



# **Railroads and Capacity Problem: Public/Private Approaches**

STB Commissioner Francis P. Mulvey

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# The Railroads and the Surface Transportation Board

Created by ICC Termination Act of 1995

Born out of the Deregulation Movement

Residual Economic Regulation of the Railroads

Far Smaller Staff and Scope of Authority



# STB Mission

Exclusive authority to approve of rail mergers

Review rail rates and practices to ensure they are reasonable and not discriminatory

Approval, including environmental review, of

(i) construction of any new rail line or

(ii) abandonment of existing lines

Motor carrier collective ratemaking activities

Rates for non-contiguous domestic water trade

Rates for pipelines not carrying energy products



# STB Responsibilities over Rates and Service

Oversee and Monitor Railroad Practices Nationally

Enforce the Railroads' Common Carrier Obligation

Ensure that Rates Charged Captive Shippers are Reasonable

Assist Railroads in Earning Adequate Revenues

Calculate the Railroads' Cost of Capital



# Rate Case Resolution-Large Shipments

Determination of Market Dominance

Stand Alone Cost Test—*Fact-based approach rooted in economic reasoning and approved by the courts*

No Substitute for Preparing a Strong Case with Solid Evidence

Strive for a Balance between Railroad's Need to Earn Adequate Returns and Shipper's Need for Fair and Reasonable Rates



# Alternative Approaches

SAC approach has been criticized as artificial  
and overly complex

SAC approach is very costly and time consuming

Only feasible for large shippers

Is it time to look for alternative approaches?

- Recent Board decisions suggest openness to proposed rulemaking on SAC changes
- April 26<sup>th</sup> hearing on the SAC process



# The Genesis of the RR Capacity Problem

Improved Earnings Still not Revenue Adequate  
Railroads “Punished” by Wall Street for Making  
Capital Investments

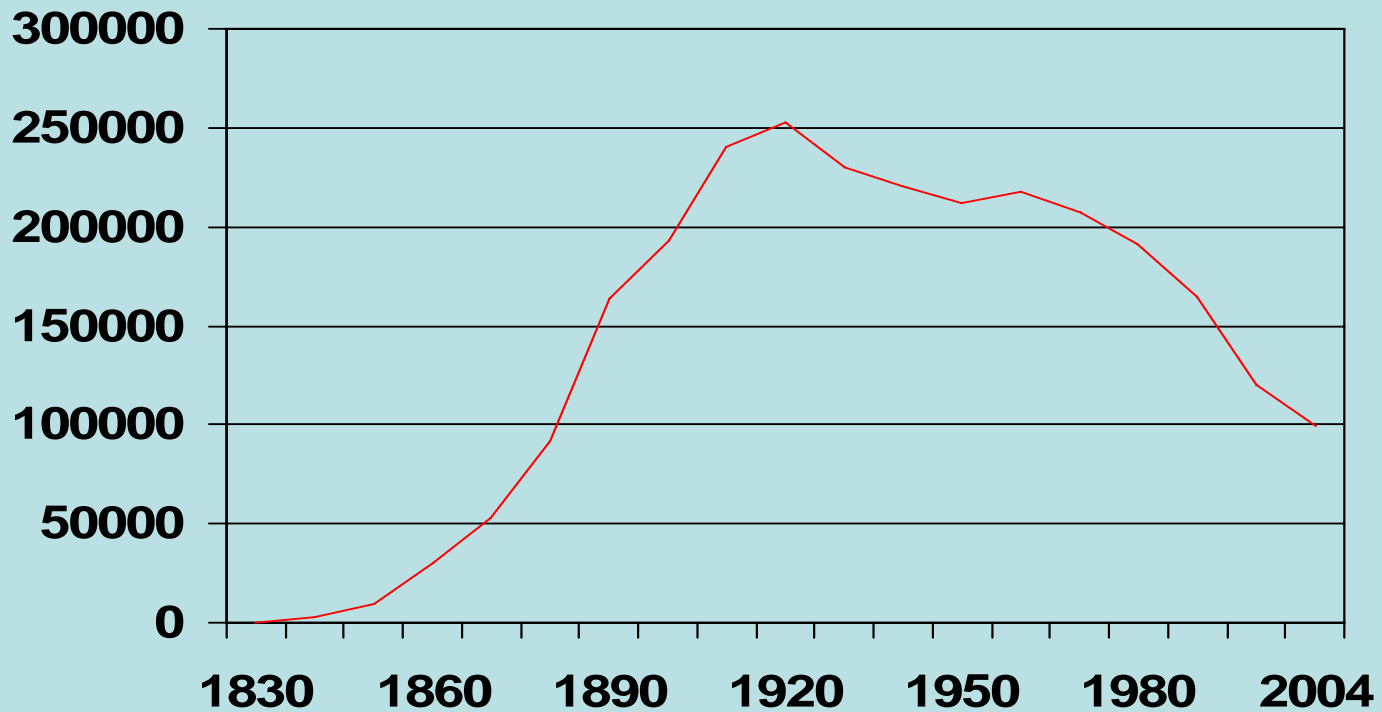
Railroads Often Found that Infrastructure Investments  
Failed to Generate Sufficient Income

