

Rail Reciprocal-Switching Mandates

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tl;dr

Background: Since taking office, the Biden administration has moved aggressively to use enforcement actions and rulemakings—many of them outlined in the administration’s [July 2021 executive order](#)—ostensibly as a means to promote market competition. Among the targets of this approach has been the freight-rail sector. The administration advocates for mandated reciprocal switching, a form of compelled network interoperability, on grounds that it would improve the rail industry’s competitive environment.

The Biden EO called on the Surface Transportation Board (STB) to “strengthen regulations pertaining to reciprocal switching agreements,” which the board [is expected to do](#) in early 2022. The regulations would be based on a six-year-old [notice of proposed rulemaking \(NPRM\)](#), which was, in turn, based on far older data.

But... Concerns about competition in the freight-rail industry, and particularly about consolidation among Class I railroads, have been both overblown and misdirected, driving officials to seek counterproductive regulatory remedies. A reciprocal-switching mandate would render rail networks both less efficient and less resilient, as it would undermine firms’ ability to schedule their operations precisely.

Such a mandate would be particularly counterproductive in the midst of the ongoing supply-chain crisis. Over the longer term, a switching mandate would undermine the very incentives that have yielded enormous private investment in the development and ongoing maintenance of rail infrastructure.

KEY TAKEAWAYS

RAIL CONSOLIDATION IS EXAGGERATED

The number of U.S. railroads identified as “Class 1” has declined from 40 in 1980 to just seven today, but the practical effect of this consolidation tends to be greatly exaggerated by rail’s critics. In truth, due to changes in definitional terms, many of 1980’s Class 1 operators would not be classified as such today. Moreover, the number of smaller railroads has boomed over the past four decades, while the share of track under Class I control has [declined](#). In real terms, concentration in the rail sector has actually fallen.

There is vanishingly little evidence that the freight-rail industry suffers from insufficient competition. Shippers pay appropriate market [rates](#), innovation is [pursued](#) aggressively, and infrastructure is [maintained](#). If regulators were to act on the belief that a certain minimum number of Class I railroads is needed to foster competition, they would risk undercutting benefits to end-customers and shippers alike.

A RESPONSE TO AN IMAGINED PROBLEM

Compulsory reciprocal switching is touted as a remedy to market concentration by guaranteeing rail operators' competitors be granted access to otherwise private infrastructure. This means a railroad that has a line to a given shipping facility would be compelled to route traffic from other railroads to that facility. This may appear reasonable on its face, as railroads are already heavily integrated and frequently undertake private switching arrangements. But unlike private agreements, compulsory access is not necessarily driven by economic efficiency. It would diminish railroads' flexibility to seek the efficiencies that have allowed the industry's capacity to grow dramatically since the turn of the 21st century.

Compulsory reciprocal switching could benefit shippers, but only insofar as it would function as a subsidy to shipping that would be financed by railroads and consumers. Reduced operational efficiency for rail networks is a luxury the nation cannot afford in the wake of ongoing [supply-chain disruptions](#).

And in the long term, a reciprocal-switching rule could cut against the administration's own competition and infrastructure objectives. Given that competition between freight rail and trucking is set to be transformed by the introduction of automated systems, it is crucial not to hamper railroads' ability to operate at peak efficiency. This would place them at a [sectoral disadvantage](#) and could even drive demand for further consolidation in the sector.

Compelled interoperability also would dampen or erase price signals about the need for infrastructure investment. Inflexible per-car rates for exchange are a poor substitute for demand-driven switching arrangements. If the users of infrastructure are insulated from the full cost of that use, there will be a tendency for overuse and underinvestment, leading to neglect.

PRECISION SCHEDULED RAILROADING

Consumers win when freight rail moves efficiently. Developments in automation and scheduling are poised to usher in just such an era of so-called "precision scheduled railroading" (PSR). The [theory](#) is that fewer, longer trains can be predictably operated to create both greater efficiency and greater capacity. Reciprocal switching would preclude railroads from realizing the benefits of PSR by forcing them to run shorter trains more irregularly, in order to accommodate access requirements. The benefits to shippers, and to labor unions seeking to offset staffing reductions made possible by automation, would come at the expense of consumers, who would pay more. There also would be detrimental impacts to supply-chain resilience and to the environment, due to the need to run more trains.

CONCLUSION

As the STB decides whether to move forward with its 2016 NPRM, begin a new rulemaking process, or defer action entirely, the last of these is the only course of action that comports with market realities and the nation's infrastructure needs. Barring that, the STB should recognize how the world has changed in the last decade, and go back to the drawing board with a new proceeding.

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