

BEFORE THE  
SURFACE TRANSPORTATION BOARD

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STB Ex Parte No. 711 (Sub No. 1)

*RECIPROCAL SWITCHING RULES*

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**COMMENTS OF  
THE DOW CHEMICAL COMPANY**

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241902

ENTERED  
Office of Proceedings  
October 26, 2016  
Part of  
Public Record

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Dated: October 26, 2016

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The Dow Chemical Company (“Dow”) hereby submits these opening comments in response to the Notice of Proposed Rulemaking (“Notice”) served by the Surface Transportation Board (“STB” or “Board”) in the above-captioned proceeding on July 27, 2016. Dow is a member of the American Chemistry Council (“ACC”) and fully supports the opening comments jointly submitted by ACC, the National Industrial Transportation League, and other interested parties in this proceeding (the “Shipper Coalition”). Dow comments separately for the purpose of emphasizing those issues of greatest concern to it and to bolster those comments with examples from Dow’s own experience.

**I. Identity and Interest of Dow.**

Dow is a diversified chemical company that harnesses the power of science and technology to constantly improve what is essential to human progress. Dow offers a broad range of innovative products and services to customers in more than 175 countries, helping them to provide everything from fresh water, food, and pharmaceuticals to paints, packaging, and personal care products. In order to provide many of these essential products and services, Dow makes significant use of rail transportation. The broad range of products that Dow produces

span virtually every industry, including railroads, and make possible approximately 90% of the goods people use every day.

Dow's major manufacturing sites in the United States are located in Texas, Louisiana, Michigan, California, and West Virginia. These sites, and others around the country, are dependent upon railroads for the safe, secure, reliable, and economic transportation of raw materials and products. Some of these facilities, or select movements to and from them, may be eligible for reciprocal switching under the proposals in the Notice. Dow anticipates that reciprocal switching will create greater rail competition that will benefit Dow, its customers, and the overall public interest.

Although Congress included the reciprocal switching provisions of the statute in the Staggers Act of 1980, which substantially deregulated the rail industry, the Board, and the Interstate Commerce Commission ("ICC") before it, have imposed standards far in excess of those in the statute itself. As a consequence, no entity has successfully requested reciprocal switching since that time and none have bothered even to try for over 25 years. This has remained the case despite a national rail transportation policy "to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail...." 49 U.S.C. 10101(1); *see also*, 49 U.S.C. 10101(4) & (5) (to ensure "effective competition" among rail carriers). During the past 36 years, the agency has given greater weight to other rail transportation policies focused upon the revenue adequacy of rail carriers. *See*, 49 U.S.C. 10101(3), (4) & (5). The Notice correctly recognizes that the time has come for the Board to take a more balanced approach towards implementing the "effective competition" and "revenue adequacy" rail transportation policies.

## II. **The Board Must Avoid The Cost And Complexity Of Rate Cases.**

While Dow generally supports the Board's proposed standards for reciprocal switching, it harbors concerns that those standards not devolve into complex, costly, and lengthy proceedings. Dow supported the original League proposal, which examined a series of factors that, if satisfied, would create a conclusive presumption of eligibility to use reciprocal switching, subject only to challenge by a rail carrier on grounds of feasibility, safety, or harm to other customers of the railroad. The League chose those factors to identify the most obvious candidates for reciprocal switching without an expensive and lengthy proceeding. Other shippers who did not meet the factors for a conclusive presumption still could request and obtain reciprocal switching upon making a more detailed evidentiary showing. In the Notice, however, the Board has declined to follow the League's approach and, instead, proposes to require that all shippers submit a more detailed evidentiary showing. This is the root of Dow's concern.

