236229

ENTERED
Office of Proceedings
June 26, 2014
Part of
Public Record

Before the U.S. Surface Transportation Board

STB Ex Parte No. 665 (Sub-No. 1)

Rail Transportation of Grain, Rate Regulation Review

Comments of the

U.S. Department of Agriculture

Edward Avalos
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

Date: June 26, 2014

Authority and Interest

The Secretary of Agriculture is charged with the responsibility under the Agricultural Adjustment Act of 1938 and the Agricultural Marketing Act of 1946 to represent the interests of agricultural producers and shippers in improving transportation services and facilities by, among other things, initiating and participating in Surface Transportation Board proceedings involving rates, charges, tariffs, practices, and services.

Introduction

The U.S. Department of Agriculture (USDA) appreciates the opportunity to respond to the U.S. Surface Transportation Board's (Board) request for input on how to ensure the Board's rate complaint procedures are accessible to grain shippers and provide effective protection against unreasonable rail transportation rates for grain.

In this proceeding, the Board is seeking input on how it might address a persisting frustration of agricultural shippers concerning access to an effective process to challenge rail rates that are believed to be excessive. The Board's established procedures for challenging excessive rail rates are not simple undertakings and require considerable legal, technical, and financial resources, limiting the ability of all but the largest shippers to challenge rates.

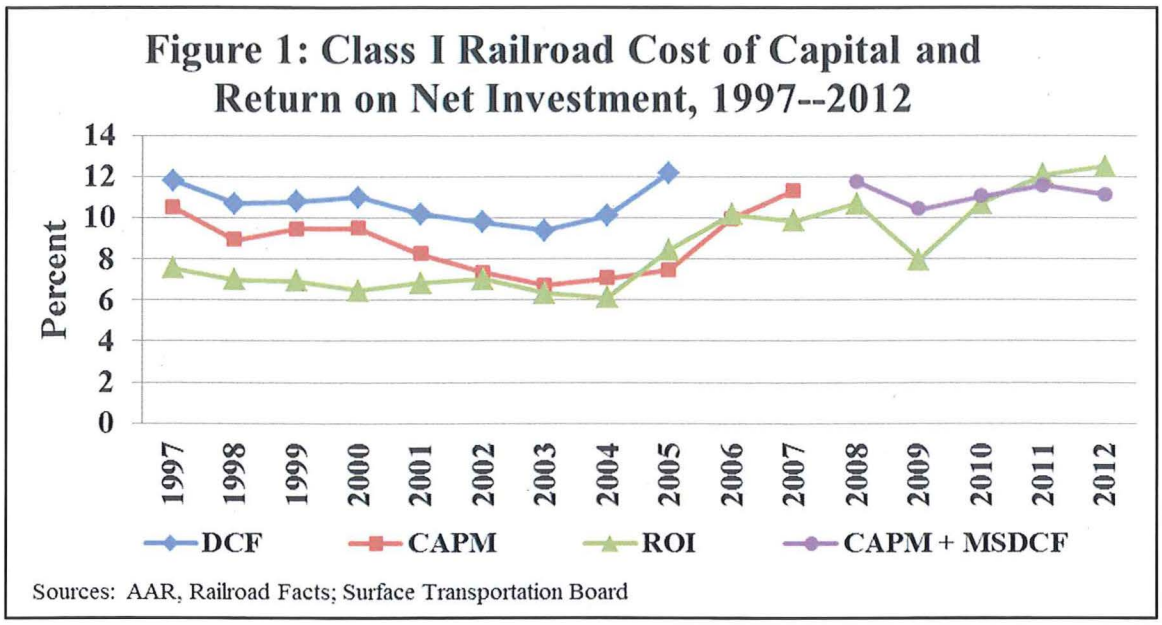
The Board has taken steps towards addressing this problem in past proceedings, but the extent of these steps has revealed an emerging disconnect between the perceptions of agricultural shippers and the Board as to how a resolution can be found. Meanwhile, most agricultural shippers continue to be left with no practically accessible means to challenge rail rates, much less seek redress. Nevertheless, it is with optimism that agricultural shippers view this current proceeding because of the apparent willingness in the Board's latest notice to consider departures from the current course of modifying existing procedures and instead examine alternative rate relief methodologies specifically tailored for agricultural commodities and their unique needs. Indeed, given its dialogue with agricultural shippers, USDA believes a new approach is necessary and warranted, and should be explored.

