



American Short Line and
Regional Railroad Association

TESTIMONY OF

Linda Bauer Darr

President

American Short Line and Regional Railroad Association

REGARDING

The impact of new and existing regulation on short line and regional railroad operations in United States

BEFORE THE

House Committee on Transportation and Infrastructure, Subcommittee on Railroads, Pipelines, and Hazardous Materials. Hearing titled: Building a 21st Century Infrastructure for America: The State of Railroad, Pipeline, and Hazardous Materials Safety Regulations and Opportunities for Reform.

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American Short Line and
Regional Railroad Association

Thank you Chairman Denham, Ranking Member Capuano and Members of the Committee. My name is Linda Darr and I am President of the American Short Line and Regional Railroad Association (ASLRRRA). ASLRRRA is a national trade organization representing the nation's 600 Class II and Class III railroads as well as 526 railroad suppliers and contractors that serve the railroad industry. Together short line railroads operate approximately 50,000 miles of track or nearly one third of the national railroad network. Short lines operate in 49 states and in 30 states they operate at least one quarter of the state's total rail network. Short lines are often called the first mile/last mile of the nation's railroad system and handle in origination or destination nearly one out of every four rail cars moving on the national system.

Thirty Members of this Subcommittee's 32 Members have at least one short line operating in your District and I know many of you are familiar with how and who we serve. For the benefit of those not as familiar with the short line industry let me comment briefly on three important differences between short lines and the large national railroads referred to as the Class I's.

First, short lines are small businesses. Our combined annual revenues are less than the annual revenues of any one of the nation's four large Class I railroads. The average short line employs 30 people or less and a significant number are run with less than a dozen employees. Those employees are cross trained so that on any given day they can be called upon to undertake a variety of tasks.

Second, the majority of short lines operate track that was headed for abandonment under previous Class I owners. These were the light density branch lines that could not make money under the cost structure of the big national carriers. They served small customers that shipped smaller volumes.

Because these were marginal or money losing lines they received little or no capital investment by their previous owners, resulting in significant deferred maintenance. To be successful short line owners must invest between 25 to 33 percent of their annual revenues in rehabilitating their infrastructure. This makes short line railroading one of the most capital intensive industries in the country.

Third, short line operating characteristics are far different than those of the Class I's. Short lines are generally operating in a much smaller geographic area than the Class I railroads. These shorter distances combined with slower speeds and shorter trains produce more predictable work schedules and more routine patterns of interchange and delivery. For the most part our employees begin and end their work day at home.

These three characteristics – our size, our capital needs and our operating requirements – shape our view of the safety regulations that impact our businesses. From our perspective we need regulations that are more efficient, more goal oriented, less reliant on a one size fits all mindset, and much more focused on costs and benefits. We hope your Committee will keep these requirements uppermost in mind as you consider how to improve the regulatory regime.

To be clear we understand the preeminent need to make railroading as safe as possible and we understand that government has an obligation to step in when necessary. But government also has an obligation to step in responsibly. Today that is not always the case. Too often government regulation

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forces companies to spend huge sums of money on solutions that don't solve much, or require operating practices that do nothing to improve operations.

Perhaps most damaging for the short line industry are the kind of one size fits all regulations that provides no basis for the presumed benefits of that compliance and that don't take into consideration our unique operating characteristics; smaller train sets, shorter distance, slower speeds and small staffs.

Let me briefly touch on four examples.

Training Rules – These proposed rules impose an enormous paperwork burden on short line railroads with no corresponding safety benefit. The proposed rule is pursuant to the Rail Safety Improvement Act of 2008 and we believe the FRA's interpretation of that requirement goes far beyond anything contemplated by the statute. In short, the proposed rule requires the creation of training manuals and reports far beyond the capability of the average short line railroad.

If I might be permitted the use of a prop here. Following the proposed rule, the Short Line Association hired a safety professional to produce a template manual that met all the requirements of the rule for just one of the 26 "crafts" or job assignments on the railroad. This is the manual. This notebook would have to be duplicated 26 times to cover all the crafts in our industry. In an effort to see if we could at least standardize this document so each short line would not have to produce its own 26 books, we gave this book to the FRA and asked them to comment on and approve it as a template that could be used by all short lines. It took FRA 3 years to reply. It is ironic indeed that the FRA with its hundreds of employees needs years to review and respond to a manual that it is asking a 10 to 30 person short line to produce in 26 different versions. The ASLRRRA believes that this regulation should be repealed and the underlying statutory requirement revised.

92-Day Locomotive Inspections – This 1980 regulation is a costly requirement that has virtually no impact on safety, in fact the 92 day inspection period was derived from locomotive manufacturer's maintenance recommendations. Inspecting a locomotive is a matter of maintenance not safety. Locomotive failures that could be found through this type of inspection, such as traction motor failures were the cause of .00035% of all main line track derailments for all railroads for the ten year period 2006 to 2016.

