Surface Transportation Board
Office of the General Counsel

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Written Statement of the Surface Transportation Board Before the Antitrust Modernization Commission

Madam Chair, Commissioners, I am Raymond Atkins with the General Counsel's Office of the Surface Transportation Board (the STB or the Board). On behalf of the Board, I welcome the opportunity to participate in today's discussion on the role of antitrust enforcement in regulated industries.

I would like to preface my remarks by explaining that I am not here to debate antitrust policy or lobby for a particular recommendation by this Commission. The Board, like this Commission, is a creation of Congress and will carry out, to the best of its ability, the assignments Congress gives to it. What I hope to do today is to assist the Commission in this hearing, by first explaining what the Board is and which specific antitrust responsibilities Congress has assigned to it, and by then discussing why Congress has given the Board those assignments and how the Board carries them out.

The Surface Transportation Board

The Surface Transportation Board is the successor to the Interstate Commerce Commission (ICC), which was created in 1887 to protect shippers from the monopoly power of the railroad industry. Between 1840 and 1880, the U.S. railroad network had grown from 2,800 to 93,000 miles. This boom brought indiscriminate construction, market manipulation, rate abuses, and discriminatory practices against certain types of freight customers and passengers. In some areas, rail monopolies were able to direct the fate of communities, shippers, and entire industries. Farmers and consumers demanded rate controls, and merchants and other shippers demanded equal treatment vis-à-vis their competitors. Congress responded by enacting the original Interstate Commerce Act, which required all rail rates be "reasonable and just," prohibited certain railroad practices (such as rate discrimination, price fixing, and rebating), and created the ICC, the first independent regulatory agency.

In various subsequent Acts through 1920, Congress broadened and strengthened the ICC's regulatory authority over railroads. It also expanded the ICC's regulatory reach to other modes, starting with pipeline transportation in 1906. In 1914, the Clayton Act was passed and the ICC was given the responsibility for enforcing that Act's provisions where common carriers subject to the ICC's jurisdiction were involved. Congress brought the nascent trucking and intercity bus industries under the ICC's authority in 1935. And in 1940, inland and coastal water carriers were added to the ICC's jurisdiction.

Because of changing marketplaces, intermodal competition, and the ailing health of the rail industry, Congress subsequently pared down and modernized the ICC's regulatory functions over each of these modes, in an incremental process that started in the mid-1970s and continued into the mid-1990s.[1] This process culminated in the ICC

[1] Significant steps in this process were taken in the Railroad Revitalization and Regulatory Reform Act of 1976, the Department of Energy Organization Act of 1977, the Staggers Rail Act of 1980, the Motor Carrier Act of 1980, the Household Goods Transportation Act of 1980, the Bus Regulatory Reform Act of 1982, the Surface Freight

Termination Act of 1995 (ICCTA), which involved a wholesale review of economic regulation across all of these transportation modes. In ICCTA, Congress eliminated those regulatory functions that were found to be outdated, and it further modernized many of the regulatory functions that were retained. The Surface Transportation Board was created to carry out those ICC functions that Congress concluded should be handled by an independent regulatory agency, free from partisan direction. Other ICC functions were transferred to the Department of Transportation, which has had primary responsibility for safety oversight since its creation in 1967.

As a result of ICCTA and the legislation leading up to it, the business environment for the various surface transportation industries has been transformed from one of near pervasive regulation to one in which regulation is selective and more narrowly focused. Board regulation is limited to those situations where shippers, carriers, and the public may need protection --- whether by enforcing the common carrier obligation, restraining abuses of monopoly power, authorizing cooperative arrangements between carriers that are not anticompetitive, or providing a specialized forum with the expertise needed for adjudication of service-related disputes between a carrier and shipper or between two or more carriers.

Express Antitrust Immunities

As you know, Congress has provided express antitrust immunity for certain actions authorized by the Board. These include:

Forwarder Deregulation Act of 1986, the Negotiated Rates Act of 1993, and the Trucking Industry Regulatory Reform Act of 1994.

- mergers, acquisitions or other forms of consolidations between railroads (49 U.S.C. §§ 11321-11328) or between intercity bus companies (49 U.S.C. § 14303);
- agreements between railroads to pool or divide traffic, services or earnings (49 U.S.C. § 11322) or such agreements between trucking or bus companies (49 U.S.C. § 14302);
- collective agreements between railroads (49 U.S.C. § 10706) or motor carriers (49 U.S.C. § 13703) that are related to rates or charges.

The focus of this hearing is on the non-rate immunities. I will discuss each of these in turn.

