

**RAILROAD SHIPPER ISSUES AND S. 919, THE
RAILROAD COMPETITION ACT OF 2003**

HEARING

BEFORE THE

**COMMITTEE ON COMMERCE,
SCIENCE, AND TRANSPORTATION**

UNITED STATES SENATE

ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

OCTOBER 23, 2003

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ONE HUNDRED EIGHTH CONGRESS

FIRST SESSION

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**RAILROAD SHIPPER ISSUES AND S. 919, THE
RAILROAD COMPETITION ACT OF 2003**

THURSDAY, OCTOBER 23, 2003

U.S. SENATE,
SUBCOMMITTEE ON SURFACE TRANSPORTATION AND
MERCHANT MARINE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2:32 p.m. in room SR-253, Russell Senate Office Building, Hon. Kay Bailey Hutchison, [Chairman], presiding.

**OPENING STATEMENT OF HON. KAY BAILEY HUTCHISON,
U.S. SENATOR FROM TEXAS**

Senator HUTCHISON. I would like to call this hearing to order. I am holding this hearing, of course, as the Chairman of the Surface Transportation and Merchant Marine Subcommittee, and at the particular request, in fact promise that I made to Senator Burns to do this.

This is not a new issue, as all of you know. You have been here before. And I do think, though, that it is a timely one and one that I would like to see resolved for the benefit of both railroads and shippers. Across the Nation our manufacturing productivity is lessened by shippers held captive in many places by railroads with no incentive to charge competitive rates.

In my years in the Senate and prior to that when I served as Vice Chairman of the National Transportation Safety Board, I have seen numerous attempts to level the playing field between captive shippers and the railroads that serve them. But Congress has not been able to agree on a single approach and the crisis continues.

Today there is a severe shortage of competition in the freight rail industry. The railroad mergers of recent years have reduced the number of class 1 railroads from 42 to 5. These mergers have brought great benefits to the railroads, with operating incomes of the class 1 carriers increasing by an average of 10 percent per year.

For manufacturers facing tough economic times, the story is different. In the absence of competition, shippers are forced to pay arbitrary rates. It is a common practice for captive shippers to send their loads without knowing how much they will pay for carriage and without a guarantee of on-time delivery. Every day captive shippers face the choice of pay the rate or lose the business.

Almost 35 percent of the Nation's railroad traffic is now considered captive. Not surprisingly, captive shippers pay a premium per mile compared to those served by more than one railroad. In Vic-

toria, Texas, a shipper once had three railroads competing for business. After the mergers only the Union Pacific remains. With no competitors, the Union Pacific has added new fees for carriage of empty cars, dispatching and storage, until overall shipping costs rose more than 35 percent for this shipper in Victoria, Texas.

Toyota currently operates five manufacturing plants in the United States, some captive, some competitive. Captive facility rates were so much higher that Toyota adopted a policy dictating that no plant could be built without service from at least two railroads. Ultimately Toyota chose to build its sixth plant in San Antonio, Texas, but not until the legislature threatened to build a spur to the site so another railroad would be able to compete with the incumbent. In San Antonio a buildout was an option due to the relative proximity of a competing rail line. For most captives this is not the case and buildouts are prohibitively expensive.

The Staggers Act was explicitly intended to protect captive rail shippers and preserve competition. However, Congress had never anticipated that the Staggers dispute resolution mechanisms would have to function in a market of only five class 1 railroads. Bringing a rate case under Staggers is slow and expensive. We need to bring this law into the 21st century.

In the 106th Congress, I introduced legislation that I thought was a fair and evenhanded approach to address the problem. The Surface Transportation Board Reauthorization and Improvement Act of 1999 would have established a mission to promote rail competition and remove so-called paper barriers to rail service. It would have required carriers where feasible to establish consistent rates for bottleneck areas with no competition. In a provision recently adopted by this committee, a streamlined procedure for adjudicating small shipper cases was set forth. Unfortunately, that bill was never considered by the full Committee and captive shippers are still facing overwhelming obstacles.

Despite these impediments, rail remains the only viable method for shipping bulk commodities such as coal, grain, and chemicals over long distances. This traffic accounts for more than 40 percent of class 1 railroad revenues.

I do not think we should deny the existence of a problem any longer. My colleagues Senator Burns and Senator Rockefeller have introduced legislation to address the crisis faced by captive shippers. I support many of the ideas behind their bill, Senate bill 919, which contains several elements addressed in my 1999 proposal.

I just would like to say that I believe that we should protect our railroads and our shippers. I really believe there should be a fair way to solve this problem that allows railroads to make a fair profit and allows shippers to have the capability to establish fair rates. It would be my intention to try to move that, either through amendments with Senator Burns bill or in some way, but it does take some movement on the part of the railroads and I do hope that we could work something out that would be fair to all.

With that, I will ask Senator Burns for his opening statement before we hear from the witnesses.

**STATEMENT OF HON. CONRAD BURNS,
U.S. SENATOR FROM MONTANA**

Senator BURNS. Thank you, Madam Chairman. Again, I want to thank you very much. She made the commitment to have this hearing and it is happening today and I am beholden to you on this particular issue.

I appreciate the witnesses coming today because I think we have to work out some way or get a dialogue started to find out that we have got a problem and we have got to identify it. I think we are doing a pretty good job identifying the problem, but we do not do a very good job of solving it.

This issue is very important to my state of Montana. When my colleagues Senators Dorgan and Rockefeller and Roberts first began this exercise, rail competitiveness was a problem in our states as well as isolated pockets around the nation. But since then we have heard from more and more shippers about decreased transportation competitiveness and as a result increased transportation rates. I think the Chairman today in her highlights made a better case than I have made in my statement.

In 1980, Congress passed the Staggers Act during a time when there were 40 class 1 railroads in this country. Under those circumstances, it was intended that regulation would be eased and competition would endure and drive the marketplace, ensuring rail rates would remain reasonable. Through regulatory involvement and an incredible amount of consolidation, we find ourselves with essentially only four class 1 railroads in the United States, without in the East and two in the West.

Together with Senators Dorgan and Rockefeller, I introduced S. 919, the Railroad Competition Act of 2003. Our intent is to correct the model and the economic structure that allows monopolistic behavior in the industry. There are no provisions in S. 919 that are reregulatory. It does not cap rates and it does not mandate open trackage rights. The bill reinstates the original intent of the Staggers Act, which has been eroded by mergers and regulatory interpretation.

S. 919 will not penalize the railroads or create an environment where railroads cannot compete with other transportation modes. In fact, S. 919 will create competition among our railroads, improving transportation efficiency in our economy.

I am the last member of Congress that would introduce a measure that would drive railroads out of the local economy, simply due to the fact that my state of Montana is nearly entirely captive to one railroad, the Burlington Northern-Santa Fe. The BNSF is a very reputable railroad and I consider them one of the greatest assets that we have in our state.

Due to the seasonality issues in agriculture, marketplace demands place a massive logistical burden on railroads and other modes of transportation. That has been the history of railroads in this country. Considering their challenges in my state, BNSF is usually, usually responsible to the needs of their customers. But they legally operate in a business model that breeds monopolistic behavior.

Montana is a classic case of what happens to rail customers when you eliminate competition in transportation alternatives. Our

rail rates are some of the highest in the nation and my shippers end up subsidizing rail rates in regions where competition really is present. Our rail customers pay more for less service. The rail customers in regions with competitive alternatives pay less and receive more service. To make things worse, in Montana we are truly dependent on railroads to transport bulk commodities that could not be efficiently transported by any other means.

American agricultural shippers are the most vulnerable to predatory marketing by monopolistic practices of the railroads and some other entities, and I am not going to go into them today. The farm producer, unlike any other entity we know in America, cannot pass the freight costs on to anyone else. They must simply bear the cost.

We are not here to debate reregulation on railroads. Rather, we need to restore the balance between rail customers and the railroads that Congress originally intended to achieve in the Staggers Rail Act of 1980. All rail customers, not just a select few, should be able to make competitive choices or at least begin to be able to negotiate with their rail carriers on a more balanced playing field.

I would like to make it evident to this committee that one thing is for certain: Regionalized monopolies over rail transportation are not good for shippers, railroad investors, or respective state economies or our national transportation network as a whole. Furthermore, this problem will not go away. It has been 23 years since the enactment of the Staggers Act and neither the marketplace nor the STB, the Surface Transportation Board, and its predecessor the Interstate Commerce Commission has corrected what I view as obvious flaws and obvious monopolistic behavior. This system needs to be restored to create a prosperous, economic, and competitive system.

Madam Chairman, again thank you for holding this hearing today and I look forward to research the testimony from our witnesses today, and we sure have I think the best of the lot.

Senator HUTCHISON. Thank you, Senator Burns.

Senator Lautenberg.

**STATEMENT OF HON. FRANK R. LAUTENBERG,
U.S. SENATOR FROM NEW JERSEY**

Senator LAUTENBERG. Thank you, Madam Chairman, and I will try not to hold up the process very long here. But I do want to make a couple of comments.

We have a duty to ensure that our national system of freight transportation can continue to function as one of the principal foundations of our economy. Right now we have the most efficient system of freight railroads in the world and I would like to be able to say that 20 years from now—I hope I am still sitting here—that will be the case. That went over everybody's head.

[Laughter.]

Senator BURNS. I will stand up, Senator.

Senator LAUTENBERG. Thanks for acknowledging that I am speaking.

I remain convinced that any discussion of how we plan to move freight through our country over the next 20 to 50 years—and I concede that—must be part of a larger discussion. I feel that we have got to look at how we plan to move passengers as well as com-

modities. Passenger rail has been the least thought-out, the least thought-out component of our national transportation system. It holds much promise as a safe, efficient, and environmentally sound method of getting people from one place to another.

Having said that, in the not too distant future we are going to be facing major challenges with respect to our freight rail system. Will we have the infrastructure to support the amount of freight which should be carried by rail in the coming years? There are very optimistic estimates about how much freight there is going to be, which is good business, and how are we going to accommodate it is the next question.

The growth in freight traffic expected in the next couple of decades could push differential pricing to an extreme that it was never intended to accommodate. There may come a time when even differential pricing will just not allow enough, with our deregulated freight railroad industry, to recoup the capital it needs to maintain and expand its infrastructure. We have got to be prepared to evaluate what our options are if we reach that point: How do we get the funds? How do we provide the encouragement to enlarge the system?

We have to do the planning necessary now. We have to show leadership at the Federal level and ensure that we have a coordinated, efficient, national system for transporting people, freight, and commodities.

I look forward, Mr. Chairman, and commend you for holding this hearing, and I look forward to working with you and Members of this Subcommittee to develop practical policies for addressing all of our surface transportation needs, freight and otherwise, in a comprehensive manner.

Thank you very much.

Senator HUTCHISON. Thank you, Senator Lautenberg.

Senator Dorgan.

**STATEMENT OF HON. BYRON L. DORGAN,
U.S. SENATOR FROM NORTH DAKOTA**

Senator DORGAN. Madam Chairman, thank you very much.

This is a really important issue. This issue has been around for a long while. We have had difficulty even getting hearings and certainly difficulty getting a markup on a piece of legislation, and I think it is safe to say a lot of us are pretty much out of patience. Nothing ever seems to happen. I appreciate very much the fact that you are holding this hearing.

A colleague of mine in the House of Representatives some long while ago said: Do not take on the railroads because you cannot beat them, you simply cannot win. Well, the problem is we are losing at the moment with respect to captive shippers who are not the beneficiaries of competition, but rather they are the victims of unfair pricing.

By that I do not mean to say I do not like the railroads. I think the railroads are a form of transportation that provides something very important to our region of the country, to our entire country. But we have seen a shrinkage of the number of rail companies in dramatic consolidation and mergers over the years and it has in

many ways created a circumstance where the economic muscle on one side of the ledger, it just overwhelms the shippers.

Let me describe what is happening in North Dakota, because Tip O'Neill used to say all politics is local, and so is all policy, it is local. And this is not theory. If you have a carload of wheat, a rail carload of wheat, and you want to ship it from Bismarck, North Dakota, to Minneapolis, Minnesota, you are shipping it 400 miles roughly and you are going to pay about \$2,600 for it. Take the same carload of wheat and ship it from Minneapolis to Chicago, about 400 miles, and it will cost you \$900.

So about the same distance, you will pay \$2,600 or you will pay \$900. Why the difference? On one route there is competition, the other there is not. So our Public Service Commission in North Dakota estimates that we are overcharged by nearly \$100 million. Farmers, businessmen and women, we are overcharged by nearly \$100 million.

Now, I have noticed that the other side to this argument is sending out massive quantities of mail to people saying this is an attempt to reregulate the railroads and call the Congress and tell them we do not want to reregulate the railroads. Well, let me say this is not an attempt to reregulate the railroads. If we wanted to do that, we could introduce a bill to ask the STB to cap rates. We could ask them to set prices for specific commodities or specific routes. We could do what we did in the telecommunications industry and we could give competitors open access to anybody's tracks.

The fact is we are not doing any of those things, and to argue that our attempt to streamline the rate reasonableness process and to fix the bottleneck problem is reregulating the railroads is farcical, just farcical. You have a right to do that. The First Amendment allows you to say this is reregulating the railroads, but it is simply not true.

So this legislation is long overdue. Perhaps we could pass it by unanimous consent this afternoon following the hearing and then have the major—you know, people around here always say, well, let us save the major debate for the floor. If the chairman would entertain that, we could just save the major debate for the floor of the Senate.

But this is serious business, lots of money, and it is a significant issue for a lot of shippers in this country, especially family farmers in my state. Madam Chairman, again thank you for calling this hearing.

Senator HUTCHISON. Thank you.

Now I would like to call on the Honorable Roger Nober, the Chairman of the Surface Transportation Board. I appreciate your serving on the panel so that we can expedite the testimony and the questions. Thank you.

**STATEMENT OF HON. ROGER NOBER, CHAIRMAN,
SURFACE TRANSPORTATION BOARD**

Mr. NOBER. Well, certainly. Thank you, Chairman Hutchison, and good afternoon to you and Members of the Subcommittee. I understand the hour is late and it is late in the afternoon and I will try to be brief in my oral testimony and summarize my written statement.

As you said, my name is Roger Nober and I am the Chairman of the Surface Transportation Board. I certainly appreciate the opportunity to appear before the Subcommittee today to discuss the rate and service issues faced by rail shippers and the provisions of S. 919, the Railroad Competition Act of 2003. This is my first appearance before this Subcommittee on these matters, but I know that you all have a longstanding interest in the issues being discussed today, as many of you stated in your opening statements, which as we all know are vitally important the freight railroads and their employees, their customers, and to the freight transportation system as a whole. So I certainly commend you for having this hearing and appreciate the opportunity to give you my perspective on these very important issues.

Now, at the outset let me say that to me the individual provisions of S. 919 are less significant than the underlying concerns that give rise to this legislation. Since I have become Chairman, I have worked hard to understand and address the core concerns of captive shippers and the railroads that serve them. Now, I believe that many of the issues raised by captive shippers are legitimate and I would like to focus my testimony today on what I think the fundamental concerns are and the steps the board is taking to address them.

Now, I would say first many shippers do not understand the board and its processes and do not believe that our agency is a fair and impartial forum for resolving disputes. Now, my most important initiative as Chairman has been to convince shippers through openness and dialogue that the board is and can be an effective regulatory body and forum for their concerns.

For example, shippers express a great deal of concern about the Board's lack of transparency and I have taken several steps to change this, including restoring regular voting conferences, holding hearings on significant matters, initiating oral arguments in large rate cases, and holding an open house for practitioners for the first time in a decade. I personally have an open door policy and have not turned down a single meeting request in the past year. I think I have met with virtually everyone on the panel today, and I have traveled around the country to better understand rail transportation and the supply chain, including again taking a trip with one of today's witnesses.

Now, while these may seem like small steps, I think they have helped our agency's stakeholders better understand how and why the board makes the decisions that it does and comes to some of the doctrines that you all have expressed concern about.

Now, second, many disputes between shippers and railroads seem to take on a life of their own because of the way shippers feel they are treated by railroads. Rail customers often conclude that, while rates are high, railroad service and attitude are bigger problems, and I think many of you have referred to that as well today. Rail customers understand the financial pressures that railroads are under, but they fundamentally feel they are not treated by railroads the way they would treat their own customers.

This has led some to assume that railroads act this way because they are monopolies and to believe that legislation like S. 919 is necessary to introduce competition into the rail network. Now, I am

sympathetic to this concern, but I do not think that legislation is the answer. Railroads must work harder to be more customer-friendly and I am working to impress upon all of our major carriers the importance of doing so. Railroads have to be nimble competitors in the transportation marketplace to increase their business and grow their revenues.

While the leadership of each of the major railroads understands this, as some of today's witnesses can also attest, that attitude does not always translate down through their entire organizations.

Helping railroads improve their operations to provide better service is one goal that carriers, shippers, and policymakers can all share. The good news is that in many circumstances railroads have worked with their customers to improve efficiency and take costs out of the supply chain, to the benefit of both parties. But these examples are just not common enough and I will work hard to ensure that they become the norm and not the exception.

Third, captive shippers believe that for the majority of their shipments they cannot challenge rates they feel are unreasonable. They feel that as a result market power is unfairly skewed in the railroads' favor and that legislation is necessary to correct it. Now, it is true that the board's processes work reasonably well for large rate cases. Thirteen such cases are currently pending, which is the most in our agency's history. But the vast majority of disputes would be classified as small rate cases and no small cases have been brought under our small rate case guidelines.

Now, this may be because there are no small rate disputes or because there is something about our agency's rules and doctrines that discourages shippers from bringing these cases. As of today, in effect, only about 75 coal shippers have a meaningful opportunity to challenge rail rates and I think this is simply unacceptable.

I am confident that a real opportunity to bring small rate cases can be achieved through procedural, rather than legislative, reform. I have described in detail many of these changes in my written testimony, but let me highlight a few for you now.

First, we can set a clear threshold for bringing cases. We can hire an administrative law judge to hear them in the first instance, limit discovery, and issue preliminary decisions in a matter of months. We can ensure that such cases are decided under a clear standard, one set in accordance with the Interstate Commerce Act, and we can assure that these cases are appealable to the full board and ultimately responsible to the courts.

Now, any new procedure for small rate cases must also take account of the fact that many shippers do have economic leverage with railroads when the totality of their relationship is considered. The economic relationship between shippers and railroads is oftentimes made to be very simple, but it is usually complex and shippers—many shippers often have many facilities which are both captive and competitively served and ship to numerous destinations on several railroads. It is a relationship that is not easily captured by simple rules.

In sum I believe that real administrative reform is possible and we are committed to working with shippers, carriers, and the Congress to address this issue.

Fourth, certain areas of the country are disproportionately dependent on rail service in general and on a single rail carrier in particular for economic health. I have come to understand that many from the Upper Midwest feel that their economies are particularly dependent upon a single railroad.

The Board must pay close attention to the unique circumstances in that part of the country. For example, I recently traveled to North Dakota and met with a number of government officials, shippers, and producers. I have also spoken numerous times with the railroad that serves that area. Now, the issues faced in the Upper Midwest are longstanding and complex and not easily solved. I was recently handed at my agency a hearing transcript from 1908 where shippers from North Dakota were concerned about the lack of rail car supply. They have been around for a while and I am not promising that I can easily solve them, not even in Senator Lautenberg's timeframe.

However, attention and not legislation I believe is the best approach and, while attention may not solve everybody problem, improvement certainly is possible.

Finally, I understand that many in the shipping community are unhappy with certain of the board's regulatory doctrines. I have met with most of the supporters of S. 919 and they almost all agree that they would not be calling for it had the board interpreted certain provisions of the Interstate Commerce Act differently.

Now, I have said that to interpret the Interstate Commerce Act as some in the shipping community advocate is tantamount to fundamentally restructuring the economic underpinnings of the freight railroad industry. That is a significant step with serious ramifications for the economy and one that I believe is for the Congress rather than for an independent agency to undertake. In the provisions of S. 919 those types of changes would be made and it is in this context that I would like to briefly address that bill now.

Taken as a whole I think that S. 919 would fundamentally change the economic model of the railroad industry and is unwise. Not a single one of our major railroads is revenue adequate and if it were enacted S. 919 would call into question the continued economic viability of our freight rail system. If it were passed some shippers may realize some rate reductions in the short term, but in the long run this legislation would significantly degrade our nation's freight rail network, to the detriment of all of its users and to the economy as a whole.

Although our nation's privately funded rail system may have some problems, it is the best freight rail system in the world. The United States is the only country with a national freight network that does not need taxpayer subsidy. If enacted, S. 919 would jeopardize both of those distinctions.

Now, I believe that the board can and will do a better job to address the concerns raised by captive shippers. But I think the kinds of reforms I have outlined today and not substantive changes to the statutory scheme are the best way to address the concerns raised by captive shippers while maintaining a healthy freight rail network. That is the balance Senator Hutchison described in her opening statement and it is a difficult one, but one that I think can be achieved.

I appreciate the opportunity to discuss these issues today and look forward to any questions you might have, and with that I will be happy to answer any questions when the panel is done.

[The prepared statement of Mr. Nober follows:]

PREPARED STATEMENT OF ROGER NOBER, CHAIRMAN,
SURFACE TRANSPORTATION BOARD

Good morning, Chairman Hutchison, Ranking Member Inouye, and Members of the Subcommittee.

My name is Roger Nober, and I am Chairman of the Surface Transportation Board. I appreciate the opportunity to appear before this Subcommittee today to discuss the rate and service issues faced by railroad shippers in general and singly-served (otherwise known as “captive”) rail shippers in particular, and the provisions contained in S. 919, the Railroad Competition Act of 2003.

This is my first appearance before this Subcommittee as Chairman of the STB. I appreciate the longstanding and deep interest that the Members have shown in the issues facing the railroad industry, which are vitally important to the financial health of the freight railroads, to the railroads’ customers and employees and to the nation’s freight transportation system as a whole. I commend the Subcommittee for holding this hearing and discussing these important issues.

In my written testimony, I would first like to provide the Subcommittee with an overview of the Board and its responsibilities. Next, I will discuss steps the Board is taking to address issues faced by singly-served or captive shippers. Finally, I will discuss S. 919.

Overview of the STB

As all of you know, the Surface Transportation Board was created eight years ago by this Committee in the ICC Termination Act of 1995. The Board is an economic regulatory agency that Congress charged with the fundamental missions of resolving railroad rate and service disputes and reviewing railroad mergers, line sales, abandonments and new construction. Structurally, the Congress determined that the Board should be decisionally independent but administratively affiliated with the Department of Transportation.

When it was created at the beginning of 1996, the Board had to accomplish its statutory missions with one-third fewer employees than had been performing those same functions at the ICC. Since 1996, the Board has met its statutory deadlines while functioning with nearly the same level of resources during that time. But as I will outline in my testimony, the Board will face new challenges in the coming year as it works to address the issues raised today and will need some modest additional resources to continue its important work.

The Board serves as both an adjudicatory and a regulatory body. The Board has jurisdiction over railroad rate and service issues and rail restructuring transactions (mergers, line sales, line construction, and line abandonments); certain trucking company, moving van, and non-contiguous ocean shipping company rate matters; certain intercity passenger bus company structure, financial, and operational matters; and certain pipeline matters not regulated by the Federal Energy Regulatory Commission.

In sum, when Congress eliminated the ICC in 1995, it created the Board to carry out two core functions—reviewing merger proposals and resolving disputes over rates and services provided by railroads. One of the main reasons the Board exists is to provide a regulatory backstop to assess the reasonableness of rates charged to captive shippers when those customers and their railroads are unable to successfully negotiate a contract for the transportation.

The Board has created a number of mechanisms to help railroads and their customers resolve disputes before availing themselves of the Board’s formal processes. For example, the Office of Compliance and Enforcement operates the Rail Consumer Assistance Program. That program is intended to provide assistance to rail consumers in addressing those issues that have not been resolved through private negotiations. When informal processes like that one cannot produce a solution, however, the Board must be the regulatory backstop that Congress intended it to be.

It is no secret that many captive shippers—the focus of today’s hearing—believe the Board has inadequately performed this core mission of ensuring that they have a forum for reaching a formal resolution of rate or service disputes. They feel that without a regulatory backstop, the transportation market for freight rail services does not properly function. Many of the issues they raise are legitimate, and I will

next turn to the fundamental concerns raised by captive shippers and the steps the Board is taking to address them.

Issues Faced by Captive Shippers

1. Unreasonable Rates

Under the Interstate Commerce Act, the Board has exclusive jurisdiction to resolve rate disputes in those instances when railroads have market dominance—in other words, the railroad is charging a rate higher than the regulatory floor and the shipper has no effective transportation alternative. Under the Interstate Commerce Act, the Board must balance the often conflicting objectives of assisting railroads in attaining revenue adequacy, on the one hand, and ensuring that the rates that individual shippers pay are reasonable and fair, on the other. The balance, as we all know, is not an easy one. Rates that are too high can harm rail-dependent businesses, while rates that are held down too low will deprive railroads of revenues to pay for the infrastructure investments needed to give shippers the level and quality of service that they require. The Board is the forum of last resort if a captive shipper feels his rate is unreasonable, and the agency must do its best to carry out the law in a way that is fair to all when deciding railroad rate cases.

The Board has one set of procedures for handling “large” rate cases and another for “small” cases. In recent years, the Board has experienced a significant increase in the number of large rail rate complaints filed with it. Whereas in past years the Board had two or three of these cases pending at any one time, today it has 13 large rail rate disputes pending (as well as two pipeline rate disputes and two water carrier rate disputes pending). The Board still has not had a single small rate case filed since it adopted its small case guidelines in 1996, but as I will discuss further, my top priority for the next year is to establish a meaningful process for quickly and surely deciding small rate cases.

a. Large Rate Cases

Determining the reasonableness of a rate in a large rate case is a complicated inquiry. The Board’s governing statute requires it first to determine whether the railroad has monopoly power over its customer—in other words, whether the railroad is market dominant. Only if the railroad is market dominant does the Board have jurisdiction to review the rate. This is so because Congress has foreclosed rate regulation where there is effective competition. Once it has determined that it has jurisdiction to review the rate, the Board applies a court-approved methodology for rate review known as “constrained market pricing” (CMP).

i. Market Dominance

The first step in a rate case is a two-part inquiry to determine whether the railroad has “market dominance” over the transportation to which the rate applies. The first part is to determine the “variable costs” of providing the service. The statute establishes a conclusive presumption that a railroad does not have market dominance over transportation if the rate that it charges produces revenues below 180 percent of the variable costs of providing the service, which means that this 180 percent revenue-to-variable cost (r/vc) percentage is the floor for regulatory scrutiny.

If the rate the railroad charges exceeds the 180 percent r/vc threshold, the second part of a market dominance inquiry involves a qualitative assessment in which the Board must determine whether there are any feasible transportation alternatives that could be used for the traffic involved. The Board considers whether there is actual or potential direct competition—that is either competition from other railroads (intramodal competition) or from other modes of transportation such as trucks, pipelines, or barges (intermodal competition) for transporting the same traffic moving between the same points. If there are effective competitive alternatives for the transportation, then the Board does not have jurisdiction to regulate the rate, even if the rate charged yields an r/vc ratio greater than 180 percent.

ii. Rate Reasonableness Standards

If the shipper can show that the railroad is market dominant, then the Board applies its CMP principles to assess whether the rate being charged that shipper is in fact unreasonable. CMP provides a framework for the Board to regulate rates while affording railroads the opportunity to cover their costs. It is premised on differential pricing, that is, pricing based on the demand for the service provided. CMP principles recognize that, in order for railroads to earn adequate revenues, they need the flexibility to charge different customers different prices based on each customer’s demand for rail service. But CMP principles also impose constraints on a railroad’s ability to price. Despite the complexity of CMP, the courts have held that

it is the most desirable available approach to railroad rate review and that the Board must use it whenever it is feasible.

Although complaining shippers can choose from three approaches, the most commonly used CMP constraint is the “stand-alone cost” (SAC) test. Under SAC, a railroad may not charge a shipper more than what a hypothetical new, optimally-efficient carrier would need to charge the complaining shipper if such a carrier were to design, build, and operate—with no legal or financial barriers to entry into or exit from the industry—a system to serve only that shipper and whatever group of traffic that shipper selects to be included in the traffic base. The ultimate objective of the SAC test is to ensure that the complaining shipper is not charged for carrier inefficiencies or for facilities or services from which the shipper derives no benefit. As with CMP in general, this assures the complaining shipper that it is not required to pay for inefficiencies or to unfairly subsidize other customers of the railroad.

iii. The Board Is Working to Reform the Large Rate Case Process

Deciding large rate cases is time consuming and costly for both the parties involved and the Board. Although the Board by statute has 9 months after all evidence is filed to decide a large rate case, it can take more than twice that long after the shipper files its complaint for the parties to file all their evidence with the Board. Preparing that evidence and presenting it to the Board are very expensive—parties have testified that a SAC case can cost as much as \$3 million to prosecute, \$5 million to defend, and generate more than 700,000 pages of material.

When I became Chairman, the Board intensified its search for ways to simplify and speed up this process, and as a result of this effort the Board recently adopted a number of changes to its rules. Last February the Board held a hearing in the rulemaking proceeding entitled *Procedures to Expedite Resolution of Rail Rate Challenges To Be Considered Under the Stand-Alone Cost Methodology*, STB Ex Parte No. 638, which was exceptionally productive.

Based on the extensive testimony received from shippers and railroads, in April the Board revised its rules in ways that ought to both shorten the decisional process and limit the expense of bringing a case. The new rules’ most significant provisions include: (1) mandatory, non-binding mediation at the beginning of the case, under the Board’s auspices, between the complaining shipper and the defendant railroad; (2) expedited procedures to resolve disputes, using Board staff, over what information the parties can be required to give to each other during “discovery”; (3) technical conferences to resolve, before the actual evidence is filed, certain factual disputes between the parties using the expertise of Board staff; and (4) requiring parties to submit versions of all filings with the Board that can be read by the opposing party and the public. These new rules have already been a success.

