Held Captive: How Increased Regulation Arrests Railroads' Ability to Serve the Nation

Beau B. Bump

Follow this and additional works at: https://via.library.depaul.edu/bclj

Recommended Citation
Available at: https://via.library.depaul.edu/bclj/vol5/iss4/6

This Comment is brought to you for free and open access by the College of Law at Via Sapientiae. It has been accepted for inclusion in DePaul Business and Commercial Law Journal by an authorized editor of Via Sapientiae. For more information, please contact wsulliv6@depaul.edu, c.mcclure@depaul.edu.
Held Captive: How Increased Regulation Arrests Railroads' Ability to Serve the Nation

Beau B. Bump*

I. INTRODUCTION

On a macroscopic level, every regulatory policy debate ultimately contemplates the economic system that is best for our country. Free enterprise and socialism occupy opposite ends of the spectrum; between the two extremes is a sliding scale in which aspects of each economic system combine with aspects of the other to strike a proper balance between unregulated competition and pervasive government control. The United States of America has long prided itself in attaining that balance through a modified free enterprise system that tempers private competition with mild government regulation. The nation's markets champion competition as their central ethos, while privately-owned industries begrudgingly accept government regulation as a necessary evil and crucial check on the entire system. Some industries, however, have been subject to more pervasive regulation than others: in particular, industries whose services garner a high de-

* Juris Doctor from DePaul University College of Law expected 2008; Bachelor of Arts in English from University of Nebraska–Lincoln, 2004.

1. See generally Benjamin N. Ward, The Socialist Economy: A Study of Organizational Alternatives (1967). The hallmarks of these economic systems are privatization and nationalization, respectively, which describe a government's relationship to its country's means of production. Private ownership of the means of production prevails in a free enterprise economy, whereas government ownership predominates in a socialist economy. Id.


The economy of the United States is often described as a competitive, private enterprise system. The largest part of the economy is organized on the decentralized lines of private property and private enterprise. The market, therefore, is the central institution regulating economic activity. But it must also be recognized that business is affected in many ways... by the activities of government.

Id.

3. See id. ("[I]n a broad sense all industries are regulated. Governmental laws which affect business include antitrust policy, fair trade laws, labor legislation, monetary and fiscal policy, public expenditures, and tariff policy.").

4. James C. Bonbright, Principles of Public Utility Rates 4 (1961) (delineating two major categories of regulated industries: (1) those enterprises which supply, directly or indirectly, continuous or repeated services through more or less permanent physical connections between the plant of the supplier and the premises of the consumer; and (2) the public transportation agencies"). The former category includes electricity and natural gas utilities as well as
gree of public interest.\textsuperscript{5} Conflict inheres in the regulation of such industries, as "[t]he basic objective of private corporations is profit maximization, while the public interest demands adequate service at the lowest possible price."\textsuperscript{6} Thus, both the private corporations and the public that relies on their services are left to lobby government for either more or less regulation.\textsuperscript{7} But where competition amongst or within industries can be relied on to protect the public interest, the efficacy of a regulatory scheme is diminished.\textsuperscript{8} The regulatory policy debate, then, becomes 1) whether adequate competition exists within or against a given industry such that the public interest is protected by market forces alone, obviating the need for regulation, and 2) where regulation is deemed necessary, what degree of regulation properly balances the private interests with the public interest.\textsuperscript{9} The American railroad industry has been steeped in this debate for the duration of its existence; in fact, the health of the industry has consistently corresponded to its level of regulation.\textsuperscript{10}

The current regulatory policy debate in the freight railroading industry, or reregulation debate,\textsuperscript{11} naturally features two opposing parties: railroad companies and shippers.\textsuperscript{12} Simply put, railroad companies oppose reregulation and shippers support it.\textsuperscript{13} Of course,
such an oversimplification beckons elucidation. The origins of the reregulation debate are largely historic: a looming remnant of the days when the federal government heavily regulated the rail industry. During that ninety-three-year period, the Interstate Commerce Commission ("ICC") promulgated maximum rate schedules for every route on the nation's interstate rail system; the maximum rate that a railroad company could charge for a shipment between any two cities was capped at a set rate, regardless of the actual cost of the movement. Railroad companies were also required to serve shippers that resided along their rail lines under their "common carrier obligation," even if doing so were inefficient and unprofitable. Thus shippers had a steady supply of rail transportation service at a relatively low rate. However, because railroad companies were prevented from recouping their costs of operation by the ICC rate ceilings, the health of the industry floundered and mass mergers and bankruptcies ensued. In response, Congress passed the Staggers Act of 1980, which dissolved much of the regulatory framework that had brought the rail industry to its knees. Particularly, the Staggers Act eliminated maximum rate schedules and emphasized competition as the primary mechanism to set railroad companies' freight shipment rates. Those rates have since been subject to market forces and confront shippers with the possibility of higher rates and decreased availability of rail services. Shippers' response has been to call for reregulation, which at least two commentators view as a transparent euphemism for lower rates.

14. I use the term "shippers" throughout the article in reference to shippers and shippers' groups that support reregulation. In all fairness, some shippers, particularly large shippers that have been able to negotiate favorable rates, ardently oppose reregulation.
15. See discussion infra Part II.
17. Id.
19. See id.
24. Woodman & Starke, supra note 16, at 273 (stating that "the ultimate goal of . . . reregulation forces is to lower rail rates, and . . . they are quite willing to engage in whatever statutory contortions may be necessary regarding the competitive access provisions in order to achieve
If lower rates are the desired end of shippers’ calls for reregulation, then the means of achieving that end in the post-Staggers era has been to argue the absence of competition. Generally, shippers argue that reregulation is needed to inject competition into markets served by only one railroad company. In those markets, shippers argue, railroad companies are able to charge exorbitant rates for rail transportation services, rates that shippers in those markets have little choice but to pay. Shippers often refer to shippers served by only one railroad company as “captive shippers,” a rhetorical tactic that re-characterizes the Staggers Act concept of “market dominance” in terms of the railroad industry alone, as opposed to the entire transportation industry. Railroad companies, on the other hand, argue that competition exists from other modes of transportation in markets served by only one railroad company, and that where effective competition does not exist, adequate safeguards are in place to protect shippers from market abuse. Further, railroad companies argue that only recently have they become able to make the kind of returns on investment that allow for reinvestment in the country’s rail infrastructure, which is anticipated to become inadequate in the next twenty years without substantial expansion. Because shippers represent nearly every type of company in the nation, from retail to energy to produce, the reregulation debate holds real-world consequences for both the nation’s companies and consumers. For instance, increased regulation may result in lower rates for a time, which ultimately benefits consumers in the form of lower prices, but those lower prices would likely skyrocket if the nation’s rail infrastructure were supersaturated ten years later because today’s railroad companies were prevented from invest-

that end”). Reciprocal switching, terminal agreements, trackage rights, and bottleneck rate setting are competitive access provisions discussed herein. See infra Part IV.B.1-4.

