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SERVICE DATE – LATE RELEASE APRIL 14, 2009

SURFACE TRANSPORTATION BOARD

NOTICE

STB Ex Parte No. 688

POLICY ALTERNATIVES TO INCREASE COMPETITION  
IN THE RAILROAD INDUSTRY

AGENCY: Surface Transportation Board.

ACTION: Notice of Public Hearing.

SUMMARY: The Surface Transportation Board will hold a public hearing beginning at 9:00 a.m. on Monday, May 18, 2009, and Tuesday, May 19, 2009, at its headquarters in Washington, DC. The purpose of the public hearing will be to examine issues related to access and competition in the railroad industry. Persons wishing to speak at the hearing should notify the Board in writing.

DATES: The public hearing will take place on Monday, May 18, and Tuesday, May 19, 2009. Any person wishing to speak at the hearing should file with the Board a combined notice of intent to participate (identifying the party, the proposed speaker, the time requested, and the topic(s) to be covered) and the person's written testimony, as soon as possible, but no later than May 11, 2009. Written submissions by interested persons who do not wish to appear at the hearing will also be due by May 11, 2009.

ADDRESSES: All filings may be submitted either via the Board's e-filing format or in the traditional paper format. Any person using e-filing should attach a document and otherwise comply with the Board's "www.stb.dot.gov" website, at the "E-FILING" link. Any person submitting a filing in the traditional paper format should send an original and 10 copies of the filing to: Surface Transportation Board, Attn: STB Ex Parte No. 688, 395 E Street S.W., Washington, DC 20423-0001.

FOR FURTHER INFORMATION, CONTACT: Timothy J. Strafford, (202) 245-0356.  
[Assistance for the hearing impaired is available through the Federal Information Relay Service (FIRS) at: (800) 877-8339.]

SUPPLEMENTARY INFORMATION: The rail network in the United States is a series of interconnected lines owned by various rail carriers. Because of the high fixed cost associated with building a rail network, sometimes there is only one railroad serving a particular destination and origin. Some companies that either ship by rail (or would like to do so) have complained about being physically limited to a single rail carrier and would like to have greater access to competition from other railroads. Some shippers have suggested that mandated access by a

second carrier to singly served businesses would be in the public interest. Railroads have responded that such an action would undermine their ability to price their services differentially based on demand and that, as a result, they would be unable to earn enough revenue to be able to invest sufficiently in their networks. Over the years, various possible measures that would change the way rail shippers currently obtain access to rail service have been debated, including: (1) requiring railroads to quote a rate between any two points they serve to allow another railroad to serve the shipper from an intermediate point to the final destination; and (2) imposing some form of competitive access, such as mandated reciprocal switching and mandated terminal use arrangements, including trackage rights.

It has been some time since the agency has conducted a comprehensive analysis of these issues. More than a decade ago, the Board conducted a comprehensive analysis of “captive shippers” and their available remedies for rate relief, as well as the incumbent railroad’s rights and obligations, in a group of cases known as the “Bottleneck cases.”<sup>1</sup> The Board also conducted some review of its competitive access standards, which were adopted by the ICC, the Board’s predecessor agency, in the mid-1980s,<sup>2</sup> in its Review of Rail Access and Competition Issues proceeding in the late 1990s.<sup>3</sup> More recently, the Christensen Study,<sup>4</sup> an independent study performed for the Board by Christensen Associates, Inc., examined these issues (see Christensen Study, Volume 3, Chapter 22, and Table 22-1). It is time for the Board to consider them again as well.

The Bottleneck Issue. A rail bottleneck rate issue arises when more than one railroad can provide service over at least a portion of the movement from an origin to a destination, but where either the origin or destination is served by only one carrier, i.e. the bottleneck carrier. In each of the three “Bottleneck cases,” an electric utility company sought to require the bottleneck carrier to establish a “local rate” for a segment of the through movement that was served only by that carrier so that the utility could combine that local rate with a rate for the remainder of the movement by another carrier. The utilities further sought to be able to separately challenge the reasonableness of the rate for the bottleneck segment of the movement, rather than having to challenge the full origin-to-destination rate in its entirety. Each of the utilities in the Bottleneck cases wanted to break up the bottleneck carrier’s long-haul and the through rate into smaller portions that could be challenged independently. The utilities believed that the total charges

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<sup>1</sup> Central Power & Light Co. v. Southern Pacific et al., 1 S.T.B. 1059 (1996) (Bottleneck I), clarified, 2 S.T.B. 235 (1997) (Bottleneck II), aff’d sub nom. MidAmerican Energy Co. v. STB, 169 F.3d 1099 (8th Cir. 1999).