This regulation is a classic case of one size fits all. The number of miles a Class I railroad locomotive will travel in 92 days is significantly greater than a typical short line locomotive. On many short lines locomotives are not even used on a daily basis. Yet the cost and paperwork associated with the regulation are the same. For the short line the cost is even greater because sometimes FRA will say that the inspection must be completed where a pit allows the inspector to get under the locomotive. Short lines are not so equipped at most locations and must therefore take the locomotive out of service as it moves to the required facility. Equipment maintenance is an important part of running an efficient and reliable railroad but it should be done when and where it is required.

Mandatory Two Person Crews – This proposed regulation provides a solution to a non-existent problem. First there is no evidence of a safety benefit generated by a second crew member. In fact it is our understanding that the FRA is currently funding a study at Duke University examining whether there is

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even a correlation between crew size and safety. In our estimation, this seems to be putting the cart before the horse.

Second, as small businesses that serve small customers, the added cost of this mandate has a serious economic consequence. Perhaps most important, this unnecessary requirement diverts limited resources from infrastructure improvements which is the most recognized and reliable way to improve railroad safety.

It is ironic that at the same time the Administration is proposing to spend nearly \$4 billion to accelerate the acceptance of driverless cars on U.S. roads it seeks to increase the number of drivers in a locomotive.

Commodity Reregulation – In response to the Ex Parte 704 motion filed with the Surface Transportation Board, the Board is proposing to revoke class exemptions on certain commodities including stone, hydraulic cement, coke and various iron and steel products. One of the most important provisions of the Staggers Act was to exempt railroads from regulation when regulation is not necessary to protect shippers against abuses from market power. But it's important to note short lines face tremendous intermodal/intramodal competition. Geographic and product competition continue and truck transload operations provide strong competition for short distance traffic of the commodities targeted. The average length of haul is 105.9 miles for stone, 19 miles for coke, 75.1 miles for cement and 38.9 miles for iron and steel. These short distances expose this freight to intense truck competition. To regulate these commodities for short lines while leaving them unregulated for trucks would be a giant step backwards.

I have attached to my testimony our filing with the STB on this subject.

Let me conclude with an anecdote that in my mind gets to the core of the importance of safety for our industry. Before joining the short line association I represented the trucking industry for almost 17 years. When we had big meetings they were usually kicked off with a pledge to the flag, or sometimes even a prayer. In the short line industry we start every meeting, big or small with a safety briefing. It's a central focus of what we do. It reflects our commitment to safety and it is an effort to make us safer today than we were the day before. As a matter of fact, with the help of Congress, we stood up the short line Safety Institute with the same goal. We dedicate ourselves to running safe railroads and we work with FRA to help us achieve those goals. And we speak up when we see overreach that is not supportable or that runs contrary to those goals.

You are undertaking a very important task here. If you are able to make regulations more efficient, more goal oriented and more focused on benefits and costs, you will have done our industry a great service and we are deeply appreciative of your effort. I am very thankful for the opportunity to provide the short line industry's perspective on this subject.

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**BEFORE THE
SURFACE TRANSPORTATION BOARD
WASHINGTON, D.C.**

STB Docket No. Ex Parte 704 (Sub-No. 1)

NOTICE OF PROPOSED RULEMAKING

**REPLY OF THE
AMERICAN SHORT LINE AND REGIONAL RAILROAD ASSOCIATION**

**President Linda Bauer Darr
American Short Line and Regional Railroad Association
Suite 7020
50 F Street, NW
Washington, D.C. 20001-1564
Telephone: (202) 628-4500
Facsimile: (202) 628-6430
E-mail: lbdarr@aslrta.org
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Introduction and Interest of the American Short Line and Regional Railroad Association

The American Short Line & Regional Railroad Association ("ASLRRA" or "Association") is an international trade organization of approximately 1,030 members consisting of about 480 short line and regional small, locally-based railroads ("Small Railroads") in 49 states and approximately 550 suppliers and contractors. In a decision served March 23, 2016, the Surface Transportation Board ("STB" or "Board") issued a Notice of Proposed Rulemaking ("NPRM") in which it stated it is seeking public comment on its proposal to revoke existing class exemptions under 49 C.F.R. Part 1039 for (1) crushed or broken stone or rip rap; (2) hydraulic cement; (3) coke produced from coal; (4) primary iron or steel products; and (5) iron or steel scrap, wastes or tailings (collectively the "Exempt Commodities").

Pursuant to a decision served by the STB Office of Proceedings on May 6, 2016, setting the revised dates for filing Comments and Replies in the captioned proceeding, ASLRRA filed Comments opposing the revocation of the in the NPRM on July 26, 2016. In its Comments, the Association opposed the STB's proposal in its entirety, particularly as the revocation of the exemptions would disproportionately harm Small Railroads.

ASLRRA July 26 Comments

ASLRRA submitted that, contrary to the assertions by the Board in its NPRM that changes in the transportation market warrant the application of the Interstate Commerce Act to the Exempt Commodities in order to carry out the federal government's rail transportation policy, the facts demonstrate that Small Railroads do not possess market power in any of the Exempt Commodity markets. Further, the STB's conclusion that waybill rate data for these commodities

shows substantial increase in revenue from potentially captive traffic is not only wrong, but is clearly misplaced insofar as Small Railroads are concerned.

