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SURFACE TRANSPORTATION BOARD

DECISION

STB Docket No. WCC-101

GOVERNMENT OF THE TERRITORY OF GUAM

v.

SEA-LAND SERVICE, INC., AMERICAN PRESIDENT LINES, LTD., AND MATSON
NAVIGATION COMPANY, INC.

Decided: August 29, 2007

This decision denies petitions for reconsideration filed by the Government of the Territory of Guam (GovGuam) and the Caribbean Shippers Association (CSA) but modifies the procedural schedule.

BACKGROUND

In the ICC Termination Act of 1995, Pub. L. No. 104-88, 109 Stat. 803 (ICCTA), Congress abolished the Interstate Commerce Commission (ICC), and transferred certain ICC functions to the Board, effective January 1, 1996, including the responsibility to hear complaints challenging joint rates in the noncontiguous domestic trade. Congress also transferred to the Board from the Federal Maritime Commission (FMC) jurisdiction over complaints challenging the reasonableness of port-to-port rates in the noncontiguous domestic trade.¹

In this proceeding, GovGuam challenges the reasonableness of the rates, rules, classifications and practices for all transportation by water (including the water portion of

¹ The noncontiguous domestic trade is defined at 49 U.S.C. 13102(15) as domestic water carrier transportation “involving traffic originating in or destined to Alaska, Hawaii, or a territory or possession of the United States.” In the past, it was often referred to as the “domestic offshore trade.” Historically, regulatory jurisdiction over rates in the noncontiguous domestic trade was bifurcated. The FMC had jurisdiction over complaints challenging the reasonableness of the so-called “port-to-port” rates (water carrier rates that do not involve the services of an inland U.S. railroad or motor carrier). The ICC had jurisdiction over complaints challenging the reasonableness of joint rates (rates held out jointly by water carriers and inland rail or motor carriers). See Joint ICC/FMC Policy Statement, 8 I.C.C.2d 243 (1991).

intermodal transportation) provided by carriers serving Guam in the noncontiguous domestic trade. GovGuam, acting on behalf of its citizens shipping goods in that trade, seeks both reparations for allegedly unreasonable rates collected by defendants on past shipments and the prescription of maximum reasonable rates for future shipments.

In a decision served on January 6, 1999, the Board adopted a phased approach for this proceeding. In a decision served on November 15, 2001 (Phase I Decision), the Board addressed the motion to dismiss the complaint filed jointly by Horizon Lines, LLC (formerly Sea-Land Service, Inc.) (Horizon) and Matson Navigation Company, Inc. (Matson) (collectively the Carriers), granting the motion with respect to GovGuam's discrimination claim, but denying the remainder of the motion. The Board also dismissed American President Lines, Ltd. as a defendant and allowed the CSA to intervene.

In a decision served on February 2, 2007 (Phase II Decision), the Board addressed the appropriate procedures and methodological approach for handling this case. The Board concluded that where the rates charged are the product of a market in which there is effective competition, the Board can conclude that the market-based rates are reasonable without having to conduct a cost-based review. Accordingly, the Board decided to bifurcate Phase III, in which the Board will rule on the underlying complaint, to examine first whether transportation alternatives constrain each of the Carriers from exercising market power.² The Board explained that the burden to demonstrate the availability of competitive alternatives in a properly functioning market would be on the defendant Carriers for this affirmative defense. The Board established a procedural schedule for the competitive inquiry and deferred any cost-based review of the challenged rates pending a determination as to whether there is effective competition in the market serving Guam.³

Also in the Phase II Decision, the Board explained that, if it proceeded to a cost-based review of the Carriers' rate levels, it would apply its Constrained Market Pricing methodology (CMP),⁴ and that GovGuam would be free to choose which CMP constraint to use in its presentation. Finally, the Board concluded that, if the challenged rates ultimately are found to have been unreasonable in the aggregate as of September 10, 1996, the zone of reasonableness (ZOR) contained in 49 U.S.C. 13701(d)(1) should be taken into account in determining maximum lawful aggregate rates for subsequent years.