<sup>2</sup> See Intramodal Rail Competition, 1 I.C.C.2d 822 (1985), aff’d sub nom., Baltimore Gas & Electric Co. v. United States, 817 F. 2d 108 (D.C. Cir. 1987); Midtec Paper Corp v. Chicago & N.W. Transp. Co., 3 I.C.C.2d 171 (1986), aff’d sub nom. Midtec Paper Corp. v. United States, 857 F.2d 1487 (D.C. Cir. 1988) (Midtec).

<sup>3</sup> See Review of Rail Access and Competition Issues, 3 S.T.B. 92 (1998).

<sup>4</sup> A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals That Might Enhance Competition (Christensen Study), available on the Board’s web site or at <http://www.lrca.com/railroadstudy/>.

would be lower if the reasonableness of the rates were adjudicated only for the bottleneck portion of the movement (with the rate set by head-to-head rail competition for the remainder of the movement) rather than for the entire movement. Because the Bottleneck cases raised issues of broad importance, the Board provided for extensive public input and held an oral argument.

In its resulting decisions, the Board concluded that a shipper could not routinely direct a bottleneck carrier that was capable of providing origin-to-destination rail service to "short-haul" itself by routing traffic over the lines of the non-bottleneck carrier. Rather, the Board held that a shipper could seek to force an alternative routing that would include the line of the non-bottleneck carrier, if it could show, under 49 U.S.C. 10705 and the Board's "competitive access" rules developed in Intramodal Rail Competition (supra n.2), that there would be sufficient benefits associated with the alternative routing. The Board also held that, under 49 U.S.C. 11101(a) and 49 U.S.C. 10742, a bottleneck carrier generally cannot refuse traffic from other carriers originating at sources that the bottleneck carrier does not serve, even if the bottleneck carrier can carry the identical commodity in its own single-line service from another source.

Finally, for either type of movement – same-source movements for which a shipper has forced an alternative routing or different-source movements that the bottleneck carrier cannot handle in single-line service – the Board held that it could not force the bottleneck carrier to quote a separately challengeable rate for the bottleneck segment unless the shipper had entered into a rail contract for the non-bottleneck segment. The Board based its decision on a 1935 Supreme Court decision, Great Northern Ry. Co. v. Sullivan, 294 U.S. 458, 463 (1935), which held that the reasonableness of through rates established by carriers should be evaluated from origin-to-destination, rather than on a segment-by-segment basis.

Competitive Access. Competitive access can take the form of mandated reciprocal switching, terminal use, or trackage rights. Reciprocal switching involves the incumbent railroad transporting traffic, usually for a short distance, over its own track on behalf of a competing railroad for a fee. Reciprocal switching thus enables the competing railroad to offer its own single-line rate, even though it cannot physically serve the shipper's facility, to compete with the incumbent's single-line rate. The agency has in the past held that the reciprocal switching provisions of the statute should not be ordered absent a showing of competitive abuse. See Midtec, supra n.2.

Unlike reciprocal switching, forced terminal arrangements (including trackage rights) involve the physical presence of a competing carrier on a host carrier's facilities owned by the incumbent railroad. Under terminal agreements, an incumbent railroad grants access to its terminal facilities or tracks to another carrier's trains for a fee so that the non-incumbent can serve traffic it would otherwise be unable to access. In order to obtain mandatory terminal access or trackage rights remedies on a permanent basis, Board precedent established that a shipper must show that such access is needed to remedy anticompetitive conduct by the incumbent railroad. More specifically, under the policy adopted in the Board's Midtec case, the complaining party must show that the incumbent railroad has used its market power to extract unreasonable terms or, because of its monopoly position, has shown a disregard for the shipper's needs by rendering inadequate service.

