

**TESTIMONY OF PATRICK J. OTTENSMEYER  
PRESIDENT AND CHIEF EXECUTIVE OFFICER  
KANSAS CITY SOUTHERN**

**BEFORE THE  
U.S. SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION  
SUBCOMMITTEE ON SURFACE TRANSPORTATION AND  
MERCHANT MARINE INFRASTRUCTURE, SAFETY, AND SECURITY**

**HEARING ON INTERMODAL AND INTERDEPENDENT: THE FAST ACT, THE  
ECONOMY, AND OUR NATION'S TRANSPORTATION SYSTEM**

**JULY 12, 2016**

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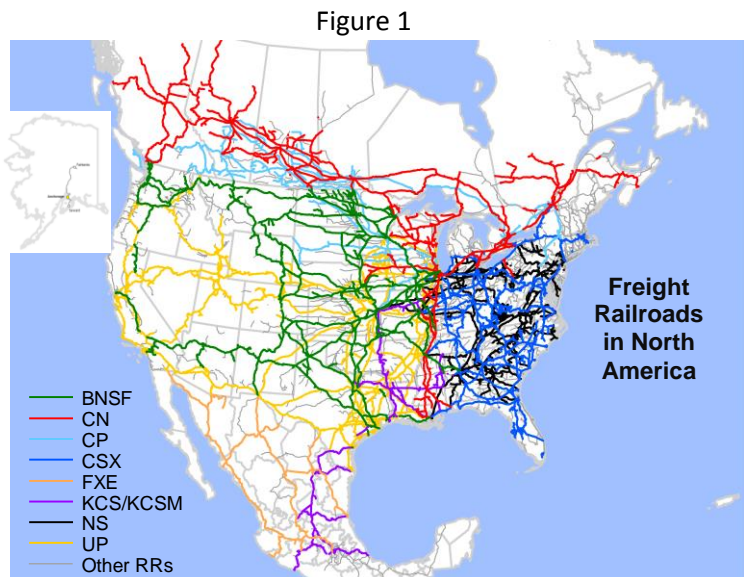
Thank you for the opportunity to appear before you today. I'm here on behalf of Kansas City Southern, but much of my testimony is applicable to U.S. freight railroads in general. I suspect that my counterparts at other railroads would agree with all or most of what follows.

Kansas City Southern has two primary subsidiaries. The first, Kansas City Southern Railway Company, is one of seven large "Class I" railroads operating in the United States. Like the other Class I railroads, we operate in many different states over thousands of miles of track — in our case, on the Gulf Coast and up into the Midwest (see Figure 1). Through our

connections with other railroads, we serve customers located in each of the 49 states that has freight rail service. In this regard, KCS is similar to other major U.S. railroads.

Our second primary subsidiary is Kansas City Southern de México, which is one of two large regional freight railroads in Mexico.

KCS's combined North American network comprises approximately 6,600 route-miles that link commercial and industrial markets in the United States, Canada, and Mexico. KCS is proud to be part of a nearly 140,000-mile U.S. freight rail network and an approximately



180,000-mile integrated North American network. Railroads in Canada, Mexico, and the United States provide the world’s safest, most productive, and most cost-effective freight rail service.

### Railroads Are the Transportation Backbone of America

The benefits associated with freight rail are difficult to overstate:

- A June 2016 study from Towson University’s Regional Economic Studies Institute found that, in 2014 alone, the operations and capital investment of America’s Class I freight railroads supported approximately 1.5 million jobs (1.1 percent of all U.S. workers — nearly nine jobs for every railroad job), nearly \$274 billion in economic output (1.6 percent of total U.S. output), and \$88 billion in wages (1.3 percent of total U.S. wages). Railroads also generated nearly \$33 billion in tax revenues. These impacts include direct, indirect, and induced effects across the U.S. economy. In addition, millions of Americans work in industries that are more competitive thanks to the affordability and productivity of America’s freight railroads.
- Freight railroads expand existing markets and open new ones by connecting producers and consumers across the country and the world. The rail share of intercity ton-miles is in the neighborhood of 40 percent, more than any other transportation mode.
- Coal from Wyoming, wheat from Kansas, cement from Missouri, construction materials from Texas, steel from Pennsylvania — the types of freight railroads carry are almost limitless. In a typical year, KCS and America’s other railroads haul 1.6 million carloads of agricultural products plus another 1.6 million carloads of countless other food products. The approximately 2.2 million carloads of chemicals America’s railroads carry in a typical year help clean our water, fertilize our farms, package our food, build our cars and homes, and protect our health. Railroads haul approximately 70 percent of new cars sold in the United States, and the parts and accessories used to build them. And just about everything you find on a retailer’s shelves may have traveled in a shipping container or truck trailer carried hundreds of miles on an intermodal train.

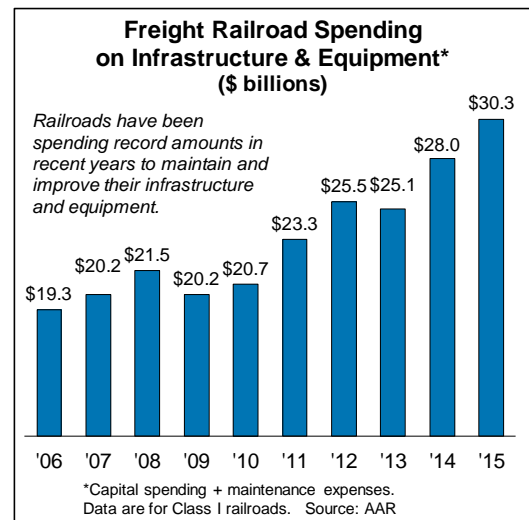
Figure 2



- Railroads’ scale enables efficiency elsewhere in the economy. One railcar of coal, for example, is enough to produce enough electricity for 21 households for a year; one railcar of wheat is enough to produce some 258,000 loaves of bread; one railcar of corn is enough to provide the lifetime corn requirements of 37,000 chickens; and one railcar of ammonia fertilizer is enough for 770 acres of grain. By enabling their customers to take advantage of their own economies of scale, railroads promote lower cost production and distribution while enhancing economic growth throughout the economy.

- Unlike trucks, airlines, and barges, which operate on highways, airways, and waterways financed mainly by taxpayers, KCS and America’s other freight railroads are privately owned and operate overwhelmingly on infra-structure they own, build, maintain, and pay for themselves.<sup>1</sup> From 1980 to 2015, they spent more than \$600 billion — their own funds, not taxpayer funds — on capital spending and maintenance expenses related to locomotives, freight cars, tracks, bridges, and other infrastructure and equipment. That’s more than 40 cents out of each revenue dollar. Freight railroads have been spending more in recent years than ever before — including \$28 billion in 2014 and \$30 billion in 2015 — to keep our economy moving.<sup>2</sup>

Figure 3



- Railroads are, on average, four times more fuel efficient than trucks. That means that moving freight by rail helps our environment by reducing energy consumption, pollution, and greenhouse gases. And because a single train can carry the freight of several hundred trucks, railroads cut highway gridlock and reduce the high costs of highway construction and maintenance.
- Thanks to competitive rail rates — 45 percent lower, on average, in 2015 than in 1980 (when Congress largely deregulated the railroad industry) — freight railroads save consumers billions of dollars every year, making U.S. goods more competitive here and abroad while improving our standard of living.
- The approximately 170,000 freight railroad employees are among America’s most highly paid workers. In 2014, the average U.S. Class I freight railroad employee earned wages of \$86,200 and fringe benefits of \$33,400, for total average compensation of \$119,600. By contrast, the average wage per full-time U.S. employee in 2014 was \$57,100 (66 percent of the comparable rail figure) and average total compensation was \$70,700 (just 59 percent of the rail figure).

