



U.S. Department of  
Transportation  
Office of the Secretary  
of Transportation

General Counsel

1200 New Jersey Avenue, S.E.  
Washington, D.C. 20590

229200

April 12, 2011

Ms. Cynthia Brown  
Chief of the Section of Administration  
Surface Transportation Board  
395 E Street, S.W.  
Washington, D.C. 20423

ENTERED  
Office of Proceedings

APR 12 2011

Part of  
Public Record

Re: Ex Parte No. 705

Dear Ms. Brown:

Enclosed herewith for filing in the above-referenced proceeding please find the Initial Comments of the United States Department of Transportation and the United States Department of Justice.

Please contact me if you have any questions.

Respectfully,

  
PAUL SAMUEL SMITH  
Senior Trial Attorney

(202) 366-9280

Enclosure

**Before the  
Surface Transportation Board  
Washington, D.C.**

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Competition )  
in the )  
Railroad Industry )  
\_\_\_\_\_)

Docket No. Ex Parte 705

**Initial Comments of the  
United States Department of Transportation  
and the  
United States Department of Justice**

Introduction

The Surface Transportation Board (“STB” or “Board”) has instituted this proceeding in order “to explore the current state of competition in the railroad industry and possible policy alternatives to facilitate more competition, where appropriate.” Notice was served January 11, 2011 (“Notice”). Specifically, the Board has invited written comments on legal, factual, and policy issues related to captive shippers and competitive access. It has been many years since the STB has reviewed most of these issues. The Board must assess the dimensions of competition and fashion regulatory relief, where appropriate, that takes into account the revenue requirements of the railroads on the one hand and the need to ensure reasonable rates and services for rail customers on the other. *See* 49 U.S.C. § 10101.

The United States Department of Transportation (“DOT”) and the United States Department of Justice (“DOJ”) (collectively, “the Agencies”) appreciate the difficulties this task presents. We are participating jointly in this proceeding to try to assist the STB by presenting a unified perspective rather than disparate views. In these initial comments, the Agencies will outline their general thoughts and concerns. If, after considering the comments of other parties,

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<sup>1</sup> *See, e.g.,* Government Accountability Office, *Railroad Regulation Current Issues Associated with the Rate Review Process*, GAO-RCED-99-46, February 26, 1999 at 3 (approximately 82 percent of rail rates not subject to STB’s jurisdiction); and *Freight Railroads: Industry Health Has Improved, but Concerns About Competition and Capacity Should be Addressed*, GAO-07-94, October 6, 2006 at 24 (70 per cent of rail tonnage and 71 percent of rail

the Agencies believe they can offer additional views useful to the STB regarding specific issues, we will do so in reply comments.

### Background

Through the Railroad Revitalization and Regulatory Reform Act of 1976 (“4R Act”) and the Staggers Rail Act of 1980 (“Staggers Act”), Congress made clear that it wanted to significantly alter the regulatory regime governing the rail industry. These statutes sought to restore the financial health of the industry by minimizing Federal regulatory control and maximizing the role of competition, granting carriers flexibility in establishing rates and offering innovative services so as to generate the revenues necessary for capital investment to ensure a safe and efficient rail transportation network. In general, maximizing the role of competition in an industry is a desirable goal.

The Staggers Act put contracts between shippers and their rail carriers beyond the reach of Federal regulation, encouraged exemptions from regulation for those classes and types of rail transportation subject to effective competition, and established rate thresholds below which Federal regulators had no jurisdiction. 49 U.S.C. §§ 10709, 10502, and 10707, respectively. These reforms ultimately resulted in removing a substantial percentage of rail traffic (estimates have ranged between 75 to 85 percent) from economic regulation.<sup>1</sup> Residual regulation focused on maintaining reasonable rates and services where there was an absence of effective competition.

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<sup>1</sup> See, e.g., Government Accountability Office, *Railroad Regulation Current Issues Associated with the Rate Review Process*, GAO-RCED-99-46, February 26, 1999 at 3 (approximately 82 percent of rail rates not subject to STB’s jurisdiction); and *Freight Railroads: Industry Health Has Improved, but Concerns About Competition and Capacity Should be Addressed*, GAO-07-94, October 6, 2006 at 24 (70 per cent of rail tonnage and 71 percent of rail industry revenue moved under contract)—to which must be added exempt traffic and traffic below the statutory revenue-to-variable cost ratio.