25. The Staggers Act contains avenues for redress, i.e. lower rates, where there is a lack of competition in a given market. See infra Part III.B.1. By no means does the reregulation debate solely focus on the rates that rail carriers charge shippers. Reregulation also includes entry into the industry, exit out of the industry, abandonment, merger, and other areas concerning railroad operation. Pertinent as those areas may be, this Comment focuses primarily on reregulation of freight rates, which has been hotly debated as of late.

26. The various methods of injecting competition into the railroad industry are discussed infra Part IV.B.1-4.


28. See infra note 146 and Part V.A.

29. See infra Part V.

30. See infra Part V.C and note 185.

31. See CURE STATEMENT, supra note 13.
ing in expanding rail capacity. Such supersaturation would shift a larger market share of freight transportation services to trucking companies, and thus result in more highway traffic. Yet, a greater market share for trucking companies may result in better highways, as maintaining interstate highways would rank higher as a national interest. As soon becomes readily apparent, the issue of railroad regulation is an important, yet difficult problem that will inevitably affect the country and its citizens in a very real way over the next twenty years. What that effect will be is the subject of this Comment.

This Comment proceeds as follows: Part II provides the back-story for the current issue: a brief history of railroad regulation, substantial deregulation via the Staggers Act of 1980, and the establishment of the Surface Transportation Board via the Interstate Commerce Commission Termination Act of 1995. Part III explores in depth current regulation of the railroad industry by the Surface Transportation Board. Part IV discusses the movement for reregulation by shippers and their proposals to inject competition into the railroad industry, including legislation and lobbying efforts in Washington, D.C. Part V addresses shippers’ proposals and explains why reregulation is both unnecessary and detrimental to the economic welfare of the nation. Part VI concludes the Comment and summarizes the importance of the railroad reregulation debate.

II. BACKGROUND

A. Pre-Federal Regulation of the Railroad Industry

The American railroad industry is deeply rooted in private ownership. The first railroads in the United States were constructed and operated entirely via private capital, and were unregulated by the

32. See PHILLIPS, supra note 2, at 5 (stating that "a higher rate of return in the short run may lead to lower rates or improved services in the long run").

33. PHILLIPS, supra note 2, at 442; William E. Thoms, Clear Track for Deregulation American Railroads, 1970-1980, 12 TRANSP. L.J. 183, 185 (1982). See also Harris, supra note 18, at 3:

The earliest railroads were merely tramways operated by horse-power and stationary engines, the use of locomotives not having begun until about 1831. It was assumed that these railroads would be public highways, open to all users who had the proper rolling stock and who paid the established highway tolls. Some of the earliest [rail]roads, in fact, were operated for a time on the toll-road principle. However, this procedure soon proved to be impractical because of the special type of equipment required and the difficulty in meeting and passing other users of the road.

(internal citations omitted). The fact that the railroad industry must maintain the ways over which its transportation moves provides the basis for differential pricing, discussed infra note 105.

34. Thoms, supra note 33, at 185 ("Although virtually all the railroads in the world were originally built with private capital, American railroads are unique in that they stayed in private
federal government until Congress passed the Act to Regulate Commerce in 1887 ("1887 Act"). Prior to the 1887 Act, regulation of the railroad industry was carried out by the several states. The states effected regulation of early railroad companies in a number of ways: 1) by granting corporate charters and authorizing railroad construction in the first instance, 2) by assessing taxes and limiting profits (if necessary), 3) by passing legislation prescribing the manner and location of railroad construction, and 4) by requiring specific services from the railroad companies once they were operational. Because states' regulation was facially comprehensive during the early formation of the railroad industry, "[f]ederal intervention seemed not only unnecessary but [also] intrusive unless State power should be abused; and the abuse not often appearing, intervention was scarcely thought of by anyone." Thus, the several states retained sole, albeit scant, regulatory power over the railroad industry during the first days of its formation, hastening its growth with largely pro-railroad legislation.

B. The Movement towards Federal Regulation

Soon, however, the railroad industry began to outgrow the relatively mild regulation then asserted by the states. Because the states did not have broad regulatory authority over the industry as a whole,
most standards concerning the operation of the railroads were developed by the railroad companies themselves. When states later passed legislation seeking to reign in perceived abuse in the industry, railroad companies challenged the legislation on Dormant Commerce Clause grounds. The United States Supreme Court upheld instances of state regulation in Munn v. Illinois; Chicago, Burlington, & Quincy Railroad Co. v. Iowa; Peik v. Chicago & North-Western Railway Co.; Chicago, Milwaukee, & St. Paul Railroad Co. v. Ackley; Winona & St. Peter Railroad Co. v. Blake; and Stone v. Wisconsin (collectively known as the Granger cases), and indicated in each case that "[u]ntil Congress acts in reference to the relations of [the railroad] company to interstate commerce, it is certainly within the power of [the state] to regulate its fares, etc., so far as they are of domestic concern." The underlying debate in the Granger cases was between western farmers and the railroad companies concerning the reasonableness of shipping rates; the farmers blamed exorbitant rail rates for their inability to profit on crops, while the railroad companies insisted that such rates were necessary in order to keep the railroad industry up and running. The Court's emphasis on the paucity of Congressional action, obsequiously noted in the Granger cases, contributed to the impetus in Washington for regulatory legislation. The Court eventually did an about-face and made its stance in the regulation debate crystal clear by invalidating state regulatory legislation on Dormant Commerce Clause grounds in Wabash, St. Louis, & Penn-

---

Railway line mileage increased three-fold in each succeeding decade from 1840 when we had 2,800 miles of track until 1860 and nearly doubled in each decade from 1860 until 1890. In the latter year the expanse of track reached 163,000 miles, and the rail network stretched from coast to coast and reached into every state of the nation.

Id.

44. Id. at 4. See also PHILLIPS, supra note 2, at 444 (explaining that although many of the state-granted charters contained maximum rate schedules and restrictions on discriminatory rates, such provisions were not often enforced).


46. Id. at 114 n.58. See, e.g., Welton v. Missouri, 91 U.S. 275 (1875); Ward v. Maryland, 79 U.S. 418 (1870); Pennsylvania v. Wheeling Bridge Co., 54 U.S. 518 (1851).

47. 94 U.S. 113 (1876).

48. 94 U.S. 155 (1876).

49. 94 U.S. 164 (1876).

50. 94 U.S. 179 (1876).

51. 94 U.S. 180 (1876).

52. 94 U.S. 181 (1876).

