous major rail customer groups.[17]

Fortune 500 Return on Equity: 2005

Industry	ROE	Industry	ROE
Household & Personal Prod.	41.5%	Aerospace and Defense	16.3%
Petroleum Refining	25.8%	**Fortune 500 Median**	**14.9%**
Mining, Crude-Oil Prod.	23.6%	Motor Vehicles & Parts	14.6%
Pharmaceuticals	23.4%	**Railroads**	**14.1%**
Food Consumer Products	21.8%	Pipelines	13.5%
Industrial & Farm Equip.	21.1%	Electronics, Electrical Equip.	12.1%
Computers, Office Equip.	19.7%	Engineering, Construction	11.8%
Oil & Gas Equip., Services	18.9%	Utilities: Gas & Electric	10.4%
Metals	18.3%	Energy	7.4%
Chemicals	18.1%	Food Production	6.2%
Medical Products & Equip.	17.3%	Packaging, Containers	4.6%
Beverages	16.4%	Telecommunications	4.2%

Source: Fortune 500

In each of the 20 years from 1986 to 2005, the median ROE for Class I railroads was less than the median for all *Fortune 500* companies, and in 15 of the 20 years, the median railroad ROE was in the lowest quartile among *Fortune 500* industries.



[17] The median railroad ROE for *Business Week* and *Fortune 500* differs because different definitions were used. *Business Week* uses net income excluding discontinued operations; *Fortune* uses net income including discontinued operations. *Business Week* uses average shareholders' equity for a year; *Fortune* uses end-of-year shareholders' equity.

Thus, even the improved rail earnings in 2005 are generally no more than (and in most cases less than) what non-regulated companies and industries earn.

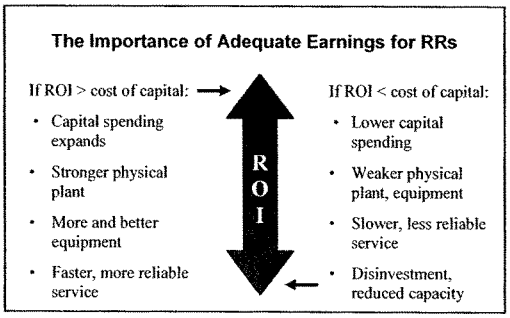
In any case, whatever may be the minimum level of earnings, profitability, or solvency considered adequate by financial analysts to declare a railroad "healthy" for short-term investment purposes, the primary question vis-à-vis those who complain about railroad "record profits" is whether a railroad's long-term profitability has reached the point at which regulatory actions can prudently be applied without adverse consequences for the rail network and the shipping public. Short-term improvements in profitability, short-term attainment of adequate revenue levels, accumulations of cash reserves, dividend pay-outs, and other similar measures do not signal that the necessary level of long-term profitability on rail operations has been achieved. Only a return on investment in excess of the cost of capital (discussed earlier) over a *sustained* period can trigger such an observation.

Reregulation is Not the Answer to Railroad Capacity and Service Problems

Unfortunately, rail critics have wrongly seized upon railroads' "record profits" in 2005 to support their claims that railroads should be forced to reduce their rates to certain shippers. This viewpoint — that short-term increased railroad profitability to moderate levels justifies a reinstatement of onerous restrictions on rail earnings — is exceedingly shortsighted and should be rejected.

Railroads have had to battle efforts to reregulate the industry since the Staggers Rail Act partially deregulated railroads in 1980. It is beyond the scope of this testimony to discuss in any detail the many ways in which reregulatory legislation (like H.R. 2047, the "Railroad Competition Act of 2005") is wrongheaded.

It should be noted, though, that the primary objective of those who call for rail reregulation is lower rail rates, even though, as discussed above, railroads are not earning excessive profits. Lower rail rates would translate directly into lower rail earnings. But proponents of reregulation ignore the fact that rail investments in infrastructure and equipment, like most private investment decisions in our economy, are driven by expected returns. The hundreds of billions of dollars invested in U.S. freight railroads since Staggers would not have been provided if not for the investors' expectation that the opportunity for a competitive return promised by Staggers would remain.



Under reregulation, rail managers could not commit, and rail stockholders would not supply, investment capital needed to improve service and expand capacity, because the railroads considering such investments would not have a reasonable opportunity to capture the benefits of those investments. Disaster might not occur overnight, but there would be little or no capacity expansion — something that certainly would have a near-term and significant adverse effect.

The financial community, on whom railroads depend for access to the capital they need to operate and expand, has consistently supported the view that, under reregulation, an era of capital starvation and disinvestment would return. They understand that no law

or regulation can force investors to provide resources to an industry whose returns are lower than the investors can obtain in other markets with comparable risk.

Proponents of reregulation cannot avoid the fundamental fact that shippers must be willing to pay for the rail service and rail capacity they say they need, and the market is far superior to the government in determining who should pay.

Some in the electric power industry are among the most vocal proponents of restrictions on rail earnings. Their advocacy of restrictions on railroads are not consistent with their claims regarding the need for cost-recovery and regulatory certainty in electricity transmission — a sector of the electricity industry with some parallels to railroading.

A representative of the Edison Electric Institute, for example, wrote "I cannot overemphasize the need for FERC to establish and put into effect a durable regulatory framework that says if I prudently invest a dollar in transmission infrastructure, that I will be able to fully recover that dollar, along with my cost of capital, through electricity rates. Such a framework is essential to raising the substantial and nearly unprecedented amount of capital necessary to construct needed, cost-effective transmission facilities."[18]

Likewise, the National Rural Electric Cooperative Association has noted that it "believes that the best way to attract capital to transmission at reasonable rates is to give investors greater certainty that they will receive a return on their investment."[19] The rail industry can think of no better way to create *un*certainty for their own capital providers "that they will receive a return on their investment" than proposals such as H.R. 2047.

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[18] Statement on behalf of the Edison Electric Institute by Alan J. Fohrer, CEO, Southern California Edison, to FERC, April 22, 2005.

[19] Comments of the National Rural Electric Cooperative Association Proposed Rulemaking Promoting Transmission Investment Through Pricing Reform," FERC Docket No. RM06-4-000, January 11, 2006, p. 17.

Such legislation is bad economics and bad public policy and should be rejected. It would mean *less* rail capacity when we need *more*.

Public Involvement in Freight Rail Infrastructure Investment

Freight railroads will continue to spend massive amounts to improve and maintain their systems. But even with their improved financial performance, funding constraints will likely prevent railroads from meeting optimal future rail infrastructure investment needs entirely on their own. As AASHTO noted in its *Freight Rail Bottom Line Report*, "The rail industry today is stable, productive, and competitive, with enough business and profit to operate but not to replenish its infrastructure quickly or grow rapidly."[20]

In its analysis, AASHTO estimated that railroads will need to carry an additional 888 million tons of freight annually by 2020 just to maintain their current market share. AASHTO also found that railroads will need $175 billion to $195 billion of infrastructure investment over this period to accommodate this traffic growth, and projected that railroads will be able to fund the majority of this investment — $142 billion — from their own retained earnings and borrowing. Unfortunately, according to the AASHTO analysis, the $142 billion will be enough to enable railroads to handle only half of their expected increase in traffic.

This funding shortfall means that many rail projects that would otherwise expand capacity and improve the ability of our nation's farms, mines, and factories to move their goods to market; speed the flow of imports and exports; relieve highway congestion; reduce pollution; lower highway costs; save fuel; and enhance safety will be delayed — or never made at all.

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[20] AASHTO, *Freight Rail Bottom Line Report*, p. 3.

I respectfully suggest that it is in our nation's best interest to ensure that optimal freight railroad capacity enhancements are made. Two ways that policymakers can help make this happen is by taking greater advantage of public-private partnerships for freight-railroad infrastructure projects and by introducing tax incentives for rail infrastructure projects that enhance capacity.

Public participation in freight rail infrastructure projects is justified because the extensive benefits that would accrue to the general public by increasing the use of freight rail would far exceed the costs of public participation. For example:

- *Highway congestion* – Highway congestion costs the U.S. economy more than $63 billion per year, but trying to eliminate it by focusing solely on highways is not practical because building more highways is becoming prohibitively expensive and time-consuming. Given budget constraints, environmental concerns, and other factors, we will be unable to simply build our way out of highway gridlock. Freight railroads, though, significantly reduce the costs of highway congestion and the need to build costly new highways. A single intermodal train takes up to 280 trucks (equivalent to more than 1,100 cars) off our highways. Trains carrying other types of freight take up to 500 trucks (equal to around 2,000 cars) off our highways.
- *Fuel efficiency* – Railroads are three or more times more fuel efficient than trucks. On average, in 2004 railroads moved a ton of freight nearly 410 miles per gallon of fuel. If just 10 percent of the intercity freight that moves by highway moved by rail instead, fuel savings would approach one billion gallons per year.
- *Pollution* – The Environmental Protection Agency (EPA) estimates that for every ton-mile of freight carried, a locomotive emits substantially less nitrogen oxides, particulates, and carbon dioxide than a typical truck.
- *Safety* – Fatality rates associated with intercity trucking are four times those associated with freight rail transportation. Railroads also have lower

> employee injury rates than other modes of transportation. Railroads and trucks carry roughly equal ton-miles of hazardous materials, but trucks have 16 times more hazmat releases than railroads.

This point was also made by AASTHO, which that "Relatively small public investments in the nation's freight railroads can be leveraged into relatively large benefits for the nation's highway infrastructure, highway users, and freight shippers."[21] The Congressional Budget Office has also concluded that public investment in rail infrastructure should be considered: "Another way of addressing the underpayment of infrastructure costs by railroads' competitors is to provide financial assistance to the railroads." Echoing AASHTO, CBO observed that, "[p]roviding federal aid for a rail investment might be economically justified if the net social benefits were large but the net private benefits to railroads were insufficient to induce them to make such an investment."[22] The Transportation Research Board has reached a similar conclusion, noting that "Greater public investment to relieve bottlenecks may improve efficiency — perhaps even in facilities that formerly were exclusively private..."[23]

Public-Private Partnerships

As members of this committee know, U.S. freight railroads are, with few exceptions, privately owned and operated, and have traditionally financed their infrastructure investments overwhelmingly through their own earnings and by borrowing from outside capital providers.

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[21] AASHTO, *Freight Rail Bottom Line Report*, p. 1.

[22] Congressional Budget Office, *Freight Rail Transportation: Long-Term Issues* (January 2006), p. 22.

[23] Transportation Research Board, *Critical Issues in Transportation* (January 2006), p. 3.

Capital providers, however, insist that railroads focus their limited investment funds on projects that promise a direct financial benefit to the investing railroad. While these projects may well provide substantial public benefits — such as reduced highway congestion, cleaner air, improved safety, and enhanced mobility — from a railroad's and capital provider's point of view, these are secondary to the project's financial return. This kind of imposed discipline by the financial markets is necessary and appropriate in a market economy, but it discourages investments that would yield significant public benefits but only limited financial benefits to the railroad.

A way to help states and localities improve rail networks that generate public benefits is through a more pronounced use of public-private financing partnerships for rail infrastructure improvement projects. Partnerships are not "subsidies" to railroads. Rather, they are an acknowledgement that private entities should pay for private benefits and public entities should pay for public benefits.

Partnerships reflect the fact that cooperation between interested entities is far more likely to result in timely, meaningful solutions to transportation problems than a go-it-alone approach. Without a partnership, projects that promise substantial public benefits in addition to private benefits are likely to be delayed or never started at all because it would be too difficult for either side to justify the full investment needed to complete them. In contrast, if a public entity shows it is willing to devote public dollars to a project equivalent to the public benefits that will accrue, the private entity is much more likely to provide the private dollars (commensurate with private gains) necessary for the project to proceed.

Going forward, the best-known public-private partnership involving freight railroads is the Chicago Region Environmental and Transportation Efficiency Program, or

CREATE. Conceived in June 2003, CREATE is a $1.5 billion program involving the State of Illinois, the City of Chicago, and the major freight and passenger railroads serving Chicago designed to modernize and improve Chicago's highway and rail transportation networks. Installing grade separations between tracks and highways will speed vehicle travel and reduce congestion and delays for motorists; updating track connections and expanding rail routes will reduce rail transit times; and adding separate, passenger-only tracks in key locations will remove numerous bottlenecks that have slowed passenger and freight movements in the region for decades.

Investment Tax Credit

Another way to bridge the funding gap between what should be invested in rail infrastructure and what railroads are likely to be able to afford on their own is to implement an investment tax credit for rail capacity enhancement projects.

Under the rail infrastructure investment tax incentive program now being developed by the rail industry, projects to *expand* freight rail capacity — by increasing the volume, weight, or speed of freight that can be carried — would be eligible for a 25 percent tax credit. Examples of qualifying capacity-expanding investments include raising tunnel clearances to accommodate double-stacked intermodal containers; upgrading single track lines to double or triple tracks; adding and lengthening sidings; strengthening bridges to carry heavier loads; and constructing intermodal terminals. In addition, new locomotives could also qualify for the credit if they met certain capacity-enhancement and other requirements.

Eligibility for the credit would extend to any taxpayer that makes a qualifying expenditure, not just railroads. For example, a shipper that built a rail spur from a

distribution center to a main line would be eligible, as would the builder of a rail intermodal terminal.

Under the rail industry proposal, infrastructure capital expenditures that do not qualify for the tax credit would be expensed (the expensing option would not apply to locomotives). This would place capital cost recovery for rail infrastructure on the same basis as competing modes of freight transportation (*i.e.*, highway and waterway), which "expense" their infrastructure costs.

Conclusion

U.S. freight railroads do a remarkable job in meeting the needs of an extremely diverse set of shippers. Railroads move tens of thousands of railcars to and from thousands of origins and destinations every day. The vast majority of these shipments arrive in a timely manner, in good condition, and at rates that shippers elsewhere in the world would love to have.

Still, it is clear that transportation capacity will have to increase as the economy expands. The railroads are committed to meeting these increased capacity needs primarily through private capital, but only if the regulatory structure gives the railroads an incentive to make the necessary investments. Policymakers can help ensure that rail capacity is adequate to meet our future freight transportation needs by ensuring that harmful economic reregulation is not instituted, engaging in more public-private partnerships for rail infrastructure projects, and instituting targeted tax incentives for projects that expand rail capacity.

Office of the President
Edward R. Hamberger
President and Chief Executive Officer

May 3, 2006

Honorable Steve LaTourette
Chairman
Subcommittee on Railroads
2453 Rayburn HOB
Washington, D.C. 20515

Honorable Corrine Brown
Ranking Minority Member
Subcommittee on Railroads
2444 Rayburn HOB
Washington, D.C. 20515

Dear Chairman LaTourette and Ranking Member Brown:

You recently received a letter from Alan Richardson, president of the American Public Power Association, providing comments in connection with the Subcommittee's recent hearing on the rail capacity issue. While he is certainly welcome to his own views, his letter wrongly implies that railroads are not doing all they can to move record volumes of coal to America's electric utilities. Nothing could be further from the truth.

While the railroad industry is only one part of an extremely complex, interconnected process of providing electricity to final consumers, following are some FACTS about the efforts that the rail industry has undertaken to efficiently serve its coal customers:

- From 1980 through 2005, Class I freight railroads invested nearly $360 billion — equal to some 45 percent of their revenue — back into their infrastructure and equipment, with much of this spending directed toward coal movements. (Coal accounts for around 43 percent of total rail tonnage.)

- Class I capital expenditures are set to rise in 2006 to around $8.3 billion, up sharply from prior years, with increasing amounts being devoted to expanding rail capacity.

- Historically the most important commodity for railroads, rail-hauled coal volumes have trended steadily upward for years. In 2005, U.S. freight railroads hauled more coal than ever before. For example, Powder River Basin shipments reached 415 million tons in 2005 and are expected to grow to 450 million tons in 2006. Similarly, movements of coal on eastern railroads grew by at least 6 percent in 2005 and are ahead of that record pace through the first quarter of 2006.

50 F Street, NW I Washington, DC 20001 I P (202) 639-2400 I F (202) 639-2286 I www.aar.org

- U.S. freight railroads are the most cost-effective in the world. Their immense productivity gains have allowed them to reduce their coal rates by an average of 32 percent in nominal dollars and 63 percent in inflation-adjusted terms from 1981 through 2004. These declines are in sharp contrast to a substantial increase in average U.S. electricity rates over this period.

- Railroads are in constant communication with coal consumers and suppliers to optimize current and future operations and to harmonize rail maintenance and other activities with those of the coal and utility communities. In fact, through our respective trade associations, AAR members have regularly scheduled meetings at both an operational level and the CEO level with members of the Edison Electric Institute and the National Mining Association.

Railroads take very seriously their commitment to provide reliable, cost effective transportation for all sectors of the economy, and they have an historical appreciation for the role they play in ensuring the reliability of the electricity grid. In fact, railroads account for approximately two-thirds of all coal movements. Coal, of course, accounts for half of U.S. electricity generation. That is why I was pleased to join with my colleagues from the utility trade associations to ask the Federal Energy Regulatory Commission to convene a workshop on the entire coal supply chain. Because of the complexity of the coal supply chain, it is important for the workshop to focus on every link of that chain: coal production, transportation (including barge), and actions taken by the utilities. Although the Surface Transportation Board is the appropriate agency to look at railroad service issues, the rail industry will take advantage of any and every opportunity to have high level strategic discussions with our partners in the electricity-by-coal process. Attached is my letter to the members of FERC supporting such a workshop.

Assuming that you are adding Mr. Richardson's letter to the hearing record, I ask that you include this letter and the attached letter as well.

On behalf of the freight rail industry, thank you both for your leadership on railroad issues.

Sincerely,

Edward R. Hamberger

Attachment

CC: Members of the Transportation and Infrastructure Committee

Office of the President
Edward R. Hamberger
President and Chief Executive Officer

May 3, 2006

Hon. Joseph Kelliher	Hon. Nora Mead Brownell	Hon. Suedeen G. Kelly
Chairman	Commissioner	Commissioner
FERC	FERC	FERC
888 First St., N.E.	888 First St., N.E.	888 First St., N.E.
Washington, D.C. 20426	Washington, D.C. 20426	Washington, D.C. 20426

Dear Commissioners:

It has come to my attention that the heads of four trade associations in Washington DC – Edison Electric Institute, the American Public Power Association, the National Rural Electric Cooperative Association and the Electric Power Supply Association – have requested that you convene a public workshop to address the role America's freight railroads play in moving coal to electric generating plants.

This past year saw record amounts of coal being moved from the Powder River Basin – 415 million tons – with expectations that 2006 will set another record of about 450 million tons. As you are aware, much of this coal moves over one thousand miles to destinations in all parts of the country. Similarly, eastern railroads' delivery of coal to utilities was up by 6.3% on Norfolk Southern and 7% on CSX. Fortunately, for the consumers of the country, we move the coal efficiently and at reasonable rates. The industry has invested about $360 billion in the last twenty five years to maintain and upgrade the rail network, with another $8.3 billion slated for capital expenditures in 2006.

Allow me to assure you that America's freight railroads take very seriously the role they play in helping produce over 50% of America's electricity. We transport about two-thirds of the coal burned at coal fired generators and have worked closely with members of each of the utility trade associations as well as the members of the National Mining Association to assure that America's electricity needs are met. In fact, twice a year railroad CEOs and Edison Electric Institute member CEOs meet to discuss issues of common concern. Similarly, railroad CEOs and coal producing CEOs have instituted bimonthly calls or meetings to coordinate on logistics matters. These efforts are bearing results. I was heartened to see Michael Morris, President and CEO of American Electric Power, the largest coal burning utility in the country, observe that his coal inventories are in reasonably good shape heading into the summer months: "We're in

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the 30-plus day range in terms of inventories at most facilities" (as quoted in Coal Trader, April 28).

Turning to the idea of a workshop, let me first emphasize that the Surface Transportation Board has jurisdiction over the freight railroads in both ratemaking and services areas. Thus, I was surprised when my association colleagues suggested that FERC convene such a workshop. Nonetheless, recognizing FERC's role in overseeing electricity reliability, the freight railroads would be willing to participate – with a few key changes.

We believe that the workshop should be expanded to cover all aspects of the supply chain. Thus, in addition to looking at railroad capacity and reliability, the following eight items should also be on the agenda:

1) Utility management decisions to cut inventories in previous years to save costs and hope for lower spot market coal prices;

2) Utility management decisions to favor investment in gas fired plants. This sent an unmistakable signal to both coal producers and transporters that their customers were moving to another fuel, thereby discouraging investment;

3) Unloading capacity at receiving power plants;

4) Lack of adequate investment in transmission line capacity;

5) Coal producers' ability to meet rapidly increasing demand;

6) Capacity of waterways to move coal;

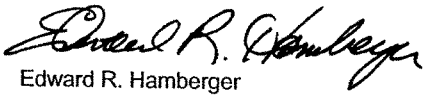
7) Impact of soaring natural gas prices on coal demand;

8) Impact of world markets on demand for coal in the U.S. For example, coal exports from China declined by 17% in 2005 from 2004, while its coal imports were up by 40%.

A final suggestion is that the participants in the workshop should be representatives of utilities, coal producers, barges, and railroads. Further, these representatives should be company employees at the highest possible level, who are actually involved in the day-to-day activities of mining, transporting, and burning America's coal. I believe this would help the workshop to focus on the facts and problem solving. In this manner, the workshop could be an opportunity for high-level strategic discussions to improve all aspects of the coal supply chain.

