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RATE REGULATION REFORMS

REPLY COMMENTS OF
CONSUMERS UNITED FOR RAIL EQUITY

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Reply Comments of Consumers United for Rail Equity

Consumers United for Rail Equity ("CURE") hereby files its Reply Comments.¹

Introduction

In *Coal Rate Guidelines-Nationwide*, 1 I.C.C.2d 520, 526 (1985) ("*Coal Rate Guidelines*"), *aff'd sub nom. Consolidated Rail Corp. v. United States*, 812 F.2d 1444 (3rd Cir. 1987), the ICC adopted four so-called "constraints" on rail rates. *Coal Rate Guidelines* is still followed by the STB today.² In its Comments filed October 23, 2012, the Association of American Railroads ("AAR")³ and other railroad parties (who have generally endorsed AAR's Comments) seem to suggest that, as a result of these four so-called "constraints," captive shippers have a variety of means available to challenge rail rates. But that is not the case.

Three of those so-called "constraints" – "revenue adequacy," "management efficiency," and "phasing" – have never been applied to constrain a rail rate;⁴ indeed, the "revenue adequacy" constraint has never even been defined by the ICC or the Board. In its Opening Comments, CURE argued that

¹ CURE's October 22, 2012 Opening Comments including an explanation of the interests of CURE and its members in the matters at issue in this proceeding.

² See cases cited in AAR's October 23, 2012 Comments (at 3 n.1).

³ AAR Comments (at 4).

⁴ As *Western Coal Traffic League, et al.* put it (October 23, 2012 Opening Submission at 9), "Between 1985 and 2012, no coal shipper has obtained any rate relief under these three standards [*i.e.*, "management efficiency," "revenue adequacy," and "phasing"]. That's 0 for the last 27 years. The only constraint that has proven to be of any value to captive coal shippers is the SAC constraint, and that value has been hard-earned." In fact, the same is true of all shippers, not just coal shippers.

the time has come to define and apply the “revenue adequacy” constraint, because the Class I railroads are all clearly revenue-adequate. In fact, the Surface Transportation Board Authorization Act of 2009, which was reported to the Senate unanimously by the Senate Commerce, Science and Transportation Committee on December 17, 2009, also contained a provision directing the Board to begin developing its “revenue adequacy” constraint. Nevertheless, for now, that so-called revenue-adequacy “constraint” is a constraint in name only, not only because it has not been defined, but also because the Board has not treated any Class I railroad as “revenue-adequate” on a “long-term basis” under its standards.⁵

The “management efficiency” constraint is not a real constraint, because of the view expressed by the ICC, when the issue first arose in the 1980s, that a shipper would have to show that the Defendant railroad’s alleged management inefficiency alone is shown to increase a railroad’s revenue need to the point where the shipper’s rate would be affected.⁶ Only such a showing would justify prescribing a reduced rate under that “constraint.” That standard, as so construed, is impractical or impossible to meet, in an individual rate challenge. Imagine the burden on a shipper, who is challenging a single rate, to scour the entire railroad, and all of its operations and ratemaking practices, to identify

⁵ The Board may have assured the D.C. Circuit that the “revenue adequacy” constraint is, in fact, a real constraint, but it is not clear from its opinion that the D.C. Circuit understands that the “revenue adequacy” constraint has never been defined or applied by the Board or the ICC. See *BNSF Ry. Co. v. STB*, 453 F.3d 473, 477 (D.C. Cir. 2006).

⁶ *Major Issues in Rail Rate Cases*, Ex Parte No. 657 (Sub-No. 1) (served Oct. 30, 2006), slip op. at 7.

railroad-wide managerial inefficiency? In most if not all instances, the transaction costs of such a search could not be justified, no matter how high the rate, especially given the restrictive interpretation applied by the ICC.

This brings us to the so-called “phasing” constraint. But, under *Coal Rate Guidelines*, “phasing” is only a “constraint” on rate increases, not a constraint on a challenged rate itself.

Therefore, as Western Coal Traffic League, *et al.* explained in their Opening Submission, only the “stand-alone cost” constraint has ever actually served as a true constraint on rail rates. As a consequence, arguments about the other three so-called “constraints” are entirely irrelevant unless the Board commits to making any of these other three so-called constraints meaningful. Given the limitation of the “management efficiency” constraint, and the fact that the “phasing” constraint only applies to rate increases, the only so-called “constraint,” other than SAC, with any potential for actually constraining rail rates is the “revenue adequacy” constraint.

Summary of Position

Inadequacies in the Board’s Existing Rail Rate Guidelines. Given the substantially changed financial and other circumstances prevailing in the railroad industry today, as compared to 1985, when *Coal Rate Guidelines* was first adopted, it is past time to make the “revenue adequacy” constraint meaningful.

