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BEFORE THE

U.S. SENATE JUDICIARY COMMITTEE
SUBCOMMITTEE ON ANTITRUST, COMPETITITION POLICY
AND CONSUMER RIGHTS

AT A HEARING ENTITLED

"AN EXAMINATION OF S. 772, THE RAILROAD ANTITRUST ENFORCEMENT ACT"

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Testimony of Charles D. Nottingham
Chairman of the Surface Transportation Board before the Senate Judiciary Committee, Subcommittee on Antitrust, Competition Policy and Consumer Rights
At a Hearing Entitled
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Good Morning Chairman Kohl, Ranking Member Hatch and Members of the Subcommittee. My name is Charles Nottingham, and I am Chairman of the Surface Transportation Board (Board or STB). I appreciate the opportunity to appear before this Subcommittee today to provide the Board's views on S. 772, the Railroad Antitrust Enforcement Act.

Before providing the Board's views on the proposed legislation, I will first provide an overview of the Board, its responsibilities with respect to competition, and the current limited immunities from the antitrust laws that apply to rail carriers.

OVERVIEW OF THE SURFACE TRANSPORTATION BOARD

The STB is charged by statute with resolving railroad rate and service disputes and reviewing railroad restructuring transactions (including mergers, line sales, line constructions and line abandonments). The Rail Transportation Policy in the Board's governing statute addresses the role of competition; it requires, among other things, that the Board regulate in such a manner "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail," and, while "minimiz[ing] the need for Federal regulatory control over the rail transportation system," acting so as to "maintain reasonable rates where there is an absence of effective competition." *See* 49 U.S.C. § 10101.

When Congress passed the Staggers Act in 1980, the Nation's rail system was in desperate financial straits. It was burdened with unproductive assets, forced to provide unprofitable services, and hampered by excessive government regulation. The industry consisted of many independent systems throughout the Nation, none of them particularly healthy or efficient. Since that time, the Board and its predecessor, the Interstate Commerce Commission (ICC), have approved mergers with competition-protecting conditions – almost always with the concurrence of the U.S. Department of Justice (DOJ) – that reduced the number of large (or Class I) U.S. railroads to seven. But those seven systems are far healthier and more efficient than the more numerous carriers that existed in 1980. Indeed, the railroad industry's financial condition has steadily improved and today the industry is considered by most independent analysts to be relatively healthy. In addition, more that 500 smaller "shortline" railroads currently operate in the U.S. and often enhance competition in the market for freight transportation.

Last month the Board initiated a $1 million national study on the state of competition in the rail industry. The study will also assess various policy issues, including current and near-future capacity constraints in the industry; how competition and regulation impact capacity investment; how capacity constraints impact competition; and how competition, capacity constraints, and other factors affect the quality of service provided by railroads. The economic consulting firm Christensen Associates, based in Madison, Wisconsin, has contracted to deliver this study in the Fall of 2008.

What we already know is that in 2005 (the most recent year for which adequate data are available), over 71% of the traffic that the railroads carried moved at rates less than 180% of variable cost and is thus deemed by statute to have been the result of a

competitive market. Of the remaining 29% of rail traffic that moved at revenue-to-variable cost ratios above 180% that year, some was traffic that was exempted from regulation pursuant to 49 U.S.C. § 10502, based on findings that the particular commodities and services involved have competitive transportation alternatives available, and some was traffic that moved under contract and was therefore, by statute, outside of the Board's jurisdiction. Thus, the rail industry is now governed by a hybrid system of partial regulation when shippers have competitive options and extensive economic regulation where such competition is not present.

When enforcing competition policy under the Interstate Commerce Act (ICA), the Board is guided by, but not limited to, the traditional antitrust principles in the Sherman and Clayton Acts. Congress has delegated to the Board discretionary authority to enforce certain provisions of the Clayton Antitrust Act, including Section 7, which governs mergers. In practice, the Board reviews acquisitions under its own statutory standard and merger guidelines, typically with comments from DOJ in major cases. The main difference between the Board's review of mergers and those of DOJ or the Federal Trade Commission (FTC) is that the Board, under the broad public interest standard, is required to consider other factors in addition to competition, including: the adequacy of transportation to the public, the effects on other carriers, rail labor issues, environmental issues, and whether the rail industry can earn adequate revenues to support capital infrastructure investment. Thus, the Board's oversight of competition and mergers in the freight rail industry takes into account both traditional antitrust principles and special characteristics of the rail industry.