² In light of its experience in rail rate cases, the Board stated that it will not consider arguments concerning product and geographic competition. Phase II Decision at 6 n.14. See Market Dominance Determinations, 3 S.T.B. 937 (1998), reaffirmed on remand, 5 S.T.B. 492 (2001), aff'd, Assoc. of Am. Railroads v. STB, 306 F.3d 1108 (D.C. Cir. 2002).

³ In a decision served on March 6, 2007, the procedural schedule was held in abeyance pending a Board decision on the petitions for reconsideration.

⁴ See Coal Rate Guidelines, Nationwide, 1 I.C.C.2d 520, 542-43 (1985), aff'd sub nom. Consol. Rail Corp. v. United States, 812 F.2d 1444 (3d Cir. 1987).

REQUESTS FOR RECONSIDERATION

On February 16 and 22, 2007, CSA and GovGuam, respectively, filed petitions for reconsideration of the Phase II Decision. The Carriers replied in opposition on March 14, 2007.⁵

GovGuam first contends that the Board does not have the statutory authority to find rates in the noncontiguous domestic trade to be reasonable based solely on the ground that the rates are the product of competitive market forces. In GovGuam's view, we must conduct a cost-based review of the reasonableness of the challenged rates. GovGuam also contends that, even if we have the authority to find rates to be reasonable based on a finding that they are the product of competitive market forces, we cannot determine whether there is effective competition in the Guam trade without examining the Carriers' rates, historic costs and other factors that would also be considered in the rate reasonableness phase.⁶ For that reason, GovGuam maintains that there would be such overlap in the discovery and evidence that bifurcation would not materially shorten the proceeding. Even if we do not reverse the earlier decision to bifurcate the rate reasonableness analysis, GovGuam asks us to revise the procedural schedule to allow it sufficient time to conduct discovery on the competitive market issue.

Finally, GovGuam and CSA ask us to reconsider the determination that the ZOR would apply in determining the amount of relief available if the challenged rates are found to have been unreasonable at the beginning of the period covered by the complaint. GovGuam argues that this determination was premature, while CSA argues that the ZOR is not applicable to the type of rates mostly at issue here.

DISCUSSION AND CONCLUSIONS

For the reasons discussed below, we deny the requests for reconsideration of the Phase II Decision. We will, however, extend the procedural schedule.

Statutory Authority to Permit Market-Based Rates

The Phase II Decision properly determined that, as a matter of law and sound economic policy, the Board can find market-based rates in the noncontiguous domestic trade to be

⁵ The Carriers' reply also lists certain exceptions to the Phase II Decision that the Carriers purport to preserve notwithstanding their decision not to seek reconsideration. However, the mere listing of objections after the time for seeking reconsideration has expired is not sufficient to preserve challenges to the Phase II Decision that have not otherwise been properly presented to the Board.

⁶ Gov Guam has not sought reconsideration of our directive that it should use CMP standards if we decide that the case should proceed to a cost-based rate review because the market is not sufficiently competitive.

reasonable under 49 U.S.C. 13701(a) where there is effective competition without undertaking a cost-based CMP analysis. The Board explained that the statute does not compel us “to use any single pricing formula,”⁷ that agency interference with price setting in competitive markets “can only distort economically efficient rates” contrary to sound economic policy,⁸ and that the federal courts have upheld agency reliance on market forces in competitive markets to set just and reasonable rates “even without a particular statutory provision directing such an approach.”⁹

GovGuam renews its argument that the Board cannot rely on market forces to determine reasonable rates in the noncontiguous domestic trade unless Congress has affirmatively directed us to do so.¹⁰ We do not find GovGuam’s interpretation of our authority under section 13701(a) persuasive. As the Supreme Court and the federal courts of appeals have repeatedly held, the just and reasonable standard gives federal regulatory agencies “broad ratemaking authority,” and, as noted above, “does not compel [the agency] to use any single pricing formula.”¹¹ GovGuam does not cite any precedent to support its argument that the absence of an explicit direction from Congress restricts our authority to modify traditional approaches to rate reasonableness in light of this agency’s experience and that of the ICC before us in regulating motor carrier, rail and pipeline transportation, and the experience of other regulatory agencies such as the Federal Energy Regulatory Commission (FERC) that have approved market-based rates.

