

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

COMPETITION IN THE RAILROAD INDUSTRY

STB Docket No. EP 705

WISCONSIN CENTRAL GROUP
(an *ad hoc* rail freight shippers coalition)

TESTIMONY, JUNE 22, 2011

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INTRODUCTION

Mr. Chairman, Members of the Board, thank you for this opportunity to be heard on this subject.

IDENTIFICATION

I am legal counsel to the Wisconsin Central Group, an *ad hoc* rail freight shippers coalition operating under the auspices of: Wisconsin Paper Council; Wisconsin Manufacturers & Commerce; and Michigan Forest Products Council.

Our group, under various names, was present (including participation in various ICC proceedings) for the transition following Staggers and the Motor Carrier Act of 1980. From the mid-1980s through the early 1990s, we were present for the withdrawal of the Class Is from Wisconsin and Upper Michigan through various spin-offs. From the late 1980s and into the 1990s, we were present for the creation, consolidation

¹ Verification and identification of the affiant follows the text of the Testimony.

and successes of the independent Wisconsin Central System. And, of course, we were present for the grant of control of the WC System to Canadian National and its aftermath.

The goal of Wisconsin Central Group is to persuade the Canadian National, or by other means if necessary: (a) to assure restoration of Wisconsin Central System level service and competition for market share for traffic that originates and/or terminates on lines of the former WC System; and (b) to assure, for CN's main line between Superior, WI and Chicago, a transparent plan to mitigate the impact of increasing international traffic and to provide ample capacity for serving traffic that originates and/or terminates on lines of the former WC System.

We are pleased to report that since we appeared before you on February 24, 2011 in Ex Parte 704 and since filing our Initial Comments in this Docket, Canadian National has opened the door to exploring potential solutions to many of the specific competitiveness problems cited in our Initial Comments. We are cautiously optimistic that progress will be made to restore the model of competitiveness for non-captive freight that Wisconsin Central had been and can be.

TESTIMONY

The purpose of our testimony today remains to persuade you that "Competitiveness in the Railroad Industry" cannot be addressed without

addressing the state of railroad competition for non-captive freight – specifically, freight which contributes to going concern value with revenue/variable cost ratios between 100 and 180. The Board’s Notice in this Docket seems too quick to narrow the focus to the Board’s access policies and regulations. WCG does not believe the Board can effectively consider changes in its access policies and/or regulations and the impacts of such changes without considering the state of competition in the railroad industry for non-captive freight.

As Chairman Elliott remarked at the outset of the February 24, 2011 hearing in *Review of Commodity, Boxcar, and TOFC/COFC Exemptions*, Docket No. EP 704,² forty percent (40%) of railroad industry revenue, \$20 billion per year, is derived from exempt (*e.g.*, non-captive) freight. Witness after witness from the railroad and intermodal industries noted how very small a market share for non-captive freight the railroad industry enjoys, and how that share has shrunk over the years that the Exemptions from regulation and the Board’s current access rules and policies have been in place.

The Board cannot effectively review competitiveness and consider changes to its access rules and policies without considering how and to

² WCG has separately filed its notice of intent to participate and written testimony in *Review of Commodity, Boxcar, and TOFC/COFC Exemptions*, Docket No. EP 704, due January 31, 2011.

what extent the state of competitiveness in the railroad industry for non-captive freight is: (a) due to increasing competitiveness between and among modes, on the one hand; or, on the other hand, (b) due to other reasons such as a competitiveness problem within the railroad industry, such as that experienced, since 2001, by shippers on lines of the former WC System.

Our Initial Comments illustrate the **current** non-captive freight competitiveness problem in the context of rail service in our region (essentially the region served by the former Wisconsin Central System lines) from the mid-1980s to the present. From 1988 through 2001, WC System aggressively competed for market share in the region it served and was successful in increasing density of traffic, mainly non-captive freight, originating and/or terminating on its lines, including lighter density feeder lines throughout its region.

WC began and conducted most of its business during a period in which most of its traffic was both exempt from regulation and subject to current access policies and regulations. Indeed, the landmark, *Midtec Cases*, involved lines that became part of WC. WC's success was a product of deregulation.

This was, however, also a period mostly prior to many, and the most important, of the Class I consolidations. Most Wisconsin and Upper

Michigan shippers supported the shortline consolidations that brought about the WC System, reducing local rail-to-rail competition.³ They did so, however, without appreciating the long term impact of Class I consolidations on the ability of the WC System to continue to provide excellent service on its lines and competitive through rates from and to origins and destinations nationwide.