Dow has watched what has occurred to rate cases over the past 36 years since the Staggers Act. The Board initially adopted stand-alone cost ("SAC") in *Coal Rate Guidelines* as the standard for rate reasonableness in unit train coal cases. There clearly was no regard for non-coal, carload traffic at that time. While SAC cases were complex from the outset, they became much more so with time, as new issues piled upon old issues and the Board continued to modify its standards and procedures through rulemakings and case-by-case determinations. SAC cases now cost millions of dollars and require several years to litigate. In the interim, the Board spent more than a decade struggling to develop simplified standards for small rate cases. When the Board finally did issue simplified standards, non-coal shippers tested them out a few times and promptly abandoned them as meaningless and still too costly. More recently, several non-coal shippers have attempted to bring cases under the SAC standard for coal unit trains. Despite proving market dominance for the overwhelming majority of movements in those cases, and

demonstrating R/VC ratios among the highest in the rail industry, those shippers ran head-on into the most expensive and complex SAC cases ever litigated before the Board and still could not demonstrate unreasonable rates to the Board's satisfaction. Reciprocal switching will be just as meaningless if the Board does not take precautions right now to ensure an efficient and expeditious process and to defend that process against the excesses that plague rate cases.

Dow understands that the Board has general concerns regarding the potential breadth and scope of reciprocal switching upon rail revenue adequacy and service to shippers without reciprocal switching. This is uncharted territory for the agency. A case-by-case approach enables the Board to control the pace of implementation and monitor the effects of reciprocal switching so that it can make adjustments as it deems necessary or appropriate to balance the needs of all stakeholders. Dow submits that the Board still can do this with rebuttable presumptions, clearly delineated discovery, and expedited procedures.

The Board should begin by clearly allocating the burden of proof for each of the various factors in a reciprocal switching case to the party asserting that factor in favor or against switching. This is of particular concern for the "practicable and in the public interest" standard where the Board has articulated seven non-exclusive factors plus the fifteen statutory rail transportation policies as relevant considerations. Several of those factors are likely to be argued only by shippers (*e.g.*, new market access, service quality, amount of traffic) and other factors only by railroads (*e.g.*, capital investment, employee impacts, rail network impacts). A shipper should not bear both the burden of affirmatively proving the former set of factors and the burden of proving there is no impact on the latter factors. Rather, the shipper should prove the former and the railroad the latter, to the extent either chooses to rely upon those factors. In addition, the Board should place upon the incumbent rail carrier the burden of proving that the proposed

switching is not feasible, is unsafe, or will unduly hamper the incumbent's ability to serve other shippers.

The Shipper Coalition has offered several proposals to streamline the discovery and evidentiary procedures for reciprocal switching which Dow supports. This includes a 210 day procedural schedule from the filing of a petition until an STB decision. To meet that schedule, both parties must make certain binding disclosures with their initial filings and discovery will be limited to those initial allegations absent good cause. For example, to expedite a reciprocal switching case under the "practical and public interest" prong and to avoid needless discovery and evidentiary presentations, the Board should require both parties to identify the factors upon which they intend to rely in their initial pleadings and restrict discovery to those factors. This is essential to keep discovery, which is the source of much expense and delay, within manageable proportions.

A streamlined and expedited approach also is critical because reciprocal switching cases may need to be conducted in two phases. First, there is the question of whether reciprocal switching should be required at all. Second, if reciprocal switching is required, there may need to be a second phase to determine reasonable conditions and compensation if the rail carriers cannot agree or if the shipper believes that the agreed-upon conditions and/or compensation are unreasonable. The Shipper Coalition's proposed schedule includes 210 days for just the first phase. While the second phase might not be necessary, if it is, it too must be expedited and far shorter than 210 days (*e.g.* 90 days).

It is worth noting that, for terminal trackage rights, which is a sister provision to reciprocal switching in 49 U.S.C. 11102, Congress mandated that the Board complete that proceeding within 180 days. 49 U.S.C. 11102(d). This is a useful guide for the Board to follow

in this proceeding. The terminal trackage rights subsection contains the same “practicable and in the public interest” standard as reciprocal switching and the Board has proposed to adapt the same methodology it uses to prescribe trackage rights fees for the prescription of reciprocal switch rates. In other words, there is nothing inherently more complex or involved for reciprocal switching cases than for terminal trackage rights cases that requires more time to complete.

