

STB FINANCE DOCKET NO. 33726

WESTERN COAL TRAFFIC LEAGUE
v.
UNION PACIFIC RAILROAD COMPANY

Decided May 10, 2000

Board finds no basis for disturbing Union Pacific's accounting practice of including various merger and congestion-related expenses in carrier's rate base.

BY THE BOARD:

In this complaint, Western Coal Traffic League (WCTL) alleges that the Union Pacific Railroad Company (UP) in its 1997 Annual Report R-1 (R-1) improperly recorded certain expenses associated with widespread congestion on its Gulf Coast region lines and with its merger with the Southern Pacific Transportation Company (SP).¹ WCTL contends that these accounting errors serve to overstate the variable costs² of UP's 1997 services and requests that UP be required to restate its R-1. Upon considering the evidence and arguments presented,³ we find that UP's accounting practices were proper and in accordance with the Uniform System of Accounts (USOA) and generally accepted accounting principles (GAAP). Accordingly, we dismiss the complaint.

¹ *Union Pacific/Southern Pacific Merger*, 1 S.T.B. 233 (1996) (*UP/SP Merger*), *aff'd sub nom. Western Coal Traffic League v. STB*, 169 F.3d 775 (D.C. Cir. 1999).

² Under 49 U.S.C. 10707(d), we cannot examine the reasonableness of a rail rate if the revenues produced by that rate are less than 180 percent of the variable costs of handling the traffic involved, nor can we provide rate relief below that level. Accordingly, the effect of overstating variable costs would be to decrease the amount of traffic potentially subject to our rate reasonableness authority, and to limit the rate relief available for such traffic.

³ WCTL filed opening evidence and argument on May 5, 1999 (WCTL Open.); UP filed reply evidence and argument on May 25, 1999 (UP Reply); and WCTL filed rebuttal on June 9, 1999 (WCTL Reb.). The Association of American Railroads (AAR) filed a motion to participate as *amicus curiae*, on May 25, 1999, contending that the accounting issues raised could establish precedent that would affect all of its members. Because WCTL has not opposed AAR's request and AAR's participation will not expand the scope of this proceeding, we grant AAR's motion.

BACKGROUND

In its 1997 R-1, UP recorded various merger-related restructuring costs and congestion-related costs as ordinary operating expenses. UP also recorded SP pre-merger restructuring liabilities as liabilities that UP assumed when it purchased SP. These liabilities were considered as part of the purchase price for SP and, consequently, as part of the basis used to value SP's assets on UP's books.

WCTL argues that the congestion-related costs claimed by UP,⁴ along with \$235 million in UP restructuring (mainly labor-related) expenses,⁵ are one-time expenditures that should be reported as "unusual" or "infrequent" items⁶ in UP's R-1, in Schedule 210, Account 555.⁷ WCTL also argues that \$958 million in SP restructuring costs should not have been treated as liabilities that were, in effect, added to the SP purchase price, but instead should have been treated as unusual or infrequent post-merger expenses. Alternatively, WCTL requests that UP be required to identify the congestion and restructuring costs as "special charges" in notes to Schedule 410 of the R-1.⁸

DISCUSSION AND CONCLUSIONS

Historically, rail carriers have treated as ordinary expenses the congestion and restructuring expenses that WCTL seeks to have UP treat as unusual or infrequent expenses. In addition, carriers have generally treated the pre-consolidation restructuring expenses of an acquired carrier as an assumed

⁴ According to UP, the majority of the \$450 million in congestion-related costs that WCTL claims are at issue represents an estimate of lost revenues. UP states that the actual congestion-related expenses at issue total approximately \$197 million.

⁵ In footnotes to its accounts, UP indicates that it expects to have incurred \$235 million in restructuring costs through 1999, of which \$60 million was incurred in 1997 and reported in that year's R-1. These costs resulted from severing, relocating and training UP employees, rationalizing facilities, and upgrading equipment.

⁶ WCTL's witnesses sometimes use the terms "transitory," on the one hand, and "permanent," on the other, in their testimony, but in effect, their testimony focuses on whether the congestion and restructuring-related expenses are unusual or infrequent.

⁷ For an expense to be recorded as unusual or infrequent, the amount of the expense must be "material." 49 CFR 1201, Instruction (Inst.) 1-2(d)(2). However, because we find that the expenses at issue do not satisfy the other requirements necessary for classification as unusual or infrequent, we do not address whether they are so large as to be material.