Long term Strategy to Reduce Size of Workforce

Added Rail Infrastructure is Long-Lived While Demand  
Increases can be Short-Lived



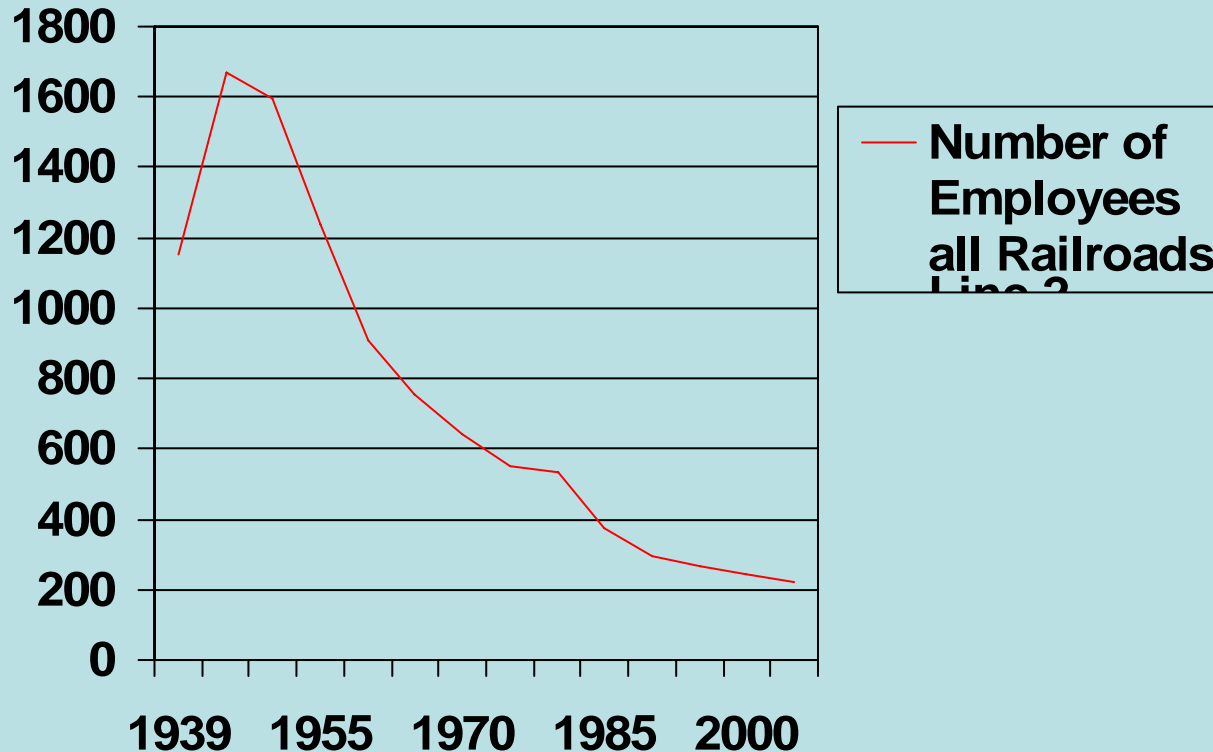
# Growth and Decline of Railroad Mileage





