BEFORE THE

SURFACE TRANSPORTATION BOARD

DOCKET NO. EP 711

PETITION FOR RULEMAKING TO ADOPT REVISED COMPETITIVE SWITCHING RULES

REPLY COMMENTS OF

ALLIANCE FOR RAIL COMPETITION
MONTANA WHEAT & BARLEY COMMITTEE
COLORADO WHEAT ADMINISTRATIVE COMMITTEE
IDAHO BARLEY COMMISSION
IDAHO WHEAT COMMISSION
MONTANA FARMERS UNION
NEBRASKA WHEAT BOARD
OKLAHOMA WHEAT COMMISSION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCERS BOARD
WASHINGTON GRAIN COMMISSION
WYOMING WHEAT MARKETING COMMISSION
NATIONAL ASSOCIATION OF WHEAT GROWERS

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In Opening Comments filed March 1, 2013 in this proceeding, Alliance for Rail Competition ("ARC") and the other shipper interests identified on the cover of these Reply Comments (hereafter collectively "ARC, et al.") predicted that the railroads would oppose the competitive switching for which NITL and other shippers seek a rulemaking proceeding. See Opening Comments of ARC, et al. at 14:

> It is a safe bet that the railroads' comments in the proceeding will not reflect broad, deep or any support for increased rail-to-rail competition. More likely is a call for access fees that guarantee the inability of second railroads to provide effective competition for incumbent railroads that now enjoy market dominance, high rates, high revenues and the freedom to provide poor service quality

This prediction was only partially correct. While the railroads in their opening comments did oppose any increase in rail-to-rail competition, their opposition did not rest on the poison pill of excessive access fees. Rather, the railroads and their witnesses make the extreme argument that competition itself is a bad thing for their industry. Even the opportunity to seek rail service by a competitor is, in the railroads' view, a threat to economic efficiency, profit maximization, and the long term best interests of railroads and shippers (both captive and non-captive). Accordingly, the railroads call on the Board to preserve the status quo.

As was made clear in the opening comments of ARC, et al., we do not regard enhanced opportunities for rail competition as a panacea. Many shippers that are members of or represented by ARC, et al. are too far from a second railroad to be able to benefit from implementation of the NITL proposal. Moreover, there has been ample evidence, in this proceeding and in others like Ex Parte No. 705, Competition in the Railroad Industry, that enabling railroads to compete with one another through access remedies may result in little or no increase in effective competition.

Put another way, access to a second railroad does not guarantee any reduction in rail rates, let alone a reduction in rail rates to reasonable levels. The railroads between which the formerly sole-served shipper has a choice may engage in conscious parallelism as to pricing, rather than price competition. Similarly, access to a second railroad may produce no improvement in service quality. Rather, the second railroad may decline to offer better service than the incumbent, out of a real or imagined concern that new competition at the site in question could lead the incumbent to compete with the second railroad elsewhere.

Based on these and other concerns, ARC, et al. have consistently called on the Board to improve the effectiveness of regulatory (as opposed to competitive) remedies for abuses of railroad market power, including unreasonable rates, charges and practices. However, it is important to note that ARC, et al. called for these reforms in addition to, rather than instead of, measures to increase effective rail competition.

ARC, et al. regard the regulatory and competitive status quo as entirely too favorable to major railroads with enormous market power. For decades, the vast majority of captive rail shippers have enjoyed neither the effective competition nor the effective regulation that Congress called for when it enacted the Staggers Rail Act of 1980.

Some of these deficiencies in the agency's implementation of its governing statute have their origin in policies and statutory interpretations of the Interstate Commerce Commission, during a period when the railroad industry may have needed more assistance in attaining revenue adequacy. However, by almost any responsible measure, the major railroads are exceeding revenue adequacy today, and yet continue to operate as they like, constrained neither by competitive forces nor by effective regulation.

The efficiency of the railroad industry has improved, and the railroads have invested heavily in infrastructure (albeit with revenues that come disproportionately from captive shippers). However, the railroads have frequently acted in ways that disserve the public interest, and that cannot be reconciled with the Rail Transportation Policy.

Examples include excessive rates, excessive charges, paper barriers, shifting costs and burdens to shipper customers, imposing fuel surcharges that collect more than the increased cost of fuel, attempting to evade their common carrier obligation, attempting to evade STB regulatory remedies through "gaming," using contracts of adhesion, etc.

A number of these practices are not unique to railroads, but they are particularly objectionable when the injured parties have no transportation alternatives, and no legal recourse other than regulatory recourse to the STB (because of the industry's antitrust immunity, which the railroads have lobbied hard to preserve).