Financial Maturity of Railroads

The Staggers Act of 1980 has been a success story for the finances of the railroad industry and has benefited shippers. The four major Class I railroads are achieving returns on revenue and operating revenues that make them among the most profitable businesses in the country. Although the railroad industry has been investing record amounts into much needed capital projects, they have been able to double dividend payments and spend billions to repurchase their stock. Berkshire Hathaway's acquisition of BNSF Railway in 2010 for $44 billion marked the largest acquisition in Berkshire Hathaway history, signaling the considerable profitability of a railroad investment. As the U.S. Senate Committee on Commerce, Science and Transportation stated in its 2010 report *The Current Financial State of the Class I Freight Rail Industry*, "These large expenditures undermine arguments that railroads still lack the income to invest in their long-term capital needs."

Decades of efficiency improvements and recent but consistent rate increases have allowed the railroads to earn approximately their cost of capital and maybe more (see Figure 1). Since 2004,

Class I railroad profitability has increased rapidly, showing revenue adequacy by earning its cost of capital during 2011 and 2012. The financial health of the railroad industry is inarguably better today than in the immediate post-deregulation period. Yet, many question how much the railroads will be allowed to earn before they are considered revenue adequate and additional protections for captive shippers are implemented.



Under *Coal Rate Guidelines, Nationwide*, it was agreed that shippers without competitive options should pay a higher share of fixed costs than other shippers in order for the railroads to efficiently recover high fixed costs.[1] However, under Constrained Market Pricing precedent, a captive shipper is not to be "required to continue to pay differentially higher rates than other shippers when some, or all, of that differential is no longer necessary to ensure a financially sound carrier capable of meeting its current and future service needs."[2] Until the "revenue adequacy constraint" on differential pricing is formulated and instituted to protect captive shippers from excessive rates, USDA believes there are immediate measures the Board can take as a result of this proceeding to offer protection from unnecessarily high rail rates to captive agricultural shippers—those shippers who currently face the most hurdles to using the Board's current rail rate challenge procedures.

The Ability to Appeal Rail Rates

Prior to discussing the merits and mechanisms of the rate challenge process, USDA notes that both agricultural producers and grain elevators may suffer injuries from excessive rail rates sufficient to confer legal standing.[3] Therefore, the processes developed or modified in the course

---

[1] 1 ICC 2d 520 (1985).

[2] *Major Issues in Rail Rate Cases*, STB Ex Parte 657 (Sub-No. 1), October 30, 2006, at 7.

[3] *BNSF Railway. v. Surface Transportation Board,* 526 F.3d 770, 774 (D.C. Circuit 2008). See also *McCarty Farms, Inc. v. Burlington Northern, Inc.,* 91 F.R.D. 486, 486 (D. Montana 1981).

of this proceeding should ideally be accessible to both parties in order to avoid unintentionally excluding a significant portion of the agricultural community.

It is well established that transportation costs can have a direct impact on agricultural producers' profits, but the producer's ability to appeal rates has been limited. Agricultural producers in remote areas have few transportation alternatives, and the price they receive for their products is net of transportation and other marketing and handling costs. Since the McCarty Farms case, agricultural producers have not filed challenges to rail tariff rates, instead relying on grain elevators to appeal those rates. Yet, grain elevators have not made such filings because they are costly, complex, time consuming, and not predictable. Some have also postulated this, in part, may be due to the elevator being less concerned about the reasonableness of grain rail rates than they are with their own competitiveness in relation to surrounding elevators and concerns regarding railroad retribution should they challenge rail rates. In addition, grain elevators may have less incentive than producers to negotiate rates with railroads in situations where they are able to pass cost increases through to agricultural producers.

Thus, the rate challenge processes proffered by all parties in this proceeding should seek to be inclusive of both grain elevators and agricultural producers (hereafter, collectively referred to as agricultural shippers). A system for challenging rail rates believed to be unreasonable is more likely to be successful when the different financial resources, impacts, and concerns of all interested parties are accommodated.