A significant component of the new rules is to increase the involvement of Board staff in the process through technical conferences and regular meetings with the parties. The Board established technical conferences because the parties were spending time and attorney and consultant fees fighting about—and the Board was expending resources to resolve—technical matters over which there should be no dispute, such as the number of miles between a coal mine and a power plant. In the first technical conference (held in the *“Otter Tail v. The Burlington Northern and Santa Fe Railway”* case), disputes over 200 pieces of data were settled in just over an hour. In the past, these disputes would have led to protracted litigation that would have cost the parties thousands of dollars in fees and could have substantially slowed resolution of the case.

Another major component of the new rules was the institution of a 60-day period of mediation at the start of any new case. All parties—railroads and shippers alike—who testified at our February hearing on Ex Parte No. 638 thought mediation would be a useful tool to help them to resolve their rate disputes privately. The first case since the Board adopted these new rules, *“AEP Texas North v. The Burlington Northern and Santa Fe Railway”*, was filed in August 2003, and I am pleased to say that I selected former Congressman John Thune to conduct the initial mediation. During his tenure on Capitol Hill, Congressman Thune served on the Committee on Transportation and Infrastructure, where he was actively involved in matters concerning railroads and their customers. He also served as the State Rail Commissioner in South Dakota. He understands the perspective of both railroads and shippers, and the involvement of a mediator in this matter will help the parties resolve the dispute.

It is important that the process for resolving major rail rate disputes be open and fair, and every party must have an opportunity to make its case so that the Board will have a full grasp of the implications of any actions it takes. In that regard, on September 10, 2003, for the first time, the agency held an oral argument in an individual large rate case (*“Duke Energy v. CSXT Transportation”*). This session was a

productive one both for the Board and for the parties, and we will continue to hold arguments, as appropriate, in future cases.

One significant outgrowth of this focus on rate cases is that recently, as the Board was putting together a decision last week in *"Duke Energy v. Norfolk Southern Railway,"* we realized that we needed to ask the parties to supplement the record, which was incomplete in one critical respect. The same issue arises in two other similar cases. The Board issued an order addressing this situation and is taking additional evidence in all three cases over a 3-week period. A decision in the first case, *Duke Energy v. NS*, will be issued by November 6, 2003.

In sum, while major litigation such as large rate cases is expensive and slow, the Board has made progress in helping to ensure that the rate cases before it proceed faster, cheaper and better. I will make it a priority to continue to make more improvements in this area, and more progress is possible.

b. Small Rate Case Procedures

Since I became Chairman, my top priority has been to provide shippers who have smaller rate disputes an effective forum for resolving such disputes. On April 22, 2003, the Board held an oral hearing on this matter where it received testimony from representatives of shippers, railroads, and unions. In sum, shippers raised the following concerns.

First, shippers contend that the ambiguity of who would qualify to use the small rate case procedures is an insurmountable hurdle that has chilled them from bringing any cases before the Board. Shippers believe that the railroads would fight any shipper's claim that it is entitled to use the expedited procedures, thus tying up the shipper in extensive, expensive threshold litigation. This uncertainty appears to be a major reason why no cases have been brought under the small-case process.

The Board can address this concern and bring some level of certainty to this issue by constructing a test that looks at the size of the shipper and the value of the case. If a shipper or its shipment met that test, the shipper automatically would be eligible to use the small case process.

Second, shippers asked the Board to ensure the expedited consideration of small rate cases and to constrain the discovery process. These shippers argued that protracted resolution of small rate case disputes under our current rules does then no good because the transportation marketplace for such shipments is so fluid. Many shippers have suggested arbitration as a way of resolving such disputes because of its speed and simplicity. Railroads oppose arbitration, since those proceedings are outside of the strictures of the Interstate Commerce Act—which requires a balance between shippers' need for fair rates and railroads' need to achieve revenue adequacy—and could produce inconsistent results. While mandating binding arbitration is beyond the Board's statutory authority, I believe it is unnecessary because the small rate case process being developed should be able to accommodate each side's concerns.

The Board can streamline the discovery and resolution process by creating an administrative process that combines the speed and simplicity of arbitration while ensuring that such cases are decided under the framework of the Interstate Commerce Act. One way for the Board to accomplish these goals is to hire an Administrative Law Judge (ALJ) to hear and decide small rate cases in the first instance. The ALJ would have a prescribed time period for overseeing discovery and for issuing a decision. The ALJ's decision could then be appealed to the full Board. This would allow cases to proceed with the speed and low cost of arbitration, but also ensure that these matters are decided under the principles of the Interstate Commerce Act. In fact, the Board is already working toward hiring an ALJ, and recently received approval to do so from the Office of Personnel Management. The hiring process will be completed once the Board's revised small case regulations are final.

The Board could also establish, resources permitting, a Special Counsel to assist small shippers in evaluating and bringing a small rate case.

The Board could also utilize the discovery and technical conferences now being used in large rate cases in small cases as well.

Finally, shippers and railroads alike have urged the Board to adopt a rate standard for small cases that is clear, unambiguous, fair, and of course, able to withstand legal challenge. The Board promulgated a standard in 1996, but that standard has been widely criticized and—despite having never been applied—was challenged in Court (although the court declined to hear the challenge before the standard is actually applied in a case). Identifying an appropriate standard for the resolution of these cases is our greatest challenge, and while I have asked the parties to provide suggestions to the Board on revising the small-case standard, none has yet done so.

After the hearing, I assembled a team from within the agency to meet with other economic regulatory agencies to gather information on how they handle smaller dis-

putes. Our team talked with other agencies, including the Federal Energy Regulatory Commission, the Federal Communications Commission, the Postal Rate Commission, and the Maryland Public Utilities Commission, in a “best practices” survey to gather information that might inform our ideas.

Unfortunately, the Board has not been able to move forward on this initiative. I have made a judgment that a rulemaking to create a new process for resolving small rate cases is significant enough that I should not take such action as a single Board member, even though I have the power to act alone. Although it is uncertain exactly how the Board’s final proposal will look, I have outlined several key elements of the process and believe that these will form the core of meaningful reform.

2. Bringing Competition to Singly-Served Customers

A common desire of singly-served rail customers is to gain service from a second, competing railroad. Singly-served rail customers who want to be served by a second railroad may work with that railroad to finance and apply for authority to construct a new rail line to the singly-served facility to gain rail competition. The Board’s experience over the past decade has shown that new line construction can bring competition while maintaining the private-sector characteristics of our rail system.

The Board must take two regulatory steps before any such construction can occur. First, it must approve the addition to the rail network. Second, it must conduct any necessary environmental review of the project. The Board has worked hard to expedite consideration of requests to construct rail lines and to approve them when appropriate.

The Board has recently been able to rule on two such proposals. First, the Board approved the construction by the Dakota, Minnesota and Eastern Railroad (DM&E) of a line into the Powder River Basin in Wyoming, which, if constructed, will provide enhanced rail transportation options for coal shippers, particularly in the Midwest. Second, the Board recently approved the construction of a line to provide BNSF access into the Bayport industrial area near Houston, which would provide competition to the large concentration of chemical companies located there.

While build-ins can increase competition and provide many benefits, we have seen recently two examples that demonstrate that at times, the construction of new rail lines can be controversial in local areas. Indeed, both DM&E and Bayport Loop have generated extensive local opposition and spawned court challenges to the Board’s decisions in those cases by various citizen and other groups.

In DM&E, the United States Court of Appeals for the Eighth Circuit reviewed the Board’s decision, and while the Court found the Board had done “a highly commendable and professional job,” it nonetheless remanded the matter to the agency for limited additional consideration of a few environmental issues. We are still studying the Court’s decision.

The Bayport Loop case has produced litigation both in Federal court (where the Board’s environmental review process is being challenged) and in state court (where the City of Houston is resisting the railroad’s attempts to use state condemnation procedures to acquire property needed for the new line). Just last week, the state court in Texas delayed construction, but has yet to issue an opinion in the matter.

Despite these two recent court decisions, the Board is confident that it will prevail in both of these cases. But notwithstanding the litigation that they can generate, construction projects represent the best way to balance the need for greater competition with the importance of preserving the private rail network.

S. 919

Finally, I would like to address S. 919, the Railroad Competition Act of 2003.

Taken as a whole, S. 919 would fundamentally change the economic model of the railroad industry and is unwise. Not a single one of our major railroads is revenue adequate, and if enacted, S. 919 would call into question the continued economic viability of our freight railroad system. While some shippers may realize a short-term gain from lower rates, in the long run this legislation, if passed, could significantly degrade our Nation’s freight rail network, to the detriment of all of its users. Although the Nation’s privately funded railroad system may have some problems, it is the best freight railroad system in the world, and the United States is the only country with a national freight rail network that does not need taxpayer subsidy.

Most of the provisions of this legislation reflect unhappiness with the Board and certain of its regulatory doctrines. I have met with most of the supporters of this legislation, and they almost all agree that they would not be calling for this legislation if the Board had interpreted certain provisions of the Interstate Commerce Act differently. But the individual provisions in the bill are less significant than the underlying concerns that gave rise to the introduction of this legislation. Since I have

become Chairman I have worked hard to understand the core concerns of captive shippers and the railroads that serve them.

First, many shippers neither understand nor have confidence in the Board. My most important initiative as Chairman has been to win that confidence through openness and dialogue. During my nomination and confirmation process, there was a great deal of concern expressed about the lack of transparency at the STB. Since I have become Chairman I have taken several steps to change this perception, including restoring regular voting conferences on cases; holding hearings on significant matters such as large rate cases and small rate cases, and on individual cases pending before the Board such as the "Highline" case in New York and the "Kansas City Southern/Tex Mex" merger proposal; and most recently holding the Board's first ever oral argument on a large rate case.

This summer, the Board also held an open house for practitioners to introduce our staff to them and explain how our agency processes cases. I have an open door policy for meetings and have met with many shippers and railroads. I have traveled extensively in the past year to better understand rail transportation. While these may seem like small steps, they have gone a long way to help our agency's stakeholders understand how and why the Board makes its decisions.

Second, many disputes between shippers and railroads often take on a life of their own because of the way shippers feel they are treated by the railroads. Rail customers often conclude that while rates are high, the railroads' service and attitude are bigger problems.

Rail customers are primarily wholesale enterprises who are themselves industrial and manufacturing companies or producers of goods. Like railroads, these shippers are capital intensive and work on thin profit margins. They have customers who demand top-notch service and low prices, and they have suppliers from whom they demand the same. All operate in a brutally competitive global marketplace. These companies understand the financial pressures railroads are under, but they feel that they are not treated by the railroads the way they would treat their own customers. This has led some shippers to assume that railroads act this way because they are monopolies and to believe that legislation like S. 919 would introduce more competition into the rail network and force railroads to be more responsive to them.

Railroads should work harder to operate in a more customer-friendly fashion, and I am working with all of our major rail carriers to impress upon them the importance of doing so. Railroads must be nimble competitors in the transportation marketplace to increase their business and grow their revenues. While the leadership of each of the major railroads understands this, that attitude does not always translate through their entire organizations. The good news is that in many circumstances railroads have worked with their customers to improve efficiency and take costs out of the supply chain to the benefit of both parties. But these examples are not common enough, and they must become the norm, not the exception.

Helping railroads improve their operations to provide better service is one goal that carriers, shippers and policy makers all share. The Board has been instrumental in bringing the railroads, the city and the state together to improve operations and devise a capital plan for improving operations in the Chicago terminal area. Approximately one-third of all rail shipments go through Chicago at some point in their journey. Improving Chicago and other rail gateways will allow for faster, more reliable shipments, to the benefit of all.

Third, a fundamental underpinning of S. 919 is that very few rail shippers feel the Board provides an effective regulatory forum in those instances when carriers and shippers cannot privately resolve their differences and the shipper has no effective recourse.

Although the agency tries to help parties informally resolve their differences and improve relations between railroads and their customers, the Board has to be an effective regulatory backstop when a dispute over rates and services is formally brought before the Board. No cases have ever been brought under our small rate guidelines. This may be because there are no smaller rate disputes, or because there is something in the Board's rules that discourage shippers from bringing such cases. If no small cases are brought, this means that in practice, only about 75 coal shippers have a meaningful opportunity to challenge rail rates. This is unacceptable.

At the same time, we must recognize that the economic relationship between shippers and carriers is complex. In many cases, shippers have many facilities—both captive and competitively served—and ship to numerous destinations on several railroads. While the legislation seeks to simplify the shipper-carrier relationship, in reality the relationships between shippers and carriers are enormously complicated and not easily understood. Many shippers do have economic leverage with railroads when the totality of their relationship is considered, and the legislation takes no account of this reality.

A more accessible process for bringing small rate cases can be achieved through procedural reform at the Board, rather than through an overhaul of the substantive regulation of railroads. Real reform is possible, and the Board is working to identify the steps in the process that are the problems and develop reforms to address those problems.

Finally, certain areas of the country are disproportionately dependent on rail service in general, and on a single rail carrier in particular, for its economic health. Many who are from the upper Midwest feel that, because of the importance of producing bulk, commodity-based products to their states' economies, their region's economies are particularly dependent upon the business practices of a single railroad.

The Board must pay close attention to the unique set of concerns of rail shippers in that part of the country. I recently traveled to North Dakota and met with a number of government officials, shippers and producers. I have spoken numerous times with the railroad that primarily serves that area about the issues raised there. The issues faced in that part of the country are complex, and not easily solved. However, attention—and not legislation—is the best way to resolve the issues faced there, and while attention may not solve every problem, significant progress is possible.

Conclusion

One of my goals as Chairman of the STB has been to ensure that the agency's processes work as well as they can. The first step was to open up the Board. The Board has taken steps to streamline the process for large rate cases, steps which are already working. The Board will continue to reevaluate and refine how the parties and our staff work through the large rate cases. The next step is to improve the agency's small rate case process.

I believe that the Board can and will do a better job to address the concerns raised by captive shippers. The reforms outlined today—and not substantive changes to the statutory scheme—are the best way to address the concerns raised by captive shippers while maintaining a healthy freight rail network. It is a difficult balance, but one that can be achieved.

I appreciate the opportunity to discuss these issues today, and look forward to any questions you might have.

Senator HUTCHISON. Thank you very much, Mr. Nober.

Our second witness is Mr. Terry Whiteside, Representative of the Montana Wheat and Barley Committee and Chairman of the Alliance for Rail Competition.

STATEMENT OF TERRY C. WHITESIDE, REPRESENTATIVE, MONTANA WHEAT AND BARLEY COMMITTEE, AND CHAIRMAN, ALLIANCE FOR RAIL COMPETITION

Mr. WHITESIDE. Thank you, Madam Chairman, and I appreciate the opportunity to appear here, and thank you—

Senator BURNS. Pull the mike up closer to you.

Mr. WHITESIDE. And thanks to all the Committee Members.

Since the passage of Staggers in 1980, the rail freight industry has undergone radical change in the number of operators. It has in some ways adapted to this new century, but in other ways it has not. In keeping with the old practices in the way it treats captive shippers, the freight rail industry has chosen short-term profit over healthy evolution and an open American marketplace.

Some results of this tenacious hold of the past have been for freight market shares for the railroads to decline and overall growth to be hindered. In 1980, the rail freight industry was a \$28 billion industry. Today it is a \$34 billion industry. Over the course of 20 years, that is not impressive growth. The railroads in 1980 originated about 1.4 billion tons. 20 years later, they originate just over 1.7 billion tons—a 20 percent increase or about 1 percent per year.

The railroads are not the villains here. They are doing exactly what the law as interpreted by the regulatory body allows. The concentration by merger in the rail industry has changed the balance. The issue here is competition, the issue of fairness that comes from competition. The issue is that the railroad Federal law that was designed to protect the U.S. public from monopoly market abuse does not work. The law needs fixing to restore the balance.

In my written testimony I give evidence of service and rate problems, abuse from market domination of whole industries by single railroads. We believe that the freight rail marketplace does not behave like a marketplace at all. There are Federal protections for railroads that do not exist in any other industry, such as antitrust exemptions.

In addition, we believe that over the years the regulatory mechanisms have skewed the intent of Congress when it passed the Staggers Act in 1980. The statute says in part that the policy of the U.S. Government is “to allow, to the maximum extent possible, competition in the demand for service and to establish reasonable rates for transportation” and “to maintain reasonable rates where there is an absence of competition.”

Evidently, the regulatory agency has not kept this Congressional intention in mind—of course I am sitting right next to the chairman—when issuing rulings and interpretations since 1980.

Let me say a word about the intent of captive rail customers that I speak for here today. Since we are captive to the railroads, we are also dependent on the railroads. Captive rail customers are the last ones who would ever want to see harm come to the availability of rail service or for further contraction of the rail system.

S. 919 is not a reregulation bill. S. 919 does not cap rates. S. 919 does not mandate open trackage rights. We believe S. 919 will initiate the necessary reforms to bring competitive forces and establish the goals of the captive shippers and consumer public that they want and need.

What do we want? A safe, growing, financially strong rail industry. We want elimination of the monopolistic practices by furthering the direction developed in the Staggers Rail Act, and we want cooperative innovation and creativity driven by rail to rail competition.

We simply do not believe this mighty historic industry cannot function in a competitive American marketplace, as do all other businesses in this country. We believe, and studies have confirmed, that competitive conditions will produce greater volumes and market shares for the railroads. Will the railroads have to adapt to the passage of S. 919? Of course, just as we have all had to adapt to conditions dictated by free markets and the global economy. We believe it is unhealthy to have railroads operate in the current federally sheltered environment. This artificial habitat is unhealthy for shippers and it is unhealthy for railroads.

Railroads may say here today they cannot survive in an S. 919 world, in other words a world in which competition drives price, not captivity. If that is true, if it is true that an American industry cannot survive without these kinds of unfair and noncompetitive market practices, then the whole issue bears an even closer examination. In that case, it would seem to me that you as policymakers

have an amplified responsibility to consider the long-term solutions to bring balance to the parties, including the consuming public which pays for all of this.

We will hear today all kinds of dire predictions of what will happen if Congress acts. But what happens if Congress does nothing? Is this, the rail business plan, a long-term business strategy that can sustain itself? The current mode of operation has not produced a panacea in the 23 years since Staggers was passed, even with massive concentrations.

While the wheat and barley groups along with ARC and the coalition of shipper groups support S. 919, we know there may be better ideas out there. In an ideal world, we would like to join in an effort find solutions which includes all parties, certainly including the railroads. But we do not believe that something substantive—we do believe that something substantive must be done.

The day has long since passed when anybody can credibly say that there is no problem or that things are just great the way they are. For those of you who make policy to avoid acting will only produce a larger problem as time passes, and, given time, the problems will certainly be larger, they will certainly be more complex, and they will be certainly more expensive to fix. The time to begin solving is now.

Madam Chairman, I would like to thank you once again for the opportunity to testify here today. It is an honor on my part. I would also like to request that my written testimony and oral statements be made a part of the record, and I would be happy to answer any questions. Thank you.

[The prepared statement of Mr. Whiteside follows:]

PREPARED STATEMENT OF TERRY C. WHITESIDE ON BEHALF OF MONTANA WHEAT & BARLEY COMMITTEE, WHEAT AND BARLEY COMMISSIONS IN COLORADO, IDAHO, SOUTH DAKOTA AND WASHINGTON, OREGON WHEAT GROWERS LEAGUE, THE ALLIANCE FOR RAIL COMPETITION

Madam Chairwoman and members of the Subcommittee, thank you for the opportunity to testify before you today. My name is Terry Whiteside, Principal in Whiteside & Associates, Billings, Montana and I represent many farm producer groups, including the Montana Wheat and Barley Committee, the Wheat and Barley Commissions in Colorado, Idaho, South Dakota and Washington as well as the Oregon Wheat Growers League. The Montana Wheat and Barley Committee is a wheat and barley producer check-off organization representing all Montana farm producers. The Idaho Wheat Commission and Idaho Barley Commission represent all of the Idaho wheat and barley producers, respectively. The Colorado Wheat Administrative Committee represents wheat producers in Colorado. The Oregon Wheat Growers League represents the wheat producers in Oregon. The Washington Wheat Commission and the Washington Barley Commissions represent the wheat and barley producers in Washington.

The Alliance for Rail Competition (ARC) is a diverse coalition of shippers that was formed five years ago for the sole purpose of developing and promoting a consensus-based plan for achieving rail-to-rail competition. I serve as Chairman of that organization. Concerns about railroad market power span all rail dependent shippers and industries. ARC's growing membership reflects the diversity of those interests: agriculture, coal, chemicals, consumer products, glass producers, industrial products, minerals and petrochemicals, and some of the trade associations that represent many of these groups, as well as port and industrial development authorities. ARC has teamed up with 12 other national organizations to combine our work efforts to bring rail competition back to this industry. These other organizations have pledged to work together in their support for S. 919: Agriculture Ocean Transportation Coalition, American Chemistry Council, American Public Power Association, Consumer United for Rail Equity, Edison Electric Institute, National Association of Wheat Growers, National Barley Growers Association, National Petroleum Refiners Asso-

ciation, National Rural Electric Cooperative Association, Paper and Forest Industry Transportation Committee, The Fertilizer Institute, and The National Industrial Transportation League.

The Heart of the Issue Is Choice

The heart of this issue is the lack of choice for vast numbers of rail customers. The issue is not about excessive rates, poor or erratic service or monopoly practices. They are the symptoms of the problem. The issue continues to be lack of choice for rail customers in the marketplace.

S. 919 is not a re-regulation bill. It does not re-regulate any part of this industry.

S. 919 Does NOT cap rates

S. 919 Does NOT mandate open trackage rights.

S. 919 Does four major things:

1. S. 919 reestablishes that the National Rail Policy is pro-competition to ensure and nurture competition in this vitally important industry.
2. S. 919 restores several provisions that Congress established in 1980 in the *Staggers Rail Act* to their original intent and purpose taking out the intervening agency interpretations that have altered original Congressional language and intent (Railroads must quote rates between any two points on their system and removal of the anti-trust provision in terminal area and switching).
3. S. 919 establishes a final offer arbitration concept being utilized successfully in Canada to bring opportunities for resolutions of disputes on rates or service to rail customers.
4. S. 919 recognizes that with concentration in the rail industry, Congress needs to establish a concept called Areas of Inadequate Rail Competition with advocacy and oversight to focus remedial attention to bring about more competitive balance in market place.

In short, S. 919 restores Congressional language and intent that The Staggers Rail Act sought in 1980. It incorporates an arbitration process that is being successfully utilized in Canada for resolution of carrier/customer issues. It reestablishes for the STB that a competitive rail industry is preferable to a non-competitive rail industry.

Congress has taken a look at many other industries that have been characterized by a monopoly or oligopoly market structure and has seen it necessary and appropriate to introduce competitive balances for the sake of national policy.

Yet, we have seen no real action to address similar issues in the railroad industry. In this national railroad industry in 2001, four mega carriers generate 95 percent of the gross ton-miles and 94 percent of the revenue. Two western carriers generate 92 percent of the gross ton-miles and 90 percent of the revenues in the west. Four of these carriers handle over 90 percent of the U.S. coal movements. Three of these carriers control over 70 percent of the grain movement.

In other industries of national importance, Congress has moved to introduce competition as the best means for ensuring consumer and customer protections. Those industries include the natural gas pipeline industry, which like the rail industry, is characterized by high fixed costs. The shipping community—of which as many as 1/3 or more of our shipments are captive—is here today to ask you to bring competition to the rail industry as the best means of protecting our collective economic competitiveness.

The 1980 Staggers Rail Act Was A Rail Competition Bill

When the Staggers Rail Act was passed in 1980, shippers understood that regulation of railroads was to be curtailed, and instead, “to the maximum extent possible,” competition was to ensure that rail rates were and remained reasonable. Congress passed a very good piece of legislation in the Staggers Rail Act but its effects have been thwarted by both regulatory interpretation and a massive concentration in the rail industry. The Staggers Rail Act passed by this Committee was intended to foster a competitive railroad system in this country. S. 919 attempts to restore those provisions.

Today, *whole states, whole regions and whole industries* are now captive to a single railroad. Such concentration comes at a time when the regulatory body which approved all of these mergers and allowed this massive concentration of economic power has seemingly chosen to ignore the effects of this concentration on the ever-increasing captive rail customers, even though Congress charged this agency to

“maintain reasonable rates where there is an absence of effective competition.” Congress in 1980 never envisioned that 40 Class I’s would be allowed to merge into the a system where four major railroads control the industry and there would be no effective backstop for the captive rail customers to shield them from the effects of monopoly pricing. Congress clearly wanted a healthy rail system full of innovation that was driven by rail-to-rail competition. The ICC and now the STB has continued to alter and undermine the spirit of the law by regulatory interpretation.

In 1980, there were over 40 Class I railroads operating in the U.S. Further the 1980 Staggers Rail Act specified that the regulatory agency, the Interstate Commerce Commission was to “maintain reasonable rates where there is an absence of effective competition.” In other words, if a rail customer found that rail-to-rail competition became ‘absent’ it was Congressional intent that they would have protection from predatory pricing and service abuse. The ICC, now the STB was also charged by Congress to work to see that the financial health of the national railroad system improved and of course, the Congress did not want to see any more railroad bankruptcies.

Montana Agricultural Producers Need Bulk Transportation To Transport Grain To Market And Are Completely Captive To A Single Railroad

The Montana Wheat & Barley Committee (MWBC) represents the wheat and barley producers of the state of Montana. Montana is a natural resources state with the main economies built upon products of the mine, lumber and agriculture as well as tourism. In order for our bulk products of the mine, lumber and agriculture to have value to Montana citizens, they require bulk transportation (rail) to points outside Montana and, in many cases, outside the U.S.

Therefore, the state’s economic survival depends on having access to good, affordable, and adequate rail transportation and attendant facilities so that its shippers can deliver a competitively priced product outside the state boundaries.

*Montana wheat and barley producers do not have economic alternatives to rail transportation. They are captive and tied to rail with no viable alternatives to movement by rail. The Montana wheat and barley producers are unique because **they are the bearers of the freight** and cannot pass on increased transportation costs, but must absorb them.* Virtually any other industry has some capability of passing on some or all of its increased costs to their consumers or customers. The farm producer is unique because they operate in an environment where they do not have any control over the price they receive for their crop and they must bear every increase, in all costs, including transportation costs, without any possibility to pass those higher costs on to anyone else. When farm producers sell their grain to a grain elevator or merchandiser the price of rail transportation is deducted from the price the farm producer receives. Thus the farm producer “bears” the rail transportation cost. The grain producer pays the transportation charges they collect from the farm producers to the railroads. The farm producers are very sophisticated marketers and producers. U.S. farmers are the most efficient and productive agricultural producers in the world. But they must compete in a world market most of which do not have a monopoly rail transportation system between the producer and the ultimate market that can dictate price and profit levels to the producer. One of the challenges for Montana grain producers comes from international competition as well as domestic competition. Most industries that utilize rail face both domestic and international competition. Montana grain producers understand that a lack of choice of rail carriers creates a burden on their ability to competitively market their products in the world.

Montana’s Primary Transportation Is A Single Railroad

Montana is a base industry state. In the 1800s, its chief industries were mining, lumber and agriculture; today and in the future, Montana’s chief industries will be the same three industries: mining, lumber and agriculture with the addition of tourism. Today, we, in Montana, have one major railroad, operating as a monopoly in the transportation of bulk commodities from the farm to market.

Outline of Industry in Montana

- The wheat industry in Montana is characterized by an export-dominant rail movement.
- The barley industry in Montana is characterized by both an export and domestic market dominated by rail.
- The lumber industry in Montana is characterized by both an export and domestic market dominated by rail.
- The coal industry in Montana is characterized by domestic rail movement.

Montana is nationally ranked in agricultural production. Montana ranks 4th in all wheat production, 9th in winter wheat production, 2nd in spring wheat production, 3rd in barley production, and 4th in durum wheat production in the U.S. (Source: Montana Agricultural Statistics Service, May, 1997 Census of Agriculture). Montana is 2nd in Land in Farms and Ranches with about 60,000,000 acres.

For the Montana farm producer, the cost of transporting grain can today represent as much as one third (1/3) the overall price received for the grain up from only 15 percent 25 years ago when Montana had rail competition.

Montana Rail Transportation Is Predominated By One Carrier

Montana's rail infrastructure is controlled by a single rail carrier controlling over 96 percent of all rail miles, over 95 percent of all grain elevator and terminal sites and move 98 percent+ of all wheat movements from the state. The rail carrier controls and dictates the rail rates in all movements from Montana eastbound or westbound. Annually, the Montana producers in normal rainfall years move about 150 million+ bushel production that is handled by rail from Montana and bear about \$200+ million in freight transportation charges per year.

Montana grain producers are being required to pay more for their rail service than their counterparts in the grain producing industry where effective rail-to-rail competition exists. That payment has come in the form of increased transit times, upward adjustments in rail rates and tight car supplies.

From Plentywood, Montana to Portland, Oregon, it is 1,207 miles on the BNSF. From Nebraska origins, e. g. Sidney, Nebraska to Portland, it is 1,566 miles on the BNSF. To ship a 52 car shipment of wheat from Plentywood to Portland, is \$67/car (\$3,484) more than to ship a 52 car shipment of wheat from Alliance, *NE even though Alliance is 359 miles further from Portland than is Plentywood*, and even though the trains from Alliance pass right through Montana on there way to Portland. Why? In Central Nebraska, e.g., the Sidney area of Nebraska, the BNSF has rail competition from the UP for its wheat traffic going to the same destination—Portland, but in Montana, the BNSF has no competition.

This is modern rate discrimination that has gone on for many decades. The graph below show the revenue to variable cost that emanate from the rate differential between Nebraska origins (where BNSF and UP compete) and Montana, Idaho, South Dakota and North Dakota origins (where there is also no rail-to-rail competition).

The wheat rates, from Western Nebraska are not river compelled rates, but rather are compelled by competition between two railroads on movements to the Pacific Northwest (PNW).

Rate spreads between Montana origins and Nebraska origins to Portland have increased since the passage of the Staggers Rail Act of 1980. The result is that Montana, Colorado, Idaho, South Dakota, North Dakota and Washington farm producers are worse off today against their traditional competitors due to their increased captive shipper status which results from the lack of choice of carriers.

The captive rail customers in the grain country are paying rail rates which range from 200 to 400+ percent of revenue to variable costs well above the 180 percent threshold of unreasonableness established by Congress in the Staggers Rail Act.

