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BEFORE THE

SURFACE TRANSPORTATION BOARD

DOCKET NO. EP 431 (Sub-No. 4)

REVIEW OF THE GENERAL PURPOSE COSTING SYSTEM

REPLY COMMENTS OF

ALLIANCE FOR RAIL COMPETITION
MONTANA WHEAT & BARLEY COMMITTEE
COLORADO WHEAT ADMINISTRATIVE COMMITTEE
IDAHO BARLEY COMMISSION
IDAHO GRAIN PRODUCERS ASSOCIATION
IDAHO WHEAT COMMISSION
MONTANA FARMERS UNION
NEBRASKA WHEAT BOARD
OKLAHOMA WHEAT COMMISSION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCERS BOARD
WASHINGTON GRAIN COMMISSION
WYOMING WHEAT MARKETING COMMISSION
NATIONAL ASSOCIATION OF WHEAT GROWERS
U.S. CLAY PRODUCERS TRAFFIC ASSOCIATION, INC.
USA DRY PEA AND LENTIL COUNCIL

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Dated: September 5, 2013

Alliance for Rail Competition ("ARC") and the other shipper groups identified on the cover of these Reply Comments (collectively, "ARC, et al.") have seen little in the comments filed by other parties in this proceeding to mitigate our concern that the Board is pursuing an arguably desirable goal – more accurate costing of railroad services for regulatory purposes – in a questionable and possibly unlawful manner.

As detailed in the attached Reply Verified Statement of Witness Fauth, ARC, et al. is not the only party to this proceeding whose ability to comment was compromised by unnecessary restrictions on access to relevant data. The resources of ARC, et al. are limited, and the allocation of those resources to STB rulemaking proceedings must reflect the potential benefits and costs of STB proposals to the captive shipper interests we represent. Here, however, we do not know what impacts are likely to follow from implementation of changes in URCS costing proposed by the Board.

It might be argued that more accurate costing is inherently beneficial, and a goal to be sought by all. Others could argue that better regulatory tools are less important than better regulatory policies. In any event, ARC, et al. cannot legitimately be asked to approach issues like those presented here as abstract math problems, unrelated to real shipper concerns. That is not ARC's mission, and even if it were, objective analysis is not possible when highly relevant data has been withheld. The question bears repeating: Why did the Board provide full access to Waybill Sample data (subject to protective orders) in EP 711, but deny such access in this proceeding?[1]

The Board must also recognize that shippers and railroads do not look at STB proceedings in isolation. Business plans, distribution patterns and the investments and hard work of captive shippers, large and small, are affected by the totality of STB regulation of the railroad industry and by railroads' operational and commercial responses to laws, regulations and policies implemented by the Board.

At present, changes may be considered in a number of proceedings, some of which could increase the effectiveness of regulation and improve access to legal remedies, and some of which may undermine those goals. In the former category, it may be that the Board's proposal, announced in its decision served July 18, 2013 in EP 715, <u>Rate Regulation Reforms</u>, at pp. 36-37, to initiate a new proceeding to consider the effectiveness of rate relief proceedings available to grain shippers is the Board's path to improve access to legal remedies for such shippers. ARC, et al. also welcome the decision in EP 715 to raise or eliminate relief caps under approaches other than full-SAC, and we support efforts in EP 711 to increase competition among railroads, which may benefit some shippers that are currently captive.

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[1] As Witness Fauth explains, Reply V.S. at 9-10__, while access to the Costed Waybill Sample was provided, key information that would have permitted assessment of the impact of the Board's proposed URCS changes and other aspects of its proposals was redacted.

On the other hand, ARC, et al. are concerned that the new "limit price R/VC ratio approach" employed in determining market dominance in Docket No. 42123, M&G Polymers USA, Inc. v. CSX Transportation, Inc., could lead to RSAM becoming the defacto jurisdictional threshold in future rate cases, effectively insulating many high rail rates covering a large number of commodity movements from challenge until such time as all major railroads are found revenue adequate. The Three Benchmark test – the only potentially affordable rate reasonableness test for most of the nation's captive rail shippers – is already too weak to deter excessive rail rates, and market dominance changes that would free railroads to raise rates on captive traffic to RSAM levels could be the last straw for many shippers, whether or not URCS is improved.

