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Statement

of the

National Grain and Feed Association

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Good afternoon. My name is Dan Mack and I am Vice President for Transportation and Terminal Operations for CHS Inc., the nation's largest farmer-owned cooperative, headquartered in St. Paul, Minnesota. I appear today on behalf of the National Grain and Feed Association, where I serve as Chairman of its Rail Shipper/Receiver Committee. We appreciate the invitation and opportunity to present our organization's thoughts.

The NGFA consists of more than 1,000 grain, feed, processing and grain-related companies that operate approximately 7,000 facilities that handle about 70 percent of all U.S. grains and oilseeds. Its membership includes grain elevators; feed and feed ingredient manufacturers; biofuels companies; grain and oilseed processors and millers; exporters; livestock and poultry integrators; and associated firms that provide goods and services to the nation's grain, feed and processing industry. Also affiliated with the NGFA are 26 state and regional grain and feed associations. NGFA works to foster an efficient free-market environment that produces an abundant, safe and high-quality supply of grain, feed and feed ingredients for domestic and world consumers.

Characteristics of Agricultural Commodity Shipments: I would like to begin with some general comments regarding the characteristics of agricultural commodity shipments.

There are several reasons that the nature of rail shipments of agricultural commodities differ from non-agricultural products. First, grains, oilseeds, grain products and other agricultural commodities are produced in diverse geographic locations, rather than centralized production centers, and there typically is no direct rail service provided to the actual producer. Second, agricultural commodity shipments are influenced heavily by fluctuating domestic and export market demand, as well as seasonal and weather-related conditions. For these reasons, agricultural commodity shipments are characterized by multiple origin-and-destination pairs – which differ markedly from the comparatively static origin-destination pairs of non-agricultural products. Further, final delivery points to which agricultural commodities are shipped often have multiple sources of supply, which means the volumes of carloads ascribed to a particular movement rarely are constant and predictable on a year-to-year basis.

In other cases, regional and local market demand from the grain processing, biofuels and livestock/poultry sectors necessitate the movement of agricultural commodities across longer distances that often require interchanges with more than one Class I railroad.   Yet, agricultural producers and shippers now rely primarily upon four U.S. Class 1 carriers to haul the vast majority of grain and oilseeds shipped by rail; in 2007, those four carriers originated 84 percent of grain and oilseed rail traffic compared to only 53 percent in 1980.

Need for Competition: These inherent characteristics of today's rail industry and agricultural product shipments explain why the NGFA is so adamant about achieving a more competitive rail environment consistent with free enterprise principles. The rail industry has consolidated to such an extent that the Class I railroads enjoy regional duopolies in the Western and Eastern United States. The rail competition envisioned by Congress when it enacted the Staggers Rail Act of 1980 gradually has diminished. This seems to be a common theme today articulated by several speakers.

In that regard, NGFA has long called for a change to the National Transportation Policy found in the Staggers Act to better balance the need for rail carriers to achieve revenue adequacy with the need to create a more competitive rail environment.

In working to achieve that objective, NGFA looks to both government and private-sector approaches and solutions. Let me touch on several examples, starting with competitive switching.

<u>Competitive Switching</u>: NGFA believes strongly that improvements in current competitive rail switching rules instituted by the federal Surface Transportation Board (STB) are essential. NGFA, along with shipper organizations represented at this meeting, are active participants in agency's current proceeding (EP 711) initiated in response to the commendable petition filed by the National Industrial Transportation League urging that the agency replace its existing switching rules.

In statements submitted to the STB, the NGFA has urged the agency to consider establishing a revenue-to-variable-cost ("R/VC") threshold (such as 180%) for switch charges which, if exceeded, would shift the burden of proof to railroads to demonstrate that such charges were reasonable. In many cases, railroad-imposed switch charges can be as high as $500 to $700 per car, which equate to approximately five to seven times the variable cost for providing the switching service. We've also pointed out that uneconomically based switch charges can be used by carriers to de-market rail traffic, which we believe the STB should view as an unreasonable business practice.

NGFA and other agricultural groups also have urged the STB to use a more liberal, case-by-case determination to decide whether an agricultural shipper/receiver's facility would be presumed to be within a 'reasonable distance' of a working interchange – rather than a firm 30-mile distance factor as contained in the NIT-League proposal. Again, this reflects the geographic dispersion of agricultural production and the location of agricultural product shippers and receivers, and the longer distances that exist to an interchange point.

In this regard, NGFA's analysis of 2011 waybill data that found that more than 94 percent of agricultural product shipments would not meet the NIT-League proposal's conclusive presumptions to qualify for competitive switching. Our analysis involved more than 44,000 individual records comprising more than 3 million rail shipments of agricultural products totaling more than $9.2 billion in freight revenue.

Further, NGFA has urged the STB as part of this proceeding to establish an appropriate "access fee" – the amount to be charged for performing the switching service. Our concern is that without establishing a reasonable access fee that makes it economically feasible to use the alternative railroad, rules that create a right to competitive switching will have little practical use to rail shippers. Commercially, this gives shippers and receivers an economic decision point on which to base their business decisions.

Simply put, NGFA believes rail carriers should not have a free hand to cut off existing access to markets through absolute closures of intersection points or by pricing switch charges beyond any justifiably reasonable economic level. Because switching movements are integral to maintaining a national rail freight network, railroads should not have the same degree of pricing freedom on switch movements that they currently are given on long-haul rates. To allow such autonomy on switching has a negative impact on the competitive fabric of U.S. agriculture and the nation's economy.