Captive Rail Traffic in the U.S. Now Comprises 1/3 of All Shipments

The result of a June 1998 study conducted by L.E. Peabody & Associates, Inc. reflects quantitatively the amount of rail captivity. Fully 1/3 of all U.S. rail movements are captive and it is spread over virtually all major shipping commodity groups.

Peabody found that for movements included in the 1996 Costed Carload Waybill Sample:

- Over 31 percent of the revenue was generated by "captive rail traffic;"
- Captive rail traffic on average has a revenue/variable cost ratio of 2.44; and,
- Movements of captive rail traffic were comprised of 129 different industry groups including coal, agriculture, chemicals, fertilizers and many manufactured goods.

Whole States, Whole Regions and Whole Industries Are Now Captive

Today, whole states, whole regions and whole industries are now captive to single railroad practices. Such concentration comes at a time when the regulatory body which approved all of these mergers and allowed this massive concentration of economic power has seemingly chosen to ignore the effects of this concentration on the ever-increasing captive rail customers, even though Congress charged this agency to "maintain reasonable rates where there is an absence of effective competition." Congress in 1980 never envisioned that 40 Class I's would be allowed to merge into the a system where four major railroads control the industry and there would be

no effective backstop for the captive rail customers to shield them the effects of monopoly pricing and service abuses. Congress clearly wanted a healthy rail system full of innovation that was driven by rail-to-rail competition. The ICC and now the STB has continued to alter and undermine the spirit of the law by regulatory interpretation.

Upon its inception in January 1996, the new Surface Transportation Board was faced with the products of the ICC's regulatory policies: a drastically consolidated rail market place and grave concerns from the shipping community about the growing level of monopoly rate abuse and deteriorating service levels. But the new STB also had a choice. At that time, the STB could have chosen to protect the shipping community from growing rail market dominance and begin to balance the scales between shippers and the railroads by promoting a competitive rail market—either by modifying existing regulatory rulemakings or requesting changes to its statutory authority—or it could continue the record of its predecessor, approving virtually any proposed merger and defining the success of its decisions based upon the success of its lawyers in the appeals court.

Based on its record, it is clear what choice the STB made. Not only did the STB in 1997, approve the largest parallel merger of two railroads in history in the name of “efficiency” –a merger that produced service deterioration unprecedented in the annals of railroad history—but it also handed down the now-legendary “bottleneck” decision and continues to wonder why shippers are reluctant to bring “competitive access” cases despite significant law and precedent that was promulgated under the ICC.

The Issue Is Not About Railroad Rates, Service or Thwarting Economic Development—The Issue is that Federal law Does Not Protect the U.S. Public from Monopoly Practices

The issue here is not about rates, or service or thwarting economic development by market dominant railroads. The examples of monopoly pricing and control are legion whether it is jeopardizing the economic development plans of a truck assembly plant in Texas, or a chemical plant in Louisiana, a fructose sugar plant in North Dakota and Minnesota that wasn't allowed by the railroads to be built, plant closings in Idaho due to rail transportation costs or rate and service issues all across the grain states. The railroads are not the villain here. They are doing exactly what the law, as interpreted by the regulatory body, allows. The concentration by merger in the railroad industry has changed the balance. The issue here is competition. The issues are of fairness that comes from competition. The issue is that the Federal law that is designed to protect the U.S. public from monopoly market abuse does not work. The law needs fixing to restore balance.

The agricultural producers have supported the Alliance for Rail Competition since its inception. They have worked hard to bring together a multitude of shipper organizations whose common bond is the belief that increasing competition in the railroad industry is the right thing to do. They believe that a continuation of the status quo is unacceptable, and that changes to existing regulatory policies must be legislated to ensure that the STB will begin to promote competition as originally directed and intended by the 1980 Staggers Act. Therefore, ARC and the Montana Wheat & Barley Committee and the agricultural rail customers urge this committee to pass S. 919 which will restore major portions of the Staggers Rail Act to their original state and further serve to promote the reemergence of competitive forces within the rail industry.

As I've noted before, the members of the Alliance for Rail Competition believe that the only real long-term solution to their concerns about rates and service quality is increasing competitive choice in the market place.

But how do you achieve free market competition in an industry that has only four major U.S. Class I railroads—two of which are in the West, and two in the East? ARC believes that S. 919 will initiate the necessary reforms to bring competitive forces and establish the goals that the captive rail customer community wants:

- *a safe, growing and financially strong rail industry*
- *elimination of monopolistic practices by furthering the direction developed in the Staggers Rail Act*
- *cooperative innovation and creativity driven by rail-to-rail competition*

Today, railroad customers do not have the right to any of these things—and in fact, based on the way existing regulations have been interpreted, they barely have the *right* to anything at all.

S. 919 Issues:

Competitive Reciprocal Switching and Terminal Trackage Rights—The Congress should provide increased rights to competition through reciprocal switching and terminal trackage rights, affirmatively requiring the grant of these rights within an established distance of existing interchanges in order to promote rail-to-rail competition.

Under the current statute, the STB is empowered to grant trackage rights and reciprocal switching in a terminal or for a “reasonable distance” outside of a terminal, when it finds such remedies to be “practicable” and “in the public interest,” or where reciprocal switching is necessary to provide “competitive rail service.” These rights, which are set forth at 49 U.S.C. 11102, have been in the statute for a number of years and were broadened in the Staggers Rail Act.

Despite these broad and seemingly pro-competitive provisions, the agency, by rule and policy, has drastically restricted the application of these rights. The agency’s rules, promulgated in 1984, have been interpreted in the *Midtec* decision (1984) and later cases to require the shipper to prove competitive “abuse” in order to qualify for competitive relief, and raise numerous other barriers. In fact, a shipper has never won a case brought under the current rules, and the precedent set by the half-dozen or so cases decided to date establish tests that no shipper could possibly meet.

We recommend that legislation reversing the agency’s approach should be adopted. This will reestablish what Congress intended in the Staggers Rail Act. The agency should have an affirmative obligation to establish competition via reciprocal switching and trackage rights at or within a reasonable distance of an existing interchange between rail carriers, and the “abuse” test established by the agency should be specifically abolished.

A substantially broadened right to competition via reciprocal switching or trackage rights would provide the benefits of competition to a number of shippers, where such shippers are at or within a reasonable distance of another carrier. Because such trackage rights would be limited to rail service at or within a reasonable distance of where two carriers already interchange cars and locomotives, such competitive rail service would be operationally feasible. Trackage rights are frequently used by carriers: indeed, as part of the UP/SP merger, the UP/SP granted the BNSF of 4,000 miles of trackage rights over its system. Our recommendations would require the agency to interpret the statute in a pro-competitive, rather than a restrictive, manner, where relatively short-distance trackage rights or switching can provide competitive opportunities.

Shipper’s Right to Competitive Routings and Reasonable Rates Over Bottlenecks — The Congress should restore to shippers the right to competitive rail routing through existing interchanges to encourage rates produced by the competitive market, and should require the provision of reasonable rates in a timely manner over rail bottlenecks.

In the agency’s 1996 “bottleneck” decision, the STB ruled that, in most situations, a rail carrier with a “bottleneck” monopoly can lawfully foreclose alternate and competitive rail routings by another carrier, where the “bottleneck” carrier can provide origin to destination service. This interpretation altered what Congress had intended in the Staggers Rail Act in 1980.

The STB’s bottleneck decision should be reversed legislatively, to restore to shippers the right to route over competitive routings at rates produced by the competitive market through existing interchanges, and to clarify that the STB can establish a maximum reasonable rate over a bottleneck segment. These changes would ensure that the monopoly bottleneck carrier couldn’t take advantage of its pricing power to foreclose competition over the competitive portion of the route. They would permit competition to flourish where it can. These changes would not bring a return to the old “open routing” system, whereby carriers were required to keep even inefficient interchanges open and were required to charge the same rate over all possible routes. Rather, only interchanges already utilized by the carriers would qualify, and rates over various routes would vary as costs and competition demand. Where a carrier controls a bottleneck, its pricing initiative would only be subject to current statutory restrictions against charging unreasonably high rates where there is no effective competition.

Finally, the Congress should also reverse the bottleneck decision to clarify that the STB can prospectively prescribe a maximum reasonable rate so that the rate is available to a shipper immediately upon expiration of the shipper’s contract.

Competition and Reasonable Rates—The Congress should require that significant weight be given to the level of rates produced in the presence of rail-to-rail competition for shipments of the same or similar commodities when reasonable rates are prescribed where effective competition does not exist. Congress should also adopt objective, easy to apply rate standards for agricultural shippers, and direct the STB to consider similar standards be considered for other non-coal shippers.

Under the STB's current so-called "Constrained Market Pricing" standards, the STB requires shippers to hypothesize the rates that would be produced if a new railroad were built from the ground up to serve the complaining shipper in competition with the existing carrier. This exercise in "imagining" a new railroad—the calculation of so-called "Stand Alone Cost"—requires massive amounts of evidence as to such things as the cost of land acquisition for this new "stand alone" carrier, the cost of track, locomotives, operating costs, etc. Hundreds of thousands of dollars can be spent in legal and consultant fees on this exercise in competitive hypothesis. In the McCarty Farms case filed by Montana producers, the ICC/STB took 19 years and cost the producers over \$3.2 million (without lawyer fees). The result even though the railroad was judged market dominant and its rates judged excessive, the ICC changed the judgment standard three times to ensure the complainants never succeeded even though the rates were 200–300+ percent of variable—again well in excess of the 180 percent standard for unreasonableness. This was not the ICC/STB's finest hour but it is illustrative of the pervasive of the problems faced by captive rail customers.

Yet, throughout the process of determining what a maximum rate should be to a captive shipper, the STB never considers what that same carrier is already charging shippers for movements of the same commodity where rail-to-rail competition actually exists.

This "never-never land" of regulation should be injected with a dose of reality.

Congress should require the STB, in determining what rate should be charged where there is an absence of competition, to consider like rates that are actually charged where there is the presence of competition. The STB should give significant weight to this evidence, though other types of evidence, such as evidence on stand alone cost current utilized by the Board, could be considered as well.

Finally, ARC recognizes that agricultural shippers, and especially the smaller agricultural shippers, have particular difficulties in bringing maximum reasonable rate complaints, given their size and the circumstances of their transportation. The Congress should establish and mandate the STB develop such standards, particularly for small agricultural shippers, and should direct the STB to consider similar standards for other non-coal shippers.

Increasing Rail-to-Rail Competition from Short Line Carriers—The Congress should make unlawful any restrictions by Class I carriers on short line carriers from interchanging with other carriers.

The railroads will state that they have, by spinning off branchlines into shortline carriers, created a more balanced and competitive system. This just is not true.

Since the passage of the Staggers Act, short line carriers have become an important part of the nation's rail transportation system. ARC believes that Congress should make statutory changes that would enable short line carriers to facilitate increased competition in the rail industry.

Short line carriers are often "captive" to a particular Class I carrier. Frequently, however, this captivity is not due to the fact that a particular short line connects solely to one Class I carrier, but rather is the result of restrictions placed upon the short line at the time that the newly-established Class III is "spun off" by the Class I parent. Specifically, when a planned short line can interchange with a carrier besides the Class I parent, restrictions are placed on the short line at the time of its spin-off that prevent the short line from interchanging with any carrier other than the Class I parent. Shippers served by the short line, then, are held captive. The Class I parent obtains the benefits of the short line spin-off, including lower labor costs, without jeopardizing its hold on its captive shippers.

This is poor public policy. ARC and the agricultural rail customers believe that Congress should make unlawful any restrictions by Class I carriers that prevent short line carriers from interchanging with other carriers. A legislative prohibition on such restrictions would free both shippers and short lines from the control of a particular Class I carrier, bringing the potential for increased traffic to the short line, and the potential for increased competition to the shipper.

Summary

We believe that the freight rail marketplace does not behave like a marketplace at all. There are Federal protections for railroads that do not exist for any other industry, such as anti-trust exemptions. We have shown in this testimony that the regulatory mechanism has skewed the Congressional intent that Congress relied upon when it passed the Staggers Rail Act in 1980.

We, as rail customers, are captive to the railroads and we also dependent upon the railroads. Captive rail customers are the last ones that would ever want to see harm come to availability of rail service or further contraction in the rail industry.

We simply do not believe that this mighty and historic industry cannot function in a competitive American marketplace, as do all other businesses in the country.

We believe that competitive conditions will produce greater volumes of traffic and market share for the railroads. Our studies confirm this belief. We believe that it is unhealthy to have railroads operate in the current federally sheltered environment. This artificial habitat is unhealthy for rail customers . . . and unhealthy for railroads too.

Railroads may say here today that they cannot survive in an S. 919 world. In other words, a world in which competition drives prices and innovation, not captivity. If that is true . . . if it is true that an American industry cannot survive without these kinds of unfair and non-competitive market practices, then the whole issue bears even closer examination.

Congress has taken a look at many other industries that have been characterized by a monopoly or oligopoly market structure and has seen it necessary and appropriate to introduce competitive balances for the sake of national policy. The consuming public ultimately pays for all of this.

Yet, we have seen no real action to address similar issues in the railroad industry. In this national railroad industry, four mega carriers generate 95 percent of the gross ton-miles and 94 percent of the revenue. Two western carriers generate 92 percent of the gross ton-miles and 90 percent of the revenues in the west. Four of these carriers handle over 90 percent of the U.S. coal movements. Three of these carriers control over 70 percent of the grain movement.

In other industries of national importance, Congress has moved to introduce competition as the best means for ensuring consumer and customer protections. The shipping community—of which as many as 1/3 or more of us are captive to only one railroad—is here today to ask you to bring competition to the rail industry as the best means of protecting our collective economic competitiveness.

For the record, characterizing such changes as “reregulatory,” as the railroads have done, would require that no regulatory system exist at all. That clearly is not the case as in July, 2003, two months ago, this Subcommittee took up the issue of reauthorization of the regulatory body empowered to oversee the railroad industry. ARC and the agricultural rail customers are interested in promoting market-based competition as a long-term replacement for regulation, and in order to achieve that end, existing regulations must be reformed to encourage the gradual re-emergence of competition.

Clearly, there are areas where the STB itself can make immediate improvements within the parameters of authority already granted by existing statutes. To date, however, STB decisions have demonstrated either an unwillingness or inability of this body to include the legitimate measurement of competition in its deliberations. It is for this reason that the Alliance for Rail Competition and the agricultural rail customers believe that these issues must be addressed legislatively. Captive rail customers will continue to advocate the passage of legislation that will encourage competition in the rail market place in both the short and long-term.

While the wheat and barley groups, along with ARC and the coalition of rail customer groups support S. 919, we know that there may be better ideas out there. In an ideal world we would like to join an effort to find solutions, which includes all parties, certainly including the railroads. But we do believe that something substantive must be done. The day has long since passed when anyone can credibly say that there is no problem, or that things are just great as they are. For those of you who make policy, to avoid acting will sure produce problems that will be larger, more complex and more expensive to fix. The time to begin solving this is right now.

Madam Chairwoman, I'd like to thank you once again for the opportunity to testify before you today about these important issues. I'd also like to request that both my written and oral statements today be made a part of this hearing record.

Thanks for your consideration, and I'd be happy to answer any questions that you may have.

Senator HUTCHISON. We will receive everyone's written testimony for the record.

Our next witness will be Mr. Charles Platz, the President of Basell North America, Inc.

**STATEMENT OF CHARLES E. PLATZ, PRESIDENT, BASSELL
NORTH AMERICA, INC., ON BEHALF OF CONSUMERS UNITED
FOR RAIL EQUITY AND AMERICAN CHEMISTRY COUNCIL**

Mr. PLATZ. Thank you very much, Madam Chairman. I would like to add into the record letters from members of the ACC supporting S. 919.

Senator HUTCHISON. Without objection.
[The material referred to follows:]

AIR LIQUIDE AMERICA L.P.
Houston, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Chairperson,
Subcommittee on Surface Transportation and Merchant Marine,
Committee on Commerce, Science, and Transportation,
United States Senate,
Washington, DC.

Dear Senator Hutchison:

I am writing in support of S. 919, the Rail Competition Act of 2003 and to inform you about the economic disadvantage that Air Liquide America is suffering as a result of the monopolistic practices of the rail carriers, particularly at our plant in Pasadena, Texas.

Air Liquide America is one of the major industrial gas suppliers in the United States with its North American headquarters based in Houston, Texas. We supply oxygen, nitrogen, hydrogen, argon and many other gases and services to nearly every industry (for example: steel, oil refining, chemicals, glass, electronics, healthcare, food processing, metallurgy, paper and aerospace). We have 132 production facilities and 3,300 employees in the United States, of which 27 production facilities employ 1600 people throughout Texas. We provide products to such Texas-based companies as Lyondell Chemical Company, Texas Instruments, Exxon Mobil, The Texas Medical Center—M.D. Anderson, The Methodist Hospital, Reliant Energy—South Texas Project, and many others.

Our Texas Gulf Coast network with its hub in Pasadena, Texas is one of the largest argon-producing complexes in the world, which ships products to customers in Western States such as California, Arizona and Colorado, and the Midwest. We depend on efficient transportation from Texas to compete effectively with foreign producers and local producers. Monopolistic rail practices threaten our competitiveness, particularly in the current struggling economy.

Congress enacted the Staggers Rail Act in 1980 with the objective of deregulating *competitive rail traffic* and retain certain targeted protections for “captive” rail traffic that have no realistic transportation option except a single railroad. Air Liquide America agrees with Congress’ objective in the 1980 legislation and welcomes any market environment where willing buyers and willing sellers can gather to make their best deal. Three regulatory actions have distorted and undercut the provisions passed by Congress in 1980. These actions are: (1) the 1996 “bottleneck” decision; (2) the “competitive access” ruling of the mid-1980’s; and (3) the approval of “paper barriers” imposed as a condition to the sale of track from major carriers to short line railroads. The impact has been that the total number of major rail carriers has declined from 30 when the law was written to seven today and, as can be expected in an industry monopolies, featured an increase in market power exerted by the remaining rail carriers. Air Liquide America and our customers suffer the imposition of that market power as a “captive” rail customer.

The higher rates paid by “captive” rail customers penalize United States industries in highly competitive global markets. Air Liquide America ships argon by rail from our Texas gulf coast facilities as well as in Plaquemine, Louisiana. Our company also operates an argon production plant in Scotford, Alberta (Canada). Each of the United States facilities is a “captive” rail customer and pays transportation rates substantially higher than our Canadian plant having open rail switching. To emphasize the point, basically we sell product to our Canadian customers at a price less than we can sell to comparable customers in the United States due to the monopoly rates that we are required to pay as a “captive” rail user.

Our Pasadena plant is captive to the Union Pacific Railroad, which operates a rail line in proximity to our facility. Today we transport product via trucks and transload the product onto rail cars of the Burlington Northern Santa Fe (BNSF) because the monopolistic rates charged by Union Pacific will not allow us to remain

competitive in those distant markets. Still, the extra step and costs of using trucks disadvantages us in competing for additional business. Of course, this is very inefficient and costly in doing business.

Air Liquide America's facilities at twenty-four other locations throughout the USA are also "captive" rail users, and subject to the burden of uncompetitive rail rates.

Air Liquide America is pleased that you are holding hearings on S. 919 and urges the Senate to pass this bill as soon as possible.

Sincerely,

B.K. CHIN,
Chief Operating Officer,
 Air Liquide America L.P.

AKZO NOBEL CHEMICALS INC.
Chicago, IL, October 23, 2003

Dear Senator Hutchison:

Thank you for holding today's hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns. Balanced commercial relationships coupled with financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The financial health of America's railroads is extremely important to the U.S. economy and the business of Chemistry. Akzo Nobel Chemicals Inc., the entire Chemical industry, and indeed the American economy simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. Captive rail customers are confronted with a lack of competitive options, ineffective remedies to enhance rail competition, and a slow and costly appeal processes through inaction by the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in further degradation of the American manufacturing job base to overseas competition.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to the competitive environment and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation *will not* re-regulate the railroads as may have been portrayed by some of its opponents nor does it cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There is a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices. I believe S. 919 can help all of us to achieve these mutually beneficial objectives allowing American business to compete successfully in the global market.

Very truly yours,

EDMUND A. STEC,
General Manager-Commercial Services.
 Akzo Nobel Chemicals Inc.

cc: Senator Richard Durbin
 Senator Peter Fitzgerald

ASHTA CHEMICALS INC.
Ashtabula, OH, September 15, 2003

Dear Senator Hutchison:

Thank you for holding today's hearing to address the significant concerns of captive railroad customers. As a captive rail customer who ships well over a thousand cars annually, ASHTA Chemicals Inc. would like to take this opportunity to communicate its support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

As a long time shipper and supporter of rail as a safe and effective means of transporting hazardous chemicals, ASHTA Chemicals Inc. has a vested interest in the financial health of America's railroad carriers. Our company, our industry, and our economy would simply not be able to operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. Too often captive rail customers are confronted with both a lack of competitive options and no swift or effective remedy at the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, and does not cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. We believe S. 919 can help us to achieve these mutually beneficial objectives.

BILL J. BRODNICK,
CFO & VP Finance,
 ASHTA Chemicals Inc.

ATOFINA PETROCHEMICALS, INC.
Houston, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
 Washington, DC.

Subject: Support for S. 919

Dear Senator Hutchison:

Thank you for holding a hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003.

Atofina Petrochemicals, Inc. has five facilities in the state of Texas, and with the exception of our plant in La Porte, Texas, we have access to the services of only one rail carrier. At the single facility where we do have two rail options, the cost to ship our product is forty percent less than to ship the same type of product from any of the other locations. This fact alone would seem sufficient proof of the need for competition.

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There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

ROBERT KILPATRICK,
Vice President and General Counsel.

cc: Karyn Grace
Charlie Kitchen
Marty Durbin

ATOFINA PETROCHEMICALS, INC.
Houston, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Washington, DC.

Subject: Support for S. 919

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Sincerely,

CAROLYN SANDERS,
*Vice President—Human Resources,
Public Affairs and General Services,
ATOFINA Petrochemicals, Inc.*

cc: Karyn Grace
Charlie Kitchen
Marty Durbin

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Sincerely,

KARYN GRACE,
*Manager, Public Affairs
& Corporate Communications.*

cc: Charlie Kitchen
Marty Durbin

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Houston, TX, September 16, 2003

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RICK CHARTER,
 CAO and Vice President—Health,
 Safety and Environment.
 ATOFINA Petrochemicals, Inc.

cc: Karyn Grace
 Charlie Kitchen
 Marty Durbin

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SCOTT MCEWEN,
Vice President, Polypropylene.

cc: Karyn Grace
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Marty Durbin

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LEE O'SHIELDS,
Vice President and CIO.

cc: Karyn Grace
Charlie Kitchen
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PAUL ARENDS.

Cc: Charles Kitchen, Marty Durbin, Karyn Grace

September 16, 2003

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CONNIE BARTON.

CC: Charles Kitchen
Marty Durbin
Karyn Grace

Kingwood, TX, September 16, 2003

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DAVID M. BOCK.

Cc: Mr. Charles Kitchen, Mr. Marty Durbin

September 16, 2003

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Thank you,

RAIME COTTON.

cc. Karlyn Grace
Charles Kitchen
Marty Durbin

Spring, TX, September 16, 2003

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Washington, DC.

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W. ALAN CRAMER

cc: Charles Kitchen
Marty Durbin
Karyn Grace

ATOFINA PETROCHEMICALS
Houston, TX, September 16, 2003

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PATRICIA DOSSETT.

CC: Charles Kitchen
CC: Marty Durbin
CC: Karyn Grace

Lake Jackson, TX, September 16, 2003

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Washington, DC.

Subject: Support for S. 919

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Best regards,

AARON DOUGHTY.

Cc: Karyn Grace
Charles Kitchen
Marty Durbin

September 16, 2003

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STEVEN GO.

Cc: Charles Kitchen, Marty Durbin, Karyn Grace

ATOFINA PETROCHEMICALS
September 16, 2003

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There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

AMY JOHNSON,
Logistics Department.

Cc: Charles Kitchen
 Marty Durbin
 Karyn Grace

September 16, 2003

Hon. KAY BAILEY HUTCHISON,
 Washington, DC.

Subject: Support for S. 919

Dear Senator Hutchison:

Thank you for holding a hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003.

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DEBRA MURON.

cc: Charles Kitchen
Marty Durbin
Karyn Grace

September 16, 2003

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KIM ONHU.

September 16, 2003

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KINII SPEAR.

cc: Charles Kitchen
Marty Durbin
Karyn Grace

ATOFINA PETROCHEMICALS, INC.
Houston, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Washington, DC.

Subject: Support for S. 919

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Sincerely,

BARBARA VEST.

CC: Charles Kitchen
Marty Durbin
Karyn Grace

Spring, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Washington, DC.

Subject: Support for S. 919

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Regards,

THE HUNG VU.

CC: Charles Kitchen, Marty Durbin, Karyn Grace

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LESLIE M. M. WILEY,
Senior Logistics Specialist.

Cc: Charles Kitchen
Marty Durbin
Karyn Grace

September 16, 2003

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Washington, DC.

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DONNA WOMACK.

Cc: Charles Kitchen
Marty Durbin
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Respectfully,

MICHAEL J. GOINS,
PE Product Manager.

September 16, 2003

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ED BRUBER,
PE National Sales Manager.

ATOFINA PETROCHEMICALS, INC.
September 16, 2003

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Washington, DC.

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MIKE JOHNSON,
U.S. Polyethylene Business Analyst.

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Thank you,

MOLLY MYERS,
Pricing Coordinator—HDPE.

ATOFINA PETROCHEMICALS, INC.
September 15, 2003

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Respectfully,

SHERI REYNOLDS.

ATOFINA PETROCHEMICALS, INC.
Houston, TX, September 16, 2003

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Washington, DC.

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MARLENE SHAKARA.

ATOFINA PETROCHEMICALS, INC.
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JENNY BLACKWELL.
Account Coordinator.

September 16, 2003

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Washington, DC.

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Regards,

LYNDA O. JONES,
Administrative Assistant
Polyethylene Department.

ATOFINA PETROCHEMICALS
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Thank you for holding a hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003.

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However, of equal importance is a balanced commercial relationship between the railroads and their captive customers. Too often, captive rail customers are confronted not only with a lack of competitive options but no swift or effective remedy regarding pricing complaints at the Surface Transportation Board (STB). Certainly, in the current atmosphere of fierce global competition, continuing the status quo of high prices due to little competition among rail carriers and no quick way to resolve pricing issues will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will not only remove the current railroad practices that block competition but will also provide effective remedies at the STB for those railroad customers denied access to competitive pricing for railroad services. The aim of this proposed legislation is not to re-regulate the railroads and does not cap rates on "captive shippers." On the contrary, this legislation is merely pro-competition and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

KIMBERLY JACOBS,
HDPE Customer Service.

September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Washington, DC.

Subject: Support for S. 919

Dear Senator Hutchison:

Thank you for holding a hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003.

Atofina Petrochemicals, Inc. has five facilities in the state of Texas, and with the exception of our plant in La Porte, Texas, we have access to the services of only one rail carrier. At the single facility where we do have two rail options, the cost to ship our product is forty percent less than to ship the same type of product from any of the other locations. This fact alone would seem sufficient proof of the need for competition.

However, of equal importance is a balanced commercial relationship between the railroads and their captive customers. Too often, captive rail customers are confronted not only with a lack of competitive options but no swift or effective remedy regarding pricing complaints at the Surface Transportation Board (STB). Certainly, in the current atmosphere of fierce global competition, continuing the status quo of high prices due to little competition among rail carriers and no quick way to resolve pricing issues will result in more American jobs moving overseas.

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There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

SHANNON TAYLOR.

Houston, TX, September 16, 2003

Hon. KAY BAILEY HUTCHISON,
Washington, DC.

Subject: Support for S. 919

Dear Senator Hutchison:

Thank you for holding a hearing to address the significant concerns of captive railroad customers. As a concerned employee of ATOFINA Petrochemicals Inc., I want to state my strong support for S. 919, the Rail Competition Act of 2003.

ATOFINA Petrochemicals, Inc. has five facilities in the state of Texas, and with the exception of our plant in La Porte, Texas, we have access to the services of only one rail carrier. At the single facility where we do have two rail options, the cost to ship our product is forty percent less than to, ship the same type of product from any of the other locations. This fact alone would seem sufficient proof of the need for competition.

However, of equal importance is a balanced commercial relationship between the railroads and their captive customers. Too often, captive rail customers are confronted not only with a lack of competitive options but no swift or effective remedy regarding pricing complaints at the Surface Transportation Board (STB). Certainly, in the current atmosphere of fierce global competition, continuing the status quo of high prices due to little competition among rail carriers and no quick way to resolve pricing issues will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will not only remove the current railroad practices that block competition but will also provide effective remedies at the STB for those railroad customers denied access to competitive pricing for railroad services. The aim of this proposed legislation is not to re-regulate the railroads and does not cap rates on "captive shippers." On the contrary, this legislation is merely pro-competition and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be an equitable way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

HARRY MITCHELL, JR.

Cc: Charles Kitchen
Marty Durbin
Karyn Grace

THE DOW CHEMICAL COMPANY
Midland, MI, September 15, 2003

Dear Senator Stevens:

Thank you for participating in the 9/18/2003 hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

First, let me state my strong interest in the financial health of America's railroads. My company, this industry, and indeed the American economy simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. Too often captive rail customers are confronted with both a lack of competitive options and no swift or effective remedy at the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, and does not cap rates on “captive shippers.” This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

W.L. (BILL) GEBO,
Manager, Rail Services Purchasing,
 The Dow Chemical Company.

DUPONT
Wilmington, DE, September 16, 2003

Senator KAY BAILEY HUTCHISON, Chair
 Subcommittee on Surface Transportation and Merchant Marine,
 Committee on Commerce, Science, and Transportation,
 United States Senate,
 Washington, DC.

Dear Senator Hutchison:

DuPont, a successful, global, science company, wants to thank you for holding a public hearing on S. 919, The Railroad Competition Act of 2003

DuPont strongly believes that robust rail-to-rail competition should be a key component of the national Rail Transportation Policy. It has been demonstrated time and again that rail competition drives carrier efficiencies and innovation. Rail competition consistently results in a significantly improved carrier offering and fuels growth. The lessons of competitive rail markets as diverse as Powder River Basin coal and intermodal trailers and containers are clear: competition works. DuPont believes customer and railroad benefits can be derived from robust competitive offerings across diverse rail markets.