If you agree that the above suggestions are appropriate, I know that top management of the railroads would be willing to participate. Please advise me of your plans in this regard so we can respond appropriately.

Sincerely,



Edward R. Hamberger

Opening Statement for the Honorable Eddie Bernice Johnson
House Subcommittee on Railroads
"Hearing on the U.S. Rail Capacity Crunch"
Wednesday, April 26, 2006 – 2167 RHOB

Thank you Mr. Chairman.

I want to thank you and Ranking Member Brown for holding this important hearing on the issue of rail capacity.

As we all know, our nation's freight rail system is an integral component of our nation's robust economy.

Each day, freight rail delivers tons of raw materials and consumer goods that support an array of business sectors throughout the country.

According to a recent report by the Congressional Budget Office, rail transportation is responsible for the transport of: 70 percent of coal delivered to power plants; 70 percent of domestic manufactured automobiles; and 32 percent of grain shipments.

As manufacturing has become more global and as supply chains have become longer and more complex, freight rail has become a critical component for firms and industries.

In the Dallas-Fort Worth Region, exploding intermodal growth, coupled with increasing international trade with China is reshaping the region's economic and freight rail landscape.

In my district the evidence of this growth is unmistakable. Union Pacific has just completed a $100 million intermodal facility to support the growing intermodal volume and increased trade to the region.

I appreciate UP's decision to invest in my district, as the economic impact on the surrounding area is expected to create 20,000 new jobs and $5 billion of development over the next 15 years.

Cargo bound for the U.S. from China has grown an average 34 percent annually since 2002.

Much of this traffic filters through the Tower 55 Corridor in the North Texas region, as China is the world's leading seller of goods to the Dallas-Fort Worth market.

Delays at Tower 55 today exceed capacity. Significant future growth in freight rail is expected and addressing this problem remains a top priority.

On a busy day the Tower already sees in excess of 120 trains and on an average day it is occupied 70 percent of the time.

Obviously this type of demand is placing enormous strains on existing rail capacity in our region, and has highlighted the need for additional infrastructure.

And while I fully understand this need, I am also aware that unlike any other mode of transportation, railroads are responsible for paying for and maintaining their own infrastructure.

This type of arrangement obviously has implications on infrastructure investment.

As a result of this, I think it is imperative that we be proactive in formulating policy that supports, not prohibits, the industry in expanding capacity to avoid a congestion crisis that could endanger, or even cripple our nation's economy.

As I close, I want to thank our witnesses that have come before us to testify this morning—particularly Mr. Matt Rose of BNSF Railroad from Fort Worth Texas.

I look forward to their testimony, as I am particularly interested in learning more about their thoughts on how we may all work together in addressing current and future capacity challenges.

Thank you Mr. Chairman.

Testimony

Before the

House Committee on Transportation & Infrastructure

Subcommittee on Railroads

"U.S. Rail Capacity Crunch"

By Kendell Keith

President, National Grain and Feed Association

April 26, 2006

Chairman LaTourette and members of the subcommittee, thank you for the opportunity to appear before you today, I am Kendell Keith, President of the National Grain and Feed Association. The NGFA has a long history of involvement in transportation issues as they are a significant area of interest for our membership and a critical aspect to the success of the grain and feed industry.

The NGFA is comprised of 900 grain, feed, processing, exporting and other grain-related companies that operate about 6,000 facilities that handle more than 70 percent of all U.S. grains and oilseeds. The NGFA's membership encompasses all sectors of the industry, including country, terminal and export elevators; feed manufacturers; cash grain and feed merchants; end users of grain and grain products, including processors, flour millers, and livestock and poultry integrators; commodity futures brokers and commission merchants; and allied industries. The NGFA also consists of 35 affiliated state and regional grain and feed associations, as well as two international affiliated associations. The NGFA has strategic alliances with the Pet Food Institute and the Grain Elevator and Processing Society, and has a joint operating and services agreement with the North American Export Grain Association (NAEGA).

The agricultural transportation and marketing system has for many decades been one of the true strengths for U.S. agriculture and its ability to function efficiently in domestic markets and be highly competitive in global markets. For domestic markets, dependable and economical rail service has allowed livestock, processing and other users of raw agricultural products to be located in areas outside of major production areas and closer to concentrations of retail consumers. In export markets, a very efficient inland

waterways system, and network of rail lines throughout the U.S. has provided the U.S. farmer one of the most economically efficient pipelines to the global marketplace.

For a number of reasons, this U.S. transportation system is turning from a strength into a potential weakness. Because of higher fuel and energy costs, congestion on railroads and highways, a lack of investment in modernization and maintenance of the inland waterway system, the cost of moving agricultural products to markets is escalating sharply in the U.S. At the same time, some of our strongest competitors in South America and elsewhere are building infrastructure to make their transportation systems more efficient. Between 1980 – 2004 Class I miles have gone from 271,000 to 167,000, a reduction of 38 percent. At the same time carloads are up by 70 percent.

The transportation capacity crunch has affected every mode in the last few years. But while the capacity challenges for truck transportation have been growing steadily for several years, the rail capacity crunch has become most critical in the last 2-3 years.

Rail Industry Capacity

The robust economy, increasing volume of intermodal business of carriers, the hurricanes and other factors have created huge demands for rail service, thus testing the capacity of the U.S. rail system like never before. Further, the predictability of service has become a huge issue. Determining when rail equipment will arrive at origin for loading, when it will be furnished locomotive power to pull the train, and when it may reach destination have all become more uncertain. One shipper from a Midwestern state reports that it is common for 100-car shuttle trains (dedicated equipment for point to point service) to arrive, be loaded within the 15 hour requirement, only to have the train sit for 5 days to be picked up. These factors combine to make the real cost of freight to rail customers even more expensive, and undermines the efficient marketing of grains and oilseeds.

Throughout the 1980s and 1990s the agricultural industry often confronted seasonal capacity shortages of transportation services when harvest pressures forced high volumes of grain into markets. Our industry learned how to deal with such seasonal shortages, but the capacity crunch we face today is chronic, and apparently much more challenging to address. Railroads are losing market share in many agricultural and food-related markets because they have proven less reliable and less predictable in service levels.

In today's rail market shippers now have to supply 54 percent of all freight cars and 100 percent of all tank cars. Unfortunately, just adding cars to the existing rail system will not solve the capacity problem. In some cases, adding more engines and more crews could make the existing systems more fluid and improve cycle times. Some of the railroads are trying to hire more people, but low unemployment in the general economy makes it a difficult environment for hiring new personnel for jobs that require considerable time away from home.

But beyond new engines and more crews to run rail equipment, railroads need to build double track in some areas, build passing lanes, and make structural changes to some key

rail yards to make them more efficient. Those kinds of investments and construction projects will take years, and if overall rail business continues to expand at its present rate, rail capacity problems may get worse, possibly for several years, before service begins to improve.

Will Railroads Invest the Necessary Capital to Solve Capacity Issues For All Customers?

The tight supply of transportation freight has led to more pricing power by rail carriers and rail profitability is generally healthy. The AAR has announced that the Class I carriers will invest more than $8 billion in 2006 in track, cars, locomotives and other enhancements. While this investment is high by historical standards---it compares to an average investment of about $6 billion per year in the last decade---how much additional transport capacity does it really buy? As a sizable portion of the capital expenditures of railroads goes toward replacing equipment and repair work, the capacity impact of such investments are difficult to measure.

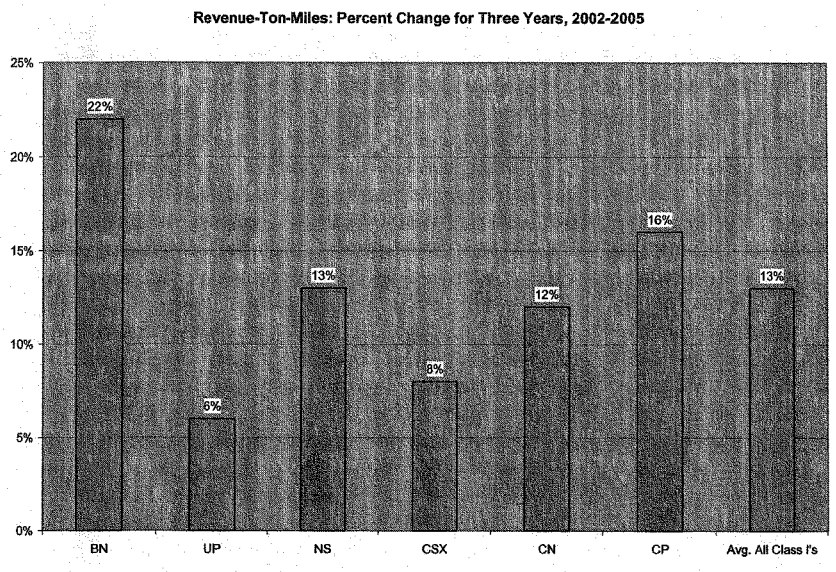
Railroad stock analyst Anthony Hatch has observed that the "old" investment model for railroads was disinvestments: eliminating redundant track, selling lines, reducing excess car supplies. But the "new" model for rail industry investment---during a capacity shortage---is "yet to be determined", and by no means a certainty that railroads will make the investments that rail customers would like to see for service improvements.

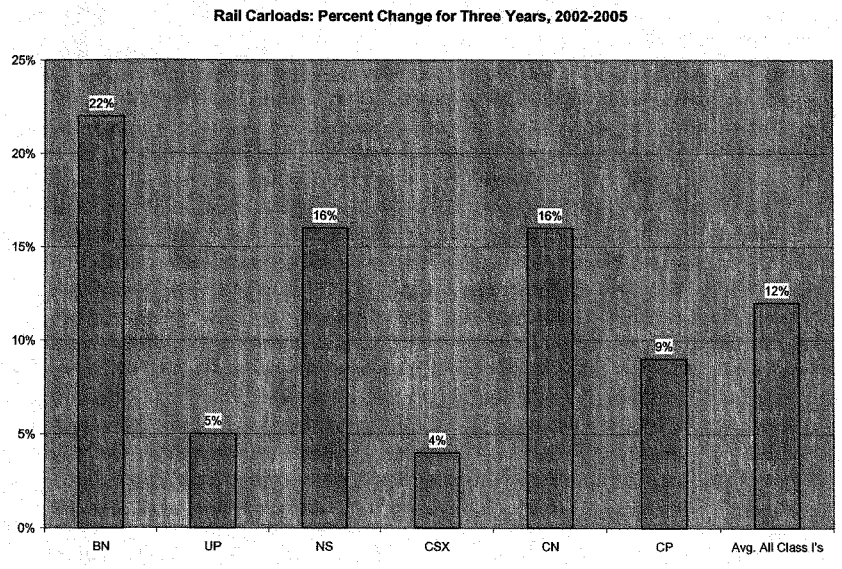
For railroads, in the past there has been a clear trade-off between expanded capacity to serve customers and Wall Street analysts assessment of stock prices. STB Vice Chairman Francis Mulvey has correctly noted that railroads have been "punished" in the past by Wall Street for making capital investments that were viewed as building new infrastructure that was "long-lived" while demand increases might be short-lived. Will Wall Street continue to play a constrictive role in railroad capital investments, or will that mindset change, given what appears to be a long-term secular rise in demand for rail freight? In our view the market fundamentals have shifted, offering much greater promise for continued growth in freight business, provided investments are made to meet demand.

How railroads have responded to heavy demand for services in the past 3 years?

In the last few years, the intermodal business of the carriers has grown quite rapidly, along with steady growth in coal and other industries. Intermodal business is projected to reach $8.8 billion in total rail revenues in 2006, a record pace that would give intermodal business the highest sector market share in the rail transportation sector.

Clearly, the railroads have had more business in the last few years that they could handle, as there have been many situations where the carriers have either refused new business or asked existing customers to accept a reduced level of service. How have the railroads responded to this expanded demand for rail service? The charts on the next page reflect gains by the carriers in "Revenue-Ton-Miles" and "Carloads" hauled over the last 3 years.


Revenue-Ton-Miles: Percent Change for Three Years, 2002-2005
25%
20%
15%
10%
5%
0%
22%
6%
13%
8%
12%
16%
13%
BN
UP
NS
CSX
CN
CP
Avg. All Class I's


Rail Carloads: Percent Change for Three Years, 2002-2005
25%
20%
15%
10%
5%
0%
22%
5%
16%
4%
16%
9%
12%
BN
UP
NS
CSX
CN
CP
Avg. All Class I's

These charts reflect that the ability of the carriers to respond to increase demand has varied across a wide range. Across the rail industry, revenue ton miles carried by the 6 major Class I carriers grew by 13% in 3 years, while carloads grew by 12%. The highest service growth has come from the BNSF that reports business volumes up 22% in the last 3 years. Other railroads that have met the industry average growth or better include the Norfolk Southern, Canadian National and Canadian Pacific. The Union Pacific and CSX reported the lowest business growth rates---substantially below the industry average.

What does this recent performance of railroads portend about future service levels? Certainly additional investments should enhance railroads' ability to respond to expanded demands for transportation, but the market and the rail customer need performance to improve quickly.

How will the agricultural and food industries fare in the competition for rail service?

As railroads ration their capacity to serve customers, there is concern among agricultural and food industry rail customers about how attractive our sectors are to the rail industry for service. How well do we compete for rail service with other sectors of the economy? While railroads continue to have a common carrier obligation under the law, the traditional meaning of that obligation---reasonable service on reasonable request---seems to be redefined each year as rail service capacity becomes more limited. The fastest growing segment of rail traffic is intermodal, and it receives by far the best rail service. Train speeds for intermodal traffic exceed train speeds on other railroad traffic by as much as 50%.

While many rail-served industries are receiving declining service from railroads, grain shippers are probably among the most affected because grain and grain products have not proven to be a high priority for service. Coal is getting a high priority today partly because of the temporary energy shortage. Intermodal freight is receiving priority treatment, because if railroads don't provide reasonably predictable service to that sector, they will lose the business, and it is a part of their business viewed as having significant growth potential.

Among grain shippers, shuttle train shippers (dedicated rail equipment cycling between shipping and receiving points) may continue to receive a higher priority because more grain can be moved efficiently with that class of rail service. But the problem is that not all grain and grain products can be moved by shuttle shipments because either the business volumes will not justify it or the shipping and receiving infrastructure is not sized to handle shuttles, and in many cases this "sizing" problem is not correctable even with new investments. Given the statutory common-carrier obligation for railroads, the NGFA has urged the carriers to continue to serve all types of agricultural shippers, providing reasonable service on reasonable request. In this regard, we believe it is important that the federal Surface Transportation Board provide more balanced regulatory oversight of the rail industry in the future by providing rail customers with balanced, transparent and cost-effective recourse to challenge unreasonable rail practices.

But even then, there will be some economic pain in a market that is short of capacity. Over a period of years, if the carriers invest in infrastructure, some of this capacity challenge can be resolved. But because of the growth in other types of rail business, some types of grain and grain product shippers may face a chronic struggle to obtain predictable rail service.

Solving Rail Capacity Issues

Infrastructure investments need to be made in the rail industry, and in our opinion, they need to be made sooner rather than later. Limited transportation capacity has the potential to constrain growth in the general economy, so improving transport capacity should be a national priority that deserves urgent attention. Are there other ways that railroads and their customers could work together to enhance rail performance and service? We think there are:

- The only way that some rail customers can receive service is by investing in privately owned or privately leased cars. However, railroads create additional risks and costs for private car owners through their policies and changes in policies, which cause disincentives for wise investment decisions. Railroads need to have fair and balanced policies so as to not distort market signals for investments by customers.
- The Canadian National Railway has reported success in improving train velocity and cycle times through a number of operational measures. One of these is a system of performance incentives and penalties for both the railroad and the customer. Wider adoption of more balanced incentive/penalty programs in the rail industry might provide greater incentives for both railroads and customers to meet expectations, which could enhance performance.
- Some railroad policies such as the ways some fuel surcharges are being applied, and the expansion of so-called accessorial charges, have become a major irritant for rail customers and very possibly a distraction in the effort to achieve the highest performance in rail operations. Accessorial charges have become so numerous that they are causing billing mistakes that rail customers have to spend enormous amounts of manpower to correct. The fuel surcharge issue has gotten to the point that the Surface Transportation Board will hold a hearing in early May. Some railroads' fuel surcharges are so extreme that they are earning more in such surcharge revenue than they are spending on fuel on the average shipment. More reasonable and fair policies implemented by railroads would eliminate some distractions toward achieving greater focus on solving the much more important issues of the day, such as overall rail capacity.

Conclusion

It certainly appears that the era of cheap fuel is behind us, and that only reaffirms the fact that the U.S. needs to get serious about modernizing and expanding U.S. transportation capacity. High volume, high fuel-efficiency modes such as inland waterway transportation and rail transportation should have an increasing advantage in a world of more expensive fuel, but both of these modes need new investment in infrastructure to

reap the rewards of new business that the marketplace will afford. Agriculture is highly dependent on transportation, because points of production and consumption often are separated by long distances. We need cost-effective, but also highly dependable and responsive transportation services to respond to customers' needs when they want to make purchases. We must be able to reliably supply domestic and international customers, livestock operations, grain processors and other users on the west and east coasts with grain and oilseed supplies from the Midwest. For too long, the United States probably has taken an efficient transportation system for granted. The difficulties we have confronted over the past year certainly affirm that now is the time to reassess our strategy for transportation investments going forward.

The NGFA appreciates this opportunity to share our views, and I would be pleased to respond to any questions you may have.

April 25, 2006
Congressman Daniel Lipinski
Committee on Transportation & Infrastructure
Subcommittee on Railroads
The US Rail Capacity Crunch

Good morning. Chairman LaTourette, Ranking Member Brown, and members of the Committee, I want to thank you for giving me the opportunity to testify today on an issue that is critical to the entire country, and is especially relevant to my district, the City of Chicago, and the State of Illinois. While the volume of freight rail traffic in the U.S. continues to increase, many of our rail systems are fairly antiquated and cannot handle the growing demand. Efficient rail transport is imperative to the economic prosperity of our nation. So it is critical that we find more ways to improve rail infrastructure and we support the railroad industry's efforts to improve the movement of goods across our country.

As you know, the Chicago area is a perpetual bottleneck for freight rail moving across the country. Regional chokepoints in our

national transportation system – such as this one – impede the efficient flow of commerce resulting in economic losses for businesses and consumers. And freight rail congestion also has a negative impact on passenger and commuter rail services.

With freight traffic expected to double by 2025, our rail infrastructure must be significantly improved or the problems will continue to mount, making congestion more difficult to alleviate and increasing the cost of fixing the situation. We must continue to provide federal support to programs and initiatives that innovatively address the capacity shortage.

One of these initiatives is currently beginning in the Chicago area, long known for its deleterious effect on our national rail system. While it takes a freight train about two days to get to Chicago from the West coast, it takes two more days just to get that train through Chicago. To address this growing congestion problem the Illinois Department of Transportation, the Chicago Department of

Transportation, Metra commuter rail, and the Association of American Railroads – including Burlington Northern Santa Fe, CSX, Norfolk Southern, Canadian National, Union Pacific, and Canadian Pacific, joined together to form a unique public/private partnership and developed a plan to ease the bottleneck.

The Chicago Regional Environmental and Transportation Efficiency project – known as CREATE – is a $1.5 billion, ten year plan that will make significant strides in reducing congestion by modernizing the antiquated northeastern Illinois rail network. CREATE will completely overhaul the system by focusing on twenty-five new grade separations, updating signalization and control technologies, and six rail-to-rail flyovers, which will separate freight and passenger lines, reroute congested tracks, and redirect right-of-ways making for a more efficient process. By fixing the Chicago bottleneck, this landmark proposal will result in national benefits and set a precedent for streamlining freight and passenger rail lines.

The CREATE program will also provide additional benefits. Traffic delays and grade crossing accidents in the Chicago area will be reduced. Air pollution from trains and vehicles on the road will be lowered, and the consumption of gasoline and diesel fuel will be decreased. And the infrastructure investments involved with the CREATE program will also generate tens of thousands of new, good-paying jobs.

The National Commission on Intermodal Transportation recognized the regional bottleneck problem and recommended that Congress provide federal funding incentives for intermodal projects of national and regional significance. The CREATE program is certainly one of these projects and was recognized as such by the Committee in last year's SAFETEA-LU bill. I thank the Committee and its leadership for providing the $100 million as we begin this critical program. Also, I would like to thank Mr. Ed

Hamberger and AAR for their continued commitment and support to CREATE throughout this past year.

Study after study after study shows that if we move freight in a more cost-efficient and time-efficient fashion, it means a more dynamic economy, more affordable consumer goods, and ultimately, a better quality of life for all Americans. I ask the committee to continue to provide support for CREATE and other critical rail projects that are essential to our nation.

Once again, the efforts and commitment of the railroads to improve the rail infrastructure in this country are to be applauded. It is my hope to continue to support and work on projects, like CREATE, that will alleviate the increasing congestion and make rail travel in this country – both freight and passenger – more efficient modes of transportation and economic engines for our nation.

I thank the Chairman and Ranking Member for my time today.

Statement of
Carl D. Martland
Senior Research Associate & Lecturer
Department of Civil & Environmental Engineering
Massachusetts Institute of Technology
Before the
Subcommittee on Railroads
Committee on Transportation and Infrastructure
U.S. House of Representatives
April 26, 2006

Chairman LaTourette and other members of the Subcommittee, it is my pleasure to present my thoughts concerning the extent and causes of and potential remedies for the "U.S. Railroad Capacity Crunch".

