# RAHALL
## Weekly Report

### REFORM OF ICC RAILROAD RATE PRACTICES URGENTLY NEEDED


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OF WEST VIRGINIA
IN THE HOUSE OF REPRESENTATIVES


*Thursday, April 14, 1983*

Mr. RAHALL. Mr. Speaker, I rise to bring to the attention of this body the roguish and irresponsible manner in which the Interstate Commerce Commission is implementing provisions of the Staggers Rail Act of 1980.

During our consideration of this railroad reform legislation, I and others worked to strike a balance between the revenue interests of the railroads with those of coal and other captive shippers by maintaining an appropriate degree of rate regulation. Since enactment of the Staggers Rail Act, I have watched as the Commission considered and decided how to interpret and promulgate key provisions of the act. I have repeatedly called for congressional oversight hearings on this process. And, I have issued alerts when I felt the Commission was ignoring the intent of the law.

However, these efforts and the intent of Congress to provide captive shipper protections, have been for naught. The ICC has taken a cavalier attitude toward implementing provisions of the act meant to protect captive shippers from monopolistic pricing practices and has mounted a campaign to administratively deregulate rail pricing for captive traffic; that traffic which lacks viable transportation alternatives and is captive to the railroads. In a number of proceedings the ICC has subverted the meaning of market dominance, sanctioned a 15 percent per year increase above inflation on coal movements, has determined that captive, or market dominant, movements may be made to pay for other less profitable traffic carried by the railroads and has exempted from any type of regulation export coal to the east, gulf and west coasts.

To the detriment of coal producers and users such as the utility industry which purchases about 80 percent of all coal produced and depends on this coal for 52 percent of its electrical generation, the ICC's various and sundry actions have lead to:

Unrealistic and illegal definition of rail market dominance by including product and geographic competition, leaving captive shippers with little prospect for recourse before the Commission;

Adoption of a cross-subsidization scheme which enables a carrier to charge a disproportionate amount of its fixed costs to captive shippers so that it can move less profitable and more competitive traffic;

A ruling that rail rates on coal may increase by the arbitrary amount of 15 percent per year above inflation despite the fact that Congress in the Staggers Rail Act already provided for inflation-based increases and a zone of rate flexibility which allows an additional 6 percent per year increase;

Unrealistic definition of railroad revenue adequacy based solely on the current cost of capital, despite past use of other relevant tools of financial analysis, which has resulted in the determination that only two class I railroads are revenue adequate; and

Exemption from regulation of coal export traffic despite the fact that U.S. coal is already 15 to 20 percent more expensive on the world market largely due to transportation costs.

In short, the ICC has declared an open season on captive coal traffic. Already faced with escalating railroad transportation costs—a 50-percent increase over the past 3 years—coal shippers and the electric utility and export markets they serve have nothing to look forward to for effective relief from oppressive market conditions. At stake is the basic fabric of a sound national energy policy. Over 65 percent of all coal produced is transported by rail with 85 percent of this amount captive to the railroads. Without a doubt, higher transportation costs for electric utilities using coal to generate over 52 percent of the Nation's electricity will be passed on to the consumer.

According to a recent study conducted by the National Economic Research Associates, Inc., deregulated rail transportation rates for coal would be anywhere from 30 to 60 percent higher than regulated rates. In 1981, the railroads earned about $6 billion in revenues for hauling coal with coal accounting for 27 percent of carloadings and 20 percent of gross freight revenues. Of this $6 billion, electric utilities paid about $4.7 billion. The NERA study indicates that if coal rates were deregulated in 1981, this would have translated into an extra delivered coal cost to utilities of between $1.4 to $2.8 billion, by 1990, an extra $2 to $4 billion. It should be noted that currently on the average 30 percent of the delivered price of coal to a utility is due to railroad transportation costs.

Mr. Speaker, I submit that this is not the scenario Congress envisioned in enacting the Staggers Rail Act of 1980. The act was intended to provide the financial mechanism for the restoration, maintenance, and improvement of the rail system. The shortage of capital to invest in rail plant has largely disappeared and the major coal-hauling railroads are now in fact highly profitable:

[In percent]

| Railroad and coal revenues (Total revenue) | Profitability (Return on equity) | Growth (Earnings per share) |
|---|---|---|
| Burlington Northern (29.4) | 10.5 | 18.2 |
| CSX Corp. (28) | 11.3 | 8.1 |
| Norfolk & Western (50.4) | 17.5 | 16.7 |
| Southern Railway (15.8) | 15.6 | 14.9 |
| Union Pacific (12) | 13.7 | 18.0 |
| Rail industry medians | 13.2 | 15.7 |

The Staggers Rail Act has served its purpose with respect to railroad revenues. Now, it is time to attend to another purpose of the act, that of providing captive shipper protections.

Today, I am introducing amendments to title 49 which will accomplish this task. In light of the recent decisions made by the ICC—decisions which run roughshod over captive shippers—it appears it is time to clarify what exactly is meant by market dominance, provide commonsense business standards for determining revenue adequacy and insert additional guidance with respect to developing standards for rail rates. In no way do these amendments run counter to the intent of the Staggers Rail Act. Rather, they enhance and reinforce the provisions of this act intended to protect captive shippers.

