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AGAINST THE GRAIN: RAILROAD RAMIFICATIONS AS OIL CROSSES WHEAT  
COUNTRY

By

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Professional Paper

Presented in partial fulfillment of the requirements  
for the degree of

Master of Arts  
Environmental Science and Natural Resource Journalism

The University of Montana  
Missoula, MT

May 2015

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Scheer, Laura, MA, May 2015

*Environmental Science and Natural Resource Journalism*

Against the Grain: Railroad Ramifications as Oil Crosses Wheat Country

Chairperson: Nadia White

Abstract Content:

Over the past two years, grain growers along Montana's Hi-Line have experienced significant shipping delays because of heavy traffic on the railroads in the northern plains. The delays caused declines in wheat prices and many farmers had to build extra storage to house the crops they couldn't get on the rails. Burlington Northern Santa Fe Railway, the main railroad serving the Hi-Line, blames the congestion on harsh winter weather, a larger than average crop harvest and an increase in shipping demands across all sectors. Farmers say the railroad has favored increasing shipments of crude oil from the Bakken shale formation in North Dakota and eastern Montana. The railroad has improved service in recent months after significant investments, but Montana farmers remain wary that service issues may continue in the years to come.

Against the Grain: Railroad Ramifications as Oil Crosses Wheat Country  
By Laura Scheer

On a sunny and unusually warm Monday in late March, Gordon Stoner digs a shallow and narrow trench in the mud to drain water from beneath six large grain storage bins on his farm in northeast Montana.

Behind him are two even larger storage bins that can hold more than 50,000 bushels of grain each. A bushel of wheat is equivalent to eight gallons and weighs about 60 pounds. They are unmistakably new because on a sunny day, you can be blinded by their metallic shine from a mile down the road if the sun hits them right. It cost around \$2.50 per bushel to build them, he said, or \$250,000.

Stoner, 59, grows grain outside of Plentywood in Outlook. His family has been farming in northeast Montana for four generations. At 12,000 acres, Stoner's farm is large, but not atypical of Sheridan County. His 84-year-old mother still lives in the house she raised him in on the property. Next to it sits the house his great grandfather built when he homesteaded the land in 1915.

In the coming months, Stoner will build two additional storage bins as big and shiny as the new ones he already has for an additional quarter million dollar investment. The investment reflects more than the sun; it reflects an enduring mistrust of railroads.

Farmers in Plentywood have been hit hard in recent years by delays in grain shipments that have driven up the cost of storing and shipping grain and delayed pay day for them. They blame delays on a surge of crude oil shipments from the Bakken oil boom, outdated grain elevators in small towns and rough weather. The solution so far has been to throw money at the problem and threaten government oversight. It remains to be seen if that's enough.

In 2013 and 2014, Stoner and other grain growers along Montana's Hi-Line struggled to get their grain to market because of a shortage of rail cars.

The "Hi-Line" is U.S. Route 2, which cuts across northern Montana. It is also the main route for Burlington Northern Santa Fe Railway (BNSF), the second largest railway in the U.S. and a bright spot in Warren Buffet's investment portfolio. Berkshire Hathaway has owned BNSF since 2009.

In the last two years, BNSF has come under fire for the worst congestion issue on the rails in history, with a majority of complaints coming from the agriculture community. For farmers on the Hi-Line, shipping their grain by rail is their only option. Trucking is too expensive.

Stoner said that he's hoping service will improve this year, but a general sense of mistrust and wariness towards the railroads lingers.

With so many moving parts, it's difficult for railroads or anyone to predict future constraints on capacity. The outlook is that rail service will improve, but it mostly depends on oil production leveling off or decreasing in the Bakken.

Predicting this year's rail traffic depends on several "unknowns", said Lochiel Edwards, chairman of the Ag Rail Business Council, a roundtable of national commodity groups and BNSF. Edwards is a third-generation wheat farmer in Big Sandy and also has a consulting group called TTMS Group, which provides trade, transportation and marketing solutions.

