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**Surface Transportation Board
U. S. Department of Transportation
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**The 25th Anniversary of the Staggers Rail Act of 1980:
A Review and Look Ahead**

STB Ex Parte No. 658

A study of the legislative history of the Staggers Rail Act of 1980 clearly indicates the Congress had several major policy objectives and purposes the legislation was intended to accomplish by "deregulating" the railroad industry.

The policy Congress enacted in the Staggers Act was that market competition should replace government regulation wherever possible. The purpose was to release the nation's Class I railroads from most government regulatory constraints in order to allow railroad companies the opportunity to achieve financial health. Deregulation was also envisioned to result in gradually increasing competition that would stimulate efficiency, reliability, and lower costs to all rail customers.

While Congress anticipated the competitive marketplace would bring significant benefits over time, it also acknowledged that – at least initially – some rail customers would be "captive" to the monopoly power resulting from single rail-carrier service. Therefore, the Staggers Act also mandated continued regulatory oversight in order to safeguard against potential economic market power abuse by individual railroads. Congress first charged the Interstate Commerce Commission, and later in 1995 the Surface Transportation Board, with protecting these captive customers from the abuse of railroad monopoly market power.

Twenty-five years after the Staggers Act, deregulation is clearly not working for "captive" rail customers in many vital industries, as evidenced by the experience of consumer-owned electric cooperatives. Today, cooperatives that are "captive" under current practices and decisions are subject to the unrestrained monopoly power of the rail carrier upon whom they are dependent.

With some rare exceptions, cooperatives that are "captive" are not able to negotiate reasonable commercial relationships with their monopoly carriers. They have rates and terms of service dictated on a "take-it-or-leave-it" basis – rates that are significantly and

unreasonably high when compared to non-captive shippers. In addition to exorbitant rates, captive shippers often receive poor service and suffer from a lack of rail capacity.

NRECA urges the Surface Transportation Board to adopt new approaches that will actually accomplish the goals and objectives embodied in the Staggers Rail Act. We implore the Board to begin anew to ensure against railroad abuse of monopoly power over captive rail customers, safeguarding fair and reasonable treatment for captive shippers.

I would point out that the dismal experience of captive shipper cooperatives is shared by a wide array of other industries and interests across a broad swath of mostly rural America. Extractive mining and minerals operations, forest and timber harvesters and wood product processors, a wide variety of chemical product manufacturers, the paper and pulp industries, and our beleaguered farm and ranch producers – any who are captive to a single rail provider face very similar economic burdens because the goals and policies of the Staggers Act are not yet fully implemented in the manner Congress envisioned.

There are a couple of overarching factors that have brought about today's captive shipper dilemma. One factor is that instead of the robust expansion and competition Congress intended, the railroad industry has undergone a drastic consolidation. In the twenty-five years since Congress deregulated rail service, the major railroads have consolidated from over forty major carriers to only two major rail carriers in the west, two in the east, and one in the center of the country (with two smaller majors providing essentially regional service).

The second factor is that the number of captive rail customers has remained relatively large and appears to have actually expanded due to these consolidations. Dr. Curtis Grimm of the University of Maryland testified to Congress in 2004 that at least 20% of current rail traffic is captive, based on STB data that is now somewhat dated.. Today, the percentage of captives may be significantly higher, but a lack of public access to information makes an exact calculation impossible. We urge the Board to require production of sufficient data in order to obtain an accurate calculation of the true extent of the captive shipper problem, while imposing any necessary safeguards to protect the railroads proprietary interests.

NRECA has determined from a recent survey of our members, however, that at least 40-percent of our coal-fired generation and transmission cooperatives are subjected to captive rail rates for their shipments of coal. This issue is particularly important to our nearly 40-million consumer-owners because about 80% of the electricity produced by cooperative generators is fired by coal. And we should all be aware that when consumer-owned, captive electric cooperatives are charged arbitrary and unreasonably high freight rates for that coal, those increased costs make it even more difficult for our industrial, manufacturing, processing, and agricultural producers to be competitive in domestic and world markets, and impairs their ability to retain and expand jobs, facilities, and operations.