I have been active in rail systems research and consulting for 35 years, starting with my graduate research in 1971-72 on "Origin-to-Destination Unreliability in Rail Freight Transportation" and continuing through recent participation in rail system performance studies, including AASHTO's Rail Bottom Line Report. I have supervised numerous research projects concerning rail freight service, capacity, productivity, and safety. During the 1970s, most of my rail research was funded by the U.S. Department of Transportation. Since 1980, most of my rail research has been funded by individual railroads or the Association of American Railroads, except for several projects concerning train control and safety that were funded by the Federal Railroad Administration. My research and consulting has involved the development and application of various models of rail capacity and performance, and I have authored or co-authored more than 100 professional papers and reports on rail systems performance.

I would like to make several main points today:

- Rail freight transportation is an important component of the national transportation system. Rising energy costs, increased economic growth, and rising highway congestion will make rail even more important in the future.
- The capacity crunch is real, it results in degradation of rail service, and it threatens to limit the role of rail transportation.
- Poor service and capacity limits are important and legitimate concerns for the public, government agencies, and Congress.
- Potential benefits from expanded rail capacity include relief for highway congestion, improvement in environmental quality, enhanced ability to move military cargo, and a more robust national transportation system, along with the general economic benefits of having an efficient rail system.
- The rail industry is investing heavily in capacity, but individual railroads will concentrate their limited funds on what they perceive to be their most profitable market segments.

- Federal, state and local agencies are also investing in rail capacity, but their resources are limited under current programs. Additional funding mechanisms are needed to ensure sufficient capacity becomes available as needed.
- Public funding for rail freight systems research and planning have been severely curtailed over the last 25 years. Allocating a small portion of rail infrastructure investment for research and planning will enable federal, state and local agencies to work more effectively with the railroads in identifying the best strategies for increasing rail capacity.

My basic thesis is that today's rail system, while currently profitable and expanding, has suffered from decades of downsizing, declining rates, and competition from highly subsidized modes. With rising energy costs, increasing highway congestion, greater demand for inter-city passenger and commuter services, there is an opportunity and a need for moving toward a modern, high quality, high capacity rail system. However, we do not well understand what such a system should look like, nor do we understand how best to expand and transform the system. To move forward, we need not only financial resources, but also the human and intellectual resources for identifying, evaluating, and choosing among the options available for increasing the capacity and improving the performance of the nation's rail system.

Our goal should be to create what I call an "Interstate Rail System" with characteristics analogous to the Interstate Highway System. The system would have:

- High capacity, multi-track mainlines capable of handling more freight and passenger traffic with less delay and fewer accidents.
- Efficient, high capacity intermodal terminals situated in and around all major metropolitan areas to facilitate intercity and international transport of containerizable goods while helping to minimize truck-miles within urban areas.
- Efficient, high-capacity heavy haul systems for coal, grain, and other bulk commodities, with most of the network able to handle cars with gross weights up to the industry standard (currently286,000 pounds).
- Modern, efficient systems for handling general merchandise traffic, including well-maintained light-density lines as well as modern classification and local support yards.

An Interstate Rail System would provide several strategic advantages over the current system.

- Average freight train speeds would be doubled, from the current 20-25mph to 40-50 mph.
- The system would be able to handle substantial additional volumes of coal and grain without compromising the ability to handle general merchandise traffic.
- Reliable 6-8 day freight service would be available for essentially all carload freight moving within the lower 48 states and Canada.
- More industrial development opportunities would be available on lines that are well-maintained, safe, and served on a more frequent basis, whether by Class I or by short line railrioads.

- More capacity would be available to support the expected increase in demand for commuter and intercity passenger trains, as well as any unexpected surges in demand related to natural disasters or national security.

Now I will provide some discussion of the key elements of my thesis.

The Capacity Crunch is Real

The capacity crunch is real, it could go on for a long time, and it has serious consequences. Over the past 10 years, there have been many occasions where mergers, bad weather, or spikes in demand have triggered prolonged periods of congestion. All of the major US railroads have suffered from such episodes, and customers have frequently complained about long and unreliable transit times and equipment shortages. Accounts of these shortages have appeared regularly in the national press since 1996.

Poor Service

The main symptom of the capacity crunch is that transit times and reliability have deteriorated, particularly for general merchandise freight. I have conducted numerous studies of freight service reliability over the past 35 years. In studies completed in 1975 and in 1992, I characterized typical rail service as having average origin-to-destination transit time of about 7 days with variability of a day or two. In the last 10 years, I have seen many instances where average origin-to-destination trip times are 10-15 days with very high variability. I have seen recent performance data where the average trip time was in excess of 10 days for all shipments destined to various short lines. In other words, trip times appear to have increased by 25-50% or more for general merchandise traffic during the past 10 years.

Terminal time is the key input to trip time for general merchandise traffic. Service quality is related less to distance than to the number of yards where a car has to be switched from one train to another (just as the time and reliability of a journey by air depends greatly upon the number of airports you must pass through). In fact, general merchandise cars spend most of their time in yards, since it usually takes in excess of 12 hours for a car to make a connection from one train to another. In the 1970s, 1980s, and early 1990s, I found that benchmarks for terminal performance in North America were 16-20 hours for train connections. Since 1996, when the railroads began reporting average terminal time to the Surface Transportation Board on a regular basis, it has been far more common to see terminal times in excess of 30 hours than below 20.

Terminal times are less important for bulk and intermodal traffic, which typically are handled at only the origin and the destination and perhaps at an intermediate yard. Line speed, another statistic reported to the STB, is the key for this traffic. The average train speed is less than 25 mph, because trains experience lengthy delays related to meets and passes and to track maintenance, especially on single track lines. On well-maintained track, most freight trains could operate at 40 mph or faster without these delays.

Rising Rates

A second symptom of the capacity problem is that rates are rising for the first time since the early 1980s. Rates were up on the order of 10% in 2005, which is a major change from the prior 20 years. Immediately following deregulation, average rail freight rates rose, as railroads were no longer constrained to offer service at a loss at rates approved by the ICC. However, the dominant effect of deregulation was to enhance rail-rail and rail-truck competition, putting pressure on rates. Average revenue per ton-mile declined every year from 1983 through 2001, after rising or remaining essentially unchanged every year from 1966 to 1982[1]. In constant dollar terms, average revenue per ton-mile began to rise only in 2004. The reversal of a 20-year trend suggests a very significant change. In my opinion, the driving factors supporting higher rail rates are the shortage of capacity in the rail system coupled with rising rates for trucking during a time when demand is growing, most notably for coal and for containerized imports. Since service quality has declined, the higher rates certainly do not reflect faster or more reliable trip times! For the first time in a generation, the railroads are able to raise rates, so they do.

Increasing Length of Haul

A third symptom of the capacity problem is the increasing length of haul along with public statements by carrier officials that they are considering cutting back on general merchandise service. The average length of haul, which was 515 miles in 1970, 615 miles in 1980, and 725 miles in 2000, reached 901 miles in 2005. Railroads prefer longer hauls because they are more profitable and because rail clearly has a competitive advantage over trucks for longer hauls. However, the bulk of the freight flows in the country are well under 500 miles, and there are numerous examples of railroads handling shorter haul freight on a profitable basis. Public transportation agencies would like the railroads to handle more freight, not less, and they would like railroads to reduce their average length of haul by increasing their share of the shorter haul markets.

State and Local Interest in Rail

A fourth symptom of the capacity problem is the interest expressed by public agencies in expanding the role of rail. In the past five years I have been asked – because of my knowledge of rail freight – to participate in the following studies, all of which were motivated to some extent by a recognition that the rail system may be able to handle the traffic volume that is expected if the railroads simply maintain their share of the market:

- Freight Analysis Framework, Federal Highway Administration, 2000
- "Benefits of the Rail System to the City of Chicago" (sponsored by the City of Chicago), 2003
- "Sustainable Mobility", sponsored by the World Business Council, 2004 (a cooperative effort funded by oil companies and automobile manufacturers)
- AASHTO "Freight Rail Bottom Line Report", 2004

[1] Source: AAR, "RR Facts", various years

- "Rail Freight Solutions to Roadway Congestion", National Cooperative Highway Research Program, NCHRP 8-42, 2006

What is interesting about this list is that all of these studies were funded by agencies other than the FRA – because the FRA lacks the authority, staff or funds to conduct such studies. During this period I have participated in various policy discussions with FRA officials, including a meeting of rail experts with the administrator of the FRA and the head of the Surface Transportation Board, a workshop conducted by TRB for the GAO concerning the effects of deregulation on the rail industry, and a recent workshop conducted by TRB for the FRA concerning FRA's research priorities. These were all very interesting – but it was rather remarkable to me that the FRA does not have the in-house capability of addressing these issues at anything close to the depth that they deserve. It is ironic that the agency that might be expected to have the most interest in and knowledge concerning rail capacity has for so long had no authority or resources to study the problem. (At the recent workshop on rail research conducted by the Transportation Research Board on behalf of FRA, I and the other participants strongly emphasized the need for a research program that goes far beyond safety.)

Causes of the Capacity Problem

The most commonly heard explanation of the capacity problem is that the railroads were forced to downsize or to limit their investments because they were not earning their cost of capital and therefore could not attract private investment. This notion has some merit, but it is not the whole story. I would like to add some additional considerations:

1. Much of the rail industry was constructed in the 19th century, long before cars, trucks and planes offered effective competition for intercity traffic. The density of rail routes reflected the dominance of the railways for both passengers and freight. The system was laid out to serve the economic geography of that century – not to serve the population centers, the ports, the manufacturing and distribution centers, or the agricultural systems of the 21st century. Capacity problems in part reflect the fact that the system was not designed to do what we now would like it to do. And now the urban areas have grown up around, impinged upon, and otherwise restricted the options for operating or expanding the rail network.

2. The rail industry went through generations of down-sizing from the 1920s to the 1990s. Many senior rail managers learned railroading in an era when anticipating growth was seldom a priority. In times of declining traffic, it is not only possible, but desirable to operate "close to the edge", i.e. close to a capacity limit, as the problems will tend to diminish next year. Rail managers now need to re-learn how best to invest in anticipation of growth.

3. For many years, the effects of traffic growth were mitigated by productivity improvements. Even though ton-miles have increased steadily ever since 1982, the extra traffic was for many years easily handled in longer and heavier trains. Bulk traffic was shifted to heavier cars in unit trains, and a great deal of

merchandise traffic was shifted from boxcars to intermodal containers and trailers. It wasn't until 1996 that train-miles reached the levels of 1973 and 1974. – and that was when serious congestion problems began to emerge. Rising demand finally caught up with declining supply.

4. Deregulation, by enhancing intra- and inter-modal competition, further emphasized cost-cutting and network rationalization. Efforts aimed at improving trip times and reliability suffered in comparison with efforts aimed at reducing costs. Service benefits were viewed by rail managers as "soft" if not fictitious.

5. At the time of deregulation, the industry suffered from a glut of general merchandise equipment. With large numbers of cars stored serviceable, the marginal benefit from improved utilization and the marginal cost of poorer utilization were both close to zero. Equipment utilization, so great a concern in the 1970s, ceased to be a problem. Only recently have equipment shortages again made it necessary to consider the marginal costs of freight cars and the potential costs of rail congestion.

6. At the time of deregulation, the FRA was required to focus its research budget on safety. During the 1970s, the FRA, DOT, and the United States Railway Administration had supported many interdisciplinary research programs that went far beyond safety: the USRA studies that led to the creation of Conrail, the Freight Equipment Utilization Research/Demonstration Program, Labor/Management Task Forces, and the creation of the Transportation Test Center in Pueblo, which was useful not only for safety analysis but also for studying heavy axle loads. Many tools developed in these research programs are still used today. The rail officials who participated in these studies – and the students who did graduate research as part of these programs - fill important positions in the industry today. However, there is not a cadre of younger rail managers or consultants who have benefited from similar experiences.

7. Lower rates help attract more demand, which eventually exacerbates the capacity problems, especially if the rates do not reflect the costs of congestion.

8. Technology has in general been quite beneficial to the railroads, but capacity is only partially a problem of technology. Better track components, lighter materials for freight cars, more efficient locomotives, and better communications and control have allowed substantial reductions in rail costs, especially the costs for unit trains and intermodal trains. In 1970, there were very few lines that handled more than 20 million gross tons per year (MGT); today, there are many lines that handle in excess of 100 MGT. Higher traffic densities plus the increase in the load limit from 263,000 to 286,000 pounds provided a "free" boost in capacity on well-maintained lines. The capacity boost was free in the sense that the savings in equipment and crews offset the increases in track costs, at least on mainline tracks. However, technology has not had much of an impact on capacity, service, or equipment utilization for general merchandise freight. These are more difficult

system problems related to operations planning, management and control, and terminal operations.

Is The Capacity Crunch a Problem?

Capacity limits and service problems are certainly concerns for freight customers, but are they a concern for the public? Perhaps these problems will be handled adequately by market forces: prices will rise, increasing profits, attracting capital, and encouraging investment. If so, then perhaps no significant public response is needed.

However, we have now experienced a 10-year period beset by multiple periods of extreme congestion and poor service. Despite very impressive investments, the rail industry has barely managed to keep up with demand. It is possible that the rail industry will be able to maintain current rate levels only so long as a capacity shortage is maintained. If capacity were adequate, then the 20-plus years of post-Staggers experience suggest that rates would continue to decline. Hence, we could have a spurt of investment that would provide some capacity relief, followed by declining rates and lower investment, ultimately ending up with more grid-lock precipitated perhaps by extreme weather, a spike in demand, a merger or some other proximate cause.

It seems to be clear that there is a public interest in ensuring that there is sufficient rail capacity to handle more traffic, safely, with a better quality of service. From reading their rail plans, it is clear that many states would like to see more freight (and more passengers) handled by the railroads. A large number of short line railroads have received some sort of public assistance, whether in the form of tax relief, public ownership of the right-of-way, public assistance in rehabilitation or other measures. The short line industry has sought and received assistance from Congress for upgrading their systems to handle heavier axle loads. Studies and reports prepared for DOT, AASHTO and TRB extol the virtues of rail in terms of energy consumption, safety, logistics costs, and environmental quality. Various metropolitan areas have invested heavily in rail infrastructure. This committee, in its actions regarding the Railroad Rehabilitation and Improvement Financing (RRIF) Program, has promoted a greater public involvement in ensuring sufficient investment in rail capacity. Congress has many times previously provided the institutional and financial mechanisms to increase or maintain rail capacity.

However, it is not clear that the Class I railroads have the means or the incentive to carry out the investments that are likely to be needed. The major railroads have, for decades, improved their performance by focusing on their most profitable markets. Today, that means focusing on high-density bulk movements and long-haul intermodal services, while cutting back on general merchandise traffic. It is not at all clear that the Class I railroads will (or should, given their financial situation) invest so as to handle shorter-haul intermodal traffic or minor bulk movement; it is probably more likely than not that they will resist significant investments in yards and equipment that will be needed to handle substantially more general merchandise traffic.

What will happen if rail investment is insufficient to allow much growth in traffic? One outcome is that more traffic will have to move by truck, which will hinder rather than help efforts to relieve congestion and reduce consumption of fossil fuels. Another possibility is that it will become even more difficult to handle commuter trains, limiting the role of public transportation in some or many metropolitan areas. Another undesirable outcome is that economic growth could be limited, either in particular areas or in large parts of the country.

The capacity crunch is especially hard for short line and regional railroads. I am currently supervising a small research project sponsored by the short line industry. They are obtaining better information concerning trip times and reliability so that they can identify ways to improve the service they provide. They for the most part have plenty of track capacity and many locations for industrial development. Many of them are enjoying substantial growth in traffic, which is often related to economic growth in the region that they serve. For the most part, they handle general merchandise traffic as opposed to intermodal traffic or unit trains. They are often run by experienced railroad officials who have a strong marketing background and a demonstrated ability to innovate and adapt as a way to attract new business. In short, they are doing precisely what is desired by the public and by public agencies. However, they interchange their traffic with the Class I railroads, so they are greatly affected by capacity and service problems.

In summary, the big question is whether or not the industry will invest so as to be able to handle – with good, efficient, safe service – what the public would view as their proper share. Will investments in the rail system reflect just the profitability of the railroads – or will investments also reflect the public benefits in terms of economic development, energy use, safety and congestion? Can public transport agencies and private sector railroads work together to understand and overcome the capacity crunch?

Prior Research Programs

There are strong precedents for public funding for railroads and for public participation in rail research and planning. During the 1970s, a great deal of research was sponsored by the federal government to help the rail industry remain profitable and competitive. Much of the research was related to the Northeast rail crisis, the formation of the United States Railway Association, the creation of Conrail, and deregulation. To some extent the current capacity problems are the reverse of the problems dealt with at that time. Then, the industry suffered because the route structure and the institutional structure were both inadequate for the competitive needs of the industry. The industry needed to be rationalized and revitalized, and it was essential to simplify the corporate structure of the industry and to achieve much productivity gains. The problems were great, but the opportunities were clear, and efforts initiated in the 1970s, including but not limited to deregulation, led to tremendous gains in productivity during the 1980s and 1990s.

Today the problem is too little rather than too much capacity, and the question is not whether the industry can survive but whether it can grow fast enough to play an expanded role in the transportation system. Nevertheless, today's problems – and the potential

solutions - do bear some resemblance to those of the 1970s. First of all, much of the problem is financial: fix the finances and the industry can invest and expand. Second, the problem is a systems problem: solutions will involve railroads, their customers, and governments at all levels; technologies related to track, facilities, equipment, and control will all be relevant; labor and management issues will be important. In many ways, investing to add capacity is not necessarily any different than investing to consolidate capacity. Preserving rail service in the northeast required a large investment in Conrail, an investment that was very successful in large part because of the resources and efforts that went into planning and analysis.

As a researcher, I would like to highlight one very successful initiative that brought all the parties together to seek improvements in rail performance, namely the Freight Car Utilization Research/Demonstration Program (FCUP). This program was initiated in 1974 by the Association of American Railroads (AAR), in cooperation with the Federal Railroad Administration in response to public concerns about freight car shortages.[2] I will go into some detail on this program because I believe that it could be a model for a similar long-term approach to improving rail performance and capacity.

An industry task force prepared a plan for the program. The task force was chaired by Dr. W.J. Harris, head of the R&T Department of the AAR, and it included officials of four railroads (with responsibilities in operations, transportation, customer service, and transportation planning), a representative from FRA, and three additional AAR officials (representing the office of the president, R&T, and management systems.) The program formally began on April 1, 1975. The program had a steering committee that was chaired by Dr. Harris of the AAR, three senior mangers from the AAR, 11 senior officials from the Class I railroads, and Howard Croft, the president of the American Short Line Railroad Association. The program was structured as a 3-phase, 8-year program with funding at a level of $1-$2 million per year, about half of which was funded by the FRA. There were 6 task forces in Phase I, each dealing with one of the topics identified in the initial report:

1. Analysis of current practices and problems
2. The development of car utilization measurement standards
3. The development of additional data on car cycles
4. Development of recommendations regarding present and proposed FRA programs on car utilization (such as freight car scheduling)
5. Studies of AAR and ICC car service rules, orders and directives
6. Freight car time reliability studies

The initial ideas for Phase II were as follows:

1. A study of the demand fluctuation for freight cars.
2. The bad-order or unserviceable car problem
3. Customer practices study
4. Car distribution practices

[2] "A Proposed AAR Car Utilization Research Program", Notice to the AAR Board, March 15, 1974

5. The assigned car problem

For Phase III, the initial ideas were as follows:

1. Improved education in regard to car distribution practice
2. Equipment design
3. Work rules
4. Railroad policy questions (including a broader consideration of all factors affecting railroad capacity)
5. Public policy questions (including demand-responsive pricing and other techniques for reducing peak demands that were not allowed by the regulations in effect at that time)

The FCUP was implemented and continued for eight years, with studies for Phases II and III adjusted by the Steering Committee. At the completion of FRA funding, the program was continued internally within the AAR as the "Freight Equipment Management Program". The FCUP produced a large number of reports and resulted in many strategies that were implemented to improve equipment management. Among the most notable features of this program were the following:

- Industry involvement: senior officials from all the major and many of the smaller railroads served on the Steering Committee or the Task Forces.
- Customer involvement: one of the assistant directors of the program was an employee of a major rail customer, and customer officials also participated in some of the task forces and in various case studies.
- Government involvement: the FRA provided significant funding for the program, FRA officials participated in the Steering Committee and the task forces.
- Academic involvement: the program supported research at universities, which enabled students and faculty to work on rail industry problems (many students who worked on FCUP projects went on to successful careers in the rail industry)
- Critical mass: the program was funded at a level that enabled the creation of a permanent staff (generally 2-3 people) at AAR headquarters; it was supported by the industry to an extent that several dozen rail officials had a continuing, active interest in designing and monitoring the research program.
- Long-term funding: the program was planned as a continuing research endeavor, and in fact continued for more than a decade.
- AAR Administration: the program was administered through the AAR, which was responsible for reporting progress to FRA and for coordinating funding and manpower contributions from many different companies.
- Practical applications: the close linkages between the researchers and the task forces ensured that the research was designed, conducted and disseminated in a way that allowed practical applications.
- Breadth: "car utilization" was interpreted very broadly, and the intent from the outset was to consider many different ways to improve performance, including engineering, car management, transportation, operating, marketing, and regulatory

issues along with traditional concerns with empty car distribution and car hire/car service rules.