Year by year, WC System provided excellent, competitive service, earned its cost of capital and enjoyed strong stock prices right up to the point that its management team purportedly concluded that WC System's success and continued growth could not be sustained in the new Class I consolidated environment.⁴

CN's top management represented to this Board that, notwithstanding the economic incentives CN enjoys as a long-haul Class I, it would maintain the "local characteristics" of the shortline or regional WC System. Chief among such "local characteristics" was Wisconsin Central's aggressively competing for market share on traffic (mainly non-

3 *Wisconsin Central Transportation Corporation, et al – Continuance in Control – Fox Valley & Western Ltd.*, 9 I.C.C.2d 233 (1992), petition to reopen denied, 9 I.C.C.2d 730 (1993); and *Sault Ste. Marie Bridge Company – Acquisition and Operation Exemption – Lines of Union Pacific Railroad Company*, Finance Docket 33290 (1997).

4 Shortly before reaching this conclusion, this management team had ousted WC System's founder and architect of its success and growth through the 1990s, who is believed to have disputed the conclusion and rationale for merger into CN.

captive freight), to, from and within the region served by WC System lines.⁵

The historic, independent WC System was a competitive model for aggressive competition for non-captive freight through its prominent role in pricing and maintaining a nationwide network of through routes and rates – that being the most prominent among WC System “local characteristics” which Canadian National promised to preserve and which this Board made a condition of Canadian National’s control of the WC System.

The Board’s objective in exploring “competition in the railroad industry and possible policy alternatives to facilitate more competition” ought to identify the level of competition for non-captive freight as a critical competitiveness problem and consider how to provide incentives and structural or regulatory changes that will facilitate similar competitive models for non-captive freight. Although sympathetic to the concerns of shippers and receivers of captive freight,⁶ Wisconsin Central Group believes the more pressing competitiveness problem is rail industry competition for non-captive freight. When our Congressional leaders talk

5 CN representations were significant, *inter alia*, because they were made in pleadings which became the basis for the Board determining the FD Docket 34000 to be a “minor” proceeding, thus, blocking inconsistent alternative applications.

6 Many shippers and receivers on former WC System lines ship and receive some captive freight and are significant consumers of electricity generated by utilities that are captive shippers.

of easing congestion on the Nation's highways and dealing with crumbling and inadequate transportation infrastructure through greater freight market share for the railroads, they are necessarily talking about non-captive freight.

Regulatory intervention must be measured and targeted, the minimum necessary to accomplish the purpose. It also must be monitored and adjusted systematically, over time and in response to the evolving character of competition in transportation markets. Such regulatory change needs to foster market incentives such that the regulation is largely self-enforcing or market enforced. WCG opposes any regulatory change that relies to any significant degree on regulatory process or administrative adjudication.

CONCLUSION AND REQUESTED ACTION

WC Group submits that the Board's exploration of competition in the railroad industry in this Docket ought to:

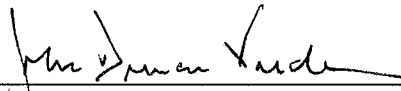
1. Focus consideration of regulatory change on creation of incentives and capacity for effective rail-to-rail and modal competition for non-captive freight, including the Board's jurisdiction and remedies available under 49 U.S.C. §§ 11101(a) and 11121-23 (car service);
2. In general,⁷ limit and/or defer consideration of regulatory change affecting captive freight, including current reliance on Constrained Market Pricing principles, until effective rail-to-rail and modal competition for non-captive freight (*i.e.*, incentives and capacity) has been firmly established; and
3. Consider the pros and cons of limited and/or targeted adaptation of specific current regulatory policies (alternative through routes and extended pricing authority, terminal facility access, reciprocal switching, bottlenecks and, if necessary, policies on reopening control proceedings) to address failures of competition or ineffective competition for both captive and non-captive freight.

⁷ WCG does not oppose changes that may be sought by captive shippers, so long as they are specifically targeted and so long as they do not impair the capability of the railroads to invest in competing for non-captive freight.

Dated this 8th day of June, 2011.

Verification

I, John Duncan Varda, counsel to Wisconsin Central Group, have, since 1970, represented Wisconsin Manufacturers & Commerce and other Wisconsin and Upper Michigan transportation shipper groups and various of their constituent members before the Interstate Commerce Commission and, lately, before the Surface Transportation Board, and do hereby affirm and verify that I have read the foregoing Initial Comments of Wisconsin Central Group and know the facts stated therein to be true and correct to my own knowledge and, as to those stated upon information and belief, I reasonably believe them to be true and correct.



John Duncan Varda

STATE OF WISCONSIN)
) ss
DANE COUNTY)

Personally came before me this 8th day of June, 2011, the above named John Duncan Varda, personally known to me to be the person who executed the foregoing verification and acknowledged the same.



Notary Public, State of Wisconsin

My commission 8-14-2011.