There are captive shippers represented by ARC, et al. that ship in larger volumes, including unit train and shuttle train volumes. These shippers share the smaller shippers' concerns regarding market dominance determinations that could redefine "effective competition" as competition that keeps rail rates at or below RSAM levels. We note too that, since 2008, railroad cost of capital determinations have been exaggerated due to the Board's decision to give significant weight to discounted cash flow data. See in this regard the petition for rulemaking filed August 27, 2013 by Western Coal Traffic League in EP 664 (Sub-No. 2), Use of Multi-Stage Discounted Cash Flow Model in Determining the Railroad Industry's Cost of Capital, a petition ARC supports. The inaccuracy challenged in that proceeding has adverse effects on captive shippers of all commodities, regardless of shipper or shipment size.

The fact remains that, of the captive shippers represented by ARC, et al., some of the most vulnerable are shippers using 50-79 cars for some or all of their shipments. Many such shippers pay high (and rapidly increasing) rates and receive poor service. In this proceeding, the Board has proposed to redefine trainload as 80 cars or more. The implications of this proposal for recourse by such shippers to Board remedies are obviously of concern to ARC, et al. However, as explained by Witness Fauth, the data necessary to analyze this proposal has not been provided. Fauth Reply V.S. at pp. 2, 5, 7- 9, and 10.

Despite our concerns, ARC, et al. have attempted to provide helpful technical comments in this proceeding, relying on Mr. Fauth's long experience in ICC and STB cases. However, the Board is urged to move ahead more cautiously as to URCS revision issues. URCS modernization should not take place based on the record in this proceeding but should be deferred until additional data is collected or produced, and made available for analysis and comment by the affected parties.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this 5th day of September, 2013, caused copies of the foregoing document to be served on all parties of record electronically or by first class mail, postage prepaid.

Terry Whiteside

BEFORE THE

SURFACE TRANSPORTATION BOARD

STB DOCKET NO. EP 431 (SUB-NO. 4)

REVIEW OF THE GENERAL PURPOSE COSTING SYSTEM

REPLY VERIFIED STATEMENT

OF

GERALD W. FAUTH III

My name is Gerald W. Fauth III. I am President of G. W. Fauth & Associates, Inc., an economic consulting firm with offices at 116 South Royal Street, Alexandria, Virginia 22314. I previously submitted an opening statement in this Surface Transportation Board (STB or Board) proceeding and a statement describing my background, experience and qualifications is attached thereto as Appendix GWF-1.

I have been asked by the Alliance for Rail Competition, Montana Wheat & Barley Committee, Colorado Wheat Administrative Committee, Idaho Barley Commission, Idaho Wheat Commission, Idaho Grain Producers Association, Montana Farmers Union, Nebraska Wheat Board, Oklahoma Wheat Commission, South Dakota Wheat Commission, Texas Wheat Producer Board, Washington Grain Commission, Wyoming Wheat Marketing Commission, National Association of Wheat Growers, U.S. Clay Producers Traffic Association, Inc. and USA Dry Pea and Lentil Council (ARC, et al.) to submit these reply comments concerning changes recently proposed by the STB to its general purpose costing system, known as the Uniform Railroad Costing System or URCS.

Clear Lack of Empirical Evidence

The Opening Comments of several other parties show that ARC, et al. are not alone in expressing concern for the lack empirical evidence to support the Board's proposed changes. For example, the Opening Comments of American Chemistry Council, The Chlorine Institute, The Fertilizer Institute, and The National Industrial Transportation League (collectively the "Interested Parties") states that the URCS proposals are "most notable for the lack of any studies or empirical analyses to support the Board's proposals."[1] The Association of American Railroads (AAR) also states that the URCS proposals "are not supported by any empirical evidence that show that the changes would result in more accurate costs" and maintains that several "special studies" would be required.[2] There is clearly a lack of empirical evidence to support the Board's URCS proposals.

In my opening statement, I noted that STB's URCS proposals should be thoroughly tested before they are formally adopted by the Board. I also noted that the railroads are in possession of the necessary data and should, without too much effort, be able to provide data for the last three years (2010, 2011 and 2012), which could then be used by the STB and other parties to test the Board's proposal in regard to the proposed URCS adjustments.[3] It is interesting to note that the AAR cites the lack of empirical evidence when, in fact, the railroads are in possession of all or almost all such evidence and/or data which could be used to produce such empirical evidence.