CURE submits that, in light of the incredible complexity that has been raised about the “stand-alone cost” (“SAC”) methodology in the Comments already filed in this proceeding, and in the proceedings in which rate challenges

under the SAC methodology have been brought since 1985, it is also time to consider whether it is still necessary⁷ to use SAC— the most complex rate-challenge methodology applied anywhere – or whether the time has come to greatly simplify the process, shorten the time involved, and reduce the cost of the Board's primary ratemaking guideline.⁸ These considerations may dovetail with the need to develop the "revenue adequacy" constraint, because it may be that the solution is an entirely different ratemaking standard than SAC. This is especially important because the Board's two other simplified rate guidelines, "Three-Benchmark" and "Simplified-SAC," are or have become almost impractical to apply.

Along those lines, the U.S. Department of Agriculture ("USDA") filed important Comments herein showing that, as a practical matter, the Board's "Three-Benchmark" and "Simplified-SAC" guidelines are not useful to grain shippers. As the USDA points out, the proof lies in the fact that no grain shipper has ever filed a complaint challenging a rail rate under the "Three-Benchmark" or "Simplified-SAC" guidelines.

Surely there are good reasons that these two methodologies have not been used in grain rate challenges. If grain rates tend to be fairly uniform, as is apparently the situation, the "Three-Benchmark" methodology will not provide relief, no matter how high the rates, because the rates at issue will be within the

⁷ CURE does not oppose use of SAC if a Complainant elects to challenge a rate on that basis.

⁸ Commendably, The Kansas City Southern Railway Company ("KCS") (Comments at 11) also expressed concern about the cost and complexity of SAC proceedings: "To the extent that the Board's proposal reduces the cost and complexity of litigating a Full-SAC case, KCS would support such an approach."

"comparable traffic group" range of rates. And, if grain shipments go to a variety of destinations, as also appears to be the case, the "Stand-Alone Railroad" ("SARR") would have to be incredibly large to bring even a Simplified-SAC case.

As for SAC, in the only grain case ever brought since the Staggers Rail Act of 1980 was enacted – the infamous *McCarty Farms* litigation, in which the ICC granted relief – was reversed by the D.C. Circuit on the ground that the ICC, having determined that SAC provided the only economically rational approach to ratemaking, had to be followed. So, grain shippers essentially have no recourse to challenge rail rates at the STB.

U.S. Magnesium is the only shipper ever to file a complaint invoking the "Simplified-SAC" guideline, and its challenge was settled. U.S. Magnesium filed Opening Comments explaining that the "Simplified—SAC" guideline, as it now exists (*i.e.*, without using replacement costs for Road Property Investment) is not practical to apply without substantial changes. No entity is in a better position to know whether the application of the "Simplified—SAC" guideline is practical than is U.S. Magnesium.

The "Three-Benchmark" methodology is less and less useful, because if most or all of the rates in the comparable traffic group are at approximately the same Revenue/Variable Cost ("RVC") level, no relief is available, no matter how high the rate level.

Other shippers and shipper groups filed opening Comments explaining at great length how some of the changes proposed by the Board could be helpful – namely, raising the remedy caps and using the Prime Rate as the interest rate for

damage awards in proceedings in which the Board has determined that a rate is unreasonably high. These same commenters noted that the other changes proposed by the Board would be highly adverse to complainants and could lead to a situation in which few if any rate challenges are likely to be brought, even if the Board raises the remedy caps and the interest rate on damages.

For example, as CURE showed in its Opening Comments, the Board's proposal to either require the SARR to carry only traffic that originates or terminates on the SARR, or be allowed to carry unit train traffic, let alone the railroads' proposals to eliminate "cross-over traffic" altogether, would make it nearly impossible in most, if not all instances, for complainants to prevail. The proposals also violate a fundamental tenet of *Coal Rate Guidelines*, i.e., that the shipper is allowed to propose the SARR that best suits its circumstances, save only (as later STB decisions hold) that the SARR have an approved operating plan.⁹ The Board's proposals would either require the shipper to make the SARR larger and larger, to include origination or termination points, and then perhaps also the traffic on the lines that are added to the SARR, ever-increasing the SARR, or limit the traffic the SARR could carry only to unit trains. But the SARR would not need to be so large, nor would the traffic it would carry necessarily be so limited, in the real world. So, the Board's proposals are not only discouraging, but also at odds with the principles of its own long-standing *Coal Rate Guidelines*.

⁹ E.g., *BNSF Ry. Co. v. STB*, *supra*, 453 F.3d at 477 (D.C. Cir. 2006)(shipper has broad flexibility to design the route of the SARR in order to lower costs by taking advantage of the economics of density, and there are no restrictions on the traffic that may potentially be included in the stand-alone group).