ASLRRA stated that with respect to Small Railroads in particular, regulation of the Exempt Commodities is inconsistent with rail transportation policy. As has been the case for decades, Small Railroads provide a limited scope of service in the movement of the Exempt Commodities in terms of the average distance the commodities are transported and the total revenue derived from transportation of the Exempt Commodities. Further, Small Railroads do not exert any market power over the Exempt Commodities as they rarely even control the rates charged.

ASLRRA said that the STB's conclusion to revoke the exemptions for these commodities is flawed. The STB's stated rationales for this conclusion are:

- (1) There have been many changes in the railroad industry;
- (2) It received informal inquiries questioning the relevance or necessity for the exemptions (without identifying the number of such alleged inquiries, from whom, and when they occurred);
- (3) A record developed in comments and a hearing held in 2011 regarding the exemptions;
- (4) An alleged change in the dynamics of the transportation markets indicating that railroads exert a greater market power for each of the commodities causing a need to regulate them; and
- (5) The STB's waybill study that allegedly shows a substantial increase in revenue from "potentially captive" traffic – described as traffic with a revenue to variable cost ratio ("R/VC") of more than 180%.

Using these faulty rationales, the Board states that the exemptions involved in this proceeding must be revoked in order to "...restore shippers' access to the Board's regulatory oversight and processes." NPRM at 4. In actuality, the whole foundation of the decision to revoke the exemptions rests on the Board's review of the confidential waybill sample and its resultant calculation of the average R/VC ratios for the Exempt Commodities.

ASLRRA participated in Docket No. EP-704, *Review of Commodity, Boxcar, and TOFC/COFC Exemptions* (February 24, 2011 hearing), providing written and live testimony at the hearing held in that docket. The Association stated in that proceeding, *inter alia*, the

following points: (1) the exemptions are effective, having worked exactly as Congress intended; (2) the low number of revocation petitions demonstrate the exemptions are not being abused; (3) the exemptions are of critical importance to short line railroads and have worked as intended for traffic handled by small railroads; (4) the exempted commodities are subject to intense intra- and intermodal competition; (5) for short lines, the competition for traffic moving 500 miles or less is particularly susceptible to diversion to truck; (6) even for traffic moving for distances longer than 500 miles, small railroads have to compete with trucks, waterways, intermodal, and transload operations; and (7) short lines are inherently incapable of abusing market power.

As shown in the Comments filed by ASLRRA on July 26, 2016, not one thing has changed for Small Railroads from the points raised in 2011. In fact, if anything, the competition for this traffic has increased exponentially, with more transloads being installed and larger trucks vying for this traffic.

While there have been changes in the rail industry in general, the operations of Small Railroads are virtually the same today as they were in 2011. As was the case when the exemptions were adopted, the Small Railroads still continue to provide the first and last mile of service, largely at the fringes of the National Rail Network. Furthermore, the market dynamics of Small Railroads remain the same. As the evidence in the Association survey shows, Small Railroads still face tremendous intermodal/intramodal competition, there still exists geographic and product competition, and transload operations provide very strong competition for their short-distance traffic. The statistics gathered from the ASLRRA survey of its railroad members cited in the initial Comments, show that the average length of haul for the Exempt Commodities is 105.9 miles for stone; 19 miles for coke; 75.1 miles for cement; 38.9 miles for iron and steel; and 46.9 miles for iron and steel scrap. These short distances expose the freight to rampant truck competition.

Thus, despite the passage of many years, the dynamics of the Small Railroads have not significantly changed.

Reply to Comments Filed by Supporters of Revocation

ASLRRA has reviewed the 12 Comments filed in this proceeding by parties who have said that the exemptions should be revoked as well as the Comments filed by the parties who

oppose revocation.¹ With some exceptions, each set of the Comments supporting revocation focused on the use by the STB of the average R/VC ratios and rely on stale evidence to support the Board's allegedly reasoned approach justifying the proposed revocations. ASLRRA believes that other respondents and filings clearly demonstrate the shortcomings of the R/VC and evidentiary issues and therefore, the Association focuses the following part of its Reply on certain exception Comments.

Reply to Comments That Are Exceptions

Several exception Comments (1) do not address the issues or those (2) make unsupported conclusory statements about the state of competition in the rail industry and the alleged market power of railroads, (3) actually support the fact there is intermodal, intramodal, product, and geographic competition for the Exempt Commodities, and (4) many mention R/VC ratios only in passing.

