A Recent History of North Dakota Grain Transportation Rates

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by

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Good Morning,

Since I anticipate my colleagues would cover the subject of Shuttle trains, I will only give that subject a brief spot in this presentation and instead will address other railroad issues as I see them. I have been attending this convention for almost 30 years now. More often than not there is always a controversial rail issue which need to be discussed or debated as the case may be, and this year is no different. We are coming out of one of the most complicated 3 month periods I can remember as it relates to car supply. It is important we understand what did or did not happen and I will address this issue. First let me say a few words about our company.

Although the Red River Valley & Western has been in business for over 10 years now there may be some of you who are not familiar with the RRVW. We serve central and southeastern North Dakota, as well as Hecla, South Dakota and Breckenridge Minnesota. Our main operating yard is also located in Breckenridge where most of our traffic is interchanged with BNSF. We also operate trains out of Carrington, and interchange cars with BNSF from this central region at both Jamestown and New Rockford.

The RRV&W has become a successful operation through improved service, customer contact, and new business recruitment. In fact, traffic has grown from 19,000 cars to over 30,000 cars over our 10 year history. Besides the 60 grain elevators on our lines, we serve Minn-Dak's Sugar Plant and Cargill's Wet Corn Milling plant at Wahpeton, Melroe's Bobcat manufacturing facility at Gwinner, the Dakota Growers Pasta plant and soon the AgriGrow Oils processing plants in Carrington along with many smaller industries.

As our economy becomes more and more global in nature, dependable and consistent rail service becomes more and more important. Recently the USDA and the Senate Commerce Committee held hearings in North Dakota, which highlighted some of the controversy surrounding rail issues of today. These hearings have reminded me of a number of issues we have been through in the past few decades that also have been controversial and have had government involvement or litigation.

Since I am one of only few railroaders left involved in grain issues over the last 30 years lets look at some of the history to show some of the issues we have dealt with over the past few decades and how they have been resolved.

1. In the 1960s many of you may remember the **inverse rate structure** that was put into effect by the railroads on wheat shipments to the Pacific Northwest. The wheat rate from Fargo to the West Coast was 70 cents per cwt., and the rate from Williston to the Coast was about a dollar per cwt., even though Williston is about 400 miles closer. The purpose of the inverse rates was to ensure that the West Coast markets were competitive with the Minneapolis market. These rates were not popular, and were greatly contested by North Dakota and the Minneapolis grain interests, but they served their purpose in helping to establish a market for spring wheat on the PNW. In the 1970s, the inverse in the rates was removed and the PNW remains an important market for your wheat today.
2. Another issue in 1960s and 70s was the barley rates from N.D. Barley rates to Minneapolis were the highest in the U.S. on a per mile basis because there was no effective truck competition to maltsters. At that

time, malsters only took barley by rail. The issue was litigated before the ICC and the ICC determined that the rates were legal. When malsters and country shippers were able to agree on grade and quality issues, trucks became an option and the rates dropped dramatically, as has the production of barley. It makes one wonder if the higher rates were better.

3. In 1972 we established the **10-hour loading rate** whereby country elevators had to load and provide billing instructions to a specific destination elevator within 10 daylight hours. No demurrage applied to these rates; if the shipper exceeded 10 hours, the shipment just reverted back to the higher tariff rate, which was about a $200-300 penalty. Shippers and receivers said they couldn't market grain without a sample and grades and therefore these rates would never be used. The day these rates went into effect and from then on they were the only rates used. These rates were also litigated, and subsequently deemed lawful by the ICC. The rates eventually disappeared in the early 1980s when exports declined and car supply was not an annual problem. Now as car supply becomes a major issue, 24 hour demurrage was implemented, and this is now an issue.

4. In the 1970s the U.S. sold huge volumes of **grain to the Soviet Union** – volumes far beyond the capabilities that the railroads and the entire transportation system could handle, so car shortages were the order of the day. The Burlington Northern had the equivalent of a harvest movement on a 12 month basis from every state we served to three export areas in

addition to domestic business. We established a car allocation system based on historical loadings of each country elevator, and elevators were allocated cars relative to your past shipping history. While this didn't satisfy anyone, at least we had a rational reason which was difficult to argue with. A system similar to this has been in effect on RRVW since start-up. While no one receives all the cars they want when demand is high, it is an equitable system. Everyone gets some cars according to their rail shipment history.