The FCUP probably would not have been possible without several key characteristics of the period. First, the crisis in car supply threatened to lead to government intervention in car management, which the railroads all wanted to avoid; a research program therefore was at worst a way to defer government intervention. Second, following the collapse of the Penn Central, it was clear to everyone that the rail industry needed major restructuring. It was a good time to be seeking new ways of doing business. Third, funding was available from the FRA, which made it much easier for the rail industry to initiate the activity. Fourth, the industry at that time had 52 Class I railroads, and the AAR and its committees were instrumental in developing policies and systems for managing the equipment fleet and other aspects of operations. It was natural for the AAR to play a lead role and it was possible to find capable people to serve on the various task forces. Fifth, the program was able to build upon prior research supported by the FRA and by the AAR, including work on equipment utilization, labor-management task forces that were trying to improve work rules, and work on freight service reliability.

What is Needed?

In summary, the big question is whether or not the industry will be willing and able to provide good, efficient, safe service for what the public would view as their proper share of the freight market. Will investments in the rail system reflect just the profitability of the railroads – or will they also reflect the public benefits in terms of economic development, energy use, safety and congestion, emergency preparedness, and national security?

Expanding capacity will need investment in facilities, equipment, and control systems. It will also require investments in people and in planning capabilities. To determine how best to allocate funds, it will be highly desirable to have a research and planning effort that is commensurate with the investments that are under consideration. I therefore recommend:

- Any program that provides significant funds for investment in rail should include a small component for planning and research. If billions are to be spent, then it is important to spend those billions effectively.
- Sufficient resources should be made available for policy analysis. Congress, transportation agencies, and the public need a better understanding of the potential role for rail for both freight and passenger transportation under various scenarios regarding energy, the labor force, and technological development. Research and planning efforts could lead to a better understanding of the potential for an "Interstate Rail System".
- The FRA should support research/demonstration programs involving the Class I railroads, short line and regional railroads, customers, and public agencies. These programs could incorporate many of the features that led to the success of the Freight Car Utilization Program.

TESTIMONY OF

WILLIAM W. MILLAR, PRESIDENT

AMERICAN PUBLIC TRANSPORTATION ASSOCIATION

BEFORE THE

SUBCOMMITTEE ON RAILROADS

OF THE

HOUSE COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

ON

THE U.S. RAIL CAPACITY SHORTAGE

****

April 26, 2006

SUBMITTED BY

American Public Transportation Association
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APTA is a nonprofit international association of more than 1,600 public and private member organizations including transit systems and commuter rail operators; planning, design, construction and finance firms; product and service providers; academic institutions; transit associations and state departments of transportation. APTA members serve the public interest by providing safe, efficient and economical transit services and products. More than ninety percent of persons using public transportation in the United States and Canada are served by APTA members.

Introduction: Grow Rail to Grow America

Chairman LaTourette, Ranking Member Brown, and members of the House Railroads Subcommittee, on behalf of the American Public Transportation Association (APTA), we thank you for this opportunity to appear before you today to discuss the U.S. Rail Capacity Crunch. We very much appreciate that the Subcommittee is taking a comprehensive view, considering both passenger and freight issues. While goods movement is critical, the emergence of America's service economy has heightened the importance of on-time movement of people as well.

America long has enjoyed the most extensive and efficient transportation system in the world. Today, other countries are catching up. Policies that support the growth of railroads – passenger and freight – are critical to America's mobility and our ability to compete in a global economy.

The critical capacity issues affecting railroads – passenger and freight – are a part of an overall crisis in transportation system capacity that also affects our airports, roadways, port facilities, and public transportation infrastructure. Such congestion is putting severe stress on America's transportation and logistics network, which historically has given America its economic edge.

Positioning for a Rail Renaissance

The past twenty-five years has been a period of significant change for the American railroad industry. While the Staggers Act of 1980 is rightfully credited with helping the once threatened railroad industry become profitable again, it has also led to significant consolidation and downsizing of America's railroad network. Rail freight traffic has grown in many places to the limits of capacity. What has been rational and profitable from a railroad shareholder viewpoint, has also resulted in a downscaling of America's overall rail network.

Meanwhile, over this same 25 year period commuter railroads have blossomed, and have also been a major success story. Last year, passengers took 423 million trips on our commuter railroads, a nationwide ridership increase of 2.8 percent from the year 2004. Ridership increases are being experienced by every commuter railroad in America. The Safe, Accountable, Flexible, Efficient Transportation Equity Act – A Legacy for Users (SAFETEA-LU), enacted in summer 2005, includes significant funding to expand rail systems and build new rail systems. This year, new commuter rail systems will open in Nashville and Albuquerque. New systems are in advanced stages of development in Minneapolis, Salt Lake City, Portland, Charlotte, Raleigh, and Denver. Other communities are not far behind, among them Phoenix, Ann Arbor, Austin, Atlanta, Harrisburg, Pittsburgh and Orlando. These projects will help reduce congestion and provide mobility options, integrate regional economies, and provide one of the quickest ways for individuals and families to beat the high cost of gasoline.

Looking to the future, railroads – passenger and freight - are poised to play an even greater role in enabling commerce and economic growth. Earlier this year America surpassed the 300 million mark in population. In 30 more years we are projected to reach 400 million. Most of the population will be living in metropolitan areas, making our use of land and transportation corridors all the more important. A look at the Los Angeles region's Metrolink commuter rail system provides a projection of demand anticipated for commuter rail services. Freight and passenger rail traffic in the L.A. / Orange County / Riverside corridor is expected to leap from 172 trains today to a total of 265 trains by 2010, and to a projected 390 trains per day in 2025.

While America needs a transportation policy balanced on the strengths and synergies of roads, ports and rails, overall there should be a higher reliance on rail modes, which are much more efficient in terms of land and energy. Indeed, adding rail capacity is imperative also for its positive impact on parallel freeways already clogged with traffic. These urban/suburban areas have roads that are not only hopelessly congested, but roads that have already been expanded to close to their maximum capacity. Adding highway capacity in these areas is enormously expensive. For a fraction of the cost of such road construction/expansion, existing railroad rights-of-way can be reactivated / expanded / improved to accommodate traffic and reduce highway congestion for both freight and passenger movements.

Tight Capacity Has Affected Commuter Railroads and Their Riders

Overcrowded trains, stations and park-and-ride lots, not to mention queues of trains waiting to pull into stations, are visible signs that existing rail infrastructure is being overburdened. Facilities that were designed for a certain level of service are now seeing passenger volumes that exceed these limits. In addition, as more trains are added to the same amount of track, scheduling and on-time performance becomes a greater challenge. Longer freight trains – as long as $2^1/_2$ miles – also make sidings hard to utilize, and makes on-time performance and shared operations more difficult.

Commuter railroads have sought to maximize throughput by lengthening trains and converting fleets to double-deck cars. Systems such as CalTrain's have also looked to creative scheduling to maximize the use of available capacity. Strategic scheduling of The Baby Bullet trains serving the San Francisco Bay Area have been a major success in this regard, increasing system ridership by over 20 percent and significantly increasing fare revenues.

Confronting system bottlenecks is another key. For example, during rush hour each day, several commuter trains per minute – carrying hundreds of thousands of passengers - pass through the Northeast Corridor tunnel linking New Jersey and New York. To accomplish such an operational feat each day is a minor miracle. Planning for future growth becomes another question.

On lines owned by freight railroads and shared with commuter lines, innovative ideas have been applied to enhance the compatibility of shared-track operations. A tighter scheduling of freight traffic, more compatible speeds, elevation of curves represent some of the operating practices that have been negotiated. In many places public funds have been used for capacity improvements in order to accommodate commuter rail operations. In Virginia, an agreement is in place providing for incremental increases in passenger train operating privileges as publicly financed capacity improvements are constructed to relieve bottlenecks. Other places have reported that funds invested in adding infrastructure capacity get eaten up by increased freight traffic.

It is possible that we can deal with rail freight bottlenecks at the same time we address the needs for high-speed rail. Proposed high-speed rail systems such as Midwest Regional Rail Initiative will benefit freight systems and will mitigate if not eliminate bottlenecks that occur in Chicago, Milwaukee, Cleveland, Toledo, St. Paul, and St. Louis. Conversely, inaction on the freight corridor capacity issue will prolong indefinitely the process of implementing new or improved corridor services. Examples include the lengthy discussion surrounding the initial commuter line proposed for Atlanta, the multi-year investments made in the Seattle-Portland route, and many other routes that are ripe for passenger service.

Strategic Importance of Rail Corridors in Built-up Urban Areas

Historically, America's rail corridors have been used for both freight and passenger purposes. Many corridors go back to the time when federal land-grants were awarded as incentives for railroad companies to build in developing sections of America. For a long period of time both passenger and freight services were operated by the private sector under laws governing public utilities. As passenger operations were abandoned by private railroads, services were often taken over and/or supported financially by public entities.

Today, over 90 percent of commuter rail trips are on lines that are publicly owned. This includes large, long-established systems such as New York's Long Island Rail Road and Metro North Rail Road, NJ Transit, the Southeastern Pennsylvania Transportation Authority, and the Massachusetts Bay Transportation Authority. Newer systems such as Florida's Tri-Rail, the Trinity Railway Express in Texas, and soon-to-open systems in Albuquerque and Salt Lake City have opted to acquire their own rights-of-way. Chicago's Metra system and the Metrolink system in Los Angeles own some of their lines, while using other lines owned by freight railroads. Systems including the Virginia Railway Express, Seattle's Sounder, the Altamont Commuter Express and Nashville's Music City Star system operate entirely on tracks owned by freight railroads.

The cost and availability of suitable real estate in built-up urban environments means that growth of rail passenger service will be highly dependent on access to existing rights-of-way. It will often make sense to use existing railroad right-of-way for new commuter rail projects. As a matter of community design and good public policy, this is preferable to dislocating homeowners and businesses in the acquisition of new right-way-way. Ironically, many transit agencies typically are able to exercise eminent domain to acquire the property they need, except with railroads. When it comes to railroad right-of-way, there is no requirement for any process for taking into consideration the public interest.

In 2001 several bi-partisan bills were introduced that would have created a federal process to protect the public interest and resolve disputes that arise when parties cannot agree on terms and conditions for the use of railroad right-of-way. Freight railroads would benefit from such a process. Simply put, when investments are made in freight corridors, such investments in track, signals and infrastructure benefit everyone, and also bring revenue to the railway owner.

The questions should be: 1) How can the freight railroad get a fair deal for the use of its property, and 2) How can we deliver to the public critical rail passenger projects without prolonged delay or consternation?

Passenger and Freight Railroads Should Grow Together!

How will commuter railroads be able to achieve the expected rate of growth? Certainly, it will require a partnership among communities, freight railroads and government partners. Collectively, we need to figure out ways to grow to the challenge.

The American economy depends on the efficient movement of people and goods. Rail freight systems operating at full capacity and providing maximum return to shareholders is good for some, but it is not where America's interest should stop. In Tennessee, Virginia and many other states, a lack of rail freight capacity has resulted in more truck traffic on the interstate highways causing congestion at near-crisis proportions. America needs new policies that will enable economic growth rather than hinder it.

Certainly, infrastructure investment is a critical factor. While APTA and stakeholder groups have celebrated SAFETEA-LU as a landmark in federal transportation policy, it remains true that in the United States about 2 percent of GNP is invested in transportation infrastructure, down from historical levels of about $2^1/_2$ percent.

Many of the ideas that have been put on the table have merit. The States for Passenger Rail organization has been adamant and consistent in its call for a dedicated fund for high-speed rail projects, to be supported through tax-exempt and tax-credit bonds, as is proposed by this Committee's Ride-21 legislation. APTA is supportive of this concept and concurs that such a fund needs to be separate and distinct from the federal Highway Trust Fund and Mass Transit Account. Continued funding and expansion of the Swift High Speed Rail Act is another important tool that can enable growth of high speed rail. The bottom line is that we need to create a favorable policy climate in which high speed rail systems can evolve and serve the mobility needs of Americans.

Freight railroads have promoted the concept of investment tax credits as a partial offset for amounts of private capital reinvested in private railroad infrastructure in instances where there is a public benefit. We believe that a key public benefit should be the accommodation of passenger trains. Difficulties in operating passenger service in a freight-owned right-of-way have caused some systems to acquire their own right-of-way. I contend, however, that the co-existence of freight and passenger rail services on common trackage / rights-of-way can and must be sustained to make fully effective use of these assets, and expanded federal investment in rail must be structured in a way that ensures reasonable access at a fair price. Some rail passenger systems are developing innovative ways to calculate the "public benefit" derived from freight railroads cooperation in rail passenger services, and what the freight railroad partner should be entitled to as a result. Perhaps this is something to build on! Passenger and freight railroads should grow together!

Certain rail bottlenecks in the national railroad system may require a national level effort. The CREATE and Alameda Corridor projects are examples. Consistent with earlier discussion, an additional Trans-Hudson rail tunnel would be another example of a project with critical national overtones. The Projects of National Significance program in SAFETEA-LU needs to become a place where multi-modal railroad megaprojects judged to have the most national merit can look to for appropriate funding. For this program to be effective, the timing of the review process must be in step with the strategic dealings of the project itself.

Other programs offer possible assistance for addressing capacity issues. The Railroad Rehabilitation and Improvement Financing (RRIF) program is a potential source of important capital funding for both freight and passenger rail projects. Only a limited number of loans have been released under this program since it was constituted in TEA 21, and APTA urges that any remaining administrative obstacles be cleared in order to put this innovative program to use.

Certainly, technology can offer solutions as well. APTA appreciates the ability of positive train control and similar technologies and its potential for enhancing safety while enabling railroad to operate at a higher level of service.

An overarching issue will be to get projects done sooner. Projects that sit on the drawing board an inordinate number of years do no good for the American economy. Project sponsors who have gotten bogged down in the federal funding process or in negotiations with freight railroads are beginning to consider whether the only way to get projects done in a reasonable timeframe is to forego these partnerships. The process should be better than that. A central theme of SAFETEA-LU was to expedite program delivery. China is one country where they cannot seem to build new rail capacity fast enough. Let's do the same in America!

In regard to high-speed rail, while America watches, industrialized countries, and some not so advanced countries, are rapidly seizing on high-speed rail systems to complement their trans and intercontinental airlines and to interconnect and support their metro area transit systems. This includes the new 7,000 – 12,000 mile high-speed rail system now under construction in China. It is a plan to connect all provinces and the 30 largest cities in a national grid system that will share corridors with freight operations but have dedicated tracks for high-speed rail in dense corridors. Annual investment in Chinese high-speed passenger rail construction will be $16 to $20 billion. New signaling technology and centralized traffic control will also improve Chinese railroad capacity. High-speed rail is also making advances in Japan, France, Germany, Sweden, Italy, Spain, South Korea and Taiwan and is being adopted in Mexico and other emerging economies. On the business side, non-American firms are the primary beneficiaries of this expansion in high-speed rail capacity. German, Japanese, French and Canadian railway equipment and signaling technology suppliers are seizing on new business opportunities, while the U.S. continues to fall behind in what could be described as "The Great Railroad Building Race."

As Congress and the Administration pursue the policy goal of energy independence, our transportation policy in many ways favors our petroleum-dependent modes and not our energy efficient systems. In contrast, Europe and Japan have used high-speed rail systems to replace short-hop airlines and a significant amount of inter-city auto travel in those areas. Short-hop airlines are more petroleum intensive and polluting than a person driving an SUV, on a seat-mile basis.

Finally, a key determinant in the growth of commuter and high speed rail relates to liability insurance requirements and conditions. Acts of terrorism against transit in Madrid in 2004 and in London in 2005 have raised the stakes on liability coverage. Some freight railroads are now requiring coverage of $500 million – at times as much as $700 million - a severe detriment for providing rail passenger service. One approach would be to build on the Amtrak Reform and Accountability Act of 1997, which caps passenger claims at $200 million. It would be an enormous boost to passenger rail operation if this cap could be clarified to apply to all claims.

Conclusion

In conclusion, America needs to grow its railroads. While some may see passenger and freight railroads as distinct and on different economic paths, I believe there are synergies that can be captured through policies that look at railroads in an inclusive way. We thank the Committee for advancing the dialogue on the future of our rail system with today's hearing.

With only a limited number of transportation corridors, strategies must include freight and passenger rail interests working together. With the completion of the interstate highway system, some have suggested that the national purpose of the federal surface transportation program has been lost. As America competes in the global economy, it is our transportation, logistics and education systems that will give us the advantage. Energy independence and emergency response are among other strategic national goals supported by an increased emphasis on rail.

Congressionally created commissions will soon begin looking at these issues in depth. I look forward to working with these commissions, as well as with this Subcommittee. It is our transportation network that can make the difference for America's position in the global economy.

STATEMENT OF
THE HONORABLE JAMES L. OBERSTAR
SUBCOMMITTEE ON RAILROADS
HEARING ON
"THE U.S. RAIL CAPACITY CRUNCH"
APRIL 26, 2006

- Mr. Chairman, I commend you and Ranking Member Brown for holding this important hearing.

- Twenty-six years ago, Congress voted to deregulate the nation's railroad industry and enacted the Staggers Act. The railroad industry at that time was in dire straits. Years of low profits, deferred maintenance, and ill-conceived regulatory policies had resulted in a very sick industry.

- We were assured that enactment of the Staggers Act was the cure. We were told that economic regulation had outlived its usefulness, and that it was preventing the industry from competing effectively with trucks, barges, and pipelines. We were told that railroad earnings were the lowest of any transportation mode and insufficient to generate funds for necessary capital improvements, and that failure to achieve increased earnings through structural reforms would result in either further deterioration of the rail system or the necessity for additional Federal subsidy.

- So we enacted the Staggers Act. It was a success for the railroads in terms of profits. Twenty-six years later, there is more demand for rail transportation than the railroads can keep up with and revenues are at record high levels. Industry rates of return that hovered in the 1-2 percent range in the 1970s are now up in the 8-9 percent range. Norfolk Southern's rate of return is at 11.6 percent, making them revenue adequate under the Surface Transportation Board's standard.

- While the Staggers Act resulted in a rebirth of the freight rail industry, it did have unintended consequences, which can best be summed up with one word: consolidation.

- Since 1980, 63 Class I railroads have consolidated into just <u>four</u> major Class I freight railroads serving the entire United States – two in the East and two in the West – which control over 95 percent of the railroad business. This unprecedented consolidation has resulted in entire States, regions, and industries becoming captive to a single Class I railroad.

- At the same time, the rail network was consolidated. The Staggers Act reforms as well as subsequent Interstate Commerce Commission policies and regulations

made it easier for the Class I railroads to shed unproductive lines. As a result, the rail network deteriorated from 252,845 route-miles to almost half of what it is today: 141,000 route-miles.

- Our current rail network cannot withstand current levels of traffic. Economic growth, booming international trade, and other factors have led in recent years to record rail traffic levels, which have created capacity constraints and service issues at many points and corridors on the rail network.

- Capacity and service issues will become even bigger issues as we move forward. According to the U.S. Department of Transportation's Freight Analysis Framework, rail traffic is expected to rise more than 50 percent, from 1.8 billion tons to 2.9 billion tons in 2020. Add that to the fact that current growth predictions indicate that container cargo at U.S. ports will quadruple in the next 20 years and you have a tremendous amount of pressure bearing down on our Nation's rail system, with no solution in sight.

- As rail traffic continues to grow, the railroads will have to concentrate increasingly on replacing and building new capacity, such as multi-tracking key corridor routes, adding new or extending sidings at key locations, constructing new intermodal or transloading facilities, and investing in new technologies.

- And the Federal Government will have to take responsibility for ensuring that all facets of our transportation system – whether it is our aviation system, our highways, waterways, or railways – are in working order. However, unlike the other modes of transportation, there is no dedicated stream of funding for rehabilitating, reconstructing, or expanding the U.S. rail network.

- Some legislative proposals to deal with congestion are circulating in Congress, from providing the railroads with a 25 percent infrastructure tax credit to creating a railroad trust fund, both of which I am reviewing.

- In the meantime, we can enact legislation now – H.R. 2047, the Railroad Competition Improvement and Reauthorization Act – to provide relief to the states, local communities, and captive rail customers who continue to suffer from unreasonably high rail rates and poor service. That relief cannot be accomplished alone through capital improvements. Some reforms to reduce impediments to competition will also need to be enacted.

- Thank you, Mr. Chairman. I look forward to hearing from the witnesses.

Testimony

Of

Matthew K. Rose
Chairman, President and CEO
Burlington Northern Santa Fe Corporation

April 26, 2006

Before the
U. S. House of Representatives
Transportation and Infrastructure Committee

Good morning. My name is Matthew Rose, and I am the Chairman, President and Chief Executive Officer of Burlington Northern Santa Fe Corporation. I am pleased to be here today. I want to thank the Committee for giving me this opportunity to testify about the state of freight rail transportation capacity, and what should be considered to ensure that the right amount of capacity is available when it is needed to meet shipper demand.