At the time the ICCTA was enacted, Congress was aware of the unbroken line of judicial precedent holding that the just and reasonable ratemaking standard is broad, expansive and flexible. Congress also was aware that the ICC had expressed a strong preference for reliance on market forces to set reasonable rates. See Georgia-Pacific Corp.–Pet. for Declar. Order,

⁷ Phase II Decision at 5, quoting Mobil Oil Explor. & Prod. Se., Inc. v. United Distrib. Cos., 498 U.S. 211, 224 (1991) (Mobil).

⁸ Id., quoting CF Industries, Inc. v. Koch Pipeline Company, L.P., 2 S.T.B. 257, 263 (1997) (Koch Pipeline).

⁹ Id., citing California ex rel. Lockyer v. FERC, 383 F.3d 1006 (9th Cir. 2004) (Lockyer) (discussing “just and reasonable” requirement of the Federal Power Act); La. Energy & Power Auth. v. FERC, 141 F.3d 364 (D.C. Cir. 1998) (La. Energy) (same); Elizabethtown Gas Co. v. FERC, 10 F.3d 866 (D.C. Cir. 1993) (Elizabethtown Gas) (discussing the “just and reasonable” requirement of the Natural Gas Act).

¹⁰ GovGuam Petition at 4 (“While Congress has expressly mandated such a threshold test [i.e., the absence of effective competition] as a prerequisite for review of rail and pipeline rates under ICCTA, there is no similar statutory support for limiting the Board’s review of the reasonableness of rates in the Guam trade to situations where the Board finds a lack of effective competition.”)

¹¹ Mobil, 498 U.S. at 224; Lockyer, 383 F.3d at 1012 (quoting Mobil); Grand Council of Crees v. FERC, 198 F.3d 950, 956 (D.C. Cir. 2000) (Grand Council of Crees), quoting FPC v. Hope Natural Gas Co., 320 U.S. 591, 602 (1944) (the Commission was “not bound to the use of any single formula or combination of formulae in determining rates”).

9 I.C.C.2d 103, 160-61 (1992)¹² (“we believe that a rate reasonableness analysis that is based on fully competitive market rates satisfies the reasonableness criteria of the Interstate Commerce Act, and is the only sensible approach to resolving motor carrier reasonableness complaints in today’s trucking industry”). Indeed, the thrust of ICCTA – which constitutes the latest in a series of Congressional actions in the transportation industry to place greater reliance on market forces – was to further “significantly reduce[] regulation of surface transportation industries in this country.” S. Rep. No. 104-176, at 2 (1995).

Given our broad ratemaking authority, our strong preference for reliance on market forces, and the history of ICCTA, we would expect to find specific directions from Congress if it wished us to adopt a markedly different regulatory regime for water carriers than the approach this agency uses for the other modes. No such directive appears in the statute. Therefore, we remain convinced that ICCTA empowers us to rely on market forces to establish reasonable rates in workably competitive markets subject to our jurisdiction.

Judicial Precedent Concerning Market-Based Rates

GovGuam argues that the Board’s decision to consider the rates in question reasonable if they were established by the Carriers in an effectively competitive market runs afoul of the Supreme Court’s decisions in MCI v. AT&T, 512 U.S. 218 (1994) (MCI) and FPC v. Texaco, Inc., 417 U.S. 380 (1974) (Texaco), and is qualitatively different than the initiatives by FERC to permit market-based rates. However, GovGuam has misinterpreted MCI and Texaco, has misapprehended the manner in which we are exercising our authority and has not distinguished the subsequent federal appellate court decisions that have upheld without dissent FERC’s authority to approve market-based rates as just and reasonable without a cost-based rate review.

