September 25, 2007

FREIGHT RAILROADS

Updated Information on Rates and Competition Issues

GAO
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Highlights

Highlights of GAO-07-1245T, a report to House Committee on Transportation and Infrastructure

Why GAO Did This Study

The Staggers Rail Act of 1980 largely deregulated the freight railroad industry, giving the railroads freedom to price their services according to market conditions and encouraging greater reliance on competition to set rates. The act recognized the need for railroads to recover costs by setting higher rates for shippers with fewer transportation alternatives. The act also recognized that some shippers might not have access to competitive alternatives and might be subject to unreasonably high rates. It established a threshold for rate relief and granted the Interstate Commerce Commission and the Surface Transportation Board (STB) the authority to develop a rate relief process for those "captive" shippers. GAO's reported on rates, competition, and other industry trends in reports issued in October 2006 and August 2007. This statement is based on those reports and discusses (1) the changes that have occurred in the railroad industry since the enactment of the Staggers Rail Act, including changes in rail rates since 1985, (2) the extent of captivity in the industry and STB's efforts to protect captive shippers, and (3) STB's actions to address GAO's recent recommendations.

What GAO Recommends

In October 2006, GAO recommended that STB analyze the state of competition and consider appropriate actions. GAO also recommended that STB review their method of data collection to ensure that all freight railroads are consistently reporting all revenues collected from shippers.

To view the full product, including the scope and methodology, click on GAO-07-1245T. For more information, contact JayEtta Z. Hecker at (202) 512-2834 or heckerj@gao.gov.

What GAO Found

The changes that have occurred in the railroad industry since the enactment of the Staggers Rail Act are widely viewed as positive, since the financial health of the industry has improved and most rates have declined since 1985. The freight railroad industry's financial health improved substantially as railroads cut costs through productivity improvements and new technologies. However, rates began to increase in 2001, and in 2005 rates jumped nearly 9 percent—the largest annual increase in twenty years—and rates increased for all 13 commodities that we reviewed. Revenues that railroads report as "miscellaneous revenue"—a category that includes some fuel surcharges—increased more than ten-fold from $141 million in 2000 to over $1.7 billion in 2005.

It is difficult to precisely determine how many shippers are "captive" because available proxy measures can overstate or understate captivity. However some data indicate that potentially captive traffic appears to have decreased, while at the same time, data also indicates that traffic traveling at rates significantly above the threshold for rate relief has increased. In October 2006, we reported that STB's rate relief process to protect captive shippers have resulted in little effective relief for those shippers. We also reported that economists and shipper groups have proposed a number of alternatives to address remaining concerns about competition—however, each of these alternative approaches have costs and benefits and should be carefully considered.

STB has taken some actions to address our past recommendations, but it is too soon to determine the effect of these actions. Our October 2006 report noted that the continued existence of pockets of potentially "captive shippers" raised questions as to whether rail rates in selected markets reflected reasonable pricing practices, or an abuse of market power. We recommended that the Board undertake a rigorous analysis of competitive markets to identify the state of competition. STB has awarded a contract to conduct this study; while this is an important step, it will be important that these analysts have STB's authority and access to information to determine whether rail rates in selected markets reflect reasonable pricing practices. We also recommended that STB ensure that freight railroads are consistently reporting all revenues, including miscellaneous revenues. While STB has revised its rules on fuel surcharges, these rules did not address how fuel surcharges are reported and STB has not yet taken steps to accurately collect data on other miscellaneous revenues. STB has also taken a number of steps to revise its rate relief process. While these appear to be promising steps, it is too soon to tell what effect these changes will have and we have not evaluated them.