The amendments would establish three basic tests in the determination of market dominance. As in current law, making a showing of market dominance is a prerequisite for the ICC to investigate a rate. The first test is the revenue-to-variable cost ratios which establish the threshold for ICC jurisdiction over rail rates contained in the Staggers Rail Act. Second, the Commission would consider whether the shipper has a substantial investment in railroad related plant and equipment and third, whether 70 percent or more of a specific movement was handled by the rail carrier. The latter two tests were used by the Commission prior to its recent proceeding on market dominance in which it decided to include both product and geographic competition during consideration of the presence of market dominance.

It should be made clear that the Staggers Rail Act did not require a change in approach to market dominance and in fact retained the definition of market dominance contained in the 4-R Act (Railroad Revitalization and Regulatory Reform Act of 1976). As such, market dominance is defined as "an absence of effective competition from other carriers or modes of transportation for the traffic or movement to which a rate applies * * *" The Commission's inclusion of product and geographic competition went far beyond the transportation competition definition of market dominance provided by both the 4-R and Staggers Acts. As such, the recent Commission proceeding did not reflect any directives of the act or the intent of the act, but rather the attitude of the present members of the ICC. This was confirmed by the Fifth Circuit Court of Appeals which—keeping in line with its ruling in the 1980 Coleto Creek case—has since remanded that proceeding because of the inclusion of the product and geographic competition factors.

In the same sense, the Staggers Rail Act did not require the ICC to rely solely on a rate of return on investment equal to the current cost of capital in determining revenue adequacy. As it did with market dominance, the act retained the definition of revenue adequacy established in the 4-R Act. The Staggers Rail Act, rather, placed emphasis on taking into consideration the adequacy of a carrier's revenues in determining the maximum reasonable rate. In addition, many of the new rate freedoms contained in the Act are tied to revenue adequacy. And, the act said that the ICC had the authority to revise its standards and procedures as necessary.

The Commission, however, took that authority and substituted as the sole measure of revenue adequacy a rate of return on net investment equal to the current cost of capital. Under this standard, almost every railroad—including those thought by the investment community to be financially sound—are considered to have inadequate revenues and it is primarily captive shippers the railroads look to obtain the increased revenues they are allowed under this formula to achieve revenue adequacy. A rate of return based solely on the current cost of capital provides for an unrealistically high standard since much of the railroads' investment base contained property that is unproductive, obsolete and inflated by capacity exceeding current market needs. Also, due to the use of betterment accounting, the rate of return for the railroad industry is understated as compared to returns for other industries which use standard depreciation accounting. It should be noted that the 1981 tax law prohibits the railroads from using betterment accounting for tax purposes.

My amendments provide guidance to the Commission in formulating revenue adequacy determinations by requiring the use of standard depreciation accounting and ratios indicative of financial health such as return on investment and bond ratings. Prior to the ICC's latest proceeding on revenue adequacy, it was relying heavily on such financial ratios.

Finally, the amendments contain additional standards for determining whether rail rates are reasonable. The Commission would have to consider the relationship of the rate to the cost to the railroad of providing the service and whether the traffic involved is being required to pay an unreasonable share of the carrier's fixed costs. These provisions are aimed at mitigating cross-subsidization and serve to further the intent of the Long-Cannon amendment to the Staggers Rail Act.

Mr. Speaker, those Members who were present during the long debate on the Staggers Rail Act of 1980 will remember efforts to address excessive rates for all commodities. They will remember the other body's adoption of the Long-Cannon amendment and the adoption by this body of the Eckhardt-Rahall amendment and the subsequent compromise Staggers-Rahall-Lee-Loeffler amendment. These actions evidenced our struggle to achieve a balance in railroad ratemaking. It is time we make good on those efforts.

I ask that a section-by-section analysis of the bill and the bill itself be printed following these remarks:

SECTION-BY-SECTION ANALYSIS

Section 1: Rail transportation policy.—States that competition for transportation services is to be used to establish reasonable rail rates and that rail rates on captive traffic must be kept at a reasonable level.

Section 2: Standards for rail rates.—In making a determination of revenue adequacy, the ICC must take into consideration factors such as the relationship of the rate to the cost of providing service, the impact of the rate on the attainment of national energy goals and the extent of additional revenues required for the carrier to achieve revenue adequacy. This section also imposes the burden of proof on the carrier to establish the reasonableness of a railroad rate where the rate in question exceeds 190 percent of variable costs in conformity with the "Long-Cannon" amendment to the Staggers Rail Act of 1980.

Section 3: Rules and practices.—This section requires adherence to sound business practices and procedures in considering whether a carrier has adequate revenue such as ratios indicative of financial health (bond ratings, return on investment) in addition to having the ICC use standard depreciation accounting practices when determining depreciated costs in the investment base for purposes of computing return on investment.

Section 4: Rail cost adjustment factor.—Simply requires the ICC to consider railroad productivity, volume and output mix during its compilation of the Index of Railroad Costs.

Section 5: Market Dominance.—This section makes it clear that product and geographic competition are not to be considered in the determination of market dominance. It places into law the standards for determining market dominance and forbids the ICC from exempting from regulation any market dominant traffic not carried under contract.

Section 6: Railraod Accounting Principles Board.—Simply reauthorizes the Board which was created by the Staggers Rail Act of 1980 but never funded.

Section 7: Requires the ICC to conclude a proceeding to implement these amendments within 180 days after enactment.