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Before the U.S. Surface Transportation Board

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STB Docket No. EP 768

Petition for Rulemaking to Adopt Rules Governing Private Railcar Use by Railroads

Comments of the
U.S. Department of Agriculture

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Authority and Interest

The Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 entrust the Secretary of Agriculture with representing the interests of agricultural producers and shippers in improving transportation services and facilities. As one of many ways to accomplish this mission, the U.S. Department of Agriculture (USDA) initiates and participates in Surface Transportation Board (STB or Board) proceedings involving rates, charges, tariffs, practices, and services.

Introduction

The U.S. Department of Agriculture (USDA) appreciates the Board opening this proceeding to consider rules to enhance the efficiency of the rail industry's use of private cars. This proceeding is one of several aimed at mitigating railroad underperformance. Whereas some aspects of underperformance are more directly related to recent events, USDA believes inefficient car use is a long-standing phenomenon not sufficiently addressed by existing STB guidelines. USDA also believes the Board has tools at its disposal to strengthen the railroads' incentives to provide better service, including the penalties for poor service that are requested in the petition. In these comments, USDA hopes to address some essential aspects of the petition on which the Board has requested comments.

Summary

USDA's main points, discussed in detail in these comments, include the following:

- Consistent shipper concerns regarding rail service over the past few years—coupled with ongoing, severe rail service disruptions—demonstrate the need for enhanced incentives for railroads to provide quality service.
- For this petition, the Board should act on its authority to incentivize better rail service and better management of shipper-owned cars in the railroads' control.
- Petitioners have proposed a workable solution to the gap in railroads' incentives to efficiently handle privately owned cars, and the Board should move forward with a Notice of Proposed Rulemaking.

Discussion

Intervention is Needed to Enhance Incentives Around Service Quality

As amply shown at the Board's April hearing on urgent issues in freight rail service, below-par rail performance has negatively affected the bottom line for numerous agribusinesses and farmers. Since the hearing, the number of unfilled grain car orders has continued to increase, and train speeds for grain have not improved. The fact that agricultural shippers are still turning to rail despite the progressively poor service shows their dependence on railroads and the lack of any cost-effective alternatives.

Given the recent history of deteriorating rail service, USDA believes the Board must enhance the railroads' incentives to provide better service. Union Pacific Railroad (UP) contends nothing is needed because shippers can contract with the railroads to obtain service commitments.¹ In theory, contracts could offer service commitments similar to what the petitioners have proposed,

¹ Union Pacific, August 30, 2021. Reply to Petitioners in Ex Parte (EP) 768.

along with penalties and rewards based on performance. However, in practice, contracts are not an option for many shippers. According to the Board’s confidential Carload Waybill Sample data, over the past two decades, only 20 to 30 percent of grain tonnage was shipped by contract. One reason for that low number is that the grain industry is too variable in its volumes and origin-destination pairings to get locked into long-term contracts. Additionally, it is not clear how *willing* railroads are to offer service commitments in their contracts. USDA has heard from shippers, for example, that the changes to service that came with Precision Scheduled Railroading were simply offered on a “take it or leave it” basis.

Another problem with UP’s suggestion that shippers pursue relief through contracts is that shippers have no way to challenge the rates and service conditions in those contracts. Just because a shipper contracts with a railroad does not mean the contract was formed fairly—the railroad may still have market power. Even if the contract is marginally better than the shipper’s next best alternative—which may be very costly—the shipper will select the contract. Given the limited recourse available in contracts, railroads should offer a schedule of various prices and service qualities in their public tariffs. That way, shippers could choose the price-service combination they need. Notably, though, this hypothetical improvement by the railroads would not necessarily avoid the Board’s need to enhance the incentives for high-quality service. Even with such a schedule of offered prices and qualities, several economic models predict regulation is needed to prevent monopolies and oligopolies from providing inefficiently low levels of service.² For these reasons, USDA believes some kind of additional reward or penalty is needed to better incentivize the railroads.

The Board has the Authority to Act and the Petition Falls Under that Authority

The railroads question whether the proposed penalties on inefficient private car use fall under 49 U.S.C. § 11122(a). “Car service” is defined under 49 U.S.C. § 10102 as “the *use*, control, supply, movement, distribution, exchange, interchange, and return of locomotives, cars, other vehicles, and special types of equipment *used in the transportation of property by a rail carrier*” (emphasis added). Further, 49 U.S.C. § 11122(a) says, “the regulations of the Board on car service shall encourage the purchase, acquisition, and *efficient use* of freight cars” and that “the regulations may include the compensation to be paid for the use of a locomotive, freight car, or other vehicle.” USDA understands the petition to fall under the third aspect of 49 U.S.C. § 11122(a), where the Board can encourage the efficient use of freight cars through compensation paid for the cars.

