

**BEFORE THE
SURFACE TRANSPORTATION BOARD**

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RAIL FUEL SURCHARGES (SAFE HARBOR)

**REPLY COMMENTS
OF UNION PACIFIC RAILROAD COMPANY**

GAYLA L. THAL
LOUISE A. RINN
REBECCA B. GREGORY
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
Phone: (402) 544-5291

MICHAEL L. ROSENTHAL
Covington & Burling LLP
1201 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
Phone: (202) 662-6000

*Attorneys for Union Pacific
Railroad Company*

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Union Pacific Railroad Company submits these reply comments to address the opening comments filed by other parties in this proceeding. The Board instituted this proceeding to obtain comments “on whether the safe harbor provision” of the Board’s fuel surcharge rules “should be modified or removed,” particularly in light of questions about growth in the spread between railroads’ actual fuel prices and the HDF Index. *Rail Fuel Surcharges (Safe Harbor)*, EP 661 (Sub-No. 2), slip op. at 3 (STB served May 29, 2014).

The opening comments provide no basis for modifying or removing the HDF Index safe harbor. A clear majority of shippers and parties supporting shipper interests indicate that they would prefer that railroads continue to use a publicly available index in their fuel surcharge programs. And no party suggests an alternate index that would perform better than the HDF Index.

Rather than focus on the HDF Index safe harbor, several shippers urge the Board to disregard the limits on its authority to micromanage fuel surcharges. They justify their requests by using misleading comparisons to suggest problems where none exist. Some ask the Board to prohibit entirely the use of fuel surcharges. Others want the Board to require that railroads obtain pre-approval of surcharge formulas, adopt different and more complicated formulas, or update

formulas more frequently. Several shippers also ask the Board to expand railroad reporting requirements to support intrusive regulation.

The Board should reject the interventionist approach that shippers advocate. Congress ended the era of excessive agency interference with railroad pricing practices when it passed the Staggers Act. In *Rail Fuel Surcharges*, EP 661 (STB served Jan. 26, 2007); *Dairyland Power Cooperative v. Union Pacific Railroad*, NOR 42105 (STB served July 29, 2008), and *Cargill, Inc. v. BNSF Railway*, NOR 42120 (STB served Aug. 12, 2013) (“*Cargill III*”), the Board recognized that its authority to regulate the reasonableness of railroad practices in establishing fuel surcharge programs is limited to addressing misrepresentations.¹ If a railroad accurately describes and implements a fuel surcharge program, no misrepresentation occurs unless “the general formula used to calculate fuel surcharges bears *no reasonable nexus* to the fuel consumption for the traffic to which the surcharge is applied.” *Cargill III* at 3 (quoting *Dairyland* at 6) (emphasis added). As discussed below, the Board’s “no reasonable nexus” test strikes the right balance in addressing the concerns raised in this proceeding that are unrelated to the HDF Index safe harbor.

In Part I, we address the HDF Index safe harbor and the Board’s concern about growth in the spread between railroads’ actual fuel prices and the HDF Index. In Part II, we address shipper calls for expanded regulation of fuel surcharge programs. In Part III, we conclude by asking the Board to reaffirm the HDF Index safe harbor and terminate this proceeding.

¹ If a shipper’s complaint is directed at the level of charges, its recourse is to file a rate complaint. See *Cargill, Inc. v. BNSF Ry.*, NOR 42120, slip op. at 5 (STB served Jan. 4, 2011) (*Cargill I*) (citing *Union Pac. R.R. v. ICC*, 867 F.2d 646 (D.C. Cir. 1989)).

I. The Opening Comments Support The Continued Use Of The HDF Index Safe Harbor.

The opening comments provide no basis for modifying or removing the HDF Index safe harbor. Shippers want railroads to use a publicly available index, shippers confirm that the HDF Index is the “best index available,” and shippers identify no harm from changes in the spread between railroad fuel prices and the HDF Index.

A. Shippers continue to support the use of a publicly available index.

The Board adopted the HDF Index safe harbor in response to the views of a wide variety of shippers that railroads should use a uniform, publicly available index to measure changes in fuel prices. *See Rail Fuel Surcharges* at 11. The opening comments show that shippers continue to support the use of a publicly available index.

- The National Industrial Transportation League (“NITL”) “has concerns with elimination of the safe harbor” because railroads might then use a variety of “opaque” adjustment mechanisms in their fuel surcharge programs.²
- Dow Chemical Company (“Dow”) expresses concern that elimination of the safe harbor could lead railroads to use “a variety of indices that could be inferior to the HDF.”³
- The U.S. Department of Agriculture (“USDA”) recognizes that eliminating the HDF Index safe harbor would be inconsistent with the desires of shippers who “strongly advocated for the usage of an index that ensured accuracy, transparency, and accountability.”⁴

Only two parties oppose the use of a publicly available index. A collection of coal interests calling themselves the “Allied Shippers” argue that the use of actual fuel prices would

² Comments of The National Industrial Transportation League (“NITL Comments”) at 8.

