

LEGISLATIVE and REGULATORY UPDATE

*Midwest Association of
Rail Shippers*

Winter Meeting
January 13-14, 2010

1

DISCLAIMER

- The views and observations expressed herein are solely those of this presenter only and do not represent any official policy or position of the *Midwest Association of Rail Shippers* or the *MARS Executive Committee*.
- However, the world we live in is not a vacuum and things, especially in Washington, D.C., tend to happen for a reason (connecting the dots).

2

Today's Agenda

- Key members of Congress to watch.
- Updates on various legislative activities.
- Brief overview of important STB activities and decisions.

3

It's An Election Year!

- The Second Session of 111th United States Congress convened on 1-5-10.
- 2010 is an election year for the U.S. Congress, as specified in the Constitution.
- All 435 voting seats in the U.S. House of Representatives are up for election.
- One-third of the total seats in the U.S. Senate are up for election.

4

Key Members to Watch

- **Rep. James Oberstar** of Minnesota's Eighth District, now in 18th term, is Chair of the House Transportation & Infrastructure Committee; remains one of the most powerful members of Congress.
- His district includes several large "captive" paper mills as well as the Iron Range and the Port of Duluth.
- As the largest committee of Congress (75 members) the T&I Committee's #1 challenge will be writing a new surface transportation authorization bill.

5

Trust Fund Troubles

- For the second year in a row in Summer 2009 the Highway Trust Fund approached insolvency.
- No increase in Federal gas tax since 1993 = 33% loss in purchasing power over 15 years.
- In August 2009 Trust Fund received \$7 billion "loan" from General Fund.

6

Reauthorization Activity

- Then the current Federal highway and transit program authorization expired on 9-30-09 at the end of the current fiscal year.
- Surface transportation authorizations cover a 6-year period; last one SAFETEA-LU finally passed in 2005, two years past prior bill's expiration date.
- Since SAFETEA-LU's expiration in September Congress has passed four short-term extensions; the latest one runs through end of February 2010.

7

Reauthorization Activity

- On 6-18-09 Chairman Oberstar announced the Surface Transportation Authorization Act of 2009, ***Blueprint for Investment and Reform*** (775-page draft).
- Authorizes \$450 billion/year = 38 percent in funding over current levels.
- Proposal includes \$25 billion for Projects of National Significance (like CREATE) plus \$50 billion for 11 high-speed rail routes.

8

Reauthorization Activity

- Oberstar was unable to complete and pass a bill by time the current authorization expired; main issue is how to pay for it.
- Both Senate and Obama Administration favor of an 18 month extension of current authorization for variety of reasons.
- Obama Administration is on record as opposing increase in fuel tax, but American Trucking Associations supports if 100% of increase goes to highway improvements.

9

Key Members to Watch

- **Sen. John D. Rockefeller IV** of West Virginia, now in his 5th term, Chair of the Senate Commerce, Science and Transportation Committee.
- Coal shippers are a major constituency and Rockefeller has actively supported so-called re-regulation efforts for past 25 yrs.
- Sen. Rockefeller and his staff spent most of 2009 preparing legislation that would change/modify current railroad regulation.

10

“The Rockefeller Act”

- The Surface Transportation Board Reauthorization Act of 2009.
- Senate Bill 2889 introduced on 12-17-09 by Senator John D. Rockefeller, Chairman, Senate Committee on Commerce, Science and Transportation.
- Senate co-sponsors: Ranking Member Hutchinson (TX) plus Lautenberg (NJ), Thune (SD), Dorgan (ND).

11

Committee Press Release

- This bipartisan legislation is the first comprehensive reauthorization of the STB since it was established under the ICC Termination Act of 1995 and the first significant reform of rail competition policy in 30 years.
- “For a quarter of a century I have worked to enact needed rail legislation that would provide real reform and address the shippers’ problems...Act is carefully crafted to address rail-shipper imbalances and strengthen the rail industry.” Sen. Rockefeller

12

A Brief Outline of the Proposed Legislation

Three Primary Sections

13

Increasing Rail Competition

- Requires major railroads to quote “bottleneck rates”.
- Sets standards for “reciprocal switching” and “terminal access” rates, by overturning mid-1980’s “Midtec Paper” ICC/Appeals Court decision.