It is the desire of NRECA and its member cooperatives that rail carriers remain economically strong and viable in order to attract adequate funding necessary to maintain and expand the rail system in the United States. When some asked us to object, we declined to voice opposition to significant new funding for railroad infrastructure development in the recently enacted highway bill legislation. In spite of our desire to work with the rail industry to ensure better service and more capacity, however, we do not believe this should be

accomplished on the backs of captive rail shippers. Such a situation was not then, nor is it now, what was envisioned by Congress in passage of the Staggers Act in 1980.

I would like to offer some additional observations regarding the current problems facing captive rail customers, and how we have arrived at this juncture, despite the well-justified and well-intentioned goals and promises expressed by the Congress and embodied in the Staggers Rail Act of 1980. There are several readily identifiable practices and decisions that have contributed to an atmosphere conducive to monopoly abuse of captive rail customers.

First, it would appear that the long-standing utilization of skewed methodologies for tracking the financial performance of the major railroads results in analyses that consistently understate their financial health. Such misleading reports then give rise to the incorrect notion that regulators and policy makers dare not grant fair and equitable relief to captive customers lest the railroads fall into a financial abyss. This problem was addressed by a staff alumnus of the Board, Frank Wilner, in an article titled "A Tale of Two (Railroad) Stories," (*Journal of Transportation Law, Logistics and Policy*, I2Q2005, Vol. 72, No. 2, pp 235 – 247).)

Wilner observes that – over the past five years - no realistic and accurate analysis of the actual annual financial reports of the major railroads or their annual filings with the Securities and Exchange Commission or the optimistic Wall Street investment recommendations regarding their stock could possibly have arrived at the gloomy prognosis of railroad financial health that has resulted consistently from the methodologies currently employed.

NRECA urges the Board to re-examine the current methodologies and make adjustments that will tell the real story of railroad financial health. It is difficult at best for policy-makers to arrive at fair and reasonable conclusions when there is such discrepancy in the data provided. In a July 28, 2005 article, "Norfolk Southern, CSX Profits Rise on Brisk Demand," the *Wall Street Journal* goes a long way in demonstrating to the public that – far from what current agency methodologies report – the freight rail companies are extremely profitable and are experiencing record profits at the expense of captive rail customers.

Second, over the past 24 years the Surface Transportation Board (and its predecessor, the ICC) have made three crucial decisions that deny captive rail customers access to railroad competition and contribute to preventing these shippers from being able to secure fair and reasonable rates. The effect of these decisions is partially responsible for denying captive rail customers the basic reasonableness and fairness that Congress intended in 1980 by promoting market competition wherever possible.

The first decision in the mid-1980s by the Interstate Commerce Commission, occurred when the ICC determined that one rail company would be required to allow another company the use of critical infrastructure facilities ("terminal access" and "reciprocal switching") to aid in facilitating competition. The ICC ruling established a burdensome standard of proof - not founded in law - and changed a relatively straight-forward proceeding into a complex antitrust case. The Board can and should remove this non-statutory standard of proof that has been engrafted onto what Congress clearly intended to be a pro-competitive provision of law.

The second area of decisions regards a more sinister and circuitous practice of the major freight rail carriers, and over the years the responsible agencies have approved the "paper barriers" practice. The "paper barriers" practice constitutes a perverse abuse of The Staggers Rail Act, circumventing the congressional objective and intent of protecting captive shippers from unreasonable and monopolistic abuse. One of the mechanisms provided to the railroads under the Staggers Act was the ability to "rationalize" their systems. This led in the early 1980s to the transfer of less profitable track from the major railroads to short line and regional railroads. Hundreds of short line railroads were created during this period of time. Many of these short lines have the potential to interconnect with more than one major rail carriers so that they could in theory provide access for captive rail customers to competitive rail service..

Unfortunately, by the late 1990s, captive rail customers began discovering that this track was not being sold by the major railroad. Instead, it was being leased under terms and conditions imposed by the major lines that severely restricted the short line railroad from interconnecting with any major railroad other than the landlord railroad. This lease provision, means that the short line essentially becomes only the alter ego of the major railroad and is not an avenue through which captive rail customers can gain access to competitive rail service. The increased competition that could have been realized from the proliferation of short lines has not occurred. Captive rail customers often remain captive to a short line railroad that is, in turn, captive to the major railroad from which it leases its track!