The federal courts have held unanimously that MCI and Texaco do not preclude regulatory agencies from determining the reasonableness of rates based on an assessment of competition in the market.¹³ The Supreme Court in MCI held only that the Federal

¹² Aff’d and clarified, 9 I.C.C.2d 796, reaffirmed, 9 I.C.C.2d 1052 (1993), aff’d sub nom. Oneida Motor Freight, Inc. v. ICC, 45 F.3d 503 (D.C. Cir. 1995).

¹³ See Pub. Util. Dist. No. 1 v. FERC, 471 F.3d 1053, 1081-82 (9th Cir. 2006), petition for certiorari filed, 75 U.S.L.W. 3610 (May 3, 2007) (No. 06-1462); Lockyer, 383 F.3d at 1013; Elizabethtown Gas, 10 F.3d at 870-71; Tejas Power Corp. v. FERC, 908 F.2d 998 (D.C. Cir. 1990). See also Pub. Util. Dist. No. 1 v. IDACORP, 379 F.3d 641 (9th Cir. 2004) (holding that civil action for rescission or reformation of electricity sales contract negotiated under FERC’s market-based rate authority during Western states energy crisis was preempted by the Federal Power Act because “[e]ven in the context of market-based rates, FERC actively regulates and oversees the setting of rates”). See generally Grand Council of Crees, 198 F.3d 950, 956 n.7 (D.C. Cir. 2000) (absence of market power justifies an agency’s “relaxing its grip” when market power is absent).

Communications Commission could not eliminate the rate filing requirement for non-dominant long-distance carriers in an effort to promote a competitive telecommunications market.¹⁴ And in Texaco, the Court held only that the Federal Power Commission (FPC) could not exempt small producers from the Natural Gas Act's requirement of just and reasonable rates.¹⁵ In contrast, by allowing the Carriers to demonstrate the reasonableness of their rates by showing that the rates are the product of a market in which there is effective competition, we are not exempting them either from the requirement in 49 U.S.C. 13702 to file rate tariffs or from the requirement in section 13701(a) that their rates be reasonable. Even if we find in Phase III that there has been and currently is effective competition in the Guam market for noncontiguous domestic trade, circumstances can change. The Board would continue to be available to hear complaints under sections 13701(c) and 13702(b)(6) that a rate charged in the future is not reasonable and to award rate relief if appropriate.

GovGuam argues that, unlike the FERC decisions granting market-based rate authority that have been upheld by the courts, the Board's decision does not provide for meaningful *post hoc* review of the reasonableness of market-based rates in the Guam trade (if approved by the Board) or an adequate remedy in the event of changes in the market. GovGuam has not acknowledged the differences between ICCTA and the statutes administered by FERC, as well as the very different circumstances in which FERC exercises its regulatory authority.

In Lockyer and other cases involving market-based rate authority under the Federal Power Act and Natural Gas Act, FERC was not reviewing specific rates. Rather, FERC was giving the sellers blanket *ex ante* approval to sell electricity or natural gas at market rates based upon a finding that the markets at issue were competitive. 383 F.3d at 1012. Under those circumstances, the courts required *ex post* reporting so that FERC could monitor price formation in transactions that it had not reviewed and potential changes in market structure that could require the rescission of market-based rate authority. Likewise, the court in Lockyer, 383 F.3d at 1017, was concerned about FERC's ability to provide effective remedies in the event of market failure because FERC does not have the power to order reparations.¹⁶ By contrast, in Phase III

¹⁴ 512 U.S. at 220.