Although the Board does not have the authority to directly enforce the Sherman Act, many of the *per se* violations of Section 1 of that Act, including horizontal price-fixing and bid-rigging, would likely also violate provisions of the ICA, including section 10702's prohibition of unreasonable practices. The Board has exclusive jurisdiction to enforce those provision of the ICA, and upon the filing of a complaint has broad investigative and remedial powers to enforce the provisions against the railroads.

RAILROAD ANTITRUST EXEMPTIONS

There is a wide-spread misconception that the railroads are not subject to the antitrust laws. That is not so. For example, in the 1980s, a massive civil antitrust lawsuit was brought against numerous railroads by a civil plaintiff.[1] In that case, a jury returned a $1 billion verdict in treble damages against the only railroad that elected not to settle that litigation, which I understand was, at the time, the largest civil, antitrust jury verdict in U.S. history. The railroad subsequently settled the case. Moreover, DOJ can investigate and prosecute the railroads for civil or criminal sanctions if they violate the Sherman Act (e.g., price-fixing, market allocation, bid-rigging). In 2005, the New York Times reported that two large railroads were under investigation by DOJ for possible violations of the antitrust laws.[2] And the railroads can be and have been sued by private parties in federal district court for violating the Sherman Act.[3]

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[1] *See In re Burlington N., Inc.*, 822 F.2d 518 (5th Cir. 1987).

[2] *See Two Railroads Under Antitrust Investigation for Rates*, N.Y. TIMES, Feb. 17, 2005.

[3] *See In re Lower Lake Erie Iron Ore Antitrust Litigation*, 998 F.2d 1144 (3d Cir. 1993); *Laurel Sand & Gravel v. CSX Transp.*, 924 F.2d 539 (4th Cir. 1991); *Transkentucky Transp. R.R. v. Louisville & Nashville R.R.*, 581 F. Supp. 759 (E.D. Ky. 1983). The Class I railroads are currently defendants in dozens of class actions alleging that the railroads colluded in establishing fuel surcharge programs. *See, e.g.*, *Dust Pro,*

Rail carriers do, however, enjoy several limited express statutory and judicially-created immunities from the antitrust laws. In this regard, the railroad industry is no different than numerous other industries that have narrow immunities created by Congress designed to serve a particular public purpose, such as air transportation (49 U.S.C. §§ 41308-09), insurance (15 U.S.C. §§ 1011-15), natural gas (15 U.S.C. § 3364(e)), or labor (15 U.S.C. § 17, 29 U.S.C. §§ 52, 101-15, 151-69). Recently, the Antitrust Modernization Commission identified more than 30 exemptions created by statutes or the courts.

In brief, relevant exemptions addressed in S. 772 are:

- **Express immunity for certain transactions approved by the STB.** A rail carrier participating in a transaction approved by the STB under 49 U.S.C. § 11321 et seq. is exempt from the antitrust laws to the extent necessary to carry out the transaction. 49 U.S.C. § 11321(a); 15 U.S.C. § 18. Such transactions include consolidations, mergers, acquisitions, leases, trackage rights, pooling arrangements and agreements to divide traffic. This immunity is part of a broader set of preemptions in the statute designed to protect the national, public interest in ensuring the free flow of interstate commerce by preventing parties that do not want to see an increased rail presence in their communities from blocking or delaying those transactions with hundreds of individual suits in every local jurisdiction affected by the transaction.
- **Express immunity for certain rate-related agreements approved by the STB.** Under 49 U.S.C. § 10706, the STB has the authority to grant antitrust immunity for certain agreements related to rates or charges. For example, the STB has approved an agreement between the railroads that establishes rules governing the charges that railroads pay each other when using the equipment (typically rail cars) of another railroad. The authority is narrow and the Board cannot authorize rail carriers to discuss or participate in agreements related to single-line rates, or to interline rates of a particular movement unless the rail carrier can practicably participate in the movement.
- **Express immunity from injunctive relief in private civil actions.** Only the federal government, not private parties, may bring suit for injunctive relief against any common carrier subject to STB jurisdiction. DOJ has broad powers to pursue injunctive relief against the railroads. The purpose of this prohibition is to ensure

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Inc. et al. v. CSX Transp. et al., Civ. Action No. 07-2251 (D.N.J., complaint filed May 14, 2007).

that the national, public interest in protecting the efficient operation of the national rail network is not stymied by a patchwork of narrow, parochial interests.