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1 Interested Parties Opening Statement, page 5.
2 AAR Opening Comments, page 7.
3 GWF Opening V.S., page 9.

AAR also cites the need for several "special studies," but recognizes that "the Board may not believe that it has the resources" to do the special studies.[4] In 2012, the STB had 134 full-time equivalent (FTE) employees and an annual budget of approximately $29 million.[5] In 2012, the U.S. Class I railroads had 163,464 employees, annual operating revenues exceeding $70 billion and net income of $12 billion.[6] Clearly, the railroads have more than adequate resources, both in terms of the necessary data and required funding, to produce the required evidence and data and develop such special studies, which could then be evaluated and scrutinized by other interested parties.

Proposed Trainload Definition Change

Despite the lack of "empirical evidence" to support the STB's proposed changes to URCS, the AAR does not object to the STB's proposed change in the definition of a trainload from 50 to 80 cars.[7] Western Coal Traffic League (WCTL) also does not object to the Board's change in the definition for costing purposes, because WCTL "notes this change will not impact unit train shippers of western coal, as their trains already contain far more than 80 cars."[8]

ARC, et al., and their members which represent a broad cross-section of this nation's shippers continue to have serious concerns regarding the proposed change in the definition of a trainload from 50 to 80 cars, due to the absence of any "empirical evidence" to show that this proposal would result in "more accurate costs." As indicated in my opening comments, this proposed change could have a significant impact on railroad shippers. In 2011, for example, 1,184,053 million carloads moved in shipments ranging from 50 to 79 carloads per shipment.

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4 AAR Opening Comments, page 12.
5 STB FY 2014 Congressional Budget Submission, Exhibit 1.
6 AAR Class I Railroad Statistics, dated July 9, 2013.
7 AAR, Opening Comments, page 7, footnote 12.
8 WCTL, Opening Comments, page 13.

This large number of shipments that are currently considered trainloads carried approximately 124 million tons and generated over $2.1 billion in annual railroad freight charges. Shippers of Farm Products (STCC 01) would be among the largest traffic groups impacted by the STB's proposed change, as over 250,000 carloads moved in shipments ranging from 50 to 79 cars .[9]

Allocation of Switch Engine Minute Cost

The STB has proposed changing the allocation of URCS switch engine minute cost from a per car basis to a per shipment basis.[10] In my Opening Comments, I noted that such a change could have a significant impact on the variable cost of a movement, especially for shippers with smaller shipments in terms of the number of cars per shipment.[11] AAR also makes this observation and states that " the Board's proposal to allocate all switching costs on the basis of the number of shipments . . . shifts considerably more costs to shipments of one-car."[12] Although AAR also points to a lack of empirical evidence and the need for special studies, it suggests as an alternative a split of 70 percent of the SEM cost related to the shipment and 30 percent related to the cars per shipment, contending that this split was developed based on "preliminary analyses" of the Costed Waybill Sample.[13] AAR maintains that a similar allocation could also be used in the development of Station Clerical costs.[14]

I have not reviewed the AAR's study (which was not publically filed but was made part of AAR's workpapers), however, I question whether this approach would be appropriate for all types of rail movements. In my Opening Verified Statement, I pointed out there are numerous

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[9] See GWF Opening V.S., pages 15 through 17.
[10] STB Docket No. 431 (Sub-No.4), decision served February 4, 2013, page 5.
[11] GWF Opening V.S., page 7.
[12] AAR Opening Comments, Baranowski/Fisher V.S., page 11.
[13] *Ibid.*
[14] AAR Opening Comments, page 16.

differences in the way different commodities are handled. For example, many unit train coal movements and shuttle train grain movements essentially involve no ($0) switching cost since, in such cases, the locomotives and crews remain with the trains and load and unload via loop tracks. I also pointed out that in many cases, shipments are switched in a single block of cars with several or many other shipments, in which cases the allocation of switching costs on a per car basis may be more appropriate. To demonstrate this fact, I showed that the 2011 Public Waybill Sample indicates that 407,240 STCC 01 carloads (which represent over 22% of the total STCC 01 carloads) moved in single-car (1 car) shipments. However, it is likely that only a very small minority of these single-car shipments were actually switched as single cars. This demonstrates that the railroads currently treat hundreds of thousands of shipments as single-car shipments, presumably for accounting purposes, even though most of these shipments involved multiple cars .[15]

