# Rail Transport of Western Coal

## The History of Rail Deregulation and its Influence on Western Coal Resource Development; Prospects for Legislative Change

Western Governors' Association
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by

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# I. Summary

Coal production has become one of the West's most active areas of resource development. Environmental control laws, the economies of surface mining practices and the oil shortages of the 1970's contributed to the development of a major new resource-based industry in the West. Not only has western coal been able to claim a new market for electric energy production in the West, it has also penetrated into the electric utility markets of the midwestern and Gulf States area -- a market that was virtually unavailable to the western producer prior to the 1970's.

Expected growth in electricity demand over the next 10 to 15 years, along with the possibility of new environmental control requirements aimed at reducing sulfur dioxide emissions from utilities could substantially increase the market for western coal. Western producers also could capture more of the existing electric coal-fired market in the Midwest/Gulf States as current contracts with midwestern and eastern coal companies come up for renewal over the next few years.

The one major cloud on the horizon for the future of western coal outside the region is the high cost of transportation. The utility coal market is highly price sensitive. With rail transportation costs running as much as 75 percent of the delivered price to some of the Gulf States, the ability to keep rail costs in check becomes critical to the future of western coal.

Unlike some of its eastern and midwestern competitors, western coal has no practical alternative to rail transport. Most western mines are too far removed from their customers to make trucking feasible, and river barge alternatives do not exist. Recent experience shows even slight increases in the delivered cost of western coal can render it noncompetitive with other domestic sources outside the region, and increasingly with imports from South America, Poland and South Africa. Imports are particularly a threat in the Gulf States market area where they already can underprice domestic producers. Only a reluctance on the part of utility managers to become dependent on foreign sources, and long term contracts with western producers, have staved off major foreign inroads into the market.

Keeping western coal price competitive outside the region will be difficult. Not only is there no intermodal

competition for long hauls from western mines, in most cases there is no intramodal or rail competition either. Producers and shippers in most instances are captive to one or another of a few large rail systems which through a series of mergers and consolidations now dominate the industry. Traditional checks on railroad pricing practices which shippers heretofore were able to invoke under the provisions of the Interstate Commerce Act have been weakened or repealed.

Legislation to deregulate rail commerce, first in the 4-R Act of 1976 and more recently the Staggers Rail Act of 1980, has left the shipper in many areas of the country without any effective means of redress from the rates and rail service practices of the railroads. This is especially true in the West, where three major railroads dominate the service area with almost no overlap of routes or services.

Whether it was really the intent of the Congress to abandon the captive shipper is doubtful. There is no question, however, that the main concern of the Congress at the time the Staggers Act was passed was insuring the future economic stability of the nation's rail systems. Deregulation was thought to be the most effective way of achieving that objective, and the Interstate Commerce Commission interpreted the law as a directive to curtail all rail regulation -- one member even recommended that the Commission itself be shut down.

Four years of experience with deregulation of the railroads and the performance of the ICC under the new regulatory environment have led many shippers and buyers of rail transported commodities to the belief that national legislation is needed to give better protection to shippers in monopoly service areas.

A tentative legislative effort began in the last Congress. Proposals for rail rate relief for captive shippers are taking more formidable shape in the 99th Congress with the organization of a well-financed and staffed coalition of coal and utility companies. They are seeking amendments to the Staggers Act which more explicitly define the protections and procedures available to captive shippers in advancing complaints through the ICC. Industrial shippers have formed a coalition of their own for fair rail service practices, looking to underline the responsibilities of the ICC to maintain competitive shipping practices in monopoly rail service areas. Finally, another group has emerged in recent months seeking a bolder strategy for rail rate relief. This group asserts that unfair rail practices violate the antitrust laws. They want assessment of treble damages for antitrust violations and access to the

railroads' tracks for their own use when unreasonable practices or rates can be established.

These groups are developing legislation and gathering support and sponsorship from influential Members of Congress. In some cases, they are also mounting consumer education programs and developing grass roots support for their legislative positions. At the same time, the railroads are building their defenses and developing alliances with interests in the shipping community that would resist a return to greater rail regulation. While the outcome of this controversy is uncertain, the issue of rail rate equity and reregulation promises to become one of the more active and hotly debated issues in the 99th Congress. However it comes out, the results will have a lasting impact on many western states, their present economy and future development. As such, they need to take an active role in the debate.

## II. Western Coal Outlook

Coal production has become the West's biggest resource development business. While the traditional resource sectors -- hard rock mining, copper and timber -- have declined drastically over the past decade, western states coal production has increased just as dramatically. Coal production in the Western Governors Association states rose from 45 million tons per year in 1970 to 225 million tons in 1983, a five-fold increase. Production is expected to increase another 60% in the next decade.

Most western coal is used for generating electricity. Western mines provide virtually all the coal used by western utilities and 51 percent of the coal for steam electric generation in the Midwestern/Gulf market area. Western coal has penetrated as far as the Ohio River and lower Mississippi utility markets.

Electrical load growth, environmental constraints such as revised tall stack regulations and possibly a new acid rain law, as well as the large number of coal supply contract renewals due over the next few years hold promise for a substantial increase in demand for western coal in the Midwestern/Gulf utility market. But transportation costs will be the key determinant as to whether this new market materializes. Increases in rail transportation costs have the potential to greatly constrain this market growth and even decrease the West's present market share.

### Western States Coal Production

The Department of Energy forecasts that by 1995 the WGA states will be producing 354 million tons of coal, or 29.7 percent of total U.S. production.*

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*Energy Information Administration, Annual Outlook for U.S. Coal 1984, October, 1984. The EIA's estimate is more conservative than most private forecasts, and represents decreasing expectations for coal's near term prospects. The National Coal Association is even more pessimistic, estimating only 1.1 billion tons of production nationwide in 1995, compared to the EIA's estimate of 1.2 billion tons. Many private forecasters, including Data Resources, Inc. and Chase Econometrics Associates Inc., put U.S. production in 1995 at or above 1.3 billion tons. DRI is much more optimistic than DOE about growth prospects for western coal.

The Western Governors Association includes the contiguous states of Arizona, California, Colorado, Idaho, Montana, Nebraska, Nevada, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington and Wyoming, as well as Hawaii and Alaska. The bulk of western coal is located in Wyoming, Montana, North Dakota, Utah, Colorado, Alaska and New Mexico, with only three states -- Idaho, Nebraska and Nevada -- lacking commercial coal reserves. Of the 236 billion tons of coal reserves identified in the WGA states, 77 percent is subbituminous, 13 percent is lignite and 10 percent is bituminous, with only small deposits of anthracite in Colorado and New Mexico. Alaska has one mining operation producing bituminous, metallurgical grade coal for export. Together, the WGA region had 123 operating mines in 1983; 70% of production was sub-bituminous coals.[1] (See Figure 1.)

Western coal production supplies virtually 100 percent of the region's steam coal needs and a major share of the market in a number of other states, as the chart below illustrates:

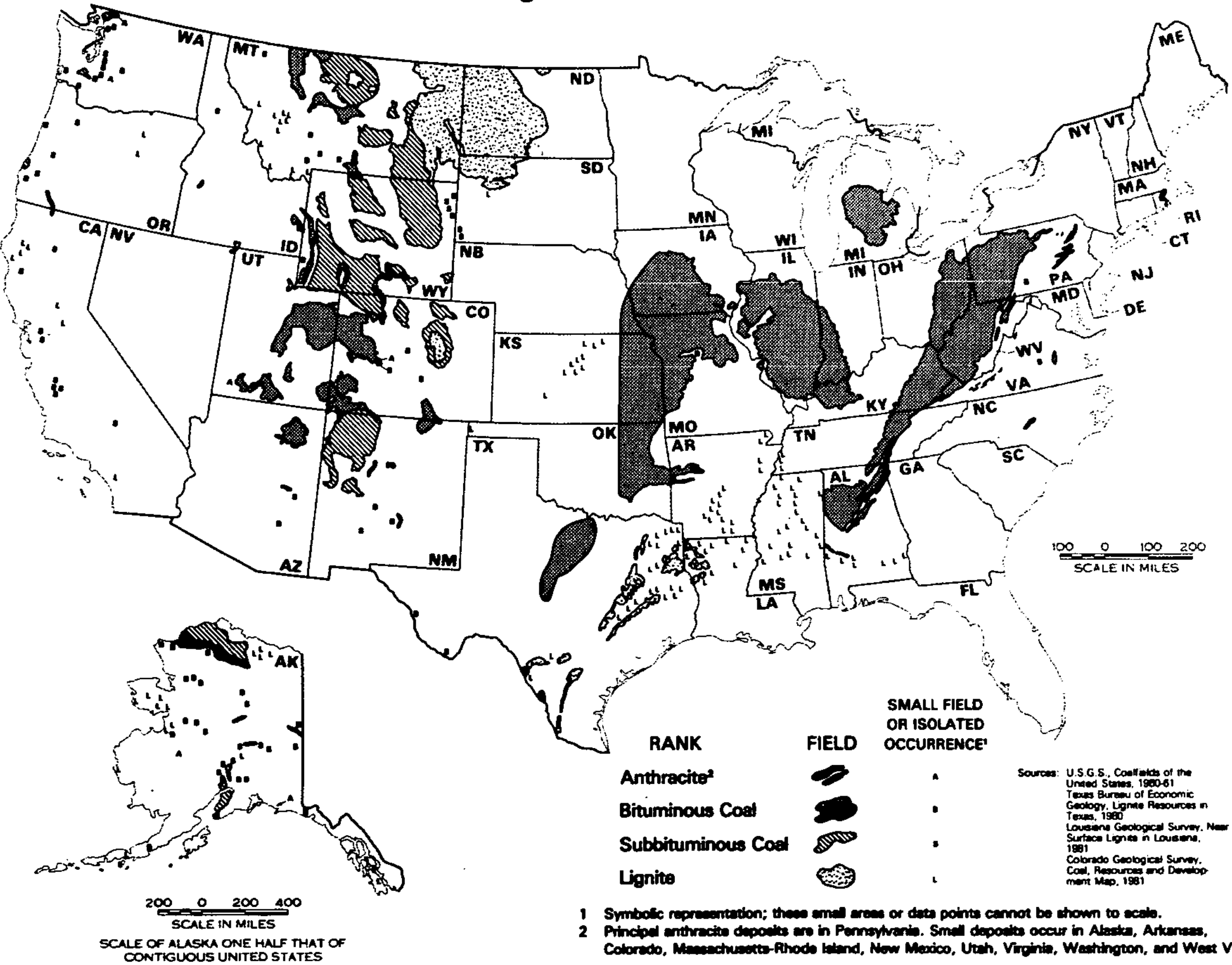
| States | Coal Market Share |
|---|---|
| Arkansas | 95% |
| Oklahoma | 95 |
| Louisiana | 91 |
| Minnesota | 91 |
| Kansas | 78 |
| Iowa | 72 |
| Wisconsin | 51 |
| Texas | 42 |
| Mississippi | 41 |

Of total western production of 225 million tons in 1983, half was transported out of the region, chiefly from two states -- Wyoming and Montana. (See Table I.)

Reasons for the phenomenal growth in the western coal market are well established. The Arab oil embargo in 1973, the implementation of air pollution control laws, and the shift from reliance on new nuclear plants rekindled interest in coal, especially low sulfur coal. The abundance of western coal, its low sulfur content, absence of labor disputes and its low price (at the mine) compared to the supplies from Midwest and Appalachian mines caused utilities, especially in the Midwest, to adapt existing plants and build new plants to use western coal and to sign long term contracts.

Figure 1

# Coal-Bearing Areas of the United States




1 Symbolic representation; these small areas or data points cannot be shown to scale.

2 Principal anthracite deposits are in Pennsylvania. Small deposits occur in Alaska, Arkansas, Colorado, Massachusetts-Rhode Island, New Mexico, Utah, Virginia, Washington, and West Virginia.

Table I

Distribution of Western Steam Coal During 1983
(In Millions of Short Tons)

| | Intra-State | Shipped Outside the State |
|---|---|---|
| Arizona | 7.0 | 4.4 |
| Colorado | 7.3 | 4.6 |
| Montana | 2.0 | 25.8 |
| New Mexico | 14.2 | 5.5 |
| North Dakota | 14.7 | 2.2 |
| Utah | 5.2 | 3.5 |
| Washington | 3.6 | -- |
| Wyoming | 15.3 | 91.8 |
| Total | 69.30 | 137.80 |

SOURCE: Data Resources, Inc., Coalink System.

A Growing Western Coal Market

If prices can be kept competitive, there are some promising indicators for the future western coal market. Indeed, a well established market already exists. In 1983 western producers had 51% of the Midwestern/Gulf steam electric market.[2] The same factors -- reliability of supply, low production costs and low sulfur content -- that have facilitated the penetration of western coal into the Midwestern and Gulf States market could, if maintained, contribute to a continued expansion of the market over the next decade.

Western coal market growth is directly related to expected increases in electricity demand. The rate of growth in demand is a highly disputed issue. Few now expect a return to pre-1970 historic levels when demand doubled every ten years.

Current DOE estimates[3] see electricity demand growing at an annual rate of 3.2 percent through the year 1995. This is relatively high compared to other forecasters.* In a shift from earlier estimates, DOE now sees electricity demand as growing faster than GNP, as it did for many years before the Arab oil embargo, rather than keeping pace with GNP, as was the case in the conservation-oriented decade of 1974 to 1984.

Some believe that pent-up residential and commercial demand will break on the market in the next few years. Chemical Bank projects that demand in these two categories will increase 50% and 80% respectively between now and the year 2000.

The projections assume that the fuel of preference for supplying this projected electricity load growth will be coal. Chemical Bank and DRI predict that coal's market share of electricity generation will increase from today's 55% to around 62-65% by the year 2000. And some believe that the instability of the international oil market and the clouded future of nuclear power could shift even more of the future market to coal. Because of its abundance and dependability, its environmental properties and relatively low cost of production, western coal stands to capture a significant share of this market. DOE projects that coal consumption west of the Mississippi will increase by 166

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*The Energy Information Administration's forecast cited above is based on a 2.9% annual growth rate. The National Coal Association assumes a more pessimistic 2.5%; the Environmental Protection Agency assumes 2.7%.

million tons from 1980 to 1990 and an additional 58 million tons between 1990 and 1995, chiefly due to construction of new coal-fired power plants.[4] Western producers are expected to get virtually all of this increased market and an increased share of the Midwest/Gulf Market as well.

In the Midwest/Gulf Market Region, RDI projects a 32,000 megawatt increase in coal fired generating capacity by 1995, requiring about 70 million tons per year of coal. If the West were to capture even its current market share, production would increase some 35 million tons per year in the next decade. RDI predicts that the bulk of this market will probably go to Powder River Basin producers in Montana and Wyoming.[5]

Even without load growth, there is potential for the western producers to increase their share of the existing market in the Midwest/Gulf region. Many of the contracts between midwestern producers and the region's utilities will expire in the next five years. Most contracts for western coal, on the other hand, extend to the end of the century and beyond. According to COALDAT,[6] an estimated 26 million tons per year of Midwestern producers' contracts will be up for renewal and/or renegotiation before 1990. Since information is not available on all contracts, the market to be opened up in the next few years might be considerably larger. Western producers could make inroads into this market, but competition will be stiff, especially in the current climate, with capacity exceeding demand. (In 1983 coal production nationwide was about 89 percent of capacity. In the West, it was lower -- about 86 percent.)

Two major uncertainties face western producers. The first is the debate over acid rain control. The second is the cost of rail transportation and the uncertainty of national policy toward future rail rates and protection of so-called "captive shippers" in areas dominated by a railroad occupying a monopoly position. Both involve the setting of national policy. As national issues, they are influenced by factors beyond the control or exclusive persuasion of the western producers or, for that matter, the western states. Both will be hotly debated in the 99th Congress in 1985-86. The outcome for both is uncertain. Consumer expectations -- and the policies themselves -- will heavily influence the coal markets.