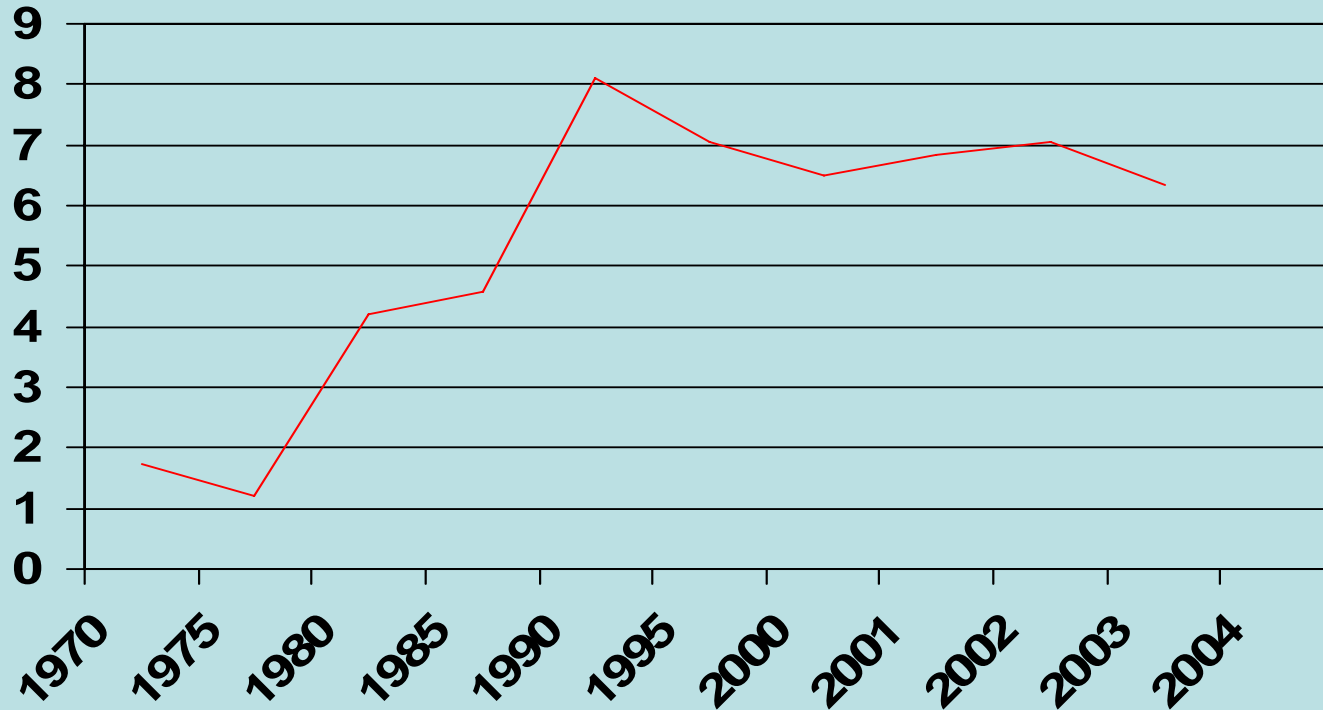


# Railroad Employment 1939-2003 (in thousands)





# Railroad ROI 1970-2003





# Railroad Cost of Capital and ROI

Sources: Annual R-1 Reports and AAR

	Cost Of Capital	BNSF	CSXT	NS	UP	KCS	SOO	GT	IC
1996	11.9%	8.6%	8.9%	13.0%	9.3%	7.2%	23.5%	0.0%	15.2%
1997	11.8%	8.4%	9.8%	13.1%	5.2%	3.6%	12.3%	5.2%	15.8%
1998	10.7%	9.7%	8.1%	10.5%	2.9%	9.1%	4.9%	3.0%	13.6%
1999	10.8%	9.5%	3.8%	5.2%	6.8%	6.4%	2.5%	25.4%	10.0%
2000	11.0%	8.8%	3.6%	5.5%	6.9%	6.3%	5.6%	5.9%	5.9%
2001	10.2%	7.1%	4.6%	8.3%	7.6%	7.0%	5.9%	4.9%	4.9%
2002	9.8%	6.4%	5.2%	9.1%	8.6%	6.5%	5.7%	3.1%	3.1%
2003	9.4%	6.2%	4.0%	9.1%	7.3%	3.7%	.01%	4.5%	4.5%