Most rail-served customers, including DuPont, are served exclusively by one railroad. Under such circumstances, robust rail-to-rail competition is not a reality. Furthermore, an other-than-competitive rail offering too often results in service inconsistency and lacks any continuous improvement imperative. Rail shippers, and/or their customers, must ultimately accept and absorb the cost of such railroad inefficiencies.

Since the 1980 passage of the Staggers Rail Act, the number of Class 1 railroads has been reduced from 40 to 5 mega-carriers that handle more than 90% of the country's rail traffic. The need to balance the economic affects of consolidation with the non-competitive environment faced by many rail customers cannot be denied. DuPont believes the best means of balance can be provided for by S. 919. S. 919 relies on competition and market forces to determine rail rates and service standards in most cases.

S. 919 will appropriately supplement, and complement, the Staggers Rail Act. DuPont believes the September 18 public hearing marks an important next step in promoting competitive, balanced behavior and benefits for the nation's railroads, rail customers, and the general public.

Sincerely,

MARY L. PILEGGI,
North America Regional Logistics Manager.

Facsimile Copies: Members, Subcommittee on Surface
 Transportation and Merchant Marine
 Committee on Commerce, Science, and Transportation
 United States Senate
 Washington, DC

GEORGIA GULF CHEMICALS & VINYL, LLC
Plaquemine, LA, September 16, 2003

Senator KAY BAILEY HUTCHISON, Chair
 Subcommittee on Surface Transportation and Merchant Marine,
 Committee on Commerce, Science, and Transportation,
 United States Senate,
 Washington, DC.

Dear Senator Hutchison:

Thank you for holding today's hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

First, let me state my strong interest in the financial health of America's railroads. My company, this industry, and indeed the American economy simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. Too often captive rail customers are confronted with both a lack of competitive options and no swift or effective remedy at the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, and does not cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

BENNIE R. NOBLES,
Manager, Distribution / Customer Service,
 Georgia Gulf Chemicals and Vinyls, LLC.

LYONDELL CHEMICAL COMPANY
Houston, TX, September 17, 2003

Hon. KAY BAILEY HUTCHISON,
 Washington, DC.

Dear Senator Hutchison:

Thank you for holding a hearing to address the significant concerns of captive railroad customers. I want to state my support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

Lyondell Chemical Company has a strong interest in the financial health of America's railroads. The chemical industry cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their customers, especially those who are captive to only one railroad for service. Captive rail customers are not only confronted with a lack of competitive options but also find it next to impossible to find effective remedies with the Surface Transportation Board (STB).

The continued commoditization of the chemical industry is making us more and more dependent on an efficient logistics process to serve our global customers. Approximately 85 percent of chemical industry products are delivered in bulk by rail. Unfortunately, with only seven major railroads left in the United States today, controlling over 90 percent of the freight, our ability to profitably transport our products to customers is becoming increasingly difficult.

Almost two out of every three chemical plants in the United States are held captive by one railroad. When this non-competitive situation exists, we find ourselves

at a severe economic disadvantage, in that freight rates are up to 60 percent higher than in a situation where there are competitive options. If we let the status quo continue, the inevitable result will be more of our U.S. industrial base moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that prevent customers from obtaining access to truly competitive services and will empower the STB to provide effective remedies for those regions that do not currently have effective railroad competition. Further, this legislation will help shippers, and even Texas taxpayers, by eliminating undesired investments in build-out projects that often place business, local government, and communities in a no-win situation.

Contrary to the arguments made by the railroad industry, this legislation does not re-regulate the railroads; neither does it cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve longterm financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S, 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

DAN F. SMITH.

MONSANTO
St. Louis, MO, October 23, 2003

Senator KAY BAILEY HUTCHISON, Chair
Subcommittee on Surface Transportation and Merchant Marine,
Committee on Commerce, Science, and Transportation,
United States Senate,
Washington, DC.

Dear Senator Hutchison:

Thank you for holding today's hearing to address the significant concerns of captive railroad customers like Monsanto Company, among others. We want to state strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

As a major rail shipper we have a very strong interest in the financial health of America's railroads. Monsanto Company, this industry, and indeed the American economy simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Equally important however, is a balanced commercial relationship between the railroads and their captive customers. Captive rail customers are confronted with lack of competitive options and no swift, effective or cost efficient remedy at the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in more American jobs being lost to import cost advantages.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not reregulate the railroads, and does not cap rates on "captive shippers." This legislation is pro-competitive and consistent with the Concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business

to compete successfully in the global market. Monsanto Company believes S. 919 can help us to achieve these mutually beneficial objectives.

Sincerely,

CHARLES O. PATTERSON,
Manager, Logistics Services.
ROBERT M. HOPPE,
Rail Asset Management Specialist.

OCCIDENTAL CHEMICAL CORPORATION
Dallas, TX, September 17, 2003

Hon. KAY BAILEY HUTCHINSON,
United States Senate,
Washington, DC.

Dear Senator Hutchinson:

Thank you for meeting with me to discuss rail competition and its impact on our economy. Your leadership on this issue, and in orchestrating the hearing on September 18, is greatly appreciated by me and many others from the shipping community. This hearing will go a long way in helping to address the significant concerns of captive rail customers. Thank you, also, for your support of S. 919, the Rail Competition Act of 2003, which represents an effective means of addressing these concerns.

First let me say that the chemical industry, the railroads and Congress must work together to stop the continual drain of jobs in this country to other places in the world, and do something constructive about the shift in the balance of trade toward imports.

I'd also like to state my strong interest in the financial health of America's railroads. My company, this industry, and indeed the American economy simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. Too often captive rail customers are confronted with both a lack of competitive options and no swift or effective remedy at the Surface Transportation Board. For example, we have a plant in the northeast that is facing the reality of potentially shutting down and one of the causes is the fact that our principle raw material rail rate to this captive plant exceeds the rate on the same material to a nearby plant in the Shared Assets Area by about 80 percent!

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system the nation needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, and does not cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Thank you, again, for your leadership on this issue. I look forward to meeting with you again on this issue and other issues that positively impact the economic status of Texas and the country.

Sincerely,

J. L. HURST III.

PPG INDUSTRIES, INC.
Pittsburgh, PA, October 15, 2003

Hon. Senator KAY BAILEY HUTCHISON,
Chairman,
Hon. Senator DANIEL K. INOUE,
Ranking Member,
Subcommittee on Surface Transportation and Merchant Marine,
Committee on Commerce, Science, and Transportation,
United States Senate,
Washington, DC.

Dear Senator Hutchison and Senator Inouye:

Thank you for holding a hearing to address concerns of shippers like PPG Industries, Inc. about rail freight industry competition and service.

PPG Industries, Inc. is a diversified manufacturer of chemicals, protective coatings, glass and fiber glass employing over 22,000 in the United States and with more than 50 major facilities in 23 states.

Many of our businesses are dependent upon railroad freight. The company supports efficient rail transportation. PPG has approximately 2,500 private rail cars in service. Some of our products cannot be moved by other modes. An efficient and successful rail industry is absolutely essential to a healthy and competitive U.S. economy and important to PPG's continued success. This is not an anti-rail issue for PPG.

As a major chemical producer, the issue of rail competition is very important to us. Approximately two-thirds of America's chemical facilities that depend on rail service are served by only one railroad. Because of a lack of competition, these single-served locations are subject to exorbitant prices and substandard service. Such facilities are "captive" to a single railroad without competitive market forces driving cost and service efficiency.

Rail mergers and acquisitions have been the major contributing factor to a diminished ability to deliver our products to market in a timely manner and at reasonable cost. The consolidation within the rail industry has led to the loss of an effective competition balance between railroads. Over the last 25 years, the number of Class I railroads has been reduced from approximately sixty-three to only seven. This unprecedented consolidation has resulted in only two Class I railroads in the east and two in the west controlling over 90 percent of rail freight traffic.

This is a serious issue for PPG Industries; the results of these mergers and acquisitions are very real. As an example, one of our major manufacturing locations, which is served by only one railroad is significantly disadvantaged by a lack of competitive access. Moreover, numerous

PPG customers are captive to a single delivering railroad, which diminishes our ability to obtain competitive transportation rates and develop service options.

In summary, PPG is dependent on rail transportation to move its chemical products to market, and our continued economic viability is dependent on an effective commercial rail system. PPG supports and needs an efficient and cost competitive rail industry to provide effective service at reasonable costs. We believe congressional action is necessary to restore and assure fair competition among railroads. PPG's continued economic viability and the security of its employees are directly affected by these concerns, and we ask that these issues be addressed soon within appropriate legislation.

We appreciate the opportunity to offer these written comments and thank you for holding such a hearing about the need for railroad access and competition.

Sincerely,

CHARLES E. BUNCH,
President and Chief Operating Officer.

cc: The Honorable John McCain, Chairman
The Honorable Fritz Hollings, Ranking Member
Senate Committee on Commerce, Science, and Transportation

SUNOCO
October 22, 2003

Hon. KAY BAILEY HUTCHISON,
United States Senate,
Washington, DC.

Dear Senator Hutchison:

Thank you for holding this week's hearing to address the significant concerns of captive railroad customers. Sunoco Inc., with four owned plants and one joint venture in the State of Texas employing over 1,050 people want to emphasize our strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns. Two of our Texas locations (Bayport and Nederland) are served by a single carrier and those two sites have more rail service problems, incur more rail storage costs and are not as competitive in the markets they serve as the two sites that have competitive rail service.

First, allow me to state our strong interest in the financial health of America's railroads. Sunoco ships and receives in excess of 40,000 carloads of oils, chemicals and fuels annually by rail and we cannot operate and market our products without a reliable and financially viable railroad industry and a secure railroad infrastructure. However, we cannot tolerate rail service transit increases of 56 days longer than 2002 on deliveries from Houston plants to plastics customers in Dallas and central Texas. The only delivering carrier has been unable to improve the delivery schedule to 2002 levels, forcing Sunoco to deliver by bulk truck.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. As a captive rail customer in Texas, we are confronted with both a lack of competitive options and no swift or effective remedy at the Surface Transportation Board. In the current atmosphere of fierce global competition, continuing the status quo will result in more American jobs moving overseas.

Both balanced commercial relationships and financially strong railroads are necessary to provide the secure, effective transportation system Sunoco needs to remain competitive in the global marketplace. Only Congress can make the necessary changes in national rail policy to achieve these critical objectives.

The Railroad Competition Act of 2003 will change the current railroad and administrative practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Very Truly Yours,

BRUCE G. FISCHER,
Senior Vice President—Chemicals.

PVS CHEMICALS, INC.,
Detroit, MI, September 18, 2003

Senator KAY BAILEY HUTCHISON, Chair
Subcommittee on Surface Transportation and Merchant Marine,
Committee on Commerce, Science, and Transportation,
United States Senate,
Washington, DC.

Dear Senator Hutchison:

Thank you for holding today's hearing to address the significant concerns of captive railroad customers. I want to state my strong support for S. 919, the Rail Competition Act of 2003, as an effective means of addressing those concerns.

First, let me state my strong interest in the financial health of America's railroads. PVS Chemicals, Inc. simply cannot operate successfully without a financially viable railroad industry and a secure railroad infrastructure. Almost 30% of our shipments move by rail.

Of equal importance, however, is a balanced commercial relationship between the railroads and their captive customers. PVS as a captive rail customer is confronted with a lack of competitive rail options. We operate a rail fleet of more than 500 cars

with a network of manufacturing plants and suppliers that covers the Eastern US. Our relatively small size, however, gives us very little leverage with the railroads in rate negotiation, especially in joint moves. At the same time, declines in rail service have forced us to compensate; because of rail inefficiencies, we have had to invest more dollars in rail equipment just to keep product flowing and meet the needs of our existing customers. Our cost of doing business is rising disproportionately. In the current atmosphere of fierce global and domestic competition, continuing the status quo puts us at an extreme disadvantage that will ultimately result in more jobs being eliminated.

Only Congress can make the necessary changes in national rail policy to achieve these critical objectives. The Railroad Competition Act of 2003 will remove the current railroad practices that block rail customer access to competition and will provide effective remedies at the STB for those railroad customers that cannot gain access to competition. This legislation does not re-regulate the railroads, and does not cap rates on "captive shippers." This legislation is pro-competitive and consistent with the concepts adopted by the Congress in 1980 when it partially deregulated the railroads.

There must be a way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. I believe S. 919 can help us to achieve these mutually beneficial objectives.

Very truly yours,

BETH A. BANIA,
Director of Logistics.

BAYER POLYMERS
New Martinsville, WV, October 9, 2003

Hon. KAY BAILEY HUTCHISON,
Subcommittee on Surface Transportation
and Merchant Marine,
U.S. Senate,
Washington, DC.

Hon. DANIEL K. INOUE, Ranking
Member
Subcommittee on Surface Transportation
and Merchant Marine
U.S. Senate,
Washington, DC.

Dear Chairman Hutchison and Ranking Member Inouye:

Senator Conrad Burns and Senator Byron Dorgan introduced a bill to promote rail competition, S. 919. We understand that you had planned to hold a hearing on Sept. 18, and that it had to be rescheduled for late October due to Hurricane Isabel.

We wanted you to know that we support holding such a hearing. It is important to explore the problems and concerns of rail shippers. Thousands of chemical plant union workers rely on the valuable jobs at many chemical plants around the country. Until rail service, costs and reliability problems are addressed properly, jobs at chemical plants will continue to be at risk, due to global competition.

As I am sure you are aware, chemical producers are struggling in the current economic climate, due to several factors. Cost of rail transportation and problems with service are two such reasons. Chemical companies and their employees depend on rail transportation because of the volume of chemicals that need to be shipped and the safety concerns inherent in the transport of chemicals. Rail shipment of chemicals is by far the safest and most cost-effective way to get chemical products to distributors, processors and fabricators. However, rail customers at captive sites experience non-competitive pricing and poor service. We need a good and effective rail system in order to be competitive in today's global market.

In recent years, chemical company employees have seen a realignment of priorities within the industry. Many operations have been tightened, and there is an increased focus on security. There is also increased focus on cost reduction and efficiency. We believe competition for service will greatly help to improve the situation. We have seen this occur at other chemical plant sites, where competition exists. For these reasons, we hope you will take a serious look at changing the law, in order to promote competition. We strongly support efforts like those of Senators Burns and Dorgan to address these issues and support S. 919 in concept.

Sincerely,

THOMAS M. SLOKAN,
*President, International Chemical Workers
Union—Council Local No. 566-C.*

INTERNATIONAL CHEMICAL WORKERS UNION
Addyston, OH, October 13, 2003

The Honorable KAY BAILEY HUTCHISON,
Subcommittee on Surface Transportation and Merchant Marine,
United States Senate,
Washington, DC.

Dear Senator Hutchison:

Senator Conrad Burns and Senator Byron Dorgan introduced a bill to promote rail competition, S. 919. We understand that you had planned to hold a hearing on Sept. 18, and that it had to be rescheduled for late October due to Hurricane Isabel.

We wanted you to know that we support holding such a hearing. It is important to explore the problems and concerns of rail shippers. Thousands of chemical plant union workers rely on the valuable jobs of many chemical plants around the country. Until rail service, costs and reliability problems are addressed properly, jobs at chemical plants will continue to be at risk, due to global competition.

As I am sure you are aware, chemical problems are struggling in the current economic climate, due to several factors. Cost of rail transportation and problems with service are two such reasons. Chemical companies and their employees depend on rail transportation because of the volume of chemicals that need to be shipped and the safety concerns inherent in the transport of chemicals. Rail shipment of chemicals is by far the safest and most cost-effective way to get chemical products to distributors, processors and fabricators. However, rail customers at captive sites experience non-competitive pricing and poor service. We need a good and effective rail system in order to be competitive in today's global market.

In recent years, chemical company employees have seen a realignment of priorities within the industry. Many operations have been tightened, and there is an increased focus on security. There is also increased focus on cost reduction and efficiency. We believe competition for service will greatly help to improve the situation. We have seen this occur at other chemical plant sites, where competition exists. For these reasons, we hope you will take a serious look at changing the law, in order to promote competition. We strongly support efforts like those of Senators Burns and Dorgan to address these issues and support S. 919 in concept.

Sincerely,

WILLIAM D. VILLINES,
President, Local 561C.

INTERNATIONAL CHEMICAL WORKERS UNION
Addyston, OH, October 13, 2003

The Honorable DANIEL K. INOUE,
Ranking Member,
Subcommittee on Surface Transportation and Merchant Marine,
United States Senate,
Washington, DC.

Dear Senator Inouye:

Senator Conrad Burns and Senator Byron Dorgan introduced a bill to promote rail competition, S. 919. We understand that you had planned to hold a hearing on Sept. 18, and that it had to be rescheduled for late October due to Hurricane Isabel.

We wanted you to know that we support holding such a hearing. It is important to explore the problems and concerns of rail shippers. Thousands of chemical plant union workers rely on the valuable jobs of many chemical plants around the country. Until rail service, costs and reliability problems are addressed properly, jobs at chemical plants will continue to be at risk, due to global competition.

As I am sure you are aware, chemical problems are struggling in the current economic climate, due to several factors. Cost of rail transportation and problems with service are two such reasons. Chemical companies and their employees depend on rail transportation because of the volume of chemicals that need to be shipped and the safety concerns inherent in the transport of chemicals. Rail shipment of chemicals is by far the safest and most cost-effective way to get chemical products to distributors, processors and fabricators. However, rail customers at captive sites experience non-competitive pricing and poor service. We need a good and effective rail system in order to be competitive in today's global market.

In recent years, chemical company employees have seen a realignment of priorities within the industry. Many operations have been tightened, and there is an increased focus on security. There is also increased focus on cost reduction and effi-

ciency. We believe competition for service will greatly help to improve the situation. We have seen this occur at other chemical plant sites, where competition exists. For these reasons, we hope you will take a serious look at changing the law, in order to promote competition. We strongly support efforts like those of Senators Burns and Dorgan to address these issues and support S. 919 in concept.

Sincerely,

WILLIAM D. VILLINES,
President, Local 561C.

Mr. PLATZ. Madam Chairman and members of the Subcommittee: Thank you for the opportunity to testify today. My name is Charles Platz and I am President of Basell North America, Incorporated, which is headquartered in Elkton, Maryland. Basell has manufacturing facilities in Texas, Louisiana, Tennessee, and also markets products manufactured at its plant in Linden, New Jersey. We produce plastic resins that our customers use in a variety of applications, such as automobile components, textiles, packaging, medical products, and household goods.

I appear in support of Senate bill 919, the Railroad Competition Act of 2003, as Co-Chair of Consumers United for Rail Equity and on behalf of the American Chemistry Council and my own company.

Madam Chairman, captive rail customers are dependent upon the railroad industry and we are vitally interested in the financial health of America's railroads. We simply cannot operate successfully without a financially viable railroad industry. Indeed, I believe that the ability of the American manufacturers and producers to compete in today's global market is highly dependent upon a rail freight industry. Today, however, the rail freight industry impedes rather than enables our global competitiveness.

The captive rail customers who are petitioning Congress for action are not a fringe group, as some of our opponents would like you to think. Our coalition includes 14 major trade organizations representing the agriculture, pulp and paper, fertilizer, chemical and plastics industries, and electric utilities that use coal. We are the largest commodity customers of the railroads and our coalition members represent companies whose industries spend more than \$18 billion a year on rail service. This represents approximately 55 percent of the railroads' total annual revenue.

More importantly, a very large number of American families depend upon wages from our industries, which provide more than 2.4 million direct jobs, and commonly accepted economic multipliers put the indirect job impact at five times that number, or 12 million jobs.

Over the course of the past year I have led a group of senior executives of U.S. companies with facilities served by only one railroad carrier. Our group met with and pursued a dialogue with the CEO's of the major U.S. railroads that serve captive customers. The dialogue has centered on two critical issues: one, the financial health and viability of the railroads, including needed infrastructure improvements; and two, the absence of satisfactory balanced commercial relationships between the captive rail customers and their rail freight carriers.

These conversations began after John Snow, then the Chair of the CSX Corporation, and I testified before this Subcommittee on the captive rail customer issues in July 2002. Following our testi-

mony, Senator John Breaux of Louisiana, then the chair of the Subcommittee, asked both Mr. Snow and me to enter into a dialogue on this issue and to involve other shippers and railroad CEO's.

Through these dialogues it has become clear to me that the major railroads are pursuing a flawed business model. Even the railroads agree that the gap between their annual income needs and their annual income is expanding, not shrinking. This is despite the fact that they have been allowed to consolidate to achieve cost synergies, they have also had the opportunity to transfer less profitable tracks to shortline railroads, and they have been able to increase the burden on captive rail customers.

The result is that rail customers without an alternative pay more, rail executives defend the status quo at all cost, and the relevant business interests cannot negotiate a solution. In my view, pursuing a strategy of continually loading more costs on captive rail customers does not appear to be a business model that will result in healthy American railroads in the long run. Captive rail customers will try to escape. Some captive customers will construct rail line buildouts, as my company is doing in Texas. Some will shift their operations offshore. Some may even go out of business.

I applaud the positive change that has taken place in the Surface Transportation Board's operating procedures since the arrival of Chairman Roger Nober. Unfortunately captive rail customers cannot expect the needed regulatory relief from the STB without help from Congress. Chairman Nober, in response to a question about the reforms sought by the captive rail customers, said in a published interview: "They have a lot of legitimate issues that they are raising. The core issues that they want to see done, though, are for the Congress."

The changes the captive rail customers are urging today cannot be pursued anywhere but in Congress because balanced, fair legislation is needed to bring about a positive relationship between the railroads and the captive customers. S. 919 is the vehicle to achieve this.

The railroad industry's allegation that S. 919 is reregulatory is simply not true and has been amply discussed by other witnesses. We believe S. 919 will enable the national rail system to evolve toward a more competitive system that serves the needs of our Nation in a highly competitive global market. The Ocean Shipping Reform Act of 1998 is an example of how market forces can restore balance to the commercial relationship.

If the railroads, the captive rail customers, and the U.S. economy are to prosper, the railroads and the captive rail customers must have mutually beneficial transportation agreements. Unfortunately, I am convinced we cannot get to that point without the help of Congress. Railroads will not negotiate on this competitive advantage that they have. The Surface Transportation Board will not act to change the policy without Congressional help. So we are at an impasse.

To make meaningful change, you need to get involved. That is why I am here today asking for your help.

Thank you, Madam Chairman, for this hearing, for your interest in this issue, and for the opportunity to present our case to you and your colleagues. Thank you.

[The prepared statement of Mr. Platz follows:]

PREPARED STATEMENT OF CHARLES E. PLATZ, PRESIDENT, BASELL NORTH AMERICA INC. ON BEHALF OF CONSUMERS UNITED FOR RAIL EQUITY AMERICAN CHEMISTRY COUNCIL

Madam Chair and Members of the Subcommittee, thank you for the opportunity to testify today on this important subject. My name is Charles E. Platz. I am President of Basell North America Inc., which is headquartered in Elkton, Maryland. Basell has manufacturing facilities in Texas, Louisiana and Tennessee, and markets products manufactured at a plant in Linden, New Jersey. We produce raw material plastic resin that our customers use in a variety of applications such as automobile components, textiles, packaging, medical products and numerous household goods. I appear today in support of S. 919, the Railroad Competition Act of 2003, as Co-Chair of Consumers United for Rail Equity and on behalf of the American Chemistry Council and my own company.

Madam Chair, I approach this issue from the perspective of an executive responsible for successfully running a U.S.-based manufacturing business in an extremely competitive global market. I am very concerned not only that our company succeeds in this dynamic global economy, but also that important American manufacturing jobs remain in this country. If Congress does not take action enabling the market to fix this problem now, American jobs will be lost and taxpayers will be forced to pay the bill later.

Captive Rail Customers

Madam Chair, want to make two initial points about captive rail customers. First, as businesses dependent on the railroad industry, we are vitally interested in the financial health of America's railroads. We simply cannot operate successfully in this country without a financially viable railroad industry and a secure railroad infrastructure. Indeed, I believe that the ability of American manufacturers and producers to compete in today's global market is highly dependent on the rail freight industry. Today, unfortunately, the rail freight industry impedes—rather than enables—our global competitiveness.

Second, the captive rail customers that are petitioning Congress for action are not a "fringe group"—as some of our opponents would like you to think. Our coalition includes 14 major trade organizations representing the agriculture, pulp and paper, fertilizer, chemical and plastics industries and electric utilities that use coal. We are the largest commodity customers of the freight railroads, spending more than \$18 billion a year on rail service, which represents about two thirds of U.S. rail shipments. *Remarkably, our coalition represents more than half—approximately 55 percent—of the railroads' total annual revenue.*

A very large number of American families depend on wages from our industries, which provide more than 2.4 million direct jobs. Commonly accepted economic multipliers put the indirect job impact at five times that number, or 12 million jobs. Our industries provide significant contributions to this country's balance of trade and the GDP. But in the current highly competitive global business environment, captive rail customers are under increasing pressure in our own businesses. Today, American manufacturers and producers find it more and more difficult to remain competitive against manufacturers and producers outside the United States. In fact, the business of chemistry, of which I am a part, suffered its first trade deficit in history last year.

Basell North America Inc.

Our rail transportation costs are a major factor in our ability to be competitive at home and abroad and in retaining and growing our employment base. For example, in Basell's North American operations, rail transportation is our *second highest cost*—trailing only feedstock—and we overwhelmingly depend on rail shipping. One hundred percent of our finished product is loaded into rail hopper cars. To meet the needs of our customers, the vast majority of whom demand delivery by railcar, we have invested in a fleet of approximately 4,000 hopper cars with a replacement value exceeding \$260 million; our railcars are not supplied by the railroads. The operation of the fleet is strictly at Basell's expense. This investment coupled with the demands of our customers ties us, as it does many other industries among our coalition, firmly to rail transportation.

At many of our facilities we are served by a single railroad for the movement of our product to our customers. Rail customers with facilities served by only one rail carrier are known as “captive rail customers.” Let me explain what captivity has meant to Basell. Although Basell is not captive at its facility in Lake Charles, Louisiana, one of the railroads at that location does have a monopoly on rail service at Basell’s Bayport, Texas facility. That railroad used its market dominance at Bayport to obtain leverage over our Lake Charles traffic.

Within a short distance of our Bayport plant, a second major railroad intersects the line of the carrier that holds us captive. At this intersection point, our hopper cars could be moved to the second railroad where competition could be utilized for the remainder of the movement, thus spurring the rail carriers to provide better, more efficient service and more cost-effective transportation to our customers. Unfortunately, under current law, as interpreted by the Surface Transportation Board in 1996, our carrier is under no obligation to provide a rate for moving our cars to the second, competing carrier. This “bottleneck,” where one railroad controls portions of a route, allows a single rail carrier to dictate the terms of the entire movement of our hopper cars from origin to destination, even over that portion of a movement where rail competition physically exists. When the bottleneck carrier can serve the customer from origin to destination, that carrier has every incentive to block access to the competitive alternative and to retain the traffic itself for the entire movement.

In Basell’s case, over time the incumbent carrier to which we are captive has charged us such an excessive rate on our movements from the Bayport plant that it has jeopardized the continued successful operation of that plant in a highly competitive plastics industry. When this occurred, we considered all of our options. One option might have been to file a rate complaint at the Surface Transportation Board, but rate cases are not a viable option for the chemical industry. The chairman of the STB has testified that rate cases are costly and long. We applaud him for recognizing this situation and speaking about it publicly. The STB has begun a process to review and revise the procedures for small rate cases and for seeking to bring about needed change. The recent provision on small rate cases that was included in the STB Reauthorization legislation reported from the Committee on July 17th is a step in the right direction. Captive rail customers note, however, that this is the second time since 1995 that Congress has directed the STB to correct this problem. Nevertheless, prospective effective alterations that may or may not occur can’t change the fact that today, just as when our situation in Bayport became critical, the only available remedy for achieving access to competition is pursuit of a build-out.

Basell and three other shippers have joined with another railroad to create competition in Bayport, of which you are very familiar, Madam Chair. We have formed San Jacinto Rail Limited, an \$80 million investment to provide competitively priced rail-service options. This is not an investment that is being made because we have more traffic than one railroad can handle. Rather, we’re building this redundant rail line simply to gain access to the existing competing railroad. Frankly, Madam Chair, I would much rather that Basell direct its efforts and resources toward developing new technology or upgrading our plant assets so that we could further improve our competitiveness and that of our customers. Unfortunately, the captive rates and poor service we endure at our Bayport plant threaten its very existence—and the jobs it provides—and breaking that captivity became paramount.

I believe, Madam Chair, if a normal commercial relationship existed between the railroads and their captive rail customers, we would have been able to negotiate a mutually acceptable transportation agreement. In doing so, we would have avoided both disrupting the community and the unnecessary capital investment. And our current carrier may very well have retained our business. Unfortunately, current Federal policy that grants virtually absolute power to the railroads over their captive customers removes major incentives for the railroads to achieve mutually beneficial commercial relationships with their captive customers.

In 1980, when Congress voted to partially deregulate the railroad industry by enacting the Staggers Rail Act, Congress believed partial deregulation was the needed cure and that economic regulation had outlived its usefulness; that railroads faced tough competition from trucks, barges, and pipelines, and that there were still a sufficient number of carriers to provide significant rail-to-rail competition. While the law did not deregulate the industry completely, Staggers freed the railroads from many regulatory burdens and allowed the rationalization of rail systems. In 1980, there were more than 40 major rail carriers. Today, however, just five major railroads handle 90 percent of the nation’s rail traffic. The damage to competition, to market-driven efficiencies, and to the quality and reliability of railroad freight services from consolidation has been enormous.

Why We Believe Congress Must Act

The power that the highly concentrated rail industry now wields in the United States can be the dominant factor in a company's investment decision. In the Chair's state, for example, Toyota only decided to invest \$800 million in a new truck assembly plant in San Antonio after the creation of rail competition at the new plant. Toyota, a Basell customer, requires that at least two competing railroad companies have access to its manufacturing sites, which allows the company to keep its shipping costs down. We understand, by the way, that the incumbent rail carrier has, reluctantly, agreed to allow Toyota access to a second, competing railroad. It's unfortunate that the same two railroads have not come to a similar agreement in response to the San Jacinto Rail Limited project in Bayport, Texas.