Acid Rain Control

Since 1981, Congress has been embroiled in a bitter controversy over the shape of a cleanup plan for acid deposition, or "acid rain." Sulfur and nitrogen oxide air

pollutants often stays aloft in the atmosphere for days, where chemical processes convert it into mild sulfuric and nitric acid. The acids fall to earth as acid rain or snow. Sulfates and nitrates can also be deposited in dry form; contact with precipitation completes the chemical transformation to acid.

Known or suspected damage includes reduced crop yields, threats to human health, possible links to forest damage and reduced forest growth, damage to buildings and monuments, and death of sensitive animal and fish species, particularly in areas where natural buffers have been exhausted by the annual onslaught of acidity.

Since sulfur dioxide is a prime cause of acid rain, Congress has concentrated its control efforts on reducing sulfur dioxide pollution. Midwestern power plants contribute the lion's share of the eastern sulfur dioxide total, and reductions there tend to be relatively less expensive, so the control proposals are aimed largely at power plants.

Preferred reduction strategies include switching to lower sulfur coal, washing or chemically treating the coal before it is burned to reduce its sulfur content, and installing "scrubbers" which remove sulfur dioxide from smokestack gas.

Since 1979, new power plants have been required to install scrubbers regardless of the sulfur content of the coal they plan to use. But power plants have a 30- to 50-year life, and many of the tall stacks were built in the early 1970's to avoid the requirements of the Clean Air Act, by dispersing rather than reduce pollution.

Rather than wait decades until newer boilers replace the current "dirty" generation of facilities, the acid rain control proposals call for retrofitting utility boilers with pollution control equipment, or requiring the use of lower sulfur coal.

These proposals create a new set of coal production "winners and losers." And depending on the size of the sulfur dioxide reductions and the shape of the program, the stakes are substantial.

Cleanup proposals fall into two major categories. One would leave individual utilities free to choose the least costly method of control, based on the usual variables of coal price, transportation costs and the cost of "scrubbers." Those near a cheap supply of high sulfur coal might find it economical to scrub the local coal. Others

might find it cheaper to switch to western low sulfur coal. The second kind of control proposal would require at least some utilities to install scrubbers regardless of economic efficiencies. Most of these proposals would in some way subsidize the scrubber installation.

Estimated costs for all control programs are in the billions of dollars annually. Proposals which would encourage utilities to choose the most cost-effective control option would cost less than those which would require installation of scrubbers; but they would reduce substantially the market for high sulfur coal. Low sulfur coal is plentiful in the West and states like West Virginia and Kentucky have both high- and low-sulfur reserves. But key Midwestern states, especially Illinois, Indiana and Ohio, have only high-sulfur reserves. Coal production in these regions is already in decline. To top it off, a high proportion of the existing power plants which would be targetted for reduction are located in these states, and the publicized damage from acid rain has largely occurred east and south of their borders.

Representatives from these states tend to view acid rain cleanup as a plan that would hurt their coal industry, drive up their energy costs and benefit other regions. It is largely to gain the support of these Midwesterners (although there are other justifications) that proposals have been advanced to require scrubbers. Mandating the technology would guarantee more use of local coal. Since requiring technology would drive up the cost of control, the proposals usually include a federal subsidy to help finance the installation; a small tax on electricity generation in turn would finance the subsidy. (In some proposals, the technology is not mandated, but the availability of a subsidy tips the economic balance more toward scrubbers and local coal.)

Representatives from southern and western low sulfur coal regions tend to support acid rain control measures, but oppose proposals to share costs through a national energy tax and most are strongly opposed to proposals to require "scrubbers," since that would reduce the potential market for low sulfur coal.

While the two approaches are expected to have little impact on the coal market overall, the potential inter-regional changes are large. The most complete comparison between the two approaches was done in 1983 by ICF Inc., a Washington, D.C. consulting firm, for the Alliance for Clean Energy. ICF concluded that the overall impact on demand for coal in 1995 was small for either a scrubber/subsidy reduction program or an equivalent reduction scheme in which

utilities could choose the least costly reduction method. But the potential increase in annual WGA coal production under the least-cost scenario amounted to 95 million tons in 1995,* compared to a 4 million ton increase under the scrubber/subsidy program. (See Table 2.)

Midwestern coal producers would see a virtually identical decline in their projected production and about 55 million tons of production would shift from Central Appalachia to Northern Appalachia.

Table 2

WGA Coal Production
Under Acid Rain Control Alternatives

| | 1980 Production | Projected Increase 1995 | Additional Change (+ or -) Technology Required | Additional Change (+ or -) Least Cost |
|---|---|---|---|---|
| Alaska | .8 | +11.5 | -- | -- |
| Arizona | 10.9 | +5.7 | -1.7 | +6.2 |
| Colorado | 18.9 | +20.4 | +5.3 | +60.5 |
| Montana | 29.9 | +41.1 | +2.0 | +12.4 |
| New Mexico | 18.5 | +26.2 | -.5 | +10.6 |
| North Dakota | 17.0 | +15.7 | -.1 | -- |
| Utah | 13.2 | +20.0 | +.3 | -.3 |
| Washington | 5.1 | +1.2 | -- | -1.9 |
| Wyoming | 94.9 | +83.9 | -1.3 | +7.6 |
| WGA Total | | +225.7 | +4.0 | +95.1 |
| WGA Production | 209.2 | 434.9 | 438.9 | 530.0 |

Source: From ICF, Inc.

Other analysts are more skeptical. Robert L. Sansom of Energy Ventures Analysis, Inc., in suburban Washington, D.C., suggested the total WGA production increase under a least-cost program would be about 29 million tons, less than one-third the size of the ICF forecast. Sansom argues that scrubbers are naturally more competitive than EPA assumes, and the current coal supply glut will spur substantial price competition. In short, Sansom concluded, "Western coal will

*A Department of Energy analysis put the potential increase in annual WGA coal production at 70 million tons in 1984. Both DOE and ICF, however, have since scaled back their national production estimates for 1995.[7]

not see a repeat of the 1970's bonanza...even with acid rain legislation."[8]

Congress has been immobilized on acid rain by its inability to bridge the regional divisions which are inherent in the design of a control program. The Reagan Administration has firmly resisted drafting a control proposal, advocating more research instead. Enactment of a control program in this Congress is unlikely.

"Tall Stacks"

The Environmental Protection Agency is redrafting its regulations governing "tall stacks," and the result could be a substantial increase in demand for low sulfur coal. The controversy over the use of tall stacks to disperse pollution goes back to 1972, when EPA approved the use of tall stacks to disperse sulfur dioxide pollution rather than requiring actual reductions. The Courts and Congress repeatedly have branded this practice illegal.

The law allows the use of tall stacks to disperse pollution only in those rare cases where pollution control hardware and/or use of lower sulfur coal are insufficient to protect public health in areas nearest the facility. EPA consistently has proposed including dispersion as, in effect, a control option. More than 150 tall stacks have been built since the early 1970's, some taller than the Empire State Building.

In 1983, a federal court ordered EPA to draft new regulations on tall stacks, and EPA held a public hearing on its draft alternatives on January 7, 1985.

Depending on the alternatives EPA chooses, ICF Inc. estimates that coal production west of the Mississippi River in 1995 will increase anywhere from 0.8 to 11.5 million tons. As in the acid rain analysis above, production will shift from Midwest and Northern Appalachia to the West and Southern Appalachia, while overall U.S. production will be only marginally affected.

Rail Rates and Regulation

Western coal production and rail transportation are inextricably linked. Approximately 75 percent of the region's coal production moves to market by rail, compared to around 59 percent for the nation. In the first six months of 1984, more than 82 million tons of western coal was rail hauled.[9]

Because of the long distances to market and the absence of transportation alternatives, the cost of rail shipment constitutes up to three-fourths of the delivered price of western coal and seldom falls below 40 percent of the delivered cost, with the average in the 50-60 percent range. Consequently, rail transportation charges become a critical factor in determining the price competitiveness of western coal in the interstate market and a major determinant in the future vitality of the western coal industry.

This is especially true since the utility coal market is highly price sensitive. Even slight increases in the delivered price of coal can tip the balance away from a given supplier. Unfortunately for western coal interests, the concerted national push to deregulate the railroads has left the western shipper with very little means to constrain rail rates through the traditional mechanism of regulatory intervention.

As the demand for coal increased, transportation charges have outstripped inflation. Western coal hauling costs increased by more than 50% between 1979 and 1983*, while consumer prices increased by only 32.9%. In the past two years, most coal haul rate increases have slowed, with notable exceptions, such as a 16 percent average annual increase in the cost of rail haul for Colorado coal to Indiana. Efficiencies of unit train hauls and contractual arrangements made legal by the 1980 Staggers Act have helped in most cases to check the upward spiral of rail rates. But apprehension as to their future capability to keep rates in check is strong among the western coal producers, especially in light of ICC's announced plans for regulating rates on such commodities. The ICC has proposed accepting annual increases of up to 15 percent, plus an inflation increment, as a matter of policy (Ex Parte 347). Such increases compounded over several years could increase rail rates on coal shipments four-fold by 1990. To illustrate, a $10 per ton shipping rate would increase to $45.20 by the end of the decade.

As prices increase, the distance western coal can penetrate markets outside the western region shrinks. Central Illinois Light, for example, recently shifted from Montana and Colorado coal to eastern Kentucky and southern West Virginia low sulfur supplies. The shift was directly related to rail costs, with the new supply costing

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*Data developed for CURE show average rate increases from 1979-83 of 62% from Colorado to out-of-state markets, 53% from Wyoming and 57% from Montana. Coal haul rates from Utah to Mississippi increased a whopping 72.4%.

approximately $18.00 per ton as compared to the delivered price of $25.33 and $28.85 per ton by the Burlington Northern and Denver Rio Grande, respectively.[10]

In a similar case, Central Power and Light of Corpus Christi, Texas, has advised Colowyo Coal that because of the delivered price of the Colorado coal, the utility will be phasing out its purchases over the next ten years.[11]

In a recent analysis of the sensitivity of the coal market to transportation costs, EIA demonstrated that low rail rates over the next ten years would increase the market for western subbituminous coal, especially in the Powder Rivern Basin. Conversely, a projection of high rail rates (63% by 1995) indicates a market loss for the Powder Rivern area of 21 million short tons per year.[12]

Even small increases in the delivered price threaten the western market. According to calculations of a group of economists at the University of Wyoming, a 5% increase in rail rates per ton-mile, with all else unchanged, could reduce Wyoming coal sales by 3% to 15%, with the greatest impact observed in the most distant markets.[13]

In its study of the effects of deregulation on domestic coal production,[14] DOE found that rate increases necessary to make the railroads "revenue adequate" under ICC's definitions would reduce coal production west of the Mississippi River almost immediately. By 1990 western production estimates would decline nearly 20% and production levels would stay depressed through 1995 (the end of the study period).

The Department of Energy reached an even more striking conclusion in a 1983 analysis of the "least cost" acid rain control program described more fully above. It concluded that a 9% annual real increase in rail rates virtually would wipe out projected production increases for the WGA states in 1995, even with enactment of acid rain legislation most favorable to western coal interests.

DOE projected in mid-1983[15] that production of WGA coal would increase about 50% by 1995 to 337 million tons.* A favorable acid rain control bill would add another 70 million tons to the total, boosting production to 407

*Interestingly, DOE's 1984 coal forecast called for WGA mines to produce 354 million tons in 1995, even though it has scaled back national production levels.

million tons, even with a 3%* annual increase in transportation costs. But when the Department factored in an additional 5% annual real increase in transportation costs, production dropped back to 345 million tons. And with an additional 9% increase, the estimate plunged to 277 million tons. (See Table 3.)

Indeed, recent experience has demonstrated that even long term coal supply contracts are no guarantee against utility cutbacks. Producers in both Montana and Wyoming with long-term contracts have experienced cutbacks in coal orders in the past year. Deliveries in 1982 to some major Wyoming coal purchasers were down from 1981 and below contracted minimums by as much as 10 to 15%.[16] Likewise, Commonwealth Edison has cut back on the delivery of thousands of tons of coal under contract with Decker Coal's Montana mine. And the Wall Street Journal reports that many utilities are exercising "minimum take" provisions in their long-term supply contracts to reduce the deliveries.[17]

Some of these current cutbacks are attributed to excessive inventories at the utilities, but it is indisputable that as the price of the fuel rises, fuel substitution becomes more attractive. The price of oil on the world market is declining but is probably still too high and subject to the vicissitudes of Middle Eastern politics to be considered a practical alternative to existing coal fired generation. But, increasingly, there is a real threat to the domestic coal producers from foreign coal competition, especially in the Gulf States and on the lower Mississippi. Lower labor costs, government subsidies of their coal industry and lower shipping costs are bringing imported coal from Poland, Colombia and South Africa competitively close to the delivered price of domestic coal at port areas.

Porter B. Bennett, an expert in energy markets, recently performed a market survey of 91 coal burning utilities on the Atlantic and Gulf Coast and lower Mississippi areas. From the survey, he concluded that Colombian coal could be delivered to 52 of the 57 plants in the Atlantic portion of the study area at a price equal to or lower than the price they were now paying for delivered domestic coal. Further, he found that high Btu coal from Canada was price competitive at 38 of the 57 plants, Poland at 27, and South Africa at 25. As for the Gulf Coast/lower Mississippi market, Bennett found the Colombian coal was price competitive in about 80 percent of the plants and that

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*EIA revised this assumption downward in early 1985, and now projects a 20% total increase by 1995.

Table 3

U.S. Bituminous Coal and Lignite Production--Base Case and Transportation Sensitivity Case, With S. 3041, 1995 (Million Short Tons)

| Coal Supply Region[b] | Base Case | Transportation Cost[a] | |
|---|---|---|---|
| | | 5% | 9% |
| Northern Appalachia | 203 | 207 | 211 |
| Central Appalachia | 439 | 430 | 401 |
| Southern Appalachia | 31 | 41 | 47 |
| Midwest | 111 | 146 | 179 |
| Central West | 23 | 30 | 53 |
| Gulf | 102 | 102 | 103 |
| WGA States | | | |
| E. Northern Great Plains | 36 | 40 | 29 |
| W. Northern Great Plains | 247 | 180 | 119 |
| Rockies | 57 | 53 | 52 |
| Southwest | 61 | 60 | 63 |
| Northwest | 6 | 12 | 14 |
| (WGA Total) | (401) | (345) | (277) |
| U.S. Total | 1,316 | 1,301 | 1,271 |

a) - S. 3041, as reported by the Senate Environment Committee in 1982, would have required an 8 million ton reduction from 1980 sulfur emissions in 31 eastern states within 10 years of enactment. The choice of control was left a state option, making this legislation favorable to western coal development.

b) - Compounded annually.

Note: Totals may not equal sum of components due to independent rounding.

Source: Energy Information Administration, 1983.

the other national imports could compete at about 50 percent of them.

The survey indicated that the utilities would not switch to heavy reliance on foreign supplies unless the price differential were substantial -- usually 10 percent or more. Even so, Bennett concludes that western suppliers to the Gulf market area are particularly vulnerable. At five of the 11 plants in that area now burning western coal, the utility would save from 15 to 40 percent over 1983 delivered prices by opting for foreign supplies. Only the existence of long-term supply contracts is sustaining the western market at some of these plants, but as Bennett warns, state public utility commissions may begin to force contract changes by disallowing automatic fuel adjustments on electricity rates. This could provide foreign suppliers with an opportunity to enter the U.S. market and displace some of the western coal supply.