However, before I begin my testimony, I would like to briefly inform the Committee about my background. I joined the former Burlington Northern Railroad in 1993 and the following year was named Vice President, Vehicles and Machinery. After the 1995 merger of BN and the Atchison, Topeka and Santa Fe Railway, I was appointed Vice President, Chemicals and, in 1996, became Senior Vice President of the Merchandise Business Unit. In 1997, I became Chief Operations Officer responsible for coordinating transportation, maintenance, quality, purchasing, labor relations and information services. In 1999, I was appointed President and Chief Operating Officer and the next year, Chief Executive Officer. Prior to joining BN, I was Vice President, Operations for Triple Crown Services (a Norfolk Southern Subsidiary), where I had functional responsibility for all facets of the truck/rail operation.

I'd like to begin my testimony with a report from the rail industry's largest competitor, the highway. Using the well-documented forecast from the 2002 American Association of State Highway and Transportation Officials (AASHTO),

freight transportation demand is expected to more than double by 2025. Further, Global Insight forecasts Transpacific trade to triple by 2025, bringing the equivalent of 84 million TEU's (or 20-foot containers) annually into West Coast ports that today are handling about 14 million containers of that size.

Another way to look at the ASSHTO report is that domestic freight ton-mileage will grow at a little more than 2 percent compounded annually from yearend 2005 through 2020. This means the nation's truck network, according to AASHTO, will have 865 million trucks operating in 2020, or a 60-percent increase over last year. For the rail industry, AASHTO says this translates to 48 million rail cars, or a 55-percent increase in 2020 over today. These are staggering numbers.

The coal story is just as staggering. According to the Energy Information Administration, western coal is forecasted to grow at a 2.2 percent compound annual rate through 2025. This projection amounts to western coal production at 900 millions tons by then. In 2005, western coal production was about 450 million tons, and 415 million of those tons came from the Powder River Basin (PRB) located in Wyoming and Montana.

To put EIA's projection into perspective in terms of the importance of PRB coal to the electricity generation needs of the United States, 400 million tons of PRB coal is equivalent to 1.2 billion barrels of oil, or 50 percent of U.S. oil production. And it is equivalent to 7 trillion cubic feet of natural gas, or 35 percent of U.S. natural gas

production. The comparative efficiency of PRB coal is a key reason why PRB coal is so important to our economy – 400 million tons of PRB coal represents a $6 billion cost; its oil equivalent is a $78 billion cost at $65 a barrel, while the natural gas equivalent has a $56 billion cost at $8 per million btus.

The question that Committee needs to consider is: How are we going to handle these huge increases in freight demand, given the current transportation infrastructure and the current rate of capital investment by the private railroads and the federal government's tightening transportation budgets? It is clear, we have to change how we incent new infrastructure capacity.

The Congressional Budget Office released a study last January that supports a change. Their paper, "Freight Rail Transportation – Long-Term Issues," outlines the same capacity concerns that the rail industry has been trying to address the past couple of years. Here are some excerpts from the paper that identify the unique infrastructure situation facing the freight railroads that is not faced by the other principal, freight transportation modes.

Here are two citations from the first page of the CBO report:

> **"Some transportation experts have expressed concern that the railroads are not investing enough to meet rising demand for their services. If they cannot keep pace, the result could be higher costs not only to shippers and consumers but also for taxpayers, because demand that railroads cannot satisfy is most likely handled by trucks and thus require more spending on the construction and maintenance of highways." (Page 1)**

> "Building new track is costly, and because track is fixed in a specific location, investing in it subjects railroads to the risk that demand will shift to other locations and that the investment will not yield an adequate return. The other major domestic freight transportation industries, trucking and water carriers, do not face that kind of risk; instead, the governments that build and maintain highways and waterways – and the taxpayers who provide their funding –bear that risk" (Page 1)

Finally, from Page 17 of the paper:

> "Current user-tax policies appear to tilt the playing field in favor of trucking and water carrier industries ...In contrast, the railroads pay for their rights-of-way and infrastructure and often must pay local taxes on those investments as well. Those factors translate into lower private costs for truckers and water carriers an enable them to attract some freight shipments that could be carried at a lower total cost by the railroads. That encourages greater spending on highway and waterway construction than would be justified on economic grounds and leads to an inefficient use of the economy's resources,"

Last October, when the Surface Transportation Board held a public hearing here in Washington to celebrate the 25th anniversary since Congress passed the Staggers Act, rail shippers and their trade organizations have also voiced their concerns

about rail capacity and what could be done to encourage more investment in the transportation infrastructure.

This is an excerpt from The National Industrial Transportation League (NITL), which considers itself the "Voice of the Shipper" with thousands of members:

> **"...the country does <u>not</u> need railroad capacity to grow at the same pace as the growth of the economy or transportation generally; it needs to grow faster. For reasons of energy independence and environmental concerns, and because it will be even <u>more</u> difficult to expand the nation's road system easily in the face of increasing opposition to new roads through densely-settled existing communities, the railroad's share of intercity freight has to <u>grow</u>."**

And from UPS,

"UPS recognizes the capital intensive nature of the rail industry and has witnessed the equity markets' punishment of railroads that aggressively invest in their infrastructure. The railroad cost of capital dynamics are indeed challenging. While perhaps outside the purview of the Surface Transportation Board, public policy initiatives addressing infrastructure improvements, adding capacity, improving rail service, and enhancing technology should be promoted."

And the U. S. Department of Agriculture said:

"Looking forward, we must consider what can be done to encourage adequate investment in transportation infrastructure by both the railroads and private investors."

And another from NITL on the economic growth engine of the railroad industry, intermodal:

"The growth of intermodal has had profound effects on the railroad system. The traffic tends to be higher speed and higher priority compared, for example, to unit train coal or merchandise traffic, and therefore 'takes up' significant 'space' on the railroads' network. A significant part of this traffic comes from the West Coast in the form of containers imported from the Far East, a fact that has caused congestion on certain lines, and a significant need to upgrade both West Coast receiving facilities and the intercontinental network from the West."

Finally, almost five years ago on May 9, 2001, I had the honor of testifying before the Senate Committee on Commerce, Science and Transportation's Subcommittee on Surface Transportation and Merchant Marine. The three major points of my testimony then were:

- **Massive amounts of capital are needed to accommodate future growth.**

- **Railroads are disadvantaged v. other modes of transportation.**
- **Our nation is not achieving maximum economic, social and environmental benefits from its freight rail network, or its surface transportation system.**

The rest of my testimony today will focus on freight rail in general and BNSF Railway in particular. I'll comment on what the intended purpose of the Staggers Act was back in 1980; how it has contributed to the rebirth of the freight railroads; and what is needed to ensure that this economic revitalization continues so that the shipping community prospers and can count on having the freight rail capacity at the right time in the future to meet their forecasted demands.

I'll also talk about the Powder River Basin, as an example, of a prudent approach to capital investment; what we intend to do going forward; and the kind of assistance we would like to get from Congress to continue to expand the infrastructure in this coal region as well as across other parts of our network to support forecasted demand for freight rail.

First, the Staggers Rail Act of 1980: It reduced the amount of economic regulation on the railroad industry. It provided for a delicate balancing act that would enable achievement of revenue adequacy by the railroads to make infrastructure investments and remain competitive with other surface transportation modes.

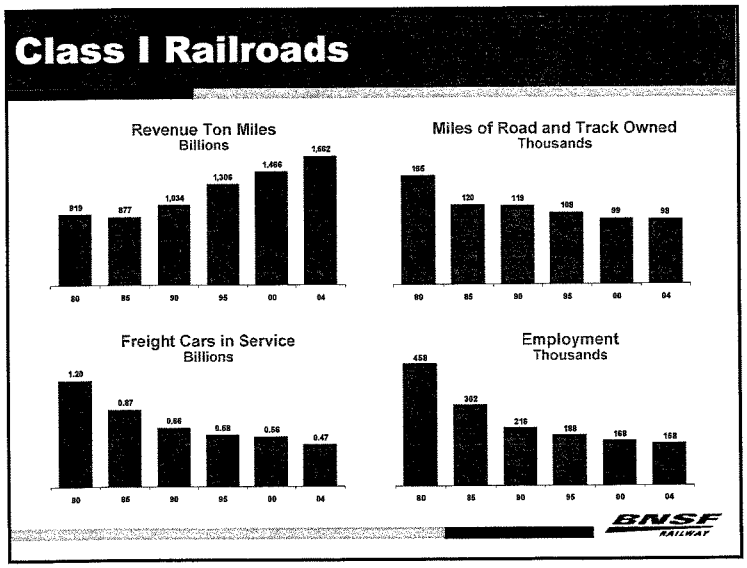
Today, the rail industry generally has a good news story to tell, some 25 years after the enactment of Staggers. BNSF, and other Class 1 railroads, are making progress toward revenue adequacy. BNSF is making such progress while it continues to handle annual volume increases, about double its normal growth rate in previous "good" economic times. This continuing volume growth and the future demand can only be met by reinvesting adequately – both to maintain the quality of infrastructure and to expand BNSF's capacity to handle more freight at the right time. This can only be done if we can reach a level of return on invested capital (ROIC) that is greater than our cost of capital, and then continue to improve our ROIC and maintain returns throughout the business cycle.

One factor that stands in the way is the fundamental "under-valuing" of freight rail. The prices BNSF charges for transportation services fell more than 50 percent, adjusted for inflation between 1980 and 2003. Only since the second half of 2003, have the railroads been able to begin receiving more value for the services provided. And in these past few years, all transportation modes have also been faced with soaring fuel prices.

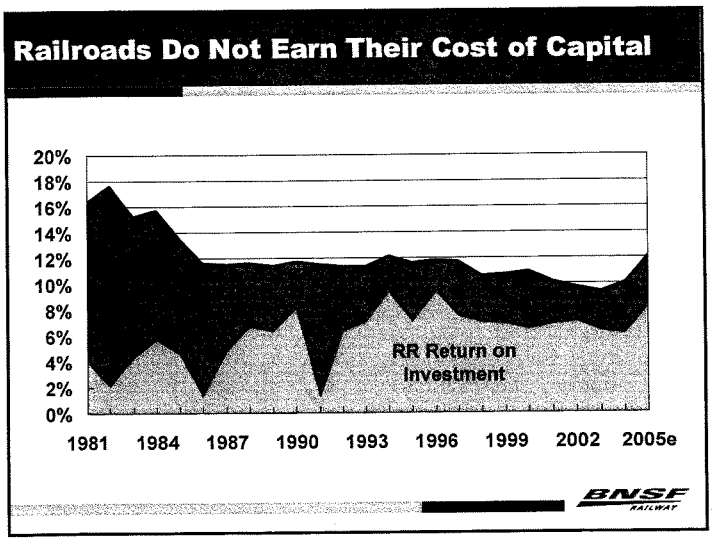
Here's quick review of how successful the Class I railroads have been as a result of the Staggers Act.

Between 1980 and 2000, the railroad industry had excess capacity. Over the last five years, GTMs or gross ton miles, have loaded up the railroads putting stress on our

infrastructures. The following charts show, as an industry, our revenue ton miles increased more than 80 percent from 1980 to 2004, while miles of track owned, freight cars in service and employment, all fell dramatically due to efficiency initiatives.

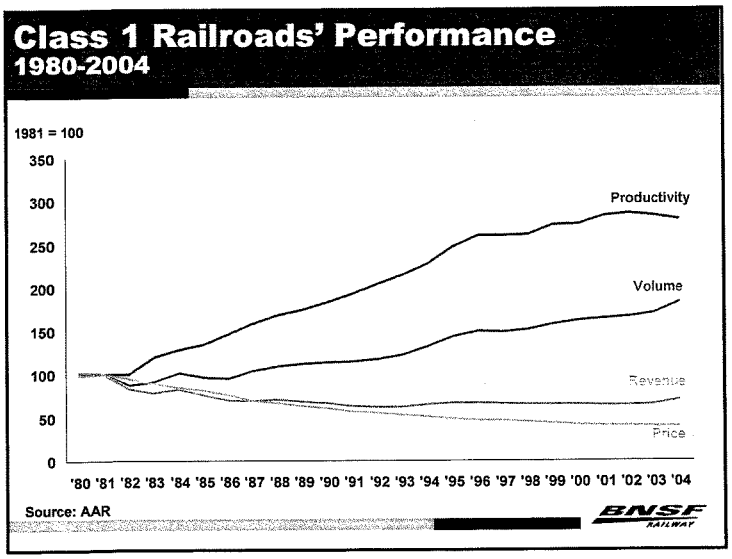


Even though BNSF has seen a definite improvement recently in its return on invested capital, Class I railroads still do not earn their cost of capital.

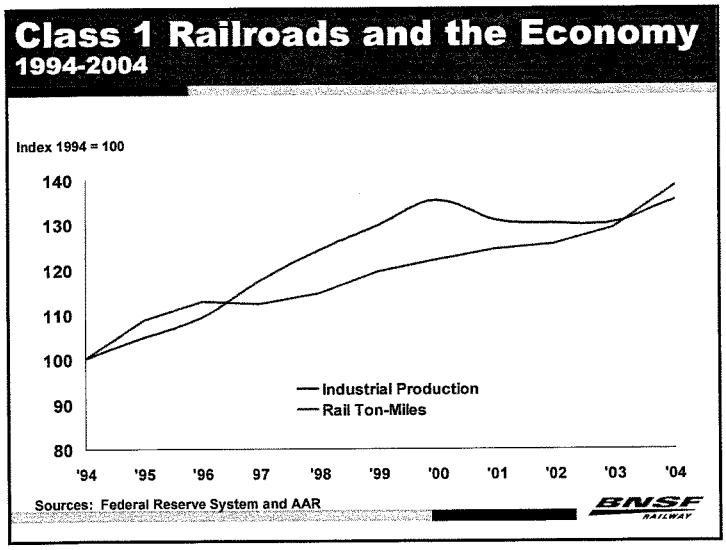


The next chart summarizes how far the rail industry has come since 1980. The passage of the Staggers Act has led to dramatic increases in railroad productivity (a 4.4 percent compound annual growth rate), which has up to now enabled the Class Is to handle sharply higher volumes (a 2.5 percent compound annual growth rate) while reducing prices (a negative 3.7 percent compound annual growth rate) as these railroads worked off its excess capacity. Today, BNSF is poised to shoulder an increased share of the transportation demand as along as it can consistently realize returns that justify new investments. And if America wants to be able to count on the rail industry even more, we must continue to embrace policies introduced with the Staggers Act that give railroads the freedom to operate in the marketplace

without artificial constraints. Bringing back the heavier hand of regulation, whether the under the guise of more competition or simply to cut back the railroad industry's ability to earn returns, would be counter productive and threatened that climate for infrastructure investment.

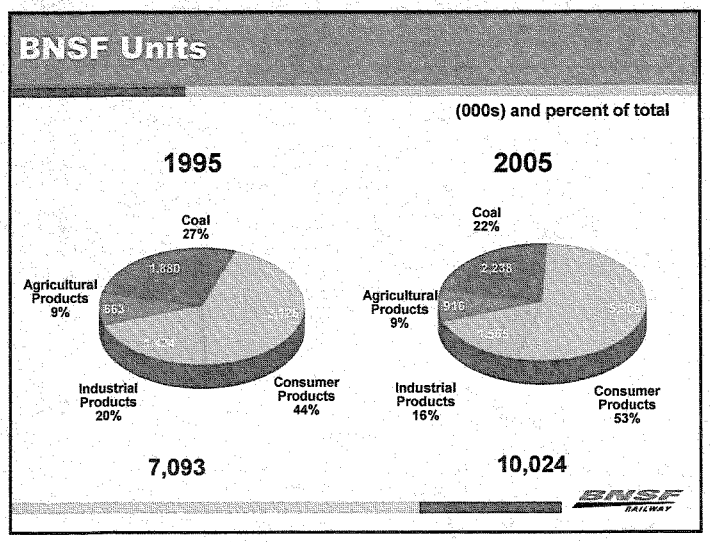


This chart shows that traditionally rail ton-miles tracked U.S. industrial production. In 2003, for the first time since 1996, rail ton-miles surpassed industrial production demonstrating the effect of the U.S. economy's shift from production to consumption.

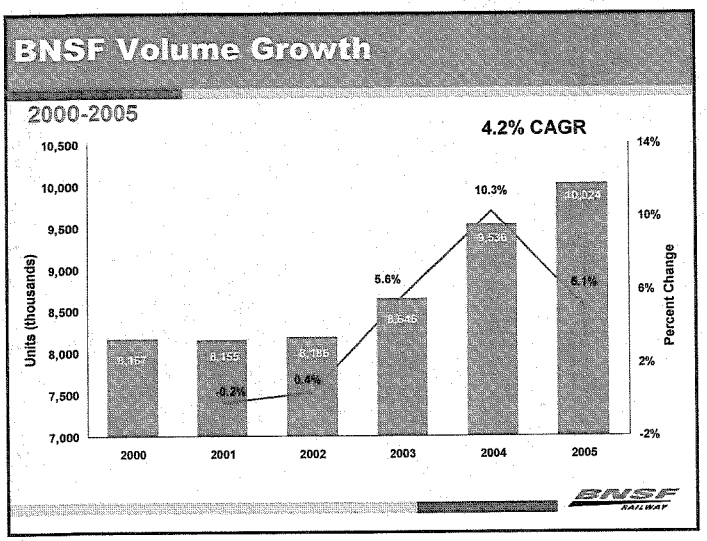


The rail industry is now entering a new era in terms of growth, driven by several major factors such as transpacific trade and coal demand, but also because truck driver shortages, fuel prices, highway congestion, agricultural trade growth and environmental considerations.

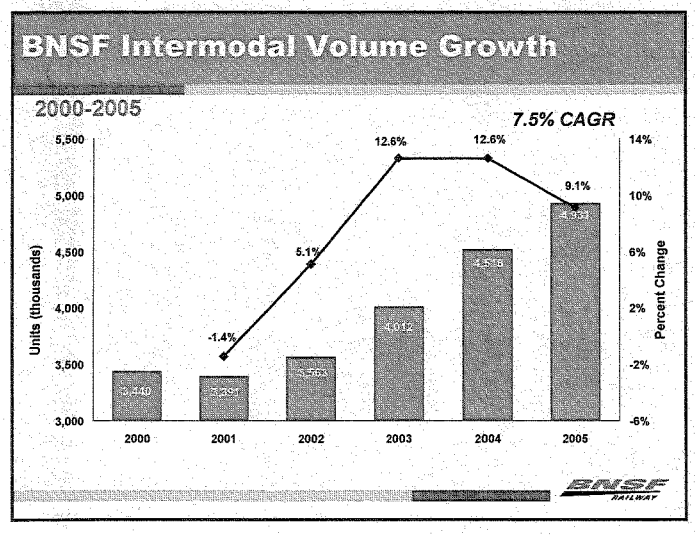
Let's look at BNSF since 1995, the year when the merger of Burlington Northern and Santa Fe Pacific became effective. These charts illustrate how dramatic the growth trends have been in the past few years. BNSF grew from a little more than 7 million units -- cars, containers and trailers -- in 1995 to a little more than 10 million units in 2005. In 2005, BNSF handled an additional 500,000 units or 50 percent of the U.S. railroad industry volume growth. All business groups – Coal, Agricultural Products, Industrial Products and Consumer Products – experience volume growth during this 11-year period, but the largest growth area was in Consumer Products, which primarily consists of intermodal traffic.



Focusing on the 2000 to 2005 time period, here's a view of BNSF's rate of volume growth each year, or 4.2 percent compounded annually over that period. BNSF has been able to achieve this rate of growth largely because of our efficiency and, to some degree, from its capital investments.

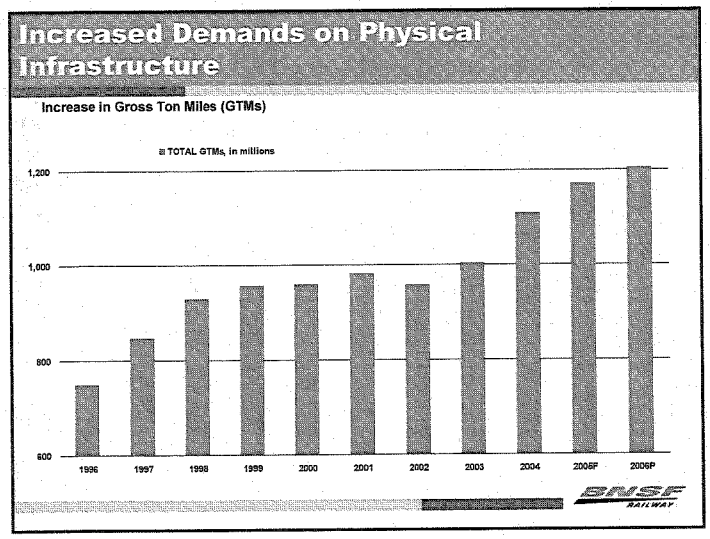


This chart illustrates the huge growth in BNSF's intermodal traffic since 2000, reflecting both the benefits from Transpacific trade as West Coast ports handle more container traffic and from the domestic trucking industry using rail for their long haul movements.



