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The Perennial Public Policy Debate

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Rail transportation of grain has been an issue of public concern since railroads first opened the vast prairies for settlement. The production, marketing, and transportation of grain often seem to raise emotions to a high level because of its importance as a food staple and necessity for life. Grain transportation, by itself, is also equally if not more of an emotional subject because it is essential to the survival of producers and the grain marketing industry. Rail grain transportation is especially important to producers, the country grain elevator industry, and the railroad industry, both short lines and class ones, in the Upper Great Plains region of the United States. The transport of grain by rail is critical to the long run economic survival of all three entities as well as the export and domestic grain marketing industry.

Producers in the Northern Plains are often at a disadvantage in shipping their bounty to market by alternative modes. Barge transportation is not accessible in most cases and truck is not an alternative in many other cases because Northern Plains producers are long distances from terminal markets. Additionally, shifting rail traffic to the highway infrastructure would have significant implications for the maintenance and rebuilding of the regional highway system. North Dakota, for instance, ships approximately 75 percent of its grain and oilseed production to domestic and export markets by rail. Moving the rail market share (nearly 400 million bushels

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annually) by truck has important implications for each of the three parties. Similarly, the country elevator industry has developed its infrastructure and marketing system around the rail mode since the European immigrants who settled the Great Plains and began to till the fertile soil. Railroads that serve the Upper Great Plains are equally dependent on grain transportation as it is a major profit center for their companies. Grain is also often a major or sole reason for maintaining the rail infrastructure in the region. Although these three economic entities are exceedingly interdependent, they continually find themselves at odds with one another because of the global nature of the grain market.

This world market for grain results in prices which are determined by factors beyond the control of any of the three entities. (This of course ignores government intervention for purposes of simplification.) This results in a fixed price during any short run period (although they fluctuate over a time span) that must be shared by all three parties at any one time. In the very short run any one of these parties can only increase their gross return by reducing the return to one or two of the other parties since grain is priced by backing off the transportation, logistical, and marketing costs from the world price. The consequence of this circumstance is a constant struggle among the three to maximize their share of the pie. It is a struggle in which any one of the players may have an advantage over the other at different times. However, railroads have an upper hand at many times because of their ability to influence economic outcomes with the setting of rates. Additionally, they also have the ability to concede preferences of one shipper over another to advance their economic interests. Although there is this continual struggle to gain an advantage over one another, there is a continuing interdependence and symbiotic relationship among them. This unusual forced partnership among the three players has resulted in years of struggle to improve their own economic status at the expense of the other. Federal, state and even local governments have developed and implemented public policy over the last 100 or more years to resolve this struggle with sometimes little success and at other times meaningful achievement. This remains true today as we find ourselves at yet another crossroad in the evolving map of public policy regarding the regulation of the rail industry via the abolishment of the Interstate Commerce Commission. The current debate in Congress regarding the elimination of the Interstate Commerce Commission should be of concern to all who have an interest in agriculture, the grain marketing industry, and the rail industry.

This debate should focus on the overall goal of a system that helps the competitive marketing of grain produced in this region in both domestic and global markets. A system that facilitates the competitive marketing of grain must meet two conditions. First, it must be able to supply competitively priced grain given certain quality and service standards, and second, it must allow all parties to be profitable in their participation in the system. If they are not profitable they will not be able to invest in the inputs, infrastructure and technology to maximize their efficiency. Moreover, profitability is a necessary condition for the parties' willingness to participate in the system. A lack of profits will eventually lead to long run decline and industry failure. The central question is how to create such a system. A second primary goal of the system should be to help increase the total market share thus increasing the overall size of the pie.

The most prevailing argument since the 1970s, characterized by the bankruptcy of several major railroads, is that markets are better at allocating resources and setting prices than regulatory bodies. This has resulted in the movement toward a more market oriented system. This movement toward a more market oriented rail industry is exemplified by the passage of the

Staggers Rail Act of 1980. The success of this major policy shift is hard to argue. Rate levels on grain are generally lower, investment in rail infrastructure and equipment has increased, equipment utilization has improved, service has improved along with capacity, innovative but sometimes controversial rail car pricing systems such as COTs and PERXs have been implemented and intra modal competition has increased. However, this does not mean that there has not been some market failure of at least a short term nature in which all three parties have experienced some economic loss. For instance, there have been several instances of capacity shortage resulting from the vagaries of the grain market and the implementation of COTs was not without some significant adversarial experience and losses among some of the parties. Also, the rail industry has been saddled for many years with excess car capacity. Overall, the changes in the 70s and early 80s can be viewed as successful if one recalls the crumbling rail system before that time. However, the recent success of this most recent evolution in grain transportation regulatory policy should not be used as a justification for further deregulation without careful analysis.

Instances of market failure occur for several reasons including the unique aspects of the world grain market and lack of a competitive environment. World grain markets which are influenced by factors ranging from worldwide weather patterns to some countries desires to be self sufficient in food supply are outside the range of influence of public policy on grain transportation and must be accepted as given, at least in the short run. However, competition is the essence of this policy. Competition within each of these three industries should be evaluated when considering changes in federal regulatory grain transportation policy and its impact on the negotiating relationship among the three parties. Changes to the system should facilitate competition within each of the three industries and encourage cooperation among them. This will result in greater efficiency and more equitable negotiated settlements among the players. This would better serve all interests and culminate in improved competitiveness in domestic and global markets.

Information seems essential for this process to work. Internal rivalry among firms of industry, geographic and product competition are stifled in an environment lacking knowledge and information. Knowledge is evolving as an important criterion for a competitive environment out of the classical list assembled many decades ago. Publication of rates seems imperative for a competitive market for grain transportation to exist. (Obviously not at the exclusion of contract rates.) Some form of common carrier obligation goes hand in hand with publication of rates since it would serve no purpose for requiring rates to be published and not requiring railroads to provide service. However, this should not be a one way street; this responsibility must be shared by railroads, country grain elevators and producers to the extent that the service railroads are required to provide must be profitable.

It is clear that, despite any changes in the regulatory mechanism, there will continue to be differences among the three vested interests in this tri-party system. Thus, some system should remain to arbitrate differences when they cannot successfully negotiate among themselves. Since railroads are insulated from the commercial code it only makes sense that a commission of some sort exists to address these issues as they arise.

In summary, Congress should evaluate any proposed changes from the standpoint of competition and negotiating equity. The fundamental questions of (1) does the change increase competition within each industry? and, (2) does it improve negotiating equity among the parties?, needs to be asked. Policies based on these principles will result in greater efficiencies in all participating sectors and a reduced need for subsequent government interference. A further question that should be addressed is whether changes in policies increases the overall size of the pie. This will help in getting the parties out of the zero sum game mind set. Congress should act carefully to ensure that the gains made in the past 15 years in rail regulatory policies are not offset in the quest for total commercial freedom. If this becomes the case, it would seem to call for a complete scrapping of the Interstate Commerce Act and a substitution of existing commercial law.