CHAPTER II FOOTNOTES:

[1]Energy Information Administration: Coal Production, 1983, pp. 4, 5, 96.

[2]Western Coal Market; Development Trends and Prospects; Ronald L. McMahon; p. 2.

[3]Annual Energy Outlook, 1984, DOE, EIA, January 1985.

[4]Energy Information Administration, Annual Outlook for U.S. Coal 1984, DOE, EIA, p. 18.

[5]Op. Cit., McMahon, II-4.

[6]Resource Data International, COALDAT, Denver, Colorado.

[7]Energy Information Administration, Impacts of the Proposed Clean Air Act Amendments of 1982 on the Coal and Electric Utility Industries, June, 1983.

[8]Presentation to Marketing Western Coal Conference, November 9, 1984.

[9]Energy Information Administration, Coal Distribution, January-June 1984.

[10]Department of Energy, "Report on Potential for Cost Reductions In Inland Transportation of U.S. Coal Exports," August 1983, p. 24.

[11]Ira E. McKeever, Jr., President, Western Coal Development, Testimony before Committee on Judiciary, U.S. House of Representatives, September 19, 1984.

[12]Energy Information Administration, Annual Energy Outlook, 1984, January 1985, p. 167.

[13]Scott F. Atkinson, et al, "Transportation Changes, Production Taxes, and Scrubber Legislation;" U. of Wyoming, Office of Research and Graduate Studies.

[14]Energy Information Administration, Railroad Deregulation: Impact on Coal, August, 1983.

[15]EIA, cited at note 7 above.

[16]Op. Cit., Atkinson Study.

[17]Wall Street Journal, December 18, 1984.

## III. Captive Markets

Just as there is no practical alternative to rail shipment for most western coal producers, there is also little competition between railroads for the western coal traffic. Three cross-continental lines dominate railroad service in the western U.S. The Burlington Northern serves the northern tier states; the Union Pacific is predominant in the central corridor; and the new consolidated line which is expected to result from the proposed merger between the Southern Pacific and the Atchison, Topeka and Santa Fe will largely eliminate competition for rail traffic in the southwestern states. The two dominant western coal hauling lines are the Burlington Northern and the Union Pacific. Only the Denver and Rio Grande Western and most recently the Chicago and North Western offer any competition to these giants in the western service area, and, except for the latter's entry into the Wyoming Powder River Basin, these lines, for the most part, do not compete in service territory. Thus, for all practical purposes, these western railroads enjoy a monopoly market for shipment of coal out of the region.

### A Matter of Pricing

Has this monopoly market situation caused the railroads to engage in exploitive pricing? The railroads say no, claiming their earnings provide only a reasonable rate of return on investment. The current regulatory structure allows the coal hauling railroads to maintain a differential pricing system, which obliges long-haul coal movements to subsidize shorter, intermittent shipment of other goods, thus permitting the carrier to continue providing a service which, on its own, would not be economically supportable. Put another way, differential pricing permits the railroad to "make hay" on the revenues from traffic on noncompetitive routes, so it can be more competitive with trucks, barges and other rail carriers, where such competition exists.

Differential pricing is the pricing of each service in relation to the demand for the service. It is an old and accepted pricing practice in regulated interstate commerce, and, as William Dempsey, President of the Association of American Railroads, recently explained to the House Judiciary Committee, an essential means by which the railroads maximize their rate making potential to achieve "revenue adequacy." Mr. Dempsey told the Committee that:

"Given the inability of railroads to recover their full costs from unregulated competitive traffic, the objective of a maximum ratemaking standard must be to regulate the rates on non-competitive traffic in a manner that is fair to the shipper who is dependent on rail service but still allow the carrier the opportunity to cover its full costs."[1]

But even with the complexities surrounding rail rate making, two facts stand out. Hauling coal is highly profitable for the railroads, and, where rail competition exists, coal rates have been substantially reduced.

No one, including the railroads, argues that coal traffic is not lucrative. According to the ICC, coal provides 22.3 percent of total rail rate revenues for the U.S. rail systems; other assessments show it as high as 26 percent.[2] The Edison Electric Institute estimates that coal operating profits on a per ton basis are 75 percent greater than for other rail traffic, with coal traffic giving a 32.6 percent operating profit as compared to a yield of 18.6 percent per ton on all other traffic.[3]

In the western U.S., this coal haul revenue has been particularly beneficial to the financial standing of the Burlington Northern and the Union Pacific, which, together with their subsidiaries, are two of the most profitable rail systems in the U.S.

Competition Helps

Where it exists, intramodal competition has had real impact on reducing rail rates. For example, Burlington Northern, with a connection with Missouri Pacific, was carrying 8 million tons annually out of the Powder River Basin of Wyoming to Arkansas Power and Light at an approximate cost of $23.00 per ton. When the Chicago North Western entered the Powder River area, it offered Arkansas Power and Light a rate in the $17.00 to $18.00 per ton range -- a potential savings of $48 million a year for the utility.[4]

While CNW may be "low-balling" the price to gain entry into the market, the fact remains that competing lines give the shipper an advantage in negotiating rates and contracts. Wisconsin Public Service, a Green Bay, Wisconsin based utility, expects to save about $100 million in fuel costs over the next 15 years as a result of Chicago and North Western's entry into the Burlington Northern's origin area. "In the past we were totally captive, and Burlington Northern pretty much dictated the terms," Edward Novak, the

utilities fuel services director, told the Wall Street Journal. Now "we drafted the contracts."[5] Other examples exist of lower rail rates from competition, especially in the East where there is more competition between rail lines as well as barge and ship movement. But even in the West, as the General Manager of the Western Fuels Association recently advised a Congressional Subcommittee, "Where true competition exists, where we have economic leverage, where a railroad wants our business and must compete to get it; the railroads have invariably been responsive to our concerns for price, terms, service commitments, and the like."[6]

While western coal producers and their utility customers would welcome reduced shipping rates, few believe this is a realistic expectation. Their real apprehension is that the rates will continue their upward trend, eventually pricing the western producers out of the market. Railroads dismiss this concern as unfounded and contrary to their own self interest in maintaining a highly profitable component of their service. Why would they price themselves out of the market, they ask?

Reflecting on the ICC proposed 15 percent allowable annual rate increase, Michael Donahue, Vice President of Burlington Northern, recently told a conference on western coal marketing, "I know of no circumstance under which our railroad company could invoke such increases. The market would not permit it -- we would simply lose the business."

Others are not so sanguine about the willingness of the railroads voluntarily to keep their rates low enough to keep western coal competitive. As we saw earlier, the price of imported coal is already a competitive threat in some of the western coal markets. Likewise, utility cutbacks on supply contracts and recent decisions by several Texas utilities to switch from Wyoming coal to local lignite presage an ominous trend.

In the absence of market competition, the shipper has traditionally turned to the ICC and the precedents developed from nearly 100 years of experience in regulating rates and rail practices of railroads in interstate commerce. National legislation to deregulate rail commerce has sharply limited these traditional avenues of redress leaving the shipper and the consumer with only limited means for appealing rail rates and practices and then only in market dominant areas.

CHAPTER III FOOTNOTES:

[1] House Committee on the Judiciary, Hearings on H.R. 4559, September 19, 1984.

[2] "Railroad Coal Rates: A Critical Analysis" (Table I), Multinational Business Services, Washington, D.C., September 12, 1984.

[3] Railroad Coal Rates, Edison Electric Institute, July 1983.

[4] Report on Potential for Cost Reductions in Inland Transportation of U.S. Coal Exports; U.S. DOE, August, 1983.

[5] Wall Street Journal, "Midwest, Southwest Utilities See Savings," September 4, 1984.

[6] Kenneth Holum, Testimony before the House Subcommittee on Monopolies and Commercial Law, September 19, 1984.

## IV. Railroad Regulation

In this century federal railroad regulation has come nearly full circle. The Act to regulate commerce of 1887, establishing the Interstate Commerce Commission (ICC), was the forerunner of national consumer legislation. It was the first attempt at bringing uniform national control over the activities of one industry -- the railroads. Initially, the ICC was a toothless tiger, ignored by the railroads and disdained by shippers, but in 1906 legislation extended its authority to control rail rates and to issue cease and desist orders, and in 1910 the Commission was given authority to suspend rates pending investigation. The regulatory framework that emerged in the early 1900's set minimum and maximum railroad rates, limited price competition and controlled railroad mergers, abandonments and extensions.

In the early part of the century, America's railroads were perceived as predatory and rapacious in their quest for profit. Regulation was designed to moderate these practices, protect the shipper and consumer and assure reasonably available service. The political perception of the railroad industry changed gradually as competition from barges and truck lines increased.

By the 1970's, not only had the railroads' market share declined, but the system was plagued by car shortages, delays and safety problems, and an increasing state of disrepair. The large railroads reported in 1978 that more than 43,000 miles of track were under "slow order" because of their condition. High interest rates made capital financing costly and made revenue difficult to raise, especially when the industry-wide rate of return dipped as low as 1.2 percent. And when the industry could least afford it, energy cost increases added an extra burden to this energy-intensive industry. The ailing Penn Central, for example, saw its fuel bill double in 1974.

After the bankruptcy of the Penn Central and six other lines and threatened bankruptcy of several others, Congress saw a national mandate to restore the railroad industry to financial health. Less regulation was considered the tonic and Congress responded by enacting two major pieces of legislation; the Railroad Revitalization and Regulatory Reform Act of 1976 (4-R Act) and the Staggers Rail Act of 1980.

With these two statutes Congress sharply limited the authorities and purview of the ICC over railroad commerce. The 4-R Act largely insulated competitive rail movement from the Commission's jurisdiction, but maintained ICC control where it was determined the carrier had "market dominance." The Congress assumed that competition would be sufficient to assure just and reasonable rail rates, but in areas without competition a particular carrier might be tempted to engage in rate gouging and other monopoly market practices. The definition of market dominance was left to the ICC, which, in part, based the determination on the relationship between revenues and variable costs and the financial health of the carrier (revenue adequacy) and not on the actual existence of a service monopoly.

The Staggers Act reaffirmed and advanced the policy of fostering competition through deregulation. The Act retained the market dominance test of the 4-R Act, but it established by law that every railroad could charge at least 60 percent more than the cost of providing the service.* The Act also established what are referred to as the "Long-Cannon factors," to be used as a guide in determining whether a railroad is attempting to overcharge captive traffic to make up for revenue lost as a result of rate reductions compelled by competition.

However intended by the Congress, the Staggers Act and the national enthusiasm for deregulation were taken by the ICC as a mandate to withdraw from the review of railroad practices whenever possible and to give the railroads the utmost benefit of the doubt in their review of reasonable rates and market practices in monopoly service areas. As a result, some would assert that today the captive shipper is as unprotected from monopoly rail practices as before the passage of the 1887 Act.

ICC's Evolving Approach to Coal Rates

For well over 50 years, the ICC pursued the goal of holding railroads to a standard of reasonable service available to all at reasonable rates uniformly applied. To avoid discrimination, one of the ICC's first decisions in 1887 forbade volume discounts. It was 1939 before lower rates reflecting operating savings for multiple car shipments were first allowed. To insure nondiscriminatory rates for coal shipments, ICC "grouped" coal mines and destinations on the basis of geography. (All shippers in any "group" were charged the same rate for service to any

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*See explanation of threshold variable cost guidelines on p. IV-6.

destination in a given "group.") And for the sake of fairness, "differentials" or step increases were established among groups based on the average distance from mine to market. As a practical matter, this policy applied only to eastern mines, since the western coal mining industry was virtually nonexistent at the time the group-rate rate structure for coal shipments was established.

By the Great Depression, ICC's geography-based system had begun to wobble. "Grouping" was an imperfect process; the geographic area of a group was often quite large. Grouping impeded competition. Rates tended to favor mines within a given group which were farthest from market. "Differentials" came to be regarded as a virtual vested right; e.g., if one group rate was increased, railroads demanded and got increases for other groups as well, regardless of individual circumstances. Rate reductions to meet competition were rejected on the grounds they would disrupt the differential system. In short, the rate structure itself and not real world considerations became the focus of ratemaking.

In 1939, the ICC was forced to recognize the realities of competition for the first time, granting permission for discount rates to multiple car shippers in order to meet competition from barges. World War II masked the continuing erosion of the railroads' economic position, but the postwar years saw a steady decline in railroad profits and a steady increase in competition, especially from trucks which benefited from the federal highway construction program.

Between the end of World War II and 1975, railroads saw their share of intercity freight fall from nearly two-thirds to less than 40%, while real earnings fell by one-quarter. The ICC tried to respond. In 1959, bowing to competition from mine-mouth generation facilities and the threat of low-priced residual oil, ICC approved discount rates on coal shipments for shippers who guarantee a minimum annual volume. In the 1960's customer equipment and special services were allowed to be considered in the pricing structure on coal shipments in the Southeast to meet competition from gas pipelines, and unit trains began to appear. In 1978, unit trains were formally upheld, and the Commission proposed to allow rates to be set by contract negotiated by shipper and railroad; under the circumstances a revolutionary proposal.

## The Deregulation Revolution

The ICC's response was too little and too late in easing the plight of the railroads.

The collapse of the Penn Central System and six smaller railroads forced Congress in 1973 to provide for the machinery leading to the establishment of Conrail and prompted a fundamental reexamination of railroad regulatory policy. A government study questioned whether the railroads could demonstrate the financial health to raise the huge sums necessary to meet the demands of the burgeoning western coal industry.* In 1976, Congress passed the 4-R Act, which effectively limited ICC's rate control authority only to areas where a railroad had "market dominance" (monopoly control).

President Carter began a shakeup at ICC which is still being felt. The President proposed rail deregulation in 1979, and Congress enacted the Staggers Rail Act of 1980. The Staggers Act's goals were to encourage competition, minimize regulatory oversight, promote the financial health of the railroads and control rates only where service monopolies existed.

The ICC was caught up in the wave of reform. Even as the ICC attempted to respond to the new limits on its authority expressed in the 4-R Act, President Carter not only proposed deregulation, but also cut the Commission from eleven to seven members and proposed its outright abolition. The election of Ronald Reagan put the deregulatory agenda on the front page of the nation's newspapers. And President Reagan's ICC Chairman, Reese H. Taylor, Jr., endorsed the abolition of ICC in one of his first appearances before Congress.

The changing political climate had two obvious effects. First, some of the ICC staff embraced deregulation with the fervor of religious converts. Second, several Commission Members bowed out early. No more than a majority of the ICC members may be of the same political party, and terms are staggered. A protracted argument ensued between Congress and the White House over replacements for three departing Democrats. This left the Commission not only short-handed but without a single Democratic member, and lacking the institutional continuity which the staggered terms are supposed to provide. The Commission was three members short for nearly two years and did not return to full strength until September 11, 1984, and one of the three new members was sworn in for a term which expired December 31 of that same year. All seven commissioners are President Reagan's appointees.

Given this political and regulatory climate, it is no surprise that ICC's decisions often have been confusing, contradictory, overbroad and tilted toward deregulation.

Regulating Western Coal

The "grouping" system had been developed to respond to the realities of coal shipments in the East. In the 1970's, western mines began to open in response to the demand for low sulfur coal and the increase in coal's competitive position following the Arab oil embargo. ICC realized it would need a new regulatory structure to respond to the different realities of western transportation needs. The Commission proposed in 1974 to establish a separate rate structure for western coal shipments, but that effort was overwhelmed by the 4-R Act and an avalanche of complaints from western shippers or customers challenging railroad rate proposals. The most celebrated case was San Antonio v. Burlington Northern, Inc., filed in 1976, which in modified form is still under way today.