It is distressing that the Board's approach in SAC proceedings already is making the possibility of relief under the "SAC" guideline more and more unlikely in nearly all instances, even though Congress intended that captive shippers have a workable methodology for obtaining relief from an unreasonable rail rate. Again, we fear that the Board's proposals in this proceeding only make rate relief less accessible for complainants. We believe the Board should be finding ways to make the process of challenging a rail rate easier, faster, and less costly, rather than ever-more complex, costly, and time-consuming as is unfortunately the case with its Simplified-SAC and Full-SAC proposals herein.

The Railroads' Comments, If Followed, Would Make the Problem Worse.

The Class I railroads – BNSF Railway Company ("BNSF"), CSX Transportation, Inc. ("CSX"), KCS, Norfolk Southern Railway Company ("NS"), Union Pacific Railroad Company ("UP"), and their trade association, Association of American Railroads ("AAR") -- all filed Opening Comments in this proceeding. The American Short Line and Regional Railroad Association ("ASLRRA") also filed Comments. All railroad parties endorsed the Comments of the AAR (although KCS stated (Comments at 4 n.2) that "While KCS has joined in the comments of the Association of American Railroads and generally supports the positions advocated therein, to the extent there are differences, these comments most accurately reflect KCS's views.").

As monopolists or oligopolists in most markets, the railroads naturally favor changes to the Board's rate-reasonableness methodologies that would lead to fewer, or even no, successful rate challenges and have proposed such

changes. Obviously, shippers support rate-reasonableness standards that permit successful challenges. Does that mean that the Board should discount the filings of both sides, on the theory that they are merely self-interested representations? No, for one simple reason.

The Board should be guided by Congressional intent, which clearly supports the ability of captive shippers to have practical and efficient means of challenging rail rates and the ability to succeed at such challenges in at least some circumstances. Based on that Congressional intent, we believe the Board should accept those Comments that would preserve the ability of shippers to file such challenges. In doing so, it should rely not only on the Opening Comments of shipper organizations, but also on those of the United States Department of Agriculture ("USDA") and should reject the arguments made by the Class I railroads, AAR, and ASLRRRA.¹⁰

¹⁰ ASLRRRA contends that the Board's proposals would have profound effects on short-line railroads even though short lines are not typically involved in large railroad rate cases, because when the rates are challenged, the larger railroads allegedly look to the short lines to recoup lost profits. ASLRRRA alleges the Board's proposal to eliminate the limits on relief in Simplified-SAC cases and to double the limit on relief in "Three-Benchmark" cases would be harmful to short lines and regional railroads because the proposals will encourage and enable shippers to bring more rate cases. As a result, ASLRRRA encourages the Board to maintain its current regulations.

As we have already shown, the Board's proposals make it more unlikely, rather than more likely, that shippers will seek relief under any of the Board's rate guidelines.

In any event, ASLRRRA's position is unsupported; there is no evidence that Board-prescribed rate reductions are taken disproportionately from short-line or regional railroads. Moreover, the issue ASLRRRA has raised is outside the scope of the proceeding, because it has to do with revenue allocations between railroads jointly participating in a movement. Generally, the Board does not allow shippers to determine the "divisions" between railroads in the belief that the shipper's interest is only in the overall rate. ASLRRRA also has not provided

As CURE explained in its Opening Comments filed on October 22, 2012 in response to the Board's Notice of Proposed Rulemaking served July 25, 2012 ("July 25th Decision" or "NOPR"), CURE appreciates and supports the Board's initiative in addressing its current rate-reasonableness methodologies, the operation of which are crucial to those rail customers without access to transportation competition. In particular, CURE supports the Board's proposals to raise the caps on remedies in "Three-Benchmark" and "Simplified-SAC" proceedings and the Board's proposal to increase the interest rate for damage awards from the T-bill rate to the Prime Rate. CURE does not support the Board's other proposals in this proceeding.

The Railroads Should Not Be Allowed to Inject Issues the Board Did Not Raise in the NOPR. In the Comments of various railroads,¹¹ the railroads (perhaps supported by AAR – it is not entirely clear) argue that "cross-over traffic" should be eliminated from the SARR traffic base altogether. This is fundamentally wrong. The SAC analysis has assumed from the beginning that

information about actual divisions in its Comments. If there is any merit to the issue at all, it would be better dealt with in an individual rate proceeding, in which a short-line or regional railroad could ask the Board to prescribe a rate in such a manner that it does not disproportionately or unfairly reduce the revenues of the participating short-line or regional railroad, rather than in this proceeding, in which the Board did not propose any change that would have a disproportionate impact on short-line or regional railroads.

