



Regulation of Railroads in America

In 1887, Congress passed the Interstate Commerce Act, which created the Interstate Commerce Commission (ICC) to supervise, regulate and investigate interstate carriers and determine whether discrimination existed against interstate commerce. By the 1970s, the American railroad system was on the brink of collapse due to decaying tracks, locomotives and railcars that bankrupt railroad companies could not afford to repair. To address this problem, Congress passed the Railroad Revitalization and Regulatory Reform Act (4R Act) to rehabilitate the railway system while deregulating the competitive market.

The 4R Act failed to achieve increased earnings for railroad companies, so Congress enacted the Staggers Rail Act of 1980 (Staggers Act) aimed at further deregulating the American railroad system. Most importantly, the Staggers Act granted greater pricing freedom to railroad companies, streamlined the merger process, expedited the line abandonment process, allowed multi-modal ownership, and permitted confidential contracts with shippers.

In 1995, Congress completed the deregulation of railroads with the ICC Termination Act (ICCTA). This act created the STB and vested STB with oversight of railroads. Since the Staggers Act and the ICCTA, the railroad industry has gone through major consolidations resulting in just seven Class I railroads, four of which control 95 percent of the traffic.

The Surface Transportation Board

The STB is a bipartisan board composed of three members nominated by the president and confirmed by the Senate for five-year terms. The STB has regulatory and adjudicatory oversight over a range of modal systems, including railroads. Congress established policies governing the STB's regulatory and adjudicatory authority over railroads, including establishing reasonable rates for rail transportation and fostering economic conditions that promote effective competition. Notably, the STB is meant to protect the public against unnecessary discontinuance, cessation, interruption or obstruction of rail service.

Challenging Unreasonable Rates

The preemption clause of the ICCTA exempts railroads from federal and state antitrust laws. Thus, shippers that seek to challenge anticompetitive rates must do so in a proceeding before the STB, subject to the STB's rules on excessive rates. The current system under which rail customers can attempt to challenge rates is cumbersome and inefficient.

In order to challenge a rate before the STB, a party must bring a formal complaint. As a threshold question, the STB determines whether the railroad has market dominance. After this determination, the STB evaluates whether the rate charged is reasonable. The STB applies a principal known as Constrained Market Pricing (CMP) to determine a rate's reasonableness. CMP provides three criteria to guide the evaluation: (1) A railroad should not charge a shipper a rate that is more than necessary for the railroad to earn adequate revenues, (2) A shipper should

not pay more than necessary for efficient service, and (3) A shipper should not bear the costs of facilities or services from which the shipper bears no benefit. Using these principals, the STB has three standards under which an individual can challenge a railroad rate: (1) stand-alone cost test; (2) three benchmark test; and (3) simplified stand-alone cost test.

Various standards and modeling are used by STB to determine whether a railroad is exploiting its market power. Despite adjudicatory options available to captive shippers, the time and cost associated with such proceedings is significant. Costs alone can reach \$5 million to adjudicate fully a stand-alone cost case and prevailing awards are subject to caps. The STB updated its rate regulation rules in 2013, and found that it may not have adequate procedures to provide meaningful relief to grain shippers. In order to address this concern, the STB opened a separate docket to investigate this issue.

Rail Transportation of Grain, Rate Regulation Review

In June 2015, the STB held a hearing as a follow-up to the 2013 findings. While a range of interests testified, from Class I railroads to farmers, there was a clear set of themes that emerged with railroads favoring status quo and customer groups urging reform of rate challenge procedures. The least vested party was the Transportation Research Board, which provided a summary of a congressionally mandated report. The TRB found that more appropriate, reliable, and usable procedures are needed for resolving rate disputes; better data is required to assess railroad service quality; and certain functions left over from the previous regulatory era, such as regulators having responsibility for merger approvals serve purposes that are no longer valid. Overall the TRB report proposed modernizing an arcane system through reducing regulatory burdens for railroads, while also giving shippers real protections against unreasonable rates.

Surface Transportation Board Reauthorization Act of 2015 (S. 808)

Government reports and anecdotal evidence demonstrate that the STB rate review process is cumbersome and inefficient. **The bill sets timelines for rate reviews and expands voluntary arbitration procedures when both parties want a quick and efficient resolution.** The timelines prescribed in the bill may help to avoid overly lengthy delays and also requires STB to study more efficient and simplified rate review methodologies to further alternatives to the stand alone cost test.

In 2014, grain car backlogs, storage constraints, and rail car premiums raised transportation and commodity costs. STB, while aware of the evolving problems did not have the authority to proactively investigate rail delay issues. **The bill** provides the STB with the authority to initiate investigations on matters other than rate cases and requires the STB to establish a database of complaints and give quarterly reports on them to provide more accountability for ongoing problems.

STB has only three appointed members; should two commissioners meet, it automatically forms a quorum. As such, a public hearing notice is required. S. 808 expands the board from three to five commissioners and, with proper disclosure, allows board members to talk with one another without a prior public hearing notice so long as it complies with certain procedures. Lastly, the bill provides such sums of funding required to carry out STB's expanded authority.

"The STB should move forward with a comprehensive package of all current proposals before the board and not piecemeal them one by one. Shippers and railroads need more certainty as some of the issues have been open for years."

-Commissioner Deb Miller, August 10, 2015

August 18, 2015