For purposes of rate making the railroads have two identifiable costs; one is fixed, the other variable. Fixed costs are costs such as track and roadbed that exist independent of the movement of particular traffic. Variable costs are costs such as fuel and labor associated with a particular shipment. The variable costs plus a portion of fixed costs and profit constitute the "full cost" of a movement. The objective in rate making is to set the rate high enough to cover the "full cost," since over the long run, the rates for all services should permit the carrier to recover both fixed and variable costs, including the cost of capital. At that point the railroad is considered to have achieved "revenue adequacy."*

While still in the middle of its inconclusive western coal rate investigation, the ICC handed down a decision on the San Antonio v. Burlington Northern case which attempted to judge the reasonableness of the BN's rate based on the cost of providing the service. ICC suggested that a "reasonable" rate be higher than the "variable" cost of service and would be 107 percent of the "fully allocated" cost.

Burlington Northern appealed the ICC decision, and the 8th Circuit Court, while upholding ICC on other grounds, suggested the ICC rate was arbitrarily set and ought to include at least all the costs of service plus a rate of return on the railroad's capital investment.

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*The ICC's variable cost guidelines have been adjusted several times and were statutorily defined in the Staggers Act in 1980 at 160 percent with an increase of 5 percent annually through 1983, to a maximum threshold of 180 percent.

Between the 4-R Act in 1976, the 8th Circuit's admonition, the political realities and the passage of the Staggers Rail Act, the world of railroad regulation was turned upside down.

The New Regulatory Agenda

By the end of 1980, ICC no longer had a mandate to establish a rate structure for western coal shipments. Its new mandate, made specific by the Congress, is to nurture the financial health of the railroads.

The statement of the conference committee on the goals of the Staggers Act is instructive:

> "The overall purpose of the Act is to provide, through financial assistance and freedom from unnecessary regulation, the opportunity for railroads to obtain adequate earnings to restore, maintain and improve their physical facilities while achieving the financial stability of the national rail system."

Competition is to safeguard the reasonableness of railroad rates, and only where "market dominance" carries the potential for monopoly pricing does ICC have jurisdiction over newly-filed rates. Even when monopoly service exists in fact, rates as high as 180 percent of the railroad's variable costs are exempted from price regulation. When rates exceed 180 percent of variable costs, and the Commission finds that "market dominance" exists, the burden is on the carrier to justify the rates.

When railroads are judged to be "revenue inadequate," or insufficiently strong financially to attract capital, ICC is to be liberal in its determinations of what constitutes reasonable rates. And, in fact, the ICC has determined in several instances that rail rates even in excess of 200 percent of variable costs were not excessive since they helped the carrier achieve the statutory objective of revenue adequacy.[1] Reflecting on this precedent, Administrative Law Judge James E. Hopkins wrote: "The Rail Transportation Policy enunciated in the Staggers Act appears generally in its overall content to allow the railroads to set their rates at whatever level they consider reasonable as long as they are not revenue adequate. Until they reach revenue adequacy...it does not appear that a rail carrier rate no matter how high can be considered above maximum reasonable level." Judge Hopkins went on to observe that such a conclusion "...while simple in its concept can be devastating in its execution. Individual shippers and

receivers captive to an individual railroad can be forced to pay an exorbitant sum for transportation...."[2]

Understandably, the railroads have warmed to this interpretation of threshold levels and revenue adequacy and have used it, as critics have described, "... to lend an air of respectability to proposals which might otherwise be judged unreasonable."[3] Western railroads have since argued that the ICC should declare rates for coal shipments up to 225 percent of variable costs to be "within a 'safe harbor' of reasonableness."

Whether or not Congress meant to provide such a sweeping redirection to ICC is debatable. But in practice the old tenets of reasonable rates and adequate service offered on a nondiscriminatory basis are no longer the guiding concerns of the Commission.

Market Dominance

In 1976, the 4-R Act limited ICC's rate suspension authority to price increases charged on "market dominant" traffic. The Act defined market dominance as "an absence of effective competition from other carriers or modes of transportation." It required ICC to rule on questions of market dominance within 90 days of a shipper's request.

ICC promptly developed a test for market dominance, proposing in 1976 four "rebuttable presumptions" for establishing its existence. A railroad could still endeavor to rebut it, but ICC would proceed on the assumption of market dominance if one of four conditions existed:

1) the carrier handled 70% or more of the traffic in question;

2) the proposed rate was more than 60% higher than the variable cost of service;

3) a shift to an alternative form of transportation would be impractical or a hardship as a result of a shipper's investment in special loading facilities, boxcars or other equipment;

4) the rate in question had been discussed with potential competitors in approved rate bureau proceedings.

At first, ICC specifically rejected the notion that effective competition could be supplied in the form of alternative sources of supply or alternative products. ICC's finding was upheld in 1978 by the D.C. Circuit Court. The argument of "geographic or product competition" asserts,

for example, that, since a power plant operator in the Midwest has his choice of midwestern or western coal, and could also purchase oil, those choices amount to effective competition which would hold rail rates to a reasonable level.

At the urging of the railroads, ICC soon issued a "clarification," and invited the railroads to offer evidence of geographic and product competition in rate cases. Then in 1979, in its Coleto Creek decision (which involved coal shipments from Colorado to Texas) the ICC ruled that Central Power and Light Co. was not captive to the Denver Rio Grande and Western Railroad, because alternative fuels were available, including importing coal from South Africa through nearby coastal ports. ICC made its finding despite the fact that the utility had already entered into a 25 year coal supply contract, built its plant and invested in rail equipment. While the decision was overturned in 1980 on procedural grounds, the Circuit Court did not rule on the question of geographic competition, and invited the ICC to make its case again.

Passage of the Staggers Act intervened. The Act reaffirmed the limitation on ICC's authority to regulate market dominant traffic, and invited ICC to review the question of geographic and product competition. The Act went further to state that dominance does not exist whenever the ratio of revenues to variable costs was less than 160%. (Congress provided for periodic increases. See page IV-5.)

The ICC seized upon the Staggers Act to scrap its presumptions based on cost, market share and substantial shipper investment in favor of "general guidelines" to be applied on a "case by case basis."[4] The guidelines make use of the presence of geographic and product competition in determining market dominance. The Western Coal Traffic League challenged the ICC decision. ICC was upheld by the Circuit Court and appeal to the Supreme Court was denied in 1984.

Contract Rates

The Staggers Act encouraged the negotiation of rate contracts between the shipper and the railroad. Contracts are becoming commonplace and will soon account for more than 50% of western coal traffic. This stands in sharp contrast with 1980 when virtually no western coal movement was under shipment contracts.

Many shippers as well as railroads are satisfied with this new contracting ability. Shippers and railroads are able to negotiate long-term arrangements which provide the

certainty which both businesses need to make long-term plans and commitments. Indeed, in the case of coal, resources far from an existing rail line might continue to be difficult to develop absent contract arrangements to apportion capital costs and establish a revenue base. More than 20,000 contracts have already been submitted to ICC.

But critics warn that contracts destroy the principle of "common carrier" service and work less well in areas lacking realistic transportation alternatives.

ICC has virtually no authority to regulate contract rates. A shipper entering into a transportation contract gives up his right to seek ICC relief for poor service or facilities, in-transit loss or damage, ignoring of transportation routes, improper boxcar allocations or changed circumstances of any description. The Commission believes that a prudent transportation consumer can protect himself against monopoly practices in negotiating rate agreements. According to ICC's notion, a power plant operator, for example, would shop around for the best energy source, and if he decided on coal, would obtain bids from competing sources of coal. He would then solicit bids from railroads, barge lines, and pipelines and make his best deal, locking it in for the long term. Then, even if the consumer invests in hopper cars and terminal equipment; even if his boiler is not economically convertible; and even if his coal contract is for 30 years and his rail contract for 10 years, he is not deemed to require the ICC's protection.

To make matters even more challenging, ICC in Ex Parte No. 387, Railroad Transportation Contracts (1982), required that only a general summary of the "essential terms" of contracts be made public. The "essential terms" do not include the shipper's name, the origin or destination of the traffic, or any special contract features. Thus, shippers accustomed to public rate setting must now negotiate without knowledge of competitors' arrangements. While the coal companies have not identified this closed contract procedure as a particular problem, some grain shippers and agricultural interests have made contract divulgence their number one legislative objective in seeking revisions to the Staggers Act. (See Part V.)

Revenue Adequacy

The 4-R Act introduced a second new concept called "revenue adequacy" into ICC railroad regulation. The Act instructed ICC to help the railroads make enough money to "attract and retain capital in amounts adequate to provide a sound transportation system in the United States." Congress saw revenue adequacy as a profit level which covered

expenses, depreciation and a reasonable amount of debt retirement, plus a rate of return on equity high enough to attract new capital.

The question of revenue adequacy comes into play in cases where market dominance exists. ICC's mandate is to balance the need for protecting captive shippers against the need to help the railroads toward financial health. Those railroads which are "revenue inadequate" are to get more leeway in rate decisions.

The ICC responded to the 4-R Act by developing a preliminary test of revenue adequacy (in Ex Parte No. 338 and Ex Parte No. 353) based on rate of return, cash flow and financial ratios designed to measure a railroad's fiscal health. Using these tests, ICC found in 1980 that 11 of the 31 largest railroads were revenue adequate.

The Staggers Act reaffirmed ICC's mandate to give special consideration to the financial health of the railroads, and ordered a prompt conclusion to ICC's attempts to define revenue adequacy. Once again, the Commission used the Act as justification for abandoning its earlier work. In a new ruling in 1981 (Ex Parte No. 393, Standards for Determining Railroad Revenue Adequacy), ICC defined adequacy as a rate of return equal to the current cost of capital for the railroad industry as a whole. The 3rd Circuit Court upheld the decision the next year. Given the high interest rates of the 1980's, it is no surprise that by 1983, ICC found that no large railroad was enjoying adequate earnings levels. (ICC sets the revenue adequacy rate annually. It is currently 15.3%.)

ICC's decision ignores other valid tests of fiscal health, such as return on shareholder's equity and debt-to-equity ratio. It also allows accounting practices which further distort the capital cost measure. For example, deferred taxes are included in the rate base. Since these taxes are carried on the books at the maximum corporate tax rate rather than the actual rate after credits and depreciation, the base is inflated.

The "revenue adequacy" condition imposed by the Staggers Act has been especially perplexing in its interpretation by the ICC. Some have alleged that the ICC "...has made a fetish of 'revenue adequacy'...as if it meant administratively guaranteed wealth (for the railroads)."[5] Others, focusing on the actual economics of the railroads, assert that the industry overall is in far better economic shape than ICC's calculations of "revenue adequacy" would indicate. Critics argue that the assurance of high rates on shipments on noncompetitive runs has contributed to

excessive profits and encourage inefficiency and waste.[6] They also point out that the recent acquisitive activities of several of the large railroads belie their lack of sufficient revenues.

The railroads point to their large capital needs for maintenance and expansion. The "slow orders" have been lifted on 27,000 miles of track since 1978, for example -- evidence of a major investment. The Association of American Railroads estimates an industry-wide return of 5.7 percent, and compares that to utility rates of return of about 14 percent.

Looking at the accounting practices allowed by the ICC in calculating "revenue adequacy," a recent analysis conducted by Multinational Business Services, Inc. concluded that "...the ICC has allowed accounting corrections which vastly understate income and overstate the investment base...."[7] Using conventional measurements such as return on permanent capital, return on equity, cash flow to total debt and fixed charge coverage, the study concluded that "the railroads are in or very near good financial health, often in better shape than the coal, utility and agricultural "captive" shippers...."

As a comparison, Potomac Electric Power Company applied the "revenue adequacy" test to its regulated electric utility and concluded that "...translated into utility regulations on an original cost basis, the equivalent authorized return on original cost rate base and equivalent authorized return on equity would be extraordinarily increased."

The Staggers Act established a Railroad Principles Accounting Board to establish principles for determining the direct and indirect costs associated with the movement of goods. The Board was not funded until the current fiscal year, and is just now seeking comments about the appropriate scope of its work. The Board must report to Congress by January, 1987.

The MBS analysis speculates that with a continuation of the deregulatory climate at ICC rail rates will increase the cost of coal generated electricity by up to $1 billion per year with a corresponding decline in the western coal market of from 25 percent to 35 percent.*[8] With an annual price increase of 4 percent above inflation (the statutory limit

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*This estimated decline in western coal production corresponds with DOE's estimates assuming an allowable price increase in coal shipment of 15% per year over inflation.

set out in the Staggers Act), the analysis concludes that revenue adequacy for all railroads is achieved by 1987 and return on investment would approach 20 percent by 1990 and nearly 30 percent by 1995. Some have indicated that this revenue adequacy scenario is wildly inflated.

Reasonable Rates

In reviewing challenges to railroad rates, the ICC first determines whether "market dominance" exists. If a railroad can point to some form of competition, whether from another railroad or another form of transportation, and if rates fall within the 180% test described above, ICC has no jurisdiction and the marketplace is left to determine the fair rate. If market dominance is found, unless and until railroads are revenue adequate, ICC applies a liberal test of reasonableness. In practice, this has been highly controversial.

In conjunction with its western coal rate structure investigation, the ICC developed a formula for determining maximum rates dubbed the "seven percent solution," and applied it to a series of rate cases beginning in 1979. The "seven percent solution" added variable costs of service, plus an additional amount which recognized the special equipment needs of heavy coal traffic, plus a portion of the railroad's fixed costs and general overhead, plus a rate of return computed under its interim guidelines, to determine "fully allocated costs at the revenue need level." Then it added an additional seven percent, on the theory that this increase would make up for revenue lost in areas where competition forces rates lower.

Five courts rejected the "seven percent solution," on various factual and traditional grounds. In 1980, as the Staggers Act was being written, ICC decided to expand its western coal rate investigation nationwide. And on the basis of its 1981 decision defining "current cost of capital" as the standard of revenue adequacy, the Commission reopened 14 long-simmering rate cases, chiefly in the West. The argument continues today.

In 1983, the ICC proposed what it described as a "constrained market pricing" approach, sometimes dubbed the "fifteen percent solution." First, a coal shipper could not be charged more than the "stand alone cost" of the service. Defined most broadly, this "stand alone cost" is equal to the cost that a shipper would incur in building and running a competing railroad to handle his traffic. Given the lack of specific case decisions, it is unclear whether the ICC meant this broad definition or something less to apply. But

shippers can expect little in the way of relief from this "constraint."

Second, as a further limitation, annual increases to captive shippers could be no higher than 15% plus inflation. Third, railroads could not pass on costs associated with inefficient management. As long as these three tests were met, revenue inadequate lines would be free to raise their rates at will. The Commission's justification again included the argument that profitable captive traffic should subsidize marginal traffic or recover losses from rates held down by virtue of competition.

This proposal has not been supported by the railroads. ICC's final decision on the "15% solution" is due soon.

Deregulating Export Coal Shipments

The ICC's decision to remove price controls on coal bound for export provides an important example of how the new philosophy at ICC is being carried out. In 1981, Norfolk and Western Railway petitioned the ICC to deregulate shipments of coal destined for Atlantic and Gulf ports, on grounds that the competitive world coal market, as well as competition among railroads and with barges would protect shippers. N&W noted the absence of shipper complaints against export coal rates. And the line said the threat of ICC-mandated maximum rates had made contract agreements difficult.

In its 1983 decision (Ex Parte No. 346 (Sub-No. 7), Railroad Exemption - Export Coal), the ICC agreed with the railroad that worldwide competition for coal restrains railroad pricing and rejected shippers' arguments that competition was undercut by long term coal contracts and such things as specialized boiler design. The Commission agreed that a handful of railroads carried the bulk of export coal, but noted that most of the coal was produced by a handful of shippers, who could wield substantial leverage of their own.