<sup>1</sup> Unlike other freight transportation modes, railroads pay substantial property taxes on their infrastructure — Class I railroads paid more than \$1.1 billion in 2015 alone in property and use taxes to localities across the country. A few small railroads are owned by various government entities such as ports or economic development authorities. The Alaska Railroad is owned by the state of Alaska.

<sup>2</sup> To put the \$30 billion that U.S. Class I railroads spent in 2015 on their infrastructure and equipment in perspective, it’s approximately equal to the combined salaries and prize money for all U.S. professional athletes for two years.

- Railroads are safe and getting safer. The train accident rate in 2015 was down 78 percent from 1980 and down 38 percent from 2000; the employee injury rate in 2015 was down 84 percent from 1980 and down 47 percent from 2000; and the grade crossing collision rate in 2015 was down 81 percent from 1980 and down 42 percent from 2000 (see Figure 4). By all of these measures, recent years have been the safest in rail history. Railroads today have lower employee injury rates than most other major industries, including trucking, inland water transportation, airlines, agriculture, mining, manufacturing, and construction — even lower than food stores (see Figure 5).

Figure 4

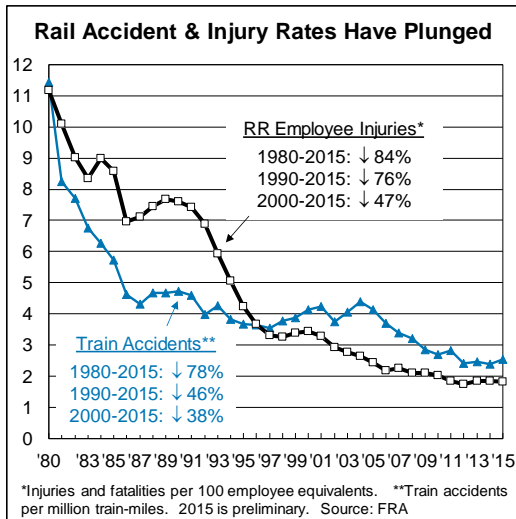
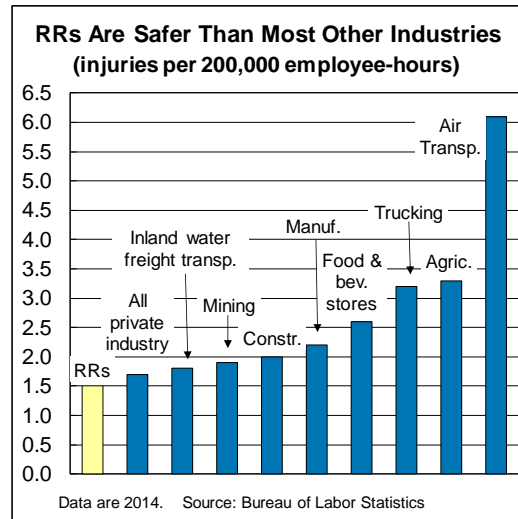


Figure 5



### Railroads and the FAST Act

On December 5, 2015, President Obama signed the Fixing America's Surface Transportation Act, commonly known as the FAST Act. The Fast Act is the first federal law in more than a decade to provide long-term funding certainty for surface transportation infrastructure planning and investment. Members of this committee were instrumental in the development and ultimate passage of this crucial legislation, and I thank and congratulate you for your efforts.

The FAST Act includes a number of provisions that are important to railroads and for which members of this committee deserve special thanks. I describe five of them below.

First, major rail expansion projects today generally must undergo comprehensive local, state, and/or federal environmental and historical preservation reviews before necessary permits

are issued. Railroads recognize the public interest benefits of a reasonable review process. However, the excessive length, scope, and cost of these reviews have often led to years-long delays for exceedingly worthy projects whose benefits vastly exceed their costs. In some cases, projects have been cancelled outright because of the time and expense involved. When reviews take too long, the substantial benefits the projects would provide to rail customers and to our economy are delayed or lost entirely too. The FAST Act, though, includes several useful provisions designed to shorten the time it takes for reviews of rail expansion projects in ways that do not adversely affect the quality of those reviews.

