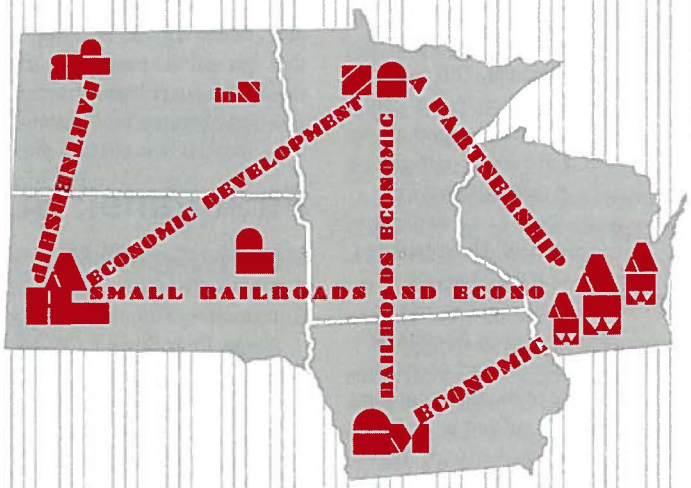
Small Railroads and Economic Development: A Partnership

June 16-17, 1997, Minneapolis, Minnesota

Sponsored by: Center for Transportation Studies, University of Minnesota

In Cooperation with: The American Short Line Railroad Association • U.S. Representative James L. Oberstar • Minnesota Department of Transportation



A Special Conference Report

The Center for Transportation Studies (CTS) sponsored the "Small Railroads and Economic Development—A Partnership" conference on June 16-17, 1997.

Moderated by Director Gerard McCullough, with opening remarks by Commissioner James Denn of the Minnesota Department of Transportation (Mn/DOT), the conference attracted nearly 160 attendees from regional development organizations, state and local government, shippers, small railroads, universities, and other organizations.

This special report summarizes the event that included: the opening keynote by U.S. Representative James Oberstar; opening session speeches by Jolene Molitoris and William Loftus; a panel on success stories; a dinner presentation by USDOT Secretary Rodney Slater; the second-day keynote by Kenneth Clayton; a panel on challenges and trends; a panel on government-industry partnerships; and a wrap-up by the session moderators.

Center for Transportation Studies, 200 Transportation and Safety Building
511 Washington Avenue S.E., Minneapolis, MN 55455-0375
Phone: 612-626-1077 E-mail: cts@umn.tc.edu

Oberstar: Small Rail Vital for Economic Vitality

"Short line railroads are the lifelines to small communities throughout the country." So declared U.S. Representative **James Oberstar,** who had initiated the conference through a request to CTS. Oberstar said that small railroads, including the 300 born since the rail industry was deregulated in 1980, are a tribute to the partnering spirit between rail and communities.

Given the importance of small railroads—they move six million carloads of goods each year—Oberstar asserted it would be "foolish public policy to ignore the needs, problems, and opportunities of this sector." Policymakers need to understand the real needs of small railroads and determine how government can help remove any obstacles to their future prosperity. Trucks can't carry all the loads required in today's growing economy; we must follow an intermodal approach to avoid being "choked in gridlock" and increasing costs.

"What's needed to make America's rail system number one? Political will."

—James Oberstar

So what can government do to help small rail? One problem that small railroads face is the difficulty in acquiring long-term financing. Because access to capital is key, Oberstar suggested that State Infrastructure Banks, as defined in NEXTEA (the National Economic Crossroads Transportation Efficiency Act), could be an option for investing in modernization and improving trackage. He also suggested that part of the Highway Trust Fund be made available for short line borrowing. He cautioned, however, that based on recent votes, "budgeting will be tough."

Oberstar said he is sometimes asked in town meetings why there are no investment programs for railroads. This is more than nostalgia; it is an understanding that we have lost a part of America's past that could make our future greater. He speculated that the public is ready for his proposals—as is Secretary Slater—but perhaps special interest groups are not. "What's needed to make our rail system number one," he asserted, "is political will—to rejuvenate small railroads, small towns, and America."

Molitoris: NEXTEA Funding Options

Jolene Molitoris, administrator of the USDOT's Federal Railroad Administration (FRA), said that small railroads—"an economic stellar success story for small towns"—are a vital part of creating a transportation system for the 21st century that is second to none. She also stressed that safety is the "foundation of everything," and praised the short lines' commitment to safety. NEXTEA will help us move to a zero tolerance level for any safety hazard, she said.