¹¹ E.g., BNSF Opening Comments (at 3); UP Opening Comments (at 3-4); see AAR Comments (at 8-10). It appears that the other Class I railroads do not agree with BNSF and UP. See CSX and NS Joint Opening Comments (at 18). Kansas City Southern Railway Company ("KCS") does not appear to agree with BNSF and UP, because it, too, does not argue that "cross-over traffic" should be eliminated but does support (Comments at 11) efforts to "reduce[] the cost and complexity of litigating a Full-SAC case."

"cross-over traffic" is something that the SARR may carry, and therefore that the Complainant shipper may include in its SAC analysis.

In AAR's Opening Comments (at 8-9) and in the Opening Comments of various Class I railroads, the railroads attempt to raise an issue the Board did not propose – whether the Board is required to use "Original Average Total Costs" instead of modified "Average Total Costs" ("ATC") in calculating the costs of the SARR. As AAR concedes (at 8-9), this issue arose on application of the Board's rate-reasonableness guidelines in the *Western Fuels* litigation.¹² As AAR also implicitly concedes (*compare* pp. 8-9 with summary of issues proposed by the Board, *id.* at 10), the modified-ATC issue was not first proposed by the Board in its NOPR in this proceeding, but was adopted by the Board in that proceeding, challenged on appeal by BNSF from the Board's action in prescribing a rate in *Western Fuels*, remanded to the Board, and again applied in *Western Fuels* in June 2012, just before this proceeding was commenced.

The Board should not, in this proceeding, allow BNSF, AAR, or any other railroad the opportunity to re-litigate the matters that BNSF had a full and fair opportunity to litigate in the *Western Fuels* litigation. The issues were fully briefed and decided. If AAR or other railroads wished to be heard in *Western Fuels*, they could have sought leave to file *amici* comments, but they did not. Further, the Board's actions were challenged on appeal and the D.C. Circuit has ruled on them. There is no need to rule on them again. Rather, the matter ought

¹² *Western Fuels Ass'n v. BNSF Railway* proceeding, STB Docket No. NOR 42088 (served Sept. 10, 2007), *remanded sub nom. BNSF Railway v. STB*, 604 F.3d 602, 613 (D.C. Cir. 2010), *decision on remand* (following modified ATC) in NOR 42088 (served June 15, 2012).

to be left to the parties in the *Western Fuels* litigation, so that BNSF¹³ is not given a second “bite at the apple.” In addition, this approach would be fair to Western Fuels Association and Basin Electric Power Cooperative, which have already litigated the issue in *Western Fuels*.

Moreover, the railroads did not just seek to re-litigate the Original ATC issue in this proceeding rather than let the parties to the *Western Fuels* proceeding be the ones to litigate it *in that proceeding*. CSX Transportation, Inc. (“CSX”) and Norfolk Southern (“NS”) are also attempting to get a second bite at the apple in this proceeding to litigate the issue of “Leapfrog” cross-over traffic that is separately at issue in STB Docket No. 42125, *E.I. Dupont de Nemours & Co. v. NS*.¹⁴ In our view, it is inappropriate for the railroads, especially one that is already a party to a separate proceeding in which a discrete issue was litigated or is being litigated, and which issue was not raised by the Board for comment in this proceeding, to raise that issue here rather than litigate it in the particular rate-reasonableness proceeding in which the issue is already being litigated. We trust the Board will not allow parties to litigate the same issues in two pending STB proceedings at the same time, but instead require those railroads that have raised issues in individual rate-challenge proceedings to be bound by the outcome of those proceedings.

¹³ BNSF acknowledges, (see Comments at 8, 13-16) that the Board's proposals spring from its evidentiary filings in *Western Fuels*.

¹⁴ CSX and NS October 23, 2012 Opening Comments at 18.

RESPONSES TO THE RAILROADS' COMMENTS.

Below, CURE replies to the railroad parties on the issues the Board did raise for comment, in the order in which these issues are addressed in AAR's October 23, 2012 Comments:

1. Remedy Cap on Simplified-SAC Methodology

The Board has never decided a rate challenge under its "Simplified-SAC" ("SSAC") guideline. The Board, however, believes that the elimination of a cap on the SSAC guideline – now \$5 million in total relief over 5 years – will be a welcome change that will result in rate challenges under the SSAC methodology. We believe the removal of the damages cap could have that result, but not in light of another proposal contained in its Decision. The Board's proposal to require the complaining shipper to provide a full analysis of the replacement costs for Road Property Investment ("RPI"), rather than a more simplified analysis of replacement costs based on previously decided cases, as is now the rule, we believe wipes out any and all benefit of the removal of the cap on remedies.

AAR argues that the Board had no foundation for its proposal to raise the remedy cap on Simplified-SAC and "Three-Benchmark" proceedings. AAR is wrong, for three reasons.

