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EXPANDING ACCESS TO RATE RELIEF

OPENING COMMENTS OF
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ALLIANCE FOR RAIL COMPETITION
IDAHO BARLEY COMMISSION
IDAHO GRAIN PRODUCERS ASSOCIATION
IDAHO WHEAT COMMISSION
MINNESOTA FARMERS UNION
MONTANA FARMERS UNION
NEBRASKA WHEAT BOARD
NORTH DAKOTA FARMERS UNION
NORTH DAKOTA GRAIN DEALERS ASSOCIATION
OKLAHOMA WHEAT COMMISSION
OREGON WHEAT COMMISSION
SOUTH DAKOTA FARMERS UNION
SOUTH DAKOTA WHEAT COMMISSION
TEXAS WHEAT PRODUCERS BOARD
US GLASS PRODUCERS TRANSPORTATION COUNCIL
WASHINGTON GRAIN COMMISSION
WISCONSIN FARMERS UNION
WYOMING WHEAT MARKETING COMMISSION
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I. INTRODUCTION

Montana Wheat and Barley Committee (“MWBC”) and the other shipper interests identified on the cover (collectively “MWBC, et al.”) welcome the opportunity to comment on the Board’s proposed methodology for smaller disputes brought before the STB over rates imposed by market dominant railroads on captive rail customers. MWBC is an association based in Great Falls, Montana that has for almost 50 years promoted the interests of the State’s wheat and barley producers, who make up its membership and leadership. The other groups joining this filing provide similar services, primarily though not exclusively for producers and/or shippers of agricultural commodities.

MWBC, et al. previously filed comments with Alliance for Rail Competition, as ARC, et al., in the last phase of this proceeding, EP 665 (Sub-No. 1), Rail Transportation of Grain, Rate Regulation Review. Those comments are incorporated herein by reference. MWBC, et al., have also participated with ARC in many other recent STB proceedings involving captive rail customer issues.

Much of what the STB proposes in its Advance Notice of Proposed Rulemaking is as yet unclear, and the value of this new initiative will depend on how it is implemented. At best, it appears to represent a modest step in the right direction that will leave most captive producers’ and shippers’ concerns unaddressed. However, the Board’s proposals may also fall short of meeting even the limited goal of providing a new approach for resolving the smallest disputes over uncommon “outlier” rail rates. MWBC, et al. provide below some suggestions for improving the Board’s new approach.

I. BACKGROUND

It has been over 35 years since the Staggers Rail Act of 1980 fundamentally changed railroad regulation, and those years have been good ones for the railroad industry. Rail lines have been abandoned or spun off the short lines, further efficiency gains have resulted from mergers and consolidations among Class Is, and the major railroads' financial strength has grown steadily, to the point where revenue adequacy has arguably been achieved or exceeded for BNSF, UP, and others.

These benefits for rail carriers, some of which have also benefited rail customers, have not been cost-free. The Staggers Act's promise of rail competition minimizing the need for regulation has been undermined by consolidation that has led to some 95% of rail freight moving via the four largest Class Is, with BNSF and UP dominating much of the West, and NS and CSX dominating much of the East. In Montana, BNSF handles over 90% of rail freight, making Montana the most captive large State in the US.

This consolidation was not accompanied by close regulatory scrutiny. On the contrary, major railroads were allowed to use paper and other barriers to limit competition from short line railroads, Class I consolidation proceedings preserved too little competition (and did nothing to enhance competition), and the ICC

effectively neutralized rail-to-rail competition under 49 USC 11102 in the Midtec decision and others like it.¹

The other side of the Staggers Act coin was the requirement that, where effective competition is absent, a rail rate “must be reasonable”. 49 USC 10701(d)(3). As the steady decline of rail competition increased the amount of captive traffic, the ICC and STB might have been expected to increase the effectiveness of unreasonable rate regulation. However, for over 35 years, the stand-alone cost test of CMP, adopted in Coal Rate Guidelines², has been the only test of rail rate reasonableness that has actually produced significant relief for some captive shippers.

Though the Constrained Market Pricing approach adopted in 1985 included “constraints” based on revenue adequacy, management inefficiency, and phasing, in addition to SAC, only SAC has actually constrained any number of rail rates. And while the Board has developed alternatives to SAC, they have always been too little, too late. Simplified SAC and Three-Benchmark were not even available until 1996³, sixteen years after Staggers and nine years after SAC, periods during which captive non-coal captive shippers had essentially no way of obtaining relief from excessive rail rates.

As the Board acknowledged in its August 31, 2016 ANPR instituting this proceeding, another decade passed with no decisions under SSAC or Three-Benchmark, and the Board belatedly realized that it had fallen short of complying

¹ Midtec Paper Corp. v. Chicago & N.W. Transp. Co., 3 I.C.C. 2d 171 (1986), aff’d, Midtec Paper Corp. v. United States, 857 F.2d 1487 (D.C. Cir. 1988).

² Coal Rate Guidelines, Nationwide, 1 I.C.C. 2d 520 (1985), aff’d, Consol. Rail Corp. v. United States, 812 F.2d 1444 (3d Cir. 1987).

³ Rate Guidelines, Non-Coal Proceedings, 1 S.T.B. 1004 (1996). That this decision was not delayed even longer is attributable to the deadline Congress established in the ICC Termination Act of 1995, in 49 USC 10701(d)(3).

with the statutory mandate to provide a methodology for “those cases in which a full stand-alone cost presentation is too costly, given the value of the case.”

Today, there are indications that the Board may be ready to explore steps that could address the concerns of non-coal captive shippers as to rail rates, and the concerns of all shippers as to rail competition.⁴ Significant improvements are possible without preventing the railroad industry’s progress toward the financial health that was also a goal of the Staggers Act. However, more needs to be done in protecting captive rail customers against abuses.

On the rail rate front, the Board is considering ways of streamlining SAC cases in EP 733, Expediting Rate Cases. Because SAC cases are prohibitively expensive for virtually all captive shippers and producers in the US, that proceeding will offer relief to, at most, a handful of rail customers. In this proceeding, the Board proposes a new approach for smaller rate disputes, different from SAC, SSAC, apparently as a small-case replacement for Three-Benchmark. In addition, while the previous phase of this proceeding focused on captive grain shippers and producers, this phase has been expanded to include other commodities. The goal of having a methodology for smaller rate disputes that avoids the characteristics that have rendered other approaches essentially useless is legitimate, if limited. As stated in the accompanying Verified Statement of Terry Whiteside, “A small amount of relief is better than no relief, which is what we have now.” VS at 6. However, the Board’s proposal needs improvements if it is to provide better regulatory recourse for captive customers with no other remedies.

⁴ Though the Board’s proposals in EP 711 (Sub-No. 1), Reciprocal Switching, should be implemented and strengthened, MWBC, et al., will in many instances be unable to take advantage of new competitive remedies, due to the absence of nearby interchanges. We also note the railroad industry’s outpouring of opposition. Regulatory remedies, necessary in any case, are even more important when competitive remedies are unavailable.

III. GRAIN CUSTOMERS HAVE SPECIAL CONCERNS

Smaller captive rail customers, or customers with smaller rail rate disputes, including producers and shippers of grain and other agricultural commodities, need regulatory recourse when negotiations with market dominant railroads produce no relief. Any captive rail customer who is put at a competitive disadvantage by excessive rail rates may not be able to survive without such recourse. Such customers are especially vulnerable to abuses when smaller amounts are at issue, even though all captive customers have a legal right to protection against unreasonable rail rates.

Railroads often argue that they have no interest in losing any business, but the fact is that larger volumes of freight matter more to railroads than smaller volumes.⁵ Moreover, railroads may welcome the disappearance of smaller accounts if they think they will retain the same freight volumes. For these reasons, MWBC, et al. understand the Board's decision to cover all small captive customer rate disputes, and not just grain rate disputes, in this proceeding. That said, the Board should recognize some special vulnerabilities of producers and shippers of agricultural commodities.

In the first place, it is well-recognized that rail rates on grain have risen significantly for many years. Whiteside VS at 16-18. And while railroads have

⁵ In Reply Comments filed August 25, 2014 in EP 665 (Sub-No. 1), BNSF said that "Approximately 85%-90% of our wheat, corn, and soybean shipments have been made by our top 10 customers" (Reply V.S. of John H. Miller at 2), and UP said "For the period July 2013 through June 2014, UP's top 20 grain customers accounted for more than 82% of our grain revenues" (Reply Comments at 7).

argued that rising wheat prices justify rate increases (as if railroads are entitled to a percentage share of farmers' incomes), the fact is that rail rates do not go down when wheat prices fall. Whiteside VS at 17.

These facts are not new. In comments filed December 22, 2008 in Ex Parte No. 280, Study of Competition in the Freight Rail Industry, MWBC cited Report GAO-07-94, Freight Railroads, for GAO's finding that the routes from Billings, MT and Minot, ND to the Pacific Northwest "had the highest percentage of traffic traveling at rates over 300% R/VC of all routes examined", and that "increases in R/VC from 1985 through 2004 were driven more by increases in revenue than by changes in variable cost." GAO Report at 34-38.

MWBC's comments also cited the November 2008 Study of Competition in the Railroad Industry and Analysis of Proposals that Might Enhance Competition, by Christensen Associates, for the finding that "rates have increased substantially in the last few years, to the point of exceeding 'revenue sufficiency'." The Christensen Report also stated "Our results suggest that grain shippers are not unjustified in viewing themselves as paying relatively high markups."

More recently, the Transportation Research Board found in its June 10, 2015 Special Report 318, Modernizing Freight Rail Regulation, at page 41, that in the period 2002-2013, rail rates on grain and oilseeds went up 80% for smaller shipments (less than 50 cars), and 70% for larger volumes, more than for any other commodity except coal. See also the Report at page 40, finding that by 2013, rail rates for smaller volumes of grain were some 35% higher than for larger volumes of 50% or more. Regulatory remedies for too many of these customers are essentially nonexistent.

Another distinctive feature of grain shipments is that rail rates from grain elevators in Montana and other States to destinations in the Pacific Northwest and other destinations are billed to and paid directly by origin grain elevators, but those amounts are deducted from what the elevators pay the grain producers. Producers and farmers thus bear the rail rates even though the elevators pay railroad freight bills. Whiteside VS at 28.

This fact raises issues of standing, and of representative standing, because of the possibility that a State or State Attorney General might challenge rates on behalf of captive grain producers. Notably, 49 USC 11701(b) provides that “the Board may not dismiss a complaint made against a rail carrier ... because of the absence of direct damage to the complainant.” In its August 31, 2016 decision in this proceeding, the Board said (at n.3) that it would address issues like standing and agricultural rate transparency in a subsequent decision, but no further decision has been issued. It is unfortunate that these comments had to be prepared in the absence of STB guidance on such issues.

IV. THE BOARD’S FOCUS ON “OUTLIERS” LEAVES TOO MANY RAIL CUSTOMERS WITH NO REMEDY

It is clear that expanding this proceeding to cover all rail rate disputes, regardless of commodity, is not the only change the Board proposes. In addition, the new methodology “would include a preliminary screen that would limit its application to shippers that are more likely to be considered captive and to have rates that are outliers.” August 31 decision at 11. In addition, relief will be capped.

Shippers with excessive outlier rates, i.e., rates that exceed comparable rates, but whose disputes do not exceed the relief cap, may benefit, depending on how the new approach is implemented. However, MWBC, et al. are troubled by the outlier focus and by the relief cap. At this point, we will address the outlier focus, leaving the relief cap for later discussion.

As the record previously developed in this proceeding establishes, many agricultural commodities move subject to rates that are similar, or that produce similar R/VCs, applying across broad commodity groups or regions. See the accompanying VS of G. W. Fauth, cost consultant for MWBC, et al., at page 15 and Figure 6. In fact, one of the criticisms raised by MWBC, ARC, et al., The National Grain & Feed Association and USDA in previous comments in EP 665 (Sub-No. 1) was that the R/VCcomp benchmark of the Three-Benchmark approach was a poor fit for agricultural commodities due to pricing with few outliers, involving uniformly high rates or R/VC percentages and similar rate increases.

Shipper and producer interests acknowledged that some grain rates may not be excessive, but argued that effective remedies are required for rates that are too high, and a comparison group limited to other rates at roughly the same level or with roughly the same margins above costs, imposed by the same railroad on similar shipments, will effectively protect many rates with high R/VC percentages. If only outliers qualify for relief, under Three-Benchmark or under the Board's new proposal, non-outlier R/VCs become irrelevant to rate reasonableness determinations, no matter how high they are. Railroads are able to immunize themselves from exposure to rate cases, and regulatory recourse for captive rail customers becomes a sham.

Relief could also be neutralized by rate increases on non-challenged rates in the comparison group. Agriculture groups also argued that there is no justification for additional differential pricing in future rate increases for railroads that have

attained revenue adequacy, much less for railroads that have exceeded revenue adequacy, as BNSF and UP have done recently.

In its August 31 decision at pages 7-8, the Board noted both of these criticisms of the Three-Benchmark approach. However, the Board apparently intends to maintain Three-Benchmark as is, with no remedy for these defects, while adopting a new approach for outlier rates and the smallest rate disputes that perpetuates these defects.

This leaves unaddressed the problem of high but similar rates, R/VCs and rate increases, which adversely affect far more captive shippers and more captive producers of agricultural commodities than outlier rates do. By definition, outlier rates affect small minorities of captive rail customers.

The Three-Benchmark test fails to provide a remedy in many cases for reasons discussed above. See also the recent InterVISTAS Report, An Examination of the STB's Approach to Freight Rail Rate Regulation and Options for Simplification:

The Three-Benchmark procedure is designed to protect individual shippers that are being singled out for abuse. With grain, the “comparable group is composed of other grain shippers. Yet those shippers argue that railroads have instituted across-the-board high rates, causing all comparison groups to face high rates. As a result, rate relief would be unavailable.

See the Report (which many shippers will find superficial in several respects) at p.53.⁶ Like the Board, InterVISTAS offered no solution to this problem, but the

⁶ We would note that InterVISTAS seems to see merit in Three-Benchmark because of analyses the consultants performed finding similarities with SAC results in two cases. This is not a comforting result for the great mass of captive shippers, for whom SAC might as well not exist, and it does not resolve the problem of railroads publishing large numbers of rates that are similar, or produce similar R/VCs. The Report may also be attacked by railroads, which regard

Report's support of Three-Benchmark seems to rest on the idea that it is well-suited to SAC-type cases involving a small number of origin-destination pairs.

MWBC, et al., know the Board cannot fix everything that is wrong with the regulatory status quo in a single proceeding. However, the Board has admitted that SSAC and Three-Benchmark have not met non-coal shippers' and producers' needs. The Board did not provide an adequate explanation for rejecting the proposed Two-Benchmark approach, which we continue to support. Nor did it adequately explain its rejection of the NGFA approach, involving an Ag Commodity Maximum Rate Methodology, for which MWBC, et al. expressed support if the Board was unwilling to pursue Two-Benchmark.

The Board's latest proposals were designed to address, at best, a very small subset of the universe of high non-coal rates on captive traffic. At page 16 of the August 31 decision, the Board suggests that its proposed "screen" would include only the top 10%-20% of rates (thereby excluding 80% to 90% of rates paid by captive rail customers). However, captive shippers of all commodities, with disputes large and small, must be able to challenge high rail rates as excessive. Between full SAC and its new proposal for the smallest rate disputes, what solutions does the Board offer?

We understand that this question could be answered in other proceedings. In particular, the possibility of an effective revenue adequacy constraint, for which we have been waiting since 1985, might give hope to shippers and producers who gain nothing from the "small dispute" test for outlier rates proposed here. In EP 722, Railroad Revenue Adequacy, the Board could fulfill the decades-old promise of

Three-Benchmark as meritless. Moreover, though the consultants note the importance of revenue adequacy, they apparently did not look at revenue adequacy determinations after 2007, the most recent of which show railroads exceeding revenue adequacy.

CMP. Captive grain and other shippers and producers whose rates are not outliers, or whose disputes are not small enough for the relief proposed in this proceeding, might finally have some effective regulatory recourse.

Relief under the revenue adequacy constraint might be limited to restrictions on further differential pricing in the form of future rate increases on captive traffic that exceed inflation or exceed increases on non-captive traffic, where the railroad is at or above revenue adequacy. “Carriers do not need higher revenues than this, and we believe that, in a regulated setting, they are not entitled to any higher revenues.” Coal Rate Guidelines, *supra*, 1 I.C.C. 2d at 535.

The Board might also supplement this relief with the possibility of some reduction in past rate increases that included excessive differential pricing by railroads at or above revenue adequacy. Such initiatives could provide effective new remedies for non-coal captive shippers who have, for decades, had little choice but to pay whatever the railroad demanded.