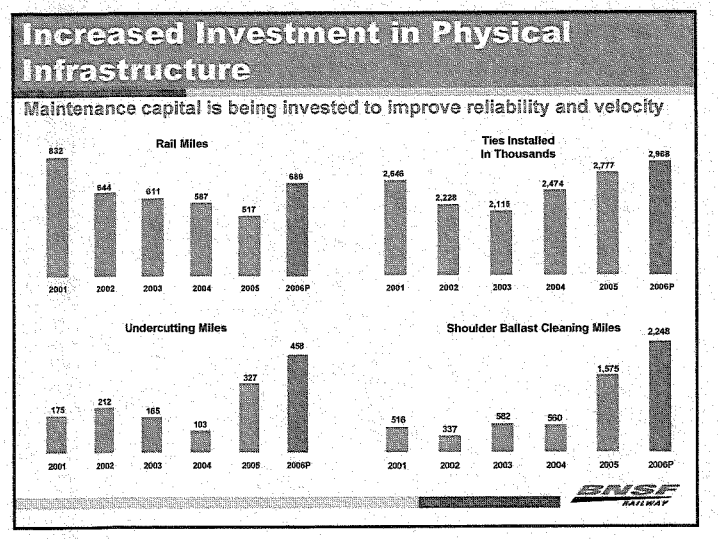
There is a lot more demand than capacity and BNSF needs to become more efficient and create more capacity. However, BNSF must also continue to invest more capital, both in the existing infrastructure to keep it strong and not constantly under undue stress, as well as to expand capacity. Expansion capital is needed to improve throughput at existing yards and intermodal hubs, and for adding more double and triple track, even fourth main lines, on core routes; building new Logistics Parks and adding locomotives and acquiring more rolling stock.

BNSF can handle the projected growth if network capacity can be expanded in the right ways at the right time. This chart shows what BNSF has been able to handle in terms of gross ton miles (GTMs) since 1996, nearly a 65-percent increase in this 10-year period. To keep growing, it's critical to have GTMs load up the railroad, but we must have a strong physical infrastructure.

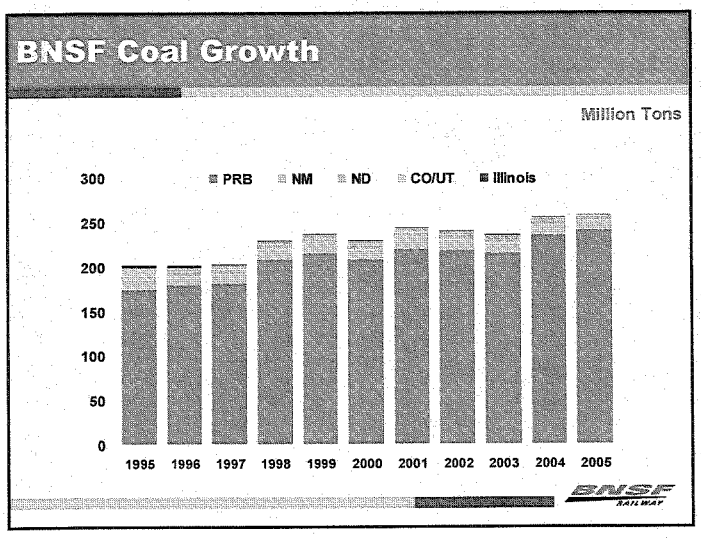


Here are the levels of investing BNSF has been making in its physical infrastructure since 2001 in terms of rail, ties, undercutting along the right of way, and ballast. BNSF is planning for another strong increase in 2006.

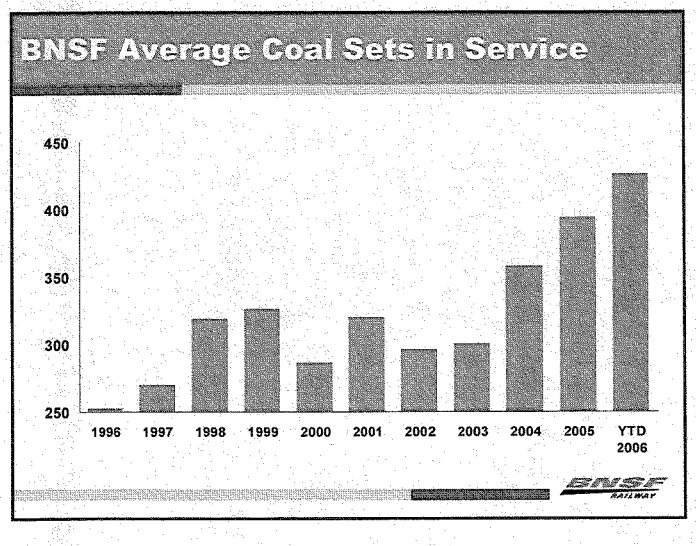
Overall, BNSF has had 30-percent increase in miles of rail laid, which has not only helped to reduce service interruptions and derailments due to rail defects, but it also has enabled us to handle the huge increase in GTMs. In 2006, BNSF will install 2.9 million ties, about 110,000 of which will be concrete ties primarily used on curved track on high density lines and on double and triple track expansions, such as on the Joint Line in the Powder River Basin (PRB). This is the route on which 65 or more loaded trains travel every 24 hours along with an equal number of empty trains to serve (10) mines and deliver coal to several dozen utilities, a growing number of which are east of the Mississippi River.



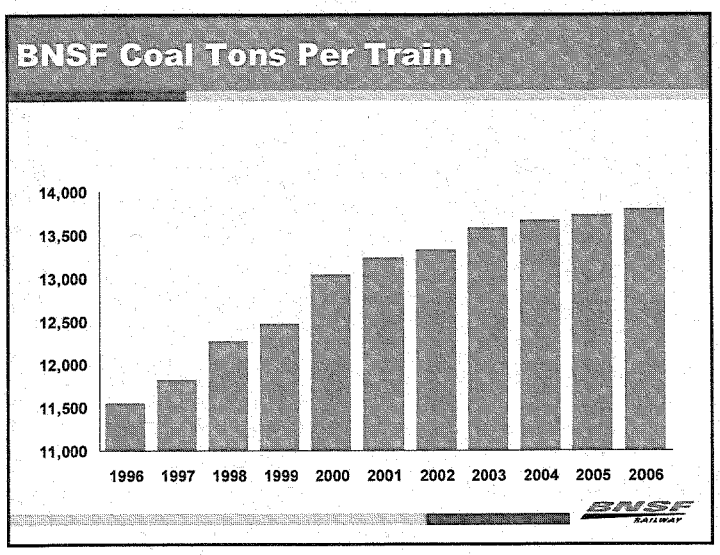
Having capacity available at the right time is not only critical for the railroads, but its customers and the U.S. economy. A clear example of this is BNSF coal business. This chart shows how improved efficiency coupled with prudent capital investment enabled BNSF to grow its coal business and leverage capacity. In the past decade, BNSF has added more than 60 million tons of coal volume to our railroad, an almost half of that just since 2003.



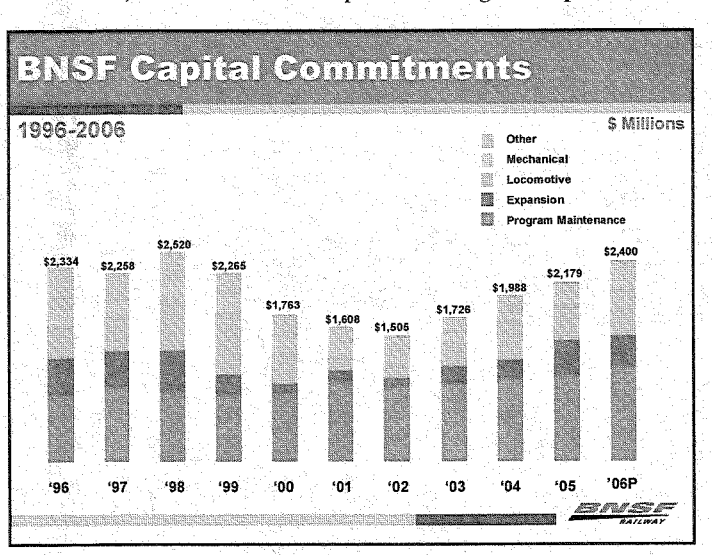
One way BNSF has met increased coal demand is through adding more than 150 coal train sets -- about 125 cars per set requiring three locomotives – to its coal network in the past decade. Today, BNSF operates about 435 coal trains every day. Some of the train sets are owned or leased by our utility customers, but all of the locomotives belong to BNSF, and each one costs in the $2 million range. Aside from these equipment investments, BNSF continues to look for ways to improve velocity and cycle times so it can improve the utilization of its coal fleet and better serve both the mines and utilities.



The chart below provides an example of productivity improvement in coal transportation. BNSF has increased the number of tons per coal train by about 2,500 tons since 1995 by loading more tons in every car. BNSF is also moving forward with other productivity measures such as better top-off systems and grooming, and precision loading; and we are also moving more and more to aluminum coal cars from steel ones. And in May 2006, we will test 150-car trains with several more customers, building on our successful earlier trials. The key to expanding this approach relates to ability of mines and utilities to handle these longer trains. We anticipate that a year from now as many as 30 of our train sets may be 150 cars long.

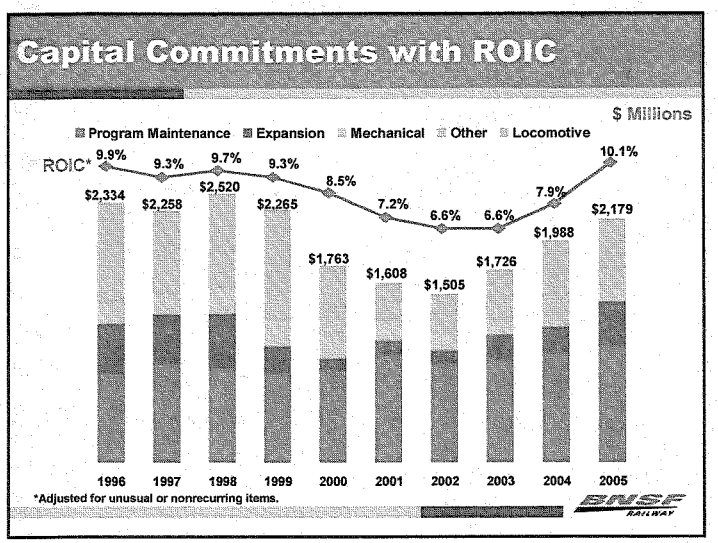


It takes a lot of money to run a low-cost, efficient railroad network. This chart highlights BNSF's capital commitments from 1996 through 2006, more than $22 billion to keep our physical infrastructure strong and to increase capacity through expanded track, yards, terminals, intermodal hubs, locomotives and new technology. In 2005, about $400 million, or 20 percent of our capital was invested in expansion. In 2006, $400 million of our capital will also go for expansion.

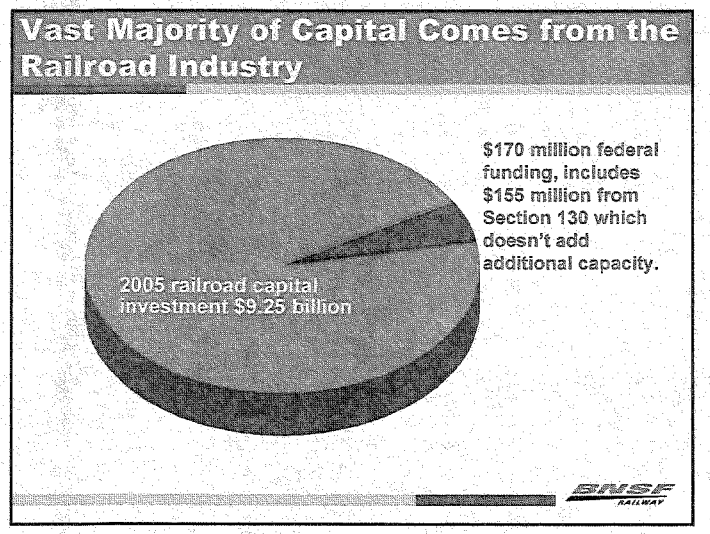


But shippers want more capacity and they want it now. We want more capacity, too, but we can only spend so much otherwise our shareholders will complain if our returns are not what they need to be.

In 2005, as you can see from this chart, we achieved a strong return on invested capital. This slide also points out the direct relationship between the rate of return on invested capital and our ability to reinvest in our business and invest for expansion of capacity. Higher returns also allow us to make the investments required to improve velocity and efficiency. We must be able to sustain our returns to reinvest at the right levels in our network. As long as volume is forecasted to grow, and we can receive proper value for our transportation services, and we do not turn back the progress Staggers made and retrench to heavier economic regulation, we will invest capital at the appropriate levels. But, we can't do it alone.



In 2005, railroads invested $9.25 billion in their networks, while federal funding only contributed $170 million. And $155 million of that $170 million was from Section 130 funding which was for grade crossings, not new capacity.



So, the question is: How do we get additional investment in rail capacity?

We have a few choices:

(1) Direct government investment, which has a place when public and private infrastructure can be improved to benefit both, but which could cause disinvestment by the rail industry if such dollars are be directed at non market-driven investments.

(2) Keep the current model with no change – railroads will continue to invest capital for expansion as long as their returns keep

improving and as long as there is no adverse change in the current regulatory system; or

(3) Supplement the current model with an investment stimulus – an incentive that is not enough to make a bad investment occur, but is enough to pull investments forward sooner in the cycle.

If we could increase expansion capital to $4 billion annually from the current level of $2 billion annually, it would have a tremendous impact on adding capacity.

That is why we support Senator Lott's 25 percent investment tax credit proposal. It is an example of public policy that will incent continued investments for capacity expansion by our industry, while providing an environmental review mechanism that allows good projects to come on line in time to meet capacity demands.

Our ability to provide an efficient rail network to handle the nation's commerce hangs in the balance. Thank you for this opportunity to express my opinion.

Opening Statement by Rep. Mike Sodrel for Hearing on U.S. Rail Capacity
House Subcommittee on Railroads
April 26, 2006

I want to thank the Chairman for having this important hearing. Railroads pay a vital role in the U.S. economy and this Subcommittee should continue to monitor the progress of rail capacity so we can address the issues facing the industry.

I have read the testimony prepared by many of the witnesses and was intrigued by the thoughts and comments on the current situation. However, there is one idea that I found troubling and would caution against it.

When taxpayers invest in highway infrastructure, there is a direct correlation between investment and return. Users pay the tax and they use the infrastructure. If taxpayers invest in rail infrastructure, they should receive a return either directly or indirectly.

For example: A private person may operate a vehicle on a highway built by his or her tax dollars. A private boat may use the locks provided by the taxes paid. A private airplane pilot may use facilities provided by tax revenues. Each of these facilities provides a direct return to the taxpayer.

In the case of rail assets, the taxpayer is asked to invest in infrastructure that is privately owned and they may not use. They are asked to invest in facilities they can not use. Furthermore, they receive no direct return on their investment. In other words, the taxpayer makes the investment; the railroad shareholder realizes the return.

I can not, with a clear conscience, ask the taxpayer to invest in assets they can not use and provides no opportunity for a tangible return on their investment.

While I may not support the idea of taxpayers footing the bill, I also do not support a return to regulation of the industry. I came from the real world and understand what government regulation can do to a business. This can be especially true to a business responsible for moving goods.

We should continue to support policies that allow companies to flourish in the marketplace so they can use their profits to reinvest in to its operations. Railroads are finally making the profits needed to hedge their place in the market to find the capital to invest in new infrastructure to avoid congestion and bottlenecking.

Again, I want to thank the Subcommittee Chairman for inviting the witnesses today and I look forward to working with him in the future to address U.S. rail capacity.

TESTIMONY OF RICHARD F. TIMMONS, PRESIDENT
AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION

BEFORE THE
RAILROADS SUBCOMMITTEE OF THE HOUSE TRANSPORTATION AND INFRASTRUCTURE COMMITTEE

APRIL 26, 2006

Thank you Mr. Chairman and Members of the Committee. I appreciate the opportunity to be here this morning to talk about the short line railroad industry. As I think you all know there are some 500 short line railroads operating nearly 50,000 miles of track across the country. We serve shippers that aren't on the Class I mainline system, preserving rail line that otherwise would be abandoned, saving rail jobs that would otherwise be lost and providing customers with competitive service that is almost always less costly than comparable truck transportation.

Just to put our role in the national transportation system in perspective, 23 of the 24 Members of this subcommittee have a short line railroad in their district. I might add that we are taking up a collection from those 23 to purchase a short line in that last remaining district, which is Congressman Porter of Nevada.

In the time I have this morning let me touch briefly on three topics that relate to the issue of capacity.

First, the short line industry strongly supports the Class I tax credit initiative. Ed Hamberger has laid out the facts and figures and we think they are compelling. As I will discuss in a moment short line infrastructure needs are different than the Class I's, yet the capacity improvements they are addressing are important to us as well. Everyone is familiar with the famous assertion that "when GM sneezes America catches a cold." The short lines are in that same boat. Nearly 90 percent of our traffic originates or terminates on a Class I railroad. Short lines handle in origination or termination one out of every four railcars moving on the national rail system. When the Class I system experiences capacity problems our customers can't get cars, can't move their product and ultimately can't market their product. This is particularly critical in rural America where truck transportation is more expensive than short line rail and where local roads cannot accommodate substantial increases in heavy truck traffic.

Our strong support for this Class I initiative also results from our own experience with the recently enacted short line rehabilitation tax credit. 2005 was the first year of the tax credit and it is already demonstrating its worth.

A railroad in Congressman Latourette's district, the Wheeling and Lake Erie, is using the tax credit to replace light jointed rail with heavier welded rail on a line where traffic has increased some 35% in the last five years. The steel, coal and utility customers on the line are making major capital improvements partly due to the competitiveness and improvements in rail service.

The Kansas & Oklahoma Railroad in Congressman Moran's district is using the tax credit for an $8 million rehabilitation project on a line that has 100 year old rail. Speeds will increase from 10 mph to 25 mph and the line will be able to handle new heavier 286,000 pound cars which are becoming the industry standard. It is likely this line would have been abandoned without the tax credit.

The Florida Northern and Florida Central Railroads in Congressman Mica's district are using the tax credit to support a $14 million track upgrade which will increase speeds from 25 mph to 40 mph and allow the short line to handle the heavier, longer trains that are so important to the shippers. The railroad believes the upgrade will result in a significant increase in the amount of coal that can be shipped over the line.

We are collecting dozens of such stories from around the country and they all share a common theme. The tax credit is allowing light density lines to take on or accelerate projects that would otherwise fall by the wayside. These projects are allowing us to handle more traffic, pick up and deliver the heavier longer trains of the Class I system and help our customers reduce their transportation costs

This is a good news story for many reasons, but one that is worth highlighting here is the reaction of our shippers. As Congress is well aware, our industry has its share of tension between railroads and shippers. This tax credit is being uniformly applauded by our customers because in a very real sense they are its ultimate beneficiary. Let me share with you just one quote that is representative of many we have received during this first year of the credit. It is from the owner of Delta Trading Company which ships hazardous materials on the San Joaquin Valley Railroad in Bakersfield, California and which operates over a line that received a $2.7 million upgrade made possible by the tax credit.

"The track rehabilitation made possible by possible by the tax credit is directly responsible for my company's decision to invest nearly $3 million in our in facility and almost triple our number of employees. We now have a short line railroad partner that can provide the volume and level of service that allows us to significantly grow our business. This tax credit was a very smart decision by the federal government and I suspect it will more than pay for itself as our experience is repeated on short lines across the country."

Mr. Chairman, you and the Members of this Subcommittee were strong supporters of this tax credit. Congressman Moran was the chief sponsor and chief cheerleader of the original legislation and many of you were among the bill's first co-sponsors. The short lines are very grateful for your support. As successful as we believe it will be there is one hitch we did not contemplate and that is the impact that the Alternative Minimum Tax is having on the credit. I know the AMT is a huge issue that has implications far beyond our industry. But, representing the world over which this Subcommittee has jurisdiction I think it is important to emphasize.

When we promoted the tax credit concept we were not sure how the AMT would impact its use. With most companies filing their tax returns just two weeks ago, we still don't have a complete picture. But we have enough of that picture to know it's not pretty. In many cases the AMT is taking up to half the credit away and in some cases it is eliminating it altogether. This tax credit is capped at $3,500/mile which is far less than it costs to rehabilitate a mile of track, and rightly so. The legislation was never intended to fully fund these upgrades, but to help us help ourselves. It jumpstarts rehabilitation on light density lines thus helping us to win back the traffic needed to finish the job. It

appears the AMT is going to reduce that benefit significantly and I would hope this Subcommittee would support some type of AMT relief for the period of this credit.

Finally, let me briefly mention the Railroad Rehabilitation and Infrastructure Financing Program, or RRIF as you know it. I know this was a subject of a Subcommittee hearing a few weeks ago and I submitted a letter for the record on that subject. Let me reiterate that the RRIF loan program is a cost effective way for the federal government to maximize railroad capacity. It allows Class II and III railroads to access capital on terms they would never be able to negotiate in the private markets.

Short line railroads are very risky businesses. Our owners are small business entrepreneurs who have already borrowed large sums to try and save the light density branch lines that could not be operated profitably by the Class I railroads. Because many of these lines could not earn their keep in the Class I system they received little investment and were often headed for abandonment. When private bankers look at these lines they see deferred maintenance, high rehabilitation costs and a history of declining traffic under the previous ownership.

The analysis under the RRIF regime is not without its hurdles. The FRA makes sure the government's interests are protected. But the relatively low interest rate and the 25 year term are, like the tax credit I spoke about earlier, a way to jumpstart the rehabilitation so badly needed by much of our 50,000 mile network. And like the tax credit I think you will find that as we publicize examples of RRIF-related projects the benefits to the railroad network are substantial and will lead to increased capacity.