He said the degree of traffic in 2015 would be influenced mostly by shipments of crude oil, which farmers blamed for the congestion issues over the last two years. Despite a drop in crude oil prices in 2014, crude oil production is expected to continue to increase.

Strong growth in domestic crude oil production in tight formations, like those found in the Bakken, is predicted through 2020, according to the 2015 Annual Energy Outlook published by the U.S. Energy Information Administration in April.

In 2014, more than 262 million barrels of crude oil were shipped by rail out of the Midwest, most of which originated in the Bakken, according to the administration.

Most crude is being shipped to the East Coast, but West Coast ports are also a major destination. Westbound crude from the Bakken is shipped on the Hi-Line, but that's also the main route for westbound Montana grain.

In 2014, more than 136 million barrels of crude were shipped from the Midwest to the East coast in 2014, while almost 51 million barrels were shipped from the Midwest to the West coast. Farmers argue that crude oil shipments took up unprecedented amounts of space on the rails, causing delays in shipments of grain.

Anton Bekkerman, assistant professor of agricultural economics at Montana State University, agreed that rail traffic will depend on crude oil shipments, but added that he's optimistic that service for farmers will improve in 2015. He said investments made by BNSF and a projected smaller crop size for the coming year will ease traffic.

In 2014, BNSF invested \$5.5 billion in infrastructure, additional rail cars and added personnel to improve service and regain farmers' trust.

"The tough part with projections is knowing whether they'll be true or not," Bekkerman said.

The main cause of the congestion in 2013 and 2014 was the railroad's incorrect projections, farmers like Stoner say.

"The railroad miscalculated. They truly did," Stoner said.

In addition to higher than average crop yields, BNSF had to slow down trains because of harsh winter weather, he said. The harsh weather also led to an increased demand in for coal.

“Then you add the Bakken on top of it, which the railroad pretends it never happened. They’re disingenuous,” Stoner said. “When you add the amount of oil they’re moving, it’s added to the problem.

### **The Perfect Storm**

In November 2013, Stoner said he had sold 95 percent of that year’s crop, but was not able to deliver a single truckload of grain until April 2014, five months later. Stoner went without payment for that period.

By June 1, 2014, he had delivered only 35 percent of his 2013 crop. With his 2014 crop harvest on the way, Stoner said he had to build the first two of his four new storage bins to make sure his crop wouldn’t sit outside on the ground.

Montana Sen. John Tester heard about the delays from farmers across the state and wrote to BNSF in early 2014, urging them to improve delivery times. The concern has been fairly widespread across Montana's Hi-Line, said Marneé Banks, communications director for Tester.

The issue is of particular concern in Montana, where trains were more than 30 days late to pick up grain orders in April last year, Banks said.

“Agriculture is Montana’s top economic driver, so the continued delays have had a real impact on its economy,” she said.

With officials and stakeholders blaming BNSF for the delay, in April 2014, the federal Surface Transportation Board held a hearing. The board is responsible for resolving railroad rate and service disputes and they heard from grains and feed associations, farmers’ unions and government officials. They also listened to an explanation from BNSF and the railroad’s plan to resolve the bottleneck in the grain states.

After the hearing, the STB required the railroad to make weekly reports on grain shipments, including data on how many days a train showed up late to pick up grain.

BNSF has placed most of the blame for delays on severe winter weather, which forced the company to shorten its trains and decrease speeds, but other factors contributed to what many have called the “perfect storm”.

In 2013 BNSF saw increased demand for shipments of coal, oil and consumer goods and an unusually large harvest from farmers in Minnesota, the Dakotas and Montana.

“Everything slammed (BNSF) at one time,” said Matt Flikkema, past president of the Montana Grain Growers Association. “They weren’t prepared.”

Over the two years, Flikkema said he’s heard from farmers all over the state who are concerned about their rail service.

As a “common carrier,” BNSF is required to provide rail service upon reasonable request to all commodities.