In order to account for this problem, I suggest that the STB gather information from the railroads relating to the number of cars per shipment per switching event or block. The railroads could produce information relating to the number of cars per shipment for each switch based on car ownership, car type and commodity and this data could be used by the STB to develop URCS Phase III adjustments to the SEM cost per shipment. For example, most coal movements would involve one shipment per switch, whereas other commodities may have a ratio of, say 1.25 or 30 shipments per switch, which could be used to adjust the URCS SEM cost. I believe such an approach would be superior to the 70%/30% approach suggested by the AAR.

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[15] See GWF Opening V.S., page 10 through 12.

AAR's Proposed Intermodal Adjustment

The AAR recognized this problem shipment size versus switching block size problem in relation to the development of URCS costs for intermodal (TOFC/COFC) movements. AAR states that "While intermodal containers and trailers are typically waybilled individually, they are loaded in larger quantities onto flatcars and frequently move in dedicated trains consisting of several flatcars."[16] AAR maintains that an average shipment size of 10 flat cars per switch should be used in lieu of the STB's current downward 25% adjustment "as a placeholder in our calculations of the redistribution of URCS switching."[17] AAR offers no empirical evidence or special studies to support this 10-car intermodal switch factor.

Certainly, this number could vary significantly by Class I railroad and by origin and destination. For example, BNSF states that in 2012, BNSF averaged 12 flat cars moving together as a block from origin to destination, but admitted that the number may vary "from year to year and across rail carriers."[18] However, the intermodal cars per switch can also vary significantly by movement. In many cases, BNSF intermodal trains from Los Angles are either 6,000 ft or 8,000 ft. in length. In 2007, however, BNSF announced that it had lengthened the transcontinental intermodal trains from Los Angeles to Chicago from an average of 8,000 ft. to 10,000 ft. and has since been testing even longer intermodal trains up to 12,000 ft., which would equate to approximately 300 40-foot flat-cars per train or 226 53-foot flat-cars per train switched moving as a unit from origin to destination.[19] For such large unit train intermodal movements,

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16 AAR Opening Comments, page 14. Footnote 32 reference excluded. AAR estimates an average of 4.4 containers per flat car (see AAR Opening Comments, Baranowski/Fisher V.S., page 11.)

17 AAR Opening Comments, Baranowski/Fisher V.S., page 13.

18 BNSF Opening Comments, page 10.

19 http://myprogressiverailroading.com/rail_forum/editors_posts/b/jstagl/archive/2009/08/14/bnsf-other-class-is-bullish-on-longer-trains.aspx?pi864299343=2

the proposed use of a 10 or 12–car switching factor would obviously overstate the switching costs.

Proposed Use of Average Empty/Loaded Ratios
for Dedicated Unit and Shuttle Trains

The STB has proposed using the carriers' system average Empty/Loaded (E/L) ratios for all trainload movements. Thus, the STB's proposed approach would treat trainloads and dedicated unit and shuttle trains the same, which could have an adverse costing impact on such efficient dedicated train movements. For URCS Phase III costing of such dedicated unit train service, the STB should allow parties to use a 2.0 E/L Ratio. The STB may also want to consider requiring the railroads to identify such dedicated shuttle and unit trains in the waybill sample reporting. This would allow the STB to properly use and apply the 2.0 E/L Ratio to dedicated unit and shuttle trains in its costing of the waybill sample records.

Proposed Locomotive Unit-Mile Adjustment

In my Opening Verified Statement, I demonstrated that the URCS Phase III Locomotive Unit Miles (LUM) cost accounted for one of the major cost differences between trainload and non-trainload movements.[20] For example, the LUM cost for a 49-car non-trainload shipment moving 1,000 miles in single-line service could be over $300 per car higher than the LUM cost for the same movement with a trainload of 50 cars.[21] The STB's proposed change in the trainload definition from 50 to 80 cars would have a similarly large impact on the development of the Phase III URCS LUM cost.