During your recent RRIF hearing a number of Committee Members indicated they had received complaints about the administration of the RRIF program by the FRA. Administrator Boardman wrote to me following the hearing to seek the Short Line Association's perspective on that subject. While there has been much to complain about since the beginning of the RRIF program, I believe the situation has dramatically improved in the recent past and I wanted to submit for the record my written response to Administrator Boardman.

I appreciate the opportunity to appear here today and am happy answer any questions.

RICHARD F. TIMMONS
PRESIDENT
AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION
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April 6, 2006

Mr. Joseph Boardman
Administrator
Federal Railroad Administration
1120 Vermont Ave., N.W., 7th Floor
Washington, DC 20590

Dear Administrator Boardman:

Thank you very much for your recent letter concerning the Railroad Rehabilitation and Improvement Financing (RRIF) program. I appreciate the opportunity to provide my perspective on the administration of this program.

As you know, the RRIF program had a difficult and far too lengthy startup period. There were a host of reasons for this including a complicated application process, an inadequate and short handed team of FRA analysts, and institutional opposition to the program among some agencies outside of FRA. In some instances those difficulties were exacerbated by inadequate applications from the short lines themselves. These problems are evidenced by the fact that only 12 loans have been approved in the program's first six years.

I believe those problems are largely behind us and that the FRA has put in place the personnel and procedures necessary to allow this program to finally meet the goals that were intended when it was first enacted. The quality of your in-house staff has improved. The information on your website is more user-friendly and useful. The process for engaging outside consultants has been streamlined. Perhaps most important, it appears that FRA is making every effort to meet the 90-day application processing deadline provided for in last year's transportation legislation. It was the significant length of the process that was the most discouraging to potential applicants.

While I am certain there are a variety of reasons for this turn around, I wanted to take special note of Mr. Joseph Pomponio who was recently put in charge of processing RRIF applications. Mr. Pomponio has been most helpful in explaining the program to potential applicants, assisting with the development of applications and in advising short line railroads as to how they might amend applications that might otherwise not meet the government's financial requirements. I hear this from my short line members and know it to be true from the many times my own staff has called seeking his advice. While he sometimes gives answers a short line does not like, he has been very accessible and responsive.

I have no doubt that individual Congressmen have heard many negative comments about this program. But I suspect that the majority of those comments relate to the past not to the present. Because you have asked me this question I will take some time to explore the subject with the short line membership. In the meantime I believe you have made significant progress and the short line community is very grateful. Obviously the final measure of progress will be an increase in the number of approvals and that remains to be seen in the months ahead, but I am confident we are headed in the right direction and increased applications and loans will result.

Respectfully,
Richard F. Timmons

Statement of
Burt Wallace
Vice President, Transportation
UPS
Before the
Subcommittee on Railroads
Committee on Transportation and Infrastructure
U.S. House of Representatives
April 26, 2006

Thank you, Mr. Chairman. At UPS, we believe the future of the nation's rail system is at the very heart of our nation's ability to compete globally, and right now, from our experience, there is much that needs to be done to ensure that future ability.

This is not a challenge to any one stakeholder – not the companies that run the railroads, not state and local governments, not the federal government, not the users of the rail system.

Rather, there is a collective need. And there must be a collective remedy. This is a fundamental national issue. As a nation, we recognize the importance of first-class highway and aviation infrastructures. Our rail network must be placed in that same category.

The railroads were drivers of prosperity and growth in the last two centuries and we believe they can and must continue to be one of the cornerstones of our nation's economic well-being. Today, commerce and the demand for efficient transport is global. U.S. companies remain leaders in innovation and our workers are as capable as any. Our nation's infrastructure, however, has failed to keep pace with the demands of the 21st Century, and railroad infrastructure is an integral and necessary part of a system that increasingly must be viewed as a single, all-encompassing network. Public funding mechanisms have been critical in maintaining our aviation and highway infrastructure network; the rail network should be no different. If any

part of that network fails to keep pace, the entire system suffers along with our ability to compete.

That explains, in part, why UPS, a company perhaps best known for delivering items to your door in brown package delivery vehicles, is interested in the railroads.

UPS remains among the largest corporate customers of Class I Railroads in the United States today and we and our customers – businesses large and small, homeowners and families, all across America – have a vital interest in the efficient operation, and future direction, of the North American railroad industry. In 2005, we directly spent more than $750 million on freight rail transportation, and controlled (through our supply chain subsidiary) another $800 million in customers' railroad transportation spend. We move thousands of trailers, filled with packages, on flat rail cars daily. We have been incorporating rail transportation into our network since the 1960s, and it is important to remember that every trailer we put on the railroads represents one less trailer moving on the highways.

UPS and our customers depend on rail service as a vital part of our worldwide intermodal transportation network, which on a daily basis delivers more than 14.8 million packages to 7.9 million customers. It is estimated that UPS delivers more than 6% of U.S. Gross Domestic Product and 2 percent of global GDP each and every day.

In addition, in recent years UPS has actively developed logistics and global supply chain management solutions for customers around the world. As UPS service offerings reflect customer demand for international transportation solutions, a healthy and vibrant U.S. railroad industry has become a critical partner in meeting the needs of our customers not just in the United States, but throughout the world.

Allow me to give you an example of how our system interacts with that of the railroads. A national hair products manufacturer uses UPS for its' nationwide shipping needs. Their Southern California distribution location supplies products to much of their West Coast retail beauty salon customers. UPS uses the rail network to feed these packages to UPS hub locations in the Pacific Northwest. This customer has had repeated service problems and delays in this region and recently stated, "Taking a week into Oregon and Washington (from California) simply does not work. Other carriers get to these locations in 2 days via truck. At this rate, we might be forced to make changes. Certainly I see excuses, but no solution being suggested by UPS."

Unfortunately, this scenario is all too common on today's rail network. When our customer confronts us with this feedback, we are left with few alternatives. UPS wants the railroads to succeed and to continue our mutually rewarding transportation partnership. But the bleak current service picture forces us to be responsive to our customers' needs and find an alternative transportation mode. Our marketplace dictates a quick and appropriate response. Along the same vein, we wish the railroads had the ability, and desire, to respond to our needs.

In the early years following deregulation, the railroads adapted to a changing environment and UPS and its' customers realized service and performance enhancements. However, recent trends have diminished performance and constrained intermodal operations, underscoring the need to eliminate the Class I "urge to merge" mentality. Let me be clear: UPS unequivocally opposes any future Class I rail mergers.

Whether as a result of 1990's rail mergers or other reasons, there has been little new rail capacity. Regrettably, the railroads have been unable to make adequate capital investments, technological enhancements and innovative solutions in responding to new market conditions.

I stress the word adequate. It's not as if the railroads have not been investing – as you will hear today from industry representatives. Rail performance clearly underscores, however, that it simply has not been enough. Spot investment – a few miles of track here, fixing a bottleneck there – will not make our rail system more efficient and the national economy will suffer for it. As an aside, the proposed Railroad Infrastructure Tax Incentive legislation is NOT sufficient. We need to devise a more comprehensive solution.

Nothing illustrates the current challenges we face more than time in transit, which remains a significant issue for railroad customers like UPS. Since the passage of the Staggers Act, the efficiency and speed of our nation's transportation system generally has increased. The lone exception, however, is railroad velocity. I'd ask you to consider what other mode of transportation in the United States moves slower than it did 30 years ago? And demands on an already overburdened rail network are increasing.

UPS has broad experience in aviation, trucking and maritime transportation, and we have seen an increase in speed and a corresponding decrease in transit times across each of these modes. Given today's emphasis on streamlined supply chains and speed to market, the railroad time in transit picture puts at risk our nation's worldwide economic competitiveness.

This is underscored by the fact that a month ago UPS initiated a new "Fast Lane" service for truck transportation, between key city pairs throughout the country, to meet the demand for time sensitive shipments that previously had been sent over the rails. That's correct, we purposefully moved package volume off the rails and on to the congested highway system. Why did we do this at a time of record fuel costs and increasing highway congestion? The answer is simple: to meet our competition; railroads are unfortunately not making the grade.

Another area of future railroad focus should be a commitment to technological innovation. Railroads generally have foregone developing Positive Train Control technology – a system like the nationwide Air Traffic Control System except for railroads – and, with a couple of exceptions such as the proposed Norfolk Southern and Kansas City Southern Meridian Speedway project, have not invested in innovative concepts and partnerships to provide better service. Both the National Transportation Safety Board and the Transportation Research Board have found that stimulating development of technologies such as Positive Train Control could produce tremendous benefits to the rail system.

In recent years, UPS has invested billions of dollars on technology, much of which is directly related to imbedding information in each individual package. Today we can provide our customers a wealth of information regarding the status and time in transit of a $6.00 single package or an ocean bound cargo container. In contrast, the railroads lack the capacity to give their customers information about trainloads of freight.

At this critical juncture, when time-sensitive information is essential to national and global commerce and to our nation's security, why should we accept not knowing many of the most basic details about rail movements on major rail arteries?

UPS understands and recognizes the capital intensive nature of the rail industry and is sensitive to the short-term vision of equity markets. The railroad cost of capital dynamics are indeed challenging and public policy initiatives addressing infrastructure improvements, adding capacity, improving rail service, and enhancing technology, should be promoted. But the railroads must carry their full burden and the recent extraordinary financial performance of virtually all Class I railroads illustrates that the capacity to significantly increase investment for the future unquestionably exists.

As noted earlier, however, this is not only an issue for the nation's railroads. Looking forward, one concept that should be explored is the notion of establishing a public-private partnership to help fund railroad infrastructure improvement projects. I would ask the Committee to consider the following: the nation's highway system has a Highway Trust Fund to support and maintain a safe and efficient federal highway system; the nation's airports have an Aviation Trust Fund to support, maintain and enhance airport infrastructure and provide necessary capacity. If the existence of these two transportation trust funds are deemed to be in the public interest, why not a Railroad Trust Fund, or a similar user-funded mechanism?

We need a public-private investment plan to address the serious challenges facing the industry. Wouldn't improving railroad capacity, safety, infrastructure and technology be in the public interest? Yet, the user-funded trust concept has not gained traction, while service levels diminish and rates continue to rise. Instead of working on capacity and technology solutions, the railroads seem more interested in resurrecting the commercial vehicle size and weight debate, or successfully lobbying to repeal the 4.3 cents per gallon diesel fuel deficit reduction tax that was directed to the U.S. Treasury general fund. This money should have been directly funneled to rail infrastructure improvement projects, not returned to railroad balance sheets.

The railroad industry should be challenged to find a mechanism that <u>does</u> meet its approval, because doing nothing is not a viable option. The Meridian Speedway project mentioned earlier demonstrates that railroads <u>can</u> make necessary and innovative investments. There is a demonstrable need for similar initiatives.

UPS strongly believes that this is an issue critical to an array of constituencies beyond the railroads themselves and major users such as UPS, the nation's farmers, retailers, the mining industry and chemicals manufacturers. Every major container seaport in North America handled

record volumes in 2005. Those containers moved out of those ports on the highways and rails. The highways and rails go through cities and towns all across the country, fueling the economy but also raising safety concerns.

UPS realizes that we are in this dilemma together. Developing a world class freight rail network is a national issue crying out for a national solution. What we need now is national leadership and a collaborative approach to solving this issue. The lead time required for major rail projects is too great for any further delay, and the storm clouds of dramatically increased freight flows across all modes are rapidly approaching.

With our vast experience in operating multimodal transportation networks, our knowledge, and our resources, we are prepared to assist the Congress and our rail service partners in this quest. We also ask our colleagues from the rail industry, from the shipper community and other rail stakeholders to join us. Let us make this a primary national transportation priority, starting today.

PCA
Portland Cement Association

TESTIMONY BEFORE THE

HOUSE COMMITTEE ON TRANSPORTATION AND INFRASTRUCTURE

SUBCOMMITTEE ON RAILROADS

SUBMITTED BY

JOHN WHITE
VICE PRESIDENT LOGISTICS
BUZZI UNICEM USA INC.

ON BEHALF OF

PORTLAND CEMENT ASSOCIATION

HEARING ON

THE U.S. RAIL CAPACITY CRUNCH

APRIL 26, 2006

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Mr. Chairman and members of the Subcommittee, my name is John White, Vice President of Logistics for Buzzi Unicem USA Inc., a leading manufacturer of portland cement in the United States. I appreciate the opportunity to testify here today to discuss issues related to rail capacity. I appear on behalf of the Portland Cement Association, of which I serve as chairman of its Logistics Committee. I look forward to a constructive dialogue addressing the need for additional rail capacity and reasonable steps we believe are necessary to improve the current national rail policy. The current national rail policy and lack of capacity impedes portland cement manufacturers from effectively and efficiently delivering an essential commodity needed to build our nation's vital infrastructure and strengthen our nation's economy. With more than 80 percent of portland cement manufacturing plants "captive" to a single railroad, the current rail policy is unnecessarily contributing to higher construction costs and in some instances making it more cost-effective to import portland cement from as far away as China.

WHAT IS PORTLAND CEMENT?

The term "portland" cement is not a brand name – rather, it is a generic name for the type of cement used in concrete, just as stainless is a type of steel. Portland cement is a manufactured powder that acts as the glue or bonding agent that forms concrete. As an essential construction material and a basic component of our nation's infrastructure, portland cement is utilized in numerous markets, including the construction of highways, streets, bridges, airports, mass transit systems, commercial and residential buildings, dams, and water resource systems and facilities. The low cost and universal availability of portland cement ensures that concrete remains one of our nation's most essential and widely used construction materials.

PORTLAND CEMENT ASSOCIATION

Portland Cement Association (PCA) is a trade association representing cement companies in the United States and Canada. PCA's membership consists of 31 companies operating 102 manufacturing plants in 36 states. PCA members account for 98 percent of cement-making

capacity in the United States. The cement industry is a crucial component of one of the largest segments of our nation's economy – the more than one trillion dollar construction industry. Nearly every construction project requires portland cement. In 2005, 127 million metric tons of portland cement were consumed in the United States; in fact, cement is the second most consumed commodity on the planet, second only to water.

BUZZI UNICEM USA INC.

Buzzi Unicem USA is the fourth largest U.S. cement company, producing 8.8 million tons of cement annually. Employing 1,600 people, Buzzi Unicem operates 10 manufacturing plant locations throughout the United States including: Cape Girardeau and Festus, Missouri; Chattanooga, Tennessee; Greencastle, Indiana; Independence, Kansas; Maryneal, Texas; Oglesby, Illinois; Pryor, Oklahoma; and Stockertown, Pennsylvania. Our corporate office is located in Bethlehem, Pennsylvania. Buzzi Unicem USA supplies cement to over 3,800 highway paving contractors, ready mixed concrete producers, concrete block producers, and other concrete product firms in 18 states. Nine of the 10 cement plants mentioned above are captive to a single railroad.

U.S. CEMENT INDUSTRY DEMOGRAPHICS

The cement industry operates manufacturing plants in 36 states, producing nearly 96 million metric tons of portland cement in 2005. Cement manufacture is a highly capital-intensive industry. Cement companies invest millions of dollars annually to upgrade manufacturing equipment and phase out more costly and less energy efficient operations. Between 1994 and 2003 the cement industry invested $7.542 billion in new capital investment. The construction and permitting costs of a new greenfield cement plant can easily exceed $250 million. Only two greenfield plants have been constructed within the past 10 years.

Cement is produced from various abundant raw materials including limestone, shale, clay and silica sand. These minerals are ground and heated in large rotary kilns to temperatures as

high as 3,400 degrees Fahrenheit. The heat of the combustion fuses these materials into clumps of an intermediate material called clinker. When the clinker is discharged from the kiln, it is cooled and later ground with a small amount of gypsum to produce the gray powder known as portland cement. Different types of portland cement are manufactured to meet various physical and chemical requirements.

Portland cement manufacturing facilities use an enormous amount of energy. In fact, energy is the largest cost component in the manufacture of portland cement. The U.S. cement industry is largely coal fired with 81.3 percent of all plants using coal, coke, or some combination of the two as primary kiln fuel in 2004. The domestic cement industry is the largest industrial consumer of coal. Much of the coal utilized to heat cement kilns on a 24/7 basis is delivered by rail.

The cement industry is regional in nature. Most cement manufacturing plants are located in rural areas near large limestone deposits, the principal ingredient in producing cement. However, at the same time plants also must be located near markets because the cost of shipping cement quickly overtakes its value. As such, customers traditionally purchase cement from local sources. Texas, California, Florida and Pennsylvania, are the leading cement manufacturing states, respectively, producing nearly 36 million tons in 2005 or 37.4 percent of domestic cement production.

U.S. CEMENT MANUFACTURERS RELY ON RAILROADS

Considering the regional nature of the cement industry, it is critical that there are reliable and cost-effective transportation options available. Average cement shipments range between 250 to 300 miles. Truck transportation is not economical beyond 100 to 125 miles. As such, the cement industry is reliant on railroads to deliver our product beyond the economical range of trucks. Several cement plants have access to water transportation for domestic shipments. The railroads have sometimes argued that these cement facilities are not captive since there are alternative modes of transportation available. This simply is not the case. Domestic portland

cement manufacturers rely on rail transportation to move 50 percent of all shipments between cement plants and distribution terminals, according to 2004 U.S. Geological Survey data, the most recent independent figures available. About 95 million tons of cement was produced domestically in the same year. Most bulk cement shipments are from the manufacturing plants to the more than 400 regional distribution terminals, where the cement is then delivered by truck to local contractors and ready mixed producers. It is vitally important to our industry that the railroads provide reliable, efficient and cost-effective service to meet the widespread demand for our product. As mentioned earlier, more than 80 percent of U.S. cement manufacturing plants are captive to a single railroad. Due to the absence of competition, these plants are charged substantially higher rates and usually receive poor service. On the other hand, dual rail-served facilities typically have lower rates and more reliable service.

The railroads also transport millions of tons of inbound coal shipments to fuel cement manufacturing plants each year. There are examples within the industry in which cement plants that are served by two railroads receive coal from a supplier that is captive to a single railroad. There are also instances where both the cement plant and the coal supplier are captive to a single railroad. These situations result in unnecessarily high rail rates that add to the cost of cement and, ultimately, to construction costs. PCA members have also reported situations in which they were forced to transport coal to the cement plant by truck, at a substantial cost, due to delivery failures by the railroad. In these instances, the situation confronting the cement plants were desperate: they had only a day or two of coal supply on hand.

U.S. CEMENT INDUSTRY LARGELY "CAPTIVE" AND SERVICE SUFFERS

The Staggers Act of 1980, which removed regulations of the railroad industry where transportation competition exists, has improved the industry's efficiency and financial stability. However, since deregulation, there has been a sharp decline from 63 Class I railroads in 1976 to just four major Class I railroads today handling 90% of the nation's rail traffic. This consolidation has contributed to diminished competition as well as ineffective and inconsistent rail service for the cement industry and many others.

Inconsistent and unreliable service from the Class I railroads is one of the most serious problems the portland cement industry confronts in our efforts to bring an affordable and essential product to market. Service encompasses many aspects of rail transportation, including picking up rail cars (covered hoppers), on-time delivery of rail cars, providing empty rail cars, handling issues, questions about the condition of the rail cars, and settling claims for service failures. The cars supplied by the railroads are typically old, poorly maintained and frequently a safety concern. Our members report that as many as 15 percent of the empty rail cars delivered to manufacturing plants in a given week are being rejected.

In recent years, several cement companies have been forced to purchase private rail cars since the Class I railroads have refused to add cement rail cars to their fleets. This, in addition to the declining and inconsistent service, has increased the need for more rail cars to deliver the same tonnage. Meanwhile the railroads have added tariff provisions charging for the storage (demurrage) of private rail cars. This results in further increased costs to the cement shipper while providing no incentive to the rail carriers to improve their service.

Further compounding the problem is the fact that at some locations, the railroad will only quote freight rates to the cement company if the cement company uses their (system) rail cars. In short, no product will move from that origin unless the railroad is collecting revenue for the use of their rail cars. In other instances, the railroads quote rates such that the difference in cost of a movement in a private rail car is so great that private rail car transports are not economical. Rail car supply is a classic Catch 22 situation that adds unnecessarily to the cost and inefficient shipment of our product and, ultimately, to construction costs.

While service continues to decline, cement manufacturers are experiencing sharp rail freight rate increases. For example, some rates increased more than 23 percent in 2005, according to some cement companies. Indeed, transit times on empty return cars have increased by more than 13 percent in some instances, increasing fleet storage costs. So, Mr. Chairman, our industry literally is paying more for less!

PCA SUPPORTS SERVICE PROVISIONS IN LEGISLATION

The cement industry has no recourse regarding rates since cement (officially "hydraulic cement") is classified as an exempt product from rate regulation by the Surface Transportation Board (STB). Since the STB has done little to address service issues, we believe Congress should enact legislation expanding the STB's authority in this area. The STB should be required to post a description of each complaint from a customer about rail service. The legislation should also require the Board to submit an annual report to Congress regarding rail service complaints and describe the procedures the Board took to resolve them. Further, either party should be allowed to submit a dispute over rail service to the STB for "final offer" arbitration. These provisions are included in bipartisan legislation (H.R. 2047), *the Railroad Competition Improvement and Reauthorization Act of 2005*. These service provisions contained in H.R. 2047 do not constitute "re-regulation," a term coined by the railroad industry to overstate the perceived negative impact of the legislation.