In a vigorous dissent, ICC Chairman Reese Taylor called the decision "a serious mistake...contrary to the intent of Congress and...unsupported by the evidence...." Taylor noted that international price competition would have no effect on the division of profits between the railroads and the mine operators.

Since 95% of coal producers active in the export market are served by only one railroad, Taylor argued, the effect of the ruling was to discourage shippers from competing internationally since increased sales would mean increased

profits only for the railroads, not the producers. "The railroads admitted that they will use discriminatory pricing," Taylor wrote.

Significantly, the Justice Department lent its qualified support to deregulation, advancing an argument with profound implications for transportation policy. Justice in essence dismissed the traditional notion of "non-discriminatory" service. On the contrary, it argued, discriminatory pricing would actually be a boon for export shipments of coal, since railroads could lower their rates for less efficient producers. Less efficient producers could utilize these rate concessions to improve their competitive position, which would mean increased business for the railroad. Given the ICC's enthusiasm for decontrolling domestic rail prices where geographical or product competition exists, these arguments have broad implications for the West.

The U.S. Court of Appeals for the District of Columbia struck down the ICC's coal export decision on September 18, 1984, generally agreeing with Chairman Taylor's dissent. Ruling on a consolidated suit brought by the Eastern Coal Transportation Conference and Coal Exporters Association, the court said the Commission had "ignored" and "misunderstood" the Staggers Act. The ICC ruling, the Court said, "does not assure that the division of revenues between the railroads and the U.S. shippers will be a reasonable one."

Staggers Act Review

Most recently the ICC has initiated an Ex Parte proceeding (No. 456), described as a Conference of Interested Parties to examine the Staggers Rail Act of 1980 and the "...problems and benefits arising from (its) implementation...." The expectation of the proceeding as stated in the ICC announcement is that it "...will lead to a more complete understanding of the changes that have occurred in rail transportation as a result of such legislation, and its implementation, and that it will assist the parties in resolving any problems that may exist."

This is an unprecedented move on the part of the ICC, made even more unusual by the fact that the Commission has heretofore demonstrated almost no interest in identifying and resolving any problems associated with the Staggers Act and its implementation of that legislation. Consequently, many, including a substantial number of Senators and Congressmen, view the ICC initiative as an attempt to divert the attention of the Congress from its interest in oversight of the Staggers Act and possible corrective legislation.

The *Ex Parte* proceeding has proved to be highly contentious. Five study groups composed of shippers and railroad representatives reviewed the major issues: Contracts, Abandonments, Rate Regulation, Market Dominance and Competitive Access issues like joint rate and route cancellations, reciprocal switching and trackage rights. The reports of these groups are now before the full ICC.

The Administrative Law Judge who supervised the studies told the Commission that only one of the five, the Contracts panel, could reach consensus. That panel concluded "there is widespread acceptance and widespread support for the contracting provisions...." But the panel disagreed over the extent of contract disclosure which should be required.

The Competitive Access Group, which involved more than 110 interests, including the major shippers' associations, did provide the catalyst for an agreement between the National Industrial Transportation League and the Association of American Railroads.

The agreement, which provides a process for negotiating differences on through route and rate cancellations, is being advertised as an example of how the Staggers Act works to foster private-sector solutions. Major interests, however, including the Union Pacific, have kept their distance from the agreement.

A bipartisan group of 18 Senators by letter dated October 9, 1984, put ICC Chairman Reese Taylor on notice that the Senate intends to examine the agency's implementation of the Staggers Act early in 1985. The Senators said they would not await the Commission's findings before taking whatever legislative action they deem advisable as a result of their own review and oversight. Comparable letters were also sent to the Commission from a number of Members of the House, including John Dingell (D-MI), chairman of the House Energy and Commerce Committee, and James J. Florio (D-NJ), Chairman of its Subcommittee on Commerce, Transportation and Tourism, which has jurisdiction over railroads.

CHAPTER IV FOOTNOTES:

*U.S. Department of Energy, <u>National Transportation Study</u>, 1980.

[1]Louisville & Nashville, No. 38946, (ICC November 22, 1982).

[2]Aluminum Co. of Am. vs. Bauxite & NRR Co., No. 37081S (ICC, December 16, 1982).

[3]Ben Johnson and Sharon D. Thomas, "The Staggers Rail Act of 1980; Deregulation Gone Awry;" <u>West Virginia Law Review</u>; Vol. 85, 1983, p. 33.

[4]Ex Parte No. 320 (Sub-No. 2), <u>Market Dominance Determinations and Considerations of Product Competition</u>, 1981.

[5]Richard Emrich and Vernon Haan, "Implementing Staggers," <u>Traffic World</u>, December 3, 1984.

[6]Ibid (West Va. Law Review).

[7]Railroad Revenue Adequacy; A Critical Analysis, Multinational Business Services, Inc., Washington, DC.

[8]Ibid.

## V. Legislative Relief


Summary

Dissatisfaction with the ICC's performance since passage of the Staggers Act has led some shippers to seek legislative redress. Several bills were introduced in the last Congress which attempt in various ways to provide relief for shippers in monopoly rail service areas. Most of the bills amend or interpret the Interstate Commerce Act to more explicitly define the responsibility of the ICC toward the captive shipper, reinforcing what many believe was the intent of Congress in 1980 when the Staggers Act was passed. Legislation was also introduced in both the House and Senate to treat unfair rail shipping practices as a violation of antitrust law. Hearings were held in several House and Senate committees, but no action on any legislation was taken.

The 99th Congress, which began in January 1985, will see a more aggressive legislative effort in regard to rail rate relief. Several formal and informal coalitions of shippers have formed in the past few months to push a variety of legislative reforms. These groups, while sharing a common definition of the problem, are not unified in their approach or their agenda for legislative relief. Nevertheless, together they span a significant cross section of the nation's industrial, commercial and agricultural economy. They have established a financial base, retained lobbyists and enlisted the support and advocacy of some influential members of Congress. Additionally, a number of associations and groups representing the public sector, such as the National Governors' Association, the Southern Governors Association, the National League of Cities, the U.S. Conference of Mayors, the National Association of Regulatory Utility Commissions and the American Association of State Highway and Transportation Officials, have passed resolutions in support of better regulation or control of rail activities in market dominant areas. (See Appendix A.) While the western governors as a group are not on record on this issue, the National Governors' Association has taken a policy stand; in fact, two. One policy coming from its Energy and Environment Committee in 1984 calls for legislation to address market dominance and rate guidelines for coal and agricultural commodities. The other, from NGA's Transportation, Commerce and Communications Committee in 1983 asks only that the ICC do a better job of balancing the needs of the captive shippers and the railroads.

The railroads, not inexperienced in protecting their own interests in the legislative forum, have begun to organize actively and solicit alliances from shipping interests. As a consequence, the rail rate equity issue could well be one of the more active and hotly debated domestic issues on the agenda of the 99th Congress.

The 98th Congress

Legislation was introduced in both the House and Senate in the 98th Congress to amend the Interstate Commerce Act. Senator Wendell Ford (D-KY) introduced S. 1082 and identical legislation, H.R. 2584, was introduced in the House by Rep. Nick Rahall (D-WV). Basically the Ford/Rahall legislation would reaffirm the intent of the Congress that the ICC should provide reasonable protection for shippers and consumers in market dominant areas, making it clear that in deregulating most aspects of rail operation, Congress did not intend to abandon protection of captive shippers. The bills provided that the burden for justifying the reasonableness of rail rates in excess of 190% of variable costs rests with the carrier and not with the shipper. By reasserting the presumption of market dominance and, by making them conclusive presumptions, they would remove any exercise of discretion in this area from the ICC. The bills also would limit the Commission's latitude for traffic exemptions, a device used increasingly by the ICC to deregulate transportation, as in the case of coal for export.

These proposals were discussed during oversight hearings on the Staggers Act in 1984 in the Senate Commerce Subcommittee on Surface Transportation and in the House Public Works Subcommittee on Surface Transportation.

Senator Danforth (R-MO), now Chairman of the Senate Commerce, Science and Transportation Committee, also introduced a Joint Resolution (S.J. Res. 331) expressing the sense of the Congress that the ICC, in making determinations on railroad revenue adequacy, should:

1) consider multiple financial indicators such as return on investment, operating ratios, and other conventional financial indications;

2) consider evidence of geographic and product competition only when the railroad can show it exists and is relevant to the rate setting proceedings;

3) clarify the meaning of the guidelines on stand alone costs and drop the proposed 15 percent allowable rate increase guideline;

4) instruct the railroads to desist from anti-competitive practices such as refusal to provide requested reciprocal switching services;

5) request the ICC to facilitate discovery of railroad contract information by parties with standing to challenge such contracts.

Bills were also introduced in the Senate and the House late in the last Congress (S. 2417 and H.R. 4559) amending the Sherman Act to make it an antitrust violation for any railroad to deny a shipper in a market dominant area use of the rail facility on reasonable terms. Failing to gain "reasonable terms" for the railroad, the proponents of this approach would assert a right to the use of the track or other rail facility under a common carrier provision, causing this approach to be labeled the "trackage rights" provision. Because the bills deal primarily with antitrust provisions of the law, they were referred to the Senate and House Judiciary Committees. Hearings were held in both committees, but no bill was reported.

In fact, none of the rail rate relief legislation came out of committee in the last Congress. The bills stalled in committee, for several reasons:

1) Regulation of rail commerce is a large and complex issue involving a diversity of interests and opinions that run counter to the conventional attitude of the Congress toward railroads in particular and deregulation in general. In the legislative setting, such issues need time to germinate.

2) The issue needs to be articulated and refined. Congress needs to be educated. Constituent groups need to be organized and make their concerns and problems known to their Congressmen. In this respect, last year's Congressional considerations were prelude to a more focused and better organized campaign in the 99th Congress.

3) Congress has been in a deregulatory mood and is still largely imbued with the idea that railroads are the "sick child" of American industry and should not be burdened with unnecessary regulation. Those promoting the legislation have not succeeded in convincing Congress that there is a substantial level of support for legislative change or that the varied industrial and commercial shipping

interests have a unity of purpose and can point the way to a viable and workable solution.

4) There has, heretofore, been little effort to portray this as a consumer issue or to solicit the involvement and support of consumer groups and state and local governments. As a consequence, to some it appears to be little more than the positioning of two industrial titans, coal and railroads, to advance their own special interests.

New Coalitions for Change

In the 99th Congress a much more concerted and better orchestrated effort to advance the case for legislative change is emerging. While there is no assurance of success, it is clear the activities of these groups will raise the visibility of the issue in Congress and intensify the debate.

Several groups, formed by aggrieved interests, have surfaced and begun to define their agendas for relief. Some seek to strengthen or underscore the procedures in the Interstate Commerce Act for protecting the shipper in monopoly areas. Others want ICC to curb noncompetitive rail haul practices. Still others would treat noncompetitive rail practices as violations of the Sherman Antitrust Act, invoking the provisions of that Act for treble damages and asserting rights of access to the tracks of the rail line under common carrier provisions.

While dissimilar in approach and solution, all share one fundamental proposition -- a conviction that railroads are acting like economic monopolies in areas where they dominate the surface transportation of bulk goods and commodities. There is also a shared awareness that, for all practical purposes, as shippers they have no recourse from any sharp or arbitrary practices in which the carriers may engage. This concern is heightened by a recognition that mergers and consolidations are creating rail monopolies in many areas of the U.S. where intramodal competition previously existed. To protect themselves, three distinct interests have emerged in the past several months. They are the Consumers United for Rail Equity, the Procompetitive Shipping Group, and those advancing the concept of trackage rights. Additionally, another coalition has formed made up of shipping interests who want to see the Staggers Act amendments untouched. This groups identifies itself as the Committee Against Revising Staggers.

Consumers United for Rail Equity, CURE, while only recently formed, has the best organizational base and

potentially the largest legislative impact. The organization is an ad hoc coalition of private and publicly owned electric utility companies and a few eastern based coal producers (list of members attached as Appendix B). It is well financed and has retained counsel and hired professional staff in Washington to analyze the legal and economic aspects of the problem and mount a lobbying effort. CURE has also lined up some influential and well-placed Members of the House and Senate as legislative sponsors and initiated a series of educational and organizational meetings across the country aimed at broadening the base of support for legislative change beyond its dues paying members. As such, it is attempting to reach out and involve the varied interests of consumer groups, farmers, labor, state and local government, etc. in an effort to achieve legislative change.

After an intensive period of drafting and internal negotiations, CURE's legislative package was unveiled on February 20 in Washington, D.C. Basically their product is an expansion and refinement of the provisions of the Ford/Rahall legislation of the previous session. The primary objective of the legislation is to enhance the opportunity for a challenger to demonstrate, before the ICC, that a rate is excessive or a practice unfair. The preamble to the bill describes it as "...a balanced approach that encourages and promotes intramodal competition while providing adequate protection for persons served by market dominant rail carriers." To accomplish this, the CURE legislation would:

-- Retain the Staggers Act jurisdictional threshold of 180 percent of variable costs as the upper limit. Any rate above this for market dominated traffic would be considered prima facie to be excessive. The burden would be shifted to the carrier to demonstrate it was not. As is now the case, contracted rates would remain free from Commission jurisdiction.

-- Place a 12-month time limitation on ICC determinations.

-- Change the market dominance test to consider only the actual circumstances of whether a shipper has an economically feasible transportation alternative. Considerations of product or geographic alternatives by the ICC would be disallowed in making market dominant determinations.

-- Replace the revenue adequacy determination with a set of conditions that include not only an economic test but a review of a railroad's stock performance, bond ratings,

recent acquisition history and other commonly accepted indicators of financial health.

-- Require railroads to make a more equitable distribution of its additional revenue needs across classes of shippers.

-- Instruct the ICC to exercise its jurisdiction to assure the maintenance of joint rate and through route agreements, reciprocal switching arrangements and fair access to terminal facilities.

-- Restrict the ICC's latitude in exempting certain types of shipments (such as coal for export) from regulation where market dominance exists.

-- Reassert the authority of the states over some intrastate rail rates and practices.

-- Require a local hearing on rail abandonments with the cost to be borne by the railroad, and require that the data used in justifying the abandonment be specific to the facility under consideration.

While the main thrust of the CURE legislation is aimed at improving the advantage of the coal shipping interests in challenging rates before the ICC, the group has also made an effort to accommodate some of the interests and concerns of other major shipping interests. To attract the pro-competitive shipping group, CURE included legislative provisions aimed at preventing the arbitrary cancellation of "joint rates," "through routings" and reciprocal switching agreements. These cooperative shipping arrangements with connecting or competing railroads are part of the traditional "common carrier" service obligation, but in recent years as railroads merged and consolidated their service areas, there has been a tendency to deny these reciprocal service arangements which are essential to the movement of cargo across competing lines.

CURE adopted the provision on rail abandonments to accommodate the agricultural shipping interests. The problem of abandoned rail lines, especially in remote service areas, has long been a major concern of farm interests. The CURE abandonment provision would require a local hearing and require that the railroad's justifying financial data be specific to the proposed line abandonment and not based on system-wide or industry-wide averages. Also, in the event of a denial, the railroad would be prohibited for one year from filing a new abandonment petition for the same line or service.

On the other hand, some provisions which CURE was considering to enhance their outreach to other interest groups were dropped from the final package. CURE did not adopt an amendment widely supported by agricultural shipping interests to require divulgence of specific contract terms between the carrier and the shipper. The probable reason for the exclusion is that contract divulgence is not an altogether popular item with most coal shippers, who prefer protecting the confidentiality of their contracts with the carrier. Likewise, a provision to trigger "trackage rights" when rates exceeded 190 percent of variable costs was also dropped from the package. In its place is a modified provision for access to rail terminal facilities for competing rail carriers. As we will describe later in this chapter, the "trackage rights" approach is an innovative, but relatively controversial provision, and many of the coal and utility interests are cool to invoking antitrust provisions.

