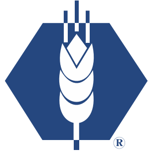

National Grain
and Feed Association
www.ngfa.org

1250 Eye Street, N.W., Suite 1003
Washington, DC 20005-3922
P: (202) 289-0873
F: (202) 289-5388

Before the U.S. Surface Transportation Board

STB Docket No. 665 (Sub-No. 1)

Rail Transportation of Grain, Rate Regulation Review

Testimony of

Bruce Sutherland

on behalf of

The National Grain and Feed Association

June 10, 2015

Good morning, Acting Chairman Miller and Commissioner Begeman. I am Bruce Sutherland, Vice President of Michigan Agricultural Commodities, headquartered in Lansing, Michigan. As Kevin noted, I also am a member of NGFA's Board of Directors, and am appearing today at the request of NGFA to add some current real-world perspectives on the rate issues you are considering in this proceeding.

As brief background, Michigan Agricultural Commodities was established in 1976 and consists of eight grain elevators at seven locations throughout Michigan, with a combined storage capacity of 43 million bushels. Our facilities annually handle approximately 50 million bushels of corn, soybeans, dry edible beans and oats. MAC also operates an agronomy business that serves producers at two locations in central Michigan.

Michigan is a short-line-dominated state, and CSX Transportation is the dominant, and often the only, Class I connection for our shortline railroads. The majority of Michigan agricultural shippers are short-line served, and therefore, are captive to CSX for the Class I connection needed to reach both domestic and export markets served by CSX and other Class I railroads.

In many ways, I regret the business-related circumstances that cause me to be here today. I also am reluctant to single out one Class I railroad for attention since the rate issues faced by agricultural commodity shippers are common to all Class I railroads. However, the recent actions finalized on May 29, 2015 by CSX that significantly changed its rates for agricultural commodities nationwide provide a timely example to this Board as to why captive agricultural commodity shippers need access to a workable, cost-effective, and expeditious rate-complaint process.

Let me provide a few specifics. CSX's rates for corn and soybeans are published in CSX Tariff 4315. Since 1999, very few movements of these commodities are by contract anymore, by carrier choice. In April of this year, CSXT announced to the agricultural industry that it had decided to simultaneously make wholesale changes to many of its common-carrier rates for agricultural commodities in Michigan and other Midwestern states. This was not done on an individual-customer basis, but rather on a system basis. The increases to rates and to rate "spreads" for Michigan shippers range from 35 to 100 percent, and they are to take effect October 1. When I refer to a rate "spread," I mean the geographical and cents per bushel

difference between Columbus Ohio, which is the base point for the CSX tariff 4315, and the specific origins named in each state of the tariff.

Two of MAC's elevators located in Breckenridge and Marlette, Michigan, were most affected by this action – with rate increases of 70 percent applied to each. This increase added 12.8 cents per bushel to those two elevators' shipping costs, which far exceeds typical grain-trading margins. The increase forced us to immediately reduce prices by 10 cents per bushel for corn and soybeans purchased from farmer-customers that do business with those two facilities, just to cover the increased freight rate. Since these two facilities handle more than 15 million bushels of corn and soybeans annually, the increased rail rates translate into a $1.5 million reduction in income to these corn and soybean customers.

Unfortunately, our company is not alone. I have heard reports from other shippers operating facilities in Michigan, Illinois, Ohio and Indiana of even more severe rate increases that resulted in reduced price bids to farmers of up to 20 cents or more per bushel. These increases in rail rates are several orders of magnitude greater than typically thin grain-trading margins. Consequently, if we are to be price-competitive in selling commodities to domestic users and foreign buyers, we inevitably have to try to pass on the cost impacts we can't absorb back to farmer-customers. Seldom are we able to pass such costs forward to the ultimate buyer, as they have alternative sources of supply in the grain market – which is a truly competitive market. The rate increases adversely affected not only our cost in the freight difference between Michigan and Columbus Ohio, but beyond Columbus to our end users that set the bids for corn, soybeans and wheat. MAC, like other grain elevator companies, posts bids based both on our local competition and sales values that we can sell. The market, which really determines the bids that we can post, fell in proportion to the rate increases. Grain margins are already well defined, and do not allow much for absorption of cost, due to the elastic supply and demand characteristics of the grain marketplace.

