SURFACE TRANSPORTATION BOARD

Ex Parte 711 (Sub-No. 1)

Summary of Ex Parte Meeting held by video conference August 4, 2021 between Shipper Associations and Surface Transportation Board Vice Chairman Robert Primus

Shipper Association Attendees:

- Karyn Booth, Counsel to the National Industrial Transportation League (NITL)
- Ross Corthell, Vice President-Transportation, Packaging Corporation of America
- Connor Hamburg, Manager of Government & Industry Affairs, Nutrien
- Jennifer Hedrick, Executive Director, NITL
- Brad Hildebrand, Vice President and Global Rail and Barge Lead, Cargill
- Justin Louchheim, Director, Government Affairs, The Fertilizer Institute (TFI)
- Jeffrey Moreno, Counsel to the American Chemistry Council (ACC) and TFI
- Randy Mullett, Senior Policy Advisor, NITL
- Jeffrey Sloan, Senior Director, Regulatory & Technical Affairs, ACC
- Alexander Stege, Director, Public Affairs, CF Industries
- Jason Tutrone, Counsel to ACC and TFI

STB Attendees:

- Robert Primus, Vice Chairman
- Elizabeth McGrath, Attorney Advisor

Meeting Summary:

The Shipper Associations began the meeting by explaining that the meeting's purpose was: to answer questions about the Board's options for advancing Ex Parte 711 (Sub-No. 1), especially in light of President Biden's recent executive order on competition; and to help educate Vice Chairman Primus on the Shipper Associations' position in Ex Parte 711 (Sub-No. 1).

The Shipper Associations explained that their preference is for the Board to proceed with completing Ex Parte 711 (Sub-No. 1) on the current record, which is extensive. They explained that, although the proposal is not perfect, it is good and feasible, provided the Board considers proposed modifications in the record to avoid lengthy proceedings. They also explained that the proposed rule reflected a case-by-case approach that addresses railroad concerns by enabling the Board to address any issues with competitive switching if and when they arise. They commented that starting the proceeding from scratch would introduce extensive delay and that it is unnecessary to supplement the record because the need for competitive switching has grown, railroad opposing arguments have not changed over time, and the financial situation of railroads has improved. They also commented that recent service issues strengthen the case for moving forward on Ex Parte 711 (Sub-No. 1), and that shippers in many other ex parte meetings regarding Ex Parte 711 (Sub-No. 1) have explained how competitive switching could help address service issues.

Vice Chairman Primus asked how some shippers have been able to access competitive switching and what data we have regarding this access. The Shipper Associations explained that those shippers had competitive switching from past mergers, where the railroads had accepted competitive switching as conditions of merger approval, or from legacy agreements that have existed for many decades. The Shipper Associations also explained that those reciprocal switching conditions have been very successful.

Vice Chairman Primus asked for the reasons that railroads have opposed competitive switching. The Shipper Associations responded that much of the railroad opposition has been on operational grounds, and that railroads have laid out the worst-case operational scenario. Vice Chairman Primus followed up by asking whether the railroads experience operational challenges today due to existing competitive switching. The Shipper Associations responded that they are unaware of any operational challenges similar to those that the railroads claim would exist under competitive switching. TFI explained that its members have extensive operations Canada, where competitive switching is broadly accessible, and there is no concern in Canada over whether Canadian competitive switching is acceptable operationally. Cargill commented that competitive switching works well where Cargill has access to it in the United States. The Shipper Associations also added that the record contains explanations from many shippers of how competitive switching has been used successfully. Vice Chairman Primus expressed a desire to improve service and produce a positive result for railroads and shippers.

The Shipper Associations commented that a second reason for railroad opposition to competitive switching is that they claim it will discourage investment in the rail network. The Shipper Associations explained that the greater competition would encourage investment. They also explained that, in the real world, railroads have invested heavily in highly competitive traffic, such as intermodal and automotive. In addition, the Shipper Associations explained that a lot of the railroad concerns are covered in the record and a hearing, with an opportunity to cross examine, might be an effective way for the Board to obtain additional information in lieu of soliciting more comments that are most likely to retread matters already thoroughly covered in the existing record.

Vice Chairman Primus and the Shipper Associations discussed how the Board could obtain additional information in an efficient manner. The Shipper Associations stated that the Board should carefully consider the scope of any reopening of the record.