⁸ WCTL's objective is to place the congestion-related and restructuring costs in accounts that it suggests should not be used to determine variable costs under our Uniform Railroad Costing System (URCS).

liability and part of the purchase price. Nonetheless, WCTL argues that the costs at issue here should have been treated, for accounting purposes, as unusual or infrequent expenses or alternatively as special charges. We agree with UP—whose records, we should note, have been audited by an independent accounting firm and found to be in accordance with GAAP—that the costs were recorded properly in the carrier’s accounts.

A. Unusual or Infrequent Expenses

The terms “unusual” and “infrequent” have specific accounting meanings. The parties agree⁹ that for an item to be classified as unusual under GAAP and our Uniform System of Accounts (USOA):¹⁰

the underlying event or transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity, taking into account the environment in which the entity operates.

They also agree¹¹ that to be considered infrequent:

the underlying event or transaction should be of a type that would not reasonably be expected to recur in the foreseeable future, taking into account the environment in which the entity operates.

1. *Congestion-Related Costs*

UP recorded as expenses certain costs, incurred to improve its service during 1997 and 1998, associated with borrowing cars from other carriers; hiring additional crews; obtaining additional locomotives; and repairing and maintaining its locomotive fleet. UP also included as expenses costs associated with customer claims that arose during the service crisis. WCTL takes the position that none of these expenses should have been recorded as ordinary operating expenses.

It is well understood that costs for car hire, crews, locomotives, and claims are normal costs of railroading, and that some costs in these categories would have been incurred even if there had been no service crisis. Yet, WCTL seeks to exclude all of these costs, on the ground that UP’s Gulf region service crisis

⁹ WCTL Open. Verified Statement (V.S.) Verrecchia/Sondhi at 8; UP Reply at 7.

¹⁰ The USOA is set forth at 49 CFR 1200-1201. “Unusual” and “infrequent” are defined at 49 CFR 1201, Inst. 1-2(d)(1).

¹¹ WCTL Open. V.S. Verrecchia/Sondhi at 8; UP Reply at 8.

qualifies as an unusual or infrequent event under GAAP and the USOA because the service crisis was markedly distinct and different from normal railroad congestion in both its intensity and its geographic scope. Although these types of railroad expenses have never been handled in this manner before, WCTL contends that the magnitude of UP's congestion-related costs requires treating these costs as unusual or infrequent.

We do not agree that any of the costs, let alone all of them, should be excluded. As UP notes, railroads regularly encounter service problems that increase operating expenses for long periods of time, but the expenses are not normally reported in Schedule 210, Account 555 as unusual or infrequent items.¹² Indeed, railroads operate in an environment in which operating and service problems resulting from a variety of causes are, unfortunately, not uncommon. The sometimes significant expenses resulting from such congestion, however, have not normally been considered to be either unusual or infrequent in an accounting sense.

WCTL argues that the scale of the service crisis requires that, in this case, we should diverge from the way in which congestion-related expenses have historically been viewed, by drawing a line separating "normal" expenses from those that are so large as to constitute "a difference not just of degree but of kind." *Amerada Hess Pipeline Corp. v. FERC*, 117 F.3d 596, 603 (D.C. Cir. 1997) (*Amerada Hess*). We do not agree. Even if such a line could be drawn in a way that would not be arbitrary, the USOA does not classify expenses on the basis of size. Indeed, as AAR points out, Accounting Principles Board Opinion No. 30 (APB-30), paragraph 22, provides that "[a]n event or transaction of a type that occurs frequently in the environment in which the entity operates cannot, by definition, be considered extraordinary, regardless of the financial effect."

In any event, WCTL's argument assumes that the congestion expenses represent a single accounting item attributable to a single event (UP's service crisis) that was of unprecedented magnitude in the rail industry. However, we do not see the service crisis as a single event for accounting purposes. As we

¹² As examples, UP points out that the washout of UP's Feather River Canyon line in 1997 interrupted service for several months and subjected the line to slow orders for an even longer period; that severe weather increased the operating expenses of The Burlington Northern and Santa Fe Railway Company (BNSF) in the first quarter of 1997 by \$50 million; that congestion problems on SP in 1995 led to increased expenses of \$35 million; that congestion problems on Conrail in 1994 contributed to increased operating expenses of some \$76 million; and that flooding in 1993 resulted in \$118 million in additional expenses to UP, SP and BNSF, and disrupted service for months. In each case, the additional expenses were recorded on the carrier's books as ordinary operating expenses.