- **Express immunity from the Federal Trade Commission Act.** The FTC Act creates no private right of action, and provides that the FTC has no jurisdiction over common carriers, including but not limited to rail carriers. Thus, the prohibition in Section 5 of the FTC Act against "unfair methods of competition" does not apply to the railroads. Other common carriers (a category that includes airlines, telecommunication firms, and pipelines) are also not regulated by the FTC. Some are also regulated by specialized federal agencies (such as the Federal Energy Regulatory Commission (FERC)), but most common carriers operate with much less federal regulatory oversight than the freight railroad industry.
- **Judicially Created Immunity from Treble Damages.** Historically, the railroads have enjoyed immunity from rate-related antitrust civil damages suits under the *Keogh* doctrine. Created by the courts in 1922, the doctrine is premised on the idea that tariffs filed with the ICC should be immune from challenge, except before the agency. But because railroads no longer file tariffs, a leading antitrust treatise has questioned whether the *Keogh* doctrine still applies to the railroads.[4]

The Board has already provided its initial views on two provisions of S. 772 at the request of the Senate Committee on Commerce, Science and Transportation and the Subcommittee on Surface Transportation and Merchant Marine Infrastructure, Safety and Security. I am glad to expand on those comments below and to provide my views on other parts of the proposed legislation. I have attached that September 13, 2007 letter to my written testimony before this Subcommittee.

ANALYSIS OF THE PROPOSED LEGISLATION

The STB believes that railroads should be governed by and subject to our Nation's antitrust laws. The core premise underlying antitrust policy – "that the unrestrained interaction of competitive forces will yield the best allocation of our economic resources, the lowest prices, the highest quality and the greatest material

[4] *See* ABA SECTION OF ANTITRUST LAW, ANTITRUST LAW DEVELOPMENTS at 1402 n.1135 (5th ed. 2002) (questioning "future relevance" of *Keogh* after ICCTA).

progress"[5]– is certainly applicable to the rail industry. The concerns I express today about S.772 relate not to whether that maxim should apply in greater or different force to rail carriers. Rather, there are practical problems that can arise when the antitrust laws are layered atop a regulatory regime. The ICA shares the same core purpose of promoting free market competition whenever possible and protecting rail customers from market power abuses. But we must also take into account the other public policy issues set forth in the national rail transportation policy (49 U.S.C. § 10101) in providing a single, overarching public interest view in regulating the complex national rail system.

The STB does not believe that immunities once granted under particular economic and legal circumstances should remain in place regardless of changes in the economic and legal environment that occur over time. I agree with the suggestion by the Antitrust Modernization Commission in its April 2007 report to Congress and the President that it is critical to reassess existing antitrust immunities and consider whether the original justifications for them continue to hold true and whether they serve a public interest that cannot be furthered by the imposition of the antitrust laws.

In May of this year, the Board did just that with regard to motor carrier rate bureaus, using our discretion to terminate antitrust immunities that had been routinely granted since 1948.[6] The motor carrier industry has long operated with collective ratemaking as its backbone, in which regional rate bureaus develop collective rates and suggest general rate increases to its members. The collectively set rates are not the actual

[5] *Northern Pacific Ry. v. U.S.*, 356 U.S. 1, 4 (1958).

[6] *Motor Carrier Bureaus – Periodic Review Proceeding*, STB Ex Parte No. 656 *et al.* (STB served May 7, 2007) (the decision becomes effective January 1, 2008).

market prices charged by the motor carriers, but served as a baseline for negotiations between individual shippers and carriers.