The Shipper Associations walked through the “Bottleneck Extensions” slide (See Exhibit-1) they presented to Vice Chairman Primus to demonstrate how past mergers have resulted in unremedied competitive losses through foreclosure of competition due to extended bottlenecks. Although the contract exception to bottlenecks could have mitigated some of that competitive loss, most mergers occurred before the contract exception existed and the Board committed to preserving the contract exception in its 2001 merger rules.

The Shipper Associations walked through the "The STB's Ex Parte No. 711 [(Sub-No. 1)] Rulemaking Proceeding Is Deregulatory and Pro-Competitive" slide that they presented to Vice Chairman Primus. They explained that reciprocal switching is deregulatory because shippers no longer would be forced to rely upon STB regulation of rates over the portion of a bottleneck that overlaps the line of the competing carrier.

The Shipper Associations walked through the "Reciprocal Switch Scenarios" slide that they presented to Vice Chairman Primus. They explained that the railroad criticism of reciprocal switching has focused solely upon scenarios that add an interchange by converting single line moves to joint line moves, whereas the most common scenarios do not add any interchange but merely change the location. They also explained that, in each switch scenario, there would be no operating impact on the incumbent carrier if it retains the issue traffic. In addition, they explained that competitive switching does not impose additional steps where an interchange occurs at existing interchange locations. They also noted that railroads have represented "worst-case" switching scenarios to be typical and explained that the case-by-case approach embodied in the proposed rule would enable the Board to consider operational impacts of such scenarios if and when they arise. The Shipper Associations also stated that their expert has explained that railroads are constantly adjusting their operations and could do so to mitigate operational issues if necessary.

The Shipper Associations commented that pricing of a competitive switch is important to the efficacy of a competitive switching rule. They stated that prices must be competitive for the rule to be effective, and that efficient component pricing would prevent competitive switching from producing benefits for consumers.

TFI explained that one of its members has locations in the southeastern United States where they have reciprocal switching today and were able to use it to avoid service issues during implementation of precision scheduled railroading. TFI also commented that many of its members use Canadian competitive switching primarily to address service challenges.

The ACC commented that competition provides an opportunity to address service issues. It also commented that, while railroads claim that competitive switching will cause operational problems, expert testimony submitted on the record by the Shipper Associations shows much of the traffic that would be interchanged under competitive switching would not require an additional switch because it would be interchanged at locations where railroads are already interchanging traffic.

The meeting concluded.

Bottleneck Extensions Through Mergers

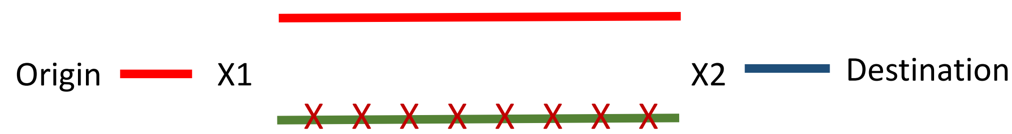
Pre Merger

Shipper is captive at origin and destination, but has competitive options at first interchange (X1)

Post Merger

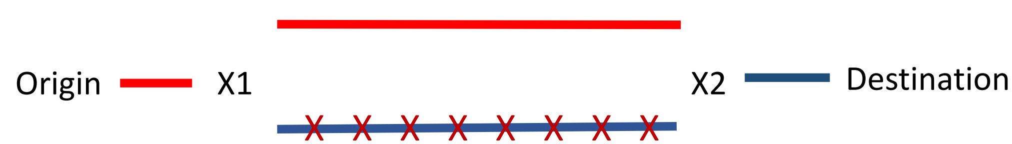
Scenario 1

Captivity at origin extended to interchange near destination (X2)



Scenario 2

Two RRs have equally efficient routes, but the origin RR can foreclose any competition from the destination RR