Madam Chair, these transportation issues present serious problems for American businesses. The continued competitiveness of America's manufacturing and producer industries demands that changes be made. That's why I am deeply involved and committed to these issues. When I first became involved, it was out of great concern for the welfare of my company. However, as I learned more about these important issues, it became clear to me that much more is at stake—that these issues are critically important not only to our business but also, and more importantly, to the greater American economy and the jobs it provides.

Over the course of the past year I have led a group of senior executives of U.S. manufacturing and production companies with facilities served by only one railroad carrier. Our group met with and pursued a dialogue with the CEO's of the major U.S. railroads that serve captive customers. The dialogue has centered on two critical issues:

- (1) The financial health and viability of the railroads, including needed infrastructure improvements, and
- (2) The absence of a satisfactory, balanced commercial relationship between the captive rail customers and their rail freight carriers.

These conversations began after John Snow, then Chair of the CSX Corporation, and I testified before the Senate Surface Transportation and Merchant Marine Subcommittee on the captive rail customer issue in July of 2002. Following our testimony, Senator John Breaux of Louisiana, then Chair of the Subcommittee, asked both Mr. Snow and me to enter into a dialogue on this issue and to involve other shipper and railroad CEOs in that dialogue. After the President nominated Mr. Snow to serve as Secretary of the Treasury, the dialogue continued with Matt Rose, the CEO of the Burlington Northern and Santa Fe Railway and current Chair of the Association of American Railroads, taking over Mr. Snow's role in the dialogue. During this effort, we assembled representatives of many of the captive shippers and the railroads for one joint meeting. Since that group meeting, the dialogue has continued through a number of one-on-one meetings, telephone calls and correspondence.

While engaged in the dialogue with the CEO's and senior management of the railroads, representatives of rail freight customers examined their position and the need for a change in the status quo. With renewed focus, rail freight customers began coalescing around a few key principles aimed at enhancing competition and represented in the provisions of S. 919. That support has continually grown throughout the year, and, as I mentioned before, S. 919 now enjoys the support of 14 trade associations representing 2.4 million American jobs and more than half of the railroads' total annual revenue.

Since beginning the dialogue with rail executives at Senator Breaux's request, I have engaged in many discussions and meetings about this issue. I am now convinced that the freight railroads will not budge from the status quo in which they have complete market dominance over their captive customers. The Staggers Act, the ICC Termination Act of 1995 and agency interpretation of those acts provided the market dominance railroads hold over their captive customers. While today's railroad CEO's may believe, or may be advised, that their fiduciary duties and corporate governance obligations require them to defend the status quo, that belief is misguided since it focuses only on the very short term. Indeed, I do not accept the status quo as a reasonable business model designed to propel the rail service business into the future. To the contrary, the current model will inevitably lead railroads to their financial brink, costing not only railroad shareholders, but also taxpayers and rail-dependent American enterprise.

A Flawed Railroad Business Model

Madam Chair, based on my experience, I believe the major railroads in the nation are pursuing a flawed business model. Even the railroads agree that the gap between their annual income needs and their annual income is expanding, not shrink-

ing. This is despite the fact that they have been allowed to consolidate to achieve cost synergies. These synergies should have allowed them to operate more efficiently and in a fashion that permits them to recover their cost of capital. They've also had the opportunity to transfer less profitable track to short line railroads and they have been able to increase the burden on captive rail customers. The result is simply that those customers with no alternative pay the most.

Pursuing a strategy of continually loading more costs on captive rail customers does not appear to be a business model that will result in healthy American railroads in the long run. Captive rail customers will try to escape and the universe of captive rail customers is likely to be reduced over time. Some captive customers will construct rail line "build-outs" as we are. Some captive customers will shift their manufacturing activities to facilities that have transportation competition. Some captives will shift their manufacturing to foreign countries, exporting American jobs overseas. Some companies might be forced to close a U.S. plant or to forego an expansion without even having an offshore alternative. Under this business model, the industry will be required to load up even more costs on the remaining captives, thus accelerating the cycle.

Let me be very clear: none of us seeks a return to the "bad old days" of the 1970s when several of the major railroads were in bankruptcy and the industry lacked the capital necessary to maintain their systems. Unfortunately, after more than two decades since passage of the Staggers Act, the industry apparently continues to fall short of the revenue needed to provide a first class rail system for the Nation. As described above, today's rail executives will defend the status quo at all costs, and thus no solution to this problem can be negotiated among the relevant business interests. Unfortunately, captive rail customers likewise cannot expect regulatory relief from the Surface Transportation Board.

While the STB has made several positive changes to its operating procedures since the arrival of Chairman Roger Nober, not everything at the railroad regulatory agency is up for review. In an interview published in the newsletter "Rail Business," Chairman Nober, in response to a question about the reform sought by the captive rail customer coalition, stated, and I quote, "They have a lot of legitimate issues that they are raising. The core issues that they want to see done, though, are for the Congress." End of quote. Madam Chair, this is a clear and definitive statement that the changes we urge today cannot be pursued anywhere but in Congress.

S. 919 Is Not Re-Regulatory

Madam Chair, there must be a better way for the railroad industry to achieve long-term financial viability while providing efficient service at prices that will allow American business to compete successfully in the global market. The time has come to move toward a partnership between government, the railroad industry and their customers—a partnership that will ensure a national rail system that can meet the demands of our Nation's role in a global economy. We believe that balanced, fair legislation is needed to bring about a positive relationship between the railroads and the captive customers.

Madam Chair, the railroad industry argues that S. 919 is "re-regulatory". Rail industry documents cite two reasons. First, that S. 919 allegedly caps rail rates. Second, that S. 919 allegedly provides for "universal trackage rights", a concept under which any railroad could run over any other railroad's tracks. These allegations are simply not true.

S. 919 does not cap rates. In fact, S. 919 does not address the rate regulatory process at all. S. 919 does not change the current rate standards of the Surface Transportation Board. S. 919 does not force the railroads to provide rates to a "special group of customers" at "lower than market rates." S. 919 does not reduce the minimum captive rail customers must prove they pay, which is 180 percent of the railroads' variable costs, in order to seek rate relief at the STB. Notably, rail freight customers enjoying competition pay on average only 106 percent of the railroads' variable costs, even though railroads state they must receive 150 percent of their variable costs in order to earn a sufficient return.

S. 919 does not shift any burden of proof in rate cases to the railroads; perhaps unique in American regulatory experience, all burdens of proof are on the rail customer. S. 919 does not require the railroads to post tariffs or to obtain prior approval of the STB for any tariffs that they do post. Finally, S. 919 does not even prescribe the rate that a railroad must quote across a bottleneck. Rather, S. 919 simply requires the railroad to provide a rate across its bottleneck to the facilities of a competing railroad. Nor does S. 919 provide for "universal trackage rights" under which one railroad may operate over the tracks of another on demand.

What S. 919 does in the area of competition is overrule three interpretations of the Staggers Rail Act by the Surface Transportation Board and its predecessor agen-

cy that we believe were not contemplated by Congress in 1980. S. 919 over-rides the “bottleneck” decision of the STB in 1996 by requiring a railroad that has a customer captive behind a “bottleneck” to provide a rate across the bottleneck to the facilities of a competing carrier. It is important to recognize that the customer will remain captive for the bottleneck movement and that S. 919 does not prescribe the rate to be charged. However, we believe strongly that a railroad should not have the right to make a customer captive artificially over that portion of a movement where a rail transportation alternative exists.

S. 919 also overturns a 1986 interpretation of the “terminal access” provision of the Staggers Rail Act. “Terminal access” governs how railroads interact with each other at various rail terminals where they exchange railcars for the purpose of moving freight across the nation and how freight moves from the bottleneck carrier to the competing railroad in the San Jacinto and Toyota examples. Since the 1986 interpretation, no captive rail customer has won a “terminal access” case at the STB or its predecessor agency.

Finally, S. 919 provides a mechanism by which “paper barriers” can be removed by the STB. The Staggers Act of 1980 allowed the major railroads to “rationalize” their systems. One way they did this was to sell their less profitable track to short line railroads. However, through provisions in their sales or leases of this track, all of which provisions were approved by the STB or its predecessor, the railroad retained control of the traffic over the short line by requiring it to come back to the major railroad for long distance movement, even when the short line could deliver the freight to a second major railroad. Thus, these “paper barriers” have prevented captive customer access to rail competition. S. 919 outlaws these provisions in the future and allows the STB to remove existing provisions that have been in place 10 years, after making certain findings.

We believe S. 919 will enable the national rail system to evolve toward a more competitive system that serves the needs of our nation in a competitive global market. The Ocean Shipping Reform Act of 1998 is an example of how market forces can restore balance to commercial relationships. That act opened the door for large and small ocean shippers and ocean transportation intermediaries to put in place creative contracts that allow them to combine freight in multiple trade lanes and reduce shipping costs.

Conclusion

Madam Chair, we believe there is nothing in S. 919 that is either re-regulatory or radical. Yes, if S. 919 or its provisions were to be enacted, the railroads would have less opportunity to load up on at least some of their captive customers. There may be temporary difficulties as the railroads move to a new, modern business model. We understand the difficulties of the competitive environment. We operate in a competitive environment every day. However, we believe S. 919 will force the railroad industry to move to more normal commercial relations and partnerships with their captive customers. We believe this will result in increased rail business as the competitiveness of their captive customers improves. This evolution is crucial to the health and viability of the railroad industry, to our nation and to our ability to compete in the global market place.

Madam Chair, I am not here today to ask Congress to resolve issues that can be resolved by captive rail customers and the railroads working together, and with the STB, to benefit their own industries. We are in fact doing that. But what I have learned over the past year in immersing myself in this issue is that there is a basic impediment to affecting any meaningful move in rail competition and it cannot be resolved without the intervention of Congress.

Finally, Madam Chair, captive rail customers are not the enemy of the railroads— we are their best customers. But, the fact is that the STB’s interpretation of the Staggers Act has given railroads a monopolistic advantage over captive shippers, which provides a major, steady stream of revenue for the railroads. Furthermore, the rail CEO’s view of their fiduciary responsibilities blinds them from considering any course of action other than to protect and exercise this monopoly advantage. Consequently, they will not give this advantage away through negotiations with their customers. If the railroads, our business and the economy are to prosper, our relationship must evolve from one of captivity with all of its negatives to one of partnerships where mutually beneficial transportation agreements can be developed. But, we cannot get to that point without your help. The railroads won’t willingly change and the STB has declared this issue is for Congress. Thus, Congress must address this situation before the current system creates more serious problems that will be very difficult and costly to correct.

Thank you, Madam Chair, for this hearing, for your interest in this issue and for the opportunity to present our case to you and your colleagues.

Senator HUTCHISON. Thank you, Mr. Platz.
Our next witness is Mr. Ed Hamberger, the President of the Association of American Railroads.

STATEMENT OF EDWARD R. HAMBERGER, PRESIDENT AND CHIEF EXECUTIVE OFFICER, ASSOCIATION OF AMERICAN RAILROADS

Mr. HAMBERGER. Thank you, Madam Chairman, for holding this hearing and for giving the AAR the opportunity to testify and register our strong opposition to S. 919. Now, that comes as no surprise and one would expect the AAR is going to oppose S. 919. But I submit to you what was not expected was the overwhelming outpouring of opposition to this bill from the railroad customer community. Some may point to some "Inside-the-Beltway" groups as saying that there is support in the customer community for this bill. But I would prefer to point to the almost 400 letters that this Committee received from actual customers who oppose S. 919. And, Madam Chairman, approximately 40 percent of those come from companies who are either singly served or have singly served stations.

They range from large international companies like Ford, General Motors, and 3M to specialized customers like Wyo Ben Inc. in Billings, Montana, Borealis Compounds in Port Murray, New Jersey, and Arizona Pacific Wood Preserving, Inc., in Eloy, Arizona. They span the entire spectrum of economic activity, from Schneider Trucking to the Port of Lake Charles, Louisiana, to Oregon Steel Mills in Portland, Oregon, to Pennington Seed Company in Madison, Georgia.

Opposition includes the American Shortline and Regional Railroad Association and, of particular importance rail labor unions representing over 80 percent of our employees, who understand better than most the devastating impact that this bill would have on the railroad industry and their ability to earn a living.

Further, customer opposition comes right from the membership of some of those same D.C. organizations agitating for this bill. For example, some 20 letters come from NIT League members. The paper and forest product industry is well represented in its opposition, from international leader Georgia Pacific to Bennett Forest Industries in Elk City, Idaho. The utility industry, represented by DTE out of Detroit and Mid America Energy, along with one of the largest coal producers, Arch Coal, have registered their opposition. Even chemical industry customers, such as Texas Petrochemical LLP and Solvay Engineered Polymers, have written to oppose S. 919.

Finally, I am pleased that Randall Linville of Scoular Grain is on the panel to say why he and his fellow customers in the grain and feed industry urge you to vote down S. 919.

In fact, I submit this is not a fight between railroads and their customers. Rather, it is a fundamental difference between some in the customer community who cling to the belief that government should dictate the marketplace and the rest of America's shippers who understand and recognize how deregulation has improved service and lowered rates.

On the one hand, there are those customers, supporters of the bill, who believe that the hand of government regulation should intrude by placing a virtual cap on prices, on rates, at 180 percent, imposing uniform pricing by severely restricting differential pricing, and taking away from the railroads the operational efficiencies of routing prerogatives—policies all designed to drag rates down, thereby making it impossible for railroads to ever earn their cost of capital.

On the other hand are those customers who oppose S. 919 because they recognize the capital, massive capital, needs of the industry, because they recognize the fact that rates have gone down by an average of 60 percent since 1980 and, according to the GAO, those reductions have been spread across all customer segments. They recognize that the level of supply and demand means that there will be differences in pricing and that reregulating the railroads through S. 919 would rob them, the customers, of the opportunity to continue to compete in world markets by relying on the best freight rail system in the world.

As Senator Smith so aptly commented at the markup of the STB reauthorization bill in July, customers understand that having one railroad is far superior to having no railroad at all.

Now, I know from our discussions, Madam Chairman, that you understand these issues as well as anyone, but that you are indeed concerned about the STB processes, particularly for small shippers. We understand that concern and that is why we supported the amendment to the STB reauthorization bill adopted in July and reported out of this Committee calling for an expedited and affordable process at the STB for small shippers.

The Chairman of the STB has indicated today again his strong desire and intent to develop a workable system for small shipper cases and you have our commitment to be creative and cooperative in the STB proceedings, which will hopefully provide meaningful opportunities for truly small shippers to have their cases heard.

In closing, let me refer you to testimony before the Senate Appropriations Committee on September 12, 2000, from Eric Aasmundstad, then President of the North Dakota Farm Bureau, who posed the rhetorical question of whether railroads should even be allowed to operate as for-profit entities. I commended him then and I commend him today for so succinctly posing the policy question before this committee: Do the railroads remain a self-sustaining private industry or do we return to an era of heavy regulation, capital starvation, poor service, and eventual bankruptcy or nationalization.

Assuming we all agree, and I am sure we do, on the need for a viable freight rail network, there are only two places from which the capital necessary for investment in rail capacity can come from: the taxpayer or the private sector. I think it is terribly ironic today that even as we meet here the Senate is considering legislation that will determine what level of public subsidy is necessary for Amtrak. Now, as you go to the Senate floor to debate the pros and cons of spending \$900 million or \$1.4 billion or even \$1.8 billion for Fiscal Year 2004 on the Amtrak system, a system comprised of little more than 700 miles, remember that freight railroads, with 140,000 route miles, must routinely spend \$14 to \$15 billion annu-

ally—\$14 to \$15 billion annually—on maintenance and capital investment to give our customers the service they need.

So today I am joining with the shortline industry, with rail labor, and a large array of those same freight rail customers to implore you to oppose S. 919 and keep the opportunity and the responsibility for earning investment capital where it belongs, in the private sector.

Thank you, Madam Chairman.

[The prepared statement of Mr. Hamberger follows:]

PREPARED STATEMENT OF EDWARD R. HAMBERGER, PRESIDENT AND CHIEF
EXECUTIVE OFFICER, ASSOCIATION OF AMERICAN RAILROADS

On behalf of the members of the Association of American Railroads, thank you for the opportunity to appear here today to discuss issues related to freight rail competition. AAR members account for the vast majority of freight rail mileage, employees, and revenue in Canada, Mexico, and the United States.

Overview

Most of us here today would probably agree that the economic prosperity of the United States and our ability to compete effectively in the global marketplace depend on the continued viability and effectiveness of our freight railroads. Today, the more than 570 U.S. freight railroads account for 42 percent of the Nation's intercity freight ton-miles—more than any other mode. Over a rail network spanning some 143,000 route miles, U.S. freight railroads connect businesses with each other across the country and with markets overseas. Our freight railroads are a vital link to our economic future.

Some of us here today, though, disagree on what steps should be taken—and avoided—in order to safeguard this vital link and allow it to continue to serve our Nation's growing freight transportation needs. I respectfully submit to you that S. 919 and its companion bill in the House (H.R. 2924)—the so-called Railroad Competition Act of 2003—represents exactly the wrong approach. It re-injects government control over wide areas of freight rail operations. It is based on misunderstandings regarding the extent of the competition railroads face. And most importantly, it dooms freight railroads to a state of perpetual capital starvation. By preventing railroads from earning enough to sustain their systems, this bill would inexorably lead to deteriorating rail infrastructure, declining rail service, fewer rail jobs, and eventually the loss of rail service completely on an increasing number of rail lines. Such an outcome is not what our Nation needs or deserves.

It can be avoided, though, by maintaining the successful deregulatory system ushered in by the Staggers Rail Act of 1980. As the World Bank's railways adviser once explained, "Because of a market-based approach involving minimal government intervention, today's U.S. freight railroads add up to a network that, comparing the total cost to shippers and taxpayers, gives the world's most cost-effective rail freight service."¹

Railroads Since the Staggers Act

Before I explain in detail why S. 919 is so pernicious to railroads and to our nation, it is important to dispel the myth that ". . . the business model that [railroads] have followed since 1980 . . . does not seem to have been successful."² Consider the following:

- Rail intercity freight market share (measured in ton-miles) has been trending upward over the past 15 years, after decades of steady decline prior to Staggers.
- Prior to Staggers, railroads lacked capital to properly maintain their tracks. More than 47,000 route-miles had to be operated at reduced speeds because of dangerous track conditions, and the amount of deferred maintenance was in the billions of dollars. Since Staggers, Class I railroads alone have been able to spend well over \$300 billion on infrastructure and equipment, and rail infrastructure investments per mile of road have risen some 28 percent in inflation-

¹Louis Thompson, World Bank Railways Adviser. Quoted in the *Journal of Commerce*, July 29, 1998.

²"The Truth About Railroad Claims of Re-Regulation and Their Fear of Competition," prepared by Consumers United For Rail Equity, July 11, 2003.

adjusted terms. Today, the Class I freight rail network is in better overall condition than ever before.

- Rail productivity rose 183 percent from 1980 to 2002, compared to 10 percent in a comparable pre-Staggers period.
- Nearly all of these productivity gains have been passed through to rail customers (including proponents of S. 919) in the form of sharply lower rates—down 60 percent in inflation-adjusted terms from 1981 to 2002—saving shippers, and ultimately all of us, billions of dollars per year.

Numerous studies have confirmed the sharp drop in rail freight rates. For example, a June 2002 U.S. General Accounting Office (GAO) report analyzed rail rates from 1997 to 2000. The GAO found that “From 1997 through 2000, rail rates generally decreased, both nationwide and for many of the specific commodities and markets that we examined.”³

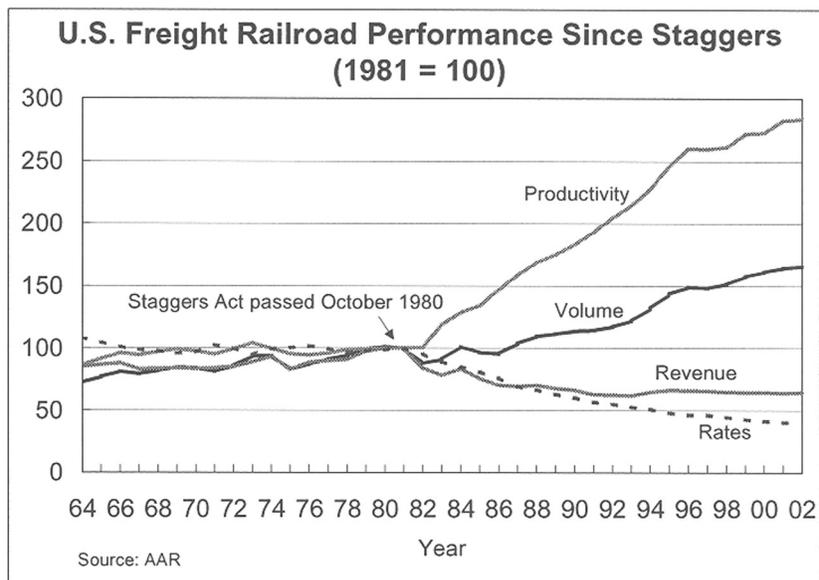
The GAO noted that “[t]hese decreases followed the general trend we previously reported on for the 1990–1996 period and, as before, tended to reflect cost reductions brought about by continuing productivity gains in the railroad industry that have allowed railroads to reduce rates in order to be competitive.” In a December 2000 report, the Surface Transportation Board (STB) found that “inflation-adjusted rail rates have fallen 45.3 percent” from 1984 to 1999. The STB also observed, “It is important to note that all types of rail customers, and not just those with competitive transportation alternatives, must have received some portion of the rate reductions we have measured here.”⁴

- The rail accident rate has fallen 68 percent since Staggers, and the employee injury rate is down 74 percent. Prior to Staggers, rail safety was generally worsening.
- Rail traffic volume (measured in revenue ton-miles) is up more than 60 percent since Staggers, far higher than comparable pre-Staggers traffic growth.
- By the 1970s, virtually every major railroad in the Northeast, including the giant Penn Central and several major Midwest railroads, had filed for bankruptcy. Most other railroads were financially weak. Since Staggers, railroads have improved their financial performance considerably, though as a whole they still fall well short of earning their cost of capital.

This is not failure by any definition. Thanks largely to the deregulatory structure instituted by the Staggers Act, the U.S. freight rail system today is universally recognized as the best in the world. From a public policy viewpoint, it makes no sense to make fundamental changes to a system that has delivered such large, widespread benefits.

³U.S. General Accounting Office, *Changes in Freight Railroad Rates from 1997 Through 2002*, June 2002.

⁴Surface Transportation Board, *Rail Rates Continue Multi-Year Decline*, December 2000.



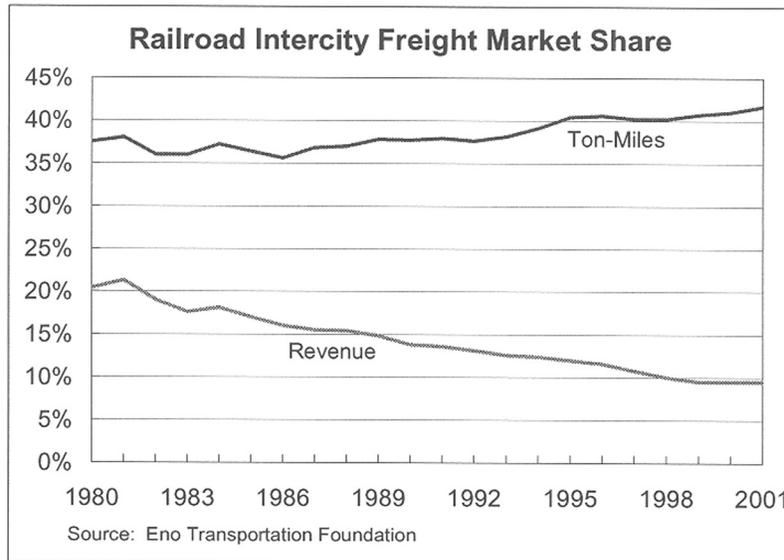
Railroad Market Power

Proponents of S. 919 typically maintain that the only competitive force that matters is rail-to-rail competition, and that service to a shipper by a single railroad is equivalent to monopoly power by the railroad over the shipper. This view overlooks the fact that railroads face extensive competition for the vast majority of their business, including cases where a shipper is served by only one railroad.

Railroads compete not just among themselves, but in the larger market for freight transportation services. Most shippers, including most of those served by only one railroad, are able to negotiate competitive rates for rail service. Shippers' considerable market leverage results from a combination of powerful competitive forces. It is unreasonable to pretend that these forces do not matter. These forces include:

- *Intermodal Competition.* Shipment via trucks, barges, or pipelines is a competitive option for most rail customers. Though railroads currently account for 42 percent of total intercity ton-miles, they receive less than 10 percent of intercity freight revenue. The rail revenue share has been trending downward for decades—a trend hardly indicative of excessive market power.

Railroads face significant competition from other modes even for commodities that some claim are "captive" to railroads. For example, U.S. Department of Agriculture figures indicate that trucks are the primary transportation mode for grain, and the chemical industry's own statistics show that railroads account for less than 20 percent of chemical tonnage that is transported.



- *Product Competition.* Since the demand for rail services is derived from the demand for the products of rail customers, competition faced by rail customers in downstream markets often constrains railroad pricing.

For example, the rates railroads can charge for hauling coal to electric utilities must be low enough to keep the electricity generated from the coal competitive, or utilities will generate (or purchase) electricity from sources other than coal. This end-product competition exerts substantial pressure on railroads to keep prices as low, and service offerings as appealing, as possible.

If a shipper has the option of substituting different products for those that require rail service, then the shipper can use this product competition to constrain rail rates. For example, if railroads attempt to raise soda ash rates too high, manufacturers of phosphate feeds and fertilizers can substitute caustic soda—which can easily move by truck—for the soda ash.

- *Geographic Competition.* The ability of many railroad shippers and consignees to obtain the same product from (or ship the same product to) a different geographic area also constrains rail pricing. For example, a poultry producer in, say, North Carolina can play a railroad delivering feed to it from Ohio off against local feed producers. Likewise, a railroad serving a Louisiana plastics facility must price its transportation service at a level that makes the plastics produced at that facility competitive at destination compared to plastics sourced from different states—or different countries—and transported by other carriers or modes.

If a railroad that serves a particular facility prices its movements or limits its service offerings in such a way as to render what is produced there uncompetitive with products made elsewhere, the railroad would lose the traffic entirely. Since such an outcome is contrary to the best interests of the railroad, a railroad will do whatever it reasonably can to avoid it.

- *Countervailing Power.* Many railroad customers are large industrial shippers with multiple plants and multiple products, some of which are served by other railroads and/or modes. These shippers can obtain price or service concessions by shifting or threatening to shift traffic among plants, causing the railroads that serve them to compete against each other or the other modes serving the plants.

For example, significant consolidation among electric utilities in recent years increasingly permits bundling the traffic of many plants into one large “package.” A utility with such a package can enhance its leverage for service to all its facilities, including those served by a single carrier. The threat of losing the busi-

ness is likely to generate price or service concessions by a railroad wanting to keep or win the contract, or to expand its current or future traffic volume. In recent years, consolidation in many other industries such as chemicals, coal, forest products, and steel has improved shippers' bargaining power over railroads. It is not unusual for a single customer to account for a large percentage of a particular railroad's revenues, especially within a specific commodity category. This relative importance and threatened loss of railroad revenues substantially increases the likelihood that a particular rail customer will be able to successfully exercise countervailing power in its negotiations with rail carriers.

- *Plant Siting and Long-Term Contracts.* Shippers can generate competition between railroads before a plant is built by considering transportation options and negotiating favorable contracts when evaluating potential plant locations. For example, rail access was an important consideration for Toyota when it recently decided where to locate a new U.S. auto plant. Moreover, over the long term, shippers can locate or relocate plants on the lines of different railroads.
- *Technological, Regulatory, or Structural Change.* Potential changes in the technology, regulation, and/or structure of a shipper's industry over time could provide leverage over railroads. For example, the siting of agricultural processing plants in or near production areas reduces demand for rail transportation and increases pressure on railroads to remain competitive.

Moreover, rail-to-rail competition today is vigorous, with rail customers constantly searching for ways to increase it, using connections to competing carriers (sometimes through a switching carrier) or establishing (or credibly threatening to establish) new connections through "build outs" of rail track.

For example, the Burlington Northern and Santa Fe Railway (BNSF) and a group of chemical shippers are moving forward with plans to build a new 13-mile line which would connect numerous major plastics and chemical-producing facilities in Houston with BNSF's network. The facilities, which ship thousands of rail carloads per year, are now served solely by the Union Pacific Railroad (UP). And according to recent press reports, United Parcel Service (UPS), which may be the single largest customer of the U.S. freight railroad industry, recently reportedly transferred significant traffic that had been moving on BNSF to UP instead. These examples are not anomalies. Rather, they are indicative of the way that railroads compete against each other all over the country.

What Would S. 919 Actually Do?

Railroads do not fear competition, including rail-to-rail competition, as long as it is the product of free-market forces. Unfortunately, S. 919 would artificially manufacture rail-to-rail competition through increased railroad regulation.

Through a variety of provisions, S. 919 would use the power of government to force down rail rates for certain shippers at the expense of other shippers, rail labor, rail stockholders, and the public at large. In doing so, it would transfer billions of dollars per year from the rail industry to favored shippers. If this happened, our Nation's freight railroads—who already offer the world's lowest rates and lag most other U.S. industries in terms of profitability—would be doomed to inadequate earnings, unable to make the massive investments required year after year to meet our Nation's rail transportation needs. Over time, unless taxpayers stepped in with a bailout, freight service over many rail lines would simply disappear. Highways would become more overcrowded and costly to build and maintain, environmental degradation would rise, safety would deteriorate, and shipping costs would rise. Policymakers should not let this happen.