have previously found,¹³ in addition to issues associated with the implementation of the UP/SP merger, the service crisis was due to a series of events involving different railroads at various locations in the Gulf Coast region, none of which, by itself, could be considered unusual or infrequent.¹⁴ In other words, the service crisis was not an event, but the result of many events, not all of which were even related. And WCTL has not sought to demonstrate that the expenses specifically attributable to any one of these events were so unusual¹⁵ (or even, under WCTL's interpretation of *Amerada Hess*, so large) as to constitute a difference in kind.¹⁶

Rail traffic ebbs and flows, and traffic surges can produce congestion at various points. Track maintenance can temporarily slow down rail traffic, and will likely continue to do so in the future. Weather can cause all sorts of disruptions to rail service. Derailments unfortunately do occur and will likely continue to occur. WCTL has not shown that any of the individual events that contributed to this particular service crisis were unrelated to normal railroad operations.¹⁷ The fact that the combined costs resulting from these various events were large does not warrant their treatment as unusual or infrequent under the USOA, as the focus of the USOA is on individual events or transactions.¹⁸

¹³ See, *Joint Petition for Service Order*, 3 S.T.B. 28 (1998) (*Service Order*) at 32-34.

¹⁴ UP notes that among the causes of the congestion were: derailments on SP lines in Texas and in the Englewood Yard; curfews imposed by BNSF for maintenance-of-way on the eastern segment of the former SP Houston-New Orleans line over which UP operates; significant increases in Gulf Coast traffic; congestion at the Laredo, TX international gateway; and a hurricane that affected interchange operations with CSX Transportation, Inc. (CSXT). See, *Service Order* at 32-34.

¹⁵ APB-30, in describing whether an event is unusual, states that "the underlying event or transaction should possess a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities of the entity."

¹⁶ WCTL argues that we should not "unbundle" a discrete event into a series of smaller events, but for accounting purposes, the service crisis was a situation produced by a variety of events, not an event itself.

¹⁷ WCTL's reliance on the treatment of certain railroads' out-of-court settlement costs of an antitrust suit filed by Energy Transportation Systems, Inc. is misplaced, as those costs were found to be unrelated to ordinary railroad operations. See, *Railroad Revenue Adequacy — 1988 Determination*, 6 I.C.C.2d 933, 945-46 (1990) (*1988 Revenue Adequacy*), *aff'd sub nom. Association of Amer. Railroads v. ICC*, 978 F.2d 737 (D.C. Cir. 1992).

¹⁸ The multiplicity of causal events is certainly one factor that distinguishes this service crisis from the (single-event) Exxon Valdez oil spill (an incident that resulted in criminal proceedings, government findings of probable fault on behalf of the company and certain of its personnel, and a jury verdict awarding \$5 billion in punitive damages). The Federal Energy Regulatory Commission chose to treat the large litigation and settlement costs associated with that spill as unusual and infrequent, even though oil spills are a normal occurrence in oil transportation, in view

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In short, considering the events that generated the congestion-related expenses in this case, we have no basis on which to conclude that those expenses “possess a high degree of abnormality” or are “of a type clearly unrelated to, or only incidentally related to, the ordinary and typical activities” of railroads. Similarly, these expenses cannot be considered “infrequent” because they are railroad-related occurrences that can “reasonably be expected to recur in the foreseeable future.”

2. UP Restructuring Costs

WCTL argues that the significant labor buyouts, major asset dispositions, and other large corporate restructuring expenses that UP has incurred or will incur in connection with its merger with SP should be treated as unusual items under GAAP, even if they are not infrequent,¹⁹ because they are peripheral to UP’s core business. WCTL claims²⁰ that its position is supported by GAAP and various general accounting references.²¹ WCTL further suggests that UP’s method of separately referencing these restructuring charges in notes to its 1997 Shareholder Report and its R-1 shows that UP management also regarded this cost as out of the ordinary.

We have reviewed the general accounting references cited by WCTL and find no specific support for requiring the restructuring expenses at issue to be treated as unusual or infrequent.²² Moreover, we do not regard the notes in UP’s

¹⁸(...continued)

of the magnitude of the single event that produced the expenses. *See, Amerada Hess.*

¹⁹ WCTL states that it has found 43 instances of labor-related charges identified as unusual items in railroad financial reports between 1985 and 1997. WCTL Reb. at 10; Reb. V.S. Verrecchia/Sondhi, Exh. JT-12. Those expenses were not reported as unusual items, however, but rather as special charges, which are discussed *infra*.