For instance, the Comment filed by the United States Department of Transportation ("DOT") does not directly address the use of the data from the confidential waybill samples, R/VC ratios "indicating lack of competition" or "undue market power." DOT quotes its testimony from the February 2011 Hearing, saying, "... each exemption should be evaluated on its own merits, and that each evaluation should be based on a careful, case-by-case review." DOT Comment at 2. DOT goes on to suggest "...that the Board remain open to considering all available evidence, without placing undue reliance upon any single measure as a proxy for market conditions." DOT Comment at 2 (Emphasis added). What the STB has done in the NPRM is precisely the opposite of what DOT recommends – it has relied almost completely on data derived from the confidential waybill sample to reach its conclusions and ignored plain record from both the February 2011 Hearing and other evidence available to it during the nearly half-decade since that hearing. Clearly, the Board has not done a careful, case-by-case approach in this proceeding and has instead placed undue reliance on average R/VC ratios calculated from its study of the confidential waybill samples.

Examples of Comments that make unsupported conclusory statements about the state of competition in the rail industry and the alleged market power of railroads are those filed by the California Construction and Industrial Materials Association ("CalCIMA") and Graniterock. In

¹ The Association of American Railroads and six of Class I railroads filed Comments and ASLRRA adopts those Comments in this Reply.

its one-page Comment, CalCIMA makes the bold, unsupported assertion that "several" of its members are captive to one railroad and "pay excessive rates[.]" without a scintilla of evidence to substantiate these allegations. Graniterock makes similar unsupported assertions in its one-page Comment when it alleges there are delivery locations for its product with no viable alternatives to rail, offering no specifics as to such locations or the rates the consignee pays. Moreover, by its own admission, there is product competition from sources in Canada.

An example of Comments filed by the proponents that actually support the fact that there is intermodal, intramodal, product, and geographic competition for the Exempt Commodities is one filed by the Wisconsin Central Group ("WCG"). WCG admits it is addressing non-captive, truck competitive freight. WCG Comment at 1. It also admits there is inter- and intramodal competition for the products when it describes the shift of a major shipper from an all-rail Canadian National Railroad move to a truck/rail transload operation involving a Small Railroad and Union Pacific Railroad. WCG Comment at 5. WCG says that "[w]e have word of several other similar transloads in the offing...". WCG Comment at 5. By its own Comment, WCG has shown the traffic involved is non-captive and that there is effective intramodal and intermodal competition for the movement of its stakeholders' freight.

The Comment filed by the Freight Customer Alliance ("FRCA")² likewise does not directly address the appropriateness of the STB's use of average R/VC ratios as the primary basis for finding that the exemptions should be revoked. Rather, it argues generally that exemptions are a barrier to shippers seeking rate or service relief from the Board. In essence, it argues that the linkage between the jurisdictional threshold, effective competition, and unavailability of regulatory relief is deficient for several reasons. It states that all exemptions should be revoked, not just those in this proceeding, to allow the STB to provide oversight and remedies to all shippers, regardless of the existence of effective competition and lack of market dominance or market power.

FRCA's position is based on a clearly flawed premise and inconsistent with overall rail transportation policy as well as ignorant of existing avenues that to resolve service issues at the STB.

² On its website, FRCA says it is the reinvention of Consumers United for Rail Equity and states it "...does not seek economic re-regulation of the railroads; rather, it seeks service options and fair prices that are not held to anticompetitive rates or service practices."

The Comment filed by Texas Crushed Stone Company ("TCSC") only mentions the subject of R/VC ratios once, in the context of what it alleges is an increase for all movements of crushed or broken stone or rip rap rather than what the R/VC ratio is for its own traffic. TCSC admits it is served by a Small Railroad that interchanges with two Class I carriers, thus allowing intermodal competition. TCSC Comment at 2. Much of its Comment is directed at what it perceives as problems with the business practices of one of the connecting Class I railroads. Re-regulation of crushed or broken stone or rip rap will not solve whatever problem it feels it faces with that Class I, as nothing it identified in the Comment constitutes an unreasonable practice, particularly when it has a competitive alternative to ship its products. ASLRRA's Comment, on the other hand, based on information extracted from the 2014 waybill sample, shows that the Small Railroad's average R/VC for crushed stone was 130.7%, which is not addressed.

Comments Focused on the Use of Average R/VC Ratios and Other Arguments

Generally, each of the Comments relying on the data derived from the confidential waybill sample and other rationale used by the STB in the NPRM raise the same arguments almost verbatim. Those arguments are (a) the confidential waybill samples show a steep rise in average R/VC ratios, thus evidencing market power by railroads; (b) there are "potentially captive shippers" with rates above 180% R/VC allegedly subject to massive rate increases; (c) consolidation in the rail industry has reduced rail competition; (d) regulatory burdens on railroads have been removed and therefore the exemptions should be revoked; and (e) the option to seek revocation to address a specific issue is impractical. The problem with all of these arguments is that items (a) through (c) do not apply to Small Railroads. With respect to (d), if the exemptions were revoked, the result would be the imposition of regulatory burdens on Small Railroads that have not been justified. Finally, nothing stated in support of argument (e) shows that a case-by-case approach is invalid.

Arguments Relying on R/VC Ratios

The reliance by the anti-exemption Commenters on the waybill data used by the STB in the NRPM is totally misplaced, particularly with respect to Small Railroads. Many shipments handled by Small Railroads do not appear in the waybill samples because the Small Railroads do not appear on the waybills or in the routings. As pointed out in the Verified Statement of Gerald Fauth, III, filed contemporaneously with the ASLRRA Comments, there are numerous problems with the STB's approach to determining to revoke the exemptions for these five commodities.