The railroads claim, falsely, that a revenue adequacy constraint is equivalent to a rate cap. It is not, because all non-captive customers would be subject to unrestricted rail rates, and most captive customers would still be subject to rate increases if those increases did not reflect further unnecessary and unjustifiable differential pricing.⁷ Moreover, as the railroads are well aware, few captive rail customers with meritorious claims against railroads pursue them. This is particularly true of ag interests, for reasons explained by Mr. Whiteside (VS at 6-7).

⁷ See also the discussion at pp 31-33 of the opening comments filed by ARC, et al., in EP 722, discussing other factors making such railroad arguments specious.

In contrast, captive rail customers able to invoke a revenue adequacy constraint would still not be entitled to the same relief as captive coal shippers in successful SAC cases, because most past differential pricing would not be subject to any remedy outside of SAC cases. But at least a revenue adequacy constraint could satisfy part of the need for a remedy for captive rail customers like those represented by MWBC, et al., for whom SAC, SSAC, Three-Benchmark and the Board's latest proposed approach are of little or no value.

V. THE BOARD'S LATEST PROPOSAL MAY PROVE INEFFECTIVE EVEN FOR SMALL DISPUTES OVER OUTLIER RATES

Not only does the new methodology proposed in the Board's August 31, 2016 decision fail to meet the needs of most non-coal captive rail customers, but it may not even meet the needs of its intended beneficiaries.

The source of the Board's new proposal is unclear. The decision cites prior filings in EP 665 (Sub-No. 1) by ARC, et al., NGFA, USDA, and by railroads and others. However, the Board has not adopted the recommendation of any party.

The Board's new proposal may derive, to some extent, from the TRB's Modernizing Freight Rail Regulation report. At page 91 of that Report, the TRB argued against continued use of SAC, SSAC and Three-Benchmark. Rather, the TRB urged basing maximum reasonable rate determinations on unregulated, market-based rail prices, as to which the Board has extensive information in its confidential Waybill Sample. Such competitive pricing data could be used to produce "models of rates developed under effectively competitive conditions", and

rates exceeding that level, or some designated level above it, could be the new benchmark.

To the extent that the Board's new proposal seeks to reflect the TRB recommendations, the methodology should be applicable more broadly, to rates that are not outliers, in cases other than the "smallest". And if the Board is undertaking a pilot project to test its new ideas, there are ways it can modify its proposal to increase its chances of success.

As proposed, the methodology appears too likely to hurt smaller shippers and producers, and others with smaller disputes. A number of deficiencies are detailed in the accompanying Verified Statement of Witness Fauth, , but problem areas include the issues discussed below.

A. URCS and Other Costing Issues

As explained by Mr. Fauth in previous comments in EP 665 (Sub-No. 1), features of STB rail costing under the Uniform Rail Costing System, or URCS, put grain shippers, and especially smaller ag customers like shippers and producers of pulse crops, at a disadvantage.⁸ In the VS filed herewith, Mr. Fauth reiterates and expands his prior comments, in light of the August 31, 2016 decision in this proceeding.

Summarizing that testimony, Mr. Fauth shows that issues raised in the past have, for the most part, not been corrected in the Board's latest decision. There are shippers of agricultural commodities whose rates are truly below 180% of variable

⁸ Pulse crops include peas, beans, lentils, etc., and many such shipments move in carload volumes. These days, many wheat and barley producers are also producers of pulse crops. Whiteside VS at 17 and 21-27.

cost, who do not qualify for rate relief. However, there are many other rail customers paying rates on grain and other agricultural commodities whose rates would generate R/VC percentages above the STB jurisdictional threshold, but for URCS costing features and railroad costing features that work to the disadvantage of such shippers and producers.

For example, the use of unadjusted URCS jurisdictional costing, which requires railroad system-average costs rather than movement-specific costs, makes costs of service appear higher than they actually are for shipments in highly efficient trainload and unit-train volumes. Shipments in smaller volumes might seem to be the beneficiaries of such costing, but the URCS “make-whole” adjustment, which effectively shifts costs to smaller shipments, can drive up those costs and drive down those R/VCs.

Mr. Fauth has also determined that there are multiple car shipments involving more than one car per switch that railroads, for reasons of their own, report as single-car shipments. See his comments in EP 665 (Sub-No. 1). These practices undermine the reliability of Waybill Sample data. In fact, not only are many multiple car shipments erroneously reported as single car shipments, but railroads routinely combine smaller shipments into larger trainload or unit-train shipments for most of the haul to distant export elevators and other destinations, like the Pacific Northwest. BNSF had in its tariff a “marriage” rule providing that shippers of wheat in 48-55 car volumes must contact other smaller shippers, including competing elevators or producers, to locate a second 48-55 car wheat shipment going to the same destination, so BNSF can combine the shipments for greater efficiency. This tariff requirement was later dropped, but BNSF continues to combine smaller volume shipments to reduce its cost of service.

B. RATE CASE LIMITS AND RELIEF CAPS

At page 16 of its August 31 decision, the Board suggests imposing a limit on the number of rate cases a complainant may bring against a defendant railroad within a set number of years, and at page 23 it proposes a relief cap similar to the one adopted for Three-Benchmark cases.

Under the relief cap, the amount of relief obtained based on the Board's finding that the challenged rate exceeded the comparison group standard would be subject to a time limit or "prescription period". If the complainant took some rate relief in the form of reparations for excessive amounts collected by the railroad prior to the Board's decision, the amount of relief that could be used to reduce the challenged rate subsequent to the Board's decision would be the total damages less the reparations amount.

As a result, the relief could be exhausted before the end of the prescription period, at which point the railroad could raise its rate back up to the level originally challenged, i.e., up to an amount exceeding the comparable rates on which relief had been based. In addition, the railroad could escalate the restored rate using the RCAF-A adjustments. If no other rate escalation were taken the shipper could file no new rate challenge. If greater increases were taken by the railroad, the shipper that exhausted its relief by taking some reparations could challenge the excess. Put another way, a shipper who sought relief from rates creating a competitive disadvantage could see those rates, and that disadvantage, restored if it took the reparations provided for in the Act.

MWBC et al., see a number of problems with these restrictions. In the first place, they diminish the value of an untested methodology whose value already appears marginal for many shippers and producers. Presumably the Board's intent is to avoid a deluge of new rate cases by increasing the number and complexity of the tests of reasonableness, and decreasing the relief available to successful complainants. The Board would be better advised to consider the likelihood that shippers who are already reluctant to file complaints against market dominant railroads will continue to regard recourse to the STB as a non-starter. As Mr. Whiteside points out (VS at 6), retaliation by market dominant railroads against smaller customers is possible, and could take a number of forms, including poor service, increased charges, and increased rates on shipments excluded by the STB's screen. The specter of too many small rate cases being filed by captive shippers unable to afford SAC has never been a legitimate ground for concern at the STB.

The Board explains its restriction on the number of rate cases as a deterrent to splitting one large case into many smaller cases brought at or near the same time. Here again, we question whether the Board's fears are realistic, and we suggest that a better approach would be for the Board to make its other simplified approaches, SSAC and Three-Benchmark, more user-friendly.

In any event, the Board should be aware of a special concern for small ag interests in Montana and possibly other agricultural States. BNSF's market dominance is so pervasive in Montana that the State Government might explore legal action on behalf of small producers like the members of MWBC, who might otherwise be unable to undertake rate litigation. It is not clear what form such a challenge or challenges might take, but a possible approach might be for the

Attorney General to bring more than one test case, challenging, for example, high wheat rates in one part of the state and high rates on pulse crops in another.

Under 49 USC 11701(b), such complaints could not be dismissed merely because the Attorney General, as nominal complainant, was not directly injured. However, the Board's proposed limit on rate cases by a complainant could set up a conflict with any such "parens patriae" actions.

It may be that the Board will address such scenarios when it issues the "subsequent decision" said to be forthcoming in footnote 3 to the August 31 decision. However, the Board should consider whether it can employ other measures to deal with its concerns about the splitting of one large case into many small ones challenging the same rate.

As for the proposed relief cap, the Board is again misconceiving the real problem if it regards too many captive shippers and producers receiving too much relief as a significant concern. Excessive generosity toward captive rail customers abused by monopoly railroads is not the way anyone would characterize the last 35 years of railroad regulation.

It may rather be that the STB sees itself as offering a "hierarchy" of remedies for unlawful rates. Full SAC might be considered the gold standard (the railroads consider it the only legitimate test of rate reasonableness). SAC costs the most and could therefore be seen as supporting the most relief. (Relief under SSAC was recently freed of its relief cap, but it may cost as much as SAC, and it cannot provide as much relief as SAC even without a cap, so SSAC's role in the hierarchy is unclear.)

Three-Benchmark cases cost significantly less than SAC cases, so Three-Benchmark relief is subject to a Board-imposed cap of \$4 million over a five year

period. And the Board may feel that the new “small-case” method proposed in this proceeding, if it costs less than a Three-Benchmark case, should be subject to an even lower relief cap.

In the last phase of this proceeding, agricultural rail customer interests explained at length why Three-Benchmark is inadequate, so it is troubling to learn that the Board sees Three-Benchmark as too generous for smaller cases. This is particularly problematic given the outcome of a Three-Benchmark case in which relief was actually awarded. In the U. S. Magnesium rate case⁹, the shipper obtained relief only to the extent that the challenged UP rates exceeded 300% of variable cost. If the new methodology for smaller rate cases must be capped in order to produce less relief than this, the only beneficiaries will have to be complainants with small rate disputes involving astronomical rates.

More fundamentally, relief caps are inherently arbitrary, and arbitrary in a way that can harm only the complainant. If the cap applies at all, that will mean the shipper was otherwise entitled to rate relief it was prevented by the cap from obtaining, and the railroad is left in possession of revenues exceeding maximum reasonable levels. The main result is to penalize smaller shippers and shippers with smaller rate disputes.

It is unfortunate that railroads which break the law by charging unreasonable rates on captive traffic are not subject to penalties that might deter further violations. The Board is able, at best, to make such railroads return, with interest, excessive amounts they have collected during the limitation period, making the victimized shipper more or less whole. Given how few rate cases are brought, this

⁹ U. S. Magnesium, LLC v. Union Pacific Railroad. STB Docket NOR 42114, decision served January 28, 2010, aff'd sub nom. Union Pacific Railroad v. STB, 628 F.3d 597 (D.C. Cir. 2010).

slight risk cannot serve to deter abuses of railroad monopoly power. Imposing a relief cap for which no justification has been offered insures that fewer shippers and producers experiencing such abuses will see the STB as a viable source of relief.

C. Broadening the Characteristics of Comparison Group Traffic

The Board proposes (Decision at 13) to exclude from its comparison group any traffic moving at R/VC percentages below 180, citing the need to protect “permissible demand-based differential pricing” by market dominant railroads. Doing this would further weaken what already appears to be a weak remedy. If a shipper pays an outlier rate because the railroad charges rates below the jurisdictional threshold to the shipper’s competitors, even a successful rate challenge under the new methodology will leave intact part of the complainant’s competitive disadvantage.

In addition, where the railroad is at or above revenue adequacy, there is little or no rationale for continuing to protect all differential pricing of captive traffic in rate cases. Complainants should be allowed to argue for inclusion in the comparison group of rates with R/VCs below 180%. As Mr. Fauth points out in his attached Statement, many ag shipments in Montana and other States may be subject to qualitative market dominance even if the R/VC is below 180% (Fauth VS at 33). URCS corrections might mitigate this problem but changing URCS cannot create transportation alternatives where none exist.

Mr. Fauth also explains the need to allow shippers or producers of one commodity to be able to cite comparisons with rates charged for another commodity. The basic problem with excessively restricted comparison groups is that they tend to facilitate, and reward, similarities of pricing, especially if the

focus is on a single commodity, or a single railroad. As explained in EP 665 (Sub-No.1), looking only at BNSF rates on Montana wheat not only eliminates most outliers, but it also enables BNSF to limit or eliminate its own exposure to small rate challenges. When more railroads, more commodities, more R/VC percentages (above and below 180%), and more mileages are available for comparison, railroads must look more closely at the reasonableness of their own pricing practices.

Greater simplicity of comparison groups and analysis may help reduce the cost and time needed rate challenges under the Board's new proposal, and shippers and producers will not be able to match the resources of railroad defendants, particularly in the "smallest" cases. However, inexpensive proceedings that cannot provide relief due to an excessively narrow comparison group are not helpful.

MWBC, et al. support the Board's proposal (Decision at 13) to include contract traffic, even if relatively few smaller grain shipments move under contracts. So does the TRB Report. As for the "common carrier adjustment" from U. S. Magnesium, *supra*, under which non-contract shipments would be marked up on the theory that contract shipments move at lower rates than tariff shipments, such an adjustment would further weaken the new methodology. In U.S. Magnesium, the markup was almost 15%. It is also unnecessary for agricultural commodity shipments. Unlike the shipments at issue in U.S. Magnesium, there is no shortage of Waybill Sample data on ag shipment tariff rates.

We support including non-defendant carrier rates in the comparison group. At a minimum, excluding such data is inconsistent with the goal of identifying and providing recourse as to high outlier rates. Railroads can be outliers vis-à-vis other railroads just as captive shipper rates can be outliers when compared with other

rates. It is highly likely that some of Railroad A's rates will be higher than arguably similar rates of Railroad B, and some of A's rates will be lower than B's.

The potential third party discovery concerns cited by the Board (Decision at 15) cannot justify exclusion of evidence as to, say, UP grain rates in a BNSF grain rate challenge. If the Board's methodology "works" in such situations but does not work if lower UP rates for similar shipments are ignored, the complainant should be allowed to pursue reasonable and cost-effective discovery. Issues of access and burdens can and should be dealt with on a case-by-case basis.

D. Revenue Adjustment, Confidence Interval and Commodity-Specific RSAM

At pages 21-22 of its August 31 decision, the Board indicates its intention to apply the "confidence interval" adjustment of Three-Benchmark to its new outlier methodology. MWBC, et al., are concerned that this is yet another element of the new test that benefits only railroads. In their Opening Comments filed June 26, 2014 in EP 665 (Sub-No. 1), NGFA argued that a confidence interval "artificially raises the rate reasonableness bar by moving the comparison group R/VC ratio to the upper boundary of the interval."¹⁰

The Board's new test is designed to help a small minority of captive rail customers. Is a thumb on the scale in the form of a confidence interval adjustment really necessary? The Board might consider testing its new approach with and without this component.

The same question could be asked about the Board's request for comments on a commodity-specific RSAM (decision at 22). Assuming an argument can be made

¹⁰ Crowley VS at 14.

for disaggregated RSAMs for rail carriers well short of revenue adequacy, it is not clear why such a complex and controversial undertaking is necessary, in rate cases that will be brought rarely and with small amounts at stake, for BNSF (most recent 4-year RSAM 182%) and UP (most recent 4-year RSAM 186%).¹¹

E. Procedural Considerations

In its discussion of procedural rules, the Board proposes standardized complaints and answers, based on required initial disclosures, sequential rather than simultaneous filing (complainant opens and respondent railroad replies), and evidentiary hearings. It also proposes page limits on presentations. For reasons explained by Mr. Fauth (VS at 39), MWBC, et al. oppose page and word limits. These are particularly troubling when a new methodology is first being explored.

In addition, the Board would issue two decisions, making final findings as to market dominance and rate reasonableness only in the second decision, after having previously resolved R/VC issues and URCS disputes, and determining whether the issue traffic meets the preliminary screen based on the initial comparison group.

MWBC, et al., have not litigated STB rate cases in the past. Hardly any non-coal captive shippers have litigation experience, for reasons discussed above. STB methodologies other than SAC (with which MWBC's counsel and consultant do have experience) were always seen as too costly and too ineffective to support a challenge to rates on agricultural commodities, especially in light of the 17-year ordeal of McCarty Farms. (Whiteside VS at 6.) As also shown above, MWBC, et

¹¹ See the decision served February 26, 2016 in EP 689 (Sub-No. 7), Simplified Standards for Rail Rate Cases – 2014 RSAM and R/VC>180 Calculations.

al., continue to have concerns about the effectiveness and viability of the Board's latest proposals.

Procedural issues are obviously secondary to substantive concerns. At first glance, some of what the Board proposes procedurally appears reasonable, though the Board may need to hold off on rigid application of restrictions on shippers, and on page/word lengths, in the first case or cases to test the new approach (assuming such cases are brought). Nevertheless, MWBC et al. reserve the right to say more about procedural issues (and discovery) after reviewing other opening comments filed in this proceeding.

VI. CONCLUSION

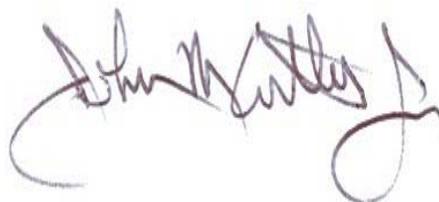
MWBC, et al. probably include potential beneficiaries of the Board's attempt to develop a new test of maximum rate reasonableness. However, we note that even in a proceeding aimed at the smallest rate disputes, and at a time when high rail rates are otherwise subject to effective regulation only in the rare SAC case, the Board's proposals reflect more concern for protecting railroad revenues than for protecting captive shippers' statutory right to reasonable rates. Doing something for shippers, but no more than the minimum, seems to be the theme. This impression may be erroneous. If it is, EP 722, EP 711 and other current and future proceedings may produce welcome changes.