We believe strongly that the lack of rail competition is the fundamental issue associated with these problems. PCA believes it is important to strike a balance between regulation of the railroad industry while also assuring rail competition. PCA believes that the intent of Congress in the Staggers Act was only to deregulate the railroads where competition exists. Unfortunately, the implementation of the Act has resulted, often, in deregulation even where there is no transportation competition – with predictable results such as those we are reporting.

The following example further illustrates the unintended consequences of the Staggers Act, as implemented, on a captive shipper.

PCA member Holcim (US) Inc. established HolRail, a limited liability corporation, to construct and operate a two-mile rail line that would provide competitive rail service to the Holcim cement manufacturing plant in Holly Hill, South Carolina. Presently, Holly Hill is

served only by CSX Transportation, Inc. (CSX). The proposed line would connect to a rail line owned by the Norfolk Southern Railroad Company (NSR).

Holcim is one of the largest suppliers of portland and blended cements and related mineral components in the United States. It ships more than 20 million tons of cement and related materials each year, of which 16 percent moves by railroad. Holcim has 14 manufacturing facilities and approximately 70 distribution terminals across the country and employs approximately 2,500 people in the United States.

The Holly Hill production facility manufactures a variety of cement and masonry products and relies on rail transportation to receive inbound raw materials and to ship outbound products. In August of 2003, Holcim completed a plant expansion project that increased the size of the facility and doubled output capacity to two million tons of cement per year. A substantial portion of Holly Hill's production is shipped by rail to Holcim distribution terminals to serve markets that are over 100 miles from the facility. Because trucking cement over distances greater than 100 miles is uneconomic and impractical, Holly Hill requires reliable, economic, and efficient rail transportation to reach optimal plant utilization.

When the Holly Hill plant operates at full capacity, the plant annually receives 3,500 inbound rail cars with fuel and raw materials and ships out 10,000 rail cars with cement. As the only rail carrier with direct access to the Holly Hill plant, CSX transports all inbound raw materials and outbound products that move by rail. CSX's service track record is weak. Its service is unreliable and inadequate, and CSX appears to be completely indifferent to Holcim's requirements and requests for service improvements. For example, CSX has refused to allow Holcim to use its private railcar fleet to transport Holly Hill's products even when CSX cannot provide its own cars to meet the needs of the plant! CSX recently eased its objection to this practice. The CSX equipment is in poor condition and is routinely rejected at the Holly Hill facility. By contrast, two other cement plants in the Holly Hill area that are not captive to a single railroad are freely allowed to ship product in private cars without the restrictions that CSX imposes on Holcim.

In addition to CSX's inadequate railcar service and its restrictions on private cars, CSX charges Holcim rates that exceed those paid by the two nearby cement manufacturers that have competitive rail service. By obtaining rail competition, through its "build out" to NSR, Holcim will place Holly Hill on equal footing with other comparable cement facilities that have access to more than one railroad.

CSX's consistently poor service, which has caused Holcim to lose business opportunities in the past, simply cannot meet the needs of Holly Hill's expanded production capacity. Holcim believes that competition between CSX and NSR at Holly Hill will produce more responsive, more reliable, and better rail service. Improved rail service will support the facility's increased production and allow Holcim to supply distant markets and to compete in new markets.

Additionally, rail-to-rail competition will lead to a reduction in rail rates, making Holly Hill more competitive with non-captive producers. Accordingly, HolRail, the Holcim subsidiary, has filed a petition with the STB to construct a two-mile rail line, running south from the Holly Hill plant to the NSR line. The petition is currently pending before the STB.

Another example of the unintended consequences of the Staggers Act involves a captive east coast cement company that must transport cement 300 miles by rail to its distribution terminal to meet customer demand. The applicable rail rate is so outrageously high the cement company concluded that importing cement from China to the east coast is less expensive than shipping it 300 miles by rail.

DEMAND FOR CEMENT TO INCREASE

United States cement consumption reached a record high during 2005, peaking at 127 million metric tons and reflecting growth of 5.6 percent over strong 2004 levels. The near term outlook for the cement market remains strong. Growth in cement consumption is expected to materialize due to continued increases in construction activity as well as increases in the use of

concrete and cement per construction dollar spent. Despite the likelihood that the growth boom in residential housing construction may be nearing an end, gains in nonresidential and public construction are emerging as new sources for growth in construction activity. Gains in these areas are expected to outweigh modest declines in residential construction – resulting in a continuation of growth in construction activity. Furthermore, various influences suggest that the increases in concrete and cement usage per dollar of construction activity will continue. The combination of sustained strength in construction activity and cement usage per dollar of construction activity is expected to result in new cement consumption records in 2006 through 2007 and beyond. From 2005's record levels, cement consumption is expected to grow 3.5 percent in 2006 and another 2.5 percent in 2007.

Cement and concrete are literally one of the building blocks of our nation's economic growth. Strong cement demand reflects the need for business to expand commerce by way of increasing its physical properties, whether it be retail shops, warehouses or office buildings. It also reflects the need for federal, state and local governments to build new schools, improve its road systems and general infrastructure. It also reflects the need to build new housing to meet growth in population and household formation. Furthermore, according to the Bureau of Census, the United States population is expected to grow by 68 million persons in the next 25 years. As a result, new demand for commercial, public and residential construction activity will increase. According to PCA's long term forecast, cement consumption is expected to grow from 127 million metric tons in 2005 to 200 million metric tons in 2030.

To meet the future U.S. cement and concrete requirements, the United States cement industry currently is engaged in its most aggressive capacity expansion in the industry's history. Based on announced and permitted plans, by 2010 the industry will add 18.6 million metric tons (20.6 million short tons) of clinker capacity – representing a 19.8 percent increase over 2005 capacity levels and a $4.1 billion commitment. The capacity expansion reflects a mix of greenfield sites, plant modernizations, and expansions of existing facilities. In addition, the industry is committed to the expansion of its import facilities – amplifying the industry's commitment to expand all sources of supply to meet the national economy's rising need for

cement and concrete. At least 63 percent of the new capacity expansion and modernizations underway at existing facilities are captive to a single railroad. Although three greenfield facilities are scheduled to start production during this period, the cement industry is largely limited to modernizing and expanding its capacity at existing facilities because of high construction and permitting costs to build a greenfield cement plant. Since cement industry capacity expansion must follow projected market demographics largely based on population growth, much of the expansion will occur in the southern and western regions of the United States where the vast majority of the cement facilities are captive to a single railroad. In short, Mr. Chairman, the cement industry is forced to expand capacity where it is captive to a single railroad – despite our industry's concern about that captivity.

While the industry has proven it commitment to providing reliable and adequate supplies of cement and concrete to meet U.S. needs, these efforts are partially offset by existing rail constraints. The existing lack of adequate rail capacity impedes portland cement manufacturers from effectively and efficiently delivering its product to the marketplace. The rail capacity shortfall relative to existing requirements of the economy is reflected in a rapid run-up in rail freight rates – rising by 11.7 percent in 2005 according to the Bureau of Labor Statistics. As the economy grows and more cement capacity is put in place, it is likely that existing rail constraints will be exaggerated, potentially leading to a repeat of the large rate hikes experienced in 2005. Furthermore, it is important to recognize that other essential building materials rely heavily on the railroads to move product to market – amplifying the adverse consequences of rail constraints on overall economic growth.

Construction currently accounts for approximately 6.7 percent of total economic activity. One out of every 18 jobs in the U.S. is directly employed by the construction industry. Since 2000, growth in construction employment has accounted for 30 percent of the United States' total employment growth. Very little construction activity can materialize without utilizing concrete at some stage of the construction project. Impairment in the ability to deliver cement to market efficiently, impairs construction activity and represents an issue that could impede future growth in this important sector of our nation's overall economic activity.

FREIGHT RAILROAD INFRASTRUCTURE TAX CREDIT

The Class I railroads state that they are committed to expanding capacity and improving service, spending an estimated $6.6 billion for capital expenditures in 2005 and projecting to spend a record $8 billion in 2006. To further enhance capital improvement and increase capacity, the Class I railroads are seeking a 25 percent federal tax credit to leverage private investment in rail infrastructure improvements and other capital expenses. The proposal reportedly would also make the tax credit available to certain shipper funded rail projects.

PCA obviously supports increasing investment in the nation's rail infrastructure to meet the current and future freight transportation needs. As the Class I railroads report profit increases, now is the time for the railroad industry to bolster investment to expand capacity and improve service, especially for captive shippers that typically pay much higher rates and experience poor to marginal service.

Without knowing the full details of the 25 percent tax credit sought by the railroad industry, PCA has not stated an official position on this proposal. PCA would be more inclined to support a tax credit if Class I railroads are required to invest in rail capacity projects that would provide relief to captive shippers. This requirement would have the benefit of reducing highway congestion, creating a more efficient freight rail system for all shippers, including particularly domestic shippers who generally are the ones that are captive, and heavy truck traffic on our highways and local streets, thus reducing highway maintenance cost. Requiring that the tax credit for rail capacity enhancements be focused on the infrastructure needed to serve captive rail customers would be the most prudent and sound use of taxpayer dollars. The cement industry also believes that Congress should further examine the concept of a railroad trust fund, similar to the Highway Trust Fund, to finance rail capacity and capital projects. Finally, we want to see any tax benefit for the railroad industry coupled with legislation that addresses the

concerns of railroad customers that the rail industry be more competitive, including that the railroad industry be subject to the same antitrust laws as the cement industry.

The higher rates and unreliable service often associated with captive cement plants often forces our industry to transport cement by bulk tank truck to distribution terminals and customers at a much higher cost. It is critical that cement manufacturers maintain adequate inventories of product to meet contractor demand. Contractors utilizing portland cement in large-scale concrete paving projects, for example, need a constant and reliable supply of cement to meet construction time tables and to plan for weather delays and other construction complications. Just as contractors expect timely shipments of cement from the cement company, it is the obligation of the railroad, we believe, to deliver shipments of cement in a timely manner.

CONCLUSION

U.S. manufacturers need a vibrant and profitable rail industry to support our nation's economic growth. The portland cement industry is a vital component of our nation's construction industry, which supports the backbone of our nation's growing economy. It is essential that the portland cement industry have access to a competitive rail transportation system to ensure that our product is delivered in a timely and efficient manner to our customers who build our nation's critical infrastructure fostering economic expansion. With more than 80 percent of the cement manufacturing plants and a similar ratio of the industry's 400 distribution terminals held captive to a single railroad, combined with the inadequate service at these facilities, only adds to our nation's construction costs. Demand for cement is forecast to increase for the foreseeable future, only exacerbating this problem.

Mr. Chairman and members of the Subcommittee, we strongly urge you to further examine H.R. 2047, *the Railroad Competition Improvement and Reauthorization Act*, especially provisions that would expand STB's authority over service-related issues. This provision, among others, would help provide some relief for captive industries, such as the cement industry.

Mr. Chairman, thank you for the opportunity to testify before the Subcommittee today on this important issue.

STATEMENT OF HONORABLE DON YOUNG
RAILROAD SUBCOMMITTEE HEARING:
THE U.S. RAIL CAPACITY CRUNCH
APRIL 26, 2006

THANK YOU, MR. CHAIRMAN. I COMMEND YOU FOR HOLDING THIS VERY TIMELY HEARING ON THE SITUATION FACING OUR NATIONAL RAILROAD NETWORK. AFTER COMING BACK FROM A WAVE OF BANKRUPTCIES AND NEAR-BANRUPTCIES IN THE 1970S, OUR FREIGHT RAILROADS HAVE NOW MOVED FROM TREMENDOUS EXCESS CAPACITY TO A SHORTFALL. SADLY, AS IS THE CASE WITH MOST FORMS OF TRANSPORTATION IN THIS COUNTRY, THE LEVEL OF INVESTMENT IN NEW AND IMPROVED INFRASTRUCTURE SIMPLY HAS NOT KEPT UP WITH THE COUNTRY'S NEEDS.

LAST YEAR'S SAFETEA LU LEGISLATION SHOULD HELP. IN THE RAIL SECTOR, THE R.R.I.F. LOAN PROGRAM, FOR EXAMPLE, MAKES AN OFF-BUDGET REVOLVING $35 BILLION LOAN FUND AVAILABLE TO IMPROVE RAIL INFRASTRUCTURE. BUT THAT KIND OF GOVERNMENT ASSISTANCE IS NOT A TOTAL SOLUTION. IT CAN ONLY SUPPLEMENT THE HUGE PRIVATE-SECTOR INVESTMENT

REQUIRED TO MAINTAIN AND IMPROVE RAIL NETWORKS. AS ONE OF THE MOST CAPITAL-INTENSIVE INDUSTRIES AROUND, RAILROADS MUST GENERATE BILLIONS IN CAPITAL JUST TO KEEP THEIR HEADS ABOVE WATER IN TERMS OF INFRASTRUCTURE CAPACITY.

IF THE UNITED STATES DOES NOT MEET THE CHALLENGE OF IMPROVING ITS RAIL NETWORK, I PREDICT SEVERE ECONOMIC CONSEQUENCES. THE U.S. WILL FALL BEHIND IN THE EVER MORE COMPETITIVE WORLD MARKETS, AND MANY INDUSTRIES THAT DEPEND ON RAIL OR RAIL-INTERMODAL TRANSPORTATION WILL HAVE A HARD TIME STAYING IN THE GAME. I HOPE THAT AT TODAY'S HEARING, BOTH RAILROADS AND USERS OF RAIL TRANSPORTATION—WHO ALWAYS HAVE SOMEWHAT DIFFERENT AGENDAS—CAN SET ASIDE THOSE DIFFERENCES AND EXAMINE THE DIMENSIONS OF THE CAPACITY PROBLEM, AND PERHAPS PROPOSE SOME ADDITIONAL STEPS WE CAN TAKE TO ADDRESS IT. IT IS AS PLAIN AS DAY THAT, IF OUR RAIL

NETWORK BECOMES CONGESTED, NEITHER THE RAILROAD NOR THE SHIPPER WINS, AND THE COUNTRY LOSES.

THANK YOU, MR. CHAIRMAN.

Arkansas Electric Cooperative Corporation

Your Touchstone Energy Cooperative

8000 Scott Hamilton Drive
P.O. Box 194208
Little Rock, Arkansas 72219-4208
(501) 570-2200

August 12, 2005

The Honorable Roger P. Nober, Chairman
Surface Transportation Board
1925 K Street, N.W.
Washington, D.C. 20423-001

Re: Railroad letters about fall peak service plans

Dear Chairman Nober:

Arkansas Electric Cooperative Corporation (AECC) is a generation and transmission cooperative providing electric generation and transmission services for the 17 rural electric distribution cooperatives in Arkansas. Our member cooperatives in turn serve their approximately 430,000 members by providing reliable and economic retail electric service. AECC uses coal, natural gas and fuel oil to generate this electric energy. We also utilize hydroelectric generation when available and purchase power when it is economical to do so.

Coal fuels the majority of AECC's generation. AECC's coal-fired generating plants are jointly owned with other utilities, and were designed to burn the abundant and clean burning sub-bituminous Powder River Basin (PRB) coal found in Wyoming and Montana. The plants in which we have an ownership interest normally consume in excess of 14 million tons of PRB coal each year. For transporting this coal to our Arkansas plants we have depended on the railroads since the late 1970's. AECC is currently in a dilemma with respect to quality rail transportation service.

AECC appreciates your efforts last year and again this year to get the railroads to publicly say how they plan to deal with the peak demand for their transportation services. The information presented by the railroads gives us some indication of how the railroads are approaching the problems we are experiencing with rail transportation. The recognition bestowed upon the Board by the Congressional Budget Office highlights the way actions by the Board can improve performance for railroads and customers alike.

Of particular importance this year, the peak planning process enables the Board to examine the railroads' efforts to satisfy the needs of PRB coal users in the context of other peak period demands. This, in turn, may enable the Board to identify further steps it could consider to further improve the situation for railroads and their PRB coal customers.

As you know, to move PRB coal to plants in Arkansas, the only options currently available involve the BNSF Railway (BNSF) and/or Union Pacific (UP). One of AECC's plants is completely captive to UP. For these reasons, AECC focuses primarily on the BNSF and UP letters.

BNSF and UP both emphasize the way the requirements of the investment community influence their actions regarding capacity. BNSF's Matthew Rose states, "...there are significant financial constraints that will not allow BNSF...to invest in sufficient capacity." UP's Dick Davidson says, "...we expect to invest in new capacity as returns on investment justify, given the revenues we are able to earn in the marketplace and the constraints that government actions place on them." Basically, the railroad position seems to be that if there's enough traffic paying high enough rates, they'll be able to supply enough capacity. The corollary to that seems to be that everyone should expect that they're going to need more revenue if the needed capacity is to materialize.

AECC is keenly aware that the railroads do not currently have the infrastructure needed to deliver the products they have contracted to transport. Even before the Joint Line situation arose, our plants did not receive all the coal transportation obligated under contract in 2004. This situation was made much worse by the crisis that began in mid-May this year on the PRB Joint Line. The railroads have indicated that this shortfall in deliveries will continue through 2005 and may even continue into 2006. Furthermore, they have indicated they will not make up these shortfalls.

This lack of performance by the railroads places a very heavy financial burden on our members and other electric consumers in Arkansas and elsewhere. AECC and the other plant owners have had to restrict the amount of coal that is being burned at our coal-fired power plants. AECC has an obligation to serve its members. Therefore, we are providing the needed electrical generation from other, much more expensive, sources. Our members, the electric consumers, are the ones who ultimately must pay the higher price.

This is the third time in the last twelve years that we have had to place burn restrictions on our coal-fired power plants due to an inability on the part of the railroads to satisfy their contractual and/or common carrier obligations. If anything, we are experiencing shortfalls of increasing severity and duration. Given the huge growth in PRB volumes that occurred during this time, AECC believes that neither coal shippers nor the Board can rely on the proposition that the railroads and the investment community, left to their own devices, will automatically supply adequate capacity.

A closer look at the origins of the current Joint Line problem demonstrates the dangers associated with this approach. BNSF and UP have both asserted that the cause of the PRB Joint Line crisis this year was the "unusual" and "unprecedented" amounts of snow and rainfall acting upon accumulated coal dust. In checking National Oceanic and Atmospheric Administration (NOAA) data for this portion of Wyoming, we find no truth in these assertions. For example, the historical average amount of moisture received in May, expressed in inches of water, is 2.50 inches for Douglas, WY (near the south end of the Joint Line) and 2.95 inches for Gillette (near the north end). In May of 2005, Douglas received 2.55 inches, just 0.05 inches above average. At the same time, Gillette received 2.89 inches or 0.06 inches below average. Both locations received less than average precipitation in April 2005. For the entire precipitation cycle beginning October 1, 2004, there appears to be no part of the Joint Line that received abnormally high precipitation.

Given that the weather really was neither "unusual" nor "unprecedented", the problem can properly be seen as the failure of the railroads to maintain the Joint Line roadbed in useable condition. As UP's letter indicates, the accumulation of coal dust was not hidden, at least not from those responsible for operating and maintaining the line. Rather, the evidence suggests strongly that the railroads chose to simply let the dust accumulate rather than take the steps needed to maintain the roadbed.

Deferring maintenance might be understandable if the line in question were a marginal branch line that didn't cover its costs. However, the PRB Joint Line is one of the busiest rail lines in the world. In maximum rate reasonableness cases, the Board has found that this facility generates traffic that "pays its own way" in terms of covering operating costs and providing a market rate of return on the capital associated with the relevant portions of the rail network. The railroads cannot credibly assert that the volumes or rates associated with PRB coal traffic are insufficient to justify proper maintenance of the Joint Line.

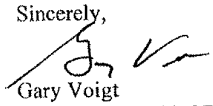
What coal shippers and the Board are left with is the apparent willingness of the railroads to "bet the rent" that the drought of recent years in eastern Wyoming would continue, and let their bottom line results be inflated by the "savings" associated with not maintaining the line. Unfortunately, pressure from the investment community to produce favorable results in the short term can lead to this type of myopic decision-making. Coal shippers, who are here for the long term, need the Board's help to send a clear message to the investment community and to railroad management: The public interest does not permit this type of trifling with the rail network in the name of short-term gains.

With the repeated and ongoing problems associated with moving PRB coal to our plants, AECC and others looking for reliable and economical fuel supply for electric generation are being forced to look at alternative fuel supplies, many of which do not involve the railroads at all. Current and future power plants may make much greater use of locally available lignite and petroleum coke or fossil fuels from Central and South America. Needless to say, actions by the railroads that push users of America's most abundant and economical energy resource to convert to more expensive imported fuels cannot be viewed as being consistent with the public interest.

AECC is still evaluating specific potential steps that may be warranted in light of the Joint Line problems and the responses we have received to date from the railroads regarding our efforts to adapt to the PRB shortfall. In some cases those efforts involve rail transportation of coal from non-PRB sources, which should not be affected by the Joint Line problems or any associated embargoes. Unfortunately, we may need the Board's help to get the rail service we are entitled to under contract and/or the common carrier obligation of railroads. We can assure the Board that any action we ultimately request will be consistent with the Board's mandate to protect the public interest regarding the rail network, and with legitimate capacity issues the railroads may have associated with the provision of service to all of their customers during the peak period.

AECC appreciates very much the opportunity to submit these comments for your consideration.

Sincerely,



Gary Voigt
President and Chief Executive Officer
Arkansas Electric Cooperative Corporation

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