The Association of American Railroads (AAR) argues that the petition falls under transportation services because the delays would apply while the cars were “in transit” and simply because private railcars, by definition, are used for freight transportation.³ However, because railcars are not typically used for anything other than rail transportation, AAR’s argument ignores the third aspect of 49 U.S.C. § 11122(a)—“the Board shall encourage...the efficient use of cars.” That fits with AAR’s later take that “the Board has authority to establish regulations for the purpose of ensuring that there is an adequate supply of railcars to meet shipper demand for transportation.”⁴ AAR’s argument focuses too narrowly on car supply and ignores efficient use. AAR concludes by accusing shippers of merely seeking windfall revenue with this petition. However, the petition

² Sappington, D. 2005. “Regulating Service Quality: A Survey.” *Journal of Regulatory Economics*; 27(2):123-154.

³ AAR, August 30, 2021. Reply to Petitioners in EP 768.

⁴ *Ibid.*

is based on applying the railroads’ own demurrage charges to delays in railcar use—the exact same practice the railroads have always said was necessary to provide efficient rail transportation. The petition is clearly about efficiency and not about transferring revenues from railroads to shippers.

According to the railroads, the petition is about regulating the way railroads provide transportation. However, at the heart of the proposal, USDA believes, is the need for owners of privately owned cars to be properly compensated for the costs of using their cars. That compensation, in turn, will incentivize railroads to use the cars efficiently. In almost any other business, if someone wants to rent a machine or use another company’s assets, they have to pay a rate commensurate with the time (opportunity) cost of their use of the asset. Even in railroading, if shippers take too much time loading or unloading the railroad’s cars, the railroad will charge them fees that presumably reflect the time cost of those assets. Every minute a car is put to one use is a minute lost for some other use of that car. That principle is true for both shippers unloading railroad-owned cars and railroads moving shipper-owned cars.

Figure 1: The Gap in Fees to Incentivize Efficient Car Use.

| | | Owner | |
|------|----------|--|--|
| | | Shipper | Railroad |
| User | Shipper | No additional fees needed. Shippers inherently account for delay costs using shipper-owned cars. | Fees already exist in the form of demurrage, so that shippers fully account for delay costs in moving railroad-owned cars. |
| | Railroad | Fees needed to ensure railroads fully account for delay costs in moving shipper-owned cars. | No additional fees needed. Railroads inherently account for delay costs using railroad-owned cars. |

Visualizing a two-by-two matrix is helpful to consider the various ways cars can be used and owned and the need for demurrage. Shown in figure 1, railroads can use railroad-owned cars or shipper-owned cars, as can shippers. The Board has recognized that demurrage fees are not appropriate to charge when shippers are handling shipper-owned cars on shipper-owned property.⁵ Similarly, it would not make sense to charge the railroad demurrage-like fees for using railroad-owned cars on railroad-owned property. As the railroads argued during the May 2019 oversight hearing on demurrage and accessorial charges, it makes sense to charge shippers demurrage fees when they are inefficiently using railroad-owned cars. Shippers’ choices about how to use the railroad-owned cars have impacts on railroad costs, and the demurrage fees ensure the shipper incorporates those costs into their decision making. The current petition simply seeks parity, in asking to charge railroads demurrage for inefficient use of shipper-owned

⁵ STB Decision, EP 707: Demurrage Liability, April 11, 2014, pp. 15-16.

cars. For better efficiency, the railroads should have to incorporate the costs shippers incur when their cars are delayed.

Figure 1 also helps answer the Board's question about how the incentives to use railroad-owned cars would be affected. In cases where shippers or railroads use their own cars, demurrage is unnecessary. Where the shippers or railroads own the assets, their opportunity costs are already accounted for and internalized in using the asset. If the railroad spends too long using its own cars, that same railroad bears the burden of reduced revenue. Because railroads already bear the full cost of inefficient railroad-owned car use, their relative cost of delaying railroad-owned versus privately-owned car shipments is currently inefficiently biased towards delaying privately-owned cars. Putting demurrage-like fees on the railroad's use of privately-owned cars would change the relative cost of delaying railroad versus privately-owned cars. Yet the change would correct an existing imbalance (and inefficiency).

Notably, reciprocal demurrage would not only better incentivize railroads to use shipper-owned cars efficiently, such a practice would also facilitate any necessary right-sizing of car supply.

Final Remarks and Conclusion

The Board has raised important questions around the Petition's specific proposal to charge railroads demurrage (or a storage fee) for cars whose location city has not changed in 72 hours. USDA believes this policy could, at least in principle, have some incentive-distorting effects: railroads might try to move cars needlessly to avoid any charges. However, it is unclear to USDA how likely those effects would be to arise in practice. USDA also believes the details of the proposal—such as the choice of 72 hours—may be somewhat arbitrary. That said, USDA believes the petition is a step in the right direction and that the Board should move forward with a notice of proposed rulemaking.

Respectfully submitted,



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