¹⁵ 417 U.S. at 394. In FERC v. Pennzoil Producing Co., 439 U.S. 508, 516 (1979), the Court recognized the limited nature of its holding in Texaco: "Our concern in Texaco was that rates of small producers might be totally exempted from the Act, and we did not indicate that producer or pipeline rates would be *per se* unjust and unreasonable because related to the unregulated price of natural gas. Texaco did not purport to circumscribe so severely the Commission's discretion to decide what formulas and methods it will employ to ensure just and reasonable rates. Indeed, the decision underscored the wide discretion vested in the Commission."

¹⁶ See Columbia Gas Trans. Corp. v. FERC, 448 F.3d 382, 387 (D.C. Cir. 2006) (FERC's authority under the Natural Gas Act "exercised at its zenith" does not include the power to award reparations); Middle South Energy, Inc. v. FERC, 747 F.2d 763, 770 (D.C. Cir. 1984)

(continued . . .)

of this proceeding, the Board is asked to undertake an *ex post* review of the rates charged by the Carriers in a known market rather than in a future market based on predictions regarding the competitive outlook.

In sum, the concerns of the federal courts over the lack of future oversight by FERC and the adequacy of the remedies under the Federal Power Act and Natural Gas Act are not present here. Under our statute, we have ample authority to provide effective redress should market conditions change so that competitive forces no longer constrain rates to presumptively reasonable levels.

Phase III Structure and Procedures

Administrative agencies have broad discretion to structure their proceedings.¹⁷ Here, the Board has exercised that discretion to provide for a bifurcated rate reasonableness analysis. We will look first only at whether competition effectively constrains carriers in the Guam trade from exercising significant market power. If the Carriers satisfy their burden of showing effective competition,¹⁸ then we can conclude that their existing rates are reasonable. If the Carriers do not make that showing, we will then examine whether, under a cost-based analysis, each carrier's aggregate rate levels are reasonable.

GovGuam argues against this bifurcated approach to the issue of rate reasonableness asserting that the same evidence can be relevant to both parts of the inquiry. We do not agree that the evidence needed to determine the state of competition in the Guam market would be the same as the evidence needed for a cost-based review of a carrier's aggregate rate levels. Therefore, we deny GovGuam's request to reconsider bifurcation of the Phase III proceeding. While it is not our intent at this point to limit the evidence that GovGuam may present with respect to effective competition, we need to have a full understanding of the structure and functioning of the market for transportation to and from Guam so that we can conduct an appropriate competition review. Therefore, we expect the parties to give us the information we will need to carry out that review during the first part of Phase III.

We agree with GovGuam that the procedural schedule should be modified to provide sufficient time for discovery under 49 CFR 1114.21 related to the issue of effective competition

(. . . continued)

("[U]nlike the ICC, [FERC] cannot order reparations to ratepayers" under the Federal Power Act).

¹⁷ Atlanta Gas Light Co. v. FERC, 140 F.3d 1392, 1400 (11th Cir. 1998); Trunkline LNG Co. v. FERC, 921 F.2d 313, 322 (D.C. Cir. 1990).

¹⁸ Because market dominance is not a jurisdictional prerequisite with respect to rates in the noncontiguous domestic trade, as it is for rail rates, see 49 U.S.C. 10701(d)(1), 10707(b), (c), the existence of effective competition is an affirmative defense and the burdens of production and persuasion will be on the defendant Carriers.

within the Guam market. Therefore we will modify the procedural schedule as set forth below. The parties are directed to meet to discuss discovery matters as soon as possible, but no later than [7 days from date of service]. If necessary, at the request of either party, the Board will hold a staff-supervised discovery conference.

Policy Objectives of the Zone of Reasonableness

GovGuam also seeks reconsideration of the portion of the Phase II Decision that addresses the potential application of the Congressional intent embodied in the “zone of reasonableness” provision of section 13701(d)(1) in determining the reasonableness of the challenged rates.¹⁹ GovGuam argues that any conclusion about the role of the ZOR is premature. It maintains that the ZOR applies only to port-to-port rates and that the majority of the traffic at issue here moved under joint intermodal rates that are not subject to the ZOR. Therefore, GovGuam claims that, until the underlying facts are more fully developed, the Board cannot determine whether or to what extent the ZOR should impact the maximum reasonable rates.