Although captive shippers bear the brunt of the deregulated industry's differential pricing, *Coal Rate Guidelines, Nationwide*, 1 I.C.C.2d 520, 526-27 (1985), the rates and services such shippers receive must nonetheless be "reasonable" and must not reflect an abuse of market power. Yet captive shippers have consistently charged in recent years that their rates and/or services are often unreasonable and that existing precedent often offers them no real protection. They allege as well that, notwithstanding recent changes for resolving small and medium-size disputes, the costs of pursuing a rate case remain high, particularly for shippers of a variety of commodities going to numerous destinations. It is these ongoing complaints that have prompted this proceeding and the issues it raises.

#### The Agencies' Perspective

DOT and DOJ share the widespread view that the 4R Act and the Staggers Act and the reforms they introduced have produced substantial benefits for railroads, shippers, and the public at large. They have fostered both an efficient, viable rail industry and a decline in average rail rates over more than twenty years. *Bureau of Labor Statistics Producer Price Index Industry Data*, <http://data.bls.gov/cgi-bin/srgate> (PCU482111482111); *Bureau of Economic Analysis*, Table 1.1.4 Price Indexes for Gross Domestic Product. But these declines ended in 2004 and average rates increased until 2009. *Id.* Similarly, decades of excess rail system capacity ended in 2006, and localized capacity constraints with their attendant impact on rail rates became a concern.<sup>2</sup> See, e.g., *Supplemental Report on Capacity and Infrastructure Investment*, Ex Parte No. 680 (Sub-No. 1), Notice served April 8, 2009.

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<sup>2</sup> The 2008 recession eased such restraints, but as the U.S. economy recovers they are expected to reappear.

It is important that the nation's railroads remain free to innovate, reduce costs, and continue to invest in system capacity.<sup>3</sup> It is just as important that rail shippers receive reasonable rates and services that they need. Where possible, those outcomes should be left to market forces. Where that is not the case, the Board must strive to approximate such outcomes. The tension inherent in the STB's responsibility requires it to exercise deft judgment on matters of law, economics, and policy.

The Agencies believe it is appropriate to investigate the extent to which relevant circumstances (such as rail capacity constraints, industry consolidation, and increasing revenue adequacy) have changed, and whether a proper balance of these or other considerations warrants different policy choices (e.g., on rate regulation or access or trackage rights) to serve the same underlying statutory goals. The principles adopted by the Interstate Commerce Commission shortly after passage of the Staggers Act, and adhered to by the Board since then, remain important. The STB's task here, however, is to ensure that these principles are properly applied under present circumstances, and to determine whether and to what extent other factors need to be considered. The principles derive from the *Coal Rate Guidelines* proceeding, and may be summarized as follows:

- 1 - Shippers should not be required to pay more than necessary for carriers to earn adequate revenues;
- 2 - Shippers should not pay more than is necessary for efficient service;
- 3 - Shippers should not pay for facilities or services that do not benefit them;
- 4 - Responsibility for payment of facilities should be based on demand elasticities of each shipper.

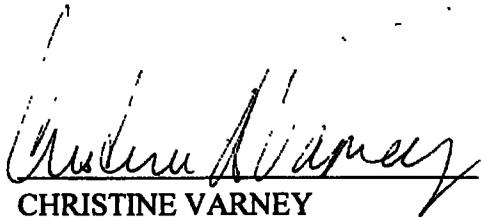
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<sup>3</sup> Railroad capital investment in the last five years has grown from \$6.4 billion to more than \$10 billion. *Association of American Railroads, Railroad Facts: 2010 Edition*, p. 44.

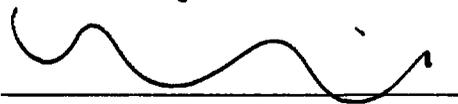
The Agencies urge the STB to consider the extent to which current circumstances warrant a different application to achieve its underlying statutory mission.

DOJ and DOT look forward to reviewing the initial comments of other parties, and to the development of a comprehensive record in this proceeding.

Respectfully submitted,



**CHRISTINE VARNEY**  
Assistant Attorney General, Antitrust Division  
U.S. Department of Justice



**ROBERT M. RIVKIN**  
General Counsel  
U.S. Department of Transportation

April 12, 2011