One, CURE showed that the reason to raise the cap is that the Board's previously articulated assumed need for its remedy caps -- that the shipper should not be encouraged to use a methodology that is less-accurate instead of one that is more accurate -- simply does not apply in the real world. Instead, the

"Simplified-SAC" methodology will produce a rate that is higher than that produced by the Full-SAC methodology, so a shipper is already motivated to use the Full-SAC methodology to obtain the maximum amount of relief to which the shipper is entitled unless the Full-SAC methodology is too costly to pursue. In addition, the "Three-Benchmark" methodology produces the highest rates of all three guidelines, so there is also every reason to remove the remedy cap on "Three-Benchmark Proceedings. A shipper will use the rate methodology that it believes will yield the lowest possible reasonable rate unless the rate and volumes at issue do not justify the costs of the standard that produces the lowest rate level (which is typically, Full-SAC).¹⁵

Two, as other shipper parties have shown, the transaction costs of developing a Simplified-SAC presentation are much higher than the Board assumed, likely higher than the \$2.75 million the Board estimated,¹⁶ even assuming that such a presentation can be made.¹⁷ Therefore, in order for Simplified-SAC to be an economically viable option for a rail shipper, the potential remedy available must be significantly greater than the transaction cost, logically more than double the transaction cost.¹⁸ In any event, the railroads need not fear that shippers will use Simplified-SAC instead of Full-SAC. As U.S.

¹⁵ CURE October 22, 2012 Opening Comments at 15 n.5.

¹⁶ July 25th Decision (at 15); *see also* Verified Statement of Gerald W. Fauth III ("Fauth Statement")(at 7, 13), filed with the October 23, 2012 Opening Comments of the Alliance for Rail Competition, *et al.*

¹⁷ E.g., October 23, 2012 Opening Comments of U.S. Magnesium, L.L.C. (at 8-11).

¹⁸ Fauth Statement (at 13), *citing* July 25th Decision (at 6).

Magnesium explained, there are fundamental problems with the methodology that may prevent its use in any event.¹⁹

2. Full Assessment of Road Property Investment in Simplified-SAC Proceedings. AAR (Comments at 13) altogether rejects the use of Simplified-SAC as a suitable substitute for Full-SAC because the “clear language of the statute” “specifically limits the use of alternatives to a ‘full stand alone cost’ presentation.” AAR argues that Full-SAC is the most accurate way to determine the reasonableness of rates, and, therefore, apparently contends that it must be used. AAR argued that the proposed change to use replacement costs for Road Property Investment (“RPI”) will be more accurate than Simplified-SAC is now and therefore, if Simplified-SAC is used, the Board’s approach to RPI must be used to make the results of that methodology more reliable and accurate.²⁰

Also, AAR argues (at 14-15) that the Board’s approach to the Simplified – SAC methodology effectively requires the Defendant Railroad to prove the Complainant’s case. AAR’s argument is obviously over the top, in that it theorizes that the Board’s Simplified-SAC guideline “could expose the railroad to

¹⁹ *Id.* at 9-10.

²⁰ CSX and NS jointly argue that RPI should be based on replacement costs because it has been almost a decade since the last Eastern coal rate challenge, and the real estate values determined in that most recent proceeding “are outdated.” Opening Comments of CSX Transportation, Inc. and Norfolk Southern Railway Company (at 15), *citing Duke Energy Corp. v. CSX Transp., Inc.*, 7 S.T.B. 402 (2004). But the SSAC methodology already reflects the higher land values in the East (*see id.* at 14, Table showing real estate values) and CSX and NS have not shown that real estate values are in fact higher than in 2004. Indeed, given the severe recession in real estate values nationwide that dates to 2008, the real estate values in the 2004 case may be higher than the value of the same real estate today. So, this is not a substantial reason to require replacement costs for RPI.

frivolous complaints and expensive discovery fishing expeditions....” While that may have been a fear when the Simplified-SAC guideline was adopted, there has only been one Simplified-SAC challenge ever filed in 16 years, and it was settled.²¹ Moreover, rail customers are not likely to undertake proceedings that cost upwards of \$3 million frivolously or to undertake expensive discovery fishing expeditions. So, this stated railroad fear is groundless.

Clearly, Congress intended that there be simplified methods for determining a maximum reasonable rail rate in circumstances in which Full-SAC is too costly, given the value of the case. But, as CURE has shown, the “value of the case” can be determined by the fact that the Simplified-SAC methodology will produce higher rates than will the Full-SAC methodology, and therefore a shipper will only use Simplified-SAC when its circumstances do not permit application of Full-SAC, since Full-SAC normally results in the lowest possible reasonable rate. Therefore, the limitations imposed by Congress in 49 U.S.C. § 10701(d)(3) “to establish a simplified and expedited method for determining the reasonableness of challenged rail rates in those cases in which a full stand-alone cost presentation is too costly, given the value of the case” -- will be self-policing, and AAR’s concerns simply do not apply.

