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**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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Docket No. EP 431 (Sub-No. 4)

REVIEW OF THE GENERAL PURPOSE COSTING SYSTEM

COMMENTS OF UNION PACIFIC RAILROAD COMPANY

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Union Pacific Railroad Company submits these comments in response to the Board's Supplemental Notice of Proposed Rulemaking served August 4, 2016 ("SNPRM"). Union Pacific also joins in the comments filed by the Association of American Railroads.

Union Pacific appreciates the Board's efforts to respond to comments on the Notice of Proposed Rulemaking served February 4, 2013 ("NPRM"), by revising its proposed changes to its general purpose costing system, the Uniform Railroad Costing System ("URCS").

Union Pacific remains concerned, however, that the Board is using its limited resources to address an unavoidable attribute of URCS, instead of pursuing other, more significant updates to URCS. As Union Pacific discussed in our comments on the NPRM, there is a compelling need to update and improve URCS. The existing model is based on historical statistical relationships and special studies that do not fully reflect railroad operations railroads today. Yet, even as URCS's empirical underpinnings have grown further removed from current conditions, the Board has expanded its reliance on URCS and revenue-to-variable cost ("R/VC") ratios in regulating the market activities of railroads. Unless URCS reflects current railroad operations, the Board's reliance on URCS may have the unintended consequences of distorting regulatory and commercial decision-making, to the detriment of shippers, railroads, and the general public.

Union Pacific’s comments on the SNPRM focus on three issues. First, we briefly discuss our continued concern with the Board’s proposals to eliminate break-points created by the URCS make-whole adjustment, locomotive unit-mile allocation, and train-mile allocation. Second, we discuss the Board’s proposed change to the URCS I&I switching mileage figure and our own study of I&I switching mileage. Finally, we discuss our concern with the Board’s proposal to apply its proposed changes only prospectively.

I. Lack Of Empirical Support For Eliminating Break-Points

As Union Pacific stated in our comments on the NPRM, we support the Board’s overall objective of accounting more accurately for operating costs and economies of scale as shipment size increases. We also recognize the Board’s interest in eliminating break-points in URCS. However, the proposals in the SNPRM contain features that are as troubling, if not more troubling, than the current URCS model.

First, in proposing to eliminate break-points between 5- car and 6-car shipments, and between 49-car and 50-car shipments, the Board appears to create even larger break-points between 1-car and 2-car shipments, and between 2-car and 3-car shipments.

The Board’s proposal is troubling because the current break-points may more accurately reflect real-world railroad operations than the proposed break-points. The current break-points reflect an empirical observation that certain costs depend more on shipment type—*i.e.*, “single-car,” “multi-car,” or “trainload/unit train”—than on the number of cars waybilled together. This accords with real-world operations. When Union Pacific pulls cars from an industry, it typically pulls all available outbound cars, regardless of how they are waybilled. Similarly, when Union Pacific spots cars at an industry, it typically spots all available inbound cars, up to the industry’s capacity, regardless of how they are waybilled. Consequently, a car that is waybilled as a 1-car

shipment is often switched along with other cars that are also waybilled as 1-car shipments.¹ The current URCS model recognizes, for example, that cars waybilled as 1 to 5 car shipments have switch engine minute costs that are generally the same, and that are higher than switch engine minute costs for multi-car or unit train shipments. Of course, no approach to calculating unadjusted URCS system-average costs will ever precisely calculate the costs for every shipment, but there is no empirical evidence that the proposed sharp break-points between 1-car and 2-car shipments, and between 2-car and 3-car shipments will produce more accurate results than the current URCS model.

Second, to eliminate break-points relating to the allocation of locomotive unit-miles (“LUMs”) and train miles, the Board is proposing to cap LUMs and train miles allocated to multi-car shipments to be equal to the LUMs and train miles allocated to unit train shipments, even though URCS would otherwise allocate more LUMS and train miles to multi-car shipments. In other words, unlike the Board’s proposals for eliminating break-points created by the make-whole adjustment, which reallocate costs among shipments of different sizes, these proposals simply assume away costs assigned to multi-car shipments in the current URCS model. Again, while we recognize the Board’s concerns with break-points, there is no empirical evidence that simply eliminating costs will produce more accurate results than the current URCS model.

¹ Union Pacific and other parties noted that actual switching operations may not precisely match how carloads are waybilled in their June 20, 2013, comments on the Board’s NPRM. *See, e.g.*, Comments of Union Pacific Railroad Company at 4-5 & n.4; Comments of the Association of American Railroads at 14; Comments of Alliance for Rail Competition et al. at 4-5.