14

- Allows parties to challenge existing and future “paper barriers”.
- Increases STB scrutiny of future railroad mergers for competitive, service and environmental effects (same level of scrutiny for mergers between Class I and Class II rail carriers as between Class I’s).

15

Strengthening STB Authority to Oversee Railroad Industry

- Updates the Rail Transportation Policy
- Gives the Board independent investigative authority.
- Directs the STB Office of Public Assistance, Governmental Affairs, and Compliance to assist shippers with complaints regarding railroad service and rates.

16

- Creates a Rail Consumer Advocate and STB Ombudsman to help rail customers resolve rail service and rate issues.
- Expands the size of the Board by increasing membership from 3 to 5.

17

Giving Shippers Real and Better Access to the STB

- Allows certain complaints to be resolved through binding arbitration.
- Opens the STB's simplified rate case process to more shippers and larger cases.
- Makes clear that service must be reasonable.

18

- Requires the STB to review current class exemptions for unregulated railroad traffic.
- Sets lower fees for filing complaints at the STB.

19

Keys to Watch For

- How many co-sponsors does the bill receive? Bi-partisan?
- Review by Congressional Budget Office (aka CBO scoring).
- How long for companion legislation to be introduced in House?
- Any comments by former Carter Administration members on original Staggers intent in 1980?

20

Some Relevant Observations

- Proposed legislation appears to make the “activist” STB a permanent fixture, and also clear up recent confusion about exact limits of STB authority and responsibility.
- Binding arbitration has been used on a voluntary basis by carriers and shippers in several recent major rate cases before the STB; approach publicly favored by the current STB Chairman in November 2009 comments at Lipinski Seminar.

21

Some Relevant Observations

- At the TCC September 2009 luncheon former CN Executive VP Jim Foote voiced the opinion that it might be time to “revisit” the Midtec Paper decision.
- Makes the regulatory process much more “user-friendly” for shippers.
- Most of ICC Termination Act of 1995 no longer relevant.

22

Some Relevant Observations

- Unclear how expansion will be paid for.
- Bill authorizes increased STB budget through FY2014, but still needs actual appropriations from different Committee.
- Key part of Clinton Administration's efforts to reduce Federal budget deficit was aggressive reduction in regulatory agency budgets combined with substantially increased user fees; deficit today far worse than 15 years ago.

23

Some Relevant Observations

- **The clock is ticking.**
- Legislation must be passed by both Houses, and signed by the President, by end of the 111th Congress a year from now.
- If one were a betting man, odds are slightly better than even bill gets through the Senate but no sign of a companion bill in the House yet.

24

Infrastructure – Class II and III

- Previous Shortline railroad tax credit was finally extended by 110th Congress on October 3, 2008; that extension subsequently expired on 12-31-09.
- “When bad things happen to good people (or good legislation)”; caught in the health care legislative crossfire.

25

Infrastructure

- EXTENSION OF THE SECTION 45G RAILROAD TRACK MAINTENANCE CREDIT.
- Would increase the allowable amount for the railroad track maintenance tax credit.
- Revise types of expenditures eligible for such credit.
- Extend such credit through 2012.

26

Infrastructure

- H.R. 1132, introduced by Rep. Pomeroy of N.D., with **247** co-sponsors, on 2-23-09 and still in the House Ways & Means Committee.
- S. 461, introduced by Senator Lincoln of Arkansas (Reilly?), with **52** co-sponsors, on 2-24-09 and still in Senate Finance Committee.

27

Infrastructure – Class I's

- ***The Freight Rail Infrastructure Capacity Expansion Act*** (25% tax credit for Class One's) died in respective House and Senate Committees during 110th.
- Similar bill, H.R. 272, re-introduced by Rep. Kendrick Meek (FL) in House Ways & Means Committee in January 2009; still in Committee.

28

Infrastructure

- H.R. 1806, Freight Rail Infrastructure Capacity Expansion Act of 2009, introduced by Rep. Meek on 3-31-09.
- So far 34 co-sponsors, bill still in House Ways & Means, no companion Senate bill.
- Moves expiration date from 2012 out to 2015, and adds Davis-Bacon requirements in Section 4 of bill.