Agricultural shippers need specially designed rail rate challenge procedures. Shipping agricultural products is unique because of the many origin-destination pairs and routes that change frequently with changing markets. Although considerable volumes of agricultural products are shipped by rail, these volumes do not compare to that of coal and chemical shippers that have dedicated routes. Therefore, the current rail rate challenge procedures are of little value to agricultural shippers.

Current Rate Appeals Procedures

There are three rate appeals procedures currently available through the Board, varying in complexity and cost. None of them are appropriate for the average agricultural shipper, which we demonstrate in the following sections.

The Board's current rate challenge procedures involve three prerequisites. First, the Board determines if the rate contested produces revenues that exceed 180 percent of the movement's variable costs. If intermodal competition exists, the Board has no authority to review the rate challenge, even if the revenues exceed 180 percent of the variable costs of providing the service. The burden of proof is on the shipper to show that there is no effective form of competition. The second prerequisite for the Board's jurisdiction is that the contested rate must be a tariff rate and not a contract or exempt rate. The third prerequisite is whether the specific rail carrier has market dominance over the transportation to which the rate applies.[4] Market dominance is

[4] 49 U.S.C. 10701(d)(1).

defined as an absence of effective competition from other rail carriers or other modes of transportation for the movement to which the rate applies.[5]

If the three conditions are met, the Board may then consider if a common carrier rate is unreasonable, via appropriate tests. If the Board ultimately determines the challenged rate is unreasonable, it will order the railroad to pay reparations for past movements, and prescribe the maximum rate the carrier is permitted to charge for future movements.[6] However, the Board may not set the maximum reasonable rate below the level at which the railroad would recover 180 percent of its variable costs of providing the service. By law, the Board must recognize that rail carriers should have an opportunity to earn "adequate revenues," defined as those sufficient, under honest, economical, and efficient management, to cover operating expenses, support prudent capital outlays, repay a reasonable debt level, raise needed equity capital, and otherwise attract and retain capital sufficient to provide a sound rail transportation system.

The first procedure is known as the Coal Rate Guidelines, which uses the Stand-Alone Cost (SAC) test. Under the SAC test, a shipper has to design an optimally efficient, hypothetical railroad to serve the traffic that includes the route used by the shipper. The shipper then develops a hypothetical rate used to judge the reasonableness of the actual rate being charged. This hypothetical rate simulates the rate which would prevail in a competitive market. The costs and complexity involved with a SAC test make it inaccessible to all but the biggest shippers who must pay, on average, $5 million or more to litigate such a case.[7] The SAC test is used almost entirely by coal and chemical shippers, and is too costly and complex for grain shippers.[8]

The second procedure was designed by the Board for medium-size rate disputes. It is known as the Simplified-SAC test, which is a scaled-down version of the original SAC test that uses simplifying assumptions to judge the reasonableness of the challenged rate. Though it is less expensive than the SAC procedure, the Simplified-SAC procedure still requires more than $2 million in legal and consulting costs to pursue.[9] U.S. Magnesium, a producer of chlorine, is the only firm to file a rate complaint using the Simplified-SAC procedures, but settled the case before a Board decision was rendered.[10]

The third procedure, known as the three-benchmark test, was designed by the Board as a less costly alternative to the SAC test to be used in small rate cases. With this test, the reasonableness of the challenged rate is determined by comparing the markup (difference between revenue and variable cost) for the challenged rate to three different comparable markups. This is designed to show whether the challenged rate markup is reasonable compared

---

[5] 49 U.S.C. 10707(a).

[6] 49 U.S.C. 10704(a)(1).

[7] U.S. Department of Agriculture and U.S. Department of Transportation, *Rural Transportation Study*, 2010.

[8] *McCarty Farms, Inc. v. Burlington Northern, Inc.*, 91 F.R.D. 486, 486 (D. Montana 1981) demonstrates the complexity and costs of appealing grain rail tariff rates using SAC procedures. This case took 17 years to decide, during which the methodology for determining the rate changed several times.

[9] Opening comments of U.S. Magnesium, at 8-11, October 23, 2012, STB Ex Parte 715, *Rate Regulation Reforms*.

