

Captive Rail Relief and the 108th Congress

THE ISSUE

U.S. manufacturers that produce bulk products (paper, chemicals, grain, coal, etc.) usually depend on rail transportation because rail is the only way they can move their products cost-effectively over long distances. Many facilities operated by these manufacturers are "captive," or served by only one railroad company.

Since the U.S. railway industry was partially deregulated by the 1980 Staggers Rail Act, it has undergone dramatic consolidation, shrinking from more than 40 Class I railroads to five dominant carriers today. This consolidation has significantly reduced rail competition, leading to substantially higher costs for many rail customers.

The Surface Transportation Board (STB) is an independent administrative agency housed within the U.S. Department of Transportation with exclusive jurisdiction over rail issues, including whether rail rates are unreasonably high. Three critical decisions made since the mid-1980s by the STB (and its predecessor, the Interstate Commerce Commission), have further reduced customer access to rail competition.

These decisions are known as:

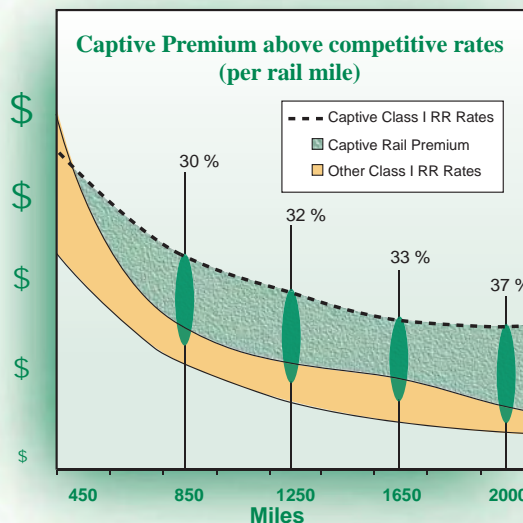
- **Bottleneck**, which prevents a captive rail customer from gaining access to rail competition where it exists;
- **Terminal Access**, which also prevents rail customers access to competition where it exists;
- **Paper Barriers**, which allow railroads to impose anti-competitive restrictions on track they sell or lease to small, "short line" railroads, thus blocking rail customer access to competing rail carriers.

THE COST OF CAPTIVITY

"Differential pricing" is a practice allowed under the Staggers Act that enables railroads to charge captive rail customers higher rates than those charged on competitive lines. A 2003 analysis by Gaithersburg, Maryland-based Escalation Consultants, Inc. published in the quarterly *Rail Price Advisor* found that captive rail customers are being charged more than double what non-captive companies pay to ship commodities on the country's four largest Class I railroads. (Imagine the reaction of railroads if four major diesel fuel suppliers were available to them, but they were allowed to purchase fuel from only one, at whatever price it dictated! That is exactly the situation faced by captive rail customers.)



Instead of evolving toward increased competition since deregulation, the rail industry has become more concentrated and less competitive. Below is a cost curve that illustrates the premium one company pays at a captive facility it owns.



Although captivity and differential pricing were envisioned in the Staggers Act, it is clear that an unintended consequence also resulted: deregulation without competition.

Transportation is one of the largest operating costs incurred by most manufacturing companies, which means that unfairly high rail freight rates weigh even more onerously on their competitiveness. The unreasonably high rail rates that result from lack of competition are leading to the loss of American jobs nationwide as commodities are being imported more cheaply than they can be produced—and transported—in our country.

CURRENT REMEDIES DON'T WORK

If they determine they can no longer absorb unreasonable captive rates, captive rail customers are left with few options but to attempt negotiations with their rail carriers, usually to no avail. After getting permission from the Surface Transportation Board, they can spend millions of dollars on a "build-out," a rail line connecting their facility to rail competition. Their only other option today is to file a "rate relief case" with the STB, which reviews the situation and has the authority to mandate that a railroad charge more equitable rates. However, just filing a case costs more than \$60,000, while the total cost of prosecuting the case generally tops \$2 million in legal and consulting fees and takes several years to resolve. The longest case on record took 12 years to complete! It is clear that these limited options are not sufficient in the face of substantial continuing railroad monopoly power. Captive rail customers remain today where they were in the late 1800s: at the railroads' mercy.

CAPTIVE RAIL CUSTOMERS LAUNCH A UNIFIED FIGHT

The captive rail debate is not new. It has surfaced in Congress on several occasions since 1980. What is different today is the hands-on involvement by executives of numerous captive companies. Senior officials working for corporations from many of the nation's leading manufacturing and producer industries – including paper, grain, chemical and utilities (coal) – have banded together and are recruiting colleagues to help take this fight to Capitol Hill.

This senior executive involvement has led to the development of a working coalition comprised of 16 leading national organizations representing captive rail customers united behind a single legislative approach.

Working closely with several U.S. Senators and Congressmen, this group helped develop and successfully advocated for introduction of S. 919 and H.R. 2924, the Railroad Competition Acts of 2003. This legislation promotes rail competition and corrects some of the inequities that the STB's bottleneck, paper barriers and terminal access decisions created. Both bills enjoy bi-partisan Congressional support and endorsements from leading trade and business organizations, including the American Chemistry Council, National Petroleum Refiners Association, Agriculture Ocean Transportation Coalition, American Public Power Association, National Rural Electric Cooperative Association, National Industrial Transportation League and Edison Electric Institute.

In addition to this legislation, other opportunities exist for captive rail customers in this Congress. One opportunity is related to the extension of TEA-21, the pending surface transportation authorization bill. Congressional committees with jurisdiction over TEA-21 also have jurisdiction over railroad issues. Railroads are expected to seek a wide range of provisions in this legislation. The captive rail customer message to Congress is simple: don't address the concerns of the railroad industry without also addressing the concerns of captive rail customers.

Alarmed by the legislative campaign being mounted by captive rail customers, the nation's railroads are aggressively lobbying against S. 919 and H.R. 2924. Railroads are erroneously characterized the bills as "re-regulatory" when in fact they are pro-competitive. The railroad industry's effort is a cynical attempt to mislead Congress and the American public about the true nature of the current debate. Captive rail customers remain open to collaborating with the railroads to forge a more equitable relationship between railroads and captive rail customers. Meanwhile, captive rail customers will continue to seek the legislative relief their industries clearly deserve.

EQUITABLE COMMERCIAL RELATIONSHIP MUST BE RESTORED

The U.S. rail system is a national asset critical to a healthy economy. Companies that rely on rail transportation have a strong self-interest in ensuring the railroads' prosperity. However, the current relationship between the rail industry and their captive customers is so out of balance that it is jeopardizing the continued economic viability of captive industries, harming local economies and exporting American jobs. For example, Texas came very close to losing a planned \$800 million Toyota truck manufacturing plant because the proposed location was served by only one Class I railroad. Toyota refused to build a plant that would be captive to a single railroad. It wasn't until the Texas state government threatened to spend \$15 million to support construction of an 8-mile rail spur that the dominant railroad agreed to give a second railroad access to the proposed site. Toyota then agreed to build the plant at the Texas site. The plant will be built in an economically depressed area and will employ 2,000 workers. "We almost missed this opportunity simply because we didn't have dual rail access," a Texas official said about the situation.

A balanced and equitable commercial relationship must be achieved between railroads and all of their customers, including their captive customers. As one U.S. senator said during a recent U.S. Senate subcommittee hearing on the captive rail issue, "When the system runs the way it has for so long, everyone loses, including the railroads. If you have to use monopoly power against the shipper, everyone suffers."