Jolene Molitoris

She then reviewed several measures in NEXTEA, including State Infrastructure Banks and the Transportation Infrastructure Credit Enhancement Program. The latter would provide $100 million in grants to assist projects that might otherwise be delayed or not constructed because of their size and uncertainty of revenues. The program's goal is to encourage the development of large, capital-intensive infrastructure facilities—such as rail—through public-private partnerships. Molitoris pledged commitment of FRA resources to help small railroads—including those that are privately owned—understand how they can become eligible for and use these programs.

Loftus: Government Aid Essential

William Loftus, chair of the American Short Line Railroad Association (ASLRA), gave a brief update on the recent success of small railroads. In 1970, 26,000 miles of the U.S. rail network were in bankruptcy. The problem was identified as excess capacity, and as a result 9,000 miles were terminated "overnight." The safety net for abandoned lines was the $400 million federal Local Rail Services Assistance Program, through which many of the 9,000 miles eventually became state or privately owned small railroads.

William Loftus

The Staggers Act of 1980, which deregulated the rail industry, further spurred the process by allowing the larger railroads to restructure and abandon low-density lines. Short lines now make up 45,000 miles and are an essential component of the rail network, Loftus said.

The key point to understand in this success story, he stressed, is that the new railroads needed one-time, initial financial assistance from government—and it worked. Without state and federal dollars, "many of them wouldn't be here." Small railroads face a similar situation today, he said, because investments are needed for heavy axle freight cars, which will be a major test for the viability of short lines.

Loftus called for NEXTEA to remove restrictions on the use of federal funds, including highway funds.

First Panel: Success Stories

Moderator: **Gary Tonkin,** Arrowhead Regional Development Commission, Duluth, Minn.

Peggy Baer, Iowa DOT. Iowa has offered rail assistance programs since 1973, Baer said. These include acquisition and surface repair programs as well as a successful railroad economic development program that provides matching funds to help companies build rail sitings. Key issues for small rail are: a stable financial base; long-term, low-interest rehabilitation funds; the relationship with Class I railroads; competent staff—including marketing staff—with diverse skills; and good relationships with cities and counties. She cited one success story: a nonprofit, community-owned railroad in southern Iowa which used a variety of sources of funds.

Gary Tonkin

Fred Yocum, Iowa Interstate Railroad. Following a major flood in 1993, federal and state funds allowed Yocum's railroad to rebuild its infrastructure—otherwise it wouldn't exist, he said. Everything they have done since involves partnering, with the state their largest creditor. For example, Iowa Interstate partnered with a local government entity to sponsor a Clean Air Act grant for which it had qualified. Along with joint ventures, "seeing the big picture and cooperation" are the keys to success, he said.

Bob Zelenka, Farmers Elevator Association of Minnesota. Zelenka described a $22 million cooperative effort to retain service on a 111-mile Milwaukee Road line in southern Minnesota. His association joined with various local interests such as Cargill, Hormel, utilities, counties, and 20 communities on the project. A key factor was the state's Rail Service Improvement Act, authored by Tim Penny and Henry Kalis, which he termed a "godsend" for project funding. Also important were FRA funds and a loan guarantee program backed by the state. "Cooperation between industry, elevators, counties—all parties—that's what it was all about," he concluded.

Frank Huntington, Southwest Wisconsin Regional Planning Commission. In the mid-1970s several rail lines were up for

abandonment in his area. To try to preserve rail service, counties decided to form four rail commissions. They also worked with the state to begin an acquisition and rehabilitation program in which the state provides 80 percent of funds, with a 20 percent local match. To date, ten counties and a number of shippers have contributed to the rail system, which "wouldn't exist" if it were not publicly owned. Although the system is marginal, the counties are still extremely committed to keeping rail service, he said: "Political will has held the system together."

Dennis McLeod, Red River Valley and Western Railroad, N.D. McLeod said that his company's carload business has grown over 50 percent in its ten-year history, largely due to track investments and close attention to customer needs. Overall, the future of the industry is very positive, but he cautioned that the larger Class I grain cars will present a problem for small rail. Federal and state DOTs need to include small rail in funding rehabilitation programs: "Since rail rehabilitation is considerably less per mile than highway rehabilitation, it makes good economic sense to provide public funds for railroads rather than continue to pay for rebuilding highways," he concluded.

Harold Halverson, President Pro Tem, South Dakota State Senate. In 1973 a state task force determined that state action—such as tax credits to firms—was needed to maintain rail service. In the early 1980s a rail authority was formed, and a sales tax was later passed to purchase more lines. The estimated cost of these programs is no more than $1.5 million per year, Halverson said—a "real good" return on investment compared with highway costs. As short lines improve their service, he pledged that South Dakota will support small rail as best it can.