5. As we at the BN entered the 1980s we were not happy about the tranquility in North Dakota, so we had to look around for another controversy. To keep the pot boiling we published the **unit train rates** for wheat in Montana wheat in late 1980 and from North Dakota in early 1981. At the time no one liked the idea of unit train shipments from North Dakota, and were convinced that they were bad for country elevators and farmers, and only good for the railroads. Now, unit train shipments are common and accepted as part of an efficient grain transportation system. I might add that in 1987 when RRVW began its operation, about 30 percent of our grain moved in units; today about 75 percent is shipped in unit trains. Today no one thinks anything of it, but in 1980-81, it was a very big deal.

6. Perhaps the most highly charged issue in my recollection has been the **branch line rationalization** program put forth by the BN in the 1980s. I personally had the good fortune of being the BN representative who was to

bring this news to North Dakota and the rest of BN as well. I was able to meet many fine people in many fine communities. To this day Steve thinks branch line rationalization and branch line abandonment are synonymous. This issue generated more controversy, more meetings, more arguments, and more letters and tons of newspaper clippings than any other program in BN's history and North Dakota led the way. But the system that remains in North Dakota is stronger, and many elevators have been able to grow stronger financially and provide much better service to their customers than if this rationalization had not occurred.

7. In 1988 the BN introduced its **COT program**, which also generated a lot of heat in North Dakota. Many shippers opposed this program; in fact this was also litigated before the ICC. By the time the ICC decision came, much of the animosity toward the program had gone away, people became more comfortable with the program, and today the program is widely used. I believe the COT program is a valuable tool for both BNSF and for shippers in North Dakota. BNSF has since added the **SWAP or Guaranteed Freight program**. The SWAP program in my opinion hasn't added much value to anyone, certainly in the last 2 years, and in fact has caused more problems than it is worth.

Enough about the past and let's look at today's issues. It seems that each year something happens in our grain system that creates a new crisis and pits shippers against the railroad, and renews old ideas of re-regulation or some other governmental action. This brings me to **the car allocation system**. Car allocation was the primary reason for the controversy this fall and winter and was the reason the USDA and Senator Dorgan held hearings. Shippers felt forced to buy cars from the COT and SWAP programs this year because there was expectations that no tariff cars would be available. This was exactly the case, BNSF filled COT orders first and I might add with difficulty and ended up paying big bucks in SWAP defaults. The interesting part of this was the demand for wheat was very soft, corn demand was also soft but corn needed a home because of a big crop so this created a supply push situation. Only soybeans wanted to move because of price. Elevators owning COTS were forced to ship when holding their wheat would have been more economical. Corn shippers, on the other hand, who had their shipping needs covered with SWAPS could not get cars. This entire fiasco might have been avoided by limiting the number of cars which are put into COTS and SWAPS, and by a tariff ordering system which allocated cars based on historical loadings. Cars would have been allocated by the market (supply & demand) rather than some being forced on customers who really don't want them. This is an area the association has discussed at great length and is hoping to have an input into this with the railroads. This would be a good start at mending relationships.

One of the newest issues facing North Dakota is the concept of the shuttle train. These trains have already been in use in corn and soybean country for over two years. This program requires a shipper to load 110 cars of corn or beans in 15 hours, with some other efficiency measures required as well. Incentives are granted to both the origin and destination for meeting the strict loading and unloading requirements. I can tell you that for corn and beans anyway, the shuttle train program will continue to grow while the jury is still out for wheat and other commodities. The economics for shuttle trains are so compelling, so strong, that shuttles will be with us as a part of our system for a long time. The speed with which they move gives BNSF far improved cycle times, reduces the amount of capital BNSF must spend for cars and locomotives, reduces the congestion along their lines, and creates additional capacity for other commodities as well as grains. Bigger trains obviously work on a more homogenous product like corn. Wheat is more quality-differentiated, and indications are that it will continue to move in that direction. It would take an exceptional crop like 1992 where volumes were huge and quality was consistent, before wheat could be a good shuttle train candidate. RRVW does expect to be a participant in the shuttle program as we serve the corn and soybean producing region of North Dakota. Today RRVW originates 60% of the rail corn and soybeans in North Dakota. RRVW origins are the closest to the PNW export houses of any corn originating area. Therefore the economics are the strongest for BNSF from the RRVW. We have had a number of discussions with BNSF and as to our participation in the shuttle train program and are hoping to finalize this shortly.