[10] *U.S. Magnesium v. Union Pacific Railroad*, Surface Transportation Board (STB), NOR 42115 and NOR 42116. The cases were initiated on June 25, 2009 and terminated on March 24, 2010.

to other markups. The cost of appealing rail rates using the three-benchmark procedure ranges from $250,000 to $500,000,[11] and the limitation on rate relief is $4 million over a 5-year period.[12]

None of the current rail rate appeals procedures are suitable for agricultural shippers. The SAC and Simplified SAC procedures are much too costly, complex, and time consuming for agricultural shippers. Agricultural shippers do not move large enough quantities to justify the cost of these procedures. Additionally, by the time a decision could be rendered, the routes or rates may have changed to fit new agricultural market conditions, nullifying most of the benefits from winning the case.

In the case of the three-benchmark procedures, as will be shown later, only a small percentage of grain shippers ship enough volume to justify the cost. In addition, the three-benchmark rate challenge procedure does not determine whether a rate is unreasonable by considering railroad revenue adequacy. Therefore, the procedure is flawed because comparing the rate to other unreasonable rates could result in finding a rate that is reasonable when, in fact, it is unreasonable based upon the revenue adequacy of the railroad.

The Decision Making Process of Agricultural Shippers in Appealing Rail Rates

Given the financial resources of any shipper, there are three constraints on a shipper's decision whether to challenge rail rates: (1) the amount of the potential reward, (2) the costs associated with an appeal, and (3) the predictability of receiving a fair and rational judgment.

Under current rules, USDA postulates it is the latter two that are the binding constraints.

Reward Amounts

In Ex Parte 715, Rate Regulation Reforms, the Board raised the limits on relief for both of its simplified procedures, yet this change alone has not been sufficient to encourage agricultural shippers to make greater use of either procedure. Because of the simplified nature of the three-benchmark procedure, most shippers probably expect rate reductions ranging from 5 to 10 percent. Under the assumption of 10 percent, less than 1 percent of all grain elevators, based on Standard Point Location Codes (SPLC), incur enough rail transportation costs to qualify for the maximum reward of $4 million under the three-benchmark test (see table 1).[13] Therefore, further raising the reward amount is unlikely to encourage additional agricultural shippers to utilize the three-benchmark test. Instead, lowering the costs for and increasing the certainty of the rate-challenge process offer the most promise of encouraging wider use of the Board's procedures when warranted.

Costs

As the Board notes, since the McCarty Farms case was decided in 1997, no grain shipper has filed a rail rate challenge using any of the Board's processes, mainly because the procedures are too lengthy and expensive for virtually all agricultural shippers. Even the least costly appeals

---

[11] Opening comments of U.S. Magnesium, at 6-7, October 23, 2012, STB Ex Parte 715, *Rate Regulation Reforms*.

[12] STB Decision 42980, July 18, 2013, Docket No. Ex Parte 715, *Rate Regulation Reforms*.

[13] Total rail costs ($40,000,000) × rate reduction (.1) = Maximum reward ($4,000,000)

procedure, the three-benchmark test, is effectively priced out of reach for the vast majority of grain shippers. For example, assuming rate reductions ranging from 5 to 10 percent, a cost of $500,000 to file a three-benchmark appeal, and a 50 percent probability of success, an elevator would need to spend between $10,000,000 and $20,000,000 on rail transportation costs before considering a rate challenge.[14]

In table 1, 87 percent of elevators have rail grain transportation costs of less than $10,000,000.[15] That is, based on the cost of the rate challenge, the probability of success, and the expected reduction in rates, less than 13 percent of elevators would potentially be in a financial position to consider bringing a rail rate case using the three-benchmark test.[16] In addition, this may be an overestimate for the percentage of elevators that are in a financial position to bring a rate case. This is because more than one elevator may be located within a SPLC, effectively dividing the amount of revenue within a SPLC by the number of elevators. Furthermore, if 87 percent of grain-shipping elevators do not ship sufficient volumes in terms of revenue to appeal rail rates using the three-benchmark procedure, the individual agricultural producer—harmed most by excessive rail rates—has even less grain volume to support a rate appeal.