In this proceeding, the Board's goals may be good, and small numbers of captive shippers and producers may be eventually gain the ability to seek small amounts of relief. This relief may be significant for some small ag producers

(depending on how the Board elects to deal with standing and other issues), and others with the smallest rate disputes, but more could and should have been done. Three-Benchmark still needs reform, to address the needs of non-outlier rates and larger rate disputes. Moreover, the Board must shift its focus to captive shipper needs where railroads are exceeding adequate revenue levels. This is the reality in the West, where MWBC et al. operate. We therefore urge the Board to implement the changes in its current proposal recommended in these comments, and to address the concerns of captive ag customers whose needs this proceeding ignores.

Dated: November 14, 2016

Respectfully submitted,



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Representing Shipper Interests
Identified Above

Attorney for Montana Wheat and
Barley Committee and ARC

CERTIFICATE OF SERVICE

I hereby certify that I have this 14th day of November caused copies of the foregoing document to be served by mail or electronic means on all parties of record.

A handwritten signature in dark ink, appearing to read "John M. Cutler, Jr.", written in a cursive style. The signature is positioned above a horizontal line.

John M. Cutler, Jr

PUBLIC VERSION

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

**DOCKET NO. EP 665 (SUB-NO. 2)
EXPANDING ACCESS TO RATE RELIEF**

**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. A statement describing my background, experience and qualifications is attached hereto as Appendix GWF-1.

In a decision in these proceedings served August 31, 2016, the Surface Transportation Board (STB or Board) is seeking comments and suggestions through an Advance Notice of Proposed Rulemaking (ANPR) regarding the Board's effort to develop a new rate reasonableness methodology for use in very small disputes, which would be available to shippers of all commodities where the challenged rates qualify as "outlier." I have been asked by Montana Wheat & Barley Committee (MWBC) to review and analyze the Board's proposal and submit these comments.

PUBLIC VERSION

The Board's decision in this proceeding is an outgrowth of its earlier decision in STB Docket No. EP 665 (Sub-No.1), Rail Transportation of Grain, Rate Regulation Review, served December 12, 2013, in which the Board invited public comment on how to ensure that the Board's existing rate complaint procedures are accessible to grain shippers and provide effective protection against unreasonable freight rail transportation rates, including proposals for modifying existing procedures or new alternative rate relief methodologies. The Board stated: "We believe it is appropriate to consider what regulatory changes could be implemented to ensure that the Board's rate case procedures are fully accessible to grain shippers and provide effective relief from excessive freight rail rates, as appropriate." (Decision at page 2).

In response to the Board's decision, several Ag-related groups submitted comments. For example, U.S. Department of Agriculture (USDA) indicated that, despite the dramatic financial improvement of the railroad industry, "most agricultural shippers continue to be left with no practically accessible means to challenge rail rates, much less seek redress." (USDA, page 2) I submitted opening comments on June 26, 2014 and reply comments on August 25, 2014 on behalf of MWBC and several other Ag-related groups. My testimony described the many problems faced by grain and grain products shippers associated with the Board's current jurisdiction costing and rate reasonableness methodologies.¹

¹ Alliance for Rail Competition (ARC), National Farmers Union, Colorado Wheat Administrative Committee, Idaho Barley Commission, Idaho Grain Producers Association, Idaho Wheat Commission, Montana Farmers Union, North Dakota Corn Growers Association, North Dakota Farmers Union, South Dakota Corn Growers Association, South Dakota Farmers Union, Minnesota Corn Growers Association, Minnesota Farmers Union, Wisconsin Farmers Union, Nebraska Wheat Board, Oklahoma Wheat Commission, Oregon Wheat Commission, South Dakota Wheat Commission, Texas Wheat Producers Board, Washington Grain Commission, Wyoming Wheat Marketing Commission, USA Dry Pea and Lentil Council, and National Corn Growers Association.

PUBLIC VERSION

As indicated therein, many captive grain and grain products producers and shippers are disadvantaged by the STB's URCS make-whole adjustments and the unadjusted URCS jurisdictional costing approach (which exaggerates the cost of service, driving many R/VC ratios below 180% and beyond STB jurisdiction). Grain and grain products shippers are also harmed by the STB's recently adopted "Limit Price" approach to market dominance determinations, under which the issue R/VC ratios may need to exceed the STB's published "RSAM" percentages (which currently range from 182% to 327%²) in order for the Board to find market dominance. These jurisdictional hurdles make it very difficult for the vast majority of railroad grain and grain products shippers to get in the STB's door in order to challenge the reasonableness of high rail rates. I also indicated that the STB's Full-SAC and Simplified-SAC tests are not viable options for most grain and grain products shippers (and most non-coal shippers) and the many problems associated with the simpler and cheaper Three-Benchmark test.

Despite initially emphasizing the problems faced by grain shippers and producers, the Board, in its most recent decision, has now decided that "the existing rate review processes present accessibility challenges for not only grain shippers, but also small shippers of any commodity." Therefore, the Board has proposed "a new rate review process that would be more affordable and accessible to shippers of all commodities with small disputes." (Decision at page 3). Unfortunately, this proposed "new rate review process," will do little to address the problems faced by most captive grain shippers and producers.

² See STB Docket No. EP 689 (Sub-No.7), Simplified Standards For Rail Rate Cases - 2014 RSAM and R/VC_{>180} Calculations, served February 26, 2016, page 3.

PUBLIC VERSION

Montana Railroad Grain Movements

In order to evaluate the potential impact of the Board’s proposed new procedures will have on grain shippers, I reviewed and analyzed *every* railroad movement of wheat (STCC 01-137), barley (STCC 01-131), peas (STCC 01-132) and lentils (STCC 01-343) originating from Montana included in the 2014 Confidential Waybill Sample. In addition to MWBC being one of my primary clients in these proceedings, Montana grain producers and shippers are also some of the most captive rail customers in the U.S.

In 2014, these four farm products accounted for 7.93 million tons produced in Montana. The following table compares the tons produced in Montana with the rail tons originated from Montana by railroad:

Figure 1

Summary of Montana Grain Tons Produced and Originated By Railroad

Item	Wheat	Barley	Peas	Lentils	Total
2014 MT Tons Produced (USDA)	6,284,100	1,035,840	512,344	98,616	7,930,900
BNSF Tons Originated					
CP Tons Originated					
UP Tons Originated					
<u>MRL Tons Originated</u>					
Total MT Rail Tons Originated					
Rail % Tons					

PUBLIC VERSION

As can be seen, the railroads originate nearly [redacted] of the total tons produced in Montana and BNSF is the dominant railroad, originating [redacted] tons out of the total 7.93 million tons, or [redacted], of the total tons produced in Montana.

I reviewed the records for every origin and destination pair. In addition to identifying, sorting, summarizing and analyzing the Waybill Sample records by STCC, for each individual origin and destination Standard Point Location Code (SPLC) pair, I also distinguished between movements in private and railroad equipment and movements in ≥ 100 car shuttle trains and trainloads versus non-trainloads, since railroad rates and URCS costing are structured differently based on these factors. Therefore, an individual origin and destination pair may represent more than one movement.

BNSF clearly dominates the Montana grain railroad transportation market, which is illustrated in the following table:

Figure 2

Summary of 2014 Railroad Grain Movements From Montana

Origin Railroad	Commodity	STCC	Carloads	Tons	Revenue (000)	Miles
	Wheat	01-137				
	Wheat	01-137				
	<u>Wheat</u>	<u>01-137</u>				
	Wheat	01-137				
	Wheat	01-137				
	Barley	01-131				
	Barley	01-131				
	<u>Barley</u>	<u>01-131</u>				
	Barley	01-131				
	Barley	01-131				
	Peas	01-342				
	<u>Peas</u>	<u>01-342</u>				
	Peas	01-342				
	Peas	01-342				
	Lentils	01-343				
	<u>Lentils</u>	<u>01-343</u>				
	Lentils	01-343				
	Lentils	01-343				

In addition to these grain commodities, a limited amount of soybeans (cars), corn (cars), oats (cars) and other miscellaneous grain commodities moved by rail.

PUBLIC VERSION

BNSF originates the vast majority of this railroad grain traffic (e.g. _____ of the grain tons studied) from Montana. Despite BNSF domination of the Montana railroad grain transportation market, only a limited number of Montana rail grain customers have access to the STB's rate procedures.

The following table compares STB jurisdictional (RVC \geq 180%) and non-jurisdictional (RVC<180%) BNSF wheat traffic from Montana:

Figure 3

**Comparison of STB Jurisdictional and Non-Jurisdictional
BNSF Wheat Movements From Montana**

Item	<180% RVC	\geq180% RVC	Total
Number of Movements			
% of Total Movements			
Average Cars Per Shipment			
Average Miles			
Total Carloads			
% of Total Carloads			
Total Tons			
% of Total Carloads			
Total Revenue			
% of Total Revenue			
Average Revenue Per Car			
Average Rate/Ton-Mile (ϵ)			
Average RVC			

PUBLIC VERSION

As can be seen, (out of movements) of the individual BNSF wheat movements from Montana have R/VC ratio below 180%. These BNSF wheat movements, on average, pay higher rates per car (\$ versus \$ per car), but do not have access to the STB’s rate reasonableness procedures. These non-jurisdictional BNSF wheat movements have smaller shipment sizes (versus cars per shipment), move significantly lower volumes (versus tons), and move much greater distances (versus miles -- which decreases potential truck competition and thus increases the likelihood of railroad market dominance).

The following table compares STB jurisdictional (RVC \geq 180%) and non-jurisdictional (RVC<180%) BNSF barley traffic from Montana:

Figure 4

**Comparison of STB Jurisdictional and Non-Jurisdictional
BNSF Barley Movements From Montana**

Item	<180% RVC	\geq 180% RVC	Total
Number of Movements % of Total Movements			
Average Cars Per Shipment			
Average Miles			
Total Carloads % of Total Carloads			
Total Tons % of Total Carloads			
Total Revenue % of Total Revenue			
Average Revenue Per Car			
Average Rate/Ton-Mile (¢)			
Average RVC			

PUBLIC VERSION

The majority () of the individual BNSF barley movements from Montana have R/VC ratios below 180% and thus do not have access to the STB's rate reasonableness procedures. These non-jurisdictional BNSF barley movements have smaller shipment sizes (versus cars per shipment), move much greater distances (versus miles) and have significantly higher average rates (\$ versus \$ per car). Unlike BNSF Montana wheat movements, most of the barley volume (% of the carloads and % of the tons) moves at rates below 180%. For both wheat and barley movements, the R/VC percentages are lower than they would be with more accurate movement costing.

Although the limited number of jurisdictional BNSF Montana barley movements (movements) have a high average R/VC of , it is likely that BNSF would claim lack of market dominance due to the short distances of these movements (average miles). The barley movement with the highest R/VC () moves a distance of only miles.

The jurisdictional numbers for peas and lentils numbers are even lower than barley. Out of carloads of peas originating from Montana, only carloads () moved at a R/VC ratio above 180% and the highest R/VC is . Out of carloads of lentils from Montana, carloads of lentils have rates which generated a R/VC above 180%.

Notwithstanding BNSF's domination of the Montana railroad grain transportation market and the captive nature of the traffic, only a limited number of Montana wheat shippers, very few barley shippers and practically no peas and lentils shippers have access to the STB's rate procedures, under current URCS costing rules and procedures that I and many others (including the Transportation Research Board (TRB)) have criticized.³

³ See June 2015 Report by TRB titled: Modernizing Freight Rail Regulation.

PUBLIC VERSION

This does not mean that BNSF is benevolent monopolist, which only charges marginally profitable grain rates. Most grain movements are very profitable for BNSF, but BNSF (and the other railroads) takes advantage of the STB's unadjusted URCS costing system and procedures that significantly overstate the variable costs for most grain movements.

BNSF's ≥ 100 Car Shuttle/Trainload Wheat Movements From Montana

Most of the BNSF wheat traffic from Montana moves in shuttle trains or trainloads of or more cars. Out of the identified BNSF wheat movements from Montana, involved movements with an average of 100 cars per train or more. These BNSF shuttle train and trainload wheat movements account for of the total wheat tons originated by BNSF and jurisdictional tons.

These ≥ 100 car shuttle/trainload movements are also very profitable for BNSF. In fact, every BNSF shuttle or unit train wheat movement from Montana has a R/VC which exceeds and the movements have an average R/VC and range from to .

BNSF knows that it has market dominance over most Montana grain movements. Therefore, BNSF knows that this grain traffic is subject to STB jurisdiction. As a result, BNSF plays close attention to the R/VC levels, which results in fairly uniform R/VC ratios with very few outliers. Although the R/VC ratios for BNSF's shuttle/trainload wheat movements from Montana range from to , most of the ratios are fairly uniform with few outliers.

PUBLIC VERSION

In fact, it appears that the limited number of ≥ 100 car BNSF Montana wheat outliers may be costed incorrectly by the STB's waybill sample costing procedures resulting in a cost understatement and R/VC overstatement.

BNSF distributes most grain cars under its Certificate of Transportation (COT) program under which customers bid for covered hopper cars according to a weekly schedule, subject to availability. The BNSF COTS fleet includes both railroad-owned and leased covered hoppers. Some of these leased covered hoppers have private car markings, such as CEFX, which is the car marking for cars leased by CIT Group/Equipment Financing to BNSF and other railroads. When these cars show up in the STB's waybill sample, the movements are treated and costed as private car movements. The following table summarizes the BNSF shuttle and trainload wheat movements which move in railroad and private cars:

Figure 5

**Comparison of >100 Car Shuttle and Trainload
BNSF Wheat Movements From Montana**

Item	Railroad Cars	Private Cars	Total
Number of Movements % of Total Movements			
Average Cars Per Shipment			
Average Miles			
Total Carloads % of Total Carloads			
Total Tons % of Total Carloads			
Total Revenue % of Total Revenue			
Average Revenue Per Car			
Average Variable Cost Per			
Average Rate/Ton-Mile (¢)			
Low R/VC			
High R/VC			
Average RVC			

As can be seen, the shuttle/trainload movements with the highest R/VC ratios were treated as private cars by the STB's unadjusted URCS costing procedure included in the Waybill Sample. Although the average variable cost assigned to these movements is lower (versus per car), the average shipment size, miles, rates per car and per ton-mile for these movements are not significantly different than for the movements in railroad cars.

PUBLIC VERSION

These “private” car movements with high R/VC ratios, which average _____ and go up to _____, represent approximately _____ of the BNSF shuttle/trainload wheat carloads and tonnage from Montana. Unless a movement truly involves dedicated private cars leased by the grain shipper or producer outside the BNSF COT program, the R/VC ratios for these movements may be overstated as a result of miscoding and treatment as a private car movement in the Waybill Sample. Therefore, I have excluded these private car grain movements from my studies.

Conversely, the R/VC ratios for most of the shuttle/trainload grain movements in railroad-owned cars are understated and depressed because of the STB’s unadjusted URCS costing approach, which fails to adequately reflect the efficiencies of these movements.