2004	10.2%	5.8%	4.4%	11.6%	4.5%	8.3%	3.3%	6.0%	16.0%



# The Developing Rail Capacity Crisis

Shrinking Workforce and Infrastructure Partly  
Offset by Productivity Improvements

But Continuous Increase in Traffic Begins to  
Absorb “Excess Capacity”

Network becomes More Vulnerable to  
Stochastic Events

A Perfect Storm or the Rail Version of Global  
Warming



# 2003-2004 Capacity Problems

Expanding Economy Led to Surge in Imports

Large Grain Harvests in 2003 and 2004

Growth in Export Coal Market

Crew Shortages due to Wave of Retirements

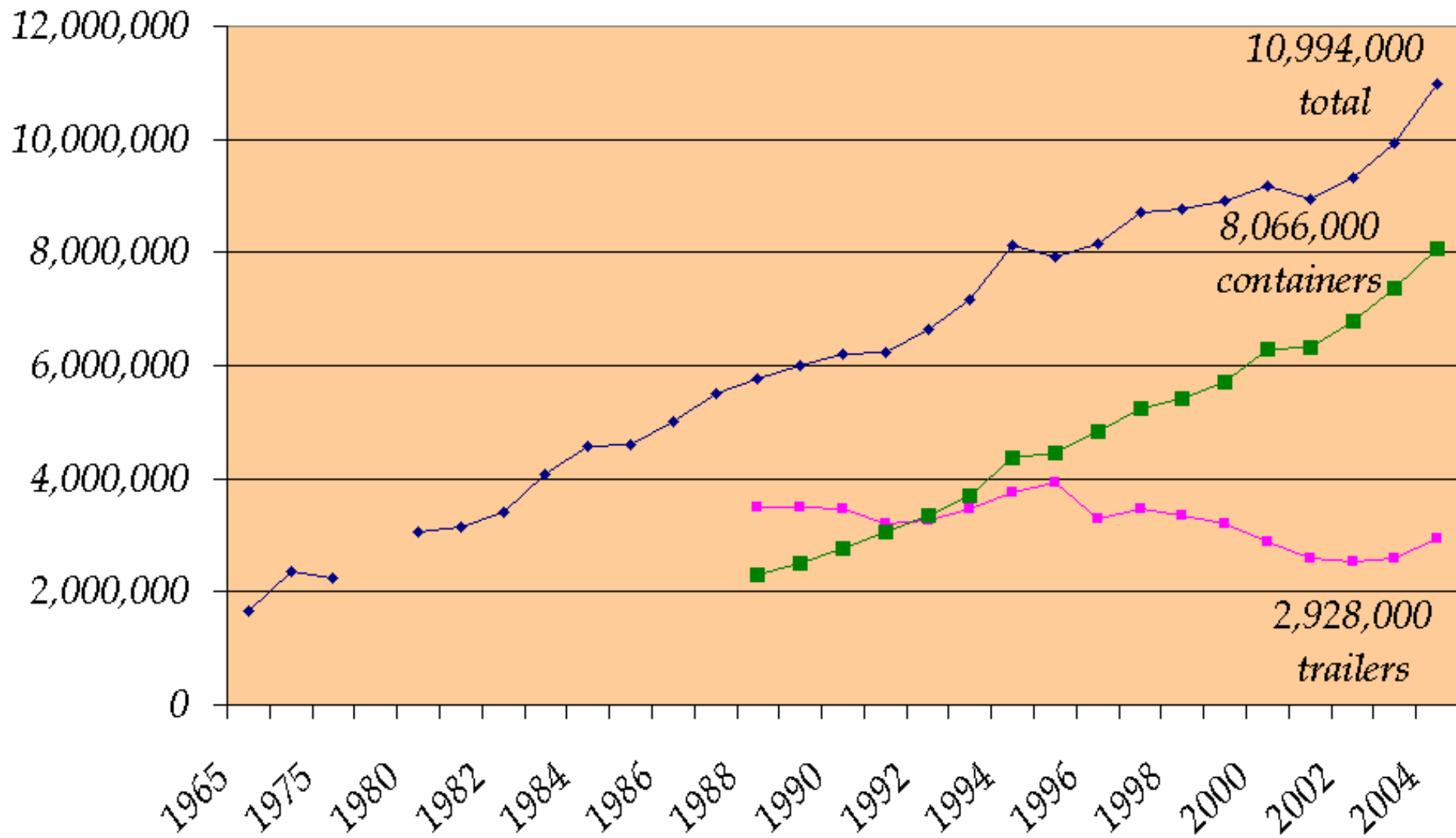
Equipment Shortages due to Reduced Purchases