Table 1:

Origin SPLCs[1] by Expanded Grain Revenue, 2011

Expanded Revenue	Cumulative Percent of SPLCs
< $100,000	5%
< $200,000	13%
< $300,000	19%
< $400,000	24%
< $500,000	29%
< $1,000,000	41%
< $2,000,000	57%
< $3,000,000	65%
< $4,000,000	70%
< $5,000,000	75%
< $6,000,000	78%
< $8,000,000	83%
< $10,000,000	87%
< $20,000,000	97%
< $40,000,000	99%

[1] Standard Point Location Code

USDA analysis of STB Confidential Waybill Sample

Therefore, whichever rail rate challenge process the Board advances from this proceeding should not have costs in excess of $50,000 for the test to be a viable option for agricultural shippers, based on the underlying assumptions mentioned above. This represents an 80 to 90 percent reduction from the current estimated costs of the three-benchmark test. Table 2 shows the inverse relationship between the cost of the three-benchmark test and the percentage of grain elevators that would have sufficient resources to apply it. This demonstrates that the costs of the Board's processes stand as a formidable barrier against

[14] A necessary condition for a shipper to consider pursuing a rate appeal is that the expected value of such a decision would be greater than or equal to $0. Under a three-benchmark test, a shipper would need to have rail transportation costs of at least $10,000,000 in order to satisfy this condition, based on a cost of $500,000 to bring a case, a 0.5 probability of success, and an expected tariff reduction of 10 percent. The minimum amount of rail transportation costs (X) for the point at which a shipper becomes indifferent to filing a rate appeals case can be found by solving the expected value, E(V), equation: $E(V) = .5(.1X - \$500{,}000) + .5(-\$500{,}000) \geq 0$, where X=$10,000,000. By decreasing the expected tariff reduction to 5 percent, the minimum amount spent on rail transportation costs (X) increases to $20,000,000. Essentially, a shipper will not file a rate appeals case when the rail transportation costs are less than X, but may consider doing so at any point X or greater.

[15] The SPLC is not necessarily unique to a single shipper. Consequently, a single SPLC may have more than one elevator loading grain to rail.

[16] USDA does not have access to the financial position of grain elevators and is using the revenue spent on rail transportation as a proxy to demonstrate that it is likely that very few would have the financial ability to appeal rates with the current costs.

challenging rail rates for small shippers, even when the limits on relief are potentially unconstrained.

Table 2: Availability of Three-Benchmark Test to Grain Elevators based on Cost*

Cost of Using Three-Benchmark Test	Minimum Elevator Costs on Rail Transportation	Percentage Eligible Elevators
$500,000	$10,000,000	13%
$400,000	$8,000,000	17%
$300,000	$6,000,000	22%
$250,000	$5,000,000	25%
$200,000	$4,000,000	30%
$150,000	$3,000,000	35%
$100,000	$2,000,000	43%
$50,000	$1,000,000	59%
$25,000	$500,000	71%
$1	$20	100%

*Assuming a 50% probability of being awarded a 10% tariff reduction.

Predictability of a Fair or Rational Judgment

Finally, even with non-prohibitive costs and sufficient rewards, the perceived presence of unpredictability within the current rate-challenge system undermines the willingness of agricultural shippers to take part in that system. One study has shown that if governing processes are viewed as arbitrary instead of fair or rational, parties are encouraged to make greater use of litigation to solve disputes because they are more likely to result in "windfalls."[17] In essence, a railroad or shipper may believe there is a chance the Board may arbitrarily find an "unreasonable" rate to be "reasonable," and vice versa.

However, under the perception of arbitrary decisions, if one party believes the other has a greater chance of prevailing in any given proceeding, that party's willingness to initiate a proceeding will be reduced accordingly. In contrast, the willingness to use litigation to settle disputes increases for the opposing party. Merely the perception of bias is sufficient to produce this outcome, whether any bias actually exists. For example, just by reducing a shipper's expectation from 50 to 40 percent of the probability of receiving a favorable decision while holding all other assumptions constant (a rate reduction of 5–10 percent and cost of $500,000 to file a three-benchmark appeal), the minimum amount of rail transportation costs a shipper would need to incur before considering an appeal rises from $10 million-20 million to $12.5 million-$25 million.[18] Thus, fewer rate appeals would be initiated, with shippers only willing to take financial risks over the most egregious appeals claims. This would add to shipper frustration, believing they essentially have no accessible or affordable recourse where only small abuses are perceived.