As the congestion on the rails continued into 2014, farmers in northeast Montana wondered why their grain was still on the ground at their farms while 100-car trains carrying crude oil rumbled past at a seemingly unaffected rate.

“(BNSF is) a for profit company, sure. I’m not surprised if they allocate more resources to oil,” Stoner said. “But they are also a common carrier and they have common carrier obligations which is to serve us all.”

### **Oil Next Door**

On a December morning at Cousins Family Restaurant in Plentywood, Stoner orders a breakfast suitable for a farmer: two eggs, hash browns, sausage and toast.

“This will keep us full until tomorrow,” his wife Bonnie said between bites and the never-ending “hellos” of small towns.

“My nephew who lives in the Twin Cities now was here visiting,” Stoner said. “We had come in (to Cousins) after church with him and I had said, ‘hello, hello, hello,’ and we sat down and he said, ‘Is there anybody in here you don’t know?’ and I said ‘No.’ That’s not so much true today with the oil field activity with the Bakken. There are a fair number of people around you don’t know anymore.”

But unfamiliar faces are not the only change the Bakken oil boom has brought to this part of Montana. The railroad that runs through town has been choked with oil trains in recent years, making it hard for local farmers to get their grain to market on time.

Plentywood is situated in the Bakken area of Montana, so the delay for farmers here has been compounded by the increase in oil shipments BNSF has seen in recent years.

The delays have hit northeast Montana farmers the hardest, said Ryan McCormick, a Kremlin farmer and a past president of the Montana Grain Growers Association. That is where the most grain has been piling up and farmers have been building more storage. The amount of grain that piled up on farms and at elevators in 2013 and 2014 is unknown.

Since 2008, shipments of crude oil by rail in the U.S. have increased almost 4,500 percent with most of that increase focused near the oil fields where crude originates.

According to congressional research, rail industry officials estimated to have carried 434,000 carloads of crude oil in 2013 (roughly equivalent to 300 million barrels), compared to 9,500 carloads in 2008.

While the shortage of freight train availability nationwide can't be entirely blamed on an increase in crude oil shipments, it's had a stronger effect in areas of heavily concentrated oil development, such as the Bakken, Edwards said.

At the April 2014 STB hearing, BNSF said its car loadings in North Dakota had more than doubled from 2009 to 2013, adding that in October 2013, crude oil and agricultural car loadings rose by more than it could manage. BNSF did not have enough train cars to meet demand, creating a bottleneck in the Bakken region that led to delays.

Because this increase in crude oil shipping demand occurred in the Bakken, it caused a bottleneck, or a back up of commodities waiting to be shipped due to a lack of available train cars.

Nationally, crude oil represents a small increase in rail traffic, but in specific areas it is enough to cause bottlenecks that "reverberate across the entire rail network," the Congressional Research Service found.

Plentywood's bottleneck was compounded by the small town's old and outdated grain elevators.

### **No Shuttles, No Service**

On a cold December morning thirty miles north of Plentywood, 50 semi trucks were lined up outside of the grain elevator in Westby. More trucks are pulling up with each passing minute. The Westby elevator posted on its website that it would be accepting durum wheat from last names beginning with letters "M" through "Z". Behind the wheel of each truck is a farmer eager to get their grain on the rails.

The previous day, the Westby elevator accepted durum wheat from last names beginning with letters "A" through "L" and the line was just as long.

Not all of the farmers are from Westby. Many drove the extra miles to come here because this elevator has something their hometown elevator does not: the ability to load long trains that carry the same commodity to a single destination without being split up. These are called shuttle trains.

"I've gone to Westby every week since they've been doing this," said Daryn Andersen, a grain grower from Plentywood. Andersen said the Westby elevator has designated days based on last names because of extremely long lines due to the congestion issues.

Plentywood has two elevators, both owned by Columbia Grain: one in town that is used for peas and lentils, known as “pulse crops,” the other on the edge of town that is used for small grains like wheat and barley. Neither has the ability to load the big shuttle trains. They purchase a smaller number of cars to fill with grain that will be attached to a train of mixed commodities.