In the Board's review proceeding, the motor carrier bureaus urged continuation of their antitrust immunities based on a set of familiar arguments: that there could be no harm to consumers because carriers routinely discount from the collective rates, that the rate bureau system "simplified" transactions, and that continued Board conditioning and monitoring of rate bureau agreements was the best way to protect the public interest. The Board rejected each of these arguments, finding that the motor carrier industry had become so deregulated and so competitive as to make the antitrust-immunized collective ratemaking system obsolete and contrary to free-market principles. Thus, the original justification for rate bureau immunity, which centered on a pervasive regulatory environment, no longer made sense when that regulatory environment disappeared. The Board also concluded, as did the DOJ and Department of Transportation (DOT), that the bureau system likely leads to higher rates than might otherwise be charged.

With this decision, the STB ended more than 70 years of antitrust immunity for motor carrier rate bureaus, demonstrating its commitment to and respect for the antitrust laws. As Congress now takes a new look at rail regulation issues, it makes sense to reassess antitrust immunities as well, including how these long-standing immunities fit in with today's regulatory environment and whether the public interest would be better served by repealing or adjusting certain immunities.

The Board's analysis of S. 772 is set forth in three parts. First, I will go through the sections of the bill that I believe have either no impact or a positive impact on the STB's regulatory efforts. Second, I will discuss those parts of the bill that would make

effective integrated economic regulation of the rail industry more difficult and complicated. Third, I will discuss those parts of the bill that raise significant questions.

I. Immunities That Can Be Repealed With A Positive Or Neutral Effect On The Board's Statutory Responsibilities

A. The *Keogh* Doctrine's Limit on Treble Damages

Section 6 of the bill would repeal the *Keogh* doctrine, derived from the Supreme Court's 1922 decision in *Keogh v. Chicago & N.W. Railway*.[7] *Keogh* held that a filed tariff was the only legal rate, and that the rate could only be adjusted by the regulator. The Court stated that even a rate that was the result of a conspiracy under the antitrust laws was not illegal if it had been filed and approved by the regulatory agency. The Court believed that permitting treble damages would create "unjust" price discrimination and would give the antitrust plaintiff (the rail customer) a trade advantage over its competitors. *Keogh* has been interpreted as an absolute bar to antitrust treble damages actions that involved rates or tariffs filed with a regulator.

However, since 1995, the railroads are no longer required to file rates and tariffs with the Board. Moreover, rates are not subject to advance approval by the Board, and even after-the-fact rate complaints are limited to those circumstances where the railroad has market dominance over the movement at issue. Indeed, as discussed above, approximately 90% of all rail traffic falls outside the rate review jurisdiction of the agency. Simply put, the *Keogh* doctrine has been overtaken by the partial de-regulation of the freight rail industry that has ended the practice of filing rates.

There is, however, a concern with the current legislation as it relates to the *Keogh* doctrine. If the legislation passes in its current form, it would overrule the *Keogh*

[7] 260 U.S. 156 (1922)

doctrine, but *only* as it applies to the rail industry. The *Keogh* doctrine currently is applied in a wide range of industries, including pipeline, energy, and water carriers. By targeting only the rail industry, the federal courts could assume that Congress has endorsed the continued application of this doctrine in all other industries where the doctrine may apply. This would mean, for example, that if water carriers subject to our jurisdiction (who still file tariffs with the STB) were to collude and then file the agreed-upon rates with the STB, the carriers would continue to be protected from treble damages in a civil suit.

B. 49 U.S.C. § 10706 Approvals By The STB

The bill proposes to eliminate the antitrust immunities for agreements approved by the STB under 49 U.S.C. § 10706. By its own terms, section 10706 is extremely limited and could not be used to approve a traditional rate-bureau agreement of the sort that used to exist prior to the Staggers Act. Moreover, the Board may only approve agreements that will further the Rail Transportation Policy. The Board also has broad conditioning power to ensure that any approved agreement, as implemented, furthers national transportation goals. The FTC is required to periodically assess any anticompetitive impacts of agreements approved under section 10706. *See* 49 U.S.C. § 10706(e).

In practice, there are very few section 10706 agreements in place today. In 1998, the Board approved certain rate-related aspects of the Rail Industry Agreement (RIA) between Class I carriers and short lines railroads.[8] Another section 10706 agreement is

[8] *See Association of American Railroads and American Short Line and Regional Railroad Association – Agreement – Application Under 49 U.S.C. 10706*, 3 S.T.B. 910 (1998). The rate-related provisions of the RIA are a series of bilateral agreements

the Association of American Railroads Code of Car Hire. Under the Code, the railroads collectively establish rules governing the charges that railroads pay each other when using the equipment (typically rail cars) of another railroad.[9] The railroads do not, however, collectively establish the rates for car hire under the Code or any other section 10706 agreement. In 1996, the Board withdrew approval for carriers to collectively establish demurrage and storages rates.[10] The ICC also approved the agreement of the National Railroad Freight Committee, which has in the past published the Uniform Freight Classification for its members.