Finally, AAR is simply incorrect in contending that the Defendant Railroad must prove the Complainant shipper’s case. Rather, the Defendant is simply required to provide the information that is only in its possession and that is necessary to make the required showing. Being compelled to produce

²¹ Moreover, the party that brought it, U.S. Magnesium, points out the limitations of the Simplified-SAC approach in its Comments.

documents or information important to a matter is not the same as bearing the burden of proof. As AAR well knows, the Simplified-SAC methodology will not work without the information required to be provided by the Defendant Railroad.

We believe the Board's proposal to require use of a full assessment of Road Property Investment ("RPI"), as compared to the current simplified approach to determining RPI, is contrary to Congressional intent as expressed in the ICC Termination Act of 1995. Congress clearly intended that the Board develop simplified methods for challenging rail rates when the use of Full-SAC is too costly, given the value of the case. By the time the shipper goes to the expense of satisfying the proposed new requirement for complete replacement-cost analysis to determine RPI, particularly in light of the other change the Board proposed with respect to the revenues for the so-called "cross-over traffic" that may be included in the SARR, a captive shipper likely would conclude that it might as well use the Full-SAC methodology to attempt to obtain the lower replacement cost that is generally available using the Full-SAC methodology.

In short, the transaction costs added by the Board's total proposed changes to the Simplified-SAC methodology may, instead of providing relief to shippers, make the Simplified-SAC methodology even less useful for most captive rail customers than it is already.

3. Raising the Remedy Cap in "Three-Benchmark" Cases

The railroads profess concerns with the Board's proposal to raise the cap on remedies to \$2 million/5 years in challenges under the Board's "Three-

Benchmark" guideline. However, the Board's proposal, even if adopted, will not correct the flaws with that methodology that increasingly limit or eliminate its use.

As the Board knows, and as CURE showed in its Opening Comments, the highest prescribed rates under any of the Board's methodologies generally result from application of the "Three-Benchmark" guideline, which compares the rate in question to other comparable rates for moving the same or similar commodities. Rail customers believe that there is no public policy reason to have a remedy cap in "Three-Benchmark" proceedings. The reason: captive shippers will file under the rate-reasonableness methodology that best fits the circumstances of their shipments, offers them the lowest prescribed rate, and is appropriate to the amount of funds they can commit to the litigation. Thus, a captive customer who challenges a rail rate under the "Three-Benchmark" methodology undoubtedly does so mindful that, even if it prevails, it will obtain the highest reasonable rate possible under any STB methodology. Therefore, such shippers must be understood to file under the "Three-Benchmark" methodology because it is almost certainly the only methodology that is useful to them. Thus, a remedy cap of any amount operates to deny captive rail customers either access to the Board's rate-challenge process altogether or full recovery of its damages under its only available rate challenge methodology.²²

²² Such shippers may also be precluded if, due to the practice railroads have been following, at least with captive chemical shippers, of "bundling" rates so that, if a shipper obtains one tariff rate (in order to challenge it at the STB) the railroad imposes higher tariff rates on all of the shipper's movements over that railroad. In such a circumstance, the cost to the shipper of the higher bundled rates may exceed any relief it could obtain from the Board in its challenges to the

Going forward, few captive shippers are likely to invoke the “Three-Benchmark” guideline. Challenged rates can be expected to be high but in the range of other, comparable rates for the same or similar commodities, so that the “Three-Benchmark” methodology likely will offer little if any relief from the challenged rate. The remedy cap of \$1 million (more recently \$1.18 million²³) over 5 years has rendered the “Three-Benchmark” guideline of little practical value, given the necessary transaction costs and the relatively small amount of damages that would be possible annually under the cap. In light of the railroad requirement of chemical shippers challenging rates on certain “lanes” -- that the chemical company pay higher tariff rates than normal on all lanes during the rate challenge -- the Three-Benchmark methodology is even less useful for chemical shippers (the only ones who have ever brought such a case). Raising the remedy cap to \$2 million over 5 years will not avoid most of the problems discussed above, and therefore will not trigger many, and most likely, any more “Three-Benchmark” challenges.

CSX and NS contend that the “Three Benchmark” and Simplified-SAC guidelines must “be limited to, at most, the litigation cost of using the next more exacting rate complaint mechanism.” (CSX/NS Opening Comments at 21). But CURE showed in its Opening Comments (at 15 & n.5) that a shipper will choose the remedy best-suited to its needs, in that the Full-SAC methodology generally

only some of the tariff rates, thereby making relief from the Board less valuable than the interim cost of the other unchallenged tariff rates.