One program that has been proven to work on the Red River Valley & Western is the concept of **multiple origin loading**. The RRVW has been using multiple origin loading for corn and soybean trains for 7 years now, and the program is an unqualified success. This program is used heavily by RRVW customers both in years where corn is plentiful and in years when corn is short. Many unit train shippers and BNSF have opposed the multiple origin concept because they feel investments in unit train facilities must be protected. The shuttle train program has already thwarted this philosophy. The history of co-loading on RRVW proves that unit shippers like multiple origin loading. On the RRVW, over 80 percent of the corn shipped in unit trains is co-loaded from at least two stations. And over 80 percent of this is from shippers who can load unit trains themselves. Because North Dakota stands out as unique with its variety of crops produced it is difficult for elevators to handle all the grains grown in their area so loading units with other shippers makes sense. This state ranks first in production of spring wheat, durum, barley, flax, dry edible beans, and sunflower, and produces many other crops as well. This diversification, less productive acres per section, lower yields and specialty crop production has always run against the strict unit train philosophy here, it strongly suggests usage of the multiple origin loading concept. I just don't believe that you can apply the philosophy of "one size fits all", in a state like North Dakota where the commodity mix and specialty crop nature of even our biggest crop, spring wheat, makes the marketing and transportation needs completely different than the corn and bean only producing areas.

The final issue I want to address is the proposal being forwarded called **competitive access**. Competitive access is a system whereby a railroad would be forced to let another railroad use its track and facilities to come in and serve its customers. Now, I acknowledge the fact that the North Dakota Public Service Commission and the ND Grain Dealers Association have both joined the Alliance for Rail Competition, which is the group proposing competitive access nationally. People supporting competitive access claim that this is necessary to promote competition in areas where shippers are served by only one railroad. They compare the railroad industry to the public utilities such as the electrical and telecommunications industry. In the electrical industry for example a user of electricity will have the option to buy power from a different supplier, and the existing company would be paid full costs to "transport" that power to the customer. These people feel that the same principle applies to the railroad industry, where a railroad should be forced to allow another railroad to come on our track to serve our customers. However it is impossible to directly compare the utilities industries to the railroads. Public utilities were created as publicly-enforced monopolies with a guaranteed customer base and a guaranteed return on their investment. Railroads were never publicly protected, and have certainly never been guaranteed a return on their investment. Electrical companies move kilowatts. Whether those kilowatts are going to a grain elevator, a sugar plant, or a manufacturing plant, they all look the same. This is far different from a railroad, where some trains move slow, some fast, some are long and some are short, some have covered hoppers, some open top hoppers, some flatcars, and so on. It does make a difference when you run a specific train and where you set out a specific car. We cannot just set out the first 10 cars in a train to any customers. The competitive access proposals being floated today would be a financial disaster to the railroad industry. Investment in locomotives and cars would decline. Track quality, which is now being improved at a rate faster than any time I can remember, would fall into disrepair similar to the 1960s and 1970s for lack of investment capital. The way we have improved our collective well being in transportation is through these types of forums of negotiation and joint problem solving, not through re-regulation. In fact, the improvement in rail capacity and our entire logistics system can be very directly attributed to the **removal** of stifling regulations 20 years ago, **not** by getting the government **more** involved in our businesses.

There is no industry that couldn't stand improvement including the rail industry. But competitive access is not the way, in fact it would do just the opposite. I hope North Dakota's joining the Alliance for Rail Competition is more out of frustration or inability to get Class 1 railroads to address issues important to North Dakota, and not a firm belief that competitive access is really an answer. I enjoyed being here today to share my thoughts and thank you for your attention.