Second, on May 8, 2015, the U.S. Department of Transportation (DOT) released a final rule setting forth new, tougher standards for tank cars carrying certain hazardous materials, including crude oil. The new standards are known as “DOT-117” specifications. KCS and other railroads had long been advocating for tougher tank car standards, so we were pleased with many aspects of the new rules. However, while a good start, the DOT-117 specifications were not stringent enough in certain areas, and we commend policymakers for including provisions in the FAST Act that address these shortcomings. Specifically, the FAST Act goes beyond the May 2015 rules by requiring increased thermal blanket protection for tank cars, restricting the use of older tank cars moving flammable liquids, and requiring top fittings protection on tank car retrofits. Railroads work very hard every day to prevent accidents from occurring in the first place, but these enhancements will mitigate the consequences of accidents should they occur.

Third, the May 8, 2015 DOT tank car rules mandated the use of a technology called electronically controlled pneumatic (ECP) brakes in certain trains carrying hazardous materials. Unfortunately, unlike the tank car enhancements discussed above, widespread use of ECP brakes

would not provide a meaningful safety benefit compared to existing braking systems.<sup>3</sup> ECP brakes would, however, present serious and unnecessary operational challenges and would substantially impair the fluidity of the rail network. Put another way, ECP brakes would entail very large costs for very small benefits. The DOT's Federal Railroad Administration (FRA) has itself stated that the use of ECP brakes is not justified. In addition, several U.S. railroads have experimented with using ECP brakes in recent years, but none of them has been able to justify regular use. In fact, nowhere in the world are ECP brakes used under conditions similar to what the May 2015 requirements would mandate for U.S. railroads.

The FAST Act includes a provision asking the Government Accountability Office and the National Academy of Sciences to conduct an independent evidence-based evaluation of ECP brake systems, due in the summer of 2017. The



DOT has until December 4, 2017, to publish a determination that the ECP mandate either is justified or should be repealed. KCS and, I'm sure, other railroads will cooperate fully with these inquiries.

The approach to rail safety used by the FAST Act in the ECP brakes example — i.e., ensure that railroad safety oversight is fact-based, rather than based on perceptions that upon closer inspection may not be well founded — deserves much wider application.

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<sup>3</sup> ECP brakes issue electronic signals to simultaneously apply and release brakes throughout the length of a train instead of each car applying brakes individually. Alternative braking systems use distributed power (locomotives located in places other than the front of a train), as well as end-of-train devices (EOTs) that allow brakes to be applied from the head of the train and locations farther back in the train, to stop the train quickly.

Fourth, the FAST Act is the first time in which passenger rail programs have been included in a comprehensive federal surface transportation bill. Freight railroads agree that passenger railroading can play a key role in alleviating highway and airport congestion, decreasing dependence on foreign oil, reducing pollution, and enhancing mobility and safety. I am confident that passenger rail-related provisions of the FAST Act will enhance passenger railroading in this country. Members of this committee deserve our thanks for that.

Fifth, Section 1116 of the FAST Act establishes a “National Highway Freight Program” that will fund projects designed to improve freight mobility on the highways and connectors to freight facilities, intermodal rail facilities, and ports. This program recognizes that freight transportation providers, including railroads, do not exist in a vacuum. Rather, they are part of an integrated and interdependent system that is only as strong as its weakest link. This freight program will help strengthen weak links in our transportation networks, especially those associated with the interface between trucks, railroads, and waterways. By doing so, firms and consumers throughout the country will benefit from improved efficiency and more reliable and resilient freight transportation networks.

This committee also deserves our thanks for something they chose not to include in the FAST Act: changes in existing federal truck weight limits. Heavier trucks would mean higher taxpayer costs to repair damage to our highways and bridges; more highway gridlock; and more harm to the environment. The taxes and fees that heavy trucks pay are already far less than the cost of the damage heavy trucks cause. This multi-billion dollar annual underpayment — which other motorists and the general public have to make up for through higher taxes — would become even greater if truck size and weight limits were increased. Congress’s decision not to change existing federal truck weight limits is consistent with the findings of an April 2016 study



from the U.S. DOT examining the impacts of increasing current federal truck size and weight limits. The DOT study concluded that no changes to federal policy on truck size and weights should be made at this time.

