

Testimony

of

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Before the

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Committee on Commerce, Science, and Transportation
Subcommittee on Surface Transportation**

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My name is Claudia L. Howells, and I am the Manager of the Oregon Department of Transportation (ODOT) Rail Division. Thank you for the opportunity to testify today on behalf of the State of Oregon and Oregon producers as the committee addresses new procedures on major railroad consolidations adopted by the Surface Transportation Board.

Role of ODOT Rail Division

Oregon State Law vests the Department of Transportation Rail Division with the responsibility of representing the customers of railroads before the Surface Transportation Board (STB) and other federal agencies. We also are responsible for maintaining a current State Rail Plan, which is an element of the Oregon Transportation Plan. The 2001 update of the Rail Plan, which includes both freight and passenger rail, is in the final stages of the approval process.

Significance of Rail Transportation to Oregon's Economy

Because Oregon's economy continues to be based in great part on agricultural and timber production and because we are distant from major markets, rail transportation is essential to keeping Oregon producers competitive. We are somewhat unusual in having over half of our rail miles under short line management, with sixty per cent of rail-served industries served by those short lines. The Union Pacific (UP) is by far the dominant Class I carrier, with the Burlington Northern Santa Fe (BNSF) generating only a small percent of the Class I railroad revenue in the state.

Oregon shippers have been significantly affected by all of the recent railroad mergers. The 2001 Oregon Rail Plan includes a survey of Oregon shippers on rail service and their perception of the effects of the recent mergers. While most Oregon shippers consider current rail service to be reasonably good, with the short lines getting most of the credit, only one shipper surveyed has found any benefit from the mergers in terms of service or rates. The best that can be said is that at present, service and rates are comparable to what they were before the mergers.

Comments on STB Merger Rules

We commend the Surface Transportation Board for taking a balanced approach in drafting new procedures governing major rail consolidations. The Board clearly recognizes that the railroad system today is profoundly different than when the Staggers Act, and its regulatory predecessors, were put in place. We will say though what I am sure others will say. These are rules that come too late, and sadly, they will have little effect on the ability of the railroads to survive.

I would suggest that had these rules been in place prior to the merger of the Union Pacific and the Chicago Northwestern, there might have been a more rational, less destructive chain of mergers that began with the merger of the Union Pacific and Chicago Northwestern. Had the new merger rules been in place before the merger of the Southern Pacific and Denver & Rio Grande Western, a stronger railroad might have emerged and been capable of standing on its own. But the rules were not in place because, in my opinion, the last fifty years of public policy decisions on railroads have come only as a result of catastrophic events—like the bankruptcies of the Penn Central, the Rock Island and the Milwaukee Road, and now the service disruptions caused by poorly planned and poorly implemented railroad consolidations.

The Future of the Railroad Industry

I suggest that we must begin to anticipate the challenges facing railroads rather than waiting for the next disaster. Based on what we see in Oregon, I will make the following predictions:

1. Break up of major carriers. I predict that we will see few, if any, major railroad consolidations in the coming years, once the [Kansas City Southern/Canadian National](#) merger is completed. Although it seemed for a time that we were headed for a round of transcontinental mergers, the resulting service disruptions, I suspect, have cooled the interest in the financial community for any more major railroad mergers. I think we will begin to see, soon, spin-offs from these new mega-railroads into small Class I or Class II railroads as the big railroads attempt to jettison the less lucrative, costlier parts of their systems. I also predict that these break ups will prove just as disruptive to shippers, and just as destructive to the overall national transportation system, as the mega-mergers. Without some clear direction now to the STB, the regulatory response will again come too late.
2. Short line consolidation. I also predict that we will see further consolidation of short line holding companies that will result in a new wave of abandonments as they, like the Class I railroads, attempt to keep stockholders and financial analysts happy by dropping less profitable lines. Under current regulatory constructs, short line consolidations are handled as minor transactions, because clearly the competitive issues do not exist, and there is little in the way of statutory direction to look much beyond those issues. The STB needs to address this issue with the same level of attention as it has the issue of Class I railroad mergers.

3. Bankrupt short lines. I also predict that many of the smaller independent short lines will head towards bankruptcy. Absent financial support from either the public, or the connecting Class I, these smaller lines will not be able to bear up under heavier cars. Many of these short lines, having experienced financial losses because of merger related service disruptions, may not ever recover. In Oregon, several short lines are facing serious financial difficulties, for the most part not of their making. The STB should play a greater role in protecting the interests of the smaller railroads, and federal law needs to allow a greater level of participation by shippers and public interests in abandonment proceedings.

4. Passenger use of freight lines. We will see growing pressure to use the freight rail system for passenger and commuter trains. The Oregon Department of Transportation fully supports redeveloping intercity, interurban and commuter rail, which is very much a mission of Oregon's rail program. However, we cannot afford to reduce the capacity of the freight system or in any way adversely affect the profitability of the freight railroads. I believe the STB should take the lead role in balancing the interests of current and future users, both passenger and freight so that the overall system remains solid.

National Rail Policy

Most importantly we need a National Rail Policy that is integrated into the overall transportation policy, and that better balances the interests of all the commercial transportation industries. If we fail in that, then I predict, railroads will continue to engage in risky financial moves, such as mega-mergers, because that is the only way to generate capital. Railroads will continue to reduce system capacity, because Wall Street punishes railroads that make long-term capital investments or retain marginal operations. Railroads will continue to hang on to their "franchise", perhaps irrationally, because it is all they have left. Shippers will be left with an increasingly unstable railroad industry; something no one wants.

What can be done to avoid this? First, the railroads, large and small, need a financial safety net. Second, railroads need to remain under a regulatory agency that has a greater mission than simply mitigating competitive damage. The STB should be given a greater mission to protect railroads as a national resource, which may not always be consistent with the desires of either railroad management or railroad labor or even rail shippers. Third, railroad mergers, acquisitions and abandonments should continue under the jurisdiction of the STB and not be transferred to any other federal agency. Fourth, the missions of the STB and the Federal Railroad Administration need to be complimentary, and these agencies need to work together. Fifth, the STB, the Federal Railroad Administration and the Federal Transit Administration need to establish compatible policies when it comes to the management of the railroad system.

With a clearly stated National Rail Policy and with the STB given an expanded role, we may be able to head off the next major railroad crisis.

Conclusion

Recently, a member of the Oregon Transportation Commission observed something that I do not believe I have ever heard so clearly stated. She began by remarking on the initial investment by the government in building the nation's railroads. She then went on to say that government has all but abandoned the railroads and in so doing has demonstrated a lack of stewardship over a valuable public resource, and over that initial public investment.

Railroads continue to be the best example of a public-private partnership that this nation has ever seen. It is clearly a partnership that needs to be reestablished if indeed we place any value on our nation's rail system. In truth, we as a nation should be grateful every day that the railroads maintain their own infrastructure, run their trains every day and help keep industries all over the country in business without costing the taxpayer a dime. We must remember that rail is not an alternative mode. It is an essential part of our transportation system, and if not in private hands, would by necessity become the responsibility of the public. In short, railroads most assuredly need to act in the public interest, but in return the public interest needs to support the railroads.

While I may believe that the STB's rules came too late, I also believe that the quality of the new rules indicate an agency that understands the industry and also understands its responsibility to shippers and the public.

Thank you again for the opportunity to testify before the subcommittee today.

Respectfully submitted by

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