No parties have asked the Board to use its Section 10706 powers in almost a decade. And the power should not, in any event, be used by parties as a tool to shield anticompetitive agreements that would otherwise violate the antitrust laws. Given that this authority is almost never used, I do not believe that repealing section 10706 antitrust immunity would have a negative effect on the Board's ability to regulate the industry.

II. Provisions That Would Hamper the Board's Ability to Regulate the Industry

A. Injunctive Relief in Private Antitrust Cases

The section of the bill that would have the greatest negative impact on the Board's ability to effectively regulate this Nation's interconnected rail network is Section 2, which would permit injunctive relief to be ordered by any of the more than 90 district courts in private civil actions. I believe that implementation of this section would

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between a larger carrier and the short line with which it interchanges governing switch charges and interline rates between those carriers.

[9] *Railroad Car Hire Compensation Rulemaking*, 9 I.C.C.2d 80, 9 I.C.C.2d 582 (1993), 19 I.C.C.2d 090 (1993), *appeal dismissed Southern Pacific Trans. v. I.C.C.*, 69 F.3d 583 (D.C. Cir. 1995).

[10] *Exemption of Demurrage from Regulation*, Ex Parte No. 462 (STB served Mar. 29, 1996).

undermine the STB's ability to achieve the regulatory objectives set forth by Congress. Shippers and rail carriers are best served by centralized oversight and the harmonization of rail related injunctive relief.

As the Board stated in our September 13 letter, the purpose of the injunction exemption traces back to the original Section 16 of the Clayton Act of 1914. As explained by the Supreme Court, the "obvious purpose" of the prohibition on district court injunctions in private suits was to "preclude any interference" when a carrier was regulated by the ICC, the STB's predecessor. *See Central Transfer Co. v. Terminal R.R. Ass'n*, 288 U.S. 469, 475 (1933). Although regulation is now less burdensome, the rail industry is still subject to substantial economic regulation. Thus, my concern about section 2 of the bill is threefold: (1) district courts do not have a broad policy oversight mandate; (2) there is a great potential for conflicting decisions between courts and between the STB and courts; and (3) the implementation of rail-related competition remedies typically requires long-term oversight.

The Board has "broad authority over the operation of railways" and rail transportation issues.[11] With that authority comes the responsibility to consider how regulatory actions affect the rail industry from both a national, regional and local perspective and to ensure that remedies resolving individual disputes comport with national rail policy objectives. The Board's policies in adjudications are guided not just by the facts presented in the individual matter, but also by rulemaking records, comprehensive industry studies, public hearings, and a long history of considering competitive behavior in the rail industry.

[11] *See, e.g., City of Lincoln v. STB*, 414 F.3d 858 (8th Cir. 2005).

District courts simply do not have the same mandate. They are not responsible for meeting the policy goals of the rail transportation policy. When deciding an antitrust case, a district court ***must reject*** the same kind of non-competition related public interest factors and policy goals that the Board ***must consider*** under the ICA. *See FTC v. Superior Court Trial Lawyers' Association*, 493 U.S. 411 (1990) (holding that proffered non-economic public interest justifications were not relevant to the question of whether a restraint of trade is unlawful under the antitrust laws). Nor do the district courts possess the institutional expertise to consider how a decision resolving one case will affect other carriers and shippers on that line, or on other lines in different parts of the country. Unlike many other industries, the national rail system – while comprising hundreds of individual railroads – nevertheless operates as a single integrated, complex, and interdependent network. Operational changes or issues arising in one location can have significant operational ramifications hundreds of miles away, including effects on other freight carriers as well as on Amtrak and commuter lines. The docket of a district court is necessarily varied and contains hundreds of cases from numerous industries. Moreover, because the courts of appeals, and not the district courts, review decisions of the STB pursuant to the Hobbs Act,[12] I expect that district courts have even less familiarity with the rail industry than they otherwise would. District courts do not conduct generalized studies or rulemaking proceedings that provide critical information about how the industry is performing or how certain regulatory policies have affected it.