Dow stresses the need to avoid a process that results in reciprocal switching cases that are just as onerous as rate cases. The Board must not allow a case-by-case approach to become unwieldy over time, as has happened with rate cases. That would not be a meaningful regulatory remedy.

### III. **Guidelines For Defining “Reasonable Distance.”**

For both of the proposed reciprocal switching standards, the Board has included the criteria that “there is or can be a working interchange between the Class I carrier servicing the party seeking switching and another Class I rail carrier within a reasonable distance of the facilities of the party seeking switching.” Notice at 18 & 19. The Board has invited comments on guidelines it may provide to parties on the definition of “a reasonable distance.” *Id.* at 21. Dow supports the Shipper Coalition comments on this subject, and comments separately to provide some real-world context.

Dow operates a major plant at Taft, Louisiana that is captive to the Union Pacific Railroad (“UP”). A substantial amount of Taft traffic is gateway traffic that UP interchanges with the Canadian National (“CN”), Norfolk Southern (“NS”), and CSX Transportation (“CSXT”). Although Taft is less than 30 miles west of New Orleans, where UP interchanges traffic with each of these Class I railroads, UP provides local train service to Taft from its Livonia yard, which is approximately 85 miles north of Taft, and then places this traffic on road trains headed north to other UP gateways with these carriers. UP does not interchange traffic at

Livonia with other carriers. A very small portion of Taft's gateway traffic currently interchanges at New Orleans, which represents traffic destined to NS and CSXT customers in the southeast for which UP does not have a longer haul.

Reciprocal switching for Taft would allow Dow greater routing flexibility for its gateway traffic by opening routes through New Orleans if Dow could obtain better rates and service from CN, NS or CSXT, allowing them to handle these joint line movements over greater distances. In other words, reciprocal switching could create competition for all of the UP route except the 30 miles from Taft to New Orleans, for which Dow would pay a switch fee. This enhanced competition creates the potential for better service at more efficient rate levels.

UP's desire to maximize its long-haul for Dow's gateway traffic may explain UP's decision to serve Taft out of Livonia rather than New Orleans. Nevertheless, UP still must and does route a small portion of the Taft gateway traffic to New Orleans for lack of a longer haul on those particular movements. Reciprocal switching would enable Dow to route more of its gateway traffic from Taft to New Orleans if it made competitive sense for Dow to do so.

Because UP already transports Dow traffic from Taft to New Orleans for interchange, this would be an example of a reasonable distance, as described in the Shipper Coalition comments, since a reciprocal switch does not require UP to change its operations. UP could choose to handle this additional New Orleans interchange traffic in the same manner as it handles the Taft traffic that UP currently interchanges at New Orleans. Of course, if the shifting volume lends itself to a different, more efficient operation between Taft and New Orleans, UP would be free to implement that operation. In an actual reciprocal switching case, UP also could argue the infeasibility, safety, and service issues that comprise the fourth criteria proposed by the Board. But that is different from the question of a reasonable distance.

#### IV. **Market Dominance Standard.**

The Shipper Coalition has asked the Board to clarify that, under the “necessary to provide competitive rail service” prong, the Board will evaluate market dominance based upon the incumbent carrier’s existing bottleneck segment rather than the whole-route on a joint line movement. Dow supports that clarification and comments separately to provide a real-world illustration of the pit-falls with a whole-route approach.

As discussed in the preceding section, Dow operates a plant at Taft, Louisiana that is within 30 miles of a working interchange at New Orleans. Some of the gateway traffic that would be a candidate for reciprocal switching currently moves in joint line service on UP to East St. Louis, where UP interchanges with NS and CSXT, which deliver Dow’s traffic to locations throughout the mid-Atlantic and northeast. Regardless of the ultimate NS or CSXT destination, this traffic travels the precise same UP route and UP charges the same rate for the same commodities. A whole-route market dominance determination, however, conceivably could produce different results depending upon the ultimate destination beyond the UP bottleneck. This makes no sense.