One amendment in the CURE legislation is likely to reduce rather than enhance the attraction of the legislation to non-coal shipping interests. In determining the "reasonableness" of a challenged rate, the ICC would be required to equitably distribute the revenue needs of the railroad to all other shippers in the captive category. The full impact of this provision is not clear, but it strikes at the differential pricing mechanism of rate making and would, if implemented, push some of the rail costs coal shipments now carry on to other major shippers.

Not surprisingly, the railroads were not caught speechless by the introduction of the CURE legislative package. In a press package released the same day as the CURE kick-off, the Association of American Railroads characterized the CURE approach as "Orwellian" and the title a misnomer. William Dempsey, President of the Association, said that "equity" had nothing to do with the group's objective. Instead, it should be called "the Utility Welfare Act," set up as "...special-interest legislation designed for the express benefit of the utility and coal industries...." Asserting that most of the problems CURE attempts to address do not, in fact, exist, Dempsey explained that "Rail coal rates have not skyrocketed, they have modified. Rail monopolies don't abound, they are rare. Competition holds down rail rates more efficiently than regulation did."

Now that they are fully in the fray, it remains to be seen whether CURE can maintain the identity of a broad-based consumer interest coalition, appealing to farm interests and electric consumer alike, or will be positioned, as the railroad would have it, as a group advancing a relief

package for coal and utility interests. CURE has lined up an impressive list of supporters, including such groups as the National Farmers Union, the National Grange, the National League of Cities and the Consumer Federation of America, behind its legislative package. (See Appendix B.) It has also initiated a grass roots consumer interest campaign and gained bipartisan support and legislative sponsorship of influential Members of Congress. Senator Russell Long (D-LA), ranking minority member of the Surface Transportation Subcommittee of the Senate Commerce, Science and Transportation Committee, and Senator Mark Andrews (R-ND), Chairman of the Senate Transportation Subcommittee of the Appropriations Committee, have agreed to lead the Senate effort for the CURE legislative package. In the House, W. J. "Billie" Tauzin (D-LA), a member of the Energy and Commerce Committee, and Nick J. Rahall (D-WV), a member of the Public Works Committee and chairman of the newly-created Interior Subcommittee on Mining and Natural Resources, are leading the sponsors, with Harold Rogers (R-KY) the chief Republican sponsor. This kind of support and cosponsorship, especially if it can be combined with a groundswell of grass roots support, will assure that the CURE proposal receives serious consideration in the 99th Congress.

But the potential strength of the CURE coalition is limited by a basic philosophical ambivalence on the part of its major members. Clearly, the members want some assurance of fairer treatment by the railroads for coal suppliers and coal users. Some reassertion of the ICC's regulatory capacity seems to hold the most promise. On the other hand, most are loath to openly support anything that suggests a return to regulation. Having been among the more vocal proponents of deregulation generally, they have difficulty suggesting that regulation might be needed to infuse certainty and price stability into their industrial operations. This ambivalence on the part of the coalition has caused some to view its legislative agenda as too measured and conciliatory.

Glenn Schleede, President of New England Energy, Inc., recently cautioned against going to Congress to ask for too little, on the time honored principle that you usually end up with even less than you ask for in legislative negotiations. In this context, he advised his colleagues in the energy industry to accept the fact that deregulation is not compatible with natural monopoly power, and press for strong regulatory protection in such areas. "Congress," Schleede said, "left shippers without adequate protection. Correcting the problem really amounts to 'reregulation' whether we like it or not."[1]

The Procompetitive Rail Steering Committee, which will be referred to as PRSC, is the second group to emerge with an agenda for changes in rail regulating practices. It is composed of a group of large shippers of chemicals, heavy equipment, timber and agricultural products and automobiles, and is organized under the auspices of the National Industrial Transportation League (see Appendix C). The group has a defined but limited agenda for legislative action. PRSC is interested in promoting better competition among railroads. To achieve this, the PRSC wants legislation to assure that cooperative shipping arrangements with connecting or competing railroads are preserved. These practices, which were common in the past and which facilitate efficient movement of traffic, are being deferred and cancelled as rail mergers and acquisition increase the monopoly pattern of rail systems.

Basically, the PRSC is caught in a dilemma between support for the concept of the Staggers Act with its declared purposes of promoting competition through deregulation and the fact of diminishing rail competition. As PRSC points out, between 1957 and 1983, 52 railroad mergers or consolidations occurred in the U.S. Even with passage of the Staggers Act, rail merger and consolidation has not abated.

When the Staggers Act was passed, there were 12 major railroads serving the nation. Today, seven rail systems account for 77 percent of total major railroad route mileage and 85 percent of operating revenues. Moreover, PRSC sees this pattern of rail merger and consolidation continuing with the bulk of the nation's commerce dominated by no more than five railroads within ten years. Accepting that the ICC cannot be counted on to forestall this process, the procompetitive shippers are seeking legislation which would put some brakes on the merger and consolidation phenomenon and, where it cannot be stopped, at least preserve some of the shippers' pre-existing arrangements for access to lines and terminals at reasonable costs.

The procompetitive proposal would amend the Interstate Commerce Act to prohibit service cancellations which are not economically justified. The proposal would also increase the number of access points to competitive rail services through the establishment of a proportional rate system, and would allow aggrieved parties the right to seek judicial relief from anticompetitive rate and route cancellations. The same judicial relief would be available with respect to protection of reciprocal switching rights, as with joint rates. Additionally, the legislation would assert the right of trackage at terminal facilities for all shippers within a given industrial area.

The PRSC posesses the strength that large industrial and agribusiness interests can bring to bear on the legislative process. Additionally, it has a potential set of allies among the nation's short-line railroads, some of whom have organized Railroads Against Monopolies (RAM), to protect their connecting lines of rail commerce with particular concern over the pattern of "joint rates" cancellations. Even so, the PRSC legislative objective is narrowly defined. So far they have not sought alliances with or embraced the agenda of CURE and recent developments may have diminished some of their vigor for pushing even their own legislative agenda. In late January, their parent group, the National Industrial Transportation League, together with the Association of American Railroads, reached an accommodation in a dispute over how the ICC handles competitive access issues. While the agreement relates to procedural conditions, it would, if implemented, have the effect of giving the shipper a better break before the ICC in protesting cancellation of joint rates and through routes. Since the competitive access issue is the major problem that many shippers identify with the implementation of the Staggers Act, the agreement for dispute resolution between NIT League and the AAR is significant. On the other hand, such an agreement between associations is not binding on its members nor does it have the force of instruction to the ICC that legislation would have. RAM, the short line railroad's coalition, had indicated that the agreement is not satisfactory from their perspective, and that they will press for other relief, including legislation. All the same, it may have dissipated some of the pressure that was developing among the pro-competitive shippers for legislative action.*

Second, and perhaps more significant, a number of the rank and file of the procompetitive group have begun moving into an opposing camp, claiming that rail deregulation has been a positive economic factor to their industry. This group, called the Committee Against Revising Staggers (CARS) is made up of more than 200 companies throughout the country, most of them shippers of manufactured goods and equipment. (See Appendix D.) They want the Staggers Act left alone, asserting that rail services have increased

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*Since the January 15th accord with the National Industrial Transportation League, the AAR has negotiated a comparable agreement with the Chemical Manufacturers Association (March 18) and an agreement with the American Paper Institute (March 1) on redefining market dominance. These parties have requested the ICC to incorporate their agreements into an administrative rulemaking under Ex Parte 458.

dramatically for the shipper since passage of the Act, and that reopening it now would serve no useful purpose. It is possible they are also mobilized by a concern that CURE's proposal for limiting the use of differential pricing in determining revenue adequacy would adversely affect them by resulting in increased rates for some intermittent shipments in captive market areas.

Trackage Rights characterizes the agenda of the other group to emerge seeking legislative changes in rail deregulation. It is a hybrid made up of coal producers, western public utility interests and the fertilizer industry. Commonly referred to as "trackage rights," the group advances a unique and disarmingly simple approach to the problem. They assert that railroads operate in most areas as economic monopolies and should be subject to the antitrust provision of the Sherman Act. Dismissing the idea that the ICC, even with legislative instruction, can be made to perform more responsively to shipper and consumer interests, this group would use the threat of invoking the Sherman Act as a means to gain access to the tracks of a particular carrier or, more likely, to negotiate favorable rates for shipments on those lines.

The trackage rights approach asserts that the railroads do not possess sole proprietorship over their lines. There is some precedent for this in public service regulation if it can be conclusively demonstrated that an "essential facility" such as an electric transmission line or a rail line, is being used by its proprietor to deny or inhibit essential commerce through monopoly practices. In Otter Tail Power Co. vs. United States, the Supreme Court affirmed that Otter Tail had monopolized or attempted to monopolize an "essential facility" by refusing to wheel power from other sources to municipalities that previously had been its captive customers. As such, the utility was found in violation of Sec. 2 of the Sherman Act, and required, by the Court, to wheel the power.[2]

More recently Congress endorsed a "common carrier" principle when it passed the Cable Telecommunications Act last year, providing that 10 to 15 percent of the privately-owned television system must be available for commercial use. This provision was justified on the basis that it was the best means to assure some measure of competitive use on what will be monopoly service systems.

There is less legal precedent for the "wheeling rights" application to rail commerce, mainly because the carriers have successfully maintained that the exclusive jurisdiction for determining rail and rate issues was with the ICC, not the Courts. The ICC has been loath to use its authority to

establish trackage rights, except in very limited circumstances such as provision of access to terminals, and as a condition to mergers or joint activities. Most recently, the ICC concluded that it has no power to compel a railroad to grant trackage rights over its lines to another carrier or to a shipper.[3]

Proponents, however, argue that the rail line in a "market dominant" area is an essential facility constituting the only practical means of moving a commodity to market. In such cases, if the railroad refuses to make the use of the track available on reasonable terms, the shipper could seek relief through the courts, citing violation of the Antitrust Act and seeking treble damages.

To make this avenue more explicitly available and to circumvent some of the disputed jurisdictional assertions that would be raised by the railroads and probably the ICC, the trackage rights proponents would amend the Sherman Act, not the Interstate Commerce Act. Proposed legislation introduced and considered in the last Congress would provide that upon determination that shipping terms are not reasonable, the shipper or the receiver of the shipment may assert a "right" to the utilization of the track under reasonable terms.

This would enable a coal shipper or governmental unit, for example, to maintain its own rail cars and move shipments over the rails of existing lines to reach markets in the fastest and most economical way. Many coal companies and other large shippers already own their freight cars, and at least one state -- Montana -- has gained authority from its legislature to take title to abandoned lines and lease the traffic operation of the lines to shippers or other competing interests.

The scenario laid out by the trackage rights proponents assumes that shippers could convince the ICC or the courts that the rates or terms offered by the carrier were not "reasonable." Thus, the determination of "reasonable terms" becomes the turning point for implementation. Proponents assert that the provision would, for the most part, be self-enforcing. By deleting the anti-injunction language from Sec. 16 of the Clayton Act, it would remove the current uncertainty as to a court's ability to fashion injunctive relief under antitrust provisions against the railroads. Because of the potential financial consequences associated with an antitrust violation -- collection of treble damages -- the railroads, they maintain, would be forced to keep the terms of usage "reasonable," or conversely, would offer to share their track for fair compensation. Consequently, neither the courts nor the ICC would be burdened by a rash

of challenges, since a few initial test cases would set the pattern and define the dimensions of "reasonable terms."

Critics, on the other hand, argue that, if left to ICC, the reasonableness determination would simply become another protracted and expensive proceeding with the railroads winning in the end. Others argue that invoking the antitrust provisions sets up dual or sequential review proceedings -- first, through the ICC and then the courts; probably doubling the time and the cost of review for both the plaintiff and the railroads.

Other issues raised about the practical application of the trackage rights proposal relate to questions of operator liability, maintenance of safety standards and fair labor practices; important questions but ones which could probably be worked out should the proposal be enacted.

Aside from operational considerations, the most imposing political problem with the trackage rights approach is the criticism that it amounts to a confiscation of private property. The railroads have already begun to portray the trackage rights approach as a provision for "unfair taking" of their property. They have testified that the approach "...is at root...an attack on the concept of 'demand' or 'differential' pricing of rail services...."[4] By limiting the amount a railroad could charge for the use of its tracks to "...a fair return on the proportion of the rail carrier's prudent investment...that the shipper's traffic bears to all traffic..." the carrier would be prohibited from loading some of its costs onto the captive shipper, thus ending differential pricing. The effect, the railroad industry maintains, would be to force most lines into bankruptcy.

Outlook for the 99th Congress

Whatever the outcome of the legislative debate over rail rate relief, its jurisdictional disposition in the Congressional committees is predictable. Legislation to amend the Interstate Commerce Act, such as CURE and the Procompetitive Group are advancing, will be referred to the committees dealing with Commerce and Transportation. In the Senate this means the Commerce, Science and Transportation Committee, and its Subcommittee on Surface Transportation.

The Chairman of the full Committee is Senator John Danforth (R-MO), who, as sponsor of last year's Joint Resolution, recognizes the existence of the problem confronting shippers in monopoly service areas. He is considered moderate in his approach to rail reform, preferring a measured approach to defining the role and

responsibility of the ICC. The effect of a Joint Resolution is nonbinding, only instructing the ICC on the intent and interest of the Congress. It is possible, however, that Senator Danforth will be persuaded that a genuine legislative remedy is necessary, in which case he may back the CURE legislation or something comparable. Much will depend on the Chairman of the Subcommittee on Surface Transportation, Senator Robert Packwood (R-OR). Senator Packwood has not been identified as a proponent of the rail equity issue, but the active support of the ranking minority member of the Subcommittee, Senator Russell Long (D-LA), in behalf of the CURE legislation could serve as a persuasive influence on the Subcommittee. Additionally, Senator Ford, who sponsored the amendments to clarify the Staggers Act last year, is also a senior member of the full Committee and a cosponsor of the CURE bill, as is Senator Ted Stevens (R-AK), another ranking Committee member.

How the proposal to amend the Interstate Commerce Act will actually fare in Senate Commerce depends on a number of factors, including how effectively the grass roots support for legislative relief can be mustered, how persuasive the hearings are and how unified and aggressive the CURE or Procompetitive members are in pursuing legislative remedy. Not least of all, the outcome will be influenced by how well the railroads organize to resist legislative change. It is also well to remember that there are other rail issues on the plate of these Committees in this Session -- the sale of Conrail, the Federal Rail Safety Act and the future of Amtrak are all priority over rail rate relief. All things considered, the climate is not bad in the Senate for favorable Committee action on a legislative package for changes to the Interstate Commerce Act, at this early reading. The same cannot necessarily be said of the corresponding Committee in the House.

In the House of Representatives, primary jurisdiction over amendments to the Interstate Commerce Act resides with the Energy and Commerce Committee and its Subcommittee on Commerce, Transportation and Tourism. The Chairman of the Subcommittee, James Florio (D-NJ), is considered a strong proponent for maintaining a climate in which the railroads can achieve economic viability and, as a champion of the deregulatory aspects of the Staggers Act, he can be expected to resist efforts to increase regulation over that industry. Even so, Florio has indicated that after four years of experience with the Staggers Act it may be useful to review its implementation and address any problems that may have resulted from oversights or shortcomings in the Act or its implementation. In this context, he has acknowledged the possibility that captive shippers were not adequately provided for in the Act, and indicated a willingness to

review those aspects of the Act to determine if further definition or refinement is necessary. While this does not promise quick or favorable resolution in the House Subcommittee, it at least indicates a less hostile atmosphere than previously existed toward rail reregulation in that Committee.