53. Peik, 94 U.S. at 178.

54. Harris, supra note 18, at 6.

55. Indeed, these are the same arguments being made today. In 140 years, the argument has changed little, which is a testament to the earnestness on each side of the debate.
sylvania Railway Co. v. Illinois;\textsuperscript{56} decided a year before Congress established the first independent regulatory agency via the 1887 Act.\textsuperscript{57}

C. Federal Regulation of the Railroad Industry: The Act to Regulate Commerce of 1887

The 1887 Act, \textit{inter alia}, created the Interstate Commerce Commission, which was vested with broad regulatory jurisdiction over the railroad industry.\textsuperscript{58} The ICC's initial functions included general oversight of railroad management, collecting and analyzing annual reports from railroad companies as mandated by the 1887 Act, hearing complaints of unlawful practices and formulating remedies, and enforcing the 1887 Act's requirement that all rates be just and reasonable.\textsuperscript{59} While the last requirement may seem like a protective measure for the sole benefit of shippers, at least one commentator insists that railroad companies welcomed the rate regulation.\textsuperscript{60} Subsequent legislation remedied both substantive and procedural flaws in the 1887 Act,\textsuperscript{61} and by the early 1910s the ICC exercised dominant control over the railroad industry, especially in the realm of rate regulation.\textsuperscript{62} The ICC promulgated maximum rates for rail routes while at the same time restricting pooling of freight, "a means by which the railroads might have cooperated in securing shipment by the shortest and cheapest route"; the ICC thus prevented railroad companies from operating efficiently and competitively.\textsuperscript{63} Over the next seventy years, the ICC's regulation of the railroad industry stifled competition not only in the railroad industry itself, but also impaired the railroad industry's ability to compete

\footnotesize{\textsuperscript{56} 118 U.S. 557 (1886). \\
\textsuperscript{57} Harris, \textit{supra} note 18, at 1. \\
\textsuperscript{58} Id. at 16. \\
\textsuperscript{59} Id. \\
\textsuperscript{60} See Hardaway, \textit{supra} note 45, at 114 n.58 (citing a handful of works chronicling railroad support of regulation). Generally, the argument that railroads supported regulation is premised on the fact that unregulated competition both within the railroad industry (rate wars) and against other modes of transportation had driven rates so low that federal regulation was needed to establish a higher minimum rate for the railroad industry. Thus, while "just and reasonable" may conjure up images of poor farmers being steamrolled by exorbitant rail rates and a burgeoning railroad industry, it can also be viewed from the other side of the track: that the expensive operation of railroads could not persist without either federal regulation or subsidy. \textit{See id.} at 113-15. \\
\textsuperscript{61} Thoms, \textit{supra} note 33, at 190 (citing R. Saunders, \textit{The Railroad Mergers and the Coming of Conrail} 34 (1978)). This legislation included the Hepburn Act of 1906 and the Mann-Elkins Act of 1910. Saundersons at 34. \\
\textsuperscript{62} Saundersons, \textit{supra} note 61, at 34. "The ICC flexed its new muscles over rate-making by denying the railroads' request for general rate increases in 1911 and again in 1912." \textit{Id.} \\
\textsuperscript{63} Phillips, \textit{supra} note 2, at 452. The result was a dramatic decrease in the quality of service, and ultimately an inability to serve the nation during wartime. \textit{See infra} note 65. Such a combination of rate regulation and practice regulation would have a similar result even today.}
with other transportation industries. By the time the United States entered World War I in 1917, the railroad industry was so beleaguered by ICC regulation that President Wilson deemed it necessary to nationalize the nation's railroads in order to meet the demands of wartime. The health of the railroad industry was so poor as the result of overregulation that the number of railroad companies had decreased from 1,564 in 1907 to seven major carriers accounting for eighty-five percent of all rail traffic in 1980. The heavy-handed regulation of the ICC set the stage for drastic regulatory refurbishment between 1970 and 1980.

D. The Movement towards Deregulation of the Railroad Industry

Although the Rail Passenger Service Act of 1970 has been regarded as the first deregulatory piece of legislation, it did little to remedy the dismal effects of regulation. Not until Congress passed the Railroad Revitalization and Regulatory Reform Act of 1976 ("4R Act") and the Staggers Rail Act of 1980 ("Staggers Act") was the railroad industry somewhat relieved of the regulatory load it had been shouldering for the better part of a century. The 4R Act did not go so far as to abolish the ICC's regulatory scheme altogether, but did loosen the reins. The most important contributions of the 4R Act, primarily be-
cause of their role in the subsequent Staggers Act, were the concepts of market dominance and demand sensitive pricing. While the 4R Act was intended to "inaugurate a new era of competitive pricing," railroad companies failed to take up the competitive ratemaking call, instead relying on general rate increases for revenue as they had in the past. The 4R Act was a step in the right direction, but it soon became apparent that its provisions did not go far enough in relaxing the regulatory framework. Its remedy came in 1980, only four years later, in the form of the Staggers Act.


The Staggers Act is the most far-reaching piece of deregulatory legislation the railroad industry has seen; however, contrary to popular verbiage, it did not completely deregulate the railroad industry. The Staggers Act instead "created a new declaration of regulation policy which stressed competition to the maximum extent possible." Specifically, the Staggers Act enabled railroad companies to 1) independently negotiate rates with shippers that would then be memorialized in private contracts not subject to ICC scrutiny, 2) more easily costing methods. Thoms, supra note 33, at 207 (citing DEPT. OF TRANSPORTATION, A PROSPECTUS FOR CHANGE IN THE FREIGHT RAILROAD INDUSTRY 114 (1978)).

73. Market dominance was the threshold requirement for challenging the reasonableness of a rate under the 4R Act. In order to successfully petition the ICC to find a rail carrier's rate as unreasonable, a shipper had to first show that there was a lack of competition from other carriers or modes for that particular shipment. Only if a rail carrier dominated the market could a rate be found unreasonable. Thoms, supra note 33, at 208. See also infra Part III.B.1. For a great discussion of the concept, see Norman H. Jones, Jr., The Meaning of Market Dominance, in RAILROAD REVITALIZATION AND REGULATORY REFORM 203 (Paul W. MacAvoy & John W. Snow eds., 1977).

74. Demand sensitive pricing, which enabled railroads to charge different rates for seasonal demand, was the prologue to the concept of differential pricing established by the Staggers Act. See infra note 105 (discussing differential pricing).

75. Thoms, supra note 33, at 208.

76. Id.


80. Thoms, supra note 33, at 212. See also 49 U.S.C. § 10101(a) (1982) (stating, inter alia, that rail transportation policy included allowing competition to establish reasonable rates, minimizing federal regulatory control over the rail industry, and enabling rail carriers to earn adequate revenues).

abandon track in order to improve system-wide efficiency,\textsuperscript{82} and 3) adjust rates in a shorter period of time in response to fluctuations in the market.\textsuperscript{83} The Staggers Act also codified the concept of demand-based differential pricing,\textsuperscript{84} while concomitantly emphasizing the need to balance the interests of the railroad industry in pursuing adequate revenues with the interests of shippers in paying reasonable rates for railroad services.\textsuperscript{85}

F. A Changing of the Guard: The Surface Transportation Board Replaces the ICC

Finally, the Interstate Commerce Commission Termination Act of 1995 ("ICCTA") completed the regulatory policy that the federal government espouses today by replacing the ICC with the Surface Transportation Board ("STB");\textsuperscript{86} the ICCTA eliminated some of the ICC's duties under the Staggers Act, transferring those remaining to the STB.\textsuperscript{87} The STB is now the primary regulatory agency with economic oversight over the railroad industry, thus far a stark contrast to the ICC's legacy of inefficient, debilitating regulation.\textsuperscript{88}