[17] Huneke, William. "A Game Theory Approach to Railroad-Shipper Negotiations." *Journal of the Transportation Research Forum* 45(1), (2006): 59-69.

[18] The minimum amount of rail transportation costs (X) can be found by solving the expected value, E(V), equation: $E(V) = .4(.1X - \$500,000) + .6(-\$500,000) \geq 0$, where X=$12,500,000. By decreasing the expected tariff reduction to 5 percent, the minimum amount spent on rail transportation costs (X) increases to $25,000,000.

Any newly proposed processes or amendments to existing ones are likely to be met with skepticism by agricultural shippers if they believe these new processes will be characterized by unpredictability and subject to increasingly unobtainable preconditions.

Past Board decisions have had this effect to some degree as noted through shipper reactions; believing new rules further shut the window to rate relief access even more.[19] If this pattern continues, a shipper's diminishing belief in receiving a favorable decision continues to reduce his/her likelihood for bringing a rate case, despite reductions in the costs or increases in the rewards of the process.

Therefore, USDA encourages the Board to purposefully seek simplicity, practicality, and predictability in whatever alternative rate relief methodologies are specifically developed for agricultural shippers and their unique needs.

New Procedures

USDA believes the most promising ways for the Board to encourage greater use by agricultural shippers of its new rate challenge procedures for agricultural shippers are through: (1) significantly lowering the costs associated with the procedure, and (2) demonstrating a commitment to a predictable set of outcomes through the development of a process that is simple to use and easy to understand, preferably formula-based using data that is easy to obtain and deterministic in nature. USDA believes the Board needs to consider an entirely new approach for captive grain shippers to challenge rail rates they believe are unreasonable, rather than through modifications to the three existing systems. Doing the latter would result in an outcome that remains complex, costly and highly litigious, and would not be helpful or used by agricultural shippers.

USDA offers the following sections as concepts for potential consideration as the Board considers its options in the development of new rate complaint procedures for agricultural shippers.

Revenue Adequacy and the Future of Railroad Regulation

As the railroad industry attains or approaches the point of revenue adequacy, the Board, shippers, and railroads need to think about how the regulatory landscape should change under this condition. It is conceivable a new set of rules governing rail rates for captive grain or the rate challenge process for grain movements could be formulated that incorporate railroad revenue adequacy. If a railroad is revenue adequate, USDA believes the Board should take this into account in conjunction with whatever new mechanisms it establishes for agricultural shippers.

---

[19] Notable examples include: *McCarty Farms, Inc. v. Burlington Northern, Inc.,* 91 F.R.D. 486, 486 (D. Montana 1981) took 17 years to decide, during which the methodology for determining the rate changed several times; Docket No. 42071, January 27, 2006, *Otter Tail Power Company v. BNSF Railway Company*, wherein the STB used a new test, the "cross-subsidy test," adopted after Otter Tail filed its complaint to deny relief; Shipper responses to STB Decision in Docket No. 42123, September 27, 2012, *M&G Polymers USA, LLC v. CSX Transportation, Inc.*, which proposed a new standard for market dominance.

Facilitate Group Action and State Involvement

The Board could also amend its rate challenge procedures in order to facilitate groups of agricultural producers, groups of elevators, or State Attorneys General to act on behalf of agricultural producers in that State. Such collective action would increase the ability of individual shippers to access the Board's rate challenge procedures, who might otherwise not be able to initiate such a challenge due to the prohibitive costs faced by a single shipper.

Mediation and Arbitration

While perhaps somewhat outside the intended scope of this proceeding, USDA believes another approach to the Board's formal rate challenge processes that could be more fully utilized is private-sector mediation and arbitration. Such systems, if broadly utilized by the Nation's shippers and railroads, could offer agricultural shippers greater access to rate dispute-settlement mechanisms that have a reputation of being fair, easily understood, accessible, and affordable. Examples of these types of arbitration systems that already exist include: the National Grain and Feed Association's (NGFA) rail arbitration system, and the Montana-BNSF mediation/arbitration system.[20] Yet, these systems have not been broadly used for rate disputes because railroads have generally not been willing to arbitrate rates. Also, the scope of these systems cannot handle all agricultural rate disputes because the NGFA system requires that at least one of the parties in a case be an NGFA member. Meanwhile, the Montana system is limited to only one State and one railroad and only for wheat and barley. Nevertheless, they serve as good examples of how such systems can effectively resolve disputes and foster good business relationships.