Cutbacks in Capital Spending Programs

Tight Capacity in Trucking Industry due to Driver

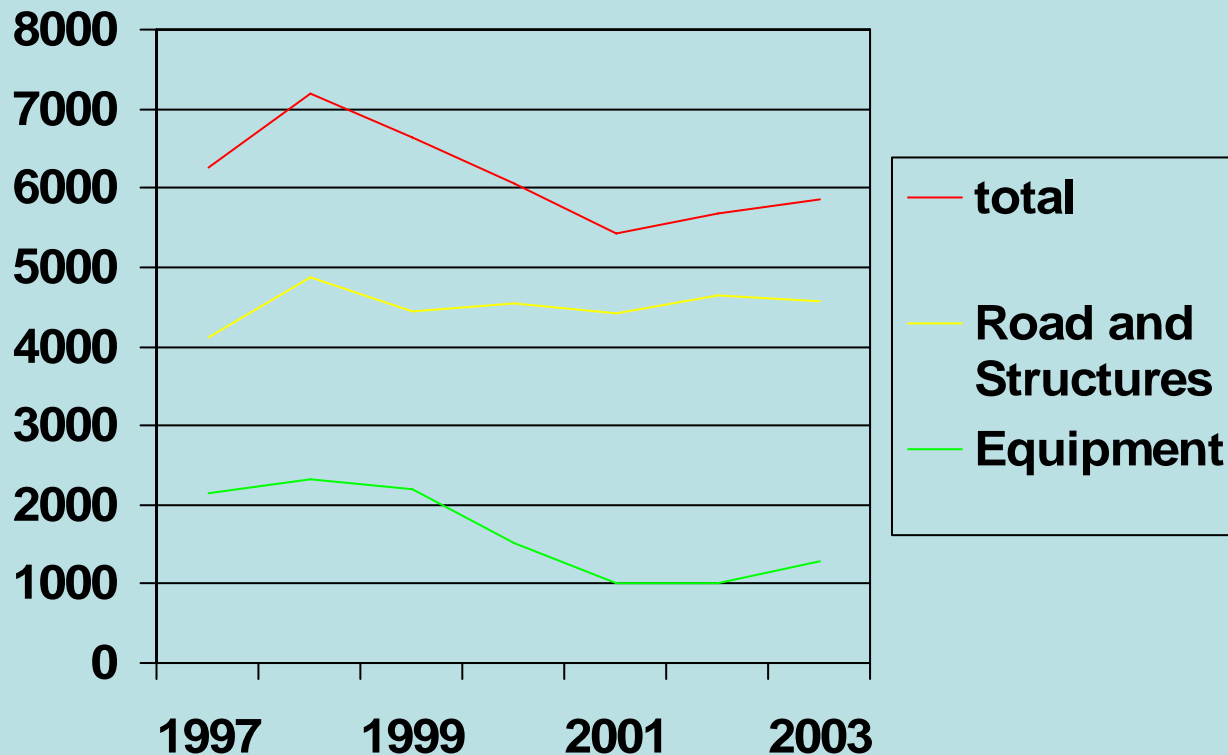
Shortages, Higher Fuel Costs, HOS Rules, etc.