It goes without saying that KCS — and, I’m sure, other freight railroads — are more than willing to work with policymakers at all levels to help ensure that the provisions of the FAST Act discussed above, as well as other provisions related to railroads, are implemented in ways that lead to enhanced railroad safety and an enhanced ability for railroads to meet the transportation demands of our nation.

### **Challenges Facing Freight Railroads**

I would be remiss if I did not discuss some of the challenges railroads are currently facing because of the state of the economy and other factors.

Freight railroads are what economists call a “derived demand” industry, meaning that demand for rail service is a function of demand elsewhere in the economy for the products railroads haul. For example, KCS transports large amounts of automobiles and auto parts both within the United States and back and forth across the U.S.-Mexico border. Automakers’ demand for service from KCS depends on how many autos consumers are buying. If consumers stop buying cars, automakers stop asking KCS to transport them. Likewise, when consumers are buying a lot of cars, demand for KCS service from automakers rises too.

This means, of course, that rail traffic is affected by general economic conditions, especially conditions on the “tangible” side of the economy — e.g., consumer spending on goods (as opposed to services), international trade in goods, growth or the lack thereof in construction, how well manufacturing and mining are doing, and so on. Figure 6 shows that growth on the “tangible” side of the economy has been negative in recent quarters. Put another way, the sectors

of the economy that generate the vast majority of rail traffic have, in aggregate, been in a recession recently, even if the economy in the broadest sense has not been. In addition, current and growing threats to existing and future trade agreements could significantly worsen economic conditions in the future. Navigating economic forces is always a tremendous challenge for railroads.

A key reason why this is the case is because particular rail submarkets are often heavily influenced by factors specific to those markets.

Today, for example, railroads are suffering from a lack of demand from several key energy-related markets. Coal is the primary example. Due to increasingly restrictive environmental restrictions on the use of coal, as well as significantly cheaper natural gas that makes electricity generated from natural gas much more prevalent than it used to be (see Figure 7), demand for coal — and thus demand for the rail

transportation of coal — is much lower today than it was even a couple of years ago. In the first six months of 2016, carloads of coal on U.S. railroads were down nearly 800,000 carloads (30.4%) from the same period in 2015. This comes on top of a nearly 700,000-carload decline

Figure 6

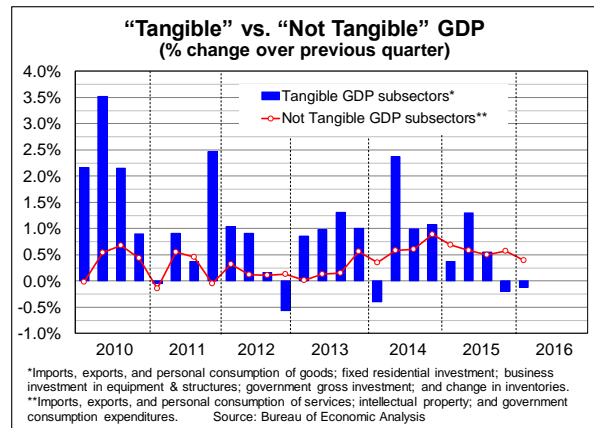
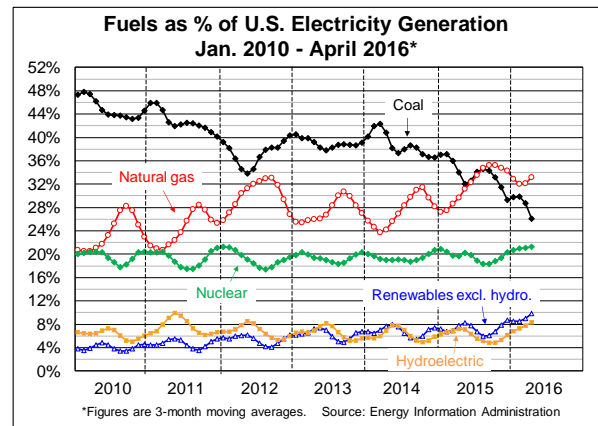


Figure 7



for coal in 2015 compared with 2014.<sup>4</sup> At KCS, we have not been immune: our coal traffic fell 10 percent in 2015 and is down significantly this year too.