In my Reply Verified Statement in EP 665 (Sub-No.1), I noted that the Opening Comments of the railroads include many references to the efficiencies associated with grain movements:

- AAR – “Railroads offer a variety of rail service options (single car, multiple cars, trainload, or shuttle trains) to grain shippers, and data show a clear trend toward more efficient grain movement types.” (AAR, page 11)
- AAR – “Large, more efficient long-hauls for grain drive down costs. The continuing trend toward such shipments is driven by competition and reflects market forces that call for grain transportation to be as efficient as possible.” (AAR page 12)
- BNSF – “Since the enactment of the Staggers Act in 1980, rail grain operation have become much more efficient.” (BNSF, page 8)
- BNSF - “The use of shuttle trains is now a major form of transportation on BNSF.” (BNSF, page 8)
- BNSF – “The increase in shipment size resulted in more efficient operations and lower cost per unit of traffic shipped.” (BNSF, page 8)

PUBLIC VERSION

- BNSF – The COT program introduced in 1988 “allows cars to be allocated more efficiently based on demand and also provides BNSF with information on expected future equipment needs to better plan for service during periods of high demand.” (BNSF, page 12)
- BNSF – “The COT’s and shuttle programs have led to significant improvements in the allocation of grain cars and the efficiency of grain transportation.” (BNSF, page 13)
- UP – “Over the past 35 years, rail grain transportation has evolved to place much greater reliance on trainload service. This evolution was driven by marketplace demands to create a more productive and efficient transportation.” (UP, page 7)
- UP – “Shuttles are therefore able to cycle back and forth between origin and destination very rapidly, which allows them to handle large amounts of grain quickly and efficiently.” (UP, page 8)
- CSX – “CSXT's core feed grain business continues to grow and become more efficient.” (CSX, page 7)

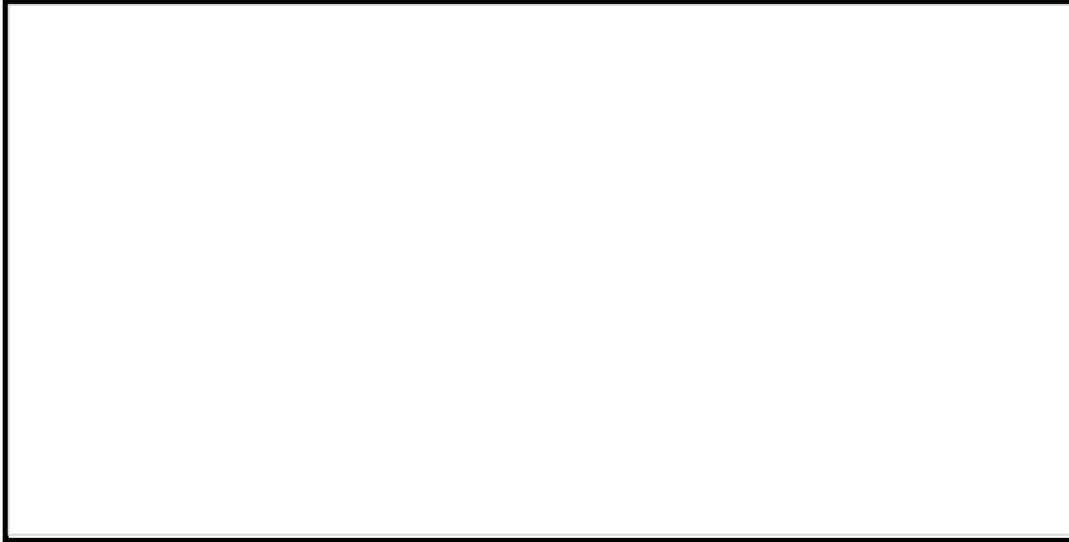
These efficiencies are not adequately reflected in the STB’s URCS costing procedures. In most cases, the R/VC ratios for BNSF shuttle and trainload movements are understated as a result of an overstatement of the variable cost stemming from the use of unadjusted URCS switching and car cost. There is little or no switching associated with these movements and the car costs are generally lower than URCS system average as a result of significantly lower than average car cycle times.

BNSF’s R/VC Uniformity

If the private car movements with higher R/VC ratios are excluded from the group of BNSF ≥ 100 car shuttle/trainload wheat movements from Montana, BNSF’s R/VC ratios for appear to be fairly uniform with no real outliers, which is illustrated in the following graph of these ratios by distance:

Figure 6

BNSF RVC Ratios For >100 Car Wheat Movements in Railroad Cars From Montana



As can be seen, the R/VC ratios are fairly uniform and generally decline as the rail distances (and rail captivity) increase. As a result of this R/VC uniformity, it is unlikely that most captive Montana wheat shippers could obtain any substantive rate relief under the STB's Three Benchmark approach, which compares R/VC ratios with comparable movements.

In order to demonstrate this problem, I have identified the BNSF ≥ 100 car shuttle/trainload wheat movement from Montana (moving in railroad cars) with the highest R/VC ratio as a movement from _____ to _____, which is a distance of _____ miles. According to the 2014 Waybill Sample, this movement's R/VC ratio is _____. I then identified comparable BNSF ≥ 100 car wheat movements moving +/- 15% (_____ miles or to _____ miles) of the distance.⁴ The following table compares this movement with other comparable BNSF movements from Montana:

⁴ The STB has proposed a 15% mileage band for use in its proposed new approach.

PUBLIC VERSION

Figure 7

Comparison of 2014 R/VC Ratios For The Highest BNSF >100 Car Wheat Movement From Montana with Comparable (+/- 15% or Miles) BNSF Wheat Movements From Montana

Item	Miles	Cars / Shipment	Cars	Rate Per Car	Rate ¢ / Ton-Mi.	R/VC
BNSF Montana >100 Car Wheat Movement With Highest R/VC						
Comparable BNSF > Car Wheat Movements () From Montana						
* Destination also served by UP						

As can be seen, these comparable Montana R/VC ratios range from _____ to _____, but are fairly uniform and most are fairly close to the average of _____. It should be noted that the movement from _____ to _____ is one of the shortest >100 car movements from Montana at _____ miles. Therefore, there is only one comparable movement with less miles (_____ to _____). This uniformity in BNSF’s R/VC ratios, however, is not limited to Montana. The following table compares this movement with BNSF ≥100 car wheat movements from other states:

PUBLIC VERSION

Figure 8

**Comparison of 2014 R/VC Ratios For The
Highest BNSF ≥ 100 Car Wheat Movement From Montana with
Other BNSF Comparable (+/- 15% or Miles) > 100 Car Wheat Movements**

Item	Miles	Cars / Shipment	Cars	Rate Per Car	Rate ¢ / Ton-Mi.	R/VC
BNSF Montana > 100 Car Wheat Movement With Highest R/VC						
BNSF Comparable > 100 Car Wheat Movements From Other States						
* <i>Origin or destination also served by UP and/or Other Class I Railroads.</i>						

PUBLIC VERSION

As previously indicated, most of the BNSF jurisdictional wheat traffic involves shuttle or trainload movements with 100 or more cars per traffic (due in part to excessive costs being allocated to smaller shipments). For these movements of 100 cars or more, there few, if any, real outliers, which is illustrated in the following table:

Figure 9

**Comparison of Comparable (654 to 885 Miles)
R/VC Ratios For >100 Car Shuttle/Trainload
BNSF Wheat Movements From MT, KS, MN, ND, SD and TX**

Item	Low R/VC	High R/VC	Average R/VC

As a result of this R/VC uniformity, it is unlikely that Montana wheat shippers could obtain any substantive rate relief under the STB's Three Benchmark approach, which compares RVC ratios for comparable movements within an excessively small universe of shipments.

PUBLIC VERSION

For example, under the “*best case*” scenario, if the rate for the movement with the highest R/VC from Montana, i.e., R/VC for the movement from to , was lowered to a R/VC level (i.e., the average R/VC for comparable BNSF wheat movements), the annual freight charges for this movement (\$) would be reduced by only per year or by for 5 years (the reparation period under Three-Benchmark).⁵ This would be unlikely to cover the cost of litigation under Three Benchmark. Litigation costs may be lower under the Board’s new proposed outlier approach, but the STB also appears to intend a lower relief cap in such cases.

Small Grain Producers and Shippers Are Also Harmed By The STB’s URCS Costing Procedures

As indicated in Figures 3 and 4, there are a significant amount of Montana wheat and barley movements which move at rates below the STB’s jurisdictional threshold of 180% (e.g. wheat movements and barley movements). Part of the reason for this is a result of the STB’s URCS make-whole adjustments, which allocates more for costs to single car shipments (1 to 6 cars per shipment) and multiple car shipments (7 to 49 cars per shipment) and less costs to trainload shipments (currently 50 or more cars per train). The Board is currently considering changes to its costing system in STB Docket No. EP 431 (Sub-No. 4), Review of The General Purpose Costing System.

⁵ The Three Benchmark approach includes a “confidence interval adjustment” under which each movement in the comparison group is adjusted by the ratio of $RSAM \div R/VC > 180$, a “confidence interval” is calculated around the estimate of the mean of the adjusted comparison group, and a challenged rate that is above this confidence interval is presumed unreasonable. In this example, I have not applied this adjustment.

PUBLIC VERSION

The Board is proposing to modify certain URCS Phase II inputs and to modify certain URCS Phase III cost calculations in order to eliminate the make-whole adjustment. The Board is also proposing certain other related changes to URCS, including proposals for allocating locomotive unit-miles (LUM) and train miles and increasing the trainload size from 50 to 75 cars per shipment.⁶ The proposed URCS changes, however, will do little to help Montana grain shippers and producers. In fact, increasing the trainload size will likely reduce the amount of Montana wheat traffic subject to STB jurisdiction.

The primary reason that nearly half of BNSF's individual wheat movements from Montana and nearly all of the barley movements from Montana do not have access to the STB's rate reasonableness procedures, however, is the STB's unadjusted URCS costing approach, which precludes parties from making movement specific adjustments to more accurately reflect the economies and efficiencies of most grain movements.

Most BNSF unit or shuttle grain trains are very efficient and most smaller wheat shipments are married or merged with other wheat shipments from nearby elevators and move in larger than average train sizes to the destinations. As a result, the true cost per carload for most grain shipments from Montana is significantly lower than the system average URCS cost and thus the actual R/VC ratios are significantly higher. In order to account for this problem, the STB could allow movement specific adjustments in grain cases. Alternatively, as I proposed in my Opening Verified Statement in EP 665 (Sub-No.1), the STB could develop and adopt Grain Cost Adjustment Factors (GCAF) in order to account for the problems and issues associated with the URCS costing procedures and the Board's unadjusted URCS approach.

⁶ See STB decision in STB Docket No. 431 (Sub-No.4), served August 4, 2016.

PUBLIC VERSION

I proposed that these developed GCAF factors would be applied to the STB's URCS Phase III Costing program for railroad movements of grain and grain products, which would more accurately reflect the fact that these movements generally have lower than system average switching, crew, locomotive, car and other costs. If properly developed and applied, such GCAF adjustments would increase the amount of grain and grain products traffic which would be potentially subject to STB rate jurisdiction. Such GCAF factors would likely significantly increase the R/VC ratios of jurisdictional grain traffic and increase the likelihood that many of these jurisdictional rates would be found unreasonable by the Board. I urge the Board to reconsider this suggestion or allow movement specific adjustments in grain cases.

The STB Current Three-Benchmark Approach Does Not Benefit Most Grain Shippers

BNSF knows that it has market dominance over most Montana grain movements. Therefore, BNSF knows that this grain traffic is subject to STB jurisdiction. As a result, BNSF plays close attention to the R/VC levels, which results in fairly uniform R/VC ratios with very few outliers.

The biggest outlier identified is BNSF wheat movement from _____ to _____ involving _____ carloads and moving only _____ miles, which has a R/VC of _____. The next highest R/VC is ____%. Since this is such a small movement moving such a short distance, BNSF might argue lack of market dominance, but the R/VC percentage exceeding _____ is plainly inconsistent with effective competition.

PUBLIC VERSION

Assuming a successful rate challenge could be brought, at a reasonable cost, as to the Silver Bow outlier movement, it is hard to be enthusiastic about a methodology that offers hope as to only one wheat movement in the most captive State in the U.S., leaving all other ag producers and shippers in Montana with no way of challenging their high rail rates.

As a result of this R/VC uniformity, it is unlikely that Montana wheat shippers could obtain any substantive rate relief under the STB's Three Benchmark approach, which compares R/VC ratios with comparable movements. Moreover, as indicated in Figure 9, this uniformity problem is not limited to similar BNSF wheat movements from Montana.

In the last phase of this proceeding, EP 665 (Sub-No. 1), ag shipper and producer interests and USDA developed extensive evidence on the difficulties of the comparable rates analysis used in the Three-Benchmark test. When almost all rates (and rate increases) are kept within a narrow range, captive shippers and producers are unable to bring rate challenges with any hope of success, no matter how high the rail rates.

All captive rail customers have a legal right to reasonable rail rates, but the Board chose not to take steps to fulfill this right for the thousands of shippers and producers whose needs are not met by the Three-Benchmark test. Instead, the Board is now proposing to keep its comparable rates approach, performing some analyses itself, but restricting the new test to a far smaller group of potential complainants.

Even if the new outlier approach offered real hope to a small number of rail customers, new and better remedies would be needed for larger rate disputes involving non-outlier rates. Unfortunately, under the Board's new approach as proposed, the likelihood of relief appears remote even for rail customers whose freight moves subject to outlier rates.

PUBLIC VERSION

These high, but fairly uniform, R/VC levels identified above essentially represents monopolistic price fixing, which is allowed and facilitated by the STB's unadjusted URCS costing approach. Because of the STB's URCS costing approach, which overstates the cost of most grain movements, BNSF knows exactly how high it can push its grain rate levels with little or no fear of an STB rate complaint. BNSF and other railroads like to claim that they do not look at URCS and employ "market-based" pricing, but if the rates were based on market-based pricing, one would obviously expect a much greater variation in the R/VC levels and more "outliers".

There are likely more outliers associated with chemical movements. For example, jurisdictional Plastic Materials or Synthetic Resins movements (STCC 28-211) from total carloads and have an average R/VC of , but range from to and have carloads with R/VC ratios in excess of .

STB's Proposed New Comparison-Based Process For Very Small Disputes Will Likely Not Help Most Grain Shippers

In its decision, the Board has proposed "a new comparison-based rate reasonableness methodology for use by shippers of all commodities in very small disputes," which it describes as follows:

PUBLIC VERSION

First, the process would include a preliminary screen that would limit its application to shippers that are more likely to be considered captive and to have rates that are outliers. Such a screen might allow for the Board to make market dominance and rate reasonableness determinations based on an abbreviated evidentiary process. Second, the process would contain a comparison-based analysis in which the Board develops an initial comparison group and then allows parties to propose modifications. By having the Board set the initial comparison group, based on pre-determined criteria, the evidentiary process could be simplified, as parties would only have to present evidence on modifications rather than creating their own comparison groups (as is currently the case in Three-Benchmark cases). Third, the process would contain other procedural modifications that help expedite and streamline the comparison-based assessment. In particular, the Board is considering ideas such as limiting discovery, establishing mandatory disclosures, limiting the length of filings, and establishing an evidentiary hearing in lieu of rebuttal evidence. Finally, because the process would only be intended for small disputes, the Board would limit the amount of relief available. (Decision at page 11)

The STB states that the first step in the process would involve a “preliminary screen’ by the STB “that would limit its application to shippers that are more likely to be considered captive and to have rates that are outliers.” Only a very limited number of grain shippers could make it past STB’s primary screening process, for reasons I have discussed. Even if the focus is expanded to all commodities, the Board proposes identifying outliers by requiring the “revenue per ton mile to be in the top 10% or 20% of the initial Board-determined comparison group.” (Decision at page 16). In other words, the revenue per ton mile analysis would screen in only 10% or 20% of rates, screening out the other 80% or 90%. What are the excluded shippers and producers expected to do if SAC and SSAC are prohibitively expensive, and Three-Benchmark is ineffective?

Because of the STB’s URCS costing procedures and rules (i.e., the make-whole adjustments and unadjusted URCS approach), which overstates the URCS variable cost for most grain shippers, combined with railroad pricing based on the STB’s URCS costing procedures and rules, many railroad grain movements, although captive to Class I railroads, cannot even get in the STB’s door to be screened.

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As indicated, because of the relative uniformity of BNSF's grain R/VC ratios, there are likely to be relatively few grain "outliers." For example, for wheat from Montana, I have only identified one outlier movement (to), which has a R/VC of), but it likely would not pass STB's preliminary screening since it moves only a short distance (miles) and the Board proposes a 500-mile minimum length of haul. (See Decision at page 16, where the Board suggests a presumption of truck competition for shorter hauls, regardless of R/VC percentage.)

In its recent decision in EP 711 (Sub-No 1), Reciprocal Switching, the Board appears to recognize that switching service for a nearby second rail carrier is no basis for presuming the existence of effective competition. Where a rail rate's R/VC percentage exceeds 600%, the Board should not presume effective truck competition based on a 200 mile haul. Other factors, such as a consignee's demand for delivery by rail rather than truck, could support a finding of market dominance.

More fundamentally, the Board's desire for rigorous threshold tests limiting the number of rail customers who might receive the opportunity to invoke the new test of rate reasonableness is misguided. The Board should worry more about the height of the barriers to relief being imposed on shippers and producers, and worry less about the possibility of meritless rate cases being brought. Complainants will typically not have the deep pockets of major railroads, and would have no interest in challenging arguably reasonable rates even if litigation costs were not a concern.

PUBLIC VERSION

A better approach would be to have less restrictive screens, or a requirement that one screening test be met, rather than three. Railroad defendants could (and would) then present their arguments as to why the case should not go forward, but captive rail customers would not be subject to so many hurdles as to make the new approach as problematic (especially for ag interests) as the Three Benchmark test that it supplements.

Assuming that a challenged rate makes it through the STB's preliminary screening process, the Board, rather than the individual parties, would develop an initial comparison group, based on pre-determined criteria, and then allow parties to propose modifications. The Board states that this would simplify the process "as parties would only have to present evidence on modifications rather than creating their own comparison groups (as is currently the case in Three-Benchmark cases)."