Shuttle trains are efficient because a large amount of grain can be shipped in a short amount of time. Trains carrying several different commodities and stopping in several locations for pick-ups and drop offs – mixed freight trains – move slower. Time, especially in the railroad business, is money.

Elevators like those in Plentywood are more vulnerable to shipping delays because they cannot serve shuttle trains. To catch up with delayed shipments, BNSF has favored shuttle trains because they can move more grain at one time.

“What happens is the railroad gets behind and tries to keep as much product moving as possible,” Edwards said. Shuttle trains are more efficient for BNSF than mixed freight. “So it would be their natural inclination to not send that train crew up to get those six cars in Plentywood than to hook them onto a shuttle and high tail it to Portland.”

The grain-growing region of the Northern Plains was once dotted with small elevators, each able to fill a few cars with grain harvested from fields just a wagon ride away. But not anymore.

“If you can’t load shuttles, you can’t be in the game,” said Danny Moore, the grain elevator manager for the elevators in Plentywood and elevators elsewhere in northeast Montana for 42 years. The cycle the delays create – late shipments that lead to late paydays – have made money tight for farmers and elevator operators alike.

“It’s a huge impact on cash flow,” Moore said. “Mentally, it’s so stressful when you’ve got pressure from the producer and pressure from the people you’re supposed to ship the grain to.”

Jeff VanPevenage, senior vice president of the Montana region for Columbia Grain, agreed that the smaller elevators that can’t service shuttle trains have suffered the most.

“Shuttle services in general are fairly reliable and on time,” VanPevenage said. “It’s single-car shipments, 20-car shipments that have been affected by inefficiencies.”

According to weekly service reports submitted by BNSF to the STB, rail service for grain in Montana has been an average of 14 days late with an average 844 delayed train car orders since mid-October 2014, when the STB began requiring the reports. These delayed car orders refer to single and multiple car shipments, like those coming from Plentywood, not shuttle shipments.

Edwards said the delays were even worse in May and early June reaching a peak of 3,000 delayed car orders with an average of 28 or 30 days late in Montana.

In response to the delay, both elevators in Plentywood are expanding in hopes of receiving better service from BNSF. The elevator on the edge of town will be able to service shuttle trains, but the update has taken longer than expected.

In the meantime, Plentywood farmers have been trucking their grain to Westby.

The elevator in town has also been building more storage on-site to help operations move quicker, something Stoner said he has been pushing VanPevenage to do for years. With more storage, the elevator will be able to clean the grains faster and get them on the rails faster too.

### **Bottom of the Food Chain**

It's before sunrise on a Monday morning in late March and five or so farmers are already gesturing to their mugs for a refill of hot coffee. One of them orders his breakfast while others wait their turn. There is not a menu in sight, but they all know what they want and so does the waitress. Gusts of chilled early morning air sweep through the tiny diner as the rest of the "regulars" file in.

Stoner is among the group of 10 or so farmers who meets every weekday at 6 a.m. at Randy's Restaurant, the other place to eat in Plentywood besides Cousins. "The boys," as they refer to each other, discuss business on the farm. They either chuckle sarcastically or lower their heads when asked about the congestion issues on the rails, a sign it's been a tough couple of seasons for them.

Just ask this banker.

In the last two years, Stockman Bank in Plentywood has provided more loans to farmers for grain storage than normal, said Paul Hansen, vice president of the bank branch.

Last year more farmers than usual also had to extend their operating loans because they couldn't get their grain on the rails, he said.

Usually farmers are able to pay off their operating loans for the year with the money they make selling grain, but they aren't paid until the grain is on the rails.

Hansen said farmers who previously had to borrow very little haven't been able to pay their loans back at the end of the year.

When it came time to renew operating loans at the end of 2014, farmers weren't able to pay off what they owed, so their debts were carried over into this year, Hansen said.

Stoner said farmers should strive to build cash reserves, allowing them to continue to operate in the case that their grain deliveries are delayed in the future.