29

Infrastructure

- Estimated cost/value at \$300 million per year for life of bill up to 2015.
- *This one has support of AAR.*
- Mr. Moorman testified before Ways & Means on behalf of AAR on 7-23-09.

30

Economic Regulation

- ***Railroad Antitrust Enforcement Act of 2007*** made it out of Senate and House Committees but never came up for full vote in either Chamber.
- Sen. Herb Kohl of Wisconsin reintroduced new version of this bill S.146, on 1-6-09, with 13 co-sponsors.
- Rep. Tammy Baldwin of Wisconsin introduced companion legislation H.R. 233, on 1-7-09, with 19 co-sponsors.

31

Economic Regulation

- S. 146 was scheduled for full Senate vote but in a classic demonstration of political power bill was pulled at last minute on May 21, 2009 by sponsor Kohl at request of Sen. Rockefeller.
- All parties agreed they wanted "comprehensive" regulation reform legislation not piecemeal and possibly conflicting legislation.
- House bill is still in Committee.

32

Economic Regulation

- However, these anti-trust provisions are not in current version of the Rockefeller regulation bill; he publicly admits doesn't have the votes yet to get this provision through the full Senate.
- "I will continue to work with Senator Kohl and other members to add antitrust reforms to our bill as it moves to the floor." Sen. Rockefeller in 12-17-09 Press Release.

33

Economic Regulation

- Remains to be seen what happens to both Kohl and Baldwin bills since they do not expire until the end of the 111th Congress, and could still be brought up to the Floor for votes.

34

The Gift That Keep's on Giving

- H.R. 3410, *Taking Responsibility for Community Safety Act (TRAC)*.
- Introduced in House on 7-30-09, by Rep. Melissa Bean (IL-8), with 17 co-sponsors, including Representatives Biggert (IL-13), Foster (IL-14), Halvorson (IL-11), Manzullo (IL-16), Roskam (IL-6) and Visclosky (IN-1)
- *Déjà vu all over again?*

35

And Giving and Giving

- "To require Surface Transportation Board consideration of the impacts of certain railroad transactions on local communities."
- Bill is still in the House Subcommittee on Railroads, Pipelines and Hazardous Materials.
- No companion Senate bill to-date.

36

Connecting the Dots

- Any resemblance here to main opposition group of a certain recent railroad merger case, also called **TRAC**, is purely (you-fill-in-the-blank).
- Coincidentally, Ms. Bean and her family have lived in Barrington, Illinois for 19 years, very close to a certain set of railroad tracks some in this room may be familiar with.

37

Here We Go Again

- This is the recycled version of HR 6707, introduced in 2008 during the CN-EJ&E acquisition case, and narrowly defeated on a procedural vote in September 2008.
- It would place transactions involving only one large railroad and smaller railroads (Class 2 and 3) under the same standard now applicable for merger of two or more large railroads.

38

The Details

- Bill would also amend existing standard to specifically include certain safety and community impacts, along with effects on passenger transportation, as mandatory criteria for analysis.
- Bill would effectively make railroad mergers an open ended process again and return us to the “*good old days*” of 1974, when ICC took 10 years to issue a final decision in the UP-Rock Island transaction.

39

Congressional Budget Office Said

- H.R. 6707 would impose a private-sector mandate.
- “Because of new standards railroads could be prohibited from engaging in certain transactions that would otherwise be allowed.”
- “It is also uncertain the extent to which railroads would have to forgo business opportunities or what the value of those lost opportunities would be.”
- *Also require additional 10 STB employees and \$2 million per year to implement.*

40

Impartial Assessment

- Congressional testimony by *Dr. Joseph Schwieterman, Director Chaddick Institute, DePaul University, Chicago.*
- *No other transportation mode providing intercity service in the U.S. is subject to the kind of criteria established in HR 6707.*
- *Act risks shifting the responsibility for solving some of the problems of rail transportation from their roots – in state and federal policy– to private railroad companies (and **YOU** their customers).*

41

Rail Safety Improvement Act of 2008

- *Railway Age Magazine* called it the “most comprehensive rail safety bill in over 30 years”.
- Requires mandatory installation of Positive Train Control (aka PTC) systems on all Class I rail lines shared by passenger, commuter and freight trains, and on freight-only lines used to transport toxic-by-inhalation materials, by 12-31-15.