## Intermodal Shipments beginning 1965





# Class I Capital Expenditures (in billions of current \$)



# Demand and Capacity for the Near Term

Intermodal Expected to Increase this Year But Rate of Growth is Slowing

Grain Carloadings to Date are Unchanged from Last Year, but Demand Could Rise if Barge Option “Dries Up”

Coal Traffic Remains Strong, but PRB Derailments and Maintenance Issues will Limit Performance

Railroad Operating Metrics Are Improving, Though Problems Remain





# Carrier Responses to Recent Capacity Problem

More Cars and Locomotives Bought and Leased

Accelerated Hiring and Training of Train Crews

Some Infrastructure Expansion Efforts

Price Rationing of Available Capacity

Railroads Choosing who they will Serve and the  
Common Carrier Obligation



# Long-Term Rail Capacity Constraint Factors

Demand for Freight Rail Transport Projected  
to Grow by 60%-70% over Next Two Decades

Railroads' Inability to Earn Cost of Capital

Pressure from Wall Street to Reduce Capital Costs  
and Improve ROI

Long-Term Contracts Limit Railroad  
Pricing Flexibility

Railroads tend to Bid Long Term Contract  
Rates Down to Long Run Marginal Costs



# What is The Role of the Public Sector?

Railroads Support Limited Role—Public/Private Partnerships (Alameda Corridor, CREATE)

Railroad Trust Fund Concept

Investment Tax Credits

- Short Lines and the 286K lb. Car Problem
- Class I Access and Limited Fiscal Capacity
- RIM and RIFF



# Railroad Regulation and Capacity

STB's Role has Centered on Rate Reasonableness  
for Regulated Traffic

Most Commodities are Exempt from  
Regulation and/or Modally Competitive

Interstate Commerce Laws and Doctrine  
Address Reasonableness of Rates and Service

Shippers want "Fairness"

What Can and Should the Board Do?



# STB's Service Initiatives

Board carefully monitors rail trends and performance metrics

Urge open communication between railroads and shippers in 2004 held carrier/shipper fora in San Francisco, Atlanta, Kansas City and Houston and will help sponsor with AAR a railroad/shipper meeting in St. Louis in mid-September

Asked railroads in 2004 to submit their fall peak plans and on June 15<sup>th</sup> asked for this year's plans

Worked with railroads and shippers on service issues



# STB – 2005 Priorities

Handle first small shipment rate case(s)

Reassess SAC Approach for Large Shipment Cases

Improved Customer Service from Carriers

Examination of Capacity Constraints

Amtrak Directed Service Mandate



# Rail Consumer Assistance Program

Facilitates informal solutions to disputes with RR's

Brings issues to RR's attention rapidly

Solves Problems without Litigation

Promotes Rail Service Improvements

120 Rail Consumer complaints handled in 2004

Over 420 handled since program began in 2000



# Is It Time to Review Rail Regulatory Policy?

Focus on 25<sup>th</sup> Anniversary of Staggers  
Act and 10<sup>th</sup> Anniversary of the  
creation of the STB

Proposed TRB study of railroads and  
regulation in the 21<sup>st</sup> Century



# Thank You, Any Questions?