“At a minimum, a farmer’s banker needs to be onboard in advancing money until the farmer can deliver crops,” he said.

Although service is expected to improve this year, the consensus among “the boys” is to be wary.

Stoner and many of his neighbors feel they can’t leave it to anyone else – not the railroad and not the elevators – to ensure last season’s grain won’t be left on the ground this winter. Stoner is not alone in wanting to build new silos. The silos will store their grain when trains might not be available or when prices are low and they want to wait to sell.

Adding to their frustration are falling grain prices, and the delays affect that too.

When there’s a shortage of grain cars, elevators have to pay extra to secure the cars available on a secondary market. That cost is passed on to farmers, who get less for their crop.

The price per-bushel of wheat offered to Montana farmers at the height of the train congestion in March 2014 fell by up to \$1, according to testimony from the National Grain and Feed Association to the STB in April 2014.

This depreciated price over the last two years translates to a \$203 million loss for Montana grain growers based on the state’s crop size, according to testimony presented by representatives for the grain growers.

Bekkerman conducted his own study of grain prices in Montana to see if prices had depreciated. It had, and the most likely reason he could offer for it was a shortage of rail cars, he said.

That was no surprise to farmers like Stoner.

“Ultimately, very much so, the farmer bears the burden of the cost of freight,” Stoner said.

Investments during 2014 and 2015 will total more than \$230 million in Montana alone, said Matt Jones, spokesman for BNSF. These investments include more than 100 miles of double track in Montana, North Dakota and Washington that will reduce some of the congestion along BNSF’s northern route along the Hi-Line, he said.

The farmers remain wary.

“BNSF will say, ‘Oh we’re spending 5 billion, next year it’s going to be 6 billion.’ They’re still not spending enough,” Stoner said. “They’re not reinvesting their profits as quickly as they can. When you have a monopolistic situation, we have to watch it.”

Sen. Tester’s office said the rail capacity problems have added an unneeded burden to farmers and created problems for them when marketing their grain.

“The rail capacity issue began early in 2014 when farmers were still waiting to get their 2013 product to market, while at the same time seeding for the 2014 harvest,” Tester’s spokeswoman Banks said. “Though small improvements were made by the time last year’s harvest rolled around, the problem continues to exist.”

In late March, a bill was introduced that would mandate STB reforms to help prevent the kind of rail congestion issues that plagued grain farmers in 2013 and 2014. The bill, sponsored by Senate Commerce Committee Chairman Sen. John Thune of South Dakota, and the committee’s ranking Democrat, Bill Nelson of Florida, would give the panel a new authority to initiate investigations into rate and service issues. Currently, the STB can initiate an investigation only if a shipper files a complaint.

Edwards said that creating a permanent reporting system on rail performance would be more effective than the changes proposed in the bill. He calls SB 808 “a benign bill” that neither hurts nor helps.

“It’s a feel good thing in my opinion,” he said.

McCormick, former president of the Montana Grain Growers Association, warned that growers need to have a strategy in mind if the delays happen again.

“I think the message to (farmers) is they really have to try to plan around this to move grain early,” McCormick said, by selling their grain to their local elevator as soon as possible.

Whatever the solution to the monopolistic situation, some grain growers remain as wary of government intervention as they are of the railroad.

“I am not in favor of government intervention in that the marketplace sorts it out,” Stoner said. “Capitalism and the marketplace, it can be a cruel taskmaster, but it’s efficient.”

In the coming months, Stoner will build a second pair of new, shiny storage bins.

He said he wants the railroads to continue to invest in infrastructure, equipment and people to handle the growing freight volumes seen in recent years, but also added that as an industry, grain shippers need to do a better job of communicating their future shipping needs.

“Farmers are on the bottom of the food chain and whatever investment is made upstream, we have to pay for,” Stoner said. “When I complain that the railroad isn’t investing enough, I know I’m going to share part of that cost. But what do we need? We need dependable, reliable service.”