The confidential waybill sample that the STB uses contains relatively few records from Small Railroads and is largely relevant only to Class I railroads. Mr. Fauth sets forth this flaw in detail in his Verified Statement. *See*, Fauth V.S. at 7-8.

Determination of R/VC ratios depends in large measure on the STB Uniform Railroad Costing System ("URCS"). In a Position Paper unanimously adopted by the Railroad-Shipper Transportation Advisory Council ("RSTAC")³ the RSTAC reported a number of problems with URCS, including the following:

- The Board has recognized that "the development of system-wide variable costs associated with a particular rail movement requires that any costing methodology incorporate many assumptions and generalizations about railroad operations." The problem as it relates to Class II and III carriers is that URCS contains no assumptions and generalizations about small railroads' operations. Without those assumptions, URCS is not useful as it relates to small railroads.
- URCS relies entirely on data obtained from the R-1 forms and other data filed with the STB by the Class I railroads. On high density Class I rail lines, the fixed costs of track maintenance, supervision, and communications and control can be spread over large amounts of traffic. As a result, average costs of operation over these lines may not be greatly in excess of variable costs and it is fairly easy to determine the costs of operation over any portion of the network.
- For light density rail lines of small railroads, fixed costs must be allocated to a much smaller amount of traffic and average total costs will be well in excess of variable costs. As a result of the small size and light densities typical of the small railroads, their fixed costs are generally the largest proportion of their total costs on a per carload basis.

³ RSTAC was established pursuant to the ICC Termination Act of 1995. Its 15 appointed members consist of senior officials representing government, shippers, and railroads who share a common goal to strengthen the national rail industry to improve service levels and foster mutually beneficial relationships between large railroads, small railroads, and shippers, across all commodity groups. RSTAC is charged to provide a private sector forum for the discussion of matters of concern to small rail shippers and small railroads and to provide advice on regulatory, policy, and legislative matters to the STB, the Secretary of Transportation, and Congress.

- Engineering time and motion analyses form the basis of the special study factors used in URCS. Some of those studies date back to the 1930's. In the decades since those studies were done, dramatic changes have occurred in the rail industry. Not least among those changes since 1980 is the emergence of hundreds of short line and regional railroads and a concentration of heavier cars and trains creating operating and maintenance factors unlike the conditions in the 1930's and unlike those experienced by any regional or short line. The engineering studies do not take into account those changes. In fact, URCS does not contain any of the operating characteristics of short line or regional railroads or their cost structures.
- There are several key general characteristics of small railroads that make them different from Class I railroads:
 - Their service territories are local or regional and their traffic densities are generally low.
 - Fixed costs are generally the largest proportion of their total costs.
 - They have lower shares of dominant rail commodities such as coal, motor vehicles, and intermodal, but a much higher concentration of non-captive, truck competitive general merchandise traffic.
 - The traffic and commodity mix varies from short line to short line.
 - They are often dependent upon a limited market and a traffic base that can be non-diversified.
 - They are mostly involved in the switching-intensive portions of rail trips, namely the "first and last miles" in serving customers.
 - Most traffic handled by short lines, however, originates within terminal areas or along light density lines where traffic volumes are much lower, train speeds are slower, and fixed costs are a much larger component of total costs.

*RSTAC Position Paper on the Uniform Rail Costing System, November 22, 2011.*⁴

The fact that URCS contains no assumptions and generalizations about Small Railroads renders URCS irrelevant to Small Railroads. Plus, the R-1 forms are not even required for Small

⁴ In its Comment, AAR describes in great detail all the problems and limitations with URCS. See, AAR Comment at 23-28.

Railroads and many Small Railroads do not even have systems or data to provide the data.

These problems with URCS result in flawed calculations of R/VC ratios, particularly for Small Railroads. The STB has recognized at least some of the problems by instituting a proceeding in EP 431 (Sub-No.4), *Review of the General Purpose Costing System*, Decision Served August 2, 2016, pursuant to which it proposes to eliminate the make-whole adjustment in URCS and make other adjustments to it as well. To permit reliance on URCS' framework in deciding the R/VC aspect of this proceeding, without resolution of these issues for Small Railroads, is widely unfair.

Arguments Relying on "Potentially Captive" Shippers

The STB and those parties who rely on a 180% average R/VC as a marker to assert that any average R/VC above 180% R/VC is a "potentially captive" shipper. However, even the Board recognizes in the NPRM that R/VC ratios at or above 180% cannot, standing alone, establish market power or abuse of market power. The use of 180% and reliance on it is entirely misplaced, as that standard is statutorily limited in its use. As noted above, this approach is in contravention of the language of the statute and also ignores the well-documented problems and limitations of R/VC as described above. Moreover, the issues of "captive shippers" are the subject of other proceedings and should not be a dispositive element of this proceeding on Exempt Commodities.