III. Current Railroad Regulation

A. The Surface Transportation Board

Together, the Staggers Act and ICCTA provide the basis for the federal government's regulation of the railroad industry today.\textsuperscript{89} The STB, an independent regulatory agency under the Department of Transportation, is the primary means by which the policies set forth in the Staggers Act and ICCTA are carried out.\textsuperscript{90} While the Staggers Act and ICCTA plainly emphasize that competition is preferred as the

\textsuperscript{82} Thoms, \textit{supra} note 33, at 213.
\textsuperscript{83} Hardaway, \textit{supra} note 45, at 126.
\textsuperscript{84} \§ 10707. \textit{See infra} note 105 (discussing differential pricing).
\textsuperscript{85} GAO \textit{REPORT}, \textit{supra} note 23, at 4; \§ 10101(1), (3).
\textsuperscript{87} For a comparison of retained functions to those eliminated, see the STB website and pdfs thereat, \textit{available at} http://www.stb.dot.gov/stb/public/resources_icc.html.
\textsuperscript{88} The consensus among economists is that the ICC's heavy-handed regulation was responsible for the railroad industry's plight during its tenure. One study estimates regulation resource misallocation by the ICC resulted in losses of three billion dollars annually. G. M. Davis, \textit{Surface Transportation Regulation—A Succinct Analysis}, 47 I.C.C. PRAC. J. 55, 62 (1979).
\textsuperscript{89} \textit{See 49 U.S.C.} \§ 10101 (2005).
\textsuperscript{90} The Department of Transportation is also in the process of memorializing a formal National Freight Transportation Policy. \textit{See Dep't of Transp., National Freight Transportation Policy Statement} (2003), \textit{available at} http://ostpweb.ost.dot.gov/policy/Data/National%20Freight%20Transportation%20Policy%20Statement.pdf.
mechanism for maintaining the balance between railroad companies' and shippers' needs, the STB has the authority to

1. adjudicate rate cases to resolve disputes between captive shippers and railroads upon receiving a complaint from a shipper; 2. approve rail transactions, such as mergers, consolidations, acquisitions, and trackage rights; 3. prescribe new regulations, such as rules for competitive access and merger approvals; and 4. inquire into and report on rail industry practices, including obtaining information from railroads on its own initiative and holding hearings to inquire into areas of concern, such as competition.

The STB has been most visibly active in asserting not only its adjudicative power regarding rate challenge cases, but its prescriptive power in promulgating rules and standards governing those challenges as well.

B. The STB's Adjudicative Power: Rate Challenge Cases

Rate-challenge cases confront the STB with implementing its most polarizing charge: ensuring both the reasonableness of rates and railroad companies' opportunity to earn adequate revenue. A rate challenge case commences when a shipper files a complaint with the STB alleging that a railroad company is charging it an exorbitant rate, a claim which the railroad forthrightly refutes. Thus, the STB is caught in the middle of shippers and railroad companies, each side contesting that the STB has a duty to protect it. The rub for the STB is that both sides are right; nevertheless, the STB must balance the respective needs of each side, all the while considering the public interest in the matter.

1. The STB's Duty to Protect Shippers

The STB's duty to protect shippers from unreasonable rates harkens back to the creation of the ICC in 1887. The concept and parlance of a "captive shipper," first adopted in the mid-nineteenth century, correlates to the concept of "market dominance" codified

---

91. § 10101(1), (3).
92. GAO Report, supra note 23, at 38. This list is by no means exhaustive.
93. See infra Part III.B-C.
94. Compare § 10101(1) with § 10101(3).
96. See supra note 94.
98. See supra Part II.C.
in Section 202 of the Staggers Act. Therefore, in order to challenge the reasonableness of a rate, a shipper must first establish that it is a captive shipper: that the rail carrier charging the contested rate has market dominance. "Market dominance" means an absence of effective competition from other rail carriers or modes of transportation for the transportation to which a rate applies; in other words, a shipper is captive if no effective competition exists in the transportation market to ship its product. In such a situation, the shipper, hampered in the negotiation process as it may be by its lack of bargaining power, has little choice but to accept the rate it negotiates with a railroad company. Once a shipper establishes its captivity, it can then challenge the reasonableness of the rate. A rate is reasonable as a matter of law if it is less than 180% of the railroad company's variable cost of moving the shipment. If a rate is equal to or more than 180% of the railroad company's variable cost of the shipment, the STB may conclude upon investigation and hearing that the rate is unreasonable and order the railroad company to pay reparations to the shipper. Although shippers have often been successful challenging rates, the cost prohibitiveness of waging such challenges has, until recently, left many shippers feeling as though they had no adequate avenue for redress.

100. § 10707.
101. Major Issues in Rate Cases, STB Ex Parte No. 657 (Sub-No. 1), 2006 WL 3087168, at *4 (S.T.B. Oct. 30, 2006). If a shipper is not captive, i.e. where market dominance does not exist, the rate is unchallengeable. Id.
102. § 10707(a).
105. § 10707(d)(1)(A). The pricing framework in the railroad industry is unique in that much of railroads' overhead expenses are fixed and not attributable to any given shipment. Indeed, railroads incur such costs irrespective of whether there is a demand for shipping services or not. One example of these "common costs" is rail maintenance; rails have to be maintained at the same high level regardless of whether ten or one hundred trains pass over them in a given month. Thus, railroad rates are (typically) propounded in two sections: variable and common. Variable costs are the costs that can be attributed to a specific shipment, such as the salaries of the crew on a particular shipment, while common costs are a portion of the railroad's systemwide common costs. The concept of differential pricing allows railroads to allocate common costs among shippers in an unequal fashion in order to ensure that their common costs are adequately recouped. Thus, a shipper that has less alternatives for transporting its product is assessed a greater portion of a railroad's common costs; because the shipper depends more on rail transportation, railroads are justified in collecting a higher percentage of common costs from it. If a railroad tried to recoup the same portion of common costs from a shipper that had more transportation alternatives, it might not be able to get that shipper's business at all. See GAO REPORT, supra note 23, at 7-8.
106. § 11704(b).
107. The STB has recently simplified the guidelines for resolving large shipment rate disputes. See Major Issues in Rate Cases, STB Ex Parte No. 657 (Sub-No. 1), 2006 WL 3087168 (S.T.B. Oct. 30, 2006). Likewise, the STB has also simplified the guidelines for resolving small- and medium-sized shipment rate disputes. See Simplified Standards for Rail Rate Cases, STB Ex
2. The STB’s Duty to Protect Railroad Companies

The STB’s duty to protect railroad companies involves ensuring that “rail carriers” have the opportunity to earn “adequate revenues.”108 Central to that end is the concept of differential pricing.109 Because railroad transportation differs from other modes of transportation in that railroad companies must maintain the routes over which their transportation moves, railroad companies must collect from their patrons the common costs of ownership and maintenance not attributable to any given shipment.110 Differential pricing enables railroad companies to collect a greater portion of their common costs from the shippers that depend on rail transportation the most; this in turn sustains the railroad industry in the long run, as the industry can rely more heavily on the business from its steady customers.111 The STB fulfills its duty of protecting the long-term sustainability of the railroad industry and, in turn, carriers’ opportunity to earn “adequate revenues” by excluding from the rate-reasonableness evaluation threshold railroad companies’ common costs; instead, the threshold for considering the reasonableness of a rate is calculated only in terms of variable costs.112 The STB also takes affirmative steps to protect railroads by determining revenue adequacy outside the framework of rate challenges.113 “STB determines the revenue adequacy of a railroad by comparing the railroad’s return on investment with the industrywide cost of capital . . . . [I]f a railroad’s return on investment is greater than the industrywide cost of capital, STB determines that railroad to be revenue adequate.”114