Slater: NEXTEA Offers Promise for Rail

U.S. Department of Transportation Secretary **Rodney Slater** recounted how, upon becoming DOT secretary four months earlier, he had set three goals: (1) to make safety the number one priority; (2) to invest in our infrastructure to ensure that America's transportation system meets the needs and desires of the American people in the 21st century; and (3) to use a common-sense approach to running a department so that it works better and costs less.

"Transportation should never be a partisan issue, for we're building more than roads and bridges—we're building a nation."

—Rodney Slater

NEXTEA—the president's $175 billion proposal—addresses these issues with an 11 percent funding increase over the prior six years, which is very good in times of budget balancing, Slater said. Of the $175 billion, "$7.5 billion will be invested in Minnesota, Wisconsin, Iowa, and the Dakotas." NEXTEA also will help Americans find an edge to compete—to win—on an international stage. "It speaks as much about the next 60 years as it does the next six years," Slater said.

He then relayed a few elements of NEXTEA. First, the proposal provides $150 million per year for State Infrastructure Banks as leverage for attracting public and private investment. Since rail freight projects have difficulty getting financing, he suggested that short lines would be excellent candidates for these loans. Second, NEXTEA raises by 30 percent the environmental funds that would allow investments in rail to reduce highway congestion, and it retains funds to continue to close highway-railroad grade crossings. Third, NEXTEA will cut red tape to give states the flexibility to build projects they want, not those that Washington dictates.

As NEXTEA is debated in Congress, Slater vowed to work closely with Representative Oberstar, a "national leader," as well as with Republicans on a bipartisan basis. "Transportation should never be a partisan issue," Slater concluded, "for we're building more than roads and bridges—we're building a nation."

[The full text of Slater's speech is on the World Wide Web at http://www.dot.gov/affairs/index.htm]

Clayton: Ag Markets Depend on Rail

Kenneth Clayton

The continued viability of small rail "is an imperative for efficient marketing of U.S. agricultural products," according to **Kenneth C. Clayton**, deputy administrator for marketing programs with the U.S. Department of Agriculture. Our ability to move products is what sets us apart and helps make the U.S. agricultural sector the envy of the world.

To appreciate the importance of small rail to U.S. agriculture, consider rail's value to its users, he said. The marketing system which connects producers to consumers determines whether grain in the Midwest remains profitable. Rural economies are often tied to the success of the grain industry. Because waterways are often not nearby, rail's cost and availability are thus key to grain marketing and small communities, Clayton said.

He voiced several concerns that the USDA has for the future of small rail: the impact of continuing mergers of the larger, "Class I" railroads; abandonment of rural rail lines, which, USDA research shows, would raise marketing costs and dent farm income; and the difficulty in acquiring capital.

The core issue is determining the public interest in small rail's survival and deciding what resources can be used to help it prosper. NEXTEA, he hopes, will "go some distance" in addressing this issue. He reaffirmed that the USDA attaches great importance to small rail and will continue to be a vocal advocate for a transportation system that protects the interests of rural America.

Second Panel: Challenges and Trends

Moderator: **Caroline Gabel,** U.S. Representative Oberstar's Office.

Caroline Gabel

Frederick Beier

Frederick Beier, Logistics Management Research Center, University of Minnesota. To survive in a ferocious market, small railroads will have to develop strong relationships with customers—that is the key to their survival, Beier said. They must become more personable, flexible organizations, responding quickly and effectively to service their clients' needs. This role, akin to a freight or travel agent, is what can set them apart from the Class I's.

How can they accomplish this? Through competitive pricing, continued cost reduction programs, joint planning activities, customer advocacy, and boundary-spanning activities, Beier answered. Other options he cited are compatible information systems to exchange traffic information, regular meetings with clients, and longer client contracts.

Gerard McCullough, CTS. McCullough defined "intelligent" transportation systems as those where users pay the full cost of using the system, with no cross-subsidies or bad external effects on society. He cited a 1996 Transportation Research Board study of the external costs (conges-

tion, accidents, air pollution, energy security, and noise) of freight transport. The study found that the external costs of railroads are five to six times lower than those of trucks—a significant difference in cost to society. He advocated full pricing of externalities and full cost allocation for all transportation modes.

Denver Tolliver, Upper Great Plains Transportation Institute, North Dakota State University. Huge infrastructure investments are needed to maintain small rail service, Tolliver said. About 30 percent of small rail miles could become obsolete with expanded use of heavier freight cars. Loss of service may result in reduced competition and increased transportation costs, as well as greater truck traffic on rural minor arterials and collector highways. Externalities could include higher handling costs for shippers and increased costs for resurfacing or reconstructing local roads. He stressed that an intermodal perspective is appropriate, and that small rail plays a valuable role in the cost-effectiveness of the grain transportation system.