²⁰ WCTL Open. V.S. Verrecchia/Sondhi at 17-18.

²¹ Specifically, WCTL cites APB-30; Financial Accounting Standards Board Statement of Financial Accounting Standards No. 121 (FASB-121); recommendation 94-3 of the Emerging Issues Task Force (EITF 94-3); and a report entitled “Impairments and Writeoffs of Long-Lived Assets” by Fried, Schiff and Sondhi.

²² The accounting references cited by WCTL do not address the treatment of restructuring expenses as unusual or infrequent expenses. APB-30 addresses unusual and infrequent events and transactions but does not suggest that restructuring expenses should be considered as either unusual or infrequent expenses. EITF 94-3 addresses when restructuring expenses can be treated as a liability, not whether they should be considered an unusual or infrequent expense. Finally, FASB-121, and the excerpt of the Fried, Schiff and Sondhi report submitted by WCTL, discuss how and when a company should account for the disposal of long-lived assets. UP states that it has not

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financial statements as an indication that UP considers this expense to be unusual or infrequent. Companies regularly explain particular expenses in notes to financial statements without treating the expenses as unusual or infrequent, and indeed, WCTL's own witnesses indicate that one of the purposes of financial reporting is to help users of a business's financial statements understand the company's financial results.

In any event, in order for a railroad to record an event as unusual or infrequent, the event must meet the USOA definition of those terms.²³ It has long been recognized that expenses associated with labor buyouts, asset dispositions, and corporate restructuring — which are incurred regularly by virtually all major carriers — are directly-related costs of running a railroad.²⁴ See, *1988 Revenue Adequacy*, 6 I.C.C.2d at 944-45; *Productivity Adjustment-Implementation*, 9 I.C.C.2d 1072, 1081 (1993) (*Productivity*) (many labor-related special charges have become a fact of life in the railroad industry and a legitimate expense associated with running a railroad). Accordingly, such expenses are neither unusual nor infrequent.²⁵

3. SP Restructuring Costs

UP accounted for its acquisition of SP using the purchase accounting method. USOA Instruction 2-15(c)(1) provides that, when an acquisition results from a purchase (including mergers or consolidations other than pooling of interests), the amount includable in account 731, Road and Equipment Property,

²²(...continued)

disposed of assets (UP Reply V.S. Rhoades at 26), and in any event, those reports do not address whether asset disposal, had it occurred, should be recorded as either an unusual or an infrequent event. Thus, none of the references supports WCTL's claim.

²³ The mere fact that particular charges are one-time expenditures does not make them unusual or infrequent, particularly if they are of a type that can be expected to recur.

²⁴ Indeed, as UP points out, it routinely has programs in place to buy out or relocate employees, and regularly incurs expenses for training, equipment, and upgrading and rationalizing facilities; and it and numerous other railroads, sometimes in connection with merger transactions, have taken restructuring charges in recent years that have not been recorded as unusual or infrequent items. UP Reply, V.S. Antle/Heflin at 10, V.S. Rhoades at 32-33.

²⁵ WCTL argues that *1988 Revenue Adequacy* and *Productivity* are not good precedent because they arose in different contexts. Its witnesses assert, for example, that in *1988 Revenue Adequacy*, the ICC simply found that a railroad would need to recover the types of restructuring expenses at issue here in order to become revenue adequate, but did not address whether those types of expenses would be considered unusual or infrequent in an accounting sense. But the point, in our view, is that in *1988 Revenue Adequacy* and *Productivity*, the ICC expressly recognized that restructuring expenses are both normal and rail-related.

shall be the cost to the purchaser of the transportation property acquired. The USOA also provides that liabilities assumed by the purchaser are a part of the cost of acquiring the company. The cost assigned the property shall be the amount of the cost consideration given. Cost shall be determined by either the fair value of the consideration given or the fair value of the assets acquired. UP followed the explicit provisions of the USOA in its treatment of the SP liabilities.