²³ CSX and NS correctly noted (at 24 n.17) that “The original *Simplified Standards* cap for Three Benchmark cases was \$1 million; the current indexed cap is \$1.18 million. See *Rate Regulation Reforms*, STB Ex Parte No. 715, Notice of Proposed Rulemaking at 12 n.9 (July 25, 2012).”

produces the lowest rates, Simplified-SAC is expected by the experts to produce the next-lowest rates, and the “Three-Benchmark” guideline the highest rates. Therefore, there is no need to cap relief under either the “Three-Benchmark” or the “Simplified-SAC” Guidelines, because the shipper will choose to proceed under those Guidelines only if there is not a better alternative – *i.e.*, SAC, or the yet-to-be adopted “revenue-adequacy” constraint – available to the shipper.

4-5. Curtailing the Use of Cross-Over Traffic in SAC Cases, and Changing the Approach for Allocating Revenue on the SARR.

AAR argues that, if the Board determines that shippers should be allowed to include “cross-over” traffic in the traffic base of the SARR, it must limit that traffic either to unit-train traffic or traffic that originates or terminates on the SARR.

Fundamentally, these arguments, and the Board’s proposal, violate one of the core principles of *Coal Rate Guidelines*, that is, that the Complainant Shipper is allowed to present in its evidence the SARR that it chooses to present and that fits its circumstances, provided only that it have a functional operating plan and that the SARR’s total revenues exceed its total costs over the prescription period (at this time, ten years).²⁴

Railroad efforts to limit the traffic that the SARR would carry are clearly intended to deny relief in most or all Full-SAC cases. Since many shippers cannot present a case under the “Three-Benchmark” and Simplified-SAC

²⁴ *E.g.*, *BNSF Ry. Co. v. STB*, 453 F.3d at 477 (D.C. Cir. 2006)(shipper has broad flexibility to design the route of the SARR in order to lower costs by taking advantage of the economics of density, and there are no restrictions on the traffic that may potentially be included in the stand-alone group).

guidelines,²⁵ the railroads' proposals, if adopted, would make nearly all rail rates immune from challenge. This reality alone should be sufficient reason to reject these railroad proposals.

AAR claims that the use of cross-over traffic in SAC proceedings necessarily introduces imprecision into the analysis because of the difficulty of dividing the revenues between the on-SARR and off-SARR portions of the movements. Moreover, AAR claims that the Board has recognized that shippers can manipulate results by ATC calculations to bias the outcome of a SAC analysis because the shippers control the SARR design and the traffic-selection process.

Since the adoption of *Coal Rate Guidelines*, the Complainant shipper has been allowed to design the SARR of its choosing, provided only that the Complainant provide a workable operating plan for the SARR. This right of the complainant is not a "manipulation" as the AAR claims. If the SARR has a workable operating plan and the revenues of the traffic on the SARR exceed its costs over the prescription period, the SAC theory as articulated in *Coal Rate Guidelines* entitles the shipper to relief. As the neutral fact-finder, the Board should not prevent a shipper with a meritorious case from obtaining relief simply because a defendant railroad contends that some of the traffic does not belong on the SARR. If the railroad has a case to make against the inclusion of the traffic, the railroad can so state and the Board can determine the merits of the

²⁵ *E.g.*, Opening Comments of the U.S. Department of Agriculture (at 3).

case. However, the complainant has the right to include all such traffic in its SARR *ab initio*.

Other shippers and shipper groups already have written extensively on this subject.²⁶ To avoid unnecessary repetition, CURE adopts and incorporates the Comments filed by those shippers and shipper groups. They demonstrate that the railroads' Comments, urging the Board to adopt its proposals with respect to cross-over traffic, should be rejected.

As we stated in our Opening Comments filed on October 22, 2012, CURE is surprised that, despite the already incredible complexity of Full-SAC proceedings, the Board seems now to be proposing a railroad-inspired suggestion that will complicate the application of the Full-SAC methodology even further going forward. We refer to the proposal in the July 25th Decision to substantially increase the size of the SARR to include traffic that originates or terminates on the SARR, or to restrict the traffic the SARR may carry to unit-train traffic, in order to derive the benefits to the SARR of that traffic, as well as to change the revenue calculation associated with "cross-over traffic." We understand from experts on this subject that the net effect of these changes would be that most captive shippers would be unable to obtain relief in Full-SAC proceedings. Thus, we fear that these proposals of the Board may actually make it more difficult for rail customers to win the cases they have won in recent years

²⁶ *E.g.*, October 23, 2012 Joint Opening Comments of American Chemistry Council, *et al.* (at 4-24); October 23, 2012 Opening Submission of Western Coal Traffic League, *et al.* (at 12-74).

through the application of the Board's current Full-SAC methodology. Railroad support for the Board's proposal only confirms our worst fears.

For these reasons, and despite the fact that CURE supports the increase in, or elimination of, the remedy caps proposed in the Decision, CURE opposes the Board's proposed changes with regard to the shipments that must be included in the SARR and in the revenues to be assigned to the SARR. These changes would prevent most shippers from bringing rate challenges under any of the Board's rate-reasonableness guidelines, regardless of the applicable remedy caps. Congress could not have intended that the Board maintain a rate-reasonableness process that provides no realistic opportunity for success for most captive rail customers.