3. The Public Interest

Along with considering railroad companies’ and shippers’ interests in a rate challenge case, the STB must factor into its decision a third

---

108. § 10701(d)(2).
109. See supra text accompanying note 105.
110. Contrarily, trucks rely on tax dollars for the maintenance of highways and barges need only follow the current.
111. See supra text accompanying note 105.
113. GAO REPORT, supra note 23, at 7.
114. Id. “Adequate revenues are defined as those that are sufficient – under honest, economical, and efficient management – to cover operating expenses, support prudent capital outlays, repay a reasonable debt level, raise needed equity capital, and otherwise attract and retain capital amounts adequate to provide a sound rail transportation system.” Major Issues in Rate Cases, STB Ex Parte No. 657 (Sub-No. 1), 2006 WL 3087168 (S.T.B. Oct. 30, 2006).
calculation: the public interest.\textsuperscript{115} This nebulous charge reinforces the notion that the public interest attached to the railroad industry provides the primary justification for its regulation.\textsuperscript{116} Although it may seem that "considering the public interest" merely restates the STB's duty to weigh shippers' interests against railroad companies' interests (that the public interest is necessarily accounted for in the STB's rate-challenge formula),\textsuperscript{117} the phrase injects a rather crucial substantive factor into the STB's rate reasonableness analysis.\textsuperscript{118} The STB must weigh in its determination of the challenged rate's reasonableness whether the rate is the result of market abuse or sound economic practice.\textsuperscript{119} Such determination derives only from a relative policy judgment between two alternatives: either the rate is permissibly high because the railroad must charge that amount in order to sustain itself economically (reasonable economic practice), or the rate is impermissibly high because the shipper has no alternative shipping option and has little choice but to pay the inflated rate, notwithstanding the fact that current rate relief may lead to poor service in the future (market abuse). Thus, at bottom, the STB is weighing the relative desirability of long-term economic benefits, say lower future rates and improved service, versus short-term economic benefits for the shipper, to determine reasonableness.\textsuperscript{120} This somewhat result-oriented analysis shows the overlapping of the STB's prescriptive and adjudicative roles.

C. The STB's Prescriptive Power

Unlike its adjudicative power, the STB can exercise its prescriptive power upon its own initiative—it need not wait until some sort of complaint is filed.\textsuperscript{121} Therefore, the STB's prescriptive power is potentially the most far-reaching of its powers.\textsuperscript{122} Typically, the STB announces a proposed ruling, fields comments from interested parties.

\begin{footnotesize}
\begin{itemize}
  \item \textsuperscript{115} 49 U.S.C. § 10705(a)(1) (2005).
  \item \textsuperscript{116} See supra note 5.
  \item \textsuperscript{117} See supra Part III.B.1.
  \item \textsuperscript{118} § 10705(a)(1); see also BNSF R.R. Co. v. Surface Transp. Bd., 453 F.3d 473, 485 (D.C. Cir. 2006) (noting that the "Board 'is not the prisoner of the parties' submissions' but rather has a duty 'to weigh alternatives and make its choice according to its judgment how best to achieve and advance the goals of the National Transportation Policy'" (quoting Balt. & Ohio R.R. v. United States, 386 U.S. 372, 430 (1967) (Brennan, J., conc.))).
  \item \textsuperscript{119} See GAO REPORT, supra note 23, at 43. Recall that even a rate greater than 180% of a railroad's variable cost of a movement can still be reasonable. The 180% of variable cost mark is merely the threshold for entering the reasonableness determination. See supra Part III.B.1.
  \item \textsuperscript{120} See PHILLIPS, supra note 2, at 5 (discussing long-term versus short-term economic benefits).
  \item \textsuperscript{121} See GAO REPORT, supra note 23, at 39.
  \item \textsuperscript{122} Through its prescriptive power, the STB is able to regulate railroad practices sua sponte. \textit{Id.}
\end{itemize}
\end{footnotesize}
regarding those rulings, and then issues an *ex parte* decision. While these proceedings are not formally adversarial, they often concern the administration of the STB’s adjudicative power and thus offer another forum for railroad companies and shippers to advocate their interests. The STB stretched its prescriptive legs this past year by reforming the rate challenge evaluation method in small- and medium-sized shipment rate disputes and large shipment rate dispute cases.  

1. Rate Reasonableness Evaluation Methods: *STB Ex Parte No. 657* and *STB Ex Parte No. 646*

In 2006, the STB addressed both shippers’ and railroad companies’ concerns that the rate challenge process had become overly complex and cost prohibitive by seeking comments on proposed changes to its rate challenge evaluation method. Particularly, the STB stated that “there [had] been major issues in large rail rate cases that were being litigated again and again, with the parties in individual cases unable to develop acceptable solutions to problems that they had identified with the existing approach.” The STB subsequently issued *STB Ex Parte No. 657*, the first of two rulings to make the rate challenge evaluation method less complex and less costly. *STB Ex Parte No. 657* adjusts the methodology of analyzing the “stand-alone cost” of a shippers’ movement, which seeks to determine whether a challenged rate improperly includes costs from which the shipper derives no benefit. By limiting the types of evidence and arguments presentable in large shipment rate challenge proceedings, *STB Ex Parte No. 657* lowers the overall cost of the rate challenge process, thereby enabling shippers to bring lower value claims and seek meaningful relief where market abuse has occurred. The STB next issued *STB Ex Parte No. 646*, a ruling in which the STB sought “to make its rail rate dispute resolution procedures more affordable and accessible to shippers of small

---

123. *See, e.g.*, Simplified Standards for Rail Rate Cases, *STB Ex Parte No. 646* (Sub-No. 1), 2007 WL 2493509, at *2 (S.T.B. Sept. 4, 2007) (“The Board heard the views of rail shippers, railroads, rail labor, state governments, and other parts of the federal government.”).

124. *Id.*

125. Major Issues in Rate Cases, *STB Ex Parte No. 657* (Sub-No. 1), 2006 WL 3087168 (S.T.B. Oct. 30, 2006). The STB also addresses practices tangential to rate challenge cases, such as fuel surcharge practices. *See Rail Fuel Surcharges, STB Ex Parte No. 661* (Sub-No. 1), 2007 WL 201205 (S.T.B. Jan. 25, 2007).


128. *Id.*

129. *Id.* at *6.

130. *Id.* at *4.
and medium-size shipments, while simultaneously ensuring that the
new guidelines do not result in arbitrary ratemaking." In that rul-
ing, the STB clearly acknowledged its role as the arbiter of shippers’,
railroads’, and the public’s interests:

The Board concluded that significant changes to Simplified Guide-
lines were necessary to achieve the dual statutory goals of providing
captive shippers meaningful access to regulatory remedies for rail
rates that are unreasonable, while recognizing the need for railroads
to earn a reasonable return on their investments so that they will
have the resources to make the investment needed to continue to
serve the transportation needs of their customers.