WCTL argues, nevertheless, that UP should not have treated the SP restructuring costs as assumed liabilities, for various reasons. First, it asserts that, just like the UP restructuring expenses, the SP costs are external to the business of running a railroad, and thus are unusual or infrequent items. We find this argument to have no more merit here than it did with respect to the UP restructuring expenses.²⁶

WCTL also argues that the SP restructuring costs should be treated as post-merger expenses attributable to UP, rather than expenses that were an essential element of the UP/SP transaction. The only support that it offers for its position, however, is the unexplained assertion of its accounting witnesses. WCTL Open. V.S. Verrecchia/Sondhi at 22 (“In our view, these expenses are more likely to have been post-merger rationalization expenses * * *”). We find no basis for concluding that the costs of turning the SP system around were not costs incurred as part of the merger.

The SP restructuring costs resulted from a management plan adopted in preparation for the merger, a merger without which SP almost surely would have failed. An independent accounting firm has certified that UP has accounted for the SP acquisition in accordance with GAAP. Given that the SP restructuring costs were obligated pursuant to a plan developed in preparation for the merger, and were certified as in compliance with GAAP by an independent firm, the supposition of WCTL’s witnesses is not sufficient to persuade us that these costs were not, under GAAP, properly recorded on UP’s books as a liability that UP assumed when it purchased SP.

Notwithstanding the thrust of the purchase accounting rules, our USOA, and GAAP, WCTL takes the position that, even if the restructuring costs are not post-merger expenses, they still cannot be considered to be UP liabilities. In support of this position, WCTL argues that EITF 95-3 “imposes very stringent

²⁶ WCTL’s Witness Crowley, at 11 of his rebuttal statement, also argues that these expenses are unusual or infrequent because they are one-time “special” charges that will not recur and that have no “causal” relationship to the traffic that UP will handle. But clearly, rationalizing the SP system should have a causal effect (a positive one) on the traffic that UP handles. And as we discuss later, even if the expenses are “special” charges, they are properly assigned as rail-related expenses in the period during which they were incurred.

requirements for an acquiring company to account for the cost of restructuring an acquired company as an 'assumed liability.'"²⁷ In particular, WCTL states that EITF 95-3 permits restructuring costs to be treated as a liability only if the costs will generate no economic benefits for the merged entity. Because the costs associated with restructuring SP will provide a future benefit to the merged railroad, by increasing efficiency and/or reducing future expenses, WCTL argues that they should not be recorded as a liability.

WCTL misinterprets EITF 95-3, which generally does not preclude a company from recording a liability in connection with an action that will benefit the merged entity. Indeed, most of the actions taken by UP in connection with the SP operations, such as severing or relocating SP employees, are explicitly addressed in a section of EITF 95-3 entitled "Involuntary Employee Termination Benefits and Relocation Costs" that contains no provisions relating to future economic benefits. The relevant language provides that "a cost resulting from a plan to involuntarily terminate or relocate employees of an acquired company should be recognized as a liability assumed as of the consummation date of the purchase business combination and included in the allocation of the acquisition cost" as long as the actions were part of a plan developed as of the consummation date, and the plan was initiated and implemented shortly after the consummation date. WCTL has presented no evidence indicating that the actions taken with respect to SP employees did not meet this test.

There is one section of EITF 95-3 that contains the "no economic benefit" provision on which WCTL relies. It provides that a plan to exit an activity of the acquired company is recognized as an assumed liability only if either (1) the cost has no future economic benefit to the combined company, or (2) the cost represents "a penalty incurred by the combined company to cancel [a preconsummation] contractual obligation."²⁸ The purpose of the no-economic-benefit provision is to preclude a company from treating certain costs, such as a write-off of equipment, as a liability while continuing to generate revenue from that equipment.

Here, UP is not exiting the railroad business that it took over from SP, and thus for the most part, this aspect of EITF 95-3 does not apply. UP did exit certain specific activities of SP — by canceling certain contracts — but EITF 95-3 states that the contract cancellation costs of those activities should be recorded as an assumed liability. In short, the contract cancellation fees included in SP's restructuring costs fall under this provision (and are appropriately treated

²⁷ WCTL Reb. Argument at 14.

²⁸ EITF 95-3 at 789.

as assumed liabilities of UP), but the no-future-economic-benefit provision has no bearing on the other SP restructuring costs.