STB Rail Merger Review

Railroads have the characteristics of a natural monopoly, with significant barriers to entry into and exit from the industry, and with a customer base that includes a sizeable amount of traffic that has no feasible alternative means of transportation. Thus, Board approval is required for entry into or exit from a rail market,[2] and for railroad mergers or acquisitions (including other forms of consolidations or market divisions that would alter the competitive landscape).[3] Where the Board approves a railroad merger or acquisition, the statute expressly exempts that transaction "from the antitrust laws and from all other

[2] 49 U.S.C. §§ 10901-10903.

[3] 49 U.S.C. §§ 11323-11327.

law, including State and municipal law, as necessary” to allow that transaction to be carried out.[4]

The statutory criteria for Board approval of a merger or acquisition depend upon the size of the carriers involved.[5] Where two or more of the largest (Class I) railroads are involved,[6] the Board is to apply a broad public interest standard, taking into account not only any adverse effect on competition but also any effect on adequacy of transportation to the public, as well as the total fixed charges that would result, the impacts on affected employees and on other carriers in the area, and any other relevant factors. In contrast, where not more than one Class I railroad is involved, the Board is directed to approve the proposed merger or acquisition unless it finds that there would be substantial anticompetitive effects and that those anticompetitive effects would not be outweighed by the public interest in meeting significant transportation needs. Also, before the Board may approve any merger or acquisition, it must conduct an environmental review under the National Environmental Policy Act.

In 1995, Congress considered whether to repeal the antitrust exemption for rail mergers, as the Justice Department had advocated. Congress chose to retain the exemption, keeping rail merger review with the same agency that regulates the economic activity of the industry. However, Congress clarified and modified the contours of that

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[4] 49 U.S.C. § 11321.

[5] 49 U.S.C. § 11324.

[6] Class I railroads have revenues in excess of $250 million in 1991 dollars. There are currently seven Class I railroads operating in the United States: (1) BNSF Railway Co.; (2) CSX Transportation, Inc.; (3) Grand Trunk Corporation; (4) Kansas City Southern Railway Co.; (5) Norfolk Southern Railway Co.; (6) Soo Line Railroad Co.; and (7) Union Pacific Railroad Co. The Soo Line Railroad is owned by Canadian Pacific Railway. The Grand Trunk Corporation is owned by the Canadian National Railway.

review to encompass features associated with merger review under the antitrust laws: a broad, national outlook on the relevant markets to be examined; use of divestiture as a remedial condition; and the ability to discuss a proposal directly with interested parties.[7]

While the Congressional reports do not spell out Congress' reasons for retaining the antitrust exemption for rail mergers, I will briefly summarize the features of the ICC/STB specialized rail merger review process that were praised by those who advocated for retention of the antitrust exemption.

1. Open process. The Board provides for full public participation – including the opportunity for comments, evidence and counter-proposals – from all interested parties on an open record. The Justice Department can (and does) present its merger analysis to the Board, as do all other interested Federal government entities, such as the United States Departments of Agriculture, Energy, Transportation, and Defense, as well as state and local bodies. Significantly, all interested parties have an opportunity to comment on the analyses of other parties. And the Board's decision is subject to judicial review by a federal court of appeals if challenged by an interested party.

2. Integrated regulatory policy. Because the Board monitors and supervises the rail industry full-time, it understands the rail industry, its customers, and the competitive landscape that railroads face (including the role of other modes and global markets). The Board can take account of all of the impacts of a proposed merger, including the effect on the Board's other regulatory policies and goals. Assessing the potential impact of a

[7] H.R. Conf. Rep. No. 104-422, at 191 (1995).

merger on rail rates requires an understanding not only of the economics of the rail industry but the regulatory oversight and policies to which railroads are subject.

3. Broad range of issues. The Board does not limit its public interest analysis to competitive concerns. It also considers operational and service issues, labor concerns, safety issues, environmental impacts, and potential "downstream" impacts on the rail industry before determining whether to approve, disapprove, or impose conditions on a proposed merger.

4. Expansive remedial powers. In deciding whether to approve a merger with conditions, the Board does not limit itself to divestiture-type remedies. Rather, the Board uses its broad conditioning powers to fashion other appropriate means of preserving and enhancing competition (such as requiring that the merged carrier afford trackage rights to other carriers to serve traffic that would otherwise be adversely affected) and to mitigate other adverse impacts (such as safety or environmental impacts).

5. Continuing oversight. Because the statute expressly retains Board jurisdiction over any mergers that it approves,[8] the Board actively monitors the results of mergers and can impose post-merger conditions as needed to address competitive, operational and environmental issues. This makes it easier for the Board to choose remedies short of divestiture to remedy potential anticompetitive effects of the merger. In recent large rail mergers, the merging railroads have, as a condition of approval, been required to submit both quarterly and annual reports, for up to 5 years, to analyze the impact of the approved transaction.

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[8] 49 U.S.C. § 11327.

6. Nonpartisan approach. The Board is a bipartisan body with fixed, staggered terms for its three members and is independent from the Executive Branch.