³ Comments of the Dow Chemical Company (“Dow Comments”) at 2. Dow’s comments include a regression analysis showing the correlation between railroad fuel prices reported to the Board and HDF Index values using quarterly data. *See Dow Comments* at 10 & Ex. 4. We reported a higher correlation between our fuel prices and HDF Index values in our opening comments because we used monthly data. *See Opening Comments of Union Pacific Railroad Company (“Union Pacific Comments”) at 7.*

⁴ Comments of the U.S. Department of Agriculture (“USDA Comments”) at 6.

be more accurate,⁵ but the vast majority of shippers urged the Board to require the use of an index that was transparent and neutral, *see Rail Fuel Surcharges* at 11; *Cargill III* at 7. The Mercury Group (“Mercury”) also opposes the use of an index, but Mercury markets its own proprietary process for addressing fuel costs, so it has no interest in a publicly available adjustment mechanism.⁶

A few parties make the puzzling suggestion that the Board retain the “safe harbor” while eliminating “immunity.”⁷ As we observed on opening – and as NITL and Dow recognize in their comments – the Board cannot require railroads to continue using a publicly available index to satisfy shippers’ desire for “transparency, availability, and neutrality,” but then hold railroads liable when the index fails to reflect precisely the changes in actual fuel prices, as will inevitably happen with any publicly available index.⁸ (USDA acknowledges that “devising an index that perfectly coincides with actual internal fuel costs is beyond the capability of the Board, shippers, or railroads.”⁹)

When parties say they favor a “safe harbor” but not “immunity,” their concern appears to be that railroads remain subject to claims that a fuel surcharge formula bears no reasonable nexus

⁵ Comments of the Western Coal Traffic League, American Public Power Association, Edison Electric Institute, National Rural Electric Cooperative Association, South Mississippi Electric Power Association and Consumers Energy Company (“Allied Shippers Comments”) at 44-47.

⁶ Comments of The Mercury Group (“Mercury Comments”) at 1.

⁷ *See* USDA Comments at 6 (“Aside from immunity, USDA does not believe there is anything fundamentally wrong with using the HDF Index as a safe harbor.”); Opening Comments of National Grain and Feed Association (“NGFA Comments”) at 7 (“[R]eliance on the HDF Index by granting it ‘safe harbor status’ should *not* immunize rail carriers . . .”). Opening Comments of Highroad Consulting, Ltd. (“Highroad Comments”) at 13 (“[I]f the Safe Harbor is eliminated, the railroads would not have an approved index on which to base their fuel surcharge programs and the result could be diminished transparency and credibility of the fuel surcharge programs. However, the Board should redefine or modify the Safe Harbor to remove the immunity . . .”).

⁸ *See* Union Pacific Comments at 10.

⁹ USDA Comments at 6.

to fuel consumption for the traffic to which the surcharge applies.¹⁰ But those parties need not be concerned because the current HDF Index safe harbor provision *does not* preclude such claims. *See Cargill III* at 9. The safe harbor provision applies only to the decision to use the HDF Index. Ultimately, most shippers favor the continued availability of the current, limited safe harbor for railroads that use a Board-approved, publicly available fuel price index.

B. Shippers do not identify any index that would be better than the HDF Index.

The opening comments validate the Board’s decision to use the HDF Index as the safe harbor. No party identifies an index that would perform better, and several shipper parties support the continued use of the HDF Index in particular:

- USDA says that “the HDF index appears to be the best candidate” to serve as a proxy for changes in railroad fuel prices.¹¹
- Arkansas Electric Cooperative Corporation (“AECC”) says that it “is not aware of any index that would serve . . . better than the HDF Index.”¹²
- Highroad Consulting (“Highroad”) says that “there is no current alternative [to the HDF Index] that would improve the processes.”¹³
- National Grain and Feed Association (“NGFA”) makes clear that it “does not argue that the Board eliminate use of the HDF Index as a benchmark for measuring fuel costs.”¹⁴

¹⁰ *See, e.g.*, Opening Comments of Colorado Springs Utilities (“CSU Comments”) at 2 (“Safe harbor treatment should be limited to application of the index and it should not apply to railroad surcharge programs generally.”); *see also* USDA Comments at 5 (“Exactly which scenarios can or cannot be immunized by the safe harbor are not clearly understood.”).

¹¹ USDA Comments at 6.

¹² Comments of Arkansas Electric Cooperative Corporation (“AECC Comments”) at 2.

¹³ Highroad Comments at 5.

¹⁴ NGFA Comments at 7.

NITL and Dow ask the Board to consider other possible indices – NITL would make reconsidering the index a biennial event¹⁵ – but neither party suggests an alternative to the HDF Index, and Dow recognizes there are a “variety of indices that could be inferior to HDF.”¹⁶ Only the Allied Shippers and Mercury criticize the HDF Index, but, as discussed above, they do not support the use of a publicly available index, which is at odds with the explicit desires of a majority of shippers.

C. Shippers have not been harmed by changes in the spread.

The opening comments confirm that no one was surprised by either the existence of a spread between railroads’ actual fuel prices and the HDF Index or the changes in the spread over time. One shipper says the Board should require railroads to perform periodic “true ups” of fuel surcharges¹⁷ – which seems similar to the periodic “rebasings” concept we discussed on opening – but it never weighs the costs and benefits. As we explained on opening, the benefits are highly uncertain because of the month-to-month variability in the spread, while frequent changes to fuel surcharge programs are guaranteed to impose significant costs on both railroads and shippers.¹⁸

Most parties say little about the growth in the spread since the Board adopted the HDF Index safe harbor. Instead, they focus on other aspects of fuel surcharge programs. They likely recognize that long-term changes in the spread have little or no impact on their rates because of three factors: (i) past changes are irrelevant for new movements; (ii) month-to-month changes

¹⁵ NITL Comments at 9 (“In addition, the League believes that the Board should commit to an ongoing review, perhaps once every two or three years, to determine if the EIA/HDF Index, as potentially modified by the Board or any replacement index, continues to track each carrier’s