B. Special Charges

In addition to arguing that the costs at issue in this case should be treated as unusual or infrequent expenses, WCTL asserts that several should be identified as special charges and excluded from UP's URCS variable costs. The term "special charges" (first used in 1985 to identify significant expenses associated with several railroad restructurings), while not defined in the USOA or GAAP, refers to one-time expenses that are specifically identified in notes to a carrier's R-1 in order for the financial statement to provide the information needed to fully understand the business' financial condition. Each of the contested items here was reported by UP in notes to its 1997 R-1, and all received the same treatment as special charges, even though they were not labeled as such.

The fact that these items were, in essence, special charges does not, however, mean that they must be excluded from URCS variable costs. Many special charges are related to normal rail operations.²⁹ Indeed, "special charges have become a fact of life in the railroad industry," and most are recognized to be "legitimate expenses of running a railroad."³⁰ Our staff's policy, which we confirm is our policy, has been to exclude a rail-related special charge as a recognizable expense in URCS only when (and then only to the extent that) the charge recorded in a particular year relates to expenses that will be, or should have been, incurred in other years.³¹ Thus, what railroads have labeled as special

²⁹ 1988 *Revenue Adequacy*, 6 I.C.C.2d at 942.

³⁰ *Productivity*, 9 I.C.C.2d at 1081. WCTL cites *CSX Corp. Et Al. — Control — Conrail Inc. Et Al.*, 4 S.T.B. 75 (1999), Decision No. 123, for the broad proposition that special charges are not normal expenses of railroading. That decision, however, addressed only whether a particular \$283 million special charge, representing an anticipated loss on the sale of certain assets, unfairly distorted Conrail's 1995 earnings and not whether they were normal expenses. The special charge clearly resulted in "an understatement of [Conrail's 1995] earnings" because Conrail's 1995 R-1 indicated that the sale (and associated loss) did not occur in 1995.

³¹ WCTL cites *Rate Guidelines — Non-Coal Proceedings*, 1 S.T.B. 1004, 1031 (1996), for the broad proposition that the URCS formula generally excludes special charges. However, the particular special charge that had been placed in issue there (*see*, 1 S.T.B. at 1031 n.80) was one that had been recorded by BNSF in 1995 for future restructuring.

charges have often been excluded from URCS because the expenses were not incurred in the years in which they were recorded.³²

Here, the congestion-related expenses and \$60 million in UP restructuring expenses were incurred in 1997³³ and — regardless of whether they are labeled as special charges — would not be excluded from UP's 1997 URCS costs. Furthermore, the \$958 million in SP restructuring costs were appropriately treated as part of the SP purchase price, and any 1997 capital costs (depreciation expense and return on investment) associated with that purchase would be properly included in UP's 1997 URCS costs. Thus, whether or not those expenses are "special charges," they are expenses that should be considered as a normal part of railroad operations.

C. Conclusion

In sum, we find no merit to WCTL's complaint that UP should restate its 1997 R-1. The congestion-related costs, the UP restructuring costs, and the SP restructuring costs are not unusual or infrequent expenses under the USOA and GAAP. Nor are these expenses the types of charges that should be excluded from UP's variable costs. Consequently, WCTL's complaint will be dismissed.

This action will not significantly affect either the quality of the human environment or the conservation of energy resources.

VICE CHAIRMAN BURKES, commenting:

The issue in this proceeding is whether or not Union Pacific Railroad Company (UP) properly recorded certain charges associated with its 1997 congestion problems in and around the Houston area and with its merger with Southern Pacific Transportation Company (SP). The amounts at issue in this proceeding are significant.

In connection with its acquisition of SP, UP recognized a \$958 million liability related to the elimination of 5,200 duplicate positions. This amount was

³² See, WCTL Reb. V.S. Verracchia/Sondhi, Exh. JT-12, identifying the types of special charges often excluded from URCS. Although our staff typically did not provide its reasons for excluding particular charges, we note that many of the excluded charges, which often were immaterial in amount, were for severance payments that were disbursed over several years or for asset write-downs made necessary by the under-recording of depreciation expenses in prior years.

³³ Had UP recorded the full \$235 million in restructuring costs in its 1997 R-1, we would not have included that full amount in the 1997 URCS calculations. To the contrary, we would ensure that the URCS variable costs for 1997 were not impacted by expenses associated with other years.

apparently added to the SP purchase price allocation, however, UP's 1997 R-1 Annual Report notes that approximately \$280 million was charged against this reserve in 1997. In addition, UP noted that the cost of the Houston area congestion-related problems was approximately \$450 million, after tax. UP subsequently stated that only \$197 million represented congestion-related costs and the remaining \$253 million represented lost revenue. Finally, UP indicated that it expects to incur \$235 million in other acquisition-related costs, of which \$60 million, after tax, was charged in 1997. Therefore, in addition to the \$958 million allocated to the purchase price of SP, it appears that at least \$257 million (\$197 + \$60) in additional costs that were included in UP's 1997 R-1 report to the STB.