While it is true that such an approach could simplify the process, I have demonstrated that the uniformity in R/VC ratios means any comparison group selected, either by the Board or by individual parties, would likely not result in a significant rate reduction for most grain shippers and producers.

Finally, because the process would only be intended for very small disputes, the Board would limit the amount of relief available to something less than the current Three-Benchmark approach, which is \$4 million over 5 years or \$800,000 per year. A relief cap (which is inherently arbitrary and can reward railroads for raising rates), on top of a minimum length of haul, and a "top 10% or 20% of revenue per ton mile" limit, adds up to a step toward effective regulatory recourse that could hardly be smaller. How many captive rail customers are likely to take the risk of antagonizing a major railroad on which they depend for service, for such little return?

PUBLIC VERSION

**Proposal to Include of Non-Defendant
Carrier Traffic in Comparison Groups**

The Board seeks comment on whether to expand the comparison group in the proposed new methodology to include traffic from non-defendant carriers operating in the same URCS region as the defendant carrier. (see Decision at pages 14 and 15). In order to demonstrate a potential problem with this approach, I have compared the BNSF ≥ 100 car Montana wheat movement from _____ to _____ which has the highest R/VC (_____) for wheat trainloads from Montana, with comparable UP and CP trainload wheat movements in the following table:

PUBLIC VERSION

Figure 10

**Comparison of 2014 R/VC Ratios For The
Highest BNSF >100 Car Wheat Movement From Montana with
Other Non-BNSF Comparable (+/- 15% or Miles) >100 Car Wheat Movements**

Item	Miles	Cars / Shipment	Cars	Rate Per Car	Rate ¢ / Ton-Mi.	R/VC
BNSF Montana ≥100 Car Trainload Wheat Movement With Highest R/VC						
Comparable () UP >100 Car Wheat Movements						
Comparable () CP Trainload Wheat Movements						
* Served by another Class I Railroad (BNSF, UP or CP)						

PUBLIC VERSION

As can be seen, comparable trainload wheat movements on UP and CP have higher R/VC ratios (i.e. versus and), therefore, inclusion of these movements in a comparison group would only reduce further the potential relief for this movement, which has the highest R/VC for BNSF trainload movements from Montana. On the other hand, the highest identified UP ≥ 100 car wheat R/VC () may benefit by including BNSF ≥ 100 car wheat movements (which average) in the comparison group. And complainants challenging UP or CP rates as outliers could find support for their claim in the lower R/VC ratios for BNSF wheat shipments. It is likely that R/VC comparisons will not always show higher levels on one railroad than another. There will be variations, but a broader comparison group will help more captive shippers and producers than a comparison group restricted to a single railroad.

It is interesting to note that of the identified UP movements have origins and destinations that are also served by BNSF. Despite the potential Class I competition between BNSF and UP, however, the R/VC ratios are, in most cases, higher. This indicates that, rather than compete with BNSF and offer rates with lower R/VC ratios, UP (and BNSF) elect to charge higher rates and R/VC ratios, presumably reasoning that there is lower risk of regulatory intervention by the STB. The railroads have always tried to downplay the statutory requirement that it takes effective competition, not the appearance of competition, to establish a lack of market dominance.

One the comparable BNSF wheat movements, to , is the same as a comparable UP movement. The following table compares the two movements:

Figure 11

**Comparison of 2014 R/VC Ratios For BNSF and UP
>100 Car Movements from**

Item	Miles	Cars / Shipment	Cars	Rate Per Car	Rate ¢ / Ton-Mi.	R/VC

In this case of apparent head-to-head direct competition, the R/VC ratios for both BNSF and UP are equally high and the rates per car are nearly identical. Clearly, the Board cannot presume that intramodal competition is effective, leading to a finding of no market dominance, just because a routing is served by two railroads.

Including comparable traffic from non-defendant carriers operating in the same URCS region as the defendant carrier may work better for other grain products, such as corn (STCC 01-132) and soybeans (STC C 01-144) originated by BNSF and UP. In fact, corn and soybeans, which are often rotated crops and move from the same origins, show that it may be appropriate, in some cases, to compare movements of commodities movements from non-defendant railroads. The following table summarizes and compares ≥ 100 car non-jurisdictional (<180%), jurisdictional (>180%) and total BNSF and UP corn and soybean movements:

PUBLIC VERSION

Figure 12

**Comparison of 2014 BNSF and UP
>100 Car Movements of Corn and Soybeans**

Item	Miles	Cars	Revenue (000)	Rate Per Car	Rate ¢/ Ton-Mi.	R/VC
BNSF ≥100 Car Corn and Soybean Movements						
BNSF ≥100 Car Corn <180						
<u>BNSF >100 Car Corn >180</u>						
BNSF ≥100 Car Corn Total						
BNSF ≥100 Car Corn Highest R/VC						
BNSF ≥100 Car Soybeans <180						
<u>BNSF >100 Car Soybeans >180</u>						
BNSF ≥100 Car Soybeans Total						
BNSF ≥100 Car Soybeans Highest R/VC						
UP ≥100 Car Corn and Soybean Movements						
UP ≥100 Car Corn <180						
<u>UP >100 Car Corn >180</u>						
UP ≥100 Car Corn Total						
UP ≥100 Car Corn Highest R/VC						
UP ≥100 Car Soybeans <180						
<u>UP >100 Car Soybeans >180</u>						
UP ≥100 Car Soybeans Total						
UP ≥100 Car Soybeans Highest R/VC						

Although BNSF dominates the number of carloads and revenues, the rate structures and average movements for BNSF and UP ≥100 car corn and soybeans movements are fairly similar. It should be noted that unlike BNSF ≥100 car Montana wheat movements, which have no movements under , and have an average R/VC of a significant amount of BNSF and UP ≥100 car corn and soybeans movements are under 180%.

In the following sections, I will address the questions posed by the Board in its decision:

PUBLIC VERSION

Application to Class II and Class III Carriers

The Board seeks “comment on whether this methodology, if adopted, should or should not be applicable to Class II and III rail carriers.” (Decision on page 12). Since the Board’s proposed approach is primarily based on the STB’s Waybill Sample, it would be difficult to apply the proposed approach to Class II and Class III railroads.

There is an under-reporting of movements by Class II and Class III railroads in the Waybill Sample. There are more than 550 Class II and Class III railroads in the U.S. However, the STB’s *2014 Carload Waybill Sample Reference Guide*, dated November 1, 2015, indicates that only 42 Class II and Class III railroads reported information which was included in the 2014 CWS. Other Class II and Class III railroad movements are either not reported or reported by the Class I railroads. For example, a movement originating on a non-reporting Class II or Class III railroad may be reported by the terminating Class I carrier. However, it is likely that a significant number of Class II and III railroad movements are unreported by the Class I carriers, especially in many cases in which the railroads may “absorb” the Class II or III railroad’s rate or switching fee. As a result, a movement may involve two railroads, but the CWS treats the movements as a Class I railroad movement.

Traffic at or Above 180% R/VC

The Board “is considering including other potentially captive traffic, i.e., traffic priced at or above the 180% R/VC level, in the comparison group, but not traffic priced below the 180% R/VC level.” However, the Board “invites comment on the advisability of including or excluding non-captive traffic in comparison groups.” (Decision at page 13)

PUBLIC VERSION

In the case of BNSF Montana wheat movements moving in 100 cars or more, it currently would not matter if traffic with R/VC ratios below 180% are included since there are none. In the case of Montana wheat moving in less than 100 cars, however, it would be logical and may even be necessary to include traffic below 180% in order to develop a comparison group.

In cases involving corn and soybeans, the inclusion of traffic below 180% is desirable. As Figure 12 shows, a significant amount of ≥ 100 car BNSF and UP corn and soybeans move at R/VC ratios below 180%, yet these movements all move much greater distances, which increases the likelihood of railroad market dominance.

I disagree with the STB's characterization of traffic below 180% as "non-captive traffic." As I have shown, Montana is perhaps the most rail captive state, yet it has many wheat, barley and pulse crop movements below 180%. Many Montana grain movements have R/VC ratios below 180%, but are very captive to BNSF. Because of the STB's URCS costing procedures, the movements under 180% cannot get in the STB's door. The Transportation Research Board (TRB) recently urged the Board to look less to URCS costs and more to competitive rates in assessing the reasonableness of rates on captive traffic. I agree. The Board should not automatically exclude rates with R/VCs below 180% from comparison groups under its new proposal.

PUBLIC VERSION

Shipper Characteristics Criteria

The STB has proposed the following shipping characteristics for use in the proposed new approach:

- a) the movement is within a +/- 15% mileage band around the actual miles travelled by the challenged traffic,
- b) the movement is of the same shipment type (e.g., unit train traffic or non-unit train traffic), and
- c) the movement is of a commodity classified under the same Standard Transportation Commodity Code (STCC). (Decision at page 13)

Unfortunately, I do not believe there is a “*one size fits all*” approach for shipping characteristics. For example, in regard to the proposed “+/- 15% mileage band,” the identified BNSF ≥ 100 car Montana wheat movement with the highest R/VC ratio moves _____ miles. Since this is one of the shortest BNSF ≥ 100 car wheat movements, there are only a few movements in the *minus* 15% band range. Therefore, the average distance for the comparison group of _____ other BNSF ≥ 100 wheat movements is higher (_____ versus _____ miles).

The proposed use of the same five digit STCC codes may also not be appropriate in all cases. For example, most BNSF wheat (STCC 01-137-10) moves west, whereas most BNSF durum wheat (STCC 01-137-20) moves east. A bigger problem, however, may be the uniformity of R/VC ratios within STCC groups. In order to account for this issue, it may be appropriate to compare ≥ 100 car BNSF wheat movements with similar ≥ 100 BNSF corn and/or soybean movements. After all, these movements move via the same railroad and in the same railroad cars.

PUBLIC VERSION

20-Observation Minimum

The Board has asked for comments on “whether a 20-observation minimum would be an appropriate requirement.” (Decision at page 14) In many cases, especially with outliers, it may be difficult to find comparable movements. Certainly, the more observations the better, but it may be difficult to find 20 movements in many cases.

I am reminded of the first ICC case to use the R/VC comparison approach, i.e., ICC Docket No. 40073, Southwest Railroad Car Parts Company v. Missouri Pacific Railroad Company, in which I was the primary expert witness. The case involved a short movement of empty railroad cars moving one way to a scrap facility. The parties and the ICC had great difficulty in finding comparable movements. In a 1998 decision in that proceeding, the STB stated:

We were unable to include the R/VCCOMP benchmark in our analysis,(29) because we were persuaded by the parties' previous arguments in court that iron and steel scrap does not constitute comparable traffic and we were unable to identify any other suitable specific commodity for comparison, given the unusual nature of the SWRC traffic. (See STB decision served February 20, 1998, page 5)

Common Carrier Adjustment

The Board invites comment on the inclusion of contract traffic and a common carrier adjustment. Additionally, the Board invites parties to propose alternative means of calculating a common carrier adjustment.” (Decision at page 14) Unlike chemical traffic, most grain moves under published rates. A limited amount of grain moves under contract and summaries of these contracts are submitted to the STB.

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Most of these grain contracts, however, are short-term contracts running approximately one-year. Therefore, the railroad can fairly quickly adjust these contracts and the contract rates. As a result, for grain traffic at least, contract traffic should be included, as it is generally in the same boat as non-contract traffic. I do not believe that a “common carrier adjustment,” such as the 14.8% adjustment referenced by the STB applied in Docket No. NOR 42114, U.S. Magnesium, L.L.C. v. Union Pacific Railroad, STB served Jan. 28, 2010, would be appropriate in grain cases as there is no evidence that grain contract rates are significantly lower than non-contract rates.

In terms of an “alternative means of calculating a common carrier adjustment,” the Board’s Waybill Sample includes a “Calculated Rate Flag” which identifies contract rates. According to the *2014 STB Carload Waybill Sample Reference Guide* “Although the railroad could report a tariff value in place of the contract rate, accurate estimation of the actual contract rate would still be required, as the relationship between the reported tariff rate and actual contract rate (at the three-digit STCC level) must be made available to the Surface Transportation Board for use in internal analysis.” (page 37). Therefore, the STB should have the means of calculating “common carrier adjustments” by commodity and by movement.

I noted that in many cases, the R/VC ratios for grain records which have a “calculated rate flag” are below 180% and therefore, would not be included in the comparison group under the current Three Benchmark test. For example, for the wheat movements from _____, to _____, records for the same movement that are flagged (i.e., “1”) have an average R/VC of only _____, whereas records without a flag (i.e. “0”) have an average R/VC of _____.

PUBLIC VERSION

Including Non-Defendant Traffic

The Board seeks “comment on the advisability of including non-defendant traffic in all or limited circumstances under this simplified methodology, and how such inclusion would affect the time and costs to bring a case.” (Decision at page 15) As previously discussed, including non-defendant traffic comparable traffic may be appropriate and should be allowed on a case-by-case basis. I do not think it would significantly affect the time and costs required to develop a comparison group. As shown in Figure 10, I identified UP and CP comparable ≥ 100 car wheat movements with little trouble.

500 Miles Limitation

The Board states that “Traffic moving fewer than 500 highway miles between origin and destination would not be eligible to be challenged under the new methodology because trucking alternatives for those movements are more likely.” (Decision at page 15) My analysis of grain movements indicates that the most of the grain outliers, i.e., movements with high R/VC ratios, involved movements moving less than 500 miles.

For example, the BNSF Montana wheat movements with the highest R/VC () moved only miles. In addition, both BNSF and UP ≥ 100 car corn movements with the highest R/VC ratios involved movements less than 500 miles (BNSF – miles and UP –). Therefore, by instituting a 500-mile limitation in the screening process, the STB would screen out many of the grain outliers.

Rate Per Ton-Mile Screen

The Board has a proposed a rate per ton-mile screen: “Specifically, the Board could require the revenue per ton mile of the challenged traffic to be in the top 10% or 20% of the initial, Board-determined comparison group. Another possibility would be to require the issue traffic to be at least one standard deviation above the mean revenue per ton mile of the comparison group.” (Decision at page 16) In my example analysis, the studied BNSF wheat with the highest R/VC, the movement had a rate per ton-mile of . This rate per ton-mile, however, did not fall in the top 10% of the comparable movements. The top 4 movements (), had rates per ton-mile ranging from to cents. Therefore, 20% may be a more appropriate screen, assuming such screening is necessary.

Prior Litigation

The Board has proposed that “a requirement that the complainant must not have brought a case against the defendant under this methodology within a certain number of years.” (Decision at page 16). The Board’s rationale for this limitation is that a complainant should not be allowed to “game” the system by splitting one large case into many small ones to take advantage of the new “outlier” test.

I believe the Board’s concerns are overblown, and could be addressed case-by case basis. For agricultural interests, the new test is not so attractive as to generate such gaming. What if a State Government wants to bring a few test cases on behalf of the smallest captive shippers?

PUBLIC VERSION

Limits on Discovery & Evidence

The Board also is “considering limiting discovery in order to reduce litigation costs for very small disputes. In particular, the Board could require that parties file certain initial disclosures with their complaint and answer,” such as “the nine standard inputs for the URCS Phase III costing program.” (Decision at page 17). The requirement for “certain initial disclosures” does not appear to be unreasonable.

However, the Board has also proposed to limit evidence under the proposed approach “In order to minimize the time and expense associated with litigating a small rate dispute . . . such as imposing word or page limits on the complainant’s opening evidence and the defendant’s reply evidence. (Decision at page 19). As a developer and preparer of such evidence, I do not believe that the Board should impose such a limitation. Each case is different, certainly, there may be some cases that are straightforward and concise, but others may be more complicated. There is no “one size fits all” in terms of evidence.

Qualitative Market Dominance Factors

The Board seeks “comments on specific qualitative market dominance factors it could consider for this type of new rate reasonableness methodology.” (Decision at page 20). The use of specific qualitative market dominance factors may be difficult to develop in grain cases. For example, in many cases, shorter grain movements have higher R/VC ratios than longer grain movements. This anomaly may have more to do with the way that URCS allocates costs than market dominance.

PUBLIC VERSION

In addition, in many cases, the R/VC ratios for railroad grain movements that have origins and destinations that are served by both BNSF and UP have R/VC ratios that are higher than movements which are solely served by either BNSF or UP. As a result, market dominance factors such as short distances or dual rail service may not be appropriate in grain cases.

Commodity-Specific Revenue Need Adjustment Factor

The Board is seeking “comment on whether the Board should modify its revenue need adjustment factor to be commodity-specific, and if so, how we can effectively disaggregate the existing RSAM on a commodity-by-commodity basis.” (Decision at page 22). The Board states that:

We believe that, on average, differences in demand elasticities are reflected in R/VC ratios—those with higher R/VC ratios tend to enjoy less direct and indirect competition while those with lower R/VC ratios tend to enjoy somewhat more competition. In an individual proceeding, we would consider applying a commodity-specific RSAM where the resulting figure reflects this intuition. (Decision at page 22)

As previously indicated, the Waybill Sample data shows that that many of the longest railroad grain movements, which are the most captive to rail transportation, have low R/VC ratios, many of which are below 180%. Therefore, “demand elasticities” for grain movements may not be accurately reflected in R/VC differences. Moreover, the idea would be difficult to implement, and the benefits seem almost nonexistent for BNSF and UP, which are exceeding revenue adequacy.