It is noteworthy from a western state perspective that the House Energy and Commerce Committee is dominated by eastern and midwestern members, with only a few members such as Tim Wirth (D-CO) and Bill Richardson (D-NM) who might be expected to bring a western perspective to rail regulation considerations. On the other hand, some of the midwestern members, including the Chairman of the full Committee, John Dingell (D-MI) and Tom Tauke (R-IA), may respond to the concerns of the utility industry and the electric consumers with the high cost of coal shipment, as well as the cost of shipping manufactured goods and commodities out of the Midwest. While Dingell has not been an active proponent, thus far, of revising the Staggers Act, he recently put the ICC on notice that its Ex Parte review of Staggers Act implementation should in no way be considered "...as either a substitute or a precondition to further Congressional oversight and review to determine whether the policies set forth in the Staggers Rail Act are being carried out in the balanced and reasoned manner that Congress intended."

Legislation amending the antitrust provisions of the Sherman Act will be considered by the Senate and House Judiciary Committees. In the Senate the full Committee has jurisdiction on antitrust matters; in the House antitrust is considered by the Monopolies and Commercial Law Subcommittee. Judiciary jurisdiction allows the bill to circumvent Energy and Commerce in the House. But while this could mean more favorable consideration in the Judiciary Committee, especially as it enjoys the sponsorship of John Seiberling (D-OH), a ranking member of the Committee, it does not assure expeditious action. The House Judiciary Committee is notoriously deliberate in its consideration of legislation, especially when it has the potential of placing new burdens on the Courts.

The Seiberling bill (H.R. 1140), introduced on February 7, is cosponsored by Congressmen Udall of Arizona, Glickman of Kansas, Dorgan of North Dakota and Synar, English, Watkins and McCurdy of Oklahoma. All of the sponsors, thus far, are Democrats.

In the Senate Judiciary Committee the trackage rights proposal was introduced last year by Senator DeConcini (D-AZ) with cosponsorship from Senators Max Baucus (D-MT), Ford (D-KY), and Don Nickles (R-OK). A slightly modified

proposal has been reintroduced this year by Senator DeConcini, and is circulating for cosponsorship. The bill (S. 447) is titled the "Railroad Antimonopoly Act" and DeConcini has announced he will push for hearings on it in the Judiciary Committee this spring.

While the outcome of the legislation is still uncertain, what is clear is that the problems of shippers in market dominant areas have been given an exceptionally high profile. In the legislative deliberations that ensue, those alleging the railroads are taking unfair advantage of their market position have gained a national forum in which to lay out their case and offer their legislative remedies. Likewise, the railroads will have an opportunity to define their case and defend the status quo. In an area of national transportation and commerce which is in rapid transformation, it is both timely and appropriate that the issue of optimal balance between unrestrained commerce and regulation be examined by the Congress and revised, if necessary. The outcome will shape the direction of national transportation policy for decades. The Governors of the western states have a critical stake in the outcome of this debate and should be heard from.

CHAPTER V FOOTNOTES:

[1] Speech before the Natural Resources Law Section, ABA, Washington, D.C., October 22, 1984.

[2] 40 U.S. 366 (1973).

[3] Ex Parte No. 347, Coal Rate Guidelines, July 14, 1983.

[4] Op. Cit., Dempsey testimony.

NATIONAL GOVERNORS' ASSOCIATION

(Adopted 2/28/84)

D. - 10

## COAL TRANSPORTATION

One of the most significant constraints of the expansion of coal production, distribution, and use is the capacity and reliability of the coal transportation system throughout the country. An estimated 75 percent of this country's annual coal production is trucked on public roads for at least part of its journey. By 1985, this tonnage is expected to increase significantly. In addition to direct coal haulage, state and county road systems must bear increased traffic due to increased employment and the movement of equipment and other supplies. In regions where coal is carried exclusively by rail, the increased volume of shipments threatens to disrupt the highway system by blocking rail crossings for intolerable periods of time each day. Furthermore, the nation's waterways and port facilities are not adequate to meet the increased demands for the transportation of coal. These problems directly concern all states between the point of production and the point of use. The NGA Coal Transportation Task Force has worked closely with the Federal Highway Administration to develop an accurate assessment of coal transportation needs.

To maintain and expand production, distribution, and use of coal to meet the nation's critical energy needs, the President and Congress should formulate and implement as soon as possible a federal-state coal transportation assistance program. Revenue-generating mechanisms to fund a new coal transportation assistance program should be enacted. The program should be designed to provide for the rehabilitation, improvement, expansion, and maintenance of transportation facilities for moving coal by rail, highway, and waterway, in order to meet present and future coal transportation needs and to minimize adverse transportation impacts that result from expanded coal production, distribution, and use.

The nation's rail freight system continues to be of key importance to the transportation of coal. In the Staggers Rail Act of 1980, Congress recognized the unique dependence of coal shippers on rail transportation and the importance of balancing the needs of rail carriers, coal shippers and the public. However, the governors are EXTREMELY concerned that the way in which the Interstate Commerce Commission (ICC) has been implementing provisions of the law ~~places a~~ IS PLACING AN UNFAIR burden on many captive coal shippers, consumers of electricity and consumers of coal. Areas of specific concern are:

- Product and Geographic Substitution or Competition. Under the Staggers Act, rates for shipments are deregulated unless the ICC determines that a particular shipment is captive or a carrier has market dominance in transporting goods. The ICC in its regulations does not consider a shipment as captive or a rail carrier as having market dominance if geographic, modal or product substitutions are available. The Governors are ~~concerned~~ TROUBLED by this overly restrictive interpretation of the law and believe that the application of this theoretical standard TO COAL SUPPLIERS is unfair and inappropriate ~~to many coal shippers~~. With regard to product substitution, the negative effect on shippers and consumers of coal is particularly severe because an electric utility plant could be required to convert to other energy sources at prohibitive costs. The Governors URGE ~~request that~~ the CONGRESS ~~ICC~~

~~revise its regulations~~ TO AMEND THE STAGGERS ACT TO ENSURE THAT

WHEN NO ECONOMICAL ALTERNATIVE MEANS OF TRANSPORTATION EXISTS FOR A PARTICULAR RAIL MOVEMENT, SUCH MOVEMENT WILL BE AFFORDED FULL PROTECTION AS A CAPTIVE SHIPMENT. ~~promptly so that a finding of captive shipments and market dominance of a railroad can be made if no economical alternative means for transportation exists for a particular rail movement.~~

o ~~Coal~~ Rate Guidelines. ~~The Governors request that the ICC consider revising these coal rate guidelines so that the needs of captive shippers are balanced against the railroads' need for a reasonable rate of return.~~ THE PROPOSED ~~COAL~~ RATE GUIDELINES FOR COAL *and agricultural* SHIPMENTS SUBJECT TO ICC REVIEW DO NOT GIVE EQUITABLE CONSIDERATION TO ALL PARTIES INVOLVED. THE GOVERNORS URGE CONGRESS IN AMENDING THE STAGGERS ACT TO CREATE AN ADEQUATE BALANCE BETWEEN THE NEEDS OF SHIPPERS AND THE RAILROADS' NEED FOR AN ADEQUATE RATE OF RETURN.

~~The Governors urge the ICC to assure that its decisions balance the needs of carriers, shippers and the public. In addition, the Governors urge the Congress, through oversight hearings, to assure itself that the Staggers Rail Act of 1980 is being administered in such a way as to achieve its purposes.~~ THE GOVERNORS BELIEVE THE FAILURE OF THE ICC TO PROPERLY IMPLEMENT THE STAGGERS ACT HAS PREVENTED THE ACT FROM BALANCING THE NEEDS OF SHIPPERS, CARRIERS, AND THE PUBLIC, AND NECESSITATES PROMPT CONGRESSIONAL ACTION TO REVISE THE STATUTE ACCORDINGLY.

THE GOVERNORS WOULD OPPOSE CHANGES TO THE STAGGERS ACT IN AREAS OTHER THAN THOSE ADDRESSED IN THIS POLICY.

National Governors' Association

1983

Deregulation of The Rail Industry

Problems confronting the rail industry prompted enactment of regulatory reforms that were essential to helping prevent further decline of the industry.

The National Governors' Association supports the greater rate-making freedom to facilitate recovery of the costs of providing service, incentive rates and contract rates. Discrimination against shippers and regions should be eliminated.

Interstate Commerce Commission (ICC) should reduce its regulation of rail operations in such areas as car service and compensation, while ensuring that small carriers and private car users are protected from discrimination. However, the ICC should retain the right to review car service practices when there are shipper complaints of discrimination.

While supporting these regulatory reforms, the Association is aware of the concerns of many states and industries associated with the movement of bulk commodities such as coal and grain as it relates to the potential for excessive rate increases. Shippers of bulk commodities who are captive to rail transportation because an economically practical transportation alternative is not readily available, should be afforded protection by ICC rate guidelines.

The final impact of deregulation cannot be fully understood at this time. Since the consequences of the major deregulation of the rail industry will be far-reaching, the Association urges careful and considered assessment of the impacts on the rail industry, competing modes and rail users. Even so, the proposed rate guidelines for some commodities have generated controversy. Therefore, the Governors request that the ICC consider revising these guidelines so that the needs of captive shippers are balanced against the railroads' need for a reasonable rate of return.

State rail regulation should not be increased to compensate for reduced ICC regulation.

## Amendments to the Staggers Rail Act of 1980

WHEREAS, fifty-two percent of electric generation in the United States today is fueled by coal, sixty-five percent of all coal produced is moved by rail, and eighty-five percent of all coal shipped by rail is captive to one railroad, so that the price of electricity in much of the country depends upon the rail transportation rates charged to captive shippers; and

WHEREAS, the Staggers Rail Act of 1980 provided for deregulation of competitive rail traffic while continuing regulation of rail rates where railroads exercise monopoly power; and

WHEREAS, under the Staggers Rail Act, the Interstate Commerce Commission was charged with impartial balancing of the revenue needs of railroads with the needs of captive shippers and American consumers for protection from monopolistic pricing practices, and the ICC has issued a series of decisions granting to railroads virtually unlimited pricing freedom on captive rail traffic, including decisions which (1) define "market dominance" so as to place ICC regulatory protection beyond the reach of many captive coal shippers; (2) set standards for "reasonable" rates which will allow coal transportation rates to double in real terms in five years; (3) exempt export coal from regulation although United States coal is already fifteen to twenty percent more costly than world market prices due in large part to transportation costs; (4) define "revenue adequacy," on which several pricing freedoms for railroads under the Staggers Act are based, unrealistically, so that no Class I railroads, no matter how profitable, are considered to have adequate revenues, and highly profitable railroads will be allowed billions of dollars in extra rate increases; and

WHEREAS, the aformentioned Interstate Commerce decisions impose an enormous cost burden on captive shippers and their electricity consumers; and

WHEREAS, legislation has been introduced to the Congress which constructively addresses many of the needs outlined herein,

NOW, THEREFORE, BE IT RESOLVED that the U.S. Conference of Mayors urges Congress to enact legislation to ensure reasonable rail rates for captive rail traffic, including provisions which:

- Define "market dominance" realistically, so that all captive shippers may obtain ICC regulatory review;
- Require ICC consideration, in setting maximum reasonable rates, of not only the revenue needs of carriers, but also such standards as the cost to the railroad of providing service; whether the traffic involved is paying an unreasonable share of the carrier's fixed costs; the impact of the rate on national energy goals; and the extent to which carrier revene shortfalls are attributable to hauling traffic at noncompensatory rate levels or failing to maximize earnings on competitive traffic;
- Require consideration, in determining "adequate revenues" for railroads, of realistic indicators of financial health, and require the use of standard depreciation accounting and exclusion of deferred tax reserves in calculating the railroad's return on investment;
- Require the ICC, in calculating the inflation index upon which automatic rate increases are based, to adjust for changes in railroad productivity;
- Reauthorize and fund the Railroad Accounting Principles Board;
- Allow for rail rate decreases when railroad costs decrease;
- Require adoption of fair and reasonable procedures for ICC review of state regulatory decisions on intrastate rail rates;
- Prevent anticompetitive or predatory cancellations of joint rates;
- Prohibit the Interstate Commerce Commission from exempting market dominant traffic from regulation; and

BE IT FURTHER RESOLVED that the U.S. Conference of Mayors supports legislative initiatives to address these critical issues, and urges the Congress to enact legislation to obtain for captive rail shippers protection from monopolistic pricing practices outlined above.

NATIONAL LEAGUE OF CITIES

POLICY RESOLUTIONS

RESOLUTION #11

AMENDMENTS TO THE STAGGERS RAIL ACT OF 1980.

WHEREAS, fifty-two percent of electric generation in the United States today is fueled by coal, sixty-five percent of all coal produced is moved by rail, and eighty-five percent of all coal shipped by rail is captive to one railroad, so that the price of electricity in much of the country depends upon the rail transportation rates charged to captive shippers; and

WHEREAS, the Staggers Rail Act of 1980 provided for deregulation of competitive rail traffic while continuing regulation of rail rates where railroads exercise monopoly power; and

WHEREAS, under the Staggers Rail Act, the Interstate Commerce Commission was charged with impartial balancing of the revenue needs of railroads with the needs of captive shippers and American consumers for protection from monopolistic pricing practices, and the ICC has issued a series of decisions granting to railroads virtually unlimited pricing freedom on captive rail traffic, including decisions which: (1) define "market dominance" so as to place ICC regulatory protection beyond the reach of many captive coal shippers; (2) set standards for "reasonable" rates which will allow coal transportation rates to double in real terms in five years; (3) exempt export coal from regulation although United States coal is already fifteen to twenty percent more costly than world market prices due in large part to transportation costs; (4) define "revenue adequacy," on which several pricing freedoms for railroads under the Staggers Act are based, unrealistically, so that no Class I railroads, no matter how profitable, are considered to have adequate revenues, and highly profitable railroads will be allowed billions of dollars in extra rate increases; and

WHEREAS, the aforementioned Interstate Commerce Commission decisions impose an enormous cost burden on captive shippers and their electricity consumers; and

WHEREAS, legislation has been introduced to the Congress which constructively addresses many of the needs outlined herein;

NOW, THEREFORE, BE IT RESOLVED that the National League of Cities urges Congress to enact legislation to ensure reasonable rail rates for captive rail traffic, including provisions which:

- Define "market dominance" realistically, so that all captive shippers may obtain ICC regulatory review.

- Require ICC consideration, in setting maximum reasonable rates, of not only the revenue needs of carriers, but also such standards as the cost to the railroad of providing service; whether the traffic involved is paying an unreasonable share of the carrier's fixed costs; the impact of the rate of national energy goals; and the extent to which carrier revenue shortfalls are attributable to hauling traffic at noncompensatory rate levels or failing to maximize earnings on competitive traffic;

- Require consideration, in determining "adequate revenues" for railroads, of realistic indicators of financial health, and require the use of standard depreciation accounting and exclusion of deferred tax reserves in calculating the railroad's return on investment;

- Require the ICC, in calculating the inflation index upon which automatic rate increases are based, to adjust for changes in railroad productivity;

- Reauthorize and fund the Railroad Accounting Principles Board;

- Allow for rail rate decreases when railroad costs decrease;

- Require adoption of fair and reasonable procedures for ICC review of state regulatory decisions on intrastate rail rates;

- Prevent anticompetitive or predatory cancellations of joint rates; and

- Prohibit the Interstate Commerce Commission from exempting market dominant traffic from regulation.

BE IT FURTHER RESOLVED that the National League of Cities supports legislative initiatives to address these critical issues, and urges the Congress to enact legislation to obtain for captive rail shippers protection from monopolistic pricing practices outlined above.