Small railroads operate and maintain 27 percent of the American railroad industry's route mileage and account for 9 percent of the rail industry's freight revenue and 11 percent of railroad employment.

—Source: ASLRA

cant funds for rehabilitation. Finally, improving crossing safety and closing some crossings entirely must be addressed. The biggest issue for small rail, he said, is to build long-term alliances with Class I's.

Lynn Anderson, Dakota, Minnesota and Eastern Railroad, S.D. His 11-year-old company recently announced a $1.2 billion project in Minnesota, South Dakota, and Wyoming that will construct 200 miles of new track and upgrade 650 miles of existing rail. The company made this decision to handle growing traffic volumes driven by the explosive demand for low-sulfur coal. The project will involve partnerships with government for developing environmental impact statements and for improving safety. Overall, the project will offer many benefits, he said. It will mean much better service to existing customers and should attract new customers. The company will work with local economic development agencies in a number of areas, plus, the project itself is a huge economic boon, creating 1,000 more full-time rail jobs and related tax revenues.

Third Panel: Strengthening Government - Industry Partnerships

Moderator: **Alice Saylor,** American Short Line Railroad Association.

Liz Prebich, St. Louis and Lake Counties (Minn.) Regional Rail Authority. Referencing the session's title, Prebich questioned whether government-industry partnerships really exist at all. In her experience, small railroads are dependent on large rail and have little bargaining power. Moreover, there is no partnership with the state.

Alice Saylor

To improve the situation, she encouraged government and industry to try to understand each other, talk the same language, and respect each others' rules. Industry must understand that government wants to be respected as more than just a bill payer and must be accountable to taxpayers. Industry also must look at what its contribution to the community should be. She challenged industry to consider making a lower profit and work towards a partnership with government to meet infrastructure costs.

Al Vogel, Mn/DOT. The relationship of government and rail has improved substantially in the past 20 years, Vogel said. Still, it is best described as a reluctant partnership. Government and rail need a shared vision that responds to the transportation needs of customers. They also need to be concerned with discussions of livable communities and be alert for competing land use interests and rail-intolerant neighborhoods. Railroads must help government understand the value they add to quality of life by sharing timely data, he said. Government in turn should communicate the information to the general population and decisionmakers. Education is a critical piece of the puzzle—for example, people should be educated to understand that their light switches work because coal was shipped by rail. Government and industry also must partner in research to find innovations and improve safety.

Dennis Wendland, Harvest States Co-op, St. Paul. For organizations such as his to compete in the world market, a viable transportation system of rail, truck, and vessels is needed. He then reviewed several issues facing small rail. First, a "staggering" investment would be needed in station facilities if Class I railroads continue to increase to 100 or 110 cars per train. Second, lines that can't improve efficiency enough to meet the demands of large companies could close. Also, tracks will need to be upgraded to accept the larger rail cars, requiring signifi-

Moderators' Wrap-Up

William Loftus. His panelists supported ISTEA as expansive and not limited to highways, with greater local options and flexibility for states. They mentioned state infrastructure banks as one method of delivery. Loftus added that rail issues are articulated well at the state level but need to be elevated to federal officials.

Gary Tonkin. The key issue emphasized in his session was partnerships: between states and small railroads as well as with local communities. Speakers stressed that small rail is critical to the communities they serve and the economies of localities and states. Communities need grassroots support to prevent rail from pulling out and cannot wait for states to save their service. Tonkin asked what role government needs to play to expand or improve programs. More than money is needed to succeed; he speculated that marketing may play a factor as well.

Caroline Gabel. Short lines are more than transportation—they are service organizations that need to build partnerships on both ends of the route. She also stressed the importance of small rail to international competition: "Anyone can grow grain; our edge is in the transportation system that gets it to market." She reminded the audience that Representative Oberstar had earlier called for political will and is a rail advocate, but he is only one vote. She challenged the audience to talk to legislators, educate them about rail's benefits and lower externalities, and tell them their standpoint. NEXTEA must be expanded to include rail.

Gerard McCullough

Alice Saylor. The presentations in her session showed that there is more work to do. She called for partners to be more effective in their roles, particularly to tell rail's story better—it pollutes less and has lower externalities. Communities are sometimes adversarial to rail and resist the side effects of rail's success. Partners need to expand their audience and explain to communities and policymakers the value of the rail system to all citizens.

Gerard McCullough. The last couple of decades show some movement toward intelligent transportation systems, where users pay the full costs of using the system. Freight rail systems in the United States are intelligent. Our nation's highways and air traffic system are not.