Arguments Relying on Consolidation in the Rail Industry

While it is true that there has been a dramatic consolidation in the Class I segment of the railroad industry, that same phenomenon has not occurred with Small Railroads. There are currently approximately 550 short line and regional railroads operating in 49 states. Many of those railroads have 10 or fewer employees and 147 of them generate annual revenues of \$2 million dollars or less. Small Railroads operate over approximately 43,131 miles of track, 38% of the nation's rail network. Their traffic base is largely general merchandise highly susceptible to diversion to other modes. The average route mile distance for Small Railroads is 91 and the median route mileage only 34. Traffic densities are light and fixed costs are high. Those statistics hardly bespeak of a consolidated industry. Thus, the arguments raised by some of the Comments supporting the revocation of these Exempt Commodities that consolidation of the rail industry removes the need for the exemptions are totally inapplicable to Small Railroads.

Arguments Relying on Removal of Regulatory Burdens

Imposition of regulatory oversight by the STB of the Exempt Commodities would be a burden on Small Railroads, an imposition not warranted by the facts concerning the transportation of these commodities by Small Railroads. The members of the Association are small businesses not staffed to handle litigation costs, filing requirements, and other regulatory burdens. Small Railroads would be expected to fulfill their common carrier obligations regarding these commodities, which means they would be required to spend scarce resources defending allegations, to the detriment of their operations. Similarly, they would be exposed to other regulatory oversight on compliance with the STB regulations, which would require them to expend time and money that is not always available addressing those issues.

While Class III carriers are exempt from some reporting and recordkeeping requirements, if these Exempt Commodities are reregulated, the approximately 480 short line and regional railroad members of ASLRRRA would still have to bear the cost of maintaining additional reports and records. For example, approximately 100 ASLRRRA members have 10 or fewer employees, all of whom typically perform multiple functions on their railroads. Additional burdens to address a spurious issue would either necessitate hiring or adding make-work duties to multi-tasking employees. Such requirements of Small Railroads would be costly both financially and operationally.

Arguments that Seeking Revocation to Address a Specific Issue Is Impractical

Some of the pro-revocation Comments argue that the ICC Termination Act of 1995, Pub. Law no. 104-88, § 102, 109 Stat. 803, 804 (1995)⁵ ("ICCTA") removed the regulatory burdens on railroads that once served as a reason to grant the exemptions in the first place and that because those burdens are no longer in place, the exemptions should now be revoked. While it is true many regulatory burdens have been removed, the corollary is that the imposition of re-regulation of the Exempt Commodities would place new and potentially expensive costs on Small Railroads. With no discernable benefit to them or the shipping public, they could be forced to defend against rate reasonableness or service complaints, sucking up scarce resources that could otherwise be used to improve their infrastructure and expand their services.

Reply to Specific Comments

⁵ ASLRRRA has addressed argument (1) previously in this Reply and therefore will not repeat that here.

The following responses are directed at individual Comments that embody one or more of the arguments set forth above as constituting rationales for revoking the Exempt Commodities.

Rail Customer Coalition ("RRC"):

This large collection of trade associations argues that all of the proposed revocations be adopted because of railroad consolidation, rate trends that demonstrate an overall increase in market power, data from the public use waybill sample for all major commodity groups for 2014 (other than intermodal) showing a general shift towards higher R/VC ratios, a significant increase in R/VC ratios over the last two decades, a higher percentage of "potentially captive traffic" – defined as traffic with rates above 180% R/VC – for each of these Exempt Commodities, and removal of regulatory burdens on railroads.⁶ It closes its Comment with the statement that the STB should provide a broad analysis of all commodity exemptions.

The problems of the analysis upon which RCC relies are many. As described above, the whole process of determining R/VC ratios is flawed and certainly inapplicable to Small Railroads. Second, the study on which RCC relies only examined Class I railroad rate data from the STB. The study erroneously states the data represent 100% of all rail shipments, but most Small Railroad shipments are not included in the Public Use Waybill Sample. Further, the analysis is also skewed because it includes commodities not involved in this proceeding.

AK Steel; Steel Manufacturers Association ("SMA") and American Iron and Steel Institute ("AISI"); and The Institute of Scrap Recycling Industries, Inc. ("ISRI"):

The Comments from all three of these entities support revocation of the exemptions concerning coke, steel, and scrap (with ISRI focusing on scrap). Their case is based on three basic arguments: (1) the burden of having to file tariffs was abolished by ICCTA; (2) railroads have greater market power because of "several" changes relating to the transportation of coke, steel, and scrap; (3) the calculation of the current average R/VC for coke is 248%, for steel 237%, and for scrap 230% and commodities with ratios that high should not be exempted from regulation; (4) petitions seeking partial revocation are impractical and time-consuming; (5) railroads are extraordinarily profitable; and (6) their members deserve access to the oversight of the STB.

⁶ Despite this argument in support of the revocation of the exemption on all the Exempt Commodities, it acknowledges that R/VC ratios are "...not a perfect metric" to determine market power. RRC Comment at 2.