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20 See GWF Opening V.S, page 18, Table 5.
21 *Ibid.*

The STB has proposed two modifications in the way URCS Phase III LUM costs are calculated. For trainload shipments (80 or more cars), the STB has proposed allocating 100% of the trains' LUM costs. For single car and multiple car shipments, the allocation would be based on the cars per shipment relative to the minimum trainload size (i.e., 80 cars).

Again, the STB has provided no empirical evidence to support its proposed change. AAR opposes this change and states that basis for the STB's proposal is "weak."[22] AAR also states that the "proposed changes to LUM costs are unrelated to the make-whole adjustment and should not be adopted."[23] I agree that the Board's proposals should not be adopted until there is empirical evidence, including impact analyses, to support the proposed change.

Proposed I&I Switching Adjustment

The STB has proposed increasing the distance between Inter and Intra Train (I&I) switching from every 200 miles to every 320 miles. The STB developed this figure "Based on a comparison of the average length of haul for the Class I railroads in 1990 (pre-mergers) and 2011 (post-mergers)." The Board "observed a 60% increase in the overall length of haul" and therefore has proposed "to increase the distance between I&I switches by 60%, from 200 miles to 320 miles."[24]

I agree with AAR that the STB's "observations regarding the historical increase in the average length of haul do not necessarily translate into an increase in the I&I switch interval."[25] AAR has proposed a special study.

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[22] AAR Opening Comments, Baranowski/Fisher V.S., page 22.
[23] AAR Opening Comments, page 17.
[24] STB Docket No. EP 431 (Sub-No. 4), served February 4, 2013, page 8.
[25] AAR Opening Comments, Baranowski/Fisher V.S., page 19.

Again, as also noted in my Opening Statement, the data necessary to produce such a study is readily available to the railroads. STB should require the railroads to submit data to the STB concerning I&I switching intervals and allow parties to evaluate and comment on the railroads' data.

Access to Waybill Sample Data

ARC, et al.'s Opening Comments state: "It is difficult to understand why the Board refused to make the most recent confidential Waybill Sample available to parties, under customary protective orders, in this proceeding, when confidential Waybill data was made available in the Board's contemporaneous proceeding in EP No. 711, Petition for Rulemaking to Adopt Revised Competitive Switching Rules, decision served July 25, 2012 at 2."[26]

Based on subsequent communications with STB staff, I wish to clarify this point. By its decision served April 25, 2013 in this proceeding, the Board did provide to parties, including ARC et al., access to certain Confidential Waybill Sample records. However, the Board limited parties' ability to use the Waybill Sample by redacting certain data fields, including revenue, origination, interchange and terminal locations, which the STB states "is not required to calculate costs using the make-whole adjustments."[27]

The STB's redactions of certain Confidential Waybill Sample fields hampered the ability of ARC et al. and other parties in their efforts to develop certain impact analyses. By redacting the revenue fields, parties were obviously not able to determine and evaluate the Revenue to Variable Cost (R/VC) ratios associated with each record. Therefore, parties were precluded from using the data to perform certain STB jurisdictional impact analyses. For example, ARC et al.

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[26] ARC Opening Comments, page 6.

[27] STB Docket No. EP 431 (Sub-No. 4), served April 25, 2013, page 2, footnote 4.

could not determine the amount of jurisdictional grain traffic (i.e., R/VC>180%) traffic moving in trainloads ranging from 50 to 79 cars which would be potentially deregulated (i.e., drop below 180%) as a result of the STB's proposed change in the definition of a trainload from 50 to 80 cars per shipment. The redaction of the origin and destination SPLC codes also precluded ARC et al. from performing certain traffic analyses associated with the movement of single-car (1 car) shipments. For example, based on the redacted location data, ARC et al. might have been able to identify single-car shipments which moved on the same day from the same facility with other shipments.

VERIFICATION

The foregoing statement is true and accurate to the best of my belief and knowledge.

Gerald W. Fauth, III

Subscribed and sworn to before me this 3rd day of September 2013.

Notary Public

JOSHUA M. GOERBIG, Notary Public
State of Michigan
County of Mason
My Commission Expires 04/28/2019
Acting in the County of Mason

My commission expires: 4-28-2019

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