As a practical way to advance fairness for agricultural rate disputes, USDA believes the Board should encourage railroads to participate in rate disputes through these types of systems. The Board should also assist in facilitating the expansion or creation of these types of systems, as USDA believes mediation and arbitration could be the most promising and viable procedures for the average agricultural shipper who may not have the disposition, inclination, or time and money for a formal process, regardless of its design or merits.

Mediation is an informal process in which the parties discuss issues in dispute with a mediator who assists them in resolving the dispute. The outcomes of mediation are not binding. Arbitration is a relatively informal process that is generally binding on the parties, in which the parties in a dispute present written and/or oral arguments before an arbitration panel of neutral qualified third-party arbitrators with expertise in the subject matter of the dispute.

USDA believes arbitration involving grain-shipper rail-rate challenges would operate most effectively with a panel of three arbitrators who collectively have strong backgrounds in arbitration procedures, grain merchandising, and rail transportation. A panel of three arbitrators is generally preferred because it improves the likelihood of well-reasoned opinions, enhances the balance and fairness with which the system is viewed, and reduces the potential for inadvertent errors. The quality of the decisions in arbitration is strongly dependent on the objectivity and

---

[20] For a more detailed description of these arbitration systems see: http://www.ams.usda.gov/AMSv1.0/getfile?dDocName=STELPRDC5106990

qualifications of the selected arbitrators. All of these reasons are especially important given that there are limited rights for court appeals under arbitration.

Unlike a court case, an arbitration decision does not set precedent. However, by agreeing to participate in arbitration, the parties agree to be bound by the arbitral decision with limited appeals rights. Thus, a desirable arbitration agreement would provide for an appeals process that broadly allows either party to appeal an arbitrated decision in addition to necessary instances involving a clear abuse of an arbitrator's authority or discretion. Without an effective avenue for appeal within the arbitration agreement, parties may not be as willing to enter arbitration proceedings because the court system generally will not vacate arbitration decisions. When an arbitration appeal to the court system occurs, the appellate court will typically look at the process of arbitration and the way in which the rules of law were applied to determine whether the proceeding was fair, but will generally not alter the arbitrator's finding of facts or decision unless impropriety, such as clear arbitral bias, is present.

If parties are to make use of an arbitration system, there must be assurances of fairness, neutrality, and openness to foster an atmosphere of trust. Publishing the decisions—excluding proprietary and confidential business information—is essential for providing transparency, building trust in individual arbitrators, and demonstrating a commitment to neutrality. In addition, publicly published decisions can discourage extreme positions, encourage voluntary settlement, and create incentives for arbitrators to render thoughtful, well-reasoned decisions. Arbitration processes that are perceived as accessible and fair by both parties are also likely to encourage the parties to try to resolve the dispute through direct discussions, thereby preserving business relationships.

A major benefit of arbitration is that it has the potential to offer less time-consuming and lower-cost rail-rate challenge procedures than the formal Board processes. One of the most important aspects of arbitration is the direct business discussions it encourages, facilitating informal mediation of many issues before they require more formal arbitration. The Montana-BNSF Railway arbitration system only charges each party an initial $400 case management fee to initiate a case. Additional fees are determined by the fee schedule of the administering body, the Judicial Arbitration and Mediation Services (JAMS). JAMS is a national-scope provider of private dispute resolution services. Its non-profit foundation encourages the use of alternative dispute resolution (ADR), supports education at all levels about collaborative processes for resolving differences, promotes innovation in conflict resolution, and advances the settlement of conflict.