STB Ex Parte No. 646 makes available to shippers challenging small-
and medium-sized shipment rates both a “simplified-stand-alone cost”
evaluation method and a “Three-Benchmark” evaluation method. Thus
the STB has reduced the cost of bringing rate challenges, while,
at the same time, increasing shippers’ avenues for proving that market
abuse has occurred.

D. **Deregulation: So Far, So Good**

The effect of the Staggers Act and the ICCTA has been overwhelm-
ingly positive. As the latest United States Government Accounta-
bility Office Report on the health of freight railroads notes, “[t]he
freight railroad industry’s financial health improved substantially as
railroads cut costs through productivity improvements; streamlined
and right-sized their rail networks; implemented new technologies;
and expanded business into new markets, such as the intermodal mar-
ket.” As the health of the industry has improved, the level of
federal regulation seems to have effected an equilibrium of sorts: rail-
road companies are able to earn near-adequate revenues from rates
established through competition, and captive shippers have a more
effective avenue of redress to challenge what they deem to be exorbi-
tant rates. Record income in the railroad industry has also enabled

---

132. *Id.*
133. *Id.* at *3* (permitting shippers to choose under which method they wage their rate challenge).
134. *See id.*
135. GAO REPORT, *supra* note 23, at 9 (“There is a widespread consensus that the freight rail
industry has benefited from the Staggers Rail Act.”).
136. *Id.* at 3.
137. *Id.* at 9-10.
138. *See id.* at 52 (noting that in 2004 the STB determined that one railroad was revenue
adequate and that others were approaching revenue adequacy).
139. *See supra* Part III.C.1.
the railroads to invest $375 billion in infrastructure, which benefits shippers through higher quality and more efficient service. Although not all of the industry’s problems have been solved, the problems that remain do not lend themselves to solution via increased regulation without collateral detriment to both shippers and railroads. But many shippers remain dissatisfied with the level of regulation in the railroad industry, some even calling for the elimination of the STB altogether.

IV. The Movement for Reregulation

Although the health of the railroad industry has substantially improved since the passage of the Staggers Act, some shippers support increased regulation of the railroads, often referred to as “reregulation.” Shippers support reregulation for a variety of reasons, but their common complaint is that without forced competition within the railroad industry, shippers that have access to only one railroad are being forced to pay exorbitant rates without any realistic alternative: a veritable Hobson's choice. These shippers often refer to themselves as “captive shippers,” even though the STB may not yet have determined the railroad that serves the shipper to have market dominance. Forced competition within the railroad industry, they argue, will benefit shippers through lower rates. In order to inject competition into the industry, shippers propose a variety of solutions.


141. See infra Part V.D.

142. See infra Part V.D.


144. See supra note 11.

145. They argue, thus, that other modes of transportation are not a realistic alternative.

146. This is the same terminology that the STB uses once it has found that a railroad has market dominance in rate challenge cases. Major Issues in Rate Cases, STB Ex Parte No. 657 (Sub-No. 1), 2006 WL 3087168, at *4 (S.T.B. Oct. 30, 2006). Thus shippers use a clever rhetorical device to characterize themselves as market dominated without the STB having made that determination. But see Gao Report, supra note 23, at 3 (“It is difficult to determine precisely how many shippers are captive because available proxy measures can overstate or understate captivity.”).

147. See Phillips, supra note 2, at 5 (discussing long-term versus short-term economic benefits).

148. See infra Part IV.B.1-4. These solutions are often collectively referred to as “competitive access.” Woodman & Starke, supra note 16, at 270.
A. The Bane of Shippers' Existence: High Rates Due to a Lack of Competition

At a glance, shippers' self-characterization as "captive" appears to stem only from their desire to have lower rates, which, in and of itself, is an integral motive to the proper functioning of the market. However, shippers' cries of captivity encompass more than rational economic dissatisfaction with high rates; their grievance is that there is a lack of competition within their market, and thus that the market is flawed. Without competition, the market forces of supply and demand do not protect shippers from not only high, but also unfair, exorbitant rates. Shippers in such markets, therefore, are unprotected from economic abuse by railroad companies—they lack any structural protection ordinarily provided by a properly functioning market. What results are rates sometimes seventy-five percent higher than rates in a competitive market. Shippers' proposals are aimed at injecting competition into the railroad industry not only to pull down rates, but also to impose structural protection from economic abuse through a properly functioning market.

B. Shippers' Proposals

Shippers propose a number of regulatory measures that, they argue, would inject meaningful competition into the railroad industry. While many of their proposals are already in practice pursuant to individual service contracts in the rail transportation industry, shippers argue that the STB should mandate that railroad companies adopt and implement each measure described below.

1. Reciprocal Switching

Reciprocal switching requires one railroad company to transport the cars of another railroad company over the first railroad company's tracks for a fee, usually within a terminal area, thereby enabling a shipper located along one railroad company's line to access a second railroad company's services. To illustrate, Shipper, located along-
side Railroad Company A’s tracks, would have access to Railroad Company B’s services if A were mandated to move B’s cars onto A’s tracks. This would give Shipper two rail shipping options and would inject competition into the railroad industry.

2. Terminal Agreements

Terminal agreements require one railroad company to grant access to terminal facilities on its rail line to another railroad company, thereby enabling the second railroad company to travel over the first railroad company’s tracks in order to reach and use the first railroad company’s terminal facilities.154 To illustrate, Shipper with access to both Railroad Company A and Railroad Company B wants to ship its product to Town X, in which only Railroad Company B has a rail yard. Because Railroad Company A does not have a rail yard in Town X, Shipper cannot ordinarily use Railroad Company A’s services to ship its product to Town X. However, if a mandatory terminal agreement existed, Railroad Company B would be required to allow Railroad Company A to access Railroad Company B’s terminal rail yard in Town X, thereby allowing Shipper to choose to ship its products with either Railroad Company A or B. A mandatory terminal agreement would require that A have access to B’s facilities and, therefore, would inject rail competition into Shipper’s market.

3. Trackage Rights

Trackage rights require one railroad company to permit another railroad company to operate over the first railroad company’s tracks.155 Therefore, Railroad Company A could travel over Railroad Company B’s tracks and vice versa. Open access to rail infrastructure would give a shipper numerous options, thus injecting competition into the rail industry.

4. Bottleneck Rate Setting

Bottleneck rate setting requires railroad companies to set rates for portions of a route where only one railroad has track between two given points.156 For instance, a shipper may have access to two railroad companies both at the point of origin of a shipment and at its final destination, but only one of those railroad companies has track along a portion of the route. Requiring that railroad company to es-

154. Id. at 45-46.
155. Id. at 45-47.
156. Id. at 48-50.
establish and disclose a rate for that portion of the shipment, along with granting the other railroad trackage rights, would give the shipper complete access to two railroad companies and inject competition into the railroad industry.