Proponents of S. 919 object to the railroads' use of "differential pricing." Like businesses throughout the economy, railroads price their services on the basis of demand: shippers with the greatest demand for rail service pay higher margins than shippers with lower demand. At first blush, differential pricing may seem unfair or harsh. In fact, though, it is the fairest, most pro-efficiency, and most pro-competitive pricing system consistent with the continued functioning of the rail industry. All shippers, *including* those who pay a higher markup, benefit from differential pricing because it maximizes the number of shippers using the rail network and, therefore, maximizes the number of shippers who make contributions to railroads' huge fixed and common costs.

Five major provisions of S. 919 are discussed below. *Each* of them would involve a substantial increase in government regulatory control over the rail industry. Together, they threaten the very existence of freight railroading as we know it in this country. For this reason, S. 919 and all its provisions should be rejected.

A. “Bottleneck” Policy

A central element of S. 919 is a provision that would overturn the STB’s “bottleneck” policy. Bottleneck cases are those in which only one railroad (the “bottleneck” carrier) serves either an origin or a destination, but multiple railroads serve the remaining route. Proponents of S. 919 present the false image that most rail shippers enjoy full two-railroad competition from origin to destination. In truth, a very large proportion of rail shippers are served by just one railroad. Therefore, bottleneck policy has enormous significance for railroads.

Existing bottleneck policy is the result of court decisions going back to the 1920s and regulatory precedent going back even further:

1. As common carriers, railroads must provide rates and routes to move traffic from an origin to an ultimate destination.
2. Railroads cannot refuse to use multiple-railroad routes that are reasonably more efficient than their own single-line routes.
3. Absent a significant disparity in efficiency, however, a railroad does not have to “short haul” itself by moving traffic just to a junction with another railroad if it can move the traffic all the way to the ultimate destination.
4. A railroad is not required to provide a shipper with a separate rate for a segment of a through movement.
5. The rate for a through movement can be challenged for reasonableness under existing maximum rate regulation, and the reasonableness test is based on the cost for the entire through movement.

S. 919 would overturn existing bottleneck policy in every major respect. Upon shipper request, a bottleneck carrier would be required to short-haul itself—*i.e.*, provide a rate for a movement to, and interchange traffic at, any junction with another railroad the shipper so designates. The rate for the short-haul segment would be subject to maximum rate regulation based on the stand-alone cost of just that segment, while the rate of the non-bottleneck segment would be driven down toward variable cost.

By effectively capping rates on segments of a through movement, the new bottleneck policy would ordain that railroads would not be able to cover their full costs or replace their assets over time. The shipper would pay a lower rate, but it is a fallacy to claim, as proponents of S. 919 do, that the rate reduction is the product of more competition. Rather, it is the product of more regulation, and it is not sustainable.

Extended over the entire U.S. rail network, this provision could be expected to lead to a revenue loss to railroads of more than \$4 billion per year.⁵ No one has convincingly explained how such an enormous revenue shortfall could be recouped, or how, in the face of such a huge revenue loss, the rail industry could continue to make the massive investments required year after year to meet our Nation’s current and future freight transportation needs. S. 919 dooms the rail industry to a *non-competitive* outcome that is clearly at odds with the needs of our Nation.

The bottleneck provision of S. 919 would have other serious negative effects:

- It would lead to an explosion in regulatory proceedings and in costly behavior oriented toward regulatory ends.
- It would compel railroads to splinter traffic over hundreds of interchanges at the direction of shippers, since shippers would be able to dictate to railroads the location of interchanges. This would constitute a return to the “open routing” that characterized the pre-Staggers era and would reverse the substantial progress railroads have made since then in creating a streamlined, efficient nationwide network of run-through trains and efficient blocking.

B. Terminal Trackage Rights and Reciprocal Switching

Existing law provides that the STB “may require terminal facilities . . . owned by a rail carrier . . . to be used by another rail carrier” and “may require rail carriers to enter into reciprocal switching agreements” if the STB finds either measure “to be practicable and in the public interest.”

In a series of decisions, the STB—and the Interstate Commerce Commission (ICC) before it—have consistently required that the owning carrier first be found to have engaged in anti-competitive conduct before granting terminal trackage and recip-

⁵Based on the 2001 STB Costed Waybill Sample. If in 2001 the rates for all traffic affected by regulation had been held to a revenue-variable cost ratio of 180 percent, the railroads would have received \$9.2 billion in revenue instead of \$13.4 billion, a revenue loss of \$4.2 billion (with no associated reduction in expenses).

rocal switching rights. This ensures that in STB access cases, like comparable court antitrust cases, relief is predicated on actual competitive conditions and marketplace demand, rather than simply on regulatory intervention on request designed to promote artificial competition. The mere fact that the incumbent is the sole railroad serving a shipper, or that the incumbent chooses not to grant another carrier access, or prices differentially, has never been considered a competitive abuse in this context.

S. 919, though, would upset this structure. It would force the STB, upon request by a shipper, to order railroads to enter into reciprocal switching agreements and provide terminal trackage rights. If, as is likely the case, the railroads involved cannot agree on access terms, government regulators would set them, including the access fee. S. 919 explicitly eliminates the requirement that a railroad must have engaged in anti-competitive conduct before such action could be mandated.

This provision of S. 919 could be interpreted as mandating terminal trackage rights and reciprocal switching whenever it was operationally feasible—thereby essentially creating forced access on demand in terminal areas. As in the bottleneck provision discussed above, the purpose of this provision is to obtain lower-than-market rates by artificially manufacturing rail-to-rail competition in ways beyond what a competitive market could justify.

Meanwhile, regulators would be inundated with unwarranted requests from shippers to grant terminal access. Moreover, regulators would need to step in to resolve myriad disputes covering priorities for use of track, operating conditions, and a host of other issues. Complex, lengthy, and costly disputes over terms of use would be inevitable as government interference replaced direct negotiation among railroads and shippers and between railroads. In addition, the complexities involved in coordination between track owners and operators could have significant safety ramifications.

C. Final Offer Arbitration

Under S. 919, railroad rate and service disputes could be subject (at the shipper's sole discretion—the railroad would have no choice in the matter) to binding "final-offer arbitration" (FOA).

The FOA process would be completely outside the STB's jurisdiction. An arbitrator's decision could be completely divorced from regulatory precedent and sound economic principles—an unacceptable condition in any case, but especially in the rail context in which "final offers" could differ by millions of dollars. Moreover, there would be no requirement that an arbitrator take into account the existing statutory requirement that regulators recognize that "rail carriers shall earn adequate revenues."⁶

Railroads know of no other case in which private-sector suppliers of a good or service are forced by the Federal government to use binding arbitration to set a price just because the purchaser desires a lower price. It is no more valid for the government to force binding arbitration on railroads than it is to force it on chemical companies, plumbers, supermarkets, or any other business.

This provision too is a frontal assault on railroads' use of differential pricing because it directs arbitrators to base rate decisions in many cases on rates paid by rail customers in the most intensely competitive markets. By definition, these markets have the lowest rates. But a railroad must have a sufficient mix of low-demand, low-margin and high-demand, high-margin shippers to cover its huge common and fixed costs. By using regulatory strictures to eliminate railroads' high-margin traffic and effectively cap rail rates, this provision of S. 919 also dooms railroads to a perpetual inability to cover costs.

Today, railroads and shippers can (and sometimes do) voluntarily agree to use binding arbitration if both parties deem it desirable. There is a huge difference, however, between the voluntary use of binding arbitration and a mandate forced on private businesses by the power of government. In addition, the rail industry has suggested ways to make rate cases quicker and less costly to resolve, while retaining the use of sound, well-established economic principles as a basis for decisions.

D. "Areas of Inadequate Rail Competition"

In a provision of striking scope, S. 919 proposes that the STB designate a state or any part of a state to be an "area of inadequate rail competition" if any of a variety of criteria are met. The criteria used to define these areas are so broad and vague that all or most of the country would qualify—an absurdity on its face, given the intensity of competition railroads face for the vast majority of their traffic. In

⁶ 49 U.S.C. 10701 (d)(2)

“areas of inadequate rail competition,” government regulators could assume control of huge areas of rail operations.

For example, regulators could:

- Control current and future rail rates;
- Force an owning railroad to allow another railroad access to its tracks where it could “cherry-pick” traffic;
- Force an owning railroad to carry freight to a junction with another carrier at a rate set by a regulator.

Regulators would be expressly prohibited from considering whether railroads engaged in any sort of anti-competitive conduct before ordering these actions.

Railroads are open to ways to improve the existing regulatory regime. However, a return to heavy-handed government regulation—as dramatically exemplified by the concept of “areas of inadequate rail competition”—is anything but an improvement.

E. Interchange Agreements (“Paper Barriers”)

Since passage of the Staggers Act, Class I railroads have spun off tens of thousands of miles to local or regional railroad operators whose lower costs and closer ties to their customers and communities enable them to operate at a profit where Class I railroads could not. These new carriers have preserved rail jobs and rail service—often in rural areas—that otherwise would be lost.

At the time of some line sales, the parties involved voluntarily agreed to a lower sales price in exchange for an agreement by the new railroad to interchange future traffic solely or largely with the selling railroad. In effect, the purchase price included a cash component and a future carload component. S. 919 would prohibit future line sales from including these types of agreements (sometimes called “interchange agreements” or “paper barriers”), thereby prohibiting interested parties from voluntarily using a legitimate tool that has helped preserve rail service on a significant number of rail lines. It would become more difficult for buyers to purchase and keep marginal lines in operation, since their up-front costs would increase. As a result, an increasing portion of the rail network would likely lose rail service entirely through abandonment, rather than have it transferred to short line carriers.

Moreover, S. 919 would allow the STB to declare interchange agreements more than ten years old to be null and void. This would constitute blatant government interference in the sanctity of private contracts—akin to the government deciding that the price someone sold his house for ten years ago was too high and ordering him to rebate some of the sales price to the buyers. It is another example of a provision in S. 919 that proponents would never support if applied to their own firms, but are willing to subject railroads to.

Does S. 919 Reregulate Railroads?

For all the reasons discussed above, it is beyond serious dispute that S. 919 would substantially increase government control over freight rail operations in numerous ways—as good a definition of reregulation as any. The ways that government control would be increased are not just minor intrusions into rail affairs. If enacted, they could be expected to lead to the transfer of billions of dollars of rail revenue each year to favored shippers.

Proponents of S. 919 do not even try to explain how railroads would be able to recoup this revenue, or how railroads could possibly make the huge ongoing investments they need in the face of the capital starvation they would confront. Instead, proponents of S. 919 simply claim “there must be a way”⁷ for railroads to remain financially healthy under the legislation. Given how critical freight railroads are, claiming “there must be a way” is not good enough.

A couple of years ago, a prominent Wall Street analyst remarked that “Capital flows to the areas of highest return. If . . . new regulations change the rules of the game and ensure poor returns, then the Street will disinvest, (or further disinvest) causing managements to begin to reallocate cash and begin “harvesting” the business. They will have no choice.”⁸

He was right. In our economy, firms and industries must produce sufficient earnings or capital will not be attracted to them. The electric utility industry understands this. Just a few weeks ago, in the wake of the huge blackout that struck the Northeast, the Midwest, and Canada, the electric industry’s major trade association suggested that “FERC and the states should utilize innovative transmission pricing

⁷“Draft Reply to Railroad Letters,” June 20, 2003, prepared by supporters of S. 919.

⁸Anthony B. Hatch, independent railroad analyst, in a speech before the American Short Line and Regional Railroad Association, September 14, 1999.

incentives, including higher rates of return, to attract capital to fund needed investments in transmission . . . [T]he amount of money that FERC

[currently] allows investors to earn on transmission facilities still is not in line with what they can earn on other investments.”⁹ Utilities recognize that “the rate of return that regulators allow for investments in new and augmented transmission facilities must be high enough to be competitive with investors’ other options for using their money or sufficient investment funds will not be forthcoming.”¹⁰

The chemical industry understands this too. For example, one of Dow Chemical’s basic financial goals is to “earn an average of 3 percent above our cost of capital.”¹¹ DuPont states that “Our goal continues to be to invest in attractive, globally competitive businesses that generate returns significantly above the cost of capital.”¹² BASF, the world’s largest chemical company, notes, “We measure our performance and our corporate decision-making against the return required by our investors—our cost of capital. We strive to earn a premium above this cost of capital.”¹³

Railroads agree with this sentiment. Without the ability to cover total costs and earn an adequate return, railroads—like electric utilities, chemical companies, or any other firm—would be unable to maintain (much less increase investment in) their infrastructure and equipment, resulting in deterioration and/or shrinkage of the national rail system. That is exactly what S. 919 would do. S. 919 ignores the fundamental point that rail competition is enhanced only when the railroads are healthy, not when their earnings, which are already substandard, are severely and artificially restricted. If S. 919 were enacted, the already large gap between the rail industry’s cost of capital and its return on investment would only widen—taking railroads farther away from the financial performance that proponents of S. 919, including some of the firms in the electric utility and chemical sectors, expect from their own businesses.

Railroad Customer Service

It is a fact of life in the rail industry that in addition to facing unrelenting competition, the service requirements of rail customers are continually becoming more stringent. Railroads recognize that service shortcomings have been a major factor behind shipper dissatisfaction in recent years, including shipper dissatisfaction that has sometimes manifested itself in calls for railroad reregulation.

I am happy to say, though, that railroads have made tremendous progress in the customer service area. There may be isolated pockets here and there that have some problems (as one would expect on a rail network with enough trackage to circle the globe nearly six times), but overall the U.S. freight rail system today is operating smoothly. Merger-related service disruptions in both the west and the east are now a thing of the past, as the synergies and efficiencies that were the basis for the mergers in the first place are taking hold.

Shippers and others recognize these improvements. Just a few recent examples:

- In an article in the August 18, 2003 issue of *Traffic World*, UPS spokesman Norman Black says, “The most important thing we see from all of our rail partners is a huge commitment to customer service. They’re doing a much better job. Trains are running when they say they’re going to run, and arriving when they say they’re going to arrive. From a UPS standpoint, that’s all we want.”
- In a July 25, 2003 article in *The Wall Street Journal*, Bill Zollars, the CEO of Yellow Corporation, one of the Nation’s largest trucking companies, says railroads “are more focused on the customer and growing their business than I’ve ever seen.”
- A February 6, 2003 article in *Purchasing* magazine notes that “[R]ail shippers continue to report consistent efforts and improvements in the level of service they receive from carriers. . . .”
- In a *Traffic World* article on rail service improvements on January 27, 2003, the rail operations manager at a major U.S. petrochemical company credits rail-

⁹ Edison Electric Institute, “Five Steps That Would Help Assure That We Have the Reliability Standards and the Transmission Capacity We Need Going Forward,” August 19, 2003.

¹⁰ Stanford L. Levin, “Electricity Competition and the Need for Expanded Transmission Facilities to Benefit Consumers,” prepared for the Edison Electric Institute (September 2001), p. 15.

¹¹ “This is Dow Public Report—2000 Results: Economic Performance,” accessed on the Internet at <http://www.dow.com/about/pbreports/00results/econ/index.htm>.

¹² Quote from Tony Pompeo, DuPont Canada CFO, in “CFO’s Address to Shareholders—Annual Meeting 2000,” accessed on the Internet at http://www.dupont.ca/english/news/Speeches/2000_annual_cfo_address.html.

¹³ “Financial Targets and Management of the BASF Group,” part of “Financial Report 2002,” accessed on the Internet at http://berichte.basf.de/en/2002/finanzbericht/finanzziele/?id=V00-133vtG**bir100.

roads with doing “an admirable job of identifying areas of concern and then addressing the problem.”

- Canadian National (CN) received on-time service awards from Toyota Canada in 2003 and 2002 and was named the “Canadian Carrier of the Year” for 2002 by Quaker-Tropicana-Gatorade. In addition, CN’s Wisconsin Central subsidiary will be a recipient later this month of a 2003 Quest for Quality Award, having been selected by the readers of *Logistics Management* as one of the Quality Carriers in the Railroads (Standard Rail Service) category.
- In July 2003, Wal-Mart recognized Burlington Northern and Santa Fe (BNSF) Railway as the recipient of Wal-Mart’s annual “Carrier of the Year” award. “BNSF has provided an outstanding service for Wal-Mart,” said a Wal-Mart official. “It is our pleasure to recognize their associates for commitment to quality and customer service.”
- In April 2003, Toyota Logistics Services recognized Norfolk Southern Railway (NS) with two awards for service excellence during 2002. Toyota awarded NS a “Logistics Excellence Award” for superior quality performance among rail carriers and an on-time performance award for transportation service. NS was also named Coors Brewing Company’s 2002 “Transportation Supplier of the Year,” the first time NS received the award.
- In June 2003, CSX Transportation was awarded the Gold Carrier Award by Shell Chemicals for the quality of the rail carrier’s overall performance in moving Shell chemicals in 2002. The award marks only the third time in the award’s 10-year history that a rail carrier was so honored. A Shell official remarked that “CSXT has worked hard at becoming one of the few Gold Carrier recipients. We at Shell would like to give CSXT and its employees a well-deserved congratulation.”
- In April 2003, Union Pacific Railroad (UP) was also named a recipient of Toyota’s “Logistics Excellence Award.” UP also earned a General Motors “Supplier of the Year” Award for 2002. A GM official remarked that UP’s “performance and contributions have been critical in helping GM become the industry’s low cost producer of high quality vehicles. They serve as a role model for other suppliers.”
- In a recent communication, a manager at a Louisiana agribusiness firm wrote: “I have been the complex manager of Terral Farm Service in Delhi, Louisiana for ten years. Over that period of time, we have shipped thousands of rail cars with Kansas City Southern and before that with Mid South. This year, the individuals at KCS performed as well as I could ask for. The service was almost perfect.”
- Canadian Pacific Railway’s (CP) won the prestigious 2003 Franz Edelman Award for Achievement in Operations Research and the Management Sciences. The award, recognized as the “Tech World Series” and sought after by operations researchers and planners around the world, is presented by the Institute for Operations Research and the Management Sciences. CP won the award for its work on improved scheduling that yields significant, direct benefits to the company’s customers.

I firmly believe that the overwhelming majority of railroad customers believe that railroads are meeting their freight transportation needs efficiently, cost-effectively, and fairly. I also believe that most rail customers do not support reregulation, and that many of those who have expressed support for S. 919 would rethink that support if they paused to consider all the implications of the legislation.

We have concrete evidence of the fact that many shippers oppose reregulation. We asked shippers opposed to reregulation to write to members of this committee to express their opposition. Hundreds of shippers, large and small, have done just that. They cover the gamut of rail shippers—auto manufacturers, chemical companies, steel companies, grain companies, coal companies. Some are “singly served” and some are not.

I’d like to share a few excerpts from those letters with you:

- The Alliance of Automobile Manufacturers, a trade association whose members account for more than 90 percent of U.S. vehicle sales, wrote: “Alliance members—as major users of the rail system—view [S. 919] as an attempt to re-regulate the rail industry and undo the progress made since the Staggers Act deregulated it in 1980. We strongly urge the Committee to reject this legislation and maintain the free market system that has been beneficial for shippers and the railroads alike.”

- The Port of Los Angeles, one of the largest and busiest ports in the world, wrote, “Increased efficiency and improved service. . .has enabled the rail industry to divert significant amounts of business from highway to the intermodal option. . . . None of this would have been possible without the billions of dollars that the railroads have invested in new technology and to improve locomotive and car fleets. To maintain these high standards, railroads will need to continue that level of investment in the future. However, their ability to do so may be negatively impacted by the re-regulation legislation currently being proposed. . . .Our railroads have recovered from the serious financial troubles, including numerous bankruptcies, of the 1970s. We cannot run the risk of that happening again.”
- Martco, a Louisiana lumber and forestry firm, wrote, “Senate Bill 919 is an attempt to reregulate the railroad industry. . .Initially the bulk shippers and bulk industries would perhaps benefit by the establishment of some noncompensatory rate structures. The reduced returns would have to be addressed and they would, through the passing of increased rates to the non-bulk and smaller shippers. Thus the pre-Staggers Act cycle would return: reduced rate for shipper A, must be met by increased rates or reduced service for other shippers who then will divert traffic onto our overcrowded highway system . . . thereby increasing logistics costs to all parties while further reducing the rail industry route structure. Soon rail rates for the few large bulk shippers would have to be increased given the absence of other traffic to spread cost and hopefully provide a return.”
- The president of Schneider National—the nation’s largest truckload motor carrier—wrote that if S. 919 were passed, “Schneider National and its thousands of shipper-customers would suffer significantly from the loss of a cost effective and efficient intermodal rail system and would be forced to divert much of our volume onto the already crowded highway system. . . .We believe that additional regulation of the rail system would have a detrimental effect on the progress achieved through a free market.”
- The CEO of Kokomo Grain in Indiana wrote to express “strong opposition” to S. 919, writing “[E]ven those shippers that are only served by one railroad and have limited shipping alternatives are better served by a business environment that is not hindered by re-regulation. On the whole, the deregulation of the railroad industry in 1980 . . . has been a positive experience for American business. I do not want to see those gains and benefits thrown aside with a move towards blanket re-regulation to fix certain competitive concerns of some shippers that would be best addressed in other fashions.”
- The general manager of the Port of Montana wrote: “S. 919 . . . would significantly reduce railroad revenues by forcing upon them governmentally mandated price “competition” which the free market would not otherwise sustain. . . . I urge you to continue your support of the current rail regulatory structure. I believe this is the best way our company can guarantee continued access to a healthy railroad network, a network which is critical to our company’s competitive success in the domestic and global marketplace.”
- Chemical company Dyno Nobel wrote: “Clearly all shippers would like to reduce the rates that they pay for transportation services, but calling for re-regulation of the rail industry is remarkably short sighted and is a move that we do not support. In the long run, all rail users will be the losers because the inevitable result will be to devastate the ability of the railroads to continue providing their present level of service, much less to make vitally needed investments for the future.”
- Pavers Supply Company in Conroe, Texas, wrote: “For 33 years we have relied on railroads for transportation of aggregates used in road construction. Railroads will continue to be the most efficient means to deliver the products we need. We strongly urge you to keep our railroad system financially self sufficient and independent of unnecessary government regulation by voting your opposition to S. 919.”
- Oregon Steel Mills, one of the most diversified minimills in the United States, wrote: “[D]ue to the influence of the unregulated marketplace, rail service is safer, more reliable, more efficient, and less costly. The situation has been good, not only for the industry itself, but also for customers like Oregon Steel Mills, who use rail service extensively. We urge you to continue your support of the current rail regulatory structure.”
- The Port of Beaumont in Texas wrote: “The Port of Beaumont and our customers depend on an economically viable rail network capable of sustaining

itself in today's competitive environment. Regulation of the entire rail industry is very short-sighted and ill advised at this time. I strongly suggest the Senate reject S. 919 and all other proposals that would re-regulate freight railroads."

The point is this: for every shipper who supports reregulation, there are many others who oppose it. And they oppose it because they rely on rail service and do not want to return to the failed policies of the past.

Conclusion

The partial deregulation of U.S. freight railroads brought about by the Staggers Act has worked. Railroads have been able to upgrade their systems, reinvest hundreds of billions of dollars in productive rail infrastructure and equipment, provide higher levels of service, raise traffic volumes, dramatically increase productivity, improve profitability, and improve safety—while at the same time sharply lowering rates for shippers.

The proposals for rail reregulation in S. 919 threaten all of these gains and are contrary to economic logic and sound policy. They would severely harm rail service, the shippers that rely on that service, and the national economy. They represent the legacy of failure and should be rejected.

Senator HUTCHISON. Thank you, Mr. Hamberger.

Our fifth witness is Mr. Randall Linville, President and CEO of the Scoular Company.

STATEMENT OF RANDALL L. LINVILLE, PRESIDENT AND CHIEF EXECUTIVE OFFICER, THE SCOULAR COMPANY

Mr. LINVILLE. Good afternoon, Madam Chair and Committee. My name is Randall Linville. I am President and CEO of the Scoular Company in Overland Park, Kansas. Scoular is a medium-sized private firm engaged in the marketing of agricultural products throughout North America. We have shipping and receiving facilities in a number of states.

I appreciate the opportunity to come before this Subcommittee to express Scoular's view on the proposed Railroad Competition Act as it might affect grain marketing in the United States. My personal experience in the grain business extends over 25 years in which the major Congressional actions affecting the railroad industry have been the Staggers Act and the STB. From the perspective of Scoular's businesses, I can say without equivocation that railroad efficiency, productivity, service, and innovation have improved substantially in that time frame.

Railroads provide a vital link, but nonetheless just a link, in the supply chain for U.S. agriculture. With production concentrated in the heartland, consumption pulls products to the coastal areas in response to demand from domestic and foreign markets. But merely moving products does not add value to them. The value is added by efficient relocation of supply to demand. Our success depends on seeing, understanding, reacting—and reacting to changing market forces.

Artificial pricing influences will serve only to mask the very market signals that we serve, ultimately impeding our ability to compete in a global marketplace. There are many examples of industry adaptation to changing market forces and I will just cite one. The dairy industry in California has expanded tremendously since 1980 in response to the growing population there. Local grain supplies were inadequate for feed and initially were augmented by rail barley supplies from Montana. Then, with larger unit size and improved operating efficiency, California feed mills eventually gained access to the western corn belt, replacing barley in their rations

with that corn. Just as the corn market adapted quickly to this new demand, the barley producers adapted by finding export markets and by converting production to milling wheat for California flour mills.

These changes did not occur because of railroads. They occurred because all of the participants in the supply chain sought the best use for their products at the greatest efficiency.

I believe that economic development in U.S. agriculture is occurring as it should. As we increase efficiency and productivity, we are finding new markets for our products. We are positioned to increase the market share that is so critical to the U.S. balance of trade. We know that adaptation never ends and we have learned much about responding quickly and well to the market forces shaping supply and demand on a daily and yearly basis. Adaptation requires creativity and flexibility and it may cause short-term stress, but adaptation is imperative if U.S. agriculture is to prosper in the global economy.

Constant evolution in the agriculture marketplace is a given. We need to operate in partnership with our carriers, using their resources to make our businesses competitive and sharing our market knowledge with them to improve their operational efficiency. For 20 years we have done this and the railroads' responsiveness to our needs has never been greater.

This is not to suggest that differences never exist, but rather that, working business to business with the carriers, we have been successful in achieving effective and productive resolution to our differences. Unfettered by regulation, railroads can and do devote their resources to the optimal utilization, just as we do with our resources and every business should be free to do. U.S. agriculture cannot afford to absorb costs that deliver no benefit. If the Railroad Competition Act is passed and results in rail carriers serving markets that they may otherwise find unattractive, or if they are required to maintain infrastructure in markets without sufficient rail traffic to generate returns on their investment, the entire system will be burdened with those costs. Not only are those costs unfair, they are difficult for our businesses to absorb. But more importantly, they tax U.S. agriculture, which is already in a struggle for market share worldwide.

I strongly believe that we must stay the course and entrust to American agribusiness its competitive place in the world.

Thank you for inviting me to share my thoughts.
[The prepared statement of Mr. Linville follows:]

PREPARED STATEMENT OF RANDAL L. LINVILLE, CHIEF EXECUTIVE OFFICER,
THE SCOLAR COMPANY

My name is Randal L. Linville. I m the President and Chief Executive Officer of the Scoular Company ("Scoular") . . .

I have been in the grain business since 1977 and with Scoular since 1984 in various capacities, including merchandising, management and executive management. I appreciate the opportunity to appear before this committee to present Scoular's views concerning S. 919 (The "Railroad Competition Act of 2003").

Scoular is a privately-owned company that started in the agriculture business 111 years ago. We consider Scoular to be middle-market in size and scope, considerably larger than many local or regional companies and cooperatives, yet smaller and much less diversified than the major multinational agricultural firms headquartered in the U.S. Our business is focused on meeting the supply chain needs of producers

and end-users of agricultural products. Although we are marketing agricultural goods, we bundle these with a logistical solution that creates the best value for our customer. In doing so, we regularly use truck, barge, rail, container and vessel freight.

For purposes of the discussion today, my comments will focus primarily on our grain business, which is Scoular's core and largest business. Geographically, Scoular's business spreads across North America, with subsidiaries in both Canada and Mexico. We operate grain handling facilities in many states of the U.S., including California, Montana, Utah, Idaho, Kansas, Nebraska, Texas, Missouri and Ohio.

Scoular's direct business is predominantly domestic, but dependence on export markets is an inescapable fact of life for U.S. agriculture. For both bulk commodities and value-added products, production exceeds domestic demand. This means that competitiveness in the world market is not a matter of choice for U.S. agriculture, it is a matter of survival.

The Railroad Competition Act of 2003 comes at an interesting time in rail history. During my career of over 25 years, the Staggers Act and the creation of the Surface Transportation Board are the only significant congressional actions directly addressing the rail industry. Both reduced government involvement. The evolution of the rail industry in that time period has been remarkably beneficial. From the perspective of Scoular's business, I can say without equivocation that efficiency, productivity, service and innovation have improved substantially since 1980.

The railroads provide a vital link, but nonetheless just a link, in the supply chain for U.S. agriculture. U.S. production is concentrated in the heartland, while consumption is concentrated increasingly on the perimeters in large coastal population centers and through U.S. ports to export markets. Like industries that must respond to supply and demand, the agriculture industry strives to meet these needs in the most efficient way possible. Scoular believes that freedom from artificial pricing influence is as critical to the domestic agriculture markets as we know it to be in global markets.

Let me provide a few illustrations that help demonstrate the role of rail carriers in the efficiency gains of U.S. Agriculture over the last few decades.

To meet the demands of a rapidly growing population, the California dairy industry has expanded. When it outgrew the capacity of California grain producers to supply it with feed, demand was created for Montana-grown barley that was shipped by rail to California. As the rail infrastructure continued to evolve, allowing for larger units to be shipped on predictable schedules, California feeders gained access to the western corn belt. Corn gradually replaced barley in the dairy ration, contributing to improved productivity. To adapt, barley producers began to ship to the Pacific Northwest for export and also to produce wheat for shipment to flour millers in the LA basin. None of this occurred for or because of the railroads. Rather, it is an example of adaptation that occurs when producers and processors strive to improve efficiency and productivity.