ARC, et al. have more faith in improved regulation than in enhanced competition as a remedy for these abuses. However, it does not follow that NITL's proposed competitive switching remedy is unsound, as a matter of law or as a matter of policy. Even if it helps a relatively small number of captive shippers, more effective rail competition would represent progress. To the extent that competitive remedies are successful, i.e. lead to less excessive rates and/or better service quality, that success could lead to improved and expanded competitive remedies, as railroads learn to cope with, and benefit from, competition.

In arguing against increased rail-to-rail competition as inefficient, the AAR and other major railroads assume that the law favors efficiency over a competitive market. If this were the case, Wal-Mart and Target could reasonably argue that neither should open a store in a market served by the other. Imagine the efficiency gains if each retailer knew that every purchase of discount housewares and clothing in each town in which it operated would take place at its checkout counters. Inventories could be minimized, supply chains rationalized, fuel saved, parking lots and sales staffs optimized, etc. The same benefits could be achieved if all groceries, gasoline, hardware, office supplies, and automobiles were sold by a single dominant retailer. But this is not the economic model this country has chosen.

At page 32 of its Opening Comments, the AAR offers a different analogy, arguing that it would be inefficient for the government to mandate that Wal-Mart turn over part of each store to Target, to promote competition. But the government has promoted competition in the electric utility industry by requiring utilities to offer transmission and distribution of power generated by others over the utilities' networks of power lines.

As the foregoing example shows, it is fallacious to suggest that competition should be trumped by efficiency considerations when dealing with network industries. In addition to the Staggers Act (and the earlier 4-R Act of 1978), consider the Airline Deregulation Act of 1978 (abolishing economic regulation of air carriers by the CAB), the Motor Carrier Act of 1980, the Telecommunications Act of 1996, FERC initiatives partially deregulating the natural gas pipeline industry (and preserving effective economic regulation where necessary), etc. Many, if not most, of the industries deregulated in whole or in part in recent decades have been network industries, and many, if not most, have argued that increased competition would do more harm than good.

These arguments, which were rejected, were certainly partly pretexts for industries seeking to preserve supra-competitive profits.[*] ARC, et al. can concede that there could be inefficiencies associated with competition. However, the tendency over time is for competition to produce better service at lower cost, as has happened in the highly competitive, and highly effi-

[*] Notably, AAR Witnesses Eakin and Meitzen are candid enough to argue against the NITL proposal because it might undermine unconstrained profit maximizing pricing. V.S. at 15.

cient, U.S. trucking industry. What is missing from the railroads' opening comments is any acknowledgement that there can also be inefficiencies associated with monopolies.

Where competition is absent, railroads are able to use pricing, or refusals to provide needed services, equipment or service quality, as means of steering shippers' traffic over routings that suit the interests of the railroads, rather than the interests of producers and buyers of coal, wheat, autos, chemicals, and any of the other commodities that move primarily by rail. Railroads can use and have used the same techniques to promote 100 car loading facilities over smaller facilities, and have utilized the same techniques to discourage the construction of factories in locations that maximize production efficiency but are suboptimal from the perspective of railroad operating efficiency. By extracting monopoly rents from captive shippers, many of which cannot afford to bring STB rate cases, railroads can arrogate to themselves resources that would, in a more efficient economy, go to shipper entrepreneurs. At worst, monopoly railroads can determine which companies and towns survive and which do not.

It was this unrestricted market power of the early railroads that led to enactment of the original 1887 Act to Regulate Commerce, better known as the Interstate Commerce Act. While no one advocates a return to pervasive regulation of the type that Act produced, shippers favor measures to increase effective competition, i.e., competition which makes regulation unnecessary. In this regard, the Board should bear in mind its obligation to take into consideration national antitrust policies, which favor competition over monopoly. See, e.g., STB Ex Parte No. 582 (Sub-No. 1), Major Rail Consolidation Procedures, decision served October 3, 2000 at 14. The railroads oppose additional effective competition, despite national policy calling for competition to the maximum extent possible. Shippers also support more effective regulation, where effective competition is absent. Railroads also oppose this.

The railroads cannot have it both ways. If even the modest increase in competition proposed by NITL is not to be implemented, the case becomes all the stronger for more effective regulatory remedies – against unreasonable railroad rates, charges and practices – for the thousands of captive shippers with no other means of countering abuses of railroad market power. To the extent that safeguards are in place against unreasonable rail rates on captive traffic, there should be fewer adverse rate impacts of expanded competitive switching on captive shippers who cannot take advantage of new competition And shippers unable to employ competitive switching may experience no reduction in service quality if other shippers are able to benefit. Diversion of freight from monopoly railroads to new rail competitors granted access through competitive switching may mean that the former monopoly rail carriers have equipment and crews available for use elsewhere on their systems.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this 30th day of May, 2013, caused copies of the foregoing document to be served on all parties of record by first class mail.

John M. Cutler, Jr.

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