This development certainly thwarts a major goal of the Staggers Act, and provides a display of raw monopolistic market power to prevent competition. NRECA strongly urges that the "paper barriers" practice be expeditiously outlawed by the Board, or if necessary that Congress be petitioned for a grant of any necessary authority to end this practice.

The third action that unfairly discriminates against captive shippers was made in the "bottleneck" decision of December, 1996. In that case, it was decided that a major railroad that can provide service to a customer at both the origin and the destination could employ that power to deny the customer access to a competing railroad. This seems to NRECA's member-owners to be a situation that cries out for a pro-competitive solution that would further the proper implementation of the Staggers Rail Act. Unfortunately, the decision once again sided with the railroads, allowing them to use their monopoly market power to deny rail customers access to competition where competition actually could exist except for this ruling.

A good example of this is that, because of the "bottleneck" decision, either of the two railroads providing originating service in the Powder River Basin can hold a utility's coal shipments captive for the entire movement if that railroad also controls the last few miles of track into the generating facility – and the rail company charges "captive" rates accordingly. Many of our rural electric cooperative and a large number of other utility generators depend on the Powder River Basin for their coal supply. Thus, utilities that move unit trains of coal from the Basin to their facilities sometimes face unfair and predatory captive rates for movements of 1500 miles, when their true captivity is only fifteen or twenty miles. This 1996 decision can and should be reversed immediately to allow competition to flow to more captive rail customers and help meet the goals of the Staggers Act.

Congress also directed the development of a "rate reasonableness" process that would protect captive rail customers from unreasonably high rail rates. The STB is the exclusive forum for rate cases, since these cases cannot be brought in the state or federal courts and are not jurisdictional to state railroad commissions.

Unfortunately, the current rate reasonableness process costs petitioners at least \$3 to \$5 million, takes at least two years and can only be brought by rail customers that move unit trains. The hundreds of rail customers that are captive, but do not move unit trains, simply have no recourse. One NRECA member – Arizona Electric Power Cooperative – did undertake an unsuccessful rate appeal costing more than \$3-million. The rate standard adopted in rate appeal cases - "stand alone cost" - makes no sense from a practical perspective. All of the information needed to successfully demonstrate the costs for a "stand alone railroad" is in the hands of the railroad defendant. All burdens of proof are on the petitioner; and the rate standard is so vague that its interpretation can shift from case to case. Indeed, over the last three years, the acceptable level of rates allowed to be charged to captive rail customers in rate reasonableness cases has increased 50% without any change in the rate standard!

The current rate reasonableness process has failed and – combined with the "paper barriers" and "bottleneck" practices - continues to pose an increasing burden on captive shippers and on the ability of hundreds of communities across the nation to retain and attract viable industries necessary for economic stability and development. NRECA calls on the Board to adopt and implement a fair and equitable process that will determine adequate and reasonable rates to protect both the railroads and shippers.

NRECA's electric cooperative members do not believe the railroads are living up to the trust that Congress bestowed in enacting the Staggers Rail Act. Our members are most concerned over exorbitant and punitive rates and poor service. I can honestly say NRECA's membership does not believe the current state of railroad oversight and regulation adheres to the spirit or the letter of the Staggers Rail Act. Our membership asks in the strongest terms possible that the Surface Transportation Board act promptly to take corrective action to implement the clearly expressed intent of Congress that mandated protections against monopoly power and transportation rate fairness for captive rail customers.

NRECA - on behalf of the nearly 40-million consumer-owners served by rural electric cooperatives spread across roughly 74-percent of America's land area – calls on the Board to begin immediately to remedy the anti-competitive practices that have grown up under the Staggers Rail Act of 1980 as interpreted and implemented over the past twenty-four years. We are sincere in wanting to work with the Board, the railroad companies, and other impacted industries in an effort to help find solutions that ensure the continued health of our rail transportation resources. All our membership asks in return is fair treatment and reasonable rates for captive rail customers as envisioned and mandated in the Staggers Rail Act of 1980.

Thank you for the opportunity to testify before you today.