This Hearing. This hearing is intended as a public forum to allow interested persons to comment on the current issues stemming from the agency's Bottleneck and competitive access decisions, the continuing propriety of the Board's policies on competitive access, the effects on rates and service these policies have had, and the possible implications of changing these policies. Parties should focus their testimony and statements on the following questions:

1. What is the extent of movements affected by the Board's competitive access policies – for example, how much traffic moves over bottleneck segments? Where are the bottleneck segments most critical – any particular geographical regions, or divisions on particular carriers? Which shippers are most affected by the policies?
2. Do carriers ever set separate bottleneck segment rates without the shipper having a contract on the non-bottleneck segment? To what extent do carriers set voluntary "Rule 11"<sup>5</sup> rates for bottleneck segments? To what extent are Rule 11 rates different from bottleneck segment rates?
3. To what extent and under what circumstances do carriers voluntarily engage in reciprocal switching or terminal use arrangements, including trackage rights arrangements?
4. Under 49 U.S.C. 10101(6), it is the policy of the U.S. government "to maintain reasonable rates where there is an absence of competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and attract capital." Please comment on the relationship between revenue adequacy and bottleneck-rate and competitive-access relief. Should the Board's competitive access policies be different for a carrier deemed to be revenue adequate? What would be the impact of such different policies on differential pricing and the ability of the industry to achieve adequate revenues?
5. Please comment on the benefits and costs of the current competitive access policies and the benefits and costs of changing those policies. How would the transportation world change if the bottleneck policy were modified to permit segment rate challenges, and if competitive access were mandated with incumbent carriers receiving access fees at or near the incremental cost level? What would be the likely impacts on transportation efficiency, rail investment incentives, and rail industry coordination? Would the establishment of bottleneck rates or mandated reciprocal switching, terminal agreements, or trackage rights actually lead to competitive responses from non-incumbent carriers? Could these changes elicit retaliation by carriers at other facilities of shippers taking advantage of bottleneck relief? How would these requirements impact the bargaining power of large shippers and railroads? What would be the likely gains for shippers? Would quality of service improve for the captive shipper?
6. Should any requirement for a carrier to quote bottleneck segment rates be related to the length of the bottleneck segment? More specifically, is there any basis for a requirement to quote

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<sup>5</sup> Rule 11 is an accounting procedure under the Railway Accounting Rules promulgated by the Association of American Railroad's accounting division. Rule 11 refers to the practice of separately billing for rail charges by each carrier in a through movement. When a carrier sets a Rule 11 rate, the shipper will get a freight bill from each rail carrier that transports the load. The rules are binding upon carriers operating in North America that are members of the division.

bottleneck segment rates only on short bottlenecks, as the Christensen study suggests? See Christensen Study, Vol. 3, at 22-7.

7. Would changes to the Board's competitive access policies require legislative changes such as overturning the Great Northern decision? Would such a change require accompanying changes to the Board's regulations and procedures?
8. How would a carrier's refusal to quote a bottleneck segment rate be analyzed under the federal antitrust laws? Would such conduct constitute an unlawful tying arrangement, tying the provision of one transportation service where the carrier has market power to another distinct service/product where there are competitive alternatives? Because our statute, as interpreted by the Great Northern line of cases, grants a carrier the right to refuse to set a separately challengeable bottleneck rate, does that right trump any general prohibition against tying in the federal antitrust laws?
9. Since changes to existing "bottleneck" and access policy would likely increase the amount of interchange transactions, how should railroads be compensated for being required to handle a competitor's traffic? How should the Board review complaints related to such compensation and related service issues?
10. What private property rights and "takings" considerations should the Board be aware of when considering new policies in these areas?

Date of Hearing. The hearing will begin at 9:00 am on Monday, May 18, 2009, and continue on Tuesday, May 19, 2009, in the 1st floor hearing room at the Board's headquarters at 395 E Street, S.W., in Washington, DC, and will continue until every person scheduled to speak has been heard.

Notice of Intent to Participate and Testimony. Any person wishing to speak at the hearing should file with the Board a combined notice of intent to participate (identifying the party, the proposed speaker, the time requested, and the topic(s) to be covered) and the person's written testimony, as soon as possible, but no later than May 11, 2009. Written submissions by interested persons who do not wish to appear at the hearing will also be due by May 11, 2009.

Board Releases and Live Video Available Via the Internet. Decisions and notices of the Board, including this notice, are available on the Board's website at "www.stb.dot.gov." This hearing will be available on the Board's website by live video streaming. To access the hearing, click on the "Live Video" link under "Information Center" at the left side of the home page beginning at 9:00 a.m. on Monday, May 18, 2009, and Tuesday, May 19, 2009.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

Dated: April 14, 2009.

Anne K. Quinlan  
Acting Secretary