Approved by the Membership of the National League of Cities
• Annual Business Meeting • November 30, 1983 • New Orleans

January 24, 1985

C.U.R.E. COALITION

Alabama Coal Association
American Bakers Association
American Public Power Association
American Trucking Association
Association of Illinois Electric Cooperatives
Association of Louisiana Electric Co-ops
AZ Agricultural Chemicals Association
Coal Exporters Association of the United States, Inc.
Colorado Rural Electric Association
Consumer Energy Council of America
Consumer Federation of America
Cooperative Power Association
Eastern Coal Transportation Conference
Edison Electric Institute
Electric Power Associations of Mississippi, Inc.
Gulf Ports Association
Houston Port Bureau, Inc.
Illinois Farmers Union
Indian Electric Cooperative, Inc.
Indiana Municipal Electric Association
Indiana Statewide Association of Rural Electric Cooperatives, Inc.
International Minerals & Chemical Corporation
Kansas Electric Cooperative, Inc.
Mining and Reclamation Council of America
Municipal Electric Systems of Oklahoma
National Association of Regulatory Utility Commissioners
National Coal Association
National Farmers Organization
National Farmers Union
National Grange
National League of Cities
National Rural Electric Cooperative Association
Ohio Rural Electric Cooperative, Inc.
Petit Jean Electric Cooperative Corporation
Riley Whittle Inc.
Rocky Mountain Farmers Union
Surface Mining Research Library
Tennessee Valley Public Power Association
The Rail Action Corporation (TRAC)
United Steelworkers of America
U.S. Conference of Mayors
West Virginia Surface Mining & Reclamation Association
Western Coal Traffic League
Wisconsin Electric Cooperative Association
Women Involved in Farm Economics
Youth for Energy Independence

February 25, 1985

# SUPPORTERS OF THE CONSUMER RAIL EQUITY ACT

SPONSORED BY SENATORS MARK ANDREWS (R-ND), RUSSELL LONG (D-LA)
TED STEVENS (R-AK), WENDELL FORD (D-KY) AND
REPRESENTATIVES BILLY TAUZIN (D-LA), NICK RAHALL, (D-WV),
HAROLD ROGERS (R-KY)

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Alabama By-Products Corp.
Alabama Coal Association
Alabama Electric Cooperative, Inc.
Algona Municipal Utilities
Allegheny Power System, Inc.
Amca Resources, Inc.
American Bakers Association
American Electric Power Company
American Public Power Association
Arizona Electric Power Cooperative
Arkansas Electric Cooperative Corporation
Arkansas River Power Authority
Association of Illinois Electric Cooperatives
Association of Louisiana Electric Co-ops
Atlantic City Electric Company
Arizona Agricultural Chemicals Association
Baltimore Gas & Electric
Blue Diamond Coal Company
Carbon Coal Company
Carolina Power and Light Company
Cedar Falls Utilities
Central Illinois Light Company
Central Louisiana Electric Company, Inc.
Central Power and Light Company
City of Austin Electric Utility
City of Lakeland, Florida
City Public Service Board of San Antonio
Cleveland Electric Illuminating Company
Coal Exporters Association of the United States, Inc.
Colorado Rural Electric Association
Consolidation Coal Company
Consumer Energy Council of America
Consumer Federation of America
Cooperative Power Association
Dairyland Power Cooperative
Dayton Power and Light Company
Delta Coals, Inc.
Department of Utilities, City of Colorado Springs
Dixie Fuel Company

Drummond Coal Company, Inc.
Eastern Coal Transportation Conference
Edison Electric Institute
Electric Power Associations of Mississippi, Inc.
Grand River Dam Authority
Gulf Ports Associacion
Heartland Consumers Power District
Houston Lighting & Power Company
Houston Port Bureau, Inc.
Illinois Farmers Union
Illinois Power Company
Indian Electric Cooperative, Inc.
Indiana Municipal Electric Association
Indiana Statewide Association of Rural Electric Cooperatives,Inc.
Indianapolis Power & Light Company
International Minerals & Chemical Corporation
Iowa Public Service Company
Iowa-Illinois Gas and Electric Company
Jim Walter Corporation
Kansas City Power and Light Company
Kansas Electric Cooperative, Inc.
Kansas Gas and Electric Company
Los Angeles Department of Water & Power
Louisiana Department of Natural Resources
Louisiana Municipal Association
Louisiana Police Jury Association
Lower Colorado River Authority
Metropolitan Edison Company
Mining and Reclamation Council of America
Minnesota Power and Light Company
Missouri Public Service Company
Municipal Electric Systems of Oklahoma
National Association of Regulatory Utility Commissioners
National Association of State Utility Consumer Advocates
National Coal Association
National Council of Farmer Cooperatives
National Farmers Association
National Farmers Union
National Grange
National League of Cities
National Rural Electric Cooperative Association
Nevada Attorney General Consumer Advocate
North Dakota Public Service Commission
North Dakota Rural Electric Cooperative
North Dakota Wheat Commission
Ohio Edison Company
Ohio Rural Electric Cooperative, Inc.
Oklahoma Gas and Electric Company
Omaha Public Power District
Otter Tail Power Company
Peabody Holding Company

Pennsylvania Power and Light Company
Pennsylvania Rural Electric Association
Petit Jean Electric Cooperative Corporation
Platte River Power Authority
Portland General Electric Company
Potomac Electric Power Company
Public Service Company of Oklahoma
Pyro Mining Company
Randall Fuel Company, Inc.
Riley Whittle Inc.
Rocky Mountain Farmers Union
Royal Fuel Company
Salt River Project
Savannah Electric & Power Company
South Carolina Electric & Gas Company
South Carolina Public Service Authority
South Mississippi Electric and Power Association
Southern Indiana Gas & Electric Company
Surface Mining Research Library
Tampa Electric Company
Tennessee Valley Public Power Association
The Rail Action Corporation (TRAC)
The Southern Company
Transco Coal Company
Union Electric Company
United Auto Workers
United Small Coal Operators, Inc.
United Steelworkers of America
U.S. Conference of Mayors
Utilities Department, City of Lafayette, Louisiana
Virginia Electric and Power Company
Western Farmers Electric Cooperative
Western Coal Traffic League
West Virginia Surface Mining & Reclamation Association
Wisconsin Power & Light Company
Wisconsin Public Service Corporation
Women Involved in Farm Economics
Youth for Energy Independence

## THE NATIONAL INDUSTRIAL TRANSPORTATION LEAGUE

### Procompetitive Rail Steering Committee

Allied Corporation
American Iron and Steel Institute
Amoco Chemicals Company
Cargill Incorporated
Celanese Chemical Company, Inc.
Chrysler Corporation
Colt Industries Inc
Ethyl Corporation
FMC Corporation
Ford Motor Company
ICI Americas, Inc.
International Harvester Company
International Paper Company
Manville Service Corporation
Monsanto Company
Occidental Chemical Corporation
Olin Corporation
PPG Industries, Inc.
Reichhold Chemicals Inc.
Union Carbide Corporation
Uniroyal, Inc.

# THE
# "C.A.R.S."
# COMMITTEE AGAINST REVISING STAGGERS
# GROUP OF COMPANIES
# (BY STATE)

As of 1-23-85

ARKANSAS

OK FEED MILL
SANYO MANUFACTURING CORPORATION
TYSON FOODS

ARIZONA

QV DISTRIBUTORS

CALIFORNIA

AGREX, INC.
AMERICAN PACIFIC FORWARDING
AMERON
R. A. BARNES, INC.
BASIC AMERICAN FOODS
BEATRICE/HUNT WESSON FOODS
CARNATION COMPANY
CROWN ZELLERBACH
DEVCO DISTRIBUTION
FOSTER COMMODITIES
FOSTER POULTRY FARMS
FREIGHT DISTRIBUTION SERVICES, INC.
E. J. GALLO
HANJIN CONTAINER LINES, LTD.
INTERMODAL TRANSPORT COMPANY (ITCO)
KERN FOODS
LAWI/CSA
R&D LATEX
SAFEWAY STORES, INC.
STAR-KIST FOODS, INC.
TOYOTA MOTOR SALES, U.S.A., INC.
TRI-VALLEY GROWERS
VALLEY GRAIN PRODUCTS
VAN WATERS & ROGERS

COLORADO

CF&I STEEL
COORS INDUSTRIES

CONNECTICUT

AMERICAN CAN COMPANY
BEKER INDUSTRIES CORP.
GEORGIA-PACIFIC CORPORATION
REED LIGNIN, INC.
H. MUEHLSTEIN & COMPANY

DISTRICT OF COLUMBIA

AMERICAN RETAIL FEDERATION

FLORIDA

CLEVELAND WHOLESALE LUMBER CO.
PUBLIX SUPER MARKETS, INC.
WINTER GARDEN CITRUS COOP

GEORGIA

BLUE BIRD BODY COMPANY
HUSKY INDUSTRIES
GREAT SOUTHERN PAPER COMPANY
MACKMILLAN BLOEDEL BUILDING MATERIAL
PEACHTREE DOORS, INC.
SOUTHWIRE COMPANY
TRAILER-MATE, INC.

IDAHO

CANFOR, U.S.A.
IDAHO GROWERS SHIPPERS ASSOCIATION
IDAHO TIMBER CORPORATION
MORRISON-KNUDSEN COMPANY
ORE-IDA FOODS, INC.
J. R. SIMPLOT COMPANY
UNIVERSAL ROYAL APEX
V-1 OIL

ILLINOIS

ALLIED TUBE & CONDUIT CORP.
ARCHER DANIELS MIDLAND COMPANY
CHANEN'S INC.
CHRISMAN FERTILIZER CO.
GENEX TERMINALS INC.
HUB CITY TERMINALS, INC.
JOAN OF ARC
KEYSTONE STEEL AND WIRE COMPANY
MARTIN-BROWER COMPANY
MIDWEST SHIPPERS' AGENTS, INC.
QUAKER OATS CO.
SEARS, ROEBUCK & COMPANY
A. E. STALEY MANUFACTURING
TRANSBULK, INC.
WESTERN INTERMODAL

INDIANA

AMERICAN MAIZE PRODUCTS CO.
GRAHAM GRAIN COMPANY
INLAND CONTAINER CORPORATION
REILLY TAR & CHEMICAL CORP.

IOWA

GRAIN PROCESSING CORP.
HON INDUSTRIES
SIOUX CITY RELOAD

KANSAS

ADM MILLING
AMERICAN INTERMODAL INTERNATIONAL, INC.
PARKER GRAIN CO.

KENTUCKY

LOUISVILLE EDIBLE OIL
THOMAS INDUSTRIES, INC.

LOUISIANA

ALLIED FIBERS & PLASTICS
RUBICON, INC.

MARYLAND

BLACK AND DECKER (U.S.) INC.
EASTALCO ALUMINUM CO.
PERDUE FARMS, INC.

MASSACHUSETTS

W. R. GRACE & COMPANY

MICHIGAN

GENERAL MOTORS CORPORATION
GERBER PRODUCTS
KELLOGG COMPANY

MINNESOTA

BENSON-QUINN CO.
FARMERS UNION CENTRAL EXCHANGE, INC.
GEORGE A. HORMEL COMPANY, INC.
I. S. JOSEPH COMPANY
MARTREX INDUSTRIAL CHEMICALS, INC.
MARVIN LUMBER & CEDAR COMPANY
STRUCTURAL WOOD CORP.
VIKING FOREST PRODUCTS

MISSISSIPPI

VERTAC CHEMICAL CORP.

MISSOURI

APEX OIL COMPANY
PET, INC.
PIONEER WOOD PRODUCTS

MONTANA

TOBACCO VALLEY LUMBER CO.

NEBRASKA

CONAGRA, INC.
IBP, INC.
LYMAN ELEVATOR

NEVADA

AMERICAN BORATE COMPANY
PACIFIC ENGINEERING & PRODUCTION CO.
SIERRA CHEMICAL COMPANY

NEW JERSEY

CPC INTERNATIONAL INC.
CAMPBELL SOUP COMPANY
CHICAGO SHIPPERS, INC.
HARTZ MOUNTAIN
JOHNSON & JOHNSON BABY PRODUCTS
T. J. LIPTON CO., INC.
NABISCO BRANDS, INC.
SUNSHINE BISCUITS, INC.
UNION CAMP CORP.

NEW MEXICO

PUCCI DISTRIBUTION CO.

NEW YORK

CONTINENTAL GRAIN CO.
WESTVACO

NORTH CAROLINA

FIELDCREST MILLS, INC.
NUCOR CORP.

NORTH DAKOTA

LAVELLE COMPANY

OHIO

AMERICAN GREETINGS CORP.
MENNEL MILLING CO.
THE PROCTER & GAMBLE COMPANY
RAIL VAN CONSOLIDATORS, INC.
ROSS LABORATORIES
J. M. SMUCKER COMPANY
STOUFFER FOODS CORPORATION

OKLAHOMA

AGRICO CHEMICAL COMPANY
GREAT NATIONAL COAL COMPANY
PETRALITE SPECIALITY POLYMERS
RIFFE PETROLEUM COMPANY
WARREN PETROLEUM

OREGON

H. E. BELL & ASSOCIATES
CASCADE STEEL ROLLING MILLS, INC.
CASCADE WAREHOUSE COMPANY
CASCADE WEST TRANS. BROKERS, INC.
CENTENNIAL MILLS, INC.
CLEAR PINE MOULDINGS, INC.
COLUMBIA STEEL CASTING COMPANY
GILMORE STEEL COMPANY
HAMPTON LUMBER COMPANY
HOFF FOREST PRODUCTS
LOUISIANA-PACIFIC CORPORATION
NORTH PACIFIC LUMBER COMPANY
ROSEBURG LUMBER COMPANY
LES SCHWAB WAREHOUSE CENTER, INC.
WALLOWA LAKE FOREST INDUSTRIES
WESTERN ALFALFA, INC.
WILLAMETTE INDUSTRIES, INC.

PENNSYLVANIA

BETHLEHEM STEEL CORPORATION
BRADFORD COAL COMPANY
INTERNATIONAL SALT CO.
PART IV ASSOCIATES
PENNZOIL PRODUCTS CO.
MOBAY CHEMICAL CORPORATION
MOLLY PITCHER SERVICES
PITTSBURGH-DES MOINES CORPORATION
ROHM & HAAS COMPANY
SCOTT PAPER COMPANY
ZURN INDUSTRIES

SOUTH CAROLINA

PROFESSIONAL MEDICAL PRODUCTS

SOUTH DAKOTA

SPRENGER MIDWEST, INC.

TENNESSEE

BUCKMAN LABS
DUNAVANT ENTERPRISES, INC.
FERRO CORPORATION
NISSAN MANUFACTURING CORP., USA
TBC CORPORATION
TOSHIBA AMERICA, INC.

TEXAS

BROWN ALCANTAR & BROWN CUSTOM BROKER
CENTEX CORPORATION
CHEMICAL ENTERPRISES, INC.
CULLUM COMPANIES, INC.
DOME PETROLEUM, LTD.
FRIONA INDUSTRIES
GROCERS SUPPLY
RUDOLPH MILES & SONS CUSTOM BROKER
MOUNTAIN STATES ENERGY CORP.
PROLER INTERNATIONAL CORP.
REDLAND WORTH CORPORATION
W. SILVER, INC.
SOUTHERN HARDWOODS CO.
SOUTHWESTERN PORTLAND CEMENT CO.

UTAH

A&K RAILROAD MATERIALS
AMALGAMATED SUGAR COMPANY
DIEHL LUMBER PRODUCTS, INC.
EVANS GRAIN & ELEVATOR
GOURMET BRANDS, DIV. OF UI GRPS.,INC
GREAT SALT LAKE MINERALS & CHEM. CO.
INTERSTATE BRICK
KENNECOTT
MOUNTAIN AMERICA SHIPPERS
MURRAY ELEVATORS
PETROLANE, INC.
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