We agree that it is not yet necessary for the Board to reach this issue. But that does not mean that it was improper for the Board to address the issue in the Phase II Decision for the purpose of providing guidance to the parties on how to proceed in the second part of the rate reasonableness inquiry should this case reach that stage.

With regard to the substance of GovGuam’s argument, we note first that GovGuam has not challenged the non-water portion of any intermodal transportation provided by the Carriers. Rather, GovGuam has asked the Board to look only at the port-to-port portion of the rates in the Guam market. In any event, GovGuam’s assertion that the ZOR does not apply to intermodal rates is incorrect. Section 13701(d)(1) specifically states (emphasis added) that the ZOR applies to “a rate or division of a . . . water carrier for port-to-port service in [the noncontiguous domestic] trade” As was noted in the Phase I Decision (at 10), the Carriers’ intermodal joint rates are typically constructed by adding the price of motor carriage to an existing port-to-port rate. Thus, the separately identified port-to-port portion of an intermodal rate is expressly included in the protections of the ZOR.

CSA argues that the ZOR was meant to apply only to proposed rates and that a rate can only be compared to the rate that was in effect one year before the proposed rate was submitted.

¹⁹ That provision reads, in relevant part: “For purposes of this section, a rate or division of a . . . water carrier for port-to-port service in [the noncontiguous domestic] trade is reasonable if the aggregate of increases and decreases in any such rate or division is not more than 7.5 percent above, or more than 10 percent below, the rate or division in effect 1 year before the effective date of the proposed rate or division.”

CSA asserts that the Board cannot expand the ZOR by applying it to a rate that was not in effect as of that date.²⁰

We stand by the analysis in the Phase II Decision of the Congressional objectives embodied in the ZOR and how it should be effectuated in an after-the-fact rate reasonableness analysis. Should a carrier's rates in effect at the outset of the period covered by the complaint be found to have been unreasonable, the rates that the carrier could lawfully charge as of that date would necessarily be lowered. Under the ZOR, however, the carrier would have had an absolute right to increase the lawful rate levels by 7.5% annually. We can reasonably assume that, had it known at the time that the rates it could lawfully charge were less than the rates that it was charging, the carrier would have exercised its absolute right to increase the lower rates to the extent permitted by statute until those rates rose to its desired level (i.e., the level of the challenged rates). For us to preclude the Carriers from realizing the benefit of the ZOR in the circumstances of this case would serve to penalize them for the delay associated with the regulatory process and would ignore the intent of Congress. Therefore, we continue to believe that, if the rates are found to have been unreasonable at the outset of the complaint period, it would be entirely appropriate to take into account, in determining the reasonableness of the challenged rates over the entire period covered by the complaint, a water carrier's statutory right to increase its rates to the extent of the ZOR.

It is ordered:

1. The petitions for reconsideration are denied except for the request to change the procedural schedule.

2. The procedural schedule is modified as follows:

October 1, 2007	End of discovery.
October 9, 2007	Carriers shall submit evidence regarding effective competition in the Guam market.
November 8, 2007	GovGuam shall submit reply regarding effective competition in the Guam market.

²⁰ CSA points to former 49 U.S.C. 10708(d), which established a zone of rate flexibility (ZORF) for motor freight carriers and freight forwarders similar to the ZOR for water carriers at issue here. CSA notes that former section 10708(d)(2) expressly empowered the ICC to increase the upper band of the motor carrier ZORF, by rule, but that Congress has not given the Board the power to increase the ZOR for water carriers.

3. The parties shall meet as soon as possible, but no later than September 6, 2007, to discuss discovery matters.

4. This decision is effective on its date of service.

By the Board, Chairman Nottingham, Vice Chairman Buttrey, and Commissioner Mulvey.

Vernon A. Williams
Secretary