Allowing district courts to order injunctive relief in individual private antitrust actions would create a potential for conflicting decisions from individual courts, as well

[12] 28 U.S.C. §§ 2321(a), 2342.

as for creating a ripple effect of unforeseeable operational and service problems outside of a particular court's jurisdictional territory. Many national companies already find it challenging to comply with the antitrust laws when there is a "split" in the courts about the legality of certain behavior; but conflicting decisions in a physically networked industry such as rail could be devastating. A single rail line may extend hundreds of miles through many federal judicial districts and circuits, creating a possibility for different rules and injunctive relief governing identical behavior on different parts of the line. It is also possible that competing carriers could be subject to different rules for identical behavior merely because one has been sued and is subject to a district court injunction and the other has not. Add to this already complicated picture the possibility that the Board may also have existing rules and remedies to fix those same competitive issues and you quickly have an unworkable system that leads to confusion and additional expense for shippers and ultimately consumers as carriers pass on the costs of complying with multiple regulatory and judicial standards. Another layer of complexity arises from the fact that carriers may need STB approval to carry out potential district court remedies. For example, if a district court in a Sherman Act Section 2 essential facilities case required Carrier A to allow Carrier B to operate over its lines, such a trackage rights agreement could not be implemented without Board approval. Likewise, divestitures of rail lines to another operator would also require Board approval.

Finally, the Board knows from experience that some rail disputes do not lend themselves to one-time remedies, but rather require continuing supervision and oversight. The ability and willingness to retain jurisdiction over a matter for a longer term is a hallmark of regulation and the Board is well-suited to retain jurisdiction to resolve long-

term network issues as they arise. A case still pending at the Board is a good example. In mid 2006, the Board authorized one carrier to operate over the lines of another carrier due to certain service inadequacies. The parties have been litigating over operating protocols, access, switches, interchange, and other issues ever since. It is difficult to see how a district court could monitor and resolve these disputes without stepping into the role of regulator.

B. Dual Merger Review

Section 3 of S. 772 would subject rail mergers and acquisitions to both the approval process and criteria of the Interstate Commerce Act and to Section 7 of the Clayton Act. Congress considered this question 12 years ago in enacting the law sunsetting the ICC and establishing the Board. At that time, Congress decided to retain the merger exemption, keeping rail merger review with the same agency that regulates the economic activity of the industry. However, Congress clarified and modified the contours of that review to encompass features associated with merger review under the antitrust laws: a broad, national outlook on the relevant markets to be examined; use of divestiture as a remedial condition; and the ability to discuss a proposal directly with interested parties.[13]

Before I discuss the problems that could arise from a dual review scheme, I would like to discuss some of the current features of the STB specialized rail merger review process. The STB's merger review process is conducted on an open record, with opportunities for comment, evidence and counter-proposals from all interested parties, including the DOJ, DOT and other interested federal entities. Because the Board

[13] H.R. Conf. Rep. No. 104-422, at 191 (1995).

monitors and supervises the industry full-time, its decisions are suffused with knowledge about the industry; its customer segments; its past, present and future competitive landscape; and the impact of the merger on the Board's other regulatory policies and goals. When deciding whether to approve, disapprove, or impose conditions on a proposed merger, the Board's public interest analysis goes beyond competitive concerns and considers operational/services issues as well as a host of other issues. This understanding is key to devising remedies that will work in the real world. And, as I discussed earlier, the Board actively monitors the results of mergers and can impose post-merger conditions as needed to address competitive, operational, and environmental issues. For example, in the Southern Pacific/Union Pacific merger, which I will discuss in more detail, the merged firm was required to submit quarterly and annual reports for 5 years to allow the Board to analyze the impact of the approved transaction.

I am also concerned that dual enforcement could result in some of the same problems raised by the potential for district court injunctions, including inconsistent Board conditioning and DOJ consent decree provisions, differences in the statutory review deadlines and the public availability of evidence and data. Moreover, proposed merger parties would incur substantial additional costs to comply with both review processes.