CSXT is but one part of the overall domestic and global agricultural marketplace, but these broad and dramatic changes in rates have resulted in changing the competitive balance in Michigan and surrounding states, and they stand to change the flow of grain that normally would occur based on response to market demand. In some cases, the new CSX rate structure will force a shift from rail to much less efficient and much more costly truck transportation, creating more burdens on

the state's highways, roads, and bridges that already are at or beyond capacity given their current condition.

We are still analyzing the effects of the new rate scheme, but it is apparent that it **could** result in fewer agricultural commodities being carried by CSX, and a greater concentration of these commodities being moved on CSX's main lines, **[Bruce, are you comfortable saying this?]** to the detriment of the Michigan short lines, which rely on agricultural volumes for their economic viability.

Unchecked rate increases for agricultural commodities also have the harmful effect of undermining investment that we and others have made in our facilities, often at the direct encouragement of the rail industry. MAC spent more than $35 million over the past five years to increase grain storage and loading capacity to be able to handle both the growth in grain production and the ability to ship 90-car unit trains, the latter of which was done in response to warnings from CSX about the need to make improvements to meet the larger train sizes being preferenced by the railroad. Millions of dollars similarly have been invested by other rail shippers in their storage and handling facilities for similar reasons.

Similarly, I know of a NGFA-member company in Ohio that invested in expanding its facilities to handle 90-car unit trains based on the implicit and/or explicit assurance from the Class I carrier that the rate spreads through Columbus would remain competitive and be preserved. However, the new 90-car unit train spreads are now the equivalent to what previously applied to only three-car shipments. This member believes the rug has been pulled out from under them.

Other Class I railroads engage in similar pricing behavior, but CSX provides a current example that substantiates the assertions in the NGFA's submissions in this proceeding about how unchecked unilateral rail rate actions can and do "demarket" the movement of agricultural commodities to domestic and export markets. In fact, another NGFA-member company in the West reports that rail rates charged for transporting milling wheat from South Dakota through the Chicago gateway increasingly are being implemented on a percentage basis, which disproportionately affects shippers with higher base rates. Rates were increased by 5 cents per bushel in January 2015 for milling wheat from South Dakota through the Chicago gateway, and are scheduled for an additional 3-cent-per-bushel increase effective Aug. 1. This shipper reports it had just invested $5 million in track and storage upgrades.

These unilateral rate actions can have the outcome of changing the competitive dynamics within our industry, in effect picking winners and losers based upon the carriers' dictates and preferences on which types and sizes of facilities it desires to serve and commodities it wishes to carry.

MAC believes broad geographic areas of CSX's grain-origin markets will see wrenching changes as a result of these rate increases and structure, with commensurate disruptions in customary grain flows to customers. From a global perspective, it is not unreasonable to anticipate that these increased freight costs will encourage customers, particularly those near ports, to pursue imports of grain from South America as a more cost-competitive alternative – to the detriment of U.S. farmers and the American economy.

MAC and NGFA believe that the existence of effective and accessible agricultural rail rate rules would help prevent or mitigate some of the adverse consequences of the railroad pricing behavior exhibited by Class I railroads. Again, we don't believe that would result through dozens of rate cases being filed before the Board. Rather, such a meaningful regulatory backstop would alter the current market dynamic such that the railroads might not be inclined to make such dramatic and arbitrary rate proposals in the first place, and captive shippers that conclude they are harmed by such practices would have a better chance of reaching mutually acceptable commercial resolutions of their differences.

Conclusion

Thank you for this opportunity to discuss some of the real-world impacts that actual rate-setting practices by rail carriers have on captive shippers, our farmer-customers and the markets we try to serve. Now, let me turn to Mr. Crowley to explain NGFA's proposal.