Similarly, the Board and NGFA have arbitration systems for resolving commercial disputes between shippers and participating railroads. The Board's recently established arbitration system is restricted to disputes regarding service issues and ancillary railroad fees. The NGFA arbitration system, established in the late 1890s, has a long history of successful resolution of disputes, but requires the approval of both parties before rate disputes can be arbitrated. Thus far, none of the Class I railroads have agreed to arbitrate rail rates under the NGFA system. The fee structure for NGFA rail arbitration is:

Up to $100,000 claim	$400, plus 1% of the claim
$100,001 to $500,000 claim	$900, plus ½% of the claim
More than $500,001 claim	$2,150, plus ¼% of the claim
Any claim	Maximum fee of $10,000

However, the fees cited in these examples do not include the possible costs of a consultant and/or lawyer that the parties may decide to use to help prepare the case.

Montana-BNSF Mediation/Arbitration System

The mediation/arbitration system between producers in Montana and the BNSF Railway is the only one that has been used thus far to mediate or arbitrate rail rates. This is the first time a Class I railroad has agreed to a system of mediation and arbitration of rail rates. BNSF does not have any current plans to enter into other bilateral arbitration agreements, but it has said that it is open to reviewing and discussing other voluntary arbitration proposals.

The Montana-BNSF mediation/arbitration system was started January 30, 2009 and is conducted through the Montana Grain Growers Association (MGGA) and the Montana Farm Bureau Federation (MFBF). It is administered by JAMS and modeled after the NGFA's arbitration rules. The Montana-BNSF arbitration system uses three mutually agreed-upon arbitrators drawn from a pool of eligible arbitrators. If the parties cannot agree on three arbitrators, the claimant chooses one, BNSF chooses one, and the remaining arbitrator is chosen by both parties.

The system is unique in that it allows grain producers, rather than the grain elevator shipping the grain, to make claims. Eligibility is limited to those producers shipping wheat or barley more than 250 miles on BNSF and is restricted to shipments having a revenue-to-variable cost ratio (R/VC) higher than 180 for non-shuttle shippers and R/VC higher than 195 for shuttle shippers. The R/VC is determined using the Board's Uniform Rail Costing System.

Arbitrators are also limited to ruling on the tariff rate, not on the fuel surcharges or other accessorial charges that can add significantly to the cost of rail service. The fuel surcharge, however, is included in mediation discussions. Finally, relief would not be granted in the event a truck rate is lower than the BNSF rate, even though the truck rate would be uneconomic over longer distances or the lower price may be given only when the trucking firm needs a backhaul. Any relief obtained by the producer is effective for no more than 1 year from the award and fourteen months prior to the commencement of the arbitration process.

In December 2009, a case filed by a Shelby, Montana, producer was successfully mediated. The rate at issue was for wheat shipments from Shelby to export facilities near Portland, Oregon. A majority of Montana's wheat crop each year is loaded on vessels at the mouth of the Columbia River, and nearly all is transported from origin to destination by BNSF. As a result of this mediation, BNSF lowered the rail rate by $165 per railcar (about 4.5 cents per bushel). In addition, BNSF reduced rates, to a smaller extent, for shuttle loaders east of Shelby and on its Northern line in order to preserve current market relationships among elevators.

Conclusion

USDA believes the most promising methods for ensuring the Board's rate complaint procedures are accessible to grain shippers and provide effective protection against unreasonable rail transportation rates will be those that address cost, timeliness, and predictability. USDA also believes that whatever new set of rules are established for challenging grain rates, they should be formulated to account for railroad revenue adequacy.

In addition, USDA suggests the Board actively encourage railroad participation in existing private-sector mediation and arbitration systems for rate disputes and perhaps inspire the development of new and more broadly used private systems, as they may produce the best results given the unique qualities of agricultural shippers.

Finally, USDA reiterates that regardless of the methods advanced from this proceeding, they should be accessible to both grain shippers and agricultural producers.

Respectfully submitted,

for Edward Avalos
Under Secretary
Marketing and Regulatory Programs
U.S. Department of Agriculture
Washington, D.C. 20250

CERTIFICATE OF SERVICE

I, Bruce Blanton, certify that on this 26th day of June, 2014, caused a copy of the foregoing document to be served by first-class mail, postage prepaid, on all parties of record in STB Docket Number EP 665 (Sub-No. 1).

Bruce Blanton
Director
Transportation Services Division
U.S. Department of Agriculture
Washington, D.C. 20250