6. Interest Rate

The Board proposed that the interest rate imposed on the damages a railroad is required to pay a shipper in the event of a successful rate challenge should be changed. The current rate, which is based on the interest rates on Treasury bills (now 0.1%), (July 25th Decision at 18), is obviously too low. This *de minimis* interest rate does not in any way relate to the opportunity cost to the shipper of the lost funds, nor does it force a railroad to disgorge funds that, according to the Board's revenue-adequacy findings, earn far more than 0.1% annually. The Board's proposal to use the Prime Rate (now 3.25%) is more reasonable than the present approach, because it more closely reflects railroad earnings on shipper funds, or the shipper's return on its own funds.

As CURE pointed out in its Opening Comments, in rate challenges the defendant railroad has the Complainant Shipper's money and has been earning a return on that money during the pendency of the rate challenge. For its annual revenue-adequacy proceedings, the Board calculates what it says is the rate of return of that Defendant Railroad during the applicable time period, so the rate of return is readily available. Thus, rather than the Prime Rate, which is itself an improvement over the current applicable rate, we believe the most appropriate measure of the proper interest rate on shipper funds is the actual rate of return the Defendant Railroad earned on the money it owes the Complainant Shipper. That rate is the rate of return the Board determines in its annual revenue adequacy determination for the railroad in question.

Some of the railroad parties seem to suggest that revenues collected from shippers are put in some reserve or special account and earn only a minimal return during the time that a shipper challenges a rate.²⁷ That is nonsense. Money is fungible. The Defendant Railroad is not required to segregate the funds and deposit them into a low-interest, "money market" type account. Rather, like all other funds of the railroads, the revenues collected (perhaps even before the Defendant Railroad knows the rate is being challenged) may be, and

²⁷ See AAR Comments (at 25) ("Reparation payments represent an essentially risk-free 'investment' of funds because the funds involved in reparations proceedings are analogous to idle funds that corporations keep in short term government securities."); UP Comments (at 19) ("Interest on a reparation award is equivalent to a risk-free investment for the shipper because the Board would order the railroad to pay the shipper interest at the specified rate on any overcharges."). Other railroads either do not comment on the Board's interest-rate proposal (BNSF, CSX, and NS), or propose a "middle ground" (KCS (at 11-13)).

so presumably is, put to good use by the Defendant Railroad, earning a return at least as high as the return calculated by the Board.

Conclusion

For the foregoing reasons, the Board should eliminate altogether the caps on remedies in "Three-Benchmark" and SSAC proceedings. In the alternative, the Board should eliminate the remedy cap in SSAC proceedings and should at least adopt its proposed increase from \$1 million over 5 years to \$ 2 million over five years as the remedy cap for the "Three-Benchmark" rate challenges.

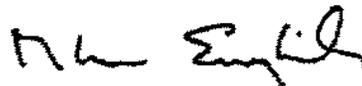
The Board should use the return the Defendant railroad(s) earn on rail customer funds that it holds improperly during the pendency of a rate challenge, rather than the Prime Rate, as the measure of interest to be paid as part of the damages the railroad defendant must pay in a successful rate challenge. In the alternative, the Board should at least adopt its proposal to change the measure of interest to be paid from the T-Bill rate to the Prime Rate.

Despite the railroads' Opening Comments, the Board should not adopt the Board's proposals to (a) require a full replacement-cost analysis for Road Property Investment in SSAC proceedings, (b) increase the amount of traffic that the SARR must include (by requiring the SARR to include only traffic that originates or terminates on the SARR) or limit traffic on the SARR to unit trains, and (c) alter the means of allocating the amount of revenues associated with so-called "cross-over" traffic. These proposed changes would make SAC proceedings more costly and more complicated; will reduce arbitrarily the cross-over traffic that the SARR may carry or prevent the shipper from designing the

SARR best-suited to its case; and are at odds with the Congressional directive to the Board in the Interstate Commerce Commission Termination Act of 1995.

Rather than adopt the proposals AAR and the other railroad parties support, the Board should look for ways to expedite rate challenge proceedings and make them less costly. Given the clear revenue sufficiency of the Class I railroads, the Board should also develop the specifics of the long-awaited "revenue adequacy" constraint.

Respectfully submitted,



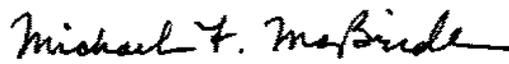
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Certificate of Service

I hereby certify that I have served, this 7th day of December, 2012, a copy of the foregoing Opening Comments of CURE on each person on the service list.


Michael F. McBride
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