Even if the argument about changes in the transportation of iron and steel necessitating the revocation of these exemptions may be true, as very little has changed regarding Small Railroads' service to shippers of coke, steel, and scrap. For example, the average length of haul for coke is 19 miles, cement 75.1 miles, iron and steel 38.09 miles, and scrap 46.97 miles. These mileage figures did not vary year-to-year over the three years reported.⁷ The carload statistics gathered in the ASLRRRA member survey underscore the importance of these Exempt Commodities to Small Railroads. For the years 2013-2015, the carriers that responded to the survey handled a total of 1,026,268 carloads of these Exempt Commodities. They handled 86,754 carloads of coke (8.45%% of their total carloads), 171,017 carloads of iron and steel (16.7% of their total carloads), and 239,850 scrap (23.3% of their total carloads). Revenues derived from the transportation of these Exempt Commodities are also vital to the Small Railroads. In response to the survey, the Small Railroads reported total operating revenues for the years 2013–2015 at \$1,186,515,100. The responding carriers earned 20.3% of their revenues from transporting coke, 7.5% from iron and steel, and 9.1% from scrap. Those percentages also did not vary over the three-year period.

These entities argue next that the Board's calculation of the "current" average R/VC ratios for coke, steel, and scrap are high; therefore, these Exempt Commodities should not be exempted from regulation. In response, ASLRRRA submits the following:

- First, as previously shown in ASLRRRA's Comment and in this Reply, the calculation done by the STB is fatally flawed and any reliance on it is without merit;
- Second, the confidential waybill sample that the STB used contains relatively few records from Small Railroads and is really relevant only to Class I railroads;
- Third, Mr. Fauth, the ASLRRRA expert witness, sets forth these flaws in detail in his Verified Statement filed simultaneously with its Comments;

⁷ As the STB says in footnote 12 on page 7 of the NPR, "Trucking becomes less viable when the length of haul exceeds 500 miles... [.]" Taking the Board at its word, the facts detailed in ASLRRRA Comments and in this Reply show that the average length of haul for these commodities remains truck (and barge) competitive since they are all substantially below 500 miles. Moreover, the fact that the average length of haul has not increased for Small Railroads is another indicium that they do not exert increased market power over shippers of these commodities.

- Fourth, the NPRM does not analyze the impact of the decision on Small Railroads at all and AK Steel and other anti-exemption Comments citing the R/VC calculation as support for removing the exemptions do not either;

These entities argue that petitions seeking partial revocation are impractical and time-consuming. Other than this conclusory-type statement, they do not elucidate why this is the case. The controlling statute not only provides shippers with the right to petition for revocation of existing exemptions but requires that the STB must expeditiously resolve them. The fact that only a few such petitions have been filed does not form a basis to determine that exemptions should be revoked on a wholesale basis. The DOT itself succinctly states the grant or revocation of an exemption should be determined on a case-by-case basis, and ASLRRRA agrees with that.

The argument that Exempt Commodity shippers deserve to have access falls woefully short of a rationale for re-regulating Exempt Commodities, given two facts. There is no cogent evidence in this record that justifies re-regulation. Additionally, Exempt Commodity shippers have multiple means of access to the STB and should take advantage of one or more of those if they have an issue.

Finally, these entities argue that "railroads are extraordinarily profitable." Without regard to whether this argument is even pertinent to the issue at hand, the fact is that Small Railroads are not "extraordinarily profitable." Unlike Class I railroads, Small Railroads are characterized by high fixed costs, short distances they transport freight, light traffic densities, intense competition from trucks, barges, intermodal, and transload operations, and lack of control over pricing.

As set forth in ASLRRRA's Comments and this Reply, the evidence adduced by the ASLRRRA shows that revoking the exemptions would have a devastating adverse effect on Small Railroads.

Portland Cement Association ("PCA"):

As this Association's name suggests, it supports the revocation of the exemption for hydraulic cement. Its principal arguments in support are that competition for the transportation of hydraulic cement has diminished; an increased average length of haul has decreased truck competition; rail mergers have reduced intramodal competition, and the increase in the R/VC ratios substantiates the revocation of the exemption on cement. The facts presented by ASLRRRA in its Comments show these arguments do not apply to Small Railroads. Their average length of

haul for cement is 75.1 miles, well within the 500-mile range within which the STB considers a commodity may be truck competitive and certainly well within the range of 100 to 125 miles that the Board says is truck-competitive. NPRM at 10. In short, this traffic is still predominantly short haul in nature, so the length of haul justification for exempting cement is still extant.

Trucks and barges remain strong competitors to transport cement. There is also intermodal competition among the railroads – both Class I and competing Small Railroads. Ninety-one of the responding railroads stated that trucks serve as the biggest competitive threat to their operations for the Exempt Commodities. That is the reality of the Small Railroad world, the reason they are often referred to as "feeder lines."

PCA's R/VC argument in support of revocation does not warrant that conclusion. The average 2014 R/VC for Small Railroads handling this commodity was 190.7%, only slightly above the jurisdictional threshold of 180%. This ratio hardly supports a finding that the average R/VC supports reinstating regulation of cement.