The accounting and allocation of these charges can have a significant impact in regulatory proceedings before the Board. The R-1 reports to the Board are used to develop Uniform Railroad Costing System or URCS data for the Class I carriers. URCS data is generally used to develop revenue-to-variable cost ratios necessary for jurisdictional threshold and rate reasonableness determinations. As we correctly state in this decision "the effect of overstating variable costs would be to decrease the amount of traffic potentially subject to our rate reasonableness authority, and to limit the rate relief available for such traffic." I also agree with a previous statement made by the Board in a decision last year in the Conrail proceeding that "Special charges represent material transactions that distort operating results for a given year."

In regard to the \$450 million in "congestion-related" costs, UP's R-1 notes that these costs "reflected the combined effects of lost business, higher costs associated with system congestion, and costs associated with implementation of the Plan, alternative transportation and customer claims." Other than UP's subsequent statement that only \$197 million were actual congestion-related expenses, there is little in the record to determine the actual breakdown of the total \$450 million figure. I agree that some costs in this category, such as car hire, crew cost, etc., may represent "normal" costs that may have been incurred even if there had been no service crisis. Therefore, it would appear to be difficult to segregate these expenses between "congestion-related" and "normal" expenses. Thus, it may be improper to exclude *all* these costs as advocated by the complainant.

The complainant argues that all of these costs should be excluded since the expenses relate to an "unusual" or "infrequent" event. In my mind, UP's Houston area service crisis was clearly an "unusual" and hopefully "infrequent" major event that disrupted railroad service and cost railroads and shippers millions in lost revenues and additional costs. I agree with the statement that

railroads regularly encounter service problems, however, I believe that the Houston area service crisis would not qualify as a "normal" railroad service problem.

The question here, however, is whether or not UP's Houston area service crisis technically qualifies as a single accounting "event" and whether or not it was "unusual" and "infrequent" under our accounting regulations. According to our standards, an event must possess "a high degree of abnormality and be of a type clearly unrelated to, or only incidentally related to the ordinary and typical activities of the entity." Although UP's congestion problems were "abnormal," they appear to be related to the "ordinary and typical activities of the entity." Therefore, it is possible that, based on our regulations, the UP's Houston area congestion problem does not "technically" qualify as an "unusual" or "infrequent" accounting event.

In terms of the \$253 million other "acquisition-related" costs, I agree with the Board's policy that rail-related restructuring charges should be excluded when "the charge recorded in a particular year relates to expenses that will be, or should have been, incurred in other years." Therefore, only the \$60 million charged in 1997 should be allowed to be included.

The \$958 million restructuring cost was treated differently in that it was used as a "write-up" of UP's asset base in the SP purchase price allocation. Apparently, this write-up treatment complies with generally accepted accounting principles or GAAP. Unlike the \$60 million charged as an expense in 1997 against the \$253 million restructuring costs, the costs charged against the \$958 million restructuring liability (e.g., \$280 million in 1997) are apparently not charged as an expense. However, this \$958 million write-up still has an impact on UP's URCS unit cost. It is estimated that UP incurred nearly \$200 million in additional depreciation and return costs as a result of this write-up.

There is also an issue here as to whether or not these UP/SP restructuring charges are "normal" or "unusual or infrequent" charges. I agree that restructuring charges, like railroad mergers, have become "a fact of life in the railroad industry." The merger was an event that was certainly related to "ordinary and typical" railroad activities. Although the merger between UP and SP may not have been "unusual," it was a unique, and thus "infrequent," event, which "would not reasonably be expected to recur in the foreseeable future."

Given the size, frequency and potential impact of these special charges, I believe that we must continue to closely monitor the railroads' accounting of these charges. I also believe that it may be time to review the treatment of these charges in regulatory proceedings.

It is ordered:

1. The motion to participate as *amicus curiae* is granted.
2. WCTL's complaint is dismissed.
3. This decision is effective June 12, 2000.

By the Board, Chairman Morgan, Vice Chairman Burkes, and Commissioner Clyburn. Vice Chairman Burkes commented with a separate expression.