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Working Party No. 2 on Competition and Regulation

RECENT DEVELOPMENTS IN RAIL TRANSPORTATION SERVICES

-- United States --

17 June 2013

This document is submitted to Working Party No. 2 of the Competition Committee FOR DISCUSSION under item VI of the agenda at its forthcoming meeting on 17 June 2013.

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1. This paper summarizes some of the developments in the rail transportation sector in the United States since the last WP2 roundtable on this subject in February 2005.[1]

2. Passenger: Beginning with the initial stimulus package of 2009[2] and continuing through the current budget proposal,[3] the Obama administration has supported funding for a network of high-speed intercity passenger rail corridors throughout the United States. The current budget proposal "provides $40 billion over five years to fund the development of high-speed rail and other passenger rail programs as part of an integrated national transportation strategy. This system will provide 80 percent of Americans with convenient access to a passenger rail system, featuring high-speed service, within 25 years."[4] One important project, which is pending approval at the U.S. Surface Transportation Board (STB), the government's rail economic regulator, involves the nation's first 220 miles per hour high-speed rail network in California.

3. Freight: Since the WP2 roundtable in 2005, the U.S. Government has issued two major studies on the competitiveness of the U.S. freight rail system, which operates in the private sector. In the first, released in 2006, the Government Accountability Office (GAO) addressed the railroad industry's performance since it was substantially deregulated in 1980. The GAO Report found that changes in the railroad industry since 1980 were generally positive and that rates in many areas declined, but that for some "captive shippers"—shippers of commodities such as coal, bulk chemicals, and grain over which the serving railroad has substantial market power—rates had increased substantially. The report recommended that the STB "undertake a rigorous analysis of competitive markets to identify the state of competition nationwide; in specific markets, determine whether the inappropriate exercise of market power is occurring; and where appropriate, consider the range of actions available to address problems associated with the potential abuse of market power."[5]

4. In response to the GAO Report, the STB commissioned a study by an independent team of consultants charged with assessing competitiveness in the U.S. rail industry. That study, commonly known as the "Christensen Report,"[6] was released in 2008 and supplemented in 2010. It found that railroad rates steadily increased since 2004, with a particularly steep increase in 2008. But the Christensen Report found that the rate increases were driven by fluctuating fuel prices and other costs and did not appear to reflect an undue exercise of market power. Overall, the study found a healthy rail industry that, since 2006, has remained largely revenue-sufficient, meaning that railroads are able to cover their operating costs and earn a rate of return that enables them to attract investment capital to pay for more locomotives and railcars and to make other improvements. The Christensen Report also found that the large productivity gains in the 1980s and 1990s—when the railroads shed excess rail lines, reduced crew sizes, and streamlined operations—are no longer strong enough to offset rising operating costs. Since 2002, "increases in the rate

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1 DAF/COMP/WP2/WD(2005)17, Roundtable on Structural Reform of the Rail Industry, Submission of the United States.

2 The American Recovery and Reinvestment Act of 2009, Pub.L. 111–5, Feb. 17, 2009, 123 Stat. 115.

3 FY 2014 Budget, Office of Management and Budget, Department of Transportation, available at www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/transportation.pdf.

4 *Id.*

5 "Freight Railroads: Industry Health Has Improved, But Concerns About Competition and Capacity Should Be Addressed" (GAO 07-94), Oct. 6, 2006, available at www.gao.gov/new.items/d0794.pdf.

6 "*A Study of Competition in the U.S. Freight Railroad Industry and Analysis of Proposals that Might Enhance Competition* (Nov. 3, 2008, supplemented in Jan. 2010), available at www.stb.dot.gov/stb/docs/CompetitionStudy/Final/January%202010%20Report.pdf.

of input price growth combined with slower productivity growth have resulted in unit cost increases." "Economies of density," the study also reports, "appear to have been exhausted in recent years."[7]

5. Subsequently, in response to a proposal made by a group of cargo shippers (the National Industrial Transportation League), the STB instituted a proceeding to consider whether to adopt new rules for mandatory switching, under which a carrier with the ability to carry a captive shipper's traffic all the way from an origin to a destination could be required under certain conditions to "switch" cargo to a connecting railroad at the direction of the shipper. Railroads operating in Canada are subject to a set of such competitive switching rules.[8]

6. Legislative: The Rail Safety Improvement Act of 2008 requires large U.S. rail carriers to implement Positive Train Control (PTC) by the end of 2015 on main lines where intercity rail passenger transportation or commuter rail transportation is regularly provided, and on main lines over which hazardous toxic-by-inhalation or poisonous-by-inhalation materials are transported. PTC is an automated system designed to prevent train-to-train collisions, over-speed derailments, incursions into established work zone limits, and the movement of a train through a switch left in the wrong position. To comply with this law, rail carriers will need to make substantial expenditures related to installation and maintenance of PTC, and one regulatory issue will be whether carriers will be able to recover these costs through the rates they charge.

7. Court Cases: Although some activities of the railroads are subject to the antitrust laws, a number of rail activities, including mergers and many unilateral actions are instead subject to regulation by the STB. Naked price-fixing by the railroads would not be exempt from the antitrust laws. A U.S. federal appeals court is currently reviewing appeals from several large railroads against a district court judge's decision to allow 30,000 freight shippers to combine their claims against the largest railroads for allegedly conspiring to fix the amount of a fuel surcharge into a class action.[9]

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7 Id.

8 "Petition for Rulemaking to Adopt Revised Competitive Switching Rules", STB Ex Parte No. 711.

9 In re Rail Freight Fuel Surcharge Antitrust Litigation, 286 F.R.D. 88 (D.D.C. 2012), 2012 WL 2870207; D.C. Cir. No. 12-8085.