PUBLIC VERSION

Summary

I commend the Board for looking for a new expedited rate review process which “would be more affordable and accessible to shippers of all commodities with small disputes.” (Decision at page 3). It is possible that such an approach could be applied in limited number of high-rated “outlier” situations. For example, some chemical shippers may be able to benefit from such an approach. Unfortunately, this proposed new rate review process will do little to help the problems faced by grain shippers. I encourage the Board to continue to “to consider what regulatory changes could be implemented to ensure that the Board’s rate case procedures are fully accessible to grain shippers and provide effective relief from excessive freight rail rates, as appropriate.” (Docket No. EP 665 (Sub-No.1) Decision at page 2).

Verification Page

I, Gerald W. Fauth III, declare under penalty of perjury that the foregoing Verified Statement submitted in Surface Transportation Board Docket No. Docket No. EP 665 (Sub-No. 2), Expanding Access To Rate Relief, is true and correct. Further, I certify that I am qualified and authorized to sponsor this testimony.

Executed, November 14, 2016, by:

A handwritten signature in black ink, appearing to read "Gerald W. Fauth III", written over a horizontal line.

Gerald W. Fauth III

**STATEMENT
OF
BACKGROUND, QUALIFICATIONS AND EXPERIENCE
OF
GERALD W. FAUTH III**

My name is Gerald W. Fauth III. I am President of G. W. Fauth & Associates, Inc. (GWF), an economic consulting firm with offices at 116 S. Royal Street, Alexandria, Virginia 22314. I am a recognized expert on transportation issues with over 37 years of experience in the private sector and in the Federal government.

This statement generally describes my background, qualifications and experience. The majority of experience has involved economic, regulatory, public policy and legislative issues primarily associated with, or related to, the U. S. railroad industry. Most of my work has involved regulatory proceedings and related projects before, or related to, the U.S. Surface Transportation Board (STB) and its predecessor, the Interstate Commerce Commission (ICC).

I have extensive experience in working in regulatory and other proceedings and projects involving railroad mergers, transactions, acquisitions, rail line construction, rail line abandonments, rate reasonableness and other railroad related issues. These matters have involved railroad issues on a nation-wide, system-wide and individual railroad line basis.

GWF has been engaged in the economic consulting business for over 50 years. My part time affiliation with GWF began in 1972. I began working for GWF on a full-time basis on May 15, 1978 and was employed by GWF continuously until November 1, 1999 at which time I took a leave of absence in order to take a position with the STB.

At the STB, I served as Chief of Staff for one of the three Board Members appointed by the President, Vice Chairman Wayne O. Burkes. I returned to GWF and consulting work effective June 23, 2003 after Mr. Burkes resigned his position to run for a political office.

Over the years, I have submitted expert testimony before ICC, STB, state regulatory commissions, courts and arbitration panels on a wide-variety of issues in numerous proceedings. In addition, I worked for 3½ years at the STB where I reviewed, analyzed and made recommendations on over 600 written formal decisions that were decided by the entire Board. These proceedings and decisions involved all matters of STB jurisdiction and had an impact on the transportation industry and the national economy.

Railroad transactions have long been the subject of ICC and STB regulatory proceedings and other matters involving: railroad merger and acquisition approval and oversight proceedings; railroad line abandonment proceedings; line sales; feeder line application proceedings; and other railroad transaction-related proceedings. I have been involved in numerous such proceedings and projects as an expert witness and as an STB staff advisor.

For example, I was an expert witness in the last two major Class I railroad merger proceedings: STB Finance Docket No. 32760, Union Pacific Corporation, et al. – Control and Merger – Southern Pacific Rail Corporation, et al. and STB Finance Docket No. 33388, CSX Corporation, et al., Norfolk Southern Corporation, et al. – Control and Operating Leases / Agreements – Conrail, Inc., et al. My testimony in these major merger proceedings concerned the potential adverse competitive impact of these mergers on two key areas.

In addition to my work in major railroad merger proceedings, I have submitted expert testimony in other railroad finance docket and abandonment proceedings before the ICC and STB. In these proceeding, I have developed and submitted evidence relating to the impacted railroad traffic and the valuation and economics of the railroad line at issue (such as: going concern and net liquidation values; freight revenues and traffic; operating costs; maintenance costs: right-of-way valuation; etc).

In addition to my testimony in railroad mergers and other rail finance and transaction proceedings, I served as an original member of the Conrail Transaction Council, which was established by the Board in Finance Docket No. 33388. This council consisted of representatives of the CSX, NS and shipper organization and provided a forum for timely and efficient communication of information and problems concerning the transaction. I was one of the original members of the Conrail Transaction Council and attended every meeting of the council until my employment with the Board.

During my time at the Board, I was actively involved in the STB merger oversight proceedings associated with the UP/SP and Conrail transactions. Perhaps the most significant merger-related proceedings that I was involved in during my time at the Board were STB Ex Parte No. 582, Public Views on Major Rail Consolidations and STB Ex Parte No. 582 (Sub-No.1), Major Rail Consolidation Procedures. These STB major rulemaking proceedings involved extensive oral hearings and written testimony from hundreds of witnesses. The Board concluded that its existing rules governing railroad mergers and consolidations, which had been developed nearly 20 years earlier, were not adequate for addressing the broad concerns expressed and initiated a major rulemaking proceeding which resulted in a major revision to the Board's railroad merger rules.

I have a significant amount of experience in issues involving railroad rate reasonableness. I was actively involved in the initial ICC regulatory proceedings over 30 years ago in which the ICC first proposed and established guidelines which have since evolved into the STB's current railroad rate reasonableness guidelines. I was actively involved in several of the first cases to test the ICC's then proposed guidelines. For example, I was the primary expert witness in ICC Docket No. 40073, South-West Railroad. Car Parts Co. v. Missouri. Pacific Railroad, which was the *first* case to test the ICC's proposed simplified guidelines, which have since evolved into STB's Three-Benchmark approach.

I submitted extensive written and oral testimony in STB Ex Parte No. 646 (Sub-No. 1), Simplified Standards For Rail Rate Cases, on behalf of a group of 30 major stakeholders and my testimony was cited by the Board in its decision served September 5, 2007. My work and testimony in these ICC/STB proceedings has helped shape the STB's current railroad rate reasonableness guidelines.

I have extensive experience in working in STB regulatory proceedings, litigation and other projects involving railroad valuation issues. These matters have involved railroad valuation issues on a nation-wide, system-wide, individual line and individual movement scope and basis.

Many of our projects have involved the development of railroad variable cost analyses based on the application of URCS and its predecessor, Rail Form A (RFA). URCS is used to determine STB jurisdiction and is an integral component of the STB's Full-SAC method, new Simplified-SAC standard and recently modified Three-Benchmark approach. I have an extensive working knowledge of the development and application of URCS and RFA. I have prepared URCS cost analyses for thousands of individual railroad movements. I also submitted expert testimony in ICC Ex Parte No. 431 (Sub-No.1), Adoption of the Uniform Railroad Costing System as a General Purpose Costing System for Regulatory Costing Purposes and more recently in STB Ex Parte No. 431 (Sub-No. 3), Review of the Surface Transportation Board's General Costing System.

Proceedings before the Board often involve traffic and market analyses using the Board's Waybill Sample, which is a computer database of approximately 600,000 records of sampled railroad movements. I am extremely familiar with this railroad traffic database. Over the years, I have performed hundreds of analyses using this data which has been used as evidence in merger and other proceedings before the Board.

I am a 1978 graduate of Hampden-Sydney College in Hampden-Sydney, Virginia where I earned a Bachelor of Arts degree. My major areas of study were history and government. My senior paper in college dealt with the History of Railroad Deregulation. I am a 1974 graduate of St. Stephen's School for Boys (now St. Stephen's and St. Agnes School), located in Alexandria, Virginia. My senior project and paper in high school dealt with the ICC and the Energy Crisis of 1973.

My professional memberships included the Transportation Research Forum and the Association of Transportation Law Professionals.

BEFORE THE
SURFACE TRANSPORTATION BOARD

DOCKET NO. EP 665 (SUB-NO. 2)
EXPANDING ACCESS TO RATE RELIEF

VERIFIED STATEMENT
OF
TERRY WHITESIDE

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Dated: November 14, 2016

VERIFIED STATEMENT

My name is Terry Whiteside and for the past thirty-five years I have been involved in the rail and freight transportation industry. I have worked both in private and government based public entities in capacities for both carriers and shippers. I am a registered practitioner and have been Principal in Whiteside & Associates, a transportation and marketing consulting firm located in Billings, MT, for the past 28 years. I also serve as Chairman of the Alliance for Rail Competition. Our clients at Whiteside and Associates cover a broad range of industries including agriculture, processing, mining, lumber, ports, manufacturing, bulk transport and finished goods.

In a decision in these proceedings served August 31, 2016, the Surface Transportation Board (STB or Board) is seeking comments and suggestions through an Advance Notice of Proposed Rulemaking (ANPR) process regarding the Board's effort to develop a new rate reasonableness methodology for use in very small disputes, which would be available to shippers of all commodities.

We have been asked by the Alliance for Rail Competition (ARC), Idaho Barley Commission, Idaho Grain Producers Association, Idaho Wheat Commission, Minnesota Farmers Union, Montana Farmers Union, Montana Wheat & Barley Committee, National Farmers Union, Nebraska Wheat Board, North Dakota Farmers Union, North Dakota Grain Dealers Association, Oklahoma Wheat Commission, Oregon Wheat Commission, South Dakota Farmers Union, Texas Wheat Producer Board, Washington Grain Commission, Wisconsin Farmers Union, Wyoming Wheat Marketing

Commission, U.S. Glass Producers Transportation Council, U. S. Dry Bean Council and U.S. Dry Pea & Lentil Council to submit these comments.

DISCUSSION

On August 31, 2016, the Surface Transportation Board (STB or Board) opened an Advance Notice of Proposed Rulemaking (ANPR) seeking comments regarding the Board's effort to develop a new rate reasonableness methodology for use in very small disputes, which would be available to shippers of all commodities.

In its decision served December 12, 2013 in the last phase of this proceeding, . EP 665 (Sub-No.1), Rail Transportation of Grain, Rate Regulation Review, the Board focused entirely on grain and invited public comment on the Board's existing rate complaint procedures following many years of comments by agricultural shippers that the STB processes are not accessible to grain shippers and do not provide effective redress or protection against freight rail transportation rates reasonableness. The Board also sought specific proposals for modifying existing procedures or new alternative rate relief methodologies that would serve the interests of agricultural shippers and their recourse to the STB for relief from excessive freight rates and charges.

Opening Comments were submitted on June 26, 2014 followed by reply comments on August 25, 2014 on behalf of MWBC, ARC and several other Ag-related groups. We focused on testimony that served to described the many problems faced by grain and grain products shippers associated with the Board's current jurisdictional costing and rate reasonableness methodologies. We also outlined and proposed modifications and alternative methodologies in response to the Board's call in the proceeding. I outlined the previous efforts for the past 30 years by agricultural shippers to bring grievance complaints to the Board, including McCarty Farms.

For those unfamiliar with the history, Montana grain producers challenged high rail rates in court, in McCarty Farms , Inc. v. Burlington Northern, 91 F.R.D. 486 (D. Mont. 1981), and the main issues of rate reasonableness came before the ICC and STB. Though BNSF market dominance was found, 17 years of litigation produced no benefits. This is partly because the SAC test is a poor fit for wheat shipments, and partly because another test used by the ICC was struck down on appeal.

Montana agricultural producers together with the State of Montana spent over \$3.3 MM to prosecute this case. The result is that ag shippers in Montana and other Western States have good reason to question whether the STB rate regulation can work for them. Contrary to railroad claims, producers and shippers of wheat, barley, corn, peas, and other crops

consider many rail rates excessive (though there are some rates which are well below 180% of variable cost). Rather, captive ag rail customers question whether the Board is able and willing to grant relief

The fact that SAC, which is prohibitively expensive for almost all captive customers (except for a few utilities), is the only test of rate reasonableness that ever seems to work, and the fact that alternatives to SAC were developed only after more than a decade, and were kept in place for another decade despite no utilization by shippers, would seem to support their feeling of being ignored. And the Board's call for comments on its new "outlier" approach in this phase of this proceeding, without addressing grain producer standing, doesn't help. (Those issues will evidently be clarified later, but it would have been helpful for MWBC, ARC and others to have the benefit of the STB's thinking while working on these comments.)

The idea of a remedy for exceptionally high "outlier" rates – the top 10% or 20% of rail rates – is not inherently objectionable, but it is inherently limited.¹ What about the other 80% to 90% of rates on agricultural commodities moving via market dominant railroads? The Board

¹ Witness Gerald W. Fauth indicates that, on a proposed rate per ton mile basis, a 10% cap would exclude the movement with the highest R/VC ratio and a 20% screen may be more appropriate (see Fauth, page 36).

must not ignore the fact that such shippers and producers have no viable remedy. SAC and SSAC cost too much, and Three-Benchmark is unworkable, mainly due to the R/VCcomp benchmark.

Not only is the “outlier” approach narrowly restricted in who it might help, but even if a shipper or producer has a small enough case involving a rate that deviates enough from the applicable norm, the Board seems determined to pile on extra barriers to success, such as confidence intervals and relief caps, which help only the railroad, and therefore serve only to further limit relief.

A small amount of relief is better than no relief, which is what we have now. However, the STB seems unable to shake the fear that too many shippers might get too much relief, when the far larger problem is that too many major railroads are charging, and have for many years charged with impunity, too many high rates, violating the Act’s requirement that rates on captive traffic must be reasonable.

Some of the concerns that appear to drive STB decision making just don’t make sense. Shippers of agricultural commodities have other priorities besides litigating rate cases against railroads they depend on for survival. Producers of agricultural commodities, including farmers, are even more reluctant to take on the Class Is. This is why simple remedies that offer reasonable certainty are better than complex remedies requiring

multiple barriers to be surmounted. For this reason, the Board should consider demonstrating how its new approach might work in practice.

Fears of railroad retaliation are real. Railroads have already argued elsewhere that shippers cannot get lower rates and also get better service. How is that different from saying a shipper getting rate relief might see worse service? What will prevent a shipper getting relief as to the top 10% of its rates from seeing increases in the other rail rates it pays, for which no remedy exists?

Many potential complainants will be deterred by the costs and burdens of showing they are captive. BNSF may control nearly 95% of rail freight in Montana, and BNSF and UP may dominate in other regions, but they are unlikely to admit market dominance even if rate challenges are limited to their highest rates. And if a shipper or producer is not found captive, not only do its existing rates become unchallengeable, but those rates are subject to increases. In contrast, a railroad found market dominant may still win the rate case. Railroads often do win under current STB rate case standards, which is why railroads fight so hard against any changes in those standards.

The likelihood that major railroads will experience significant (or any) adverse impacts on their current revenues from the Board's new "outlier" approach is negligible. Why then does the Board take such small steps

toward a better balance between the needs of railroads and the needs of captive rail customers? And why retain costing procedures under URCS that, as Mr. Fauth explains (Fauth VS at pages 12-20) overstates the costs allocated to grain shippers and producers and exaggerates the already high obstacles to regulatory recourse?

Jurisdictional hurdles make it very difficult for the vast majority of railroad grain and grain products shippers to even get in the STB's door in order to utilize its rate reasonableness guidelines. Gerald Fauth in his Verified Statement also indicated that the STB's Full-SAC and Simplified-SAC tests are not viable options for most grain and grain products shippers (and most non-coal shippers) and that there are many problems associated with the simpler and cheaper Three-Benchmark test.

The Board requested in Ex Parte No. 665 (Sub No. 1) that respondents develop proposals for "new alternative rate relief methodologies, should they be necessary."² With the problems faced by grain and grain products shippers associated with the application of the SAC and Three-Benchmark tests, we continue to urge that the Board seriously consider a new rate reasonableness methodology, or combination

² STB Docket No. EP 665 (Sub-No.1), served December 12, 2013, page 2.

of approaches, for grain and grain products. The STB's SAC and Simplified-SAC tests are essentially useless for most grain and grain products and other bulk commodity shippers .

In the Western U.S. and the Great Plains states, the distances to market are very long and direct rail-to-rail competition is rare. Coupled with the lack of ability to seek redress for anti-competitive behavior by the nation's railroads, this Board continues to focus on rate relief for "outliers" or extremely small shipments or very small shippers, while the entire grain and grain products industry, large or small, is effectively left out of a workable, viable process to attain redress for excessive grain rates charged by market dominant railroads.