7. Effective implementation. Mergers that are approved by the Board can be implemented more readily and smoothly as a result of both the rail labor conditions that are imposed and supervised by the Board,[9] and the express exemption from other laws that might be used to impede or delay implementation of an approved transaction.

In leaving rail merger review with the Board, Congress was aware that the ICC had almost always agreed with the Justice Department on whether a particular merger should be approved. In the Santa Fe/Southern Pacific merger in 1986, the ICC followed the Justice Department's recommendation and blocked the merger. In eight other major rail mergers, the ICC followed the Justice Department's recommendation and approved the merger. And in two "end-to-end" mergers (UP/CNW and CN/IC) approved by the ICC or STB, the Justice Department chose not to participate, having evidently concluded that those mergers raised no competitive concerns.

The Board's views have diverged modestly from those of the Justice Department in one recent case, and more dramatically in another, but the federal courts also do not always agree with Justice Department on the likely impact of a particular merger or the appropriate action to take. When the Board approved the acquisition of Conrail by CSX and Norfolk Southern and the division of Contrail's assets between the two carriers, there was general agreement that the transaction was largely pro-competitive, particularly given the creation of "shared assets" areas that resulted in new competition between

[9] 49 U.S.C. § 11326.

Norfolk Southern and CSX for over $700 million of rail traffic that had previously been exclusively served by Conrail.[10] There were only modest differences of opinion between the Board and the Justice Department on the number and type of conditions that should be attached to the Board's approval.

Only in the Union Pacific/Southern Pacific merger did the Board not follow the Justice Department's recommendation that merger authority either be denied or conditioned on expansive divestitures. The Board concluded that, on balance, the merger would be in the public interest, as it would permit the financially weak Southern Pacific to become part of large, financially healthy rail system that would sustain efficient operations and invest in the SP's deteriorating infrastructure.[11] The Board also concluded that a divestiture requirement would be problematic for ensuring adequate service levels for many of SP's customers, and that a trackage rights remedy, in combination with continuing Board oversight, would be sufficient to preserve competition for those shippers that had been served by both carriers and would otherwise no longer have a choice of carriers. Finally, the Board disagreed with the Justice Department about whether many of the significant efficiency benefits claimed by the applicants were likely to be achieved, or whether they could be achieved short of merger.

[10] *See CSX Corp. et al. – Control – Conrail, Inc., et al.*, 3 S.T.B. 196 (1998), *aff'd sub nom. Erie-Niagara Rail Steering Committee v. STB*, 247 F.3d 437 (2d Cir. 2001).

[11] *See Union Pacific/Southern Pacific Merger*, 1 S.T.B. 233 (1996), *aff'd sub nom. Western Coal Traffic League v. STB*, 169 F.3d 775 (D.C. Cir. 1999).

Subsequent studies by economists at GAO and the FTC have validated the Board's findings.[12]

In June 2001, the Board revised its merger guidelines for major rail transactions, which had become outdated.[13] The changes were prompted by the announcement in 1999 of a planned BNSF/CN merger proposal. That announcement raised concerns of a final round of proposed rail mergers that, if approved, would reduce the number of Class I railroads in North America to two or three. The Board was also concerned that recent large rail mergers had been accompanied by significant rail service disruptions as the merging companies struggled to integrate massive rail networks. Because the Board determined that the guidelines it had at the time were not adequate to address this changed environment, the Board imposed an 18-month moratorium on merger proposals between Class I railroads and used that time to promulgate new merger guidelines through a notice-and-comment rulemaking.

The new guidelines are designed to address the potential end-game situation and service problems with major rail mergers. They recognize that the potential reduction in

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[12] Denis A. Breen, *The Union Pacific/Southern Pacific Rail Merger: A Retrospective on Merger Benefits*, Bureau of Economics, Federal Trade Commission, Working Paper No. 269, at 1. (March 2004) ("Contrary to skepticism expressed about merger efficiency claims, both generally and with respect to this particular rail merger, a variety of available evidence suggests that a number of the claimed efficiencies were plausibly merger-specific and were actually realized post-merger."); John Agyei Karikari, Stephen M. Brown, and Mehrzad Nadji, *The Union Pacific/Southern Pacific Railroads Merger: Effect of Trackage Rights on Rates*, 22:3 J. Reg. Econ. 271 (2004) (authors are economists at GAO) (concluding that the trackage rights remedy for shippers in the Salt Lake City area was effective as "BNSF provided more effective competition to UP in the post-merger era than SP did in the pre-merger era").

