

**Surface Transportation
Ex Parte No. 705 - Rail Competition Hearing
Oral Testimony of Wayne Hurst, NAWG President
June 22, 2011**

Chairman Elliot, Mr. Mulvey and Ms. Begemen, Members of this Board, my name is Wayne Hurst. I am a wheat, sugar beet and barley grower from the Burley, Idaho, area. I currently serve as president of the National Association of Wheat Growers (NAWG) and have served in the past as an officer of the Idaho Grain Producers Association Board.

I am honored and pleased to be here today on behalf of the National Association of Wheat Growers and farmers across the country. NAWG is a federation of 21 state wheat grower organizations that work to represent the needs and interests of wheat producers before Congress and federal agencies. We are grower-governed and grower-funded, and we work in areas as diverse as federal farm policy, trade, environmental regulation, research and, like today, transportation.

Members of the Board **railroads are vital to agricultural production and the value chain.** They are extremely important to us, and in my experience, the people who run them are good, smart, hard-working Americans, much like American farmers. In fact, many of those I have worked with over the years have farm backgrounds. But those facts do not take away from the reality that there are billions of dollars to be made each year in the railroad business, and the pressure to maximize that profit is real.

Agricultural producers are “price takers” rather than “price makers,” with little control over the price they receive for their products. They are unable to pass cost increases on to customers, and must absorb those costs because of a lack of market power.

In most cases, our grain is priced on the three electronically-traded wheat futures markets here in the U.S. However this is not the price that we as farmers receive because marketing and transportation costs – what we call basis – are then applied. In most cases, this basis is subtracted from the wider set futures price to give the available cash price in the local grain collection point. Increases in transportation costs result in larger basis and therefore lower cash prices available to farmers. For agricultural shippers with no cost-effective alternative to rail, and located far from end-use markets, rail is the only transportation available.

Wheat and grain growers know that an effective railroad system is necessary for the success of the wheat industry. However, they continue to face many problems with rail rates and service. Study after study has shown that with each successive rail merger over the last 30 years there has been a substantial reduction in rail-to-rail competition. Over time, rail customers in the United States have grown more captive to single rail carriers. As captivity levels rise, a larger and larger share of the cost of transportation has been shifted to rail customers and state and local governments. Helping our members find solutions to these freight problems remains one of NAWG’s top priorities.

I will talk today about rates and service, and specifically how rail captivity interacts with these. I will also describe the effect we believe a proactive and empowered STB can have on finding solutions to these problems.

Since the passage of the Staggers Rail Act of 1980, the degree of captivity in many wheat growing regions has increased dramatically, and America’s farmers continue to experience both service issues and ever higher freight rates. We have had continuing rail equipment spot

shortages since the railroads started aggressively consolidating and merging in the early 1990s. We continue to have grain piled on the ground in many states in the late summer and fall due to lack of rail equipment availability.

Twenty years ago, there were multiple transcontinental railroads servicing agricultural regions. Today, however, whole states, whole regions and now whole industries have become completely captive to single railroads as a result of many railroad mergers that were allowed by this agency. At the time, those merging railroads promised greater efficiency and more competition.

In the wheat industry alone there are substantial pockets of captivity in at least 14 states stretching from Texas to the Pacific Northwest that are primarily attributable to the effects of mergers. In these areas the rates are higher and the service levels are not the same as service that is provided in areas where there is rail-to-rail competition.

In October 2007, the Government Accountability Office issued a report, GAO 07-94, *Freight Railroads – Industry Health Has Improved, But Concerns About Competition and Capacity Ought to Be Addressed*, confirming what we in the captive shipper industry have been stating for years: those areas that are captive pay the highest freight rates yet receive some of the worst service.

The Christensen study further confirmed the high freight rates in captive areas. An extensive USDA study further revealed that the GAO correctly established the link between single railroad access and elevated percentage of tonnage above the threshold for rate relief. In our own studies within the grain industry, examining the R/VC levels on rates to common destinations of the Pacific Northwest, we find large areas moving at rates considerably above the threshold, confirming the findings in the GAO study, the Christensen Study and the USDA study.

For most of us, rates remain high. Farmers experience and suspect it, and both government studies and work by independent consultants confirm it.

Lower prices and incomes hinder farmers from borrowing funds to purchase fertilizer, seed and machinery, thus reducing economic prosperity in rural areas. Higher transportation costs also affect the competitive position of U.S. agricultural products in highly competitive export markets. The rates agricultural shippers pay for rail transportation can facilitate or inhibit American competitiveness in world agricultural markets. This point is of particular concern for wheat producers, since about half of the annual U.S. wheat crop is exported each year.

I have come to realize in my meetings and exposure to the railroads that they are under internal and external pressure to maximize profits, because, as monopolies, they can. I have heard division managers speak of expectations within their companies to deliver profits. It's also obvious that their stockholders and lenders expect large returns and have been receiving them. Warren Buffet didn't buy the BNSF because he thought it would be fun to own a railroad! He is very much aware of the power the railroad has in controlling its ability to produce revenue.

When I testified a few years ago before the House Transportation Committee, a few days before the hearing I was out hauling hay, and I got a call from a guy from the Bank of New York, asking me why I was against the ability of the railroads to attract capital. The investment and banking industries play a huge role in this issue, and the excess rates that we farm families pay go directly to those investors, pension funds and bankers. There needs to be a mechanism to protect the captive shipper in this equation, much like a governor on a tractor. I believe that,

within the current system, that mechanism should primarily be a proactive STB.

Farmers are willing and expect to pay their fair share of costs to get our goods to the market, but we in most cases pay far more than we should.

I liken it to shopping for a new pickup truck. Say a truck on the lot is marked at \$30,000. At that price the variable costs are paid (100 percent R/VC), the factory fixed costs are paid (another 30-40 percent R/VC), and the investors receive a return on their investment (40 percent more R/VC). So if the pickup at \$30,000 pays all the labor and other bills, as well as a return, and I have to pay \$50,000 because I have no other choice (about 300+ percent R/VC) which is what most of us in wheat land pay for our freight right now.

On a brighter note, it has been my understanding and experience in recent years that generally speaking, service has improved. The economy has slowed, and railroads have had the capacity to meet service needs. Railroads have gradually realized that many past complaints were service-related and affected the handlers profitability, so they have made moves to mitigate these problems while transferring the extra costs directly to their customer – the farmers.

In other words, improved service with faster delivery times helped the handlers and the farmers, but we – not anyone else - have paid the bills for it. I am very concerned about what will happen to service when the economy becomes more robust and competition for priority service increases.

Agricultural producers truly believe that a healthy and competitive railroad industry is essential for their continued viability on a rapidly developing world market for commodities. However, with continuing service issues and increasing rail rates coupled with a regulatory agency that does not meet the needs of shippers, it is increasingly difficult for agricultural producers to remain competitive.

The proposals outlined by this Board, such as terminal access and bottleneck (rate quotes over segments, paper barriers, etc.) might mark progress in dealing with these specific issues, but they will not solve captivity problems. The distances are too great for these remedies to work.

Farmers believe that both railroads and shippers would be better off with more competition in the marketplace. We fervently believe that a strong, pro-active STB can provide a host of benefits where competition cannot physically be created.

We believe that the STB needs to be the facilitator and the catalyst for increasing competition in this historically strong industry of grain handling. We believe the railroad industry can survive and prosper in a competitive environment and, indeed, we know from history that competition breeds innovation and efficiency.

As a farmer, as a taxpayer and as a shipper, I encourage you to take a proactive role in addressing shipper concerns. I appreciate, again, the opportunity to speak before you today, and I look forward to continued discussion about these important issues.