The Board in this proceeding has decided to pivot away from dealing with the problems faced by agriculture shippers in order to explore more limited relief for a group of captive shippers defined by size rather than commodity. The Board appears to be missing the biggest problem: The comparable test does not work when all rates or R/VCs are high and there will be very few if any outliers. Board also may be turning a blind eye and missing the mark by not focusing on effective remedies.

The Board apparently has tossed out most of the proposals put forth by ARC, et al., USDA and The National Grain and Feed Association (NGFA) in Ex Parte 665 (Sub No. 1). However, its proposed "new rate

review process,” will do little to help the problems faced by grain shippers. The Board has gone from “what regulatory changes could be implemented to ensure that the Board’s rate case procedures are fully accessible to grain shippers and provide effective relief from excessive freight rail rates, as appropriate,”³ and instead has decided “to develop a new rate reasonableness methodology for use in very small disputes, which would be available to shippers of all commodities.”⁴

Although a very limited number of shippers and producers may benefit from the proposed new rules in “very small disputes,” the Board should be trying to solve the plight of the agricultural shippers in a real world environment of very limited rail-to-rail competition over a vast area of the United States. The agricultural shipper and producer problems do not involve, in most cases, very small disputes or “outlier” rates. Rather, they are systemic and pervasive on the entire agricultural industry originating traffic over the Western half of the entire geographical U.S. I work with these industries and other bulk shipments industries on a daily basis. Their problems associated in dealing with market dominant railroads are real and

³ STB Docket No. EP 665 (Sub-No.1), Rail Transportation of Grain, Rate Regulation Review, served December 12, 2013, page 2.

⁴ STB Docket No. EP 665, (Sub No. 2) served August 31, 2016

the problems of producers and shippers continue to not be addressed by present regulatory rate and service relief standards at the Board.

As stated in EP 665 (Sub-No. 1), agricultural producers and shippers have two major markets for their products: domestic consumption and markets accessible from tidewater transfer points (export). What is common to both of these two markets is that in order for agricultural production to have or create value to the farm producing industry, the farm products must be moved from fields and elevators to the ultimate markets or ports. The distance of move and the amount of harvest can vary from a few miles and a few truckloads to thousands of miles and hundreds of thousands of carloads. Generally agricultural commodities require movement in bulk quantities.

The bottom line is that all rail movements ultimately depend on rate and service levels. Rail rates that are too high to economically compete in the market place effectively shut down farm production. Service levels on rates that don't move traffic do not matter. Rail service levels become important only when rail rates are reasonable enough to foster competitive movements of products.

In the states where our clients originate shipments, analysis by Mr. Fauth and myself finds high rates and R/VCs through entire states and routings. Where all rates are high – one does not readily find “outliers” but

rather a situation where the general rate and R/VC levels are excessive. The Board appears, to once again, be side stepping the real issue that is prevalent as to agricultural movements to market as well as in various other markets including sand and glass, coal and many manufacturing industries. The Board is ignoring the discussion we have put forth that Three Benchmark remedies don't work for agricultural and other bulk shippers.

Instead the Board is focusing on the "smallest rate cases" involving outlier rates. Such a selection criteria will screen out 80-90% of the captive shipments that need regulatory oversight. Frankly, the outlier focus is not much of a workable solution. I have read Gerald Fauth's Verified Statement and from conversations I have had with agricultural and bulk shippers all over the United States, the problems of high and increasing rail rates, market access and unreliable service seem unabated. I have studied the tariff increases in grain and they have continued to go up for years, even when demand for grain falls and even when all other facets of the economy are suffering through a recession. Why during this last year of weak wheat prices, would carriers continue to increase their tariff rates for moving grain while trains and equipment are being idled? Answer – because they can and they are not focused increasing movements of grain through price reductions but rather focus continually on ever higher pricing on movements.

OUTLINE OF TERRY WHITESIDE VERIFIED TESTIMONY:

1. **Continuing need for increased transparency of railroad metrics and actions**
2. **Rail Rates on Grain continue to exhibit high Revenue/Variable Cost levels**
3. **Need for increased access to railroad public documents such as tariffs** which serve to provide education (to agricultural producers, small and large elevators, and merchandisers), and access to more complete summaries of transportation contracts and operational data
4. **The grain mix in the northern plains is expanding to the harvesting of pulse crops⁵**
5. **As discussed in our previous verified statements, Carriers' goals lead to conflict in the transport of farm production.** A main goal of railroad carriers is to maximize profit. Railroads in agricultural America desire to move agricultural commodities in trainload quantities to market (highest return to railroads). There is continued resistance to moving stratified farm products (multiple grades, alternative crops or non-homogeneous mixes) and products that do not lend themselves to trainload shipments such as peas, lentils, pulse and developing varieties. Today, railroad profit goals do not necessarily coincide with long term profitability for farm production.

⁵ Dried peas, edible beans, lentils and chickpeas are the most common varieties of **pulses**. **Pulses** are very high in protein and fibre, and are low in fat. Like their cousins in the legume family, **pulses** are nitrogen-fixing **crops** that improve the environmental sustainability of annual cropping systems.

6. Rail carriers now believe it is their right to set the market price of the commodity they are transporting. This has led to rail carriers demarketing certain shippers while promoting others and limiting their access to their markets. In recent years -- especially the last decade -- we continually hear from shippers of numerous reductions in rail service by major railroads and their **inability to utilize the current STB rate standards to access regulatory review.** Rail rates and charges that exceed maximum lawful levels cannot be justified by service quality, no matter how good. High rates are even more objectionable when accompanied by poor service. Given their market power throughout the grain agricultural region, the railroads have been able to restructure the way wheat and other grains move to market. A railroad with market power is in a position to use its control of pricing and service to encourage some routings and shipments, and to discourage others, thus influencing where and when products or product mixes move.

7. Summary

1 CONTINUING NEED FOR INCREASED TRANSPARENCY OF RAILROAD METRICS AND ACTIONS

The shippers and the regulators need to have published, timely reports from the railroads showing trends such as velocities, back orders by state and regions within states, backorders by region within states, etc.

When smaller elevators fold, leaving fewer, larger elevators that producers must use, many producers find themselves driving significantly longer distances from farms to elevators. The loss of these smaller elevators also injures the ability of the farm community to access their market for crops that are not marketable through the shuttle system, including crops such as rotational crops, pulse crops, peas, lentils, barley, durum and white wheat as well as new and developing wheat or grain classes and varieties.

2 RAIL RATES ON GRAIN CONTINUE TO EXHIBIT HIGH REVENUE/VARIABLE COST LEVELS

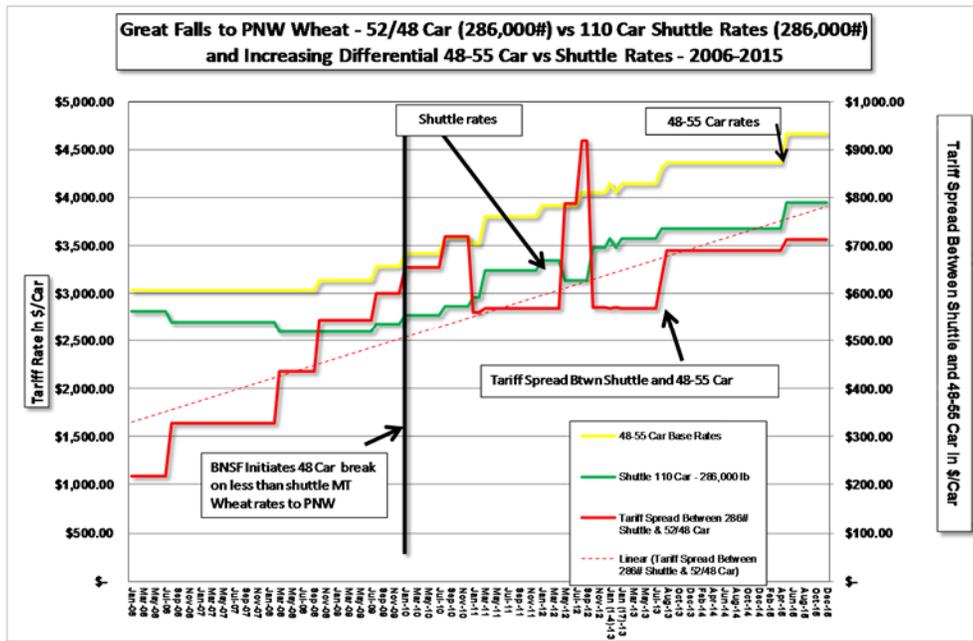
Grain rates are published in tariffs for the majority of rates moving farm produce in the United States. The grain rates are, for the most part, also distance based, meaning that rates are a function of distance. There is little use of group or zone rates as the rail carriers tend to price from origins to destination.

When examining the wheat rate structures, it is clear that the rate structures are uniform in their R/VC ratios for an entire region. This may

include entire states, entire regions and even the rate structures that apply to multiple origins (see Fauth VS Figure 9 at page 17). Finding useful comparison groups of rates in a region or into a specific market will rarely be possible.

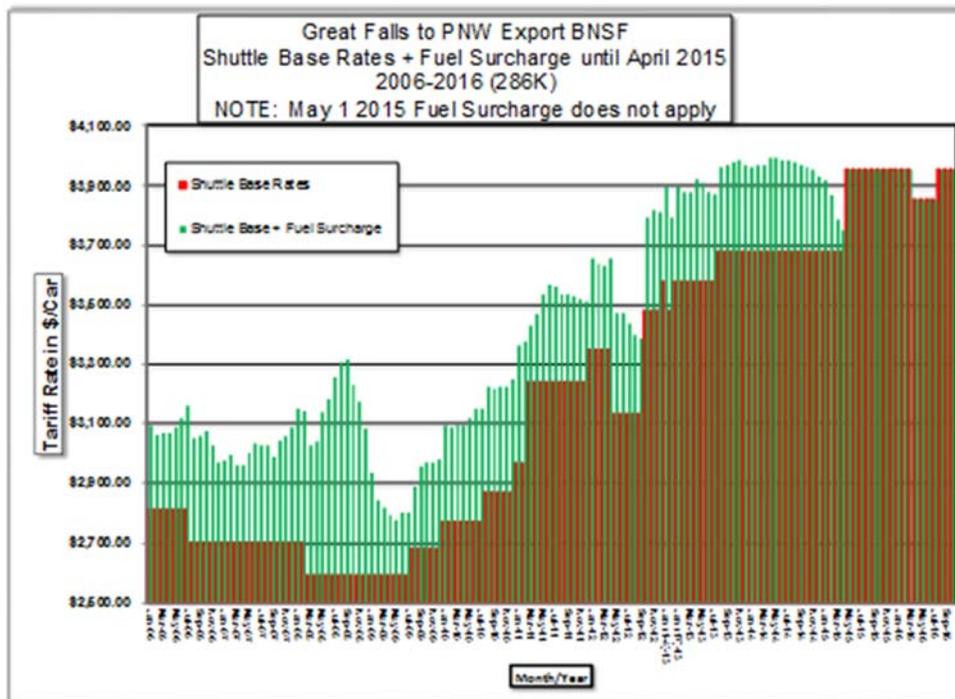
It is also not possible, in most cases, to find ‘outliers’ as the carriers maintain excessive or elevated rates for all shippers in regions where the carrier dominates the market. Mr. Fauth has examined hundreds of R/VCs on grain rates throughout the central plains. As he demonstrates, the railroads are setting the rate structures through vast areas based upon shipments sizes and distances (two major URCS cost input factors) and maintaining fairly uniform R/VC’s. As we stated in EP 665 (Sub-No. 1), this creates problems when defining comparison groups under Three-Benchmark.

Other shippers in a comparison group of shippers of a commodity such as wheat would be paying relatively the same R/VC rates as for the complained-of rate, i.e., the rate being challenged. It also creates a barrier to identifying “outliers” that the Board wants to focus on here. If there are no outliers because every shipper and producer in a territory is charged high rates, the situation cries out for regulatory review, but the standards the Board is proposing will do little to meet the needs of captive producers and shippers.



The Chart above indicates another trend that continues to create hardship on both the smaller shipments and the rising new pulse industry. The BNSF rate structures are increasing the less than shuttle rates by an amount greater than the increase on shuttle rates. This action continues to put economic pressure upon smaller elevators and the crops that do not ship in trainload quantities such as barley, lentils, dry peas and chick peas (known as pulse crops).

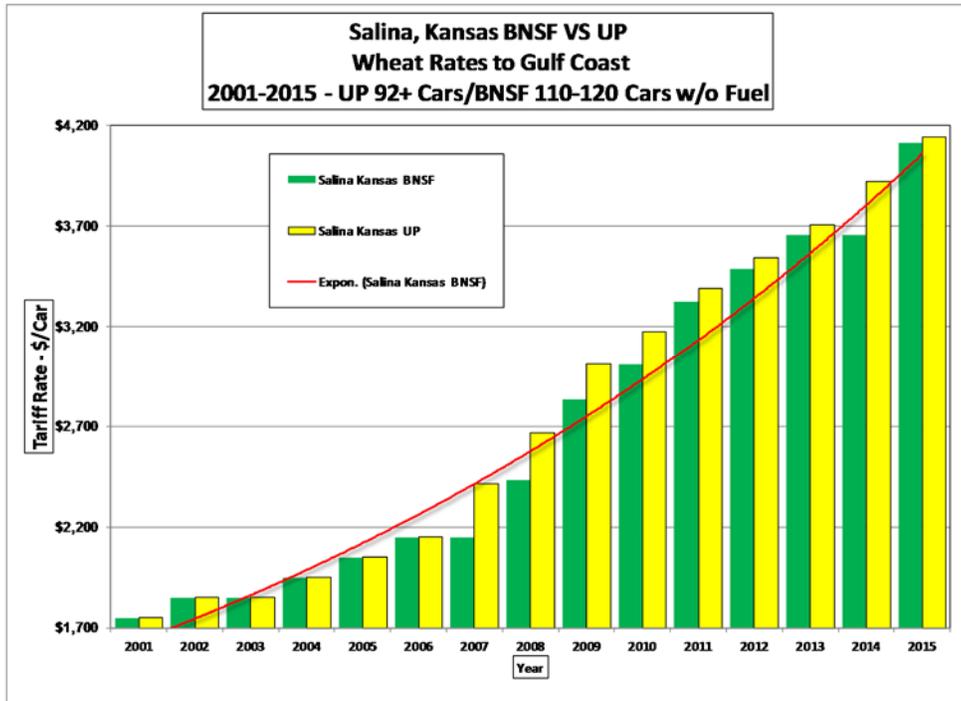
Throughout the plains states from Texas to the PNW states of Oregon and Washington and the northern plains states from Wisconsin to Montana, the less than shuttle (less than trainload) rates are continuing to rise faster than inflation. The charts below, showing several Great Plains origins to Gulf Coast destinations, outline the steep upward curves of the rail (BNSF and UP) increases over the last 15 years.

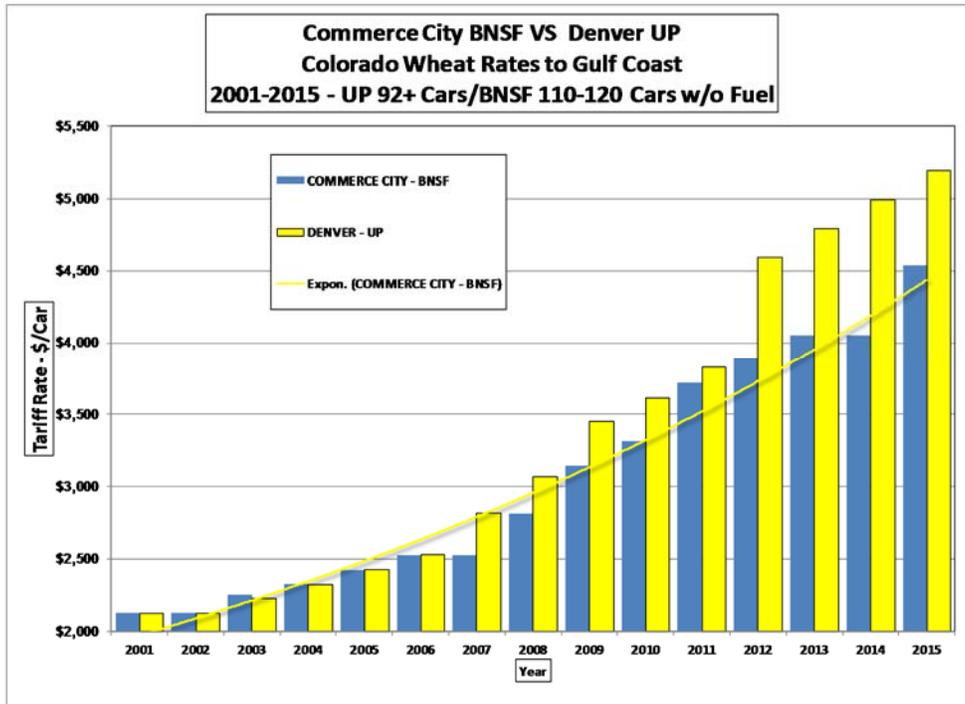


It is evident from the chart above that the BNSF export wheat rates have continued to escalate even after the BNSF did away with fuel surcharges in April, 2015. The BNSF chose to continue to raise the Northern wheat rates (MT, ND and SD) in August, 2016 even though the price of wheat across the Northern Plains had fallen to precipitously low levels.