[13] *Major Rail Consolidation Procedures,* STB Ex. Parte No. 582 (Sub-No. 1) (STB served June 11, 2001) (final rules).

geographic competition would be difficult to remedy and that service integration problems are likely, and they direct future merger applicants to present not only efficiencies that would be produced by a proposed merger but also competition-enhancing features sufficient to offset possible adverse competitive or service impacts. The new rules state that the Board does not favor consolidations that reduce the transportation alternatives available to shippers unless there are substantial and demonstrable public benefits to the transaction that cannot otherwise be achieved. The guidelines also direct merger applicants to address the potential down-stream ramifications of the proposed transaction. Parties are required to submit detailed service implementation plans for technology, customer service, and operations, which must include contingency plans for possible service disruptions.

The new requirements apply only to major mergers between Class I railroads (with the exception of Kansas City Southern, the smallest of the Class I carriers). No major rail merger has been proposed since the adoption of these new merger guidelines.

Pooling – Railroads

Railroads need Board approval to enter into arrangements for the pooling or division of traffic, service, or earnings, and Board approval carries with it an exemption from the antitrust laws.[14] The agency may approve a pooling agreement if it finds that the proposal: (1) would promote better service to the public or of economy of operation, and (2) would not unreasonably restrain competition. In making this determination, the Board considers whether any potential anticompetitive effects would be outweighed by

[14] 49 U.C.S §§ 11321, 11322.

the agreement's benefits. As with merger proceedings, the approval of these agreements is done on an open record, with participation by interested parties including federal and state antitrust authorities.

The most recent exercise of this authority was the Board's decision to extend for another 10 years the authority of ten large railroads to pool, through TTX, a fleet of specialized rail flatcars that are used in the transportation of containers, truck trailers, automobiles, lumber, extra-dimensional loads, and other commodities.[15] This authority had been first approved by the ICC in 1974, and renewed several times. Although the Justice Department had opposed the arrangement in 1989, the experience of the following decade had illustrated no significant harm to competition, and a broad array of benefits that could not be achieved through lesser means. The Justice Department did not participate in the most recent proceeding.

Motor Carrier Exemptions

In contrast to the rail industry, the motor carrier industry is inherently competitive, with no significant economic barriers to entry or exit. Thus, motor carriers – trucking companies and intercity bus companies – are not as heavily regulated as railroads. But they continue to be regulated to some extent, in view of their common carrier obligation and the importance of a smooth-functioning transportation system to interstate commerce. And Congress in ICCTA decided to retain specialized regulation of certain motor carrier activities, with antitrust exemption when those activities are

[15] *See TTX Co., et al. – Application For Approval of Pooling of Car Service With Response to Flatcars*, STB Docket No. 27590 (STB served Aug. 31, 2004).

approved, presumably because those activities generally would not be scrutinized under the antitrust laws given the modest revenue levels involved.

In contrast to rail regulation, the Board is not the only body charged with economic regulation of motor carriers. In ICCTA, Congress divided that responsibility between the Board and the Department of Transportation.[16] The Board has only those responsibilities that are adjudicatory in nature, which include the activities for which there is an express antitrust exemption.

As with the other Board proceedings that may give rise to an antitrust exemption, the Board has an open process in which all interested parties, including the Justice Department or the Federal Trade Commission, can participate. And the Board bases its decision on the formal record that is developed.

Pooling. Like railroads, motor carriers must obtain Board approval to enter into agreements to pool or divide their traffic, services, or earnings.[17] For bus carriers, the Board may approve such an arrangement if it would (1) promote better service to the public or economy of operation and (2) not unreasonably restrain competition. For trucking companies, the Board must summarily approve the proposed arrangement unless it involves a matter of major transportation importance and there is a substantial likelihood that it would unduly restrain competition. And where the proposal has major transportation importance, the Board must approve it to the extent it would meet the same criteria that are applied to bus carriers. Finally, for household goods movers, there is a statutory presumption that an arrangement is acceptable if it is similar to arrangements

[16] 49 U.S.C. § 13301(a).

[17] 49 U.S.C. § 14302.

that were approved prior to 1980.

Household goods movers, who operate through a network of agent carriers, consider pooling arrangements important to their operations. And smaller, more localized trucking companies serving other types of traffic also consider it necessary to be able to combine forces through pooling arrangements to compete with larger, nationwide carriers. Thus, the agency has received and approved a modest number of pooling applications. For the most part, these arrangements have been uncontroversial and have attracted little interest from the Justice Department or the Federal Trade Commission.

Bus Mergers. Board approval is required for a merger or acquisition involving intercity bus companies that have combined annual operating revenues above $2 million.[18] To approve a proposed bus merger or acquisition, the Board must find that the consolidation would be consistent with the public interest, and it must take into consideration such factors as the effect on the adequacy of transportation to the public, the resulting fixed charges, and the impact on the carriers' employees. And, as with rail mergers, the Board retains continued oversight over bus company consolidations that it has approved, and may issue appropriate supplemental orders where necessary.

The Board has received and approved numerous proposals for a small, more localized bus company to be acquired by a larger bus holding company. These proposals have not been controversial.

[18] 49 U.S.C. § 14303.