42

Reality Check

- FRA estimates PTC will require an investment of \$10-\$14 billion over a 20 year period.
- The \$5 billion that Class Ones will have to spend just to install PTC by 2015 is roughly equal to a full year's worth of rail industry's infrastructure-related capital spending.
- FRA estimates that railroads will incur at least \$15 in PTC costs for each \$1 of PTC benefits (*what's wrong with this picture?*)

43

Reality Check

- **This legislation is essentially an "unfunded mandate".**
- **Where does the money come from?**
- **What other capital investments do NOT get made?**
- ***Who pays the actual costs is unknown at this time (could very well be all of YOU).***

44

Surface Transportation Board

- Currently consists of three Commissioners all of whom are appointed by the President and confirmed by the Senate.
- The Chairman is appointed directly by the President and Vice Chairman is elected by the Board.
- Commissioner Francis Mulvey was designated Acting Chairman by President Obama on March 16, 2009, replacing Charles D. Nottingham who had served as Chairman since August 2006.

45

Surface Transportation Board

- Nottingham's term of office as STB Commissioner expires 12-31-10 (the Republican seat).
- Mulvey, a Democrat, is in his second term expiring in December 2012; at time of first appointment was working for Mr. Oberstar on House T&I Committee staff.

46

Surface Transportation Board

- Dr. Mulvey was in line to become permanent Chairman but appointment was blocked by Senator Durbin of Illinois.
- Reportedly Durbin did not think that Mulvey had been aggressive enough in opposing a certain railroad acquisition case in Durbin's home state.
- Mulvey was designated Vice Chairman on January 5, 2010, in accordance with current STB rules and procedures.

47

Surface Transportation Board

- On July 6, 2009, President Obama announced his intention to nominate Daniel Elliott III as next Surface Transportation Board (STB) chairman.
- Elliott had been Associate General Counsel of the United Transportation Union since 1993.
- Confirmed by Senate on 8-7-09 and sworn in as 5th Chairman on 8-14-09; 5-year Commissioner term expires in December 2013.

48

The Nominee

In his prepared statement nominee Elliott stated that he intended to “be an open-minded fair and impartial decision maker at the STB....I come here with no preconceived notions as to who is right and who is wrong. I believe that I will look at the facts and the laws of each case and handle them in a fair manner.”

49

Public Feedback

“The appointment of Elliott will result in a decided shift from the pro-railroad position that we’ve seen under every STB chairman since Linda Morgan (in 1995) to one of a minimum of neutrality,” and shippers can expect to see “far greater balanced decisions” out of the STB, according to Fritz Kahn, transportation attorney and former ICC chairman.

50

Freight vs. Passenger

- In October 2008 Congress passed the ***Passenger Rail Investment and Improvement Act***.
- This act “enhances” the Board’s role in disputes between freight railroads and Amtrak and others, regarding cost and service aspects of both commuter and intercity rail passenger service.

51

Freight vs. Passenger

- Will STB now become the referee between freight railroads and passenger train supporters for access to limited mainline capacity??
- ***Will rail shippers get caught in the middle?***
- Ex Parte 683 public hearings held in February 2009; proceeding still underway to define STB’s new role.

52

Railroad Revenue Adequacy

- Ex Parte 552 (Sub No. 13), issued 10-26-09.
- Found that only one Class I railroad, Norfolk Southern Railway Company (congrats Wick!), was revenue adequate for 2008; all other Class I railroads found to be revenue inadequate, i.e. not earning their cost of capital.

53

Railroad Cost of Capital

- Ex Parte 558 (Sub No. 12), issued 9-25-09.
- STB determined that railroad industry cost of capital for 2008 was 11.75%.
- Berkshire Hathaway-BNSF deal could alter formula; cost of capital hard to calculate without stock price (equity) information.

54

The Outlook?

- *Is it renaissance, reformation or revolution???*
- *Looks like the renaissance is on indefinite hold if not permanently over; Martin Luther wins for now.*

55

QUESTIONS

- We can arrange to send copies of presentation via email.
- For specific questions or more information contact:
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56