II. Changes to I&I Switching Mileage

In Union Pacific's comments on the NPRM, we supported the Board's proposal to update the I&I switching mileage assumption. However, as we explained, we were not comfortable with the Board's assumption that the average distance between I&I switches has increased in direct proportion to the increase in average length of haul since 1990. We therefore responded to the Board's request for data by presenting the results of a study in which we determined that, on average, I&I switching of manifest shipments occurs approximately every 250-miles.

Union Pacific updated its study in preparing these comments. Our updated study shows that in the years 2013-2015, I&I switching occurred approximately every 250-260 miles. We provide a more detailed version of the results in Appendix A.²

In the SNPRM, the Board requested additional information regarding Union Pacific's methodology. *See* SNPRM at 22 n.52. Our methodology was straightforward. The operating data we collect in the normal course of business for our manifest traffic captures all en route switches, including I&I switches, for each loaded and empty car cycle, as well as the number of miles for each car cycle. Thus, calculating the average number of miles per I&I switch for manifest traffic is a straightforward exercise. In preparing the tables in Appendix A, we grouped movements by two-digit STCC, assigning empty cars based on the STCC of the prior loaded move, because we thought the added detail might be of informative. However, in calculating the totals, we included

² Pursuant to the 2013 Protective Order in this proceeding, the table in Appendix A is designated as "Highly Confidential." The data regarding I&I switching are verified by Jeffrey S. Meyer, General Director – Measurement & Evaluation for Union Pacific.

cars with unknown or missing STCC codes, so the overall average includes all cars moving loaded or empty in manifest service.³

Union Pacific's empirical study produces results that are similar to the I&I switching mileage figure that the Board proposes to adopt in the SNPRM—now that the Board has adjusted the methodology it used in the NPRM. We continue to believe that use of an individual railroad's actual data regarding the average number of miles per I&I switch would be preferable to using assumptions based on changes in average length of haul, but we appreciate that the Board's proposal is empirically based, and the ultimate results do not appear to be significantly different.

III. Implementation

In Union Pacific's comments on the NPRM, we urged the Board to address how it plans to incorporate the changes into the many uses of URCS and ensure an orderly transition. In the SNPRM, the Board proposes to apply the proposed changes "prospectively," which means that for calculations involving multiple years of URCS data, there would be a period in which there would be a mixing of methodologies. *See* SNPRM at 30.

Union Pacific believes there are uses of URCS for which mixing of methodologies would prove problematic. For example, in Three Benchmark cases, R/VC ratios for four-year comparison group traffic might vary meaningfully from R/VC ratios for current-year issue traffic simply because the former are calculated using the current URCS methodology or a mix of methodologies, while the ratio for the issue traffic is calculated using the proposed methodology. Likewise, changes in the Costed Waybill Sample's calculation of each record's R/VC ratio will undoubtedly change the calculation of each year's RSAM and average R/VC ratios because

³ To be clear, Union Pacific did not intentionally exclude any STCC group from our study. If a two-digit STCC group does not appear in the tables in Appendix A, it is because our source data did not show any movements of manifest traffic with that two-digit STCC.

different movements will fall below or above the 180% jurisdictional threshold. Changes in RSAM will also influence results in the Limit Price Test, which the Board now relies on to determine its jurisdiction in rate cases. The Board's nearly total reliance on changes in R/VC ratios as justification for revoking commodity exemptions in Ex Parte 704(Sub-No. 1) and thereby expanding its regulatory reach provides another cautionary tale against mixing results from different URCS methodologies.

We believe there are other circumstances in which a mixing of costing methodologies could potentially produce significant distortions, such as in the application of Board's Average Total Cost methodology to determine revenues from cross-over traffic and the use of URCS to calculate operating costs for Simplified-SAC. Our concern is not merely the one the Board addresses in the SNPRM—that calculations requiring multiple years of data, as RSAM or R/VC_{>180}, could be calculated using a mix of methodologies. *See* NPRM at 30.

The Board's final rule should acknowledge that mixing of costing methodologies could produce significant distortions during the transition to the proposed costing methodologies, and the Board should expressly allow parties to raise such issues in individual proceedings.

Respectfully submitted,

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October 11, 2016

VERIFICATION

I, Jeffrey S. Meyer, General Director – Measurement & Evaluation for Union Pacific Railroad Company, declare under penalty of perjury that I have read the foregoing Comments of Union Pacific Railroad Company and that the facts and information relating to the average distance between switches for manifest traffic in Union Pacific set forth in Part II and in Appendix A are true and correct, to the best of my knowledge, information, and belief. Further, I certify that I am qualified and authorized to file this Verification.

Executed on October 11, 2016.

/s/ Jeffrey S. Meyer

APPENDIX A

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