From a substantive standpoint, possibility for disagreements between the antitrust regulatory agencies and the Board on merger competitive issues is not a major concern. Under section 11324(d), the Board must accord "substantial weight" to any recommendation of DOJ. The Board is also guided in its competitive impact analysis by cases decided under Section 7 of the Clayton Act and Section 1 under the Sherman Act.

Critics of the current review scheme cite to the much-discussed but rare cases where the Board declined to follow the DOJ's recommendation that merger authority be either denied or conditioned on expansive divestitures. When the Board approved the acquisition of Conrail by CSX and Norfolk Southern and the division of Conrail's assets between the two carriers, there was general agreement that the transaction was largely pro-competitive. I understand that there were only modest differences of opinion between the Board and DOJ on the number and type of conditions that should be attached to the Board's approval.

The differences of opinion were more pronounced in the Board's review of the Union Pacific/Southern Pacific merger, where the Board declined to follow DOJ's recommendation that the merger either be denied or conditioned on expansive divestitures. The Board concluded that, on balance, the merger would be in the public interest, as it would permit the financially weak Southern Pacific (SP) to become part of a large, financially healthy rail system that would sustain efficient operations and invest in the SP's deteriorating infrastructure. The Board also concluded that a divestiture requirement would be problematic for ensuring adequate service levels for many of SP's customers, and that a trackage rights remedy, in combination with continuing Board oversight, would be sufficient to preserve competition for those shippers that would otherwise have lost a choice of carriers. Finally, the Board also disagreed with DOJ about whether the significant efficiency benefits claimed by the merging parties were likely and merger-specific.

Significant differences between the Board's and DOJ's competition analysis are rare, however. And in such cases, the DOJ may challenge a Board merger decision in the courts of appeals.

Finally, a dual merger scheme overlooks the impact of the Board's new merger rules. These new rules were put into place following the Board's merger moratorium that forestalled what was widely expected to be the final round of mergers, which would have resulted in two (or three) large transcontinental systems.[14] Under traditional merger analysis by DOJ or FTC, such vertical integration of two partners with complementary systems (e.g. a western railroad merging with an eastern railroad) would not be perceived to carry as significant a risk of competitive harm as a horizontal merger of two direct competitors (e.g. two western or two eastern railroads). However, under the new STB rules, a Class I merger would be in the public interest "only when substantial and demonstrable gains in important public benefits – such as improved service and safety, enhanced competition, and greater economic efficiency – outweigh any anticompetitive effects, potential service disruptions, or other merger related harms."[15] To offset any harms that could not be mitigated, merging carriers would need to show how the proposed merger would enhance competition.[16]

Although a Class I merger has not been proposed since the Board adopted the new rules, the Board has in place a comprehensive review scheme that would address both competition and service issues and the interplay between them. It is difficult to see how the imposition of Section 7 would enhance the collective ability of the federal

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[14] *See Western Coal Traffic League v. STB*, 216 F.3d 1168 (D.C. Cir. 2000).

[15] 49 CFR § 1180.1(c).

[16] 49 CFR § 1180.1(c)(2)(iv).

government to protect consumers from potentially anticompetitive and disruptive transactions.

III. Provisions That Raise Significant Questions

A. Limitation on Primary Jurisdiction

Section 4 of the bill would instruct district courts that they need not defer to the primary jurisdiction of the STB in antitrust civil actions. The doctrine of primary jurisdiction provides that a district court may stay a civil action in order to refer a complex matter to a regulatory agency for preliminary findings. Courts refer such matters "when the protection of the integrity of the regulatory scheme dictates preliminary resort to the agency that administers the scheme."[17] Although the factors under which a district court decides to refer a case differ by circuit, when determining whether to make a referral under the primary jurisdiction doctrine, courts generally consider whether there is "(1) the need to resolve an issue that (2) has been placed by Congress within the jurisdiction of an administrative body having regulatory authority (3) pursuant to a statute that subjects an industry or activity to a comprehensive regulatory scheme that (4) requires expertise or uniformity in administration." *U.S. v. General Dynamics*, 828 F.2d 1356, 1362-63 (9th Cir. 1987). Once district courts have preliminary findings from the administrative agency, the findings may be upheld or rejected.