Consider also the development of the ethanol industry in the U.S. This evolution has been underway for three decades, driven nationally by a desire for reduced dependence on foreign oil and locally by an interest in value-added agriculture. A map of ethanol production sites would quickly demonstrate that these have been built predominantly in the corn belt, taking grain off the railroads and diverting it to local consumption in ethanol plants. I read recently that a unit train of ethanol was shipped from South Dakota to California. Again, the conversion of corn to ethanol in South Dakota was a response to economic forces well beyond the control of the railroads.

Another example would be the concentration of cattle feedlots in the southern plains. These evolved because warmer temperatures allow for more efficient utilization of energy in fattening cattle and the local supplies of feed were excellent. However, the growth of cattle numbers coupled with declining water supplies has turned a grain surplus market into a grain deficit market. Investment in infrastructure by railroads and private industry has created a cost-effective way to import the volume of feed grains needed to maintain cattle production in this region on a basis that will allow it to compete in the world market.

So what do these illustrations indicate? To me, they indicate that economic development is occurring as it should in U.S. agriculture. We are creating more markets for our products. We are increasing efficiency and productivity. We are positioned to maintain or increase global market share. We understand that this is a dynamic process that requires adaptation throughout the supply chain. We know that Montana barley growers replaced the California dairy shed with alternative markets. We know that some grain elevators in South Dakota are now receiving harvest grain and storing it for future use in ethanol production. We know that cattle feeders on the southern plains have found a way to stay competitive.

In each of these instances, the producers and processors were compelled by market forces to adapt, but the temporary strain of adapting should not mask the beneficial outcome when resources ultimately find their highest and best use. If legislation had altered the impact of market forces, adaptation would have been impeded and the economic disequilibrium that stimulated it would have been prolonged.

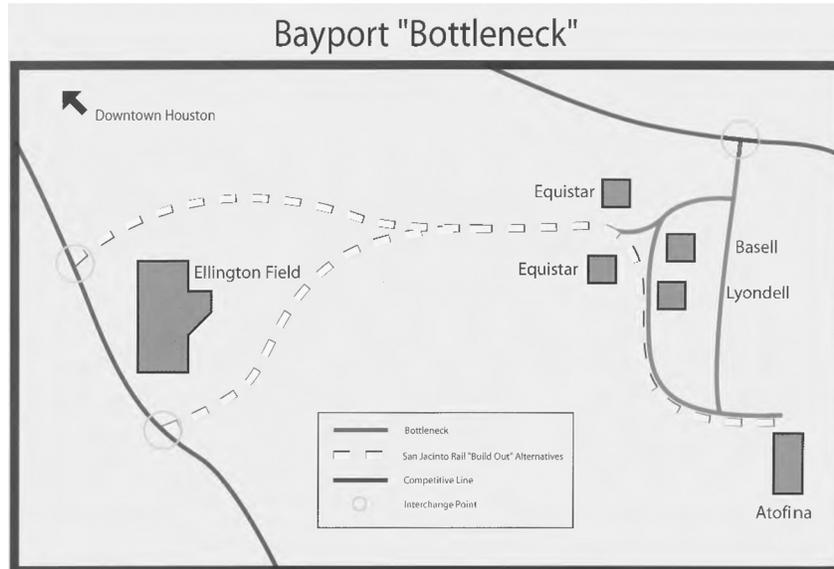
The evolutionary changes we have seen and continue to expect require a railroad industry with the capacity and incentive to adapt with U.S. agriculture. If Federal law makes it the duty of railroads to ensure that competition exists for every shipper, railroads will be forced to divert funds to uneconomic use. Instead of investment where the market demands improved rail access, they may be creating it in a market where non-rail alternatives are better. Instead of encouraging a captive shipper to invest in efficiency improvements, they may have to take service away in order to provide it elsewhere. Railroads do not create competition for agricultural products, but they can substantially impair the ability of those products to compete if they are unable to respond to market signals.

S. 919 is important to Scoular because we understand how costs are borne. If the rail transportation system is forced to absorb costs that are not returned in the marketplace, rail will be unfairly disadvantaged versus other modes of transportation. Shippers that alone are not sustainable will be subsidized to the detriment of their eventual adaptation.

From a corn grower in Minnesota to a flour miller in Los Angeles, all depend on an efficient and responsive rail transportation system. Without that, the entire agricultural supply chain will be penalized and, most importantly, foreign markets for U.S. production will be jeopardized.

Senator HUTCHISON. Thank you very much. I thank all of you for the very good testimony. I would like to start with a couple of questions and then we will move on the list.

Mr. Nober, on October 8, a Harris County court at law judge blocked BNSF's attempt to build a new rail line into the Bayport industrial district. Here is a picture of the Bayport bottleneck. The rail was proposed to be built here [indicating], with several people contributing to the cost of it, and the judge blocked it without giving a reason.



Mr. Hamberger said in his written testimony that this was one example of actually how competition can work. But in fact we are

now seeing the difficulties of the process of executing a successful buildout which was ordered by the STB.

My question is: Will STB get involved in the appeal of this case or what would be your thoughts about it?

Mr. NOBER. Well, Senator Hutchison, we certainly are concerned about the decision that the state court put forward. The first thing is that I would say the legal situation in this case is, to be fair, to be honest, muddled. As you said, the judge—the case that was before the Texas state court was one to take certain by the City of Houston by eminent domain.

To back up for a minute, when we approve a new rail line build-in that is a permissive authority. We give them the right to add to the national freight rail network if they can then acquire the right of way. They then went to the state court and Texas has state laws that govern condemnation and has certain doctrines that apply to that.

Here many, many questions about the railroads' ability to take Houston city property by eminent domain were raised and, as I understand it, the judge issued an order denying the ability to take the case, to take the property by eminent domain, but without a reason. So until we—we have been in close contact with that. I have here today our environmental attorney who handled the appeal. We just got an update on that 15 minutes before the hearing and the answer is we do not have an opinion from the court yet.

So until we see on what basis the judge blocked the build-in, whether or not we can get involved in a state court proceeding I just do not know. We certainly are committed to seeing this go forward as well and we will do what we can to protect our regulatory decision.

At the same time, there is also a case in Federal court going forward challenging the sufficiency of our environmental impact statement. While we feel we did an over and above job on the environmental impact review of this case, this has not been the best month for our environmental impact statements in court, so we have to be mindful of that as well.

But we certainly stand behind our decision. We believe that it is an important competitive option here. We think build-ins are a critical part of our regulatory doctrine and we would like to see it go forward.

Senator HUTCHISON. I do think it sort of points out how hard it is to get competition, and I would prefer to see some mechanism where you could get a rate, some kind of a rate across the lines. It would be a whole lot less expensive. But I realize there are difficulties with that as well.

But you said in your testimony that the only viable rate cases really come from the coal industry. In these cases it is estimated that the rail customer normally spends about \$3 million prosecuting the case and the railroad spends about \$5 million defending, and the case can take 2 to 3 years. That just does not seem like a viable option in very many instances. Other than the coal industry, is there any other industry that really could pursue something that is that expensive and have any kind of a hope of a real determination in a timely fashion?

Mr. NOBER. Well, Senator, it certainly is a concern. It is one that we have taken many steps to address, I have taken many steps to address since I got to the board. We have already come up with one round of changes to our process for looking at large rate cases to try to take some of the time and expense and cost out of it. We have looked at the process as a whole and looked at each individual piece of it to see, what can we do at every step of the way to try to make it cheaper and faster, all while preserving the rights, the important rights, of the parties.

These large rate cases can be fights over hundreds of millions of dollars, sometimes as much as \$300 to \$500 million. So on the one hand 3 or \$5 million in legal fees to debate a case like that is a relatively small amount. On the other hand, 3 to \$5 million and 2 to 3 years of time, not to mention we have records that can generate as many as 700,000 pages of material, is entirely too much.

We have tried to interject alternative dispute resolution into this, and we have our first mediation going on right now. It involves the Burlington Northern and it ends on Sunday. It has not been settled yet, but I am still hopeful that the parties will be able to.

We have tried to shorten the discovery timeframes and cut down on some of the discovery abuses that have gone on. In many ways it is a process that only a lawyer could love, where the parties cannot even talk to one another, and we have tried to put some order into that as well.

We have started having oral arguments in these cases because by and large we found that the paper records did not give us the best understanding of what the parties were putting forward. We recently discovered as a result of that oral argument that we had misinterpreted some of the evidence and had to go back and redo it, and we have had to toll the statutory deadline for a few weeks in order to fix those changes.

But making the large rate cases quicker and cheaper is certainly a priority and I think we have taken a lot of steps toward getting there. We have fights in these cases over the number of miles between the mine and the power plant. Now, the last I knew that is pretty much a fixed number, but the parties would debate it, and they would spend thousands of dollars fighting about things like that, or how much coal was in the car. Again, I do not know how much coal is in the car, but I know how much the shipper paid for. While there may be some variances, we have tried to standardize those kinds of measures and get the lawyers out of fighting about them and try to bring some order to the process, and I think we have been somewhat successful. There is more that we can do.

Senator HUTCHISON. Thank you, Mr. Nober.

Senator Burns.

Senator BURNS. While we have got you on the hot seat, we might as well leave you right there. Mr. Nober, there is a quote here that is sort of made by you that has some of us sort of—gave us some anxious moments. I quote from you: “Look, I am not going to insult your intelligence and tell you I could not change, that our board could not interpret some of the core rulings that you want us to make a change.” You were talking to some shippers. “We could, but we are not going to.”

Could that be the core of our problem here? Would you like to revise and extend?

Mr. NOBER. Certainly, Senator. In my testimony I did, I acknowledged that that is true, that the doctrines that many of the shippers would like to see changed, which are our bottleneck doctrine and our Midtek or terminal trackage rights doctrine, are administrative doctrines and as a matter of law an administrative agency can change administrative doctrines. Not everyone on our board has always acknowledged that but I as a student of Congress will tell you that we certainly can.

Now, whether or not we should and we would are different questions. I believe that under the law we are required to balance a whole list of factors when we make decisions and that those decisions represent the proper balance of factors. However, are there problems with them? Yes, and the main problem has to do with on the one hand our board is statutorily charged with ensuring that railroads are revenue adequate, and you have heard a great deal about that, and on the other hand ensuring that shippers' rates are reasonable.

A problem that I see is that, and we have talked about extensively, is the fact that only large coal shippers have a meaningful opportunity to bring a rate case to challenge whether their rate is reasonable. Any other shipper cannot do that.

So our doctrines have, and I acknowledge, put shippers in something of a heads I win, tails you lose situation, where on the one hand if you have a rate that you feel is too high there is no place to challenge it for being unreasonable, but on the other hand there is no other remedy available to you. You cannot order another railroad to come and compete with that, to have the trackage rights.

Now, I do not think the answer is to order access on carriers' lines or I do not think the answer is to order bottleneck rates, either. But I do think the answer is to provide a meaningful and quick and fair process for determining whether rates are reasonable, whether small cases are reasonable, and that is my top priority at the agency.

In fact, I have a fairly good idea of what that process ought to look like. We have had a hearing on the subject. Several of the folks here today or their organizations have testified before us and I think it is difficult, but it is not impossible to do.

Now, I have not done anything on this because I am a single board member and it is a significant policy initiative, and I have tried when I have been as a single board member not to take new major policy initiatives. I have decided cases that have deadlines because the agency has to function and the industry needs us to function, but I have not taken new steps. Now, we could do that, but I have not yet.

Senator BURNS. Mr. Nober, I have never seen you come out and say that, I would like to do this, or I think the board should do it. I have never seen a statement along that line until today. I guess that is what this is all about.

Mr. Linville, you ship grain. Do you pay the shipping cost?

Mr. LINVILLE. Yes, sometimes.

Senator BURNS. How much of the time do you?

Mr. LINVILLE. A large percent of the time. We are in the business of getting it to domestic consumers, delivered across the U.S.

Senator BURNS. If I sell my corn from Galatin, Missouri, into one of your elevators and you ship it to Portland, Oregon, do you pay the shipping on that grain?

Mr. LINVILLE. In that case—it would likely go to the poultry market in Arkansas—but yes.

Senator BURNS. I do not care where it goes. Say yes or no?

Mr. LINVILLE. Yes.

Senator BURNS. Is that deducted from my negotiated price on my grain, is that shipping cost?

Mr. LINVILLE. Certainly, the shipping and the handling.

Senator BURNS. Then you are not paying for that shipping. I am paying for it, am I not?

Mr. LINVILLE. We both are.

Senator BURNS. This ain't my first rodeo, you know.

[Laughter.]

Senator BURNS. But when I sell my grain into one of your elevators, and that is what you operate, you deduct transportation costs off of that grain?

Mr. LINVILLE. Certainly.

Senator BURNS. Thank you. In other words, I am paying the freight. And that is another misnomer that we should bring to light here, that I as a producer pay for the grain.

Now, there was a statement being made by Mr. Hamberger—I would just like to say, I do not have anything against the railroads, but we have got to find—would anybody at this table agree that we do not have a problem?

Mr. HAMBERGER. Define “a problem”?

Senator BURNS. Do you think—

Senator HUTCHISON. What is the meaning of “is”?

[Laughter.]

Senator BURNS. I will tell you—would you agree that we have got a problem?

Mr. HAMBERGER. I do not agree that captive shippers do not have competitive options in many cases. I do not believe that the STB is not an adequate place for them to take their case, no.

Senator BURNS. Anybody else want to comment on that?

Mr. PLATZ. We have got a problem.

Mr. WHITESIDE. We have got a problem.

Mr. NOBER. We are going to fix the problem.

Mr. HAMBERGER. When rates have gone down 60 percent since 1980, I am not quite sure what the problem is.

Senator BURNS. How about you, Mr. Linville?

Mr. LINVILLE. I think we have a challenge. I think the market-place can fix the challenge and I think business to business can fix the challenge.

Senator BURNS. Well, I will just make the case. There will be another round and I know my time is up, and I will allow—we have Mr. Rockefeller here, and I am going to stay for another round.

The point I am trying to make, we have got a problem. It is pretty evident at this table. And we have kind of give everybody time to work it out, but nothing is happening, and that is what I want to pursue in my next round of questioning.

Thank you very much.

Senator HUTCHISON. Thank you, Senator Burns.

Senator Dorgan.

Senator DORGAN. Madam Chairman, thank you very much.

Let me, Mr. Nober, ask you a few questions. First of all, let me compliment you for going out and riding on some trains and seeing the country. I understand you are a Surface Transportation Board of one, is that right?

Mr. NOBER. That is correct, sir.

Senator DORGAN. So it is you as the Chairman, Chairperson, and you have two vacancies?

Mr. NOBER. That is also correct.

Senator DORGAN. So we have a very important regulatory agency of three people and two of the seats are unfilled at this point. We are waiting for a Republican and a Democrat nominee to be approved by the Senate, I understand; is that correct?

Mr. NOBER. I do not believe anyone has been nominated yet.

Senator DORGAN. To come to the Senate from the White House. How long have these seats been vacant?

Mr. NOBER. The Republican seat since March, the Democratic seat since May.

Senator DORGAN. Does that concern you?

Mr. NOBER. Well, yes. But I think that our Board, I on behalf of the Board, have the power to act alone. As I said, I—

Senator DORGAN. But you are not acting alone in most cases, correct? You are waiting—in fact, I can cite you. You are waiting until you have a Board.

Mr. NOBER. It depends on the matter, Senator Dorgan.

Senator DORGAN. You are certainly not taking big, bold policy actions, I think?

Mr. NOBER. No, Senator, I am not. Unless if you all think that I should, that is a different question. But I understand that we are a multi-member bipartisan board.

Senator DORGAN. As long as you would make the right decisions, we would encourage you to do that.

[Laughter.]

Senator DORGAN. Mr. Nober, let me—you talked a moment ago about revenue adequacy. In your statement you said that, you know, there is not revenue adequacy, not a single one of our major railroads is revenue adequate. I had to step out for a moment, so I did not hear all of Mr. Hamberger's presentation.

I said at the start I like railroads. I had some model trains when I was a kid. I have ridden on the Galloping Goose, which is a little train that came through my home town. I love railroads. But I also like fair prices and I like competition, I like the market system.

You talk about revenue adequacy. Let me just run through some headlines: "Burlington Northern's Profits Rise," "Record Revenue for Union Pacific," "CSX Rallies As Core Revenue Gains, Tops Street's EPS Consensus." I can read more if you would like to hear more. I am sure you have read the same thing.

Tell me how you decide that the railroads somehow are operating on a short string, do not meet the revenue adequacy test?

Mr. NOBER. Well, our revenue adequacy test is not—earnings is just one part of it. What we do is we look at how much—basically,

what is their return on investment and compare that to the cost of capital. So we look at all the investment base, their entire investment base, look at that over a 20-year, depreciated over a 20-year period, and then compare that to what is the actual opportunity cost of that money, which is either going to the private capital markets or issuing stock or preferred stock.

So revenue adequacy is not simply looking at what are the third quarter revenues and saying, well, their third quarter revenues are up, therefore the railroads are doing better. That is one measure. It is certainly what some on Wall Street may look to. I take it from context you are reading from analysts' reports.

But on the other hand, revenue adequacy is a different kind of measure. It looks at whether or not the investments the railroad is making in itself are higher than they could get if they made those, if they made investments elsewhere. When we say they are not—

But you are—I am sorry, Senator.

Senator DORGAN. Go ahead.

Mr. NOBER. When we say they are not revenue adequate, we may railroads could essentially earn more on their capital by investing in something other than a railroad and it is hard for them to justify improving their infrastructure when they are in that circumstance.

Senator DORGAN. Yes, well, that is a wonderful test that is set up, it seems to me, to victimize consumers. If one thinks that the railroads are sort of moving along, just barely making ends meet, go listen to the presentations they make to Wall Street and then disabuse yourself of that.

You indicate, Mr. Nober—and I am going to ask you the questions exclusively if I might. I appreciate very much the testimony, I have read all the testimony by the other witnesses. I think it is a good cross-section of this debate, so I appreciate your being here.

But Mr. Nober, you are opposed to S. 919 and you indicate that you want to take some action somehow to streamline the complaint process. Apparently you seem to think everything is pretty good out there, let us not worry too much about it, let us just allow people to complain more easily than they are now allowed to complain.

But the small shippers, as you know, you have really no complaints that have been filed. Do you know why? Because they do not think the system is honest, they do not think it is up and up, and they do not think they have got a ghost of a chance at dealing with you or anybody else in the Federal Government, and they do not think a regulatory agency is interested in regulating fairly. So they do not even bother. And if they bothered, my colleague from Montana can tell you how long it used to take. It can take 10, 15, 20 years, and then they would not get a satisfactory result.

So the whole system is broken and you are saying S. 919 is not an approach that you like. So what do you like? What do you think, other than just saying, I want to try to fix the complaint process? I just gave you when I started my presentation the rates from Bismarck to Minneapolis, Minneapolis to Chicago. If you want to start, let me just complain this morning to you, or this afternoon rather: That is unfair. More than two and a half times, that is unfair; so fix that. And how would you fix that?

Mr. NOBER. Well, Senator, the first question is whether or not it is unfair and whether or not it is unreasonable. Under the statute we are required—every shipper who does not have a competitive option has a right to a reasonable rate. That is what the statute provides. That is what we are here to do.

Now, I accept that right now only large coal shippers have the opportunity to say, my rate is unreasonable, and prove it. And what you have said about the administrative process is correct. I have heard many of the same things, many of the same folks that you have heard from, and I agree with that.

So we are trying to come up with, I am trying to come up with, a process where the vast majority of shippers who are in situations where the railroad has market dominance over them—we have to look at that—have an opportunity to come in and say: my rate was unreasonable.

Now, I will also say, Senator, that just because a rate is high does not mean that it is unreasonable. There is a lot of factors that we have to look at, that we should look at, when we do that, and that we will do when we have a test.

But the arbitration provision in S. 919 is intended to get quick results, where folks can come in, you can limit—I know the case you are referring to, 20 years of discovery and decisions and court decisions in McCarty Farms. It was not the finest hour for our agency, and in fact the agency that oversaw that is not even around any more. So I certainly understand the kinds of concerns. I would not even think of defending that.

But the kind of process that you have in place where, in your bill, where you have an arbitrator who quickly and surely can hear the evidence, limit discovery, and give you a quick decision, I think we can mimic administratively. I think if we hired an administrative law judge he could hear cases in the first instance, limit discovery, try to rein in the abuses of the lawyers on both sides on this, and try to get a decision out in the first instance.

However, the arbitration provision in your bill does not require that the arbitrator look at anything, any factors. It looks at what—it looks at 180 percent of variable cost and whatever else then the arbitrator would like to look at. The statute requires us to balance things. It balances the needs of shippers, which are significant, with the fact that railroads do need to earn adequate revenues. How that will come out I do not know.

Senator DORGAN. Mr. Nober, we have been over that, for God's sake. You think the railroads are not earning adequate revenues? I mean, what on earth is going on? All you have to do is look at their reports. Of course they are earning adequate revenues.

The question is are the shippers one day, after 20 or 30 years, going to get somebody to pay attention to them. With all due respect—I think you are a good person—what you just told me would persuade me as a small shipper to never file a complaint with you, because you say, you know, the test is not the question whether it is fair, the question is whether it is reasonable, and you parse words.

The fact is, it is true the ICC is gone because it was dead from the neck up, but it has a perfect clone.

Mr. NOBER. I hope not.

Senator DORGAN. Well, the fact is the reason that you see some passion up here is we would like to see some action. And this has gone on year after year after year. And if you are the one that is making the money, you think it is just fine. If you are the one that is shelling out the money, it is not fine.

And I am just telling you, if you are shipping a carload of wheat from Bismarck, North Dakota, and you are paying two and a half times the price, that by God is unfair, and you cannot resolve it because nobody out there is willing to resolve it. There is no regulatory agency willing to embrace it and resolve it for you. I think there is anger out there among shippers and the anger is properly directed at a whole series of enterprises and institutions in the Federal Government that seem only here to protect the big economic interests.

Now, let me say again, I like railroads. God bless you. I want you to exist, I want you to be a part of our future. But I want you to understand that fair pricing is essential for people all across this country.

Where there is no competition, you must as a regulator step in and provide some basic protection for small shippers.

Senator HUTCHISON. Senator Rockefeller.

**STATEMENT OF HON. JOHN D. ROCKEFELLER IV,
U.S. SENATOR FROM WEST VIRGINIA**

Senator ROCKEFELLER. Thank you, Madam Chairman. Well said, Senator.

Mr. Hamberger, have you read Senate bill 919?

Mr. HAMBERGER. Yes, sir.

Senator ROCKEFELLER. Good. I would like to have John Roberts, who works on this for me, to bring the bill to you.

[Pause.]

Senator ROCKEFELLER. John, you stay there.

Now, I want you to show John the provisions in S. 919 that cap rates. I want you to, if you have a ballpoint pencil, just to put them, just to mark a little thing beside it. Or provide trackage rights, that is allowing one railroad operating over another's tracks.

[Pause.]

Mr. HAMBERGER. It is the area where the arbitrator—

Senator ROCKEFELLER. Arbitrating is not what we are talking about. Just please do what I asked. Caps rates or provides trackage rights, just mark it where it is. Then when you have marked it I want you to read it out to me.

Mr. HAMBERGER. The way that I interpret—

Senator ROCKEFELLER. No. I am saying I want you to mark those places where—you can say interpret, but where it says cap rates or—

Mr. HAMBERGER. The words "cap rates" are not used. It is my belief on pages 18 and 19 where the designation of an area of inadequate rail competition, which is anybody who pays more than 180 percent, would have the practical effect of driving those rates down to 180 percent.

Senator ROCKEFELLER. So it is not mentioned?

Mr. HAMBERGER. The words "cap rates" are not, the two words are not in there.

Senator ROCKEFELLER. That is correct.

Mr. HAMBERGER. That is my interpretation of the impact of this bill.

Senator ROCKEFELLER. Now, providing trackage rights, have you found that in the bill?

Mr. HAMBERGER. The trackage rights would be the overturning of the Midteck, where you then have to allow another carrier into your terminal.

Senator ROCKEFELLER. That is correct, operating over another's track rights. Can you find that in the bill?

Mr. HAMBERGER. The bill talks about ordering access to terminals without regard to a Midteck kind of finding, and that again is the practical effect of that provision.

Senator ROCKEFELLER. Practical effect. So there is speculation.

Mr. HAMBERGER. There is a lot of speculation in any piece of legislation, I suspect.

Senator ROCKEFELLER. No, there is not. I do not think there is—

Mr. HAMBERGER. People who draft it expect a certain outcome—

Senator ROCKEFELLER. I do not think there is in this.

Mr. HAMBERGER.—and I disagree with that expectation of that outcome.

Senator ROCKEFELLER. And I would remind you that when I ask you these questions, you made this presentation of all these petitions and letters that you got, that we know from various groups that they were caused to have to write those letters if they wanted to keep their prices from you. That is pretty disgusting from my point of view. You will deny it, of course.

Mr. HAMBERGER. Of course.

Senator ROCKEFELLER. And you have not pointed out either trackage rights or you have not pointed out cap rates. You have speculated. So that there is nothing about that and the reregulation that you constantly hammer on in our bill.

So what is the AAR's new definition of "reregulatory"?

Mr. HAMBERGER. It is the same definition. I disagree with your interpretation of what your bill would do. That is what this is all about.

Senator ROCKEFELLER. But you have not pointed anything out in the bill.

Mr. HAMBERGER. My interpretation of your bill is that it would drive rates down to 180 percent and give trackage rights.

Senator ROCKEFELLER. Of course it would. For 20 years that has been your interpretation of anything that has been sent up. I am asking you to point out and you cannot do it.

Mr. HAMBERGER. Well, I am pointing out, I am, by saying that anybody who pays rates over 180 percent can have it declared an area of inadequate rail competition and get those rates driven to 180 percent. That is the way it is going to work out.

Senator ROCKEFELLER. That is the way it is going to work out.

Madam Chairman, I stipulate that the well-paid, "Inside-the-Beltway" Washington lobbyist for the railroad association was not

able to point out either "cap rates" or providing trackage rights and is not able to therefore give any understanding of the word "reregulatory," how this would be reregulatory.

You know perfectly well, Mr. Hamberger—we had a pleasant meeting in my office. You seem to have changed somewhat since that time. But you all have been playing a vicious game by operating underneath the radar. When I came to this place there were 50 class 1 railroads. There are now four, four-and-a-half, something of that sort, probably to be fewer.

You play a very successful, very tough game. You negotiate—I voted for John Snow for Secretary of the Treasury because it was very important to me that he no longer be associated with the CSX system, because he and others would cut deals. They would threaten. I had people come to me from the coal industry, from the steel industry, from the chemical industry, and talk about the kinds of—and some of the names are very, very, very large—that they were working under threats and that sometimes CSX or others would come in and they would cut a deal. And I can name you some of those companies. They would cut a deal so they would just keep the pressure down just enough so that you could continue to operate under the radar.

You are extraordinarily successful at that. But when you go to bed every night you need to understand that you are causing great harm, great peril and economic disadvantage to all kinds of people all over this country who, for reasons which are not entirely clear to me, have not been able to galvanize successfully enough to defeat you.

The STB, I am not going to say anything about the present, but it has been pretty much the property of the AAR, owned and operated by the AAR. It may be different now. We will see about that.

You are a very powerful person. You do a great deal of damage to this country. You cannot point out in S. 919 and there is a very good reason for that, is your argument is fallacious all the way down the line. You do not want any competition. You do not understand or you choose not to understand the Staggers Act, the fact that when there is a single line that bears consequences and that that has to be done also with the STB.

You just plow ahead. You make lots of money. You have the evidence against you, as Senator Dorgan was pointing to. It makes no difference to you whatsoever because you have got a good thing going.

My great-grandfather would have really liked you and your people. He would have felt very comfortable, and he believed in rebates and I will bet if you could do rebates you would do them, too, or maybe you do. But he would have thought you were terrific. I will tell you, I am very grateful to him for what he did for me. I am not at all grateful to you for what you are doing to my State of West Virginia and shippers and chemical people and steel people and coal people and farmers all over this country.

Thank you.

Senator HUTCHISON. Mr. Smith—let me just ask, did you have any other comment?

Mr. HAMBERGER. I resent very much the remarks that the Senator has made.

Senator ROCKEFELLER. Good.

Mr. HAMBERGER. Because I do not in any way believe that this industry is causing the kind of pain and suffering that the Senator asserted. In fact, this industry is the backbone of the economy of this country. It moves 40 percent of America's freight, at a lower rate and safer than it ever has. So to assert, as the Senator has, that ruin and perdition is occurring because of this industry, I just totally disagree with. And I thank you for letting me put that on the record.

Senator HUTCHISON. Senator Smith.

**STATEMENT OF HON. GORDON H. SMITH,
U.S. SENATOR FROM OREGON**

Senator SMITH. For the record, I have just heard it asserted—I do not have the facts, but I understand the railroads are making money now; is that correct?

Mr. HAMBERGER. The third quarter of this year has apparently been a decent quarter. The first two quarters were not. Like every industry and every company, there are good quarters and bad quarters. The economy—as you know, Senator, we are a leading edge indicator and in the first 5 months of this year I am told by our western carriers that we were behind on projected revenues.

Beginning in July and August, as the bumper crop came in, as the drought that occurred in Europe impacted world markets, American farmers were able to sell into those world markets because they could get to those world markets on rail. We moved those grain shipments to the ports efficiently. There is some increase now also in intermodal imports. The Christmas rush usually peaks in September. It is actually occurring now. And finally, coal is beginning to rebound as well. Automobiles are up. So the economy does appear to be moving, based on our car loading data.

Senator SMITH. For the record, I hope the railroads are profitable. I think that is a good American concept, and so I hope you succeed. And I hope you are fair. I think some points that are being made here need to be made, but I also want to be on record as saying I hope the railroads made a lot of money, because there is a lot of investment that needs to take place in the rails of our country or else we are not going to keep up with 40 percent of the freight moving in this country. And then that is your responsibility, because that is your lifeblood to staying in business, and I think we are way behind on investment in our rails in this country.

So I am concerned about our shippers and I am concerned about our railroads. We need you both to succeed.