Grain Rail Rates: I now would like to shift my focus to grain rail rates. As documented by the U.S. Department of Agriculture in its presentation to you previously, grain rail rates have escalated dramatically since 2003, and have continued to rise in 2013 and 2014

NGFA's major concern when it comes to rail rates is that there currently is not a workable mechanism within the STB or other venues for agricultural shippers to challenge rates they believe are unreasonable. Even with improvements made last year by the STB to its rate-challenge procedures, the risk-reward proposition – the cost of bringing a case versus the potential gains in rate relief that can be attained – makes the current system largely unworkable for grain shippers. In addition, the pricing behavior of Class I railroads has eliminated the STB's three-benchmark rules as an effective deterrent to unreasonable rail rates. In the grain marketplace, another deterrent is the multi-year process involved in adjudicating a rate case at the STB. Shipping patterns for various grains can change quickly, and frequently the buy-sell transactions – which include the cost of rail transportation – can change and be of short duration.

For these reasons, NGFA and the Alliance for Rail Competition each urged the STB to launch a new proceeding focused exclusively on grain rail rates. We're pleased that the agency saw the merit in doing so, and we're expending considerable resources to develop new concepts and methodologies that we believe will warrant consideration in providing a more workable approach for grain shippers to challenge rates they believe are unreasonable. Again, our goal is to enhance a competitive rail marketplace by providing at least some reasonable opportunity for recourse for shippers to challenge rates and charges they believe are unreasonable.

Rail Arbitration: Reflective of its belief in encouraging direct private-sector dialogue to resolve certain types of shipper-carrier disputes, the NGFA in 1998 launched a Rail Arbitration System with all major U.S. and Canadian rail carriers (Class 1), numerous shortline railroads and NGFA-member grain, feed and grain processing companies that utilize rail. These Rail Arbitration Rules were added within the rubric of NGFA's existing Arbitration System, which has existed since the late 1890s as a method for resolving commercial disputes involving grain, feed and feed ingredients, as well as barge transportation and barge freight.

These rail carriers and rail user companies are required to arbitrate certain types of disputes, including: application of demurrage rules or terms; disputes involving receipts and bills of lading, such as loss-and-damage claims; transportation contracts between rail carriers and users; mishandling of private cars or locomotives; most disputes involving the reasonableness of published service rules and practices, including demurrage; application of general car-distribution rules that govern so-called "regular tariff" service; application of special car or equipment program rules; leases of railroad-owned land by rail users; misrouting of loaded rail cars or locomotives; and property damage claims arising under or related to rail sidetrack agreements. In addition, rail carriers and users may have other types of rail-related disputes resolved through NGFA arbitration if mutually agreed.

Based upon our decade-and-a-half experience, the principal benefit of the NGFA Rail Arbitration System is that simply having access to it encourages direct business communication between shippers, receivers and their rail carriers to resolve disputes, often without the need to ever filing an actual arbitration case. It's a simple, balanced, timely, cost-effective and fair way to adjudicate certain types of disputes, and we're hopeful it can be expanded at some point in the future.

Rail Service Disruptions Confronting Agricultural Shippers: Finally, let me conclude by discussing the severe rail service disruptions involving several Class I railroads that are being experienced by the grain, feed, grain processing and export sectors, as well as by our farmer-customers.

These recent service disruptions have been widespread, involving Class I rail carriers operating in both the West and East, as well as in Canada. As a result, U.S. export elevators and grain processors generally are operating at far less than capacity – largely because they cannot predictably rely on sourcing sufficient quantities of commodities by rail. Millers throughout the country are facing facility shut-downs because they're running out of raw commodities. Other grain processing and animal feeding operations are shifting to trucks in an attempt to obtain sufficient grains and oilseeds. Still others are switching rail origination to other carriers in the limited instances where that is possible. In addition, country elevators and other originators of grain and grain products are extremely hesitant to book forward sales to customers because they cannot count on predictable rail service.

Another fallout are the values paid in the secondary rail car freight market, which has traded at levels of up to $4,000 per car on one carrier – translating into a $1-per-bushel additional cost. That's a stark reflection in monetary terms of the extent to which service disruptions have affected agricultural shippers. These impacts ultimately are felt directly by our farmer-customers – reflected in lower price bids for grains and oilseeds. These service disruptions have had ripple effects throughout the grain-based value chain, increasing transportation costs dramatically and hindering our industry's ability to meet commitments to customers.

NGFA and its members have been in active discussions with affected rail carriers on the root causes of these service disruptions, as well as each carrier's recovery plans for restoring service. But it is clear that while the harsh winter weather has been an exacerbating factor, these service disruptions began occurring last fall well before the onset of winter.

NGFA is encouraging each affected carrier to provide more information on when measurable improvements in rail service realistically can be expected, and to ramp up their ongoing communications with customers to provide timely and frequent information if their service commitments cannot be attained. We welcome the increased monitoring that the STB is providing regarding these service issues. Our industry and our farmer-customers need sufficient logistical information from rail carriers to manage market risk. Simply put, there needs to be significantly more predictability in the level of rail service, and mechanisms need to be put in place to reduce service variability that our industry has experienced over the last six months or longer.

Conclusion

Thanks again for the opportunity, and I'll be pleased to respond to your questions at the appropriate time.