C. Shippers' Efforts on the Hill: Lobbying and Legislation

Shippers' calls for competitive access have been rebuffed by the STB repeatedly, with the STB stating that "competitive access raises basic policy questions that are more appropriately resolved by Congress." The STB's advice did not fall on deaf ears. Legislation has been introduced in each Congress since the STB stated its deference to the legislative branch, most recently in the 110th Congress via the Railroad Competition and Service Improvement Act of 2007. Previous legislation died in committee in the 109th Congress and Senator Dorgan of North Dakota vehemently vowed to reintroduce similar legislation in the Democratic-controlled 110th Congress, which may prove to be a friendlier landscape for shippers' interests. He stated that "[t]he railroads have a pretty good thing going. They have monopoly power in their industry and the Surface Transportation Board, which was supposedly created to protect rail customers, instead seems to be more concerned with making sure the railroads don't have to compete with one another." Shippers' have also lobbied for legislation that would remove railroads' exemption from antitrust laws, most recently via the Railroad Antitrust Enforcement Act of 2007. Shippers' reregulation efforts in Washington, in one form or another, all seek a common end: imposing mandatory intra-industry competition on the nation's railroads.

V. Increased Regulation Is Not The Answer

Shippers' calls for reregulation are misguided. Contrary to shippers' rhetoric, shippers in markets that are served by only one railroad are

157. GAO REPORT, supra note 23, at 41.
158. S. 953, 110th Cong. (2007); H.R. 2125 110th Cong. (2007). This piece of pending legislation memorializes shippers' proposals for competitive access. The Railroad Competition and Service Improvement Act of 2007, if passed in its current form, would require a railroad company, upon shipper request, to establish a rate and provide service between any two points on the railroad's system; mandate that railroad companies enter into reciprocal switching agreements upon an STB determination; require the STB to refer certain cases to binding arbitration; and empower the STB to investigate railroad company violations on its own initiative.
not necessarily captive shippers.\textsuperscript{161} Rather, "captive" is a term that refers to shippers in markets where no "effective competition from other rail carriers or modes of transportation for the transportation to which a rate applies" exists.\textsuperscript{162} Thus non-captive shippers that are served by only one railroad have little basis for complaint, as, by definition, other modes of transportation are available to ship their products, and therefore create competition in their market.\textsuperscript{163} With competition from other modes of transportation present, non-captive shippers’ justification for reregulation desists. Captive shippers, however, have a legitimate gripe.\textsuperscript{164} Without effective competition to drive down railroads’ rates, captive shippers pay much higher rates, primarily due to the railroad industry’s demand structure and differential pricing.\textsuperscript{165} But even captive shippers are protected from anticompetitive behavior or market abuse on the part of railroads; the STB rate challenge safeguards currently in place offer fair and adequate avenues for redress.\textsuperscript{166} The strongest protection that the STB offers shippers, however, also provides the strongest argument against reregulation: the STB’s charge to protect the public interest.\textsuperscript{167} By weighing the public interest in short-term versus long-term benefits, the STB ensures that shippers have a railroad industry to rely on twenty years down the road.\textsuperscript{168}

A. Competition from Other Modes of Transportation

Only where a railroad has market dominance is a shipper "captive."\textsuperscript{169} Otherwise, shippers are protected from market abuse by competition against the railroad industry vis-à-vis other transportation industries.\textsuperscript{170} For instance, take the case of a grain shipper in North Dakota whose grain elevators sit alongside tracks served by only one railroad. Let us assume that the grain shipper has been shipping its crop via railroad for the last fifty years, and that, as a steady customer, it has been assessed an increasingly greater portion of the railroad’s

\textsuperscript{161} See supra Part III.B.1. See also supra text accompanying note 146.


\textsuperscript{163} § 10707(a).

\textsuperscript{164} See infra Part V.B.

\textsuperscript{165} See supra note 105.

\textsuperscript{166} See supra Part III.B.1.

\textsuperscript{167} 49 U.S.C. § 10705(a)(1) (2005). Indeed, the American public has a strong interest in having a healthy rail industry now and well into the future.

\textsuperscript{168} See infra Part V.D.

\textsuperscript{169} See supra Part III.B.1.

common costs over that period. Because it shoulders a greater proportion of the railroad's common costs than a similarly situated new or sporadic shipper would, the overall rate for the current year's shipment is therefore relatively high. However, the grain shipper also has at its disposal a trucking company that can carry out the shipments, albeit at a greater cost or over a longer period of time. Unless the STB determines the competition from the trucking company to be ineffective, the grain shipper's decision to ship via the railroad despite the relatively high rates represents an economic determination that the railroad's service is more beneficial to the shipper than that of the trucking company. In such a hypothetical situation, the market functions properly and the best quality service for the price wins out. Absent a determination by the STB that a railroad company has market dominance, adequate competition exists in a shipper's market to safeguard it against market abuse on the part of the railroad.

B. Adequate Safeguards for Captive Shippers

Captive shippers have a legitimate gripe when it comes to their protest of high rates, but reregulation is not the cure to their ailment. The captive shippers' problematic situation is unique to the railroad industry, largely because railroad is the only mode of transportation in which the industry's companies carry the burden of maintaining the ways over which its carriers move. In contradistinction to railroads, trucks travel over roads ultimately financed by tax dollars and barges over water that need not be maintained. The result is that railroad companies must recoup their common operating costs either through rates paid by their customers or by an alternative source. The practice of differential pricing puts a large onus of recouping common

171. See supra text accompanying note 105 (discussing differential pricing).
172. There may also be other considerations, such as degree of risk, coordination with buyers, etc.
173. See § 10707.
175. See supra text accompanying note 33.
176. The decision to have railroads be served by the same companies that own them goes back to the early days of the railroad when individuals owned their own cars and pulled them by horse. Substantial problems developed when parties would meet each other in the middle of a track traveling in opposite directions and one would have to remove its equipment so the other could pass. See supra text accompanying note 33.
177. Private funds are also a source of recouping common costs for railroads. But in order to attract private capital, return on investment must be competitive with other markets. Rate regulation that would result in less profits for railroad companies would also detract private investment, resulting in less reinvestment in infrastructure and ultimately poorer service. See GAO REPORT, supra note 23, at 55.
costs on shippers in markets lacking competition from other modes of transportation, which unequally burdens those captive shippers.\textsuperscript{178} But even captive shippers are protected by the STB from market abuse or anticompetitive behavior on the part of railroad companies. The STB's rate reasonableness analysis has in place adequate safeguards to prevent market abuse. Upon receiving a complaint from the shipper, the STB can find a rate unreasonable only if the rate is equal to or exceeds 180\% of the variable cost of the shipment and the railroad has market dominance over the shipper.\textsuperscript{179} Only shippers that establish market dominance, captive shippers, present a difficult problem to resolve. Contrarily, non-captive shippers have other modes of transportation at their disposal, and thus are subject to the competition of the market. While the captive shipper may argue that the STB's analysis unfairly fails to take into account the relatively large percentage of common costs that the shipper is subjected to in the challenged rate, it would also have to concede that it is paying less in common costs than if the railroad instead had to include the same common costs being charged to the captive shipper in a rate bid in a more competitive market and lost the bid to another mode of transportation. Such a loss of business would ultimately shift a greater portion of common costs to the shipper, further increasing its rate. The STB's analysis takes into account this precarious problem unique to the railroad industry by setting the rate reasonableness threshold on the basis of variable cost only.\textsuperscript{180}

\textbf{C. The Public Interest: Long-Term versus Short-Term Benefits}

The STB is charged with overseeing the railroad industry in a manner that protects the public interest in having reliable, efficient rail transportation.\textsuperscript{181} With this function comes the responsibility of analyzing the long-term and short-term consequences of certain regulatory measures, as well as the relative desirability of implementing such measures. Shippers’ proposals for injecting competition into the railroad industry share a common thread: each proposal offers moderate short-term benefits at the expense of certain long-term detriment. First, each proposal seeks to inject competition into the railroad industry in order to lower rates without considering the competition that the railroad industry faces from other modes of transportation.