Figure 8

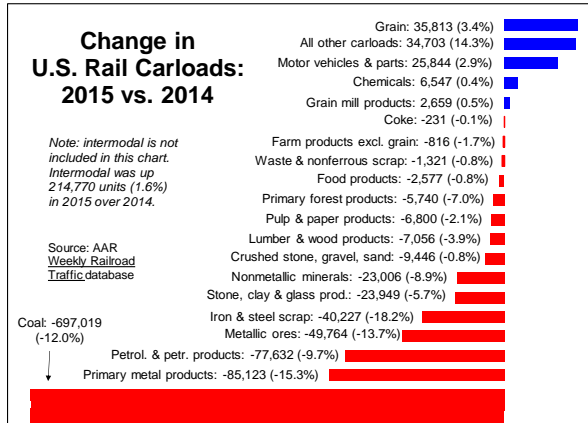
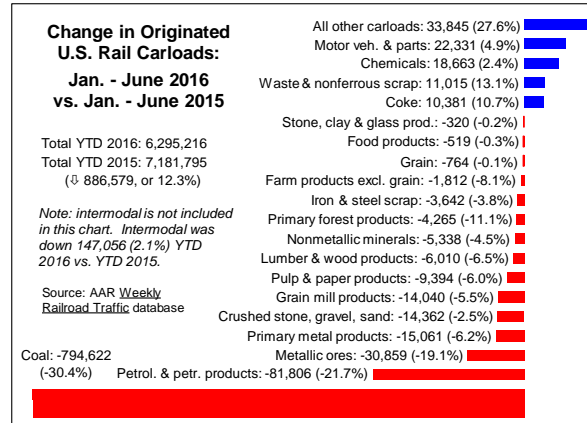


Figure 9



Likewise, recent slowdowns in crude oil production have led to reduced rail carloads of crude oil and associated products such as sand used in fracking, steel pipes used at drilling sites, and scrap iron and metallic ores used to create steel used in energy industries.

On the other hand, KCS and other railroads are benefiting right now from strong U.S. auto sales and associated rail movements, and are working with chemical firms as they build and expand petrochemical facilities in the Gulf Coast and elsewhere in the United States to take advantage of low-priced natural gas used as a raw material.

All of this illustrates that the U.S. and global economies are constantly evolving. Firms — even entire industries — can and do change rapidly and unexpectedly, and railroads must be able to deal with that flux. These broad, often unanticipated economic changes are reflected in changes not only in the volumes but also in the types and locations of the commodities railroads are asked to haul. If the commodities with rail traffic declines traveled on the same routes as commodities with traffic increases, the challenges these changes presented to railroads would

<sup>4</sup> These traffic figures are aggregates from the Weekly Railroad Traffic report from the Association of American Railroads. They differ from rail traffic totals from other sources.

have much less impact. However, when traffic changes occur in different areas — as is usually the case and has certainly been the pattern in recent years — the challenges to railroads become magnified.

### **The Challenge of Positive Train Control**

As members of this committee are aware, positive train control, or PTC, describes technologies designed to automatically stop a train before certain accidents caused by human error occur. Specifically, the Rail Safety Improvement Act of 2008 mandates that railroads' PTC systems be designed to prevent train-to-train collisions, derailments caused by excessive speed, unauthorized incursions by trains onto sections of track where maintenance activities are taking place, and the movement of a train through a track switch left in the wrong position.<sup>5</sup>

In October 2015, the statutory deadline for PTC installation was extended to the end of 2018, with further extensions available up to the end of 2020 to allow time for railroads to adequately test their systems. PTC development and implementation on U.S. railroads constitute an unprecedented technological challenge, on a scale that has never been attempted on railroads anywhere in the world.