Mr. Nober, as you know, the Commerce Committee reported legislation to reauthorize STB with an amendment by Senators McCain and Hollings to address longstanding concerns about small rate cases. I apologize, I have been covering a research in the Finance Committee as well, so you may have addressed this. But I just need to ask the question if you are going to issue these new rules for small rate challenges to be done within 180 days following its enactment? The rules would establish standards for determining what rate cases will be eligible for the expedited procedures and, equally important, establish the specific test or tests that will be used in determining whether the rate is reasonable.

Do you have a comment about the McCain-Hollings amendment in the reauthorization of STB?

Mr. NOBER. Yes, Senator. I certainly support the kinds of initiatives that were in that amendment. We worked with the Committee some and commented on it. I certainly believe that our agency should move as expeditiously as possible on that subject.

I had hoped to already have those kinds of rules in place by now. But, as I told the Senators earlier, I have been reluctant to initiate, take on new policy initiatives, while I am serving as a single board member. It is my view that our agency was set up as a multi-member, bipartisan board and that is a significant step and I think that that should only be done when we have a fully constituted board or at least more than one member, rather than just myself.

Now, as I said, if the Senators feel differently then I certainly would have the board act on that to try to implement that provision as quickly as possible. But I think it is very important and, candidly, I think having a swift and meaningful procedure for shippers to be able to challenge their rates that apply to all the various levels of shippers and not just large coal shippers would go a long way toward addressing many of the core concerns that have been raised today. So I think it is a critical thing, a critical element for us to do. It is my top priority, and that is why it has not been done yet.

Senator SMITH. Do you have any other recommendations for us, anything else that you think should be changed in the Staggers Act that we have not addressed?

Mr. NOBER. Senator, I think the Staggers Act really provides our agency with the ability to balance the kinds of factors that have been raised today. I do think, as I said earlier, that without the ability to bring smaller rate cases, shippers really are in a heads I win, tails you lose situation with the railroads, where on the one hand if they have a rate that they think is too high they have no place to challenge it, but on the other hand they cannot petition to have a different railroad come in and serve them. That is an unfair situation to be in, I agree with that.

Would I go as far as some of the proposals here today? No, I do not think they are necessary. I think that would fundamentally restructure the economics of the railroad industry and those are not necessary. The law now provides that shippers can have a rate that is reasonable and right now many of them cannot, and we need to fix that.

Senator SMITH. Mr. Whiteside, do you have a comment about this as a provision? Does this help you? It does not go as far as some on the Commerce Committee I understand are advocating, but does this help?

Mr. WHITESIDE. Well, I think—

Senator BURNS [presiding]. Pull the microphone over.

Senator SMITH. I apologize if I missed your testimony earlier, but I just want to know if what is being proposed by Senators McCain and Hollings can help address some of these problems.

Mr. WHITESIDE. I think it is a start. I guess the thought I would have is that we do agree, Chairman Nober and I, on one thing—that S. 919 would fundamentally change the railroads. But that is what we think is needed.

Let me just—I have got a note here that I am hunting for, and I apologize for it. I just want to get it in front of me so that we can talk a little bit about that.

That is why we are here. The current economic model does not work. It does not work for the railroads and it does not work for the shippers. From a wisdom standpoint, it is best I think for us to leave the decision on this to elected officials and Members of this Committee. Shippers have repeatedly expressed the desire to sit down and work out their problems with the railroads. But the railroads have not been forthcoming.

The lack of rail competition and its effects are severe in the areas where we have no competition. I think what we have to do is recognize that a start with just the fundamentals of the regulatory process that does not work is not going to be helpful enough. When Senators Burns and Dorgan and Rockefeller brought this bill, there is a coalition of 14 groups together now that support this bill, that comprise 55 percent of all of the revenues of the railroads.

The problems that surfaced in last year's bill proved to be distracting, so what they did was that we modified the bill. Senator Burns came up with a bill that was very focused on what we were trying to do and it represents the best efforts of the possible solutions. That is where we think we have to go.

What we are here to do is open the dialogue.

Senator SMITH. I appreciate that.

Mr. WHITESIDE. Thank you.

Senator SMITH. Ed Hamberger, I wonder if the association has taken a position on this amendment?

Mr. HAMBERGER. Yes, we strongly supported it during the markup in July.

I would just, if I might, echo Mr. Nober: Heads you win, tails I lose. Gee, we got some good news third quarter and now we are being told that we are earning monopoly profits, and sitting next to me here is someone who says that the economic model does not work. I do not know. It is one or the other.

I happen to think that the balance is proper, that the STB is there to provide that balance. And I am pleased, as you have indicated as well, that finally in this third quarter this year there has been a little bit of a rebound in the economy in which our companies have been able to participate.

But as far as the STB amendment that was adopted by this Committee, we strongly supported it.

Senator SMITH. Ed, can you give the Committee any assurance that—I am sorry if my time is up.

Senator BURNS. Go ahead.

Senator SMITH. I just have one question to follow up on this. If the association is supporting of the McCain-Hollings amendment in the STB reauthorization, is there any assurance the railroads want to give to us that you will not simply challenge in court all of the rules and frustrate the situation?

Mr. HAMBERGER. One never gives away one's rights. But what I said in my opening statement was that we want to work with the STB and come up with an approach. In fact, the chairman has asked for suggestions from all parties. We have made some. Others

at this table have made some. I am hopeful that we can begin a formal process.

It is not our intent—I give you that commitment—it is not our intent to frustrate this process. It is not our intent to go to court. It is our intent to come up with workable, affordable procedures at the STB to benefit small shippers.

Senator SMITH. I think that is critical, I think for a lot of reasons that ought to be evident to anybody attending this hearing today. We have got to get beyond just the parties coming to Congress to settle these small shipper claims. We have got to get to a system that is fair and is rational and that leaves the railroads profitable and shippers with the chance to be profitable as well. You have got a community of interests between you. You need each other.

Mr. HAMBERGER. That is correct, Senator. If our customers are not profitable, if our customers are not able to compete in world markets, then we do not get their business. That is the essence of the partnership that we have formed with many of our customers.

Senator SMITH. Thank you, Mr. Chairman.

Senator BURNS. Thank you, and that is a good line of questions.

While we are at that, if you were a wheat farmer in Montana or North Dakota you would probably have a different attitude. He is just a little guy sitting out there on the prairie and he falls victim to every kind of thing that can happen to him that Mother Nature wants to throw to him. And then you go down there and then you sell your grain, and they will quote you a Portland price or a Minneapolis price and then take the freight off, and that is when he gets hammered.

And he has not made any money, Mr. Hamberger. I will tell you that right now, and that is what is causing this hearing today. That is exactly why we are here.

When looking at S. 919, the exchange you had with Senator Rockefeller is very interesting. Mr. Whiteside, do you think S. 919 has elements that is going to change—that goes beyond the extent of the Staggers Act of 1980?

Mr. WHITESIDE. S. 919 basically restores the provisions of Staggers in large part. What it starts to do is go back to what we were trying to accomplish in Staggers and what we talked about. It was a good bill that this Committee passed, and what it does is it simply says: Allow competition, but protect those who become captive in the process.

As we have concentrated and concentrated and concentrated the railroads, we have larger areas that have become more and more captive. Today whole states, whole regions, whole industries are captive. And that is what we have to get back to.

So what S. 919 does is it starts us down the path of simply starting to look at what is possible. It opens the dialogue.

Mr. HAMBERGER. I thought it is fundamentally changing the industry. That is what you said 5 minutes ago.

Senator BURNS. Pardon?

Mr. HAMBERGER. The gentleman said it fundamentally changed the industry 5 minutes ago. It does not start a dialogue. It fundamentally changes the industry. That is what he just said.

Mr. WHITESIDE. What we are here to do today is to have a dialogue. What we are here to do is restructure, if you will, the proc-

ess that we have been under. It is interesting, when Senator Dorgan was talking about revenue adequacy and how that term just gets flipped around and it means different things. There was a study, and I will give a copy to the Committee of this study. This was a study by Alfred Kahn, who is known as the father of deregulation. One of the things he said—this was given to the STB—the meaningful relationship between STB’s measure of revenue adequacy and the financial wellbeing of the railroads, there is no meaningful relationship. There is none.

What happens in all of these terms and terminologies is that when you start working with the real person working in the field, working in the world, they are having problems with dealing with a monopoly and they have no recourse. What S. 919 does is start to get that recourse back. It gives them avenues.

Senator BURNS. Mr. Hamberger, in your statement in regards to final offer arbitration you state that you “know of no other case in which the private sector suppliers of a good or service are forced by the Federal Government to use binding arbitration to set a price because the purchaser desires a lower price. It is no more valid for the government to force binding arbitration on railroads than it is to force it on chemical companies, plumbers, supermarkets, or any other business.”

Basically, in essence are you saying, pointing out that it could give special treatment to shippers?

Mr. HAMBERGER. Final offer arbitration is, as you know, used in Canada. It is their way of providing some safety net for the shippers. Our way here is the STB.

Senator BURNS. Is it working?

Mr. HAMBERGER. I think the STB is working. I do not know what is going on in Canada. But to overlay the STB with a final offer arbitration plan would be doubly mixing apples and oranges there. The short answer to your question is yes.

Senator BURNS. Do you know of any other—do you know of any other private entity other than baseball that has antitrust protections like railroads?

Mr. HAMBERGER. I have not done a study on that.

Senator BURNS. Would you consider that a special treatment?

Mr. HAMBERGER. The statutory antitrust exemption that the rail industry has, does not exempt railroads from prohibitions against collectively fixing rates for the transport of goods. So I am not quite sure that the issue really is germane.

Senator BURNS. Well, I think it is germane. In other words, you are saying that nobody else has the right to look into the protection of small shippers, and these corporations and companies right here that you haul 50 percent of—that are 50 percent of your revenue, that they do not have a right of recourse to come in and negotiate.

And sometimes theirs is done in good faith and yours is not. That is the stories we are hearing, Mr. Hamberger, and I do not drum this up. It comes from a lot of different sources, other than the folks, other than the folks that grow crops in my state.

I mean, I know, Mr. Scouler over there, we have got to have elevators. You have got to have an elevator to have a town, plus a school and a saloon, or you do not have a town. But nonetheless, we are getting hammered. Nobody is listening to us. So as a result

of that, thus comes legislation that will at least bring people to the table in good faith. And if bad faith is exemplified, then Congress is going to do something to protect the small shipper, because I do not care how much of a Republican you are or how much of a Democrat you are; if you have got a monopoly, we have to deal with it.

Mr. HAMBERGER. Senator, I—

Senator BURNS. Do you agree with that?

Mr. HAMBERGER.—I would reject out of hand that there is bad faith in the negotiations between the railroads and our shippers, and our customers. I believe the small shipper that you are talking about is exactly what Chairman Nober referenced and exactly what this Committee passed an amendment on to address those issues at the STB, to afford an opportunity for the small shipper's case to be heard in an affordable and expeditious way, and that is what we support.

Senator BURNS. Mr. Dorgan.

Senator DORGAN. Mr. Chairman, thank you.

Mr. Nober, do you agree with Alfred Kahn's assessment that revenue adequacy has nothing to do with financial well-being of the railroads?

Mr. NOBER. I have seen the study. That is his opinion. Our statute requires us to measure revenue adequacy and therefore we do.

Senator DORGAN. But I am asking your opinion, not the statute.

Mr. NOBER. I would be reluctant to disagree with an economist as eminent as Alfred Kahn. However, my own instincts tell me that any relationship between the return on capital that you can get versus the return on capital that a company can produce is a meaningful measure. Whether or not there are better ones, I do not know. But whether or not that—if you look at could a company get more money by investing it in an entity other than itself, is that a meaningful measure of its health, I think it is. It is a measure. I am not sure it is—what it shows in this case, Senator, is that railroads require a lot of capital, and that is why they show up to not be revenue adequate. The fact of the matter is it is expensive to run a railroad.

Senator DORGAN. I have known Alfred Kahn for many years. I taught economics very briefly and I was able to overcome that myself. But the statement by Mr. Kahn seems to me to be perfectly plausible, that the revenue adequacy test that is a test at the Federal level that we use has nothing to do with the financial condition of the industry. That is what Mr. Kahn says.

I was simply asking, what is your opinion of that? Do you generally agree with that?

Mr. NOBER. As I said, my opinion is that a measure that looks at whether or not a company would make more by investing in something other than itself is a measure of the financial—of the long-term health of the industry. Whether or not it is meaningful in an individual quarter, I do not know, I confess.

Senator DORGAN. From the standpoint of the shipper, it seems to me they look at this and they think that it is a rigged game. The railroads can make a substantial amount of money and you as a regulator will say that they are not revenue adequate, and that is why you get people looking at this and saying, "This is not on the level. Are you kidding me?"

Mr. Hamberger, are you annoyed at being here? I mean, you seem annoyed.

Mr. HAMBERGER. No, sir.

Senator DORGAN. OK. I mean, we do not want to annoy you. I like railroads, as I indicated.

But you obviously have the ability to fix rates. You used the term "fix rates" a while ago. I mentioned the example of Bismarck to Minneapolis, 400 miles, they charge \$2,600 to move a carload of wheat 400 miles. The same 400 miles, Minneapolis-Chicago, they charge \$900. Now, those who charge the \$2,600 fix the rate, correct? I mean, they are fixing the rate?

Mr. HAMBERGER. I was using that as a term of art, Senator, in that I was asserting that there is no antitrust immunity for railroads to get together to, quote, "fix rates." If you are asking the question, obviously the railroad has a tariff that it charges, yes.

Senator DORGAN. That railroad fixes the rate. I am not using it as a term of art in terms of antitrust. They fix a rate of \$2,600, saying, your carload of wheat, that is what we are going to charge you from Bismarck to Minneapolis. Now, people tell me and economists tell me and the Public Service Commission of North Dakota tells me the only reason that rate is fixed at that level is because there is no competition. And the reason it is about one-third of that level from Minneapolis to Chicago is because there is competition on that line.

Do you understand the angst, then, of a shipper who is putting a carload of wheat on the rails at Bismarck who says, why am I more than double-charged the same price? Do you understand? I am just asking you now as a policymaker and as an executive with the railroad industry, do you understand the angst and where it comes from, the origin of it?

Mr. HAMBERGER. I understand the political pressure that that exerts on you and Senator Burns, yes.

Senator DORGAN. I am not talking about our political pressure. I am talking about the angst that comes from shippers.

Mr. HAMBERGER. The political pressure would come from the angst, yes.

Senator DORGAN. And their basic feeling that that is unfair. Senator Burns just asked the question, if you had some wheat that you were shipping on that line would you think it unfair?

Mr. HAMBERGER. I do not know how I would feel if I was the shipper. But I do know from where I sit and from where the railroads sit that it is fair, because economically the allocation of resources is best done by the supply and demand model, and if we did not get the return to the railroads such that they could invest and provide that shipment, provide that capacity to Bismarck, North Dakota, then it would be even more unfair because there would be no options for shipment.

Senator DORGAN. You are absolutely correct, I think, that the marketplace as a allocator of goods and services and a regulator—not a regulator—a balancing of supply and demand is an extraordinarily effective mechanism. I do not know of any that is nearly as effective as the marketplace itself.

But would you not agree, then, that the marketplace with respect to rail service between Bismarck and Minneapolis is not a marketplace at all?

Mr. HAMBERGER. I would not agree to that, of course not. But I would agree that, if that is an unreasonable rate, that there should be a process at the STB to determine that. I would point out, as we were talking about Alfred Kahn, there is another quote that I will supply for the record. I believe he said: You cannot expect there to be two airlines to serve Schenectady, New York. It is an economic supply and demand. Either there will be enough demand to warrant another airline or another railroad or there will not. So that is the economics of the marketplace.

Senator DORGAN. Yes, but the marketplace itself is a marketplace that works if you have price as a regulating mechanism and price as a function of competition between more than one entity will determine the allocation of goods and services. It is true that you cannot have perhaps two carriers serving the same route going to Schenectady, New York, but if you have a monopoly, therefore one carrier, you have to have some basic price regulation in order to protect against monopoly abuse or, if not price regulation, then you have to have a regulatory body that oversees it.

My contention is this: We have a regulatory body that does not regulate, does not oversee it, because it essentially is frozen in time.

Mr. Nober, I did not mean to browbeat you. I was not trying to browbeat you at all. But I have been in Congress I guess about the same length of time, perhaps just a bit longer than, Senator Burns and we have been going over and over and over this issue and nothing ever changes. It does not matter whether they call the agency the ICC or the STB. It still acts like a glacier, except a glacier you can actually see move from time to time.

That is why consumers are so angry and so upset, because they believe they are being treated unfairly. They do not dislike the railroad. They very much value the service. But they do not value the service more than double the cost out of Bismarck and Minneapolis than a shipper from Minneapolis to Chicago. They do not value it that much, because they feel that is an unfair price.

Mr. Whiteside, when you started your testimony I was not sure which side you were on. Then you very quickly moved to the right side, I felt, at least from my perspective.

[Laughter.]

Mr. WHITESIDE. That is good to know, Senator.

Senator DORGAN. But tell me, if you would, your sense of the answer today by the STB that: Do not pass legislation, Congress; the STB is available to make changes in the review process and the complaint process that will be effective and that will solve your problems. Your response, please?

Mr. WHITESIDE. We do not feel that the answers are at the STB. If S. 919 were passed, it would start to make changes in the marketplace. Introducing S. 919 should start the dialogue, and that is what is needed here. What is needed here are fundamental changes.

Senator DORGAN. Yes, well, we have been dialoguing for 20 years.

Mr. WHITESIDE. Yes, sir.

Senator DORGAN. I submit we need some changes. I am a little tired of the dialogue.

I just was passed a note. As is always the case, there are these pettifoggers around here who say that there is no airport in Schenectady.

[Laughter.]

Mr. WHITESIDE. Even worse. There is not even one. You were right all along.

Senator DORGAN. God bless the details.

Mr. NOBER. Can I disagree with Alfred Kahn now?

Senator DORGAN. Is there an airport?

Mr. NOBER. No. But can I disagree with him if he got it wrong on Schenectady?

Senator DORGAN. Disagree with whom?

Mr. NOBER. Mr. Kahn. No, no; I was making a joke, Senator. I am sorry.

[Laughter.]

Senator BURNS. We are going to have a vote here in about 5 minutes and I want to kind of round this up, because there are going to be some more questions from other Senators and there are going to be some more from me.

Senator DORGAN. Let me thank them. I have to leave, but let me thank you for presiding in the absence of the Chair, and let me thank the witnesses for being here. We need dialogue, but we also want some action.

Mr. WHITESIDE. Yes, sir.

Senator DORGAN. Senator Burns, thank you.

Senator BURNS. Well, and I thank my good friend from North Dakota. We do not vote together on a lot of things, but on some of these things we get very close to. That is the beast of politics and the body politic.

On this demand and that line of thinking, Mr. Nober—and I want to ask all of you—what is your knowledge and experience or thoughts on the Canadian arbitration of last choice?

Mr. NOBER. Well, my understanding is that the Canadian arbitration system is not frequently used. But the Canadian rail system is different than ours. It does provide for access in a much broader way, very similar to what you have in S. 919. But Canada has many fewer terminal areas. I guess at some point I could tackle Senator Rockefeller's question about what the bill does, but this bill has—in our country we have a very broad definition or a very broad understanding of what terminal areas are and the areas where companies would be able to get—railroads would be able to achieve trackage rights. We also have many more—a much larger network here.

So I think that, while the arbitration provisions in Canada have not been extensively used, there are differences with how our networks work and there are some differences in the effect of other parts of the bill as well.

Senator BURNS. Mr. Platz.

Mr. PLATZ. Yes, Senator, if I can just make a comment about it. We have operations in Canada, so we have come up against this. Basically, there is three elements that go into this. It is the arbi-

tration side of it, the competitive line rates, and this inter-switching, terminal switching. It forms the basis in which negotiations can take place between the customer and the supplier, the railroads and the shipper.

It is really, if you look at any of the surveys, the literature, on this particular issue, they talk about the railroad and the customer would much prefer to negotiate one on one. They do not really want a third party in this. But you need a structure that allows that to take place.

So what has been created in Canada creates that background, because both parties know that if they cannot negotiate, they cannot come to the solution, there is a way to solve it, and it is actually fairly rapid, the way that works.

Unfortunately, the work that we have going on right now, it is very, very long to get anything done down here, arduous and so forth. And on top of that, all of the burden rests with the shipper, with the customer. He has to prove everything. The railroads do not have to do anything. He has to prove everything.

So basically what we need to do is bring some structure to this. So that is why we are suggesting this arbitration side of it, as a way to create this environment where negotiation in fact takes place.

Senator BURNS. Do you agree with that, Mr. Hamberger?

Mr. HAMBERGER. What I wanted to say, I do not know—I do not have the experience on the Canadian Arbitration system to judge what Mr. Platz said. But the answer to your question is that we have some concerns, deep concerns, with the Canadian system. It does not have any standards as I understand it and the only party that can invoke final offer arbitration, invoke arbitration, is the customer. So it does not seem to be a level playing field certainly.

I would ask that if I could get together with our two class 1's, Canadian National and Canadian Pacific, and put together some comments for the record on that, if you would indulge us on that.

Senator BURNS. That would be acceptable.

Mr. Whiteside.

Mr. WHITESIDE. The Canadian system is an interesting system. It is a duopoly. It is very similar to what we have in the West in the United States. The Canadian final offer arbitration system is a system that was designed to level the playing field and facilitate negotiations between the carrier and the shipper.

In our experience with some of the companies that we have in our organizations that have operations on both sides of the border, they have found in fact that is what it does. The avenue, from a shipper's standpoint it has proven to be a proactive, noninvasive tool to facilitate rail-customer negotiations and it has in fact speeded up those negotiations.

So they like the system. It has not been invoked very often because the railroads are negotiating. That is where we are trying to get to.

Senator BURNS. Mr. Linville, do you have a thought on that?

Mr. LINVILLE. No, just to say that in the grain industry we have private arbitration in the National Grain and Feed that has added non-price issues, service issues, to our arbitration program and that has worked effectively.

Senator BURNS. Well, the economic scale, and this I guess is the point where I am going to close because we are going to do something here. I do not know what is going on down there, but I got my bill passed yesterday, so I feel the load is off.

My State nationally ranks, it is fourth in wheat production and ninth in winter wheat, second in spring wheat, third in barley, fourth in durum. They say there is all kinds of demand for those commodities. But yet we are setting up there at the end of the line.

My dad taught me a long time ago. He said always keep in mind and it will never change, and it has not in the last, the years since I been here, and I just did not exactly arrive on the last load of pumpkins. But my farmer—and you can say it in Kansas and you can say it in Missouri and you can say it in Nebraska, where my wife's folks, they ranch up there in North Platte, you see them old Scouler cars go scooting through there. You see them go through Laurel, Montana, knowing, knowing, that that grain is getting from Omaha or in Kansas to Portland cheaper than my grain is and it is setting right there, knowing that.

Agriculture, the producer has always sold wholesale, buys retail, and he pays the freight both ways. And the only system we have—and it may be here in S. 919, because we pretty much established that this is to restore what the Staggers Act meant and also a way to bring arbitration of the small shipper to the notice of the railroad or transportation that they have a monopoly.

I think that is fair. I think that is fair. And that is basically all S. 919 does. It does not set any rates. it does not empower anybody any more, other than the fact that it sets up that framework in order to get that done.

So we are going to push very hard on S. 919 because I really believe in it. We have got some little people out here that is being hurt and we just, we cannot talk any more. It is pretty easy to sit here in this 17 square miles of logic-free environment and justify why we are here. But when you are getting hammered it is pretty tough.

I want to thank—and I think a lot of the Burlington Northern up there. They do a lot of great things in the State of Montana. But there has to be a way that the small voice can be heard. And if there is not, then all the goodwill that we do and all the good things that we perform across the country and across the world goes for naught. And that is what this was all about.

I appreciate your testimony and I appreciate your participation in this dialogue. But if this cannot get it done, then tell us how. Do not go back to the office and say: We ain't talking no more; we are just going to use a lobbying effort to kill it. I will tell you, that may be pretty tough to do, because there are small shippers everywhere in this nation that I know of.

So thank you for coming today. Any closing thoughts? Any closing thoughts?

Mr. WHITESIDE. I have one thought. We can be pro-competitive and pro-railroad at the same time.

Senator BURNS. I think so.

Mr. NOBER. Senator Burns, I would just like to say that I do believe our agency can solve these problems administratively and, while I understand the pressures that have led, the reasons why

you want this bill to move forward, I think our agency can address many of those and I hope that you would give us a chance to do that.

Senator BURNS. My comment to that is: Cowboy up. Get after it.

Mr. NOBER. The team with that slogan lost.

Mr. PLATZ. Senator, I think time is running out here. I think jobs are at stake. We are competing in a global economy now. Every day it becomes more and more obvious how jobs are leaving the United States. I am not putting this on the back of rail at all, but rail is a part of making the United States economically viable in this global economy, and we need to do something about it.

The model the railroads are following is flawed. They are putting all of the burden on the customers that have no choice. That is not right, it is not fair, and in the end it will be their undoing. So we need to do something, and I think it is in the hands of the Congress to do it. We need to set policy and I think that is in your hands, not in the regulatory side.

Senator BURNS. Mr. Hamberger.

Mr. HAMBERGER. Senator, thank you so much for your attention and interest in our industry and in this hearing today.

I, to try and paraphrase Mr. Whiteside, say you can be pro-rail and pro-shipper, and that is exactly what we are. We want to work with our customers. We want to make them competitive in world markets. I noticed ACC's testimony. I still think of that as a basketball league myself, but the American Chemistry Council—

Senator BURNS. I have got to stand up. I did not get that either.

Mr. HAMBERGER.—testimony, indicating that of course it is the increase in natural gas prices, which this energy bill needs to address and do something about, but that is driving jobs offshore. We are concerned about those jobs leaving. Once they leave they will not come back, and our industry depends upon a strong manufacturing base in this country, and so we want to work with our customers to make sure that that base stays as strong as it possibly can.

Thank you.

Senator BURNS. Mr. Linville, thank you.

Mr. LINVILLE. Yes, one closing comment. I would say that I think the challenge that you describe is more acute in States that have sparse production or low density of production. I think as the density of production is greater the industrializing and obtaining efficiencies of the evolving transportation system is easier to gravitate to.

I have been to Montana many times, really enjoy the state, but I know it is challenged with production per acre and lack of production density. Capital will flow to where you have dense production, grain shipper capital, railway capital. There are some facts of life that we cannot get around.

So I would submit to you that this may not be at the doorstep of rail shippers and railways. It may be a rural development challenge.

Senator BURNS. Thank you very much. That is a good thought.

Thank you very much today and thank you for coming and offering your testimony. There will be some more questions coming to you in the mail. This hearing is over. Thank you.

[Whereupon, at 4:34 p.m., the hearing was adjourned.]

A P P E N D I X

RESPONSE TO WRITTEN QUESTIONS SUBMITTED BY HON. RON WYDEN TO HON. ROGER NOBER

Question 1. Small volume shippers consider the existing rate complaint process to be too complicated and uncertain to be of any value. In fact, no one has filed a case under the Surface Transportation Board's (STB's) small rate case guidelines. What actions can the STB take to alleviate the concerns of small shippers about resolving rate disputes?

Question 2. Is the Board's ability to take action to reform the rail shipper complaint process affected by the current vacancies?

Question 3. Quality of rail service is another significant source of concern for many of my rail using constituents. Car availability, fees, on-time arrival and departure are just some of the issues I've heard about in the past. What relationship do you see between these kinds of quality complaints and the availability of rail-to-rail competition?

Question 4. In an interview with *Rail Business*, you were asked about the Rail Competition Act, S. 919, and you said "If Congress wants to do that, they should have a full debate about it. They should understand what the ramifications are for the taxpayers and for the folks that rely on the system." Could you elaborate on your comment and explain what the ramifications are for taxpayers and rail users?

Question 5. I have been contacted by a constituent who operates an intermodal freight facility about a proposal to create a new classification of service providers. My questions are: does the STB currently have authority to create a new classification of service providers; should there be any new classifications of service providers, such as the proposal described below; and if not, why?

Answer. As you know, there is a revenue-based definition of categories of U.S. Railroads found in the regulations of the STB. Currently, there are three classifications:

Class 1: Carriers with annual carrier operating revenues of \$250 million or more

Class 2: Carriers with annual carrier operating revenues of less than \$250 million, but in excess of \$20 million

Class 3: Carriers with annual carrier operating revenues of \$20 million or less, and all switching and terminal companies regardless of operating revenues.

My constituent is proposing adding a fourth class for companies like his which specializes in moving cargo in shipping containers via rail. Generally speaking, class IV carriers would be short-haul intermodal service providers in regions located across two or three states with agreements with Class 1, 2 or 3 railroads for hook and haul services of less than 600 miles. Class IV intermodal service providers would be entities which own or lease railcars and terminals and would provide transportation on a single through bill between shipper and receiver docks, or between docks and piers. The proposed definition for the new Class 4 would be: *Class 4: Carriers with annual operating revenues of \$100 million or less for short-haul intermodal rail, and terminal operations, and other services.*

WRITTEN QUESTION SUBMITTED BY HON. FRANK R. LAUTENBERG TO EDWARD R. HAMBERGER

Question. In page one of your testimony, you state that "most importantly, it [S. 919] dooms freight railroads to a state of perpetual capital starvation." But according to the AASHTO Bottom Line report, the freight rail industry will fall \$53 billion short in capital investment over the next 20 years even in the absence of legislation such as S. 919, just to maintain its current market share. If the freight railroads don't get Federal assistance in maintaining their infrastructure over the next 20

years, what will be the effect on captive shipper pricing? Won't the lack of capital take "differential pricing" to an extreme?

When I asked you about the AASHTO Bottom Line report the last time you appeared before this Subcommittee, you replied that the freight railroads are looking forward to working with their public and private partners to ensure there is sufficient capital investment in our country's railroad infrastructure. Please provide more detail on the type of funding conditions/arrangements you look forward to that may involve public funding of U.S. railroad infrastructure.

WRITTEN QUESTION SUBMITTED BY HON. FRANK R. LAUTENBERG TO
HON. ROGER NOBER

Question. What has the STB done to aid municipal commuter rail operations in gaining access to railroad right-of-way? In general, do you feel commuter rail holds sufficient public benefits to warrant additional leverage in dealing with railroad right of way owners to obtain access?