\textsuperscript{178} See supra text accompanying note 105.
\textsuperscript{179} Major Issues in Rate Cases, STB \textit{Ex Parte} No. 657 (Sub-No. 1), 2006 WL 3087168, at *4 (S.T.B. Oct. 30, 2006).
\textsuperscript{180} See supra text accompanying note 105.
\textsuperscript{181} See supra Part III.B.3.
Forced competition that initially results in lower rates for shippers would also prevent railroad companies from recovering their common costs of operation. In order to recoup those costs, a railroad company would have no choice but to include those costs in bids in markets where competition from other transportation modes is fierce, thus presenting the possibility that it would not get the shipping contract. Thus, the railroad company would have to recoup an even greater percentage of its common costs from captive shippers, a result the shippers likely did not intend.  

Second, the moderate benefit of lower rates for a time carries with it collateral detriment. Mandating reciprocal switching, for example, would entail considerable coordination between railroad companies, resulting in lost time and higher common costs. Those costs would be passed on to shippers (and ultimately consumers) in the form of higher rates. Forced trackage rights and terminal agreements present maintenance allocation problems: where one railroad company is deriving a larger benefit from a shipper by running trains over another railroad company’s tracks than the railroad company that owns the tracks, the owner lacks the incentive to maintain those tracks. The result is decreased efficiency, poor track maintenance, and, ultimately, lower safety standards. While forced competition may drive rates downward at first, a practical analysis of the proposals put forth by shippers reveals that forced, artificial competition would result in lost time and money and would harm the industry as a whole over the long run.  

Such a downfall of the American railroad industry would inevitably affect the United States’ economic position in the world; a less reliable and less efficient rail

---

182. Woodman & Starke sum up this argument eloquently:

Any mandated reduction in rates . . . would have a destructive effect on the rail carriers’ ability to differentially price. Any such mandated reduction would require rail carriers to increase rates on other traffic. As a result, traffic subject to intermodal competition would shift to other transportation modes where it could move at lower rates, leaving the rail carriers with less market share and decreased sources of revenue to cover their costs. Any contribution made by those shippers to capital and operating costs would be lost, forcing carriers to make up that shortfall through rate increases on the remaining traffic to the extent competitive pressures permit. The ultimate effect would be a loss of the ability to differentially price rail service, resulting in rate increases, lost traffic, decline in revenues, lost jobs, and deterioration in service—the same litany of woes, it should be noted, that characterized the rail industry in the days of significant Government regulation.  


183. See id. Joint trackage rights and reciprocal switching occur in the open market, without having to be forced. See GAO REPORT, supra note 23, at 44-48. Mandating the shippers’ proposals would upset the balance of resource allocation and lead to inefficiency and lower safety standards.
transportation system impinges the nation's ability to export its products and ultimately compete with other nations on the global market.

Finally, the main reason that reregulation is not the proper solution to shippers' cries for rate relief is that the economic atmosphere in the next twenty years requires investment in infrastructure today. Studies predict that the demand on the railroad industry is going to increase by more than fifty percent, and that the ever-aging infrastructure of the national railroad system is going to require substantial refurbishment in order to handle that demand. The sources of capital for reinvestment are few and far between: federal subsidy, private reinvestment by the railroads themselves, or an innovative cost-sharing arrangement. As the regulatory framework stands today, railroads are beginning to earn substantial income which they are generously reinvesting in infrastructure. The last two years of record income by the four largest railroads has led to record investment in infrastructure and increasing capacity. Although captive shippers certainly have cause to demand relief from high rates, reregulation would be a short term solution with colossally negative long-term consequences.

D. Looking Forward: Suggestions for Salvage

Shippers' complaints of high rates ultimately stem from a problem that has no easy solution. While their grievances focus on the lack of competition within the railroad industry, the root of their problem is the demand structure and differential pricing method unique to the railroad industry. The hard problem that needs to be resolved in order for the American railroad industry to survive is the problem of railroad companies recouping their common costs of operation. Because the cost of maintaining rail lines is constant and not tied to demand, railroad companies have significant outlay costs. Their return on investment does not adequately cover their operation costs, as evidenced by a near forty billion dollar shortfall between 1981 and

185. The studies discussed in the GAO Report, supra note 23, project that demand for freight services will increase between thirty-two and ninety-nine percent. One study estimates that four billion dollars annually in reinvestment will be needed to meet that demand. GAO Report, supra note 23, at 54.
187. See supra note 182.
188. See supra note 105.
189. See supra text accompanying note 105.
In order to bridge that gap, railroad companies rely on private investment, which must be competitive with other markets to attract capital. The practice of differential pricing enables railroad companies to recover a larger portion of their common costs from steady and captive shippers currently, but as other modes of transportation become more competitive in those markets railroad companies will be left without any source of recouping those costs. The problem is a tough one, and, to date, only by charging their most reliable customers the highest rates are railroad companies able to sustain the railroad infrastructure and industry—this seems an odd way of rewarding loyalty indeed. But differential pricing is the best solution to the common costs problem to date, and much more beneficial to the nation as a whole than reregulation. Perhaps the STB can request innovative proposals regarding common cost allocation among shippers, railroad companies, and taxpayers in a more equitable manner. The problem, however, is not going to solve itself and promises to be a thorn in the railroad industry's side in the near future. Only by remedying that problem can shippers and railroad companies both benefit and optimally serve the nation together.

VI. Conclusion

The importance of competition in a market economy cannot be overstated. However, shippers' assertion that an absence of competition within the railroad industry translates to monopoly power in the freight transportation market is simply incorrect. The railroad industry must compete with other modes of transportation for shipping contracts in most of the markets it serves; such competition provides shippers the structural protection of the market against possible economic abuse by railroad companies. Because the public interest is also protected by market forces, reregulation is unnecessary and would only harm the future of the railroad industry. The next twenty years promise to put an unprecedented demand on the efficient rail system that the railroad industry's escape from heavy regulation created. By maintaining a low level of economic regulation, the federal government will enable the nation's railroad companies to reinvest in the nation's infrastructure, thereby avoiding a slew of foreseeable national problems before they materialize while maintaining the United States'
economic position in the global market. Such is the federal government's responsibility to the nation, its citizens, and the many generations of Americans that will one day inherit a greater nation than did their ancestors.