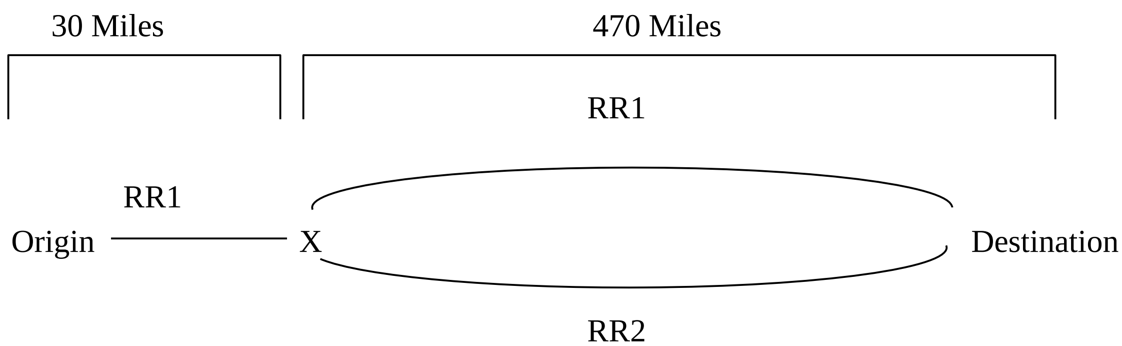


The STB’s Ex Parte No. 711 Rulemaking Proceeding Is Deregulatory And Pro-Competitive

Objective: Allow competition to replace regulation of the rail industry when a competing railroad is accessible within a reasonable distance of an origin or destination that is captive to a single railroad.

How It Works: Upon a shipper’s demonstration of a need for competitive rail service, the STB will grant a request for reciprocal switching, which requires a railroad to interchange the shipper’s rail cars to a competing railroad within a reasonable distance of the captive origin or destination, provided that the interchange is safe and feasible.

Illustration:



Deregulatory Impact: Today, existing regulations require the captive shipper to use RR1, in the above illustration, for the entire 500 mile distance, despite the ability of RR2 to compete for 470 miles. Therefore, to protect the captive shipper from monopoly pricing by RR1, the STB must regulate RR1’s rate for the entire 500 mile distance.

Under EP 711, reciprocal switching will allow the STB to regulate just the first 30 miles of physical captivity to RR1, in the above illustration, and allow competition between RR1 and RR2 to determine the rate for the remaining 470 miles.

Additional Benefits: Competition through reciprocal switching, instead of regulation, provides greater incentives for railroads to improve service and invest in new infrastructure that will make American businesses more competitive.

Competition through reciprocal switching will reduce reliance upon existing STB rate regulation, which requires incredibly complex litigation over several years and costs millions of dollars for an uncertain result. Because most captive shippers do not tender sufficient volumes between the same points over a sufficiently long time period to economically justify this time and expense, competition is a more effective constraint upon rail market power than rate regulation.

RECIPROCAL SWITCH SCENARIOS

Fig. 1

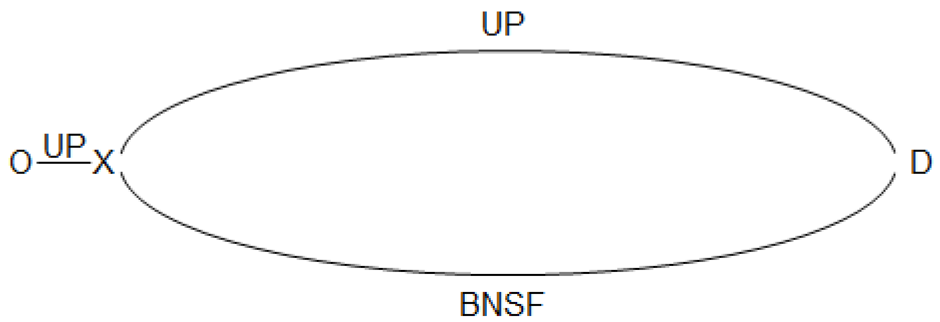


Figure 1, which is the only scenario the railroads address, converts single-line service to two-carrier service as a result of a reciprocal switch. Shippers are likely to request switching in this circumstance only when the competitive carrier offers other efficiencies to offset the additional handling.