Another example of nonsense created by a whole-route approach to market dominance involves rail transportation of polymers. Dow stages many of its polymers at transload facilities that serve multiple customers in the surrounding region. A whole-route market dominance approach must include rail transportation to the bulk terminal and truck transportation to the ultimate customer. But neither Dow nor the railroad typically knows who is the ultimate customer when Dow tenders the rail car. Furthermore, Dow may supply multiple customers from the contents of a single rail car, which could result in different market dominance determinations for the exact same rail movement. Lastly, the Board could not calculate quantitative market dominance when the whole-route includes non-rail modes.

V. **Class II and III Rail Carriers.**

The Board has proposed “to limit the availability of reciprocal switching prescriptions to those situations that only involve Class I rail carriers due to the lack of specific information on this matter and the concerns raised by ASLRRRA.” Notice at 20-21. As noted by the Board, the ASLRRRA asserted that the Board “should expressly limit the application [of reciprocal switching] to situations in which no Class II or Class III railroad participates at any point in the movement of the traffic whether or not the small railroad appears on the waybill.” *Id.* at 20 (*quoting* ASLRRRA Reply at 1-4) (underline added). But as the underlined text demonstrates, it would prohibit reciprocal switching for any movement involving a Class II or III railroad anywhere in the route even if that railroad is not the incumbent carrier that is the subject of the reciprocal switch request. Dow objects to this unduly broad prohibition.

Dow does not believe that is the Board’s intent. The actual text of the regulation proposed by the Board at 1145.2(a)(1)(i) and (2)(i) focuses upon whether the facilities for which switching is sought are served by a Class I rail carrier. The final rule should more closely resemble the proposed regulatory text rather than the ASLRRRA comment.

However, Dow also objects to applying the restriction even when a Class II or III rail carrier is the alternate carrier as opposed to the incumbent. The Board states that, “[u]nder both prongs of the proposed regulations, prescriptions of reciprocal switching would be limited to instances in which both the incumbent railroad and the competing railroad are Class I carriers.” Notice at 20 (underline added). Neither ASLRRRA nor the Board has articulated a reason as to why a Class II or III rail carrier should not be allowed to provide rail service as the competing railroad in a reciprocal switching arrangement. Again, the text of the proposed rules does not apply the restriction as broadly as the narrative discussion quoted above suggests. Dow urges the Board to follow the text of the proposed rule over the restriction described in the narrative.

Finally, Dow is concerned that the restriction creates problems even when the Class II or III railroad is the incumbent carrier. There conceivably are situations where, to immunize or exempt a major customer's facility from reciprocal switching, a Class I rail carrier might opt to divest a rail line to a Class II or III railroad. That sort of "gaming" should not be permitted. Recently, NS leased several lines in West Virginia to a new Class III rail carrier, the Kanawha River Railroad ("KNWA"). See Kanawha River Railroad, L.L.C. – Lease Exemption Containing Interchange Commitment – Norfolk Southern Railway Company, STB Docket No. 36028 (served July 15, 2016). Dow owns a facility on that line at Institute, West Virginia. Moreover, that facility is reasonably close to an interchange with CSXT, thus making Dow's facility a potential candidate for reciprocal switching but for this recent lease to a Class III rail carrier. While Dow is not suggesting that NS entered into this particular transaction to avoid reciprocal switching, Dow points to this recent transaction as a real-world example of how a rail carrier might "game" the shortline exemption. Therefore, Dow urges the Board to accept and evaluate challenges to the shortline exemption on a case-by-case basis and to refuse to apply the exemption when it believes such gaming may have occurred.