Throughout the plains statement from Texas to the PNW states of Oregon and Washington and the northern plains states from Wisconsin to

Montana, the rates are continue to rise faster than inflation





3 NEED FOR INCREASED ACCESS TO RAILROAD PUBLIC DOCUMENTS SUCH AS TARIFFS

The railroads continue to deny access to their public tariff systems to many organizations and even small shippers and that practice needs to be stopped by the Board. Tariffs are not meant to be secret documents but should be readily available to public inspection.

4 PULSE CROPS – THE NEW CROPS OF CHOICE IN THE NORTHERN GREAT PLAINS AND THE TRANSPORTATION PROBLEMS THAT EMINATE FROM THE MAREKTING OF PULSE CROPS

In Montana, farmers have incorporated pulse crops into their crop rotations to reduce the amount of land left fallow (idle). Pulse crop acres have increased from 350,000 in 2009 to over 800,000 in 2015. According to USDA data, Montana production of peas and lentils more than doubled from 513,464 in 2013 to 1,030,120 tons in 2016.

“Dry peas, lentils and chickpeas are “nutrition powerhouses,” according to the USA Dry Pea and Lentil Council in Moscow, Idaho. They’re high in vegetable protein, iron, potassium, magnesium and dietary fiber”, according to U.S. Peal and Lentil Council CEO Tim McGreevy. “Farmers who raise them cite their ability to break up disease pressure in crop rotations for wheat production and put much-needed nitrogen back into the soil.”⁶

In 2011, Montana took a leadership role in U.S. pulse crop acreage. As of today, Montana retains its leadership position in pulse production, selling markets through the nation and in India, Japan, and

⁶ Source: http://www.capitalpress.com/Nation_World/Nation/20150730/popularity-of-pulse-crops-poised-to-grow (with permission)

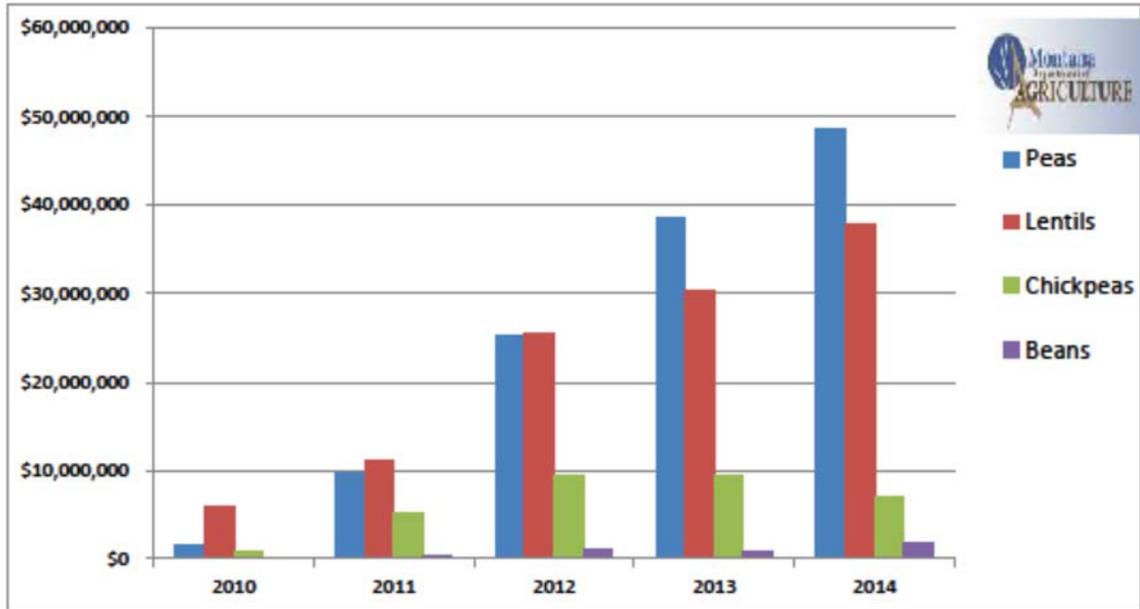
many other countries around the world. Montana has become one of the top producers of pulse crops in the nation over the past couple of years. The value of this production has grown from just over \$8MM to almost \$151.6MM in 2014.⁷

Potential exists for substantial continued growth of the pulse industry in Montana, North Dakota, the Palouse area of eastern Washington state, in the coming years. If additional acres of pulse crops were grown on 25% of Montana's fallow cropland (approximately 900,000 acres) the annual benefit to Montana's economy could exceed \$240 million. As the pulse industry grows, Montana and North Dakota communities will benefit from job creation and increased economic activity resulting from additional in-state processing.⁸

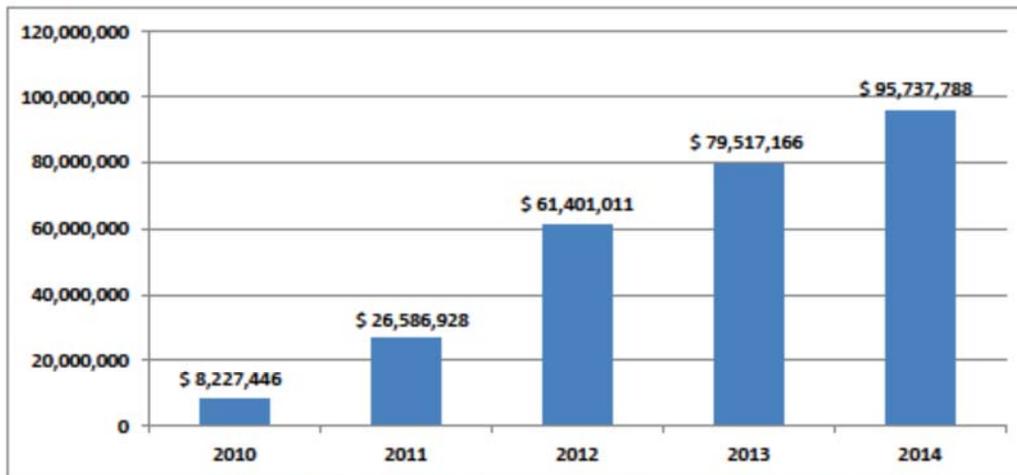
⁷ Montana Agricultural Fact for 2014 – www.nass.usda.gov/mt

⁸ Source: <http://agr.mt.gov/agr/Producer/PulseCrops/>

**Value of Montana Foreign Exported Pulse Crops by Type
(Including Seed)**



Total \$ Value of Montana Foreign Exported Pulse Crops (including seed)

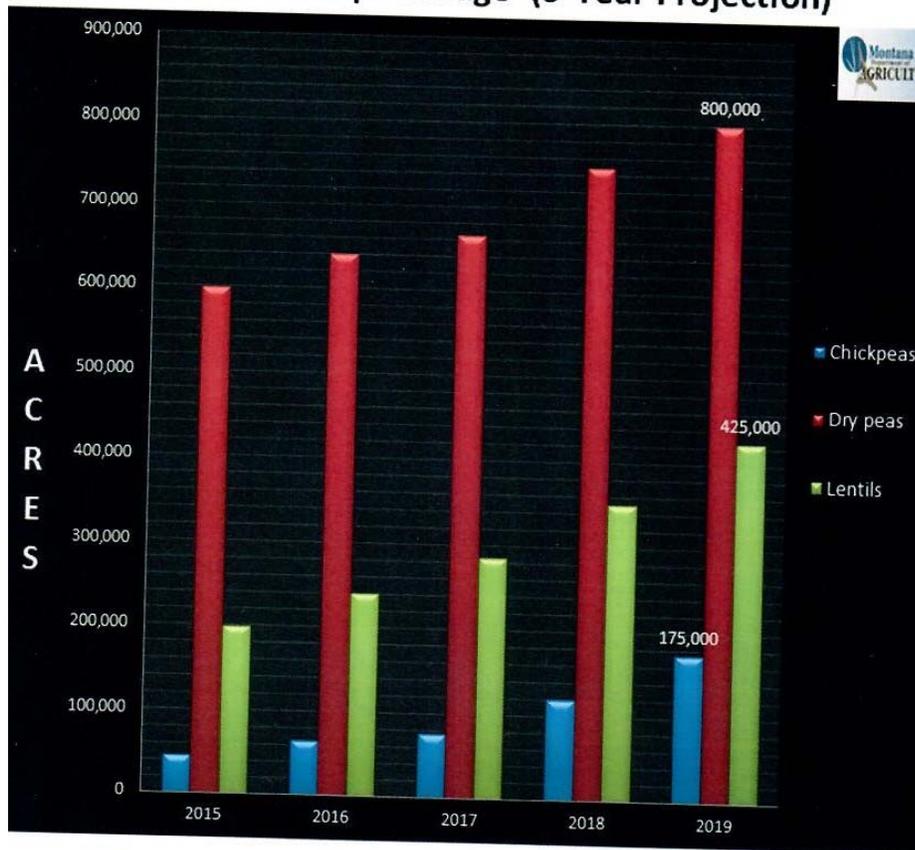


5-Year Total of Montana Foreign Exports=\$ 271,470,339

Source: WISER Trade State Online Database

Pulse Crop production is skyrocketing in the Great Plains and is becoming a major cash crop. The Montana projections⁹ are shown below.

Montana Pulse Crop Acreage (5-Year Projection)



It is predicted that Montana Pulse crop acreage has the potential to increase to 1,400,000 acres in the next 5 years.

⁹ http://agr.mt.gov/agr/_downloadGallery/Pulse_Acreage_Predictions.PNG

Value of Montana Foreign Exported Pulse Crops

<u>Pulse Crops</u>	2010	2011	2012	2013	2014
<i>Peas</i> (including seed)	\$1,497,288	\$9,802,790	\$25,330,712	\$38,559,990	\$48,610,794
<i>Peas</i> (Fresh or Chilled)			\$4,045	\$32,250	\$338,974
<i>Lentils</i> (including seed)	\$5,850,127	\$11,218,260	\$25,400,660	\$30,398,897	\$37,860,639
<i>Chickpeas</i> (including seed)	\$720,611	\$5,187,384	\$9,616,049	\$9,590,211	\$7,008,140
<i>Beans</i> (including seed)	\$159,420	\$378,494	\$1,049,545	\$935,858	\$1,919,241
Total Value	\$8,227,446	\$26,586,928	\$61,401,011	\$79,517,166	\$95,737,788

North Dakota leads the nation in lentil and dry pea production up until a few years ago. More recently, Montana has taken the lead in total pulse crop production.

Lentil production began in the Palouse growing area of Eastern Washington state in 1916, dry pea production in the 1920s, and chickpea production in 1981. The region offered excellent growing conditions and a

growing season with annual rainfall of 15 inches to 24 inches (400 mm to 600 mm), most of which fall in the autumn and winter months.

More recently, the Northern Plains region has become an increasingly important production area. Since the 1990s, the lion's share of U.S. food legume production has moved from the rolling hills and loess soils east of the Palouse into the Northern Plains region, where pulses fit well with the established crop rotation.

By 2009, North Dakota had become the largest producer of pulse crops in the U.S. In 2009, Montana occupied the second position, cultivating the greatest number of yellow peas in the U.S., in addition to significant acreage devoted to lentils. Pacific Northwest farms in Washington and Idaho remain the largest producers of green peas and chickpeas. In those areas, which receive sufficient rainfall to support annual cropping, food legumes continue to replace summer fallow. The region boasts considerable potential and its role as an important producer of dry peas and lentils is expected to continue. Meanwhile, the range of U.S. food legume varieties has changed over time and is likely to continue to evolve as breeding programs develop improved types.

This newly emerging cash crop, must, of necessity be moved to markets both domestic and international. India, an emerging buyer with a

huge appetite for pulses, is beginning to assert itself on the world food market.

Transportation in shuttle and less than shuttle quantities is the general movement pattern. Those facilities handling the pulse crops are most cases, not the large shuttle loaders but rather the multi-car loaders. Pulse crops can be damaged by rough or multiple handling and require careful handling by merchandiser and loaders.

The BNSF has been increasing less-than-shuttle rates (such as those utilized in the transportation of pulses and barley) much faster than the shuttle rates (such as those utilized for wheat and other bulk commodity shipments), because the railroads see the growth of production and the prices being received by the producers for the pulse crops and barley and the railroads business model likes shuttle movements (110+ car) over less than shuttle movements.

5 CARRIERS' GOALS LEAD TO CONFLICT IN THE TRANSPORT OF FARM PRODUCTION.

A main goal of railroad carriers is to maximize profit. Railroads in agricultural America desire to move agricultural commodities in trainload quantities to market (highest return to railroads). There is continued resistance to moving stratified farm product (multiple grades, alternative

crops or non-homogeneous mixes) and products that do not lend themselves to trainload shipments such as peas, lentils, pulse and developing varieties. Stratification of farm production through diversification creates greater returns to farm production but railroads provide disincentives to such actions. Today, railroad profit goals do not necessarily coincide with long term profitability for farm producers.

Be mindful that the farm producers bear the freight charges associated with transportation of grains, but the elevator/merchandisers pay the railroads for freight transportation. The farm producers bear the cost of transportation of their grain. However, the elevator, which has deducted the transportation cost from the price paid to the farm producer, actually pays the railroads for the freight charges. That fact makes agricultural transportation unique: namely, the farm producer bears the cost of transportation, while the elevator pays the cost of transportation.

The STB has, in the past, acknowledged understanding of this unique situation. The STB needs to clearly state that in agricultural rate cases, the farm producer has, and will continue in the future to have, standing to file rate actions, and complaints filed by or on behalf of producers will not be subject to dismissal because the producers pay rail rates indirectly.

6 RAIL CARRIERS HAVE ESTABLISHED A DEMARKETING PROGRAM WHICH THEY PORTRAY AND DISGUISE AS “MARKET BASED PRICING”. THIS HAS LED TO RAIL CARRIERS DEMARKETING CERTAIN SHIPPERS WHILE PROMOTING OTHERS AND LIMITING THEIR ACCESS TO THEIR MARKETS.

Why is this important in this proceeding? Market based pricing is a concept of the railroads trying to legitimizing their exercise of dominance in the movement by setting tariff pricing to favor where the carriers wants to ship to not necessarily where the producer or merchandiser desires to build a market. By blanketing a region, or product producing area, the carriers will raise prices to limit access into a particular market.

While this will not produce “outlier” rates, it will produce high overall rates that the regulatory schemes available from the Board should address. The common carrier obligation should limit the railroads from demarketing any shipper on their systems and the Board needs to set the bar and regulatory remedy access so that it is more difficult for the railroads to pick winners and losers in the market place.

The railroad here is making (setting) the price in the marketplace and the farm producers, coal producers, chemical producers, etc. are the ones

paying for the transportation cost that is now dictated by captivity and not by market demands. Only a company with absolute market power and little or no effective competition can price in this way.

7 SUMMARY:

We commend and thank the Board for taking on this most important issue. It is long overdue. However, at the same time, the limited scope to “outliers” and “very small shipments” does little to address the problems of bulk shipper industries including agriculture. There continue to be NO effective regulatory remedies to address agricultural producer and other bulk shipper concerns.. Agriculture continues to need the Board to focus on solving this 35 year old problem. If the Board doesn’t act now, while the railroads are setting profitability records, then when will it act to protect and provide pathways to remedies for captive rail customers? With the revisions to regulatory practice and procedure passed in S. 808, the STB Reauthorization Act of 2015, we feel now is the time to find pro-active solutions.

ARC, the USDA and National Grain and Feed Association have provided for the Board ideas that are worthy of consideration but the Board

seems to have pivoted away from finding solutions to this industry specific problem.

We reiterate, transportation policy has had little overall goal or orientation other than helping railroads achieve revenue adequacy. To a marked degree, our national policy has been patched up to address real or apparent emergencies as they arose. Our policy in this country has been backward looking rather than forward looking. As we look at this proceeding, this Board has a real chance of taking a forward look at access to regulatory oversight for agricultural production. But the Board must be pro-active in this process and this holds great hope that the future may lead to forward-looking, well-thought-out changes that will promote a more economical, efficient, fair and productive rail transportation system for the national economy.

VERIFICATION:

I hereby certify that the foregoing is true and correct on penalty of perjury.

A handwritten signature in cursive script that reads "Terry Whiteside". The signature is written in dark ink on a light-colored background.

Date: 11-14-16

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