Fig. 2

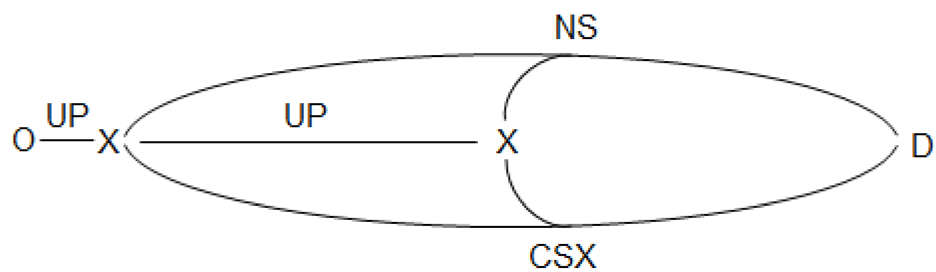
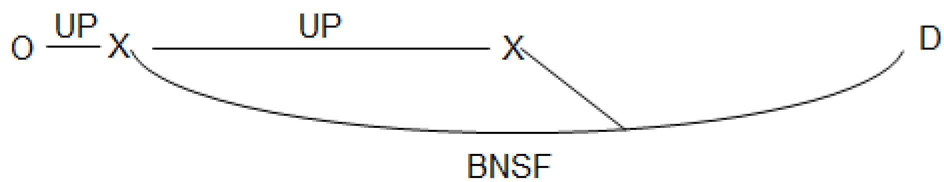


Fig. 3



Figures 2 and 3 reflect more common scenarios where reciprocal switching does not increase the number of interchanges or carriers in the route, but merely changes the interchange location.

- Figure 2 is a movement that occurs on east-west (and vice-versa) gateway movements where the origin carrier achieves its long-haul by handling the traffic in the north-south direction (and vice versa) for the longest distance that is practical before interchanging to the east-west carrier.
- Figure 3 is common in the west between BNSF and UP, in the east between NS and CSX; and along the Mississippi River between BNSF, UP, CN and KCS.
- In both Figures, reciprocal switching allows the destination railroads that participate in the route to claim a longer haul when they can be more efficient, without any additional handling.

EP 711 Ex Parte Meetings: Key Messages

1. **Congress intended reciprocal switching to address railroad market power where (1) practical and in the public interest, or (2) necessary to provide competitive rail service. (Op. at 14-16; Reply at 14-17, 37-42)[1]**

2. **There is a strong need for reciprocal switching to address the exercise of railroad market power over captive shippers (Op. at 5-14; Reply at 19-37, 55-67).**

3. **Reciprocal Switching is Deregulatory (Reply at 55-60).**

   a. Reciprocal switching is not "artificial" competition created through reregulation, but a statutory tool to prevent carriers from foreclosing competition that otherwise exists on large portions of routes beyond a short distance bottleneck segment.

   b. Competition would limit the need for rate regulation to the shortest captive distances.

4. **Operational impacts are greatly exaggerated (Reply at 60-61, 96-116).**

   a. Railroads have created "worst case" scenarios and misrepresented them as typical.

      i. There will be zero operating impacts when the incumbent retains the traffic.

      ii. Reciprocal switching does not impose additional operating steps on the incumbent when it occurs at an existing interchange.

      iii. Case-by-case approach allows STB to deny switching in the "worst case" circumstances posited by the railroads.

   b. Operating plans are not static, inflexible, plans as portrayed by the railroads.

5. **Competition does not discourage investment (Reply at 116-22).**

   a. Competition will spur investment by creating powerful incentives for each railroad to attract and retain competitive traffic, whereas the incumbent otherwise would have little need to make such investments to retain captive traffic.

   b. Railroads have made extensive investments in highly-competitive traffic, including in areas with large concentrations of reciprocal switching.

6. **Including lost contribution (i.e. "Efficient Component Pricing") in the switch fee would nullify the benefits of reciprocal switching reform (Op. at 53-54; Reply at 131-33).**

7. **The Board has ample information to act on reciprocal switching.**

8. **Case-by-case approach enables the Board to consider cumulative impacts (Op. at 20-23; Reply at 86-89).**

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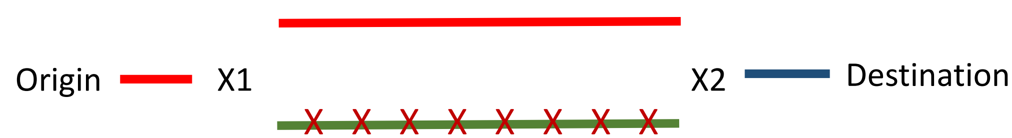