#### **VI. Definition of a "Working Interchange."**

Dow supports the Board's proposal that there "is" a working interchange if one already exists and is currently engaged in switching operations. Notice at 21. However, the Board's determination of whether there "can be" a working interchange is unduly narrow. Specifically, the Board proposes that "there 'can be' a working interchange only if the infrastructure currently exists to support switching, without the need for construction, regardless of whether switching operations are taking place or have taken place using that infrastructure." *Id.* This situation could arise in various scenarios, such as when the incumbent claims to have insufficient yard capacity to handle the additional switch traffic or the change in traffic flow, or when an

interchange location only has sufficiently long tracks to interchange manifest traffic but not unit train switch traffic. If and when the incumbent carrier proves that those or comparable situations exist, either the shipper or the alternate carrier should have the option of paying for the necessary infrastructure enhancements to provide reciprocal switching. In those situations, the Board should determine that there “can be” a working interchange.

## VII. **Access Price**

Absent a reasonable switch fee, reciprocal switching is a meaningless regulatory remedy. The fee must be reasonable and there must be an economic and expeditious process for determining a reasonable fee in the absence of agreement. A reasonable charge should provide no greater compensation to the incumbent than is necessary for it to recover the variable cost of its switching operation, a proportionate share of the fixed costs, and a reasonable return. An alternate carrier with a comparable or better cost and/or routing structure to the incumbent should be able to compete effectively. As a general matter, Dow supports the Shipper Coalition comments with respect to the methodology for determining the access price. In these comments, Dow raises certain corollary issues of substantial importance.

First, Dow stresses its complete objection to including “lost contribution” in the access fee. Notice at 25. This concept, also known as efficient component pricing (“ECP”), was suggested by UP. If the Board were to adopt ECP, it would completely undermine the very objective of reciprocal switching by setting an access fee that effectively ensures the shipper will pay the same price for the full origin to destination movement regardless of which carrier it uses. The recently released InterVISTAS report to the STB on freight rail rate regulation reflects Dow’s objections to ECP, when it acknowledges that ECP “can perpetuate the unreasonable exercise of market power by the incumbent carriers” and notes that other federal agencies have

rejected ECP because it “enables incumbent carriers to recover their full opportunity costs, including any monopoly profits.”<sup>1</sup>

Second, Dow urges the Board to clarify that it will use the same standard for setting access fees for both disputes between the incumbent and alternate rail carriers and between the shipper and incumbent rail carrier. The reciprocal switching statute provides for the STB to set compensation “if the rail carriers cannot agree...within a reasonable period of time.” 49 U.S.C. 11102(c)(1). Conceivably, the two rail carriers may reach agreement upon an access fee that the shipper believes is unreasonable and non-competitive. The shipper undoubtedly has a right to challenge that rate under the statute. It would be arbitrary to apply a different standard for the access fee based solely upon the status of the challenger as a shipper or another railroad.

Finally, the STB should adopt a short, 15-day, time period for the incumbent and alternate carrier to agree upon the access fee. After that time has elapsed, the shipper should have a right, but not the obligation, to ask the Board to set the rate. That way, if the shipper is persuaded that the two rail carriers are making progress, it could elect to allow that process more time without waiving its right to invoke the STB’s jurisdiction if and when negotiations subsequently stall. Without a defined time period, a shipper could be deprived of the benefits of a reciprocal switching order for months or even years while waiting for the rail carriers to agree upon term in a process over which the shipper has no input or control.

#### **VIII. Conclusion.**

Dow commends the Board for its determination that the time has arrived to revisit its longstanding and seldom-used reciprocal switching standards. Generally, Dow supports the direction of the Board’s proposed changes. However, Dow strongly cautions the Board against a

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<sup>1</sup> InterVISTAS Consulting Inc., “An Examination of the STB’s Approach to Freight Rail Rate Regulation and Options for Simplification,” Project FY14-STB-157, pp. 109 & 110 (Sept. 14, 2016).

case-by-case approach that is overly complex, lengthy and expensive. Therefore, Dow supports the modifications offered by the Shipper Coalition and as elaborated upon in the foregoing comments.

Respectfully submitted,



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October 26, 2014

**CERTIFICATE OF SERVICE**

I hereby certify that on this 26th day of October 2016, I served a copy of the foregoing upon all parties of record via U.S. first-class mail, postage prepaid.



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Jeffrey O. Moreno