



## GAO Report Freight Rail Pricing and Shipping Contracts

### FRCA Position

FRCA believes that the Government Accountability Office (GAO) report, *Freight Rail Pricing: Contracts Provide Shippers and Railroads Flexibility, but High Rates Concern Some Shippers*, provides valuable insights into pricing relationships between freight railroads and their customers, particularly on rail-dependent or captive shippers who often are hit with higher rates.

FRCA encourages Members of Congress and their staff, officials in the Trump Administration, and all stakeholders to review this GAO report and consider the observations raised when developing and implementing freight rail shipping policies – especially as policies affect shippers and those who are held captive or rail-dependent.

### Issue Background

The GAO conducted this study on freight rail shipping contracts as required by the *Surface Transportation Board Reauthorization Act of 2015* (P.L. 114-110) which was signed into law on December 18, 2015.

The report, publicly released December 7, 2016, presents information on similarities and differences in shipper freight rates under a tariff versus a contract, and the potential benefits of using each. This report can be accessed via <http://www.gao.gov/products/GAO-17-166>

GAO interviewed representatives of the four major Class 1 railroads, the Association of American Railroads and representatives of nine shipper groups, including FRCA.

In addition, the report describes the STB's process under which shippers that transport their freight by tariff could potentially challenge the reasonableness of a rail rate and seek financial release from the railroads.

Of particular interest to rail-dependent or captive shippers is the GAO discussion of differential pricing, a pricing strategy where railroads charge shippers with few or no other options more than shippers with more options for their freight. All railroads and the AAR (Association of American Railroads) told GAO that that railroads use differential pricing to charge the higher rates to shippers are willing to pay so railroads can cover infrastructure costs.

GAO found that the STB reviewed 50 rate reasonableness cases resolved between 1996 and 2016. Twenty-six of the cases were settled without an STB decision, while those that were decided by STB were split evenly: 11 in favor of the shippers and 10 in favor of the railroads. Shippers also told GAO that the STB rate-relief process can be complicated, time consuming and expensive, in part, due to the challenges in determining reasonable and unreasonable rates.

The GAO also found that contracts provide certain advantages, and their use by certain shippers has increased. However, the GAO found some disadvantages with contracts: 1) the contracts have become more standardized in recent years, resulting in some contract features being more difficult to negotiate; 2) shippers and one railroad representative said that contract lengths have decreased over the past decade, with longer contracts becoming less common; and 3) shippers told GAO that railroads may be shifting certain costs to shippers.



Another downside to contract rates is that they cannot be challenged before the STB if all or a portion of the rail segment is captive.

While GAO found that contract and tariff rates are based on similar market factors, railroads told Federal auditors that they look at the extent of competition when determining contract rates. However, shippers told GAO that tariff rates may not always reflect current commodity market conditions.

Further, shippers with fewer shipper options said they have high rates for some contract routes and limited recourse for rate relief for tariffs. “Despite the volume discounts and other advantages with multiple origin-destination routes, some shippers said that contracts effectively constrain them into paying higher rates on some routes,” GAO found.

Although shippers have the option of challenging a tariff rate before the STB, they do not have this option for challenging rates they view as unfair if agreed to in a contract, since the STB does not have authority to review contract rates.

### **Status**

This GAO report, along with a 2015 report by National Academy of Science’s Transportation Research Board titled, *Modernizing Freight Rail Regulation*, provides an important context to the important rulemakings pending before the STB, notably on revenue adequacy and expediting rate cases. This report can be accessed via <http://www.trb.org/Main/Blurbs/172736.aspx>

Please refer to the FRCA position papers, *Rate-Reasonableness Standards* and *Revenue Adequacy*, for more information.