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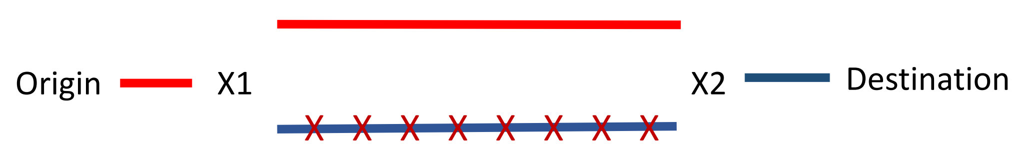

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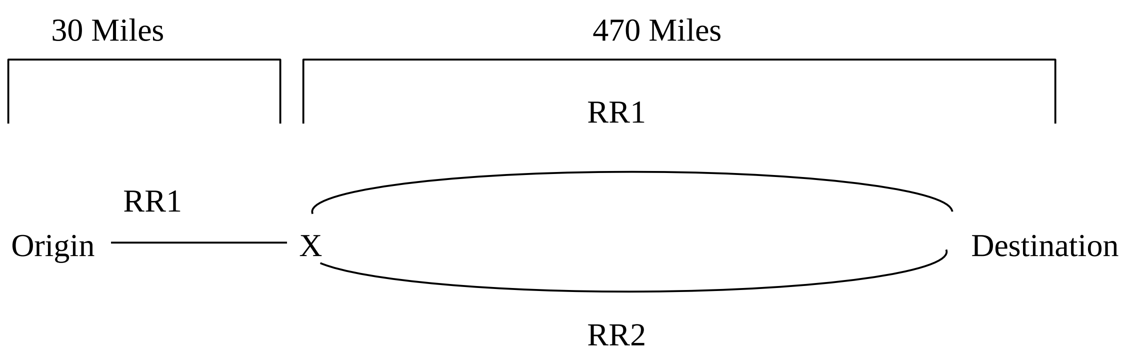

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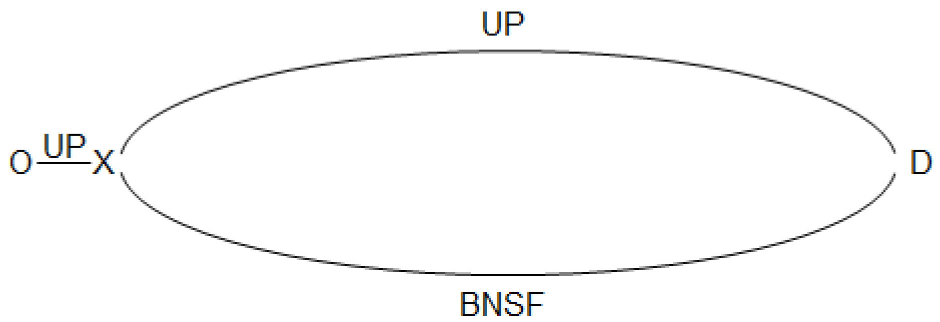

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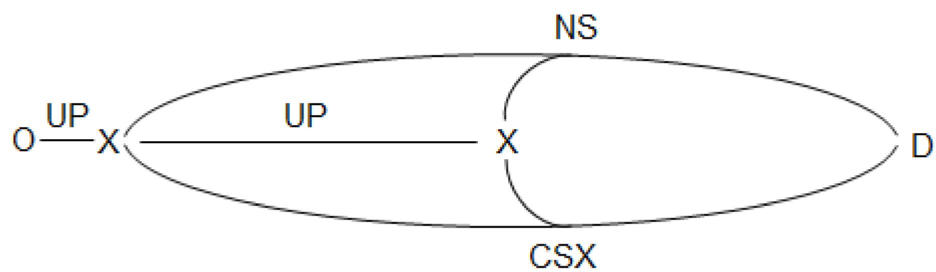

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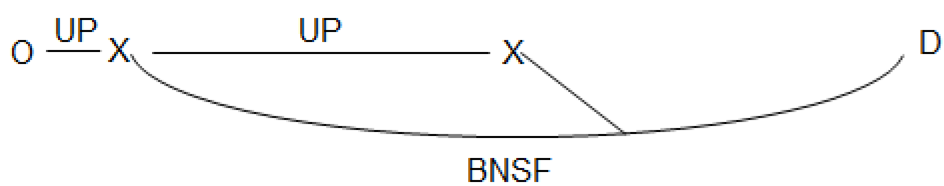

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