Extending the statutory deadline for nationwide PTC installation was the right move for Congress to make. Rushing PTC development and installation and foregoing a logical plan for sequencing its implementation does not make sense. It would sharply increase the likelihood that the system would not work as it should. Making the PTC implementation deadline more realistic helps ensure that a fully-interoperable PTC system can be deployed in a logical manner and thoroughly tested prior to implementation. The extension is consistent with the fact that PTC should be implemented as well as possible, not as quickly as possible.

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<sup>5</sup> In this context, a switch is equipment that controls the path of trains where two sets of track diverge.

The extension has not led railroads to become complacent, however. In fact, their aggressive implementation of PTC continues unimpeded. As of the end of 2015, more than 14,800 locomotives were at least partially equipped with PTC, out of more than 18,500 that will require it. Nearly 18,200 “wayside interface units” (WIUs) have been deployed, out of 29,500 that will be required.<sup>6</sup> And nearly 1,700 out approximately 3,600 base station radios were installed. I’m confident that the next tally of installations, covering the period through the end of June, will show substantial further progress. KCS and other freight railroads are committed to PTC and are hopeful that it will lead to substantial safety benefits for our employees and the communities we serve.

### **Reacting to a Changing Market for Rail Services**

Successfully navigating the marketplace and other challenges railroads face requires nimbleness, creativity, and constant attention — both by railroads and by policymakers and regulators who oversee railroads — to the need for flexibility and efficiency. This is why KCS and other railroads respectfully submit that members of this committee and other policymakers should reject unnecessary legislation and regulations that hinder railroads from adopting to changing marketplace needs; that make it more difficult for railroads to make the massive investments a best-in-the-world, privately owned and managed rail network requires; or that impede railroads’ adoption or best use of new technologies.

As Lance Fritz, my counterpart at Union Pacific Railroad, explained in testimony to this committee in January 2015, the need for efficiency helps explain why railroads strongly oppose efforts to reverse existing policy under which the Surface Transportation Board (STB) must first

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<sup>6</sup> Wayside interface units provide the mechanism for transmitting information from signal and switch locations along railroad tracks to locomotives and railroad back office facilities.

find that a railroad serving a terminal area is engaged in anti-competitive conduct before the STB can order the railroad to “switch,” or interchange, traffic to another railroad when such an interchange is not necessary for freight delivery.

Forced reciprocal switching would significantly harm efficiencies at rail terminals, compromise the service improvements they have created for rail customers, and raise rail costs. The added switching activity that would be required, the increased possibility of service failures caused by that new switching activity, and the complex operations that would be required to bring about the new interchanges would disrupt rail traffic patterns, produce congestion in rail yards, and undermine efficient service to customers.

The need for efficiency also helps explain why railroads oppose a variety of other proposals that have been proffered in recent years, including (but not limited to) forcing railroads to prioritize certain types of traffic over other types, the imposition of speed limits on certain types of traffic that are not necessary from a safety standpoint, and local bans on the transport of certain commodities in certain areas. When considering these and similar proposals, policymakers should take great care in weighing the supposed benefits of the proposals with the substantial harm they would cause to railroad efficiency and, consequently, to our nation’s economic well-being. It’s also crucial that policymakers remember that railroads are integrated and interconnected networks: what happens in one location could easily have ramifications in locations hundreds or even thousands of miles away.

## **Conclusion**

As America’s economy and population grow, the need to move more freight will likely grow too. Speaking for KCS, as I look ahead I’m optimistic (changes in the transportation marketplace and an unsettled economy notwithstanding) that the future for freight railroads

remains bright. I'm confident in the abilities of our highly skilled and dedicated employees. I'm confident that our investments in new infrastructure and equipment will lead to a stronger, more reliable, and safer network that will help our customers and our economy to prosper. And I believe that, by working with members of this committee and other policymakers in Washington and elsewhere, we can together make sure that our freight railroads remain the best in the world.