It is not clear what the effect of section 4 would be on the primary jurisdiction doctrine, nor do I understand the problem that exists with the existing primary jurisdiction doctrine that this provision seeks to remedy. My interpretation is that it would permit district courts to decline to refer a matter to the Board even if all of the

[17] *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 353 (1963).

primary jurisdiction factors were present. If the bill is intended to achieve this outcome, then I question whether it is prudent to restrict the judiciary from gathering information and expertise that the court decided is necessary for the effective administration of justice, or "when the protection of the integrity of the regulatory scheme" dictates seeking the guidance of the Board.[18]

B. Duplicative Regulation By The FTC

Section 5 of the bill would permit broad regulation of the rail industry by another regulatory body, the FTC. It would amend the Federal Trade Commission Act (FTC Act) to permit the FTC to investigate and adjudicate "unfair methods of competition" by rail carriers. This provision of the FTC Act, however, is to our understanding largely duplicative of the federal antitrust laws in the Sherman Act that are already enforced against the railroads by DOJ.

Moreover, there is also considerable overlap between the FTC's unfair competition authority under 15 U.S.C. 45 (were it to apply to railroads) and the Board's unreasonable practices authority under 49 U.S.C. 10702. Both statutory provisions could be used to assess behavior that reduces competition, etc. However, the Board considers unreasonable practices through its broader public interest lens while the FTC's review is limited to competitive issues. As always, there is the possibility that the different statutory mandates could lead to different and conflicting results, particularly with regard to cases that consider the responsibilities of a monopolist rail carrier.

Competition issues are already subject to regulation by the Board and DOJ. While I appreciate that many industries are subject to overlapping economic regulation

[18] *United States v. Philadelphia Nat'l Bank*, 374 U.S. 321, 353 (1963).

under two or more regulatory regimes, I am concerned that introducing a third regulator would make it more difficult to administer any sort of uniform regulatory approach to the national rail system.

CONCLUSION

The railroads have been subject to the federal antitrust laws since those laws were first enacted by Congress in 1890. And for the most part, those competition laws and the economic regulatory scheme that governs the railroads have co-existed for decades without serious conflict. Yet Congress has, over time, carefully created a few narrow immunities or exemptions to the federal antitrust laws. I believe most of those exemptions were designed to permit the STB to carry out its statutory obligations to protect the public when competition does not exist, while also promoting a safe and efficient rail system by adopting policies that will permit the carrier to earn sufficient returns to make the critical investment in their infrastructure.

Some of those exemptions may no longer be needed, and the judicially created *Keogh* doctrine is a fine example of a judicially created antitrust immunity that has no valid purpose in the current regulatory environment. This bill is not, however, targeted to remove just those exemptions that have grown outdated or are no longer useful, but rather is a sweeping change that removes them all. I am concerned that doing so will make it more difficult for the STB to perform its regulatory oversight responsibilities required by Congress under the Interstate Commerce Act. Moreover, there has not been a pattern of antitrust complaints or anti-competitive conduct in the railroad industry. And the bill seems premised on the inaccurate notion that the railroads presently are broadly immune from antitrust liability, which is not the case.

The Board understands, and is sensitive to, the concerns of rail customers about rail rates and service. That is why we have taken, or are taking, a number of initiatives related to those issues, including: modifying our major merger rules to promote enhanced competition; streamlining our major rate case procedures; revising our procedures for small and medium-sized rate cases to make them more accessible and affordable; examining our methodology for calculating the rail industry's cost of capital; examining issues related to "paper barriers;" and sponsoring a million-dollar, yearlong study of the state of rail competition throughout the country.

It is doubtful, however, that rail customers would benefit from the changes proposed in the present legislation; indeed, the legislation may well make rate and service concerns worse rather than better. The bill would make efficient, uniform regulation of the rail industry more difficult by creating duplicative and overlapping regulatory schemes. Subjecting the rail industry to a patchwork of judicial injunctions at the behest of localities scattered across the country could cause a ripple effect of operational problems for freight, Amtrak, and commuter rail transportation. District courts are not equipped to anticipate, monitor, or remedy such problems, and those problems could impede the railroads' ability to provide efficient and timely freight and passenger rail service and raise the cost of providing those services—costs that likely would be passed on to rail customers in the form of higher rates.

I appreciate having the opportunity to discuss this legislation with the Subcommittee today.