The American Forest and Paper Association ("AF&PA"):

AF&PA addresses commodities that are not even the subject of the NPRM; namely forest products and paper products and boxcars, insofar as the latter haul forest products. They argue that the exemptions for those products and boxcars need to be revoked. The major points raised in support of their position are largely the same as raised by other pro-regulation parties; namely, (1) the average R/VC ratios as calculated by the STB allegedly show "...an obvious increase of market railroad power..." regarding forest products; (2) there no longer is intramodal and intermodal competition; (3) today railroads are financially strong; (4) the regulatory burdens on railroads have been removed; and (5) the pricing policies demonstrate the market power of railroads.

ASLRRRA has previously replied to AF&FP's arguments (2), (3) and (4) in this Reply and will not repeat those facts but rather adopts them in response to the Comments of these associations.

Regarding the argument about the average R/VC ratios for forest products supporting re-regulation of forest products, ASLRRRA has two responses. First, the methodology AF&FP's expert witness used in calculating the R/VC ratios uses waybill samples for a vast range of commodities not involved in this proceeding and thereby grossly overstates the ratios and

distorts the record. Second, the consultant's study ignored Small Railroads in their entirety, leaving a major hole in the study. In that regard, the statistics related to Small Railroads' average R/VC ratio of for the largest STCC group, 26-311-17- Pulpboard or Fiberboard, shows that Class II and III railroads handle 57,840 carloads, which represents 20.24% of the total carloads handled and over \$242 million in revenue derived from handling those carloads (which is likely understated because of the waybill sample reporting problems involving Class II and III railroads). The average R/VC ratio for movements involving Class II and III railroads is 138.51%.

AF&PA also makes some sweeping allegations that lack any support in their comments. For example, it asserts that one-third of all forest products facilities and many paper mills across the country are captive to a single railroad without presenting any evidence to substantiate these allegations.

In summary, AF&PA offer no substantive arguments to revoke the exemptions it seeks. The economic study supporting its position is deeply flawed and includes commodities beyond even the scope of what it proposes to have reregulated, thus distorting the record and rendering its conclusions unreliable.

Summary

There is no basis under the law to regulate the Exempt Commodities. Regarding Small Railroads specifically, regulation of the Exempt Commodities would be completely inconsistent with rail transportation policy. Small Railroads provide a limited scope of service in the movement of the Exempt Commodities in terms of the average distance and revenue derived from their transportation. Small Railroads do not exert any market power over the Exempt Commodities since they rarely even control the rates charged.

ASLRRRA's Comments and this Reply respond in detail to each of the STBs proposed rationales and show that the STB's reliance on them to justify its conclusion to revoke the exemptions is simply wrong. Not one of these rationales applies to Small Railroads. The NPRM does not analyze the impact of the decision on Small Railroads at all. As set forth in these Comments, the evidence adduced by the ASLRRRA in its Comments shows that revoking the exemptions would have a devastating adverse effect on Small Railroads.

ASLRRRA agrees with the summation of Vice Chair Miller that the record in this proceeding is less than robust. Therefore, the Board should not have relied on it to make the

findings it did in this NPRM. The market dynamics of Small Railroads remain largely unchanged. They face tremendous intermodal/intramodal competition, there still exists geographic and product competition, and transload operations provide very strong competition for their short-distance traffic. The average length of haul for these commodities is 105.9 miles for stone; 19 miles for coke; 75.1 miles for cement; 38.9 miles for iron and steel; and 46.9 miles for iron and steel scrap. These short distances expose the freight to rampant truck competition. The STB's assertion that there is no effective competition for this traffic and that there is an undue concentration of market power in the rail industry is fatally flawed with respect to Small Railroads. Unlike Class I railroads, Small Railroads are characterized by high fixed costs, short distances they transport freight, light traffic densities, intense competition from trucks, barges, intermodal, and transload operations, and lack of control over pricing.

The NPRM did not perform any analysis to determine the impact of the proposed rules on Small Railroads. Nor is there any indication in this record that the STB notified the Small Business Administration Office of Advocacy of the proposed rules. ASLRRRA respectfully submits that both of these steps must be undertaken before any final rules are promulgated or face the possibility that a court would later reject any rules the STB adopts.

The record clearly does not support the premise that there is a lack of competition facing Small Railroads with respect to the Exempt Commodities, nor do they support an assertion that the Small Railroads exercise undue market power in the rail industry. All rationales used by the STB to revoke the exemptions are contradictory to the reality of operations of Small Railroads and the facts that were presented. ASLRRRA respectfully submits the STB dismiss the NPRM and not allow the regulation of these Exempt Commodities.

Respectfully submitted,

American Short Line and Regional Railroad Association



By: Linda Bauer Darr, President
American Short Line and Regional Railroad Association
50 F Street N.W., Suite 7020
Washington, D.C. 20001-1564
Telephone: 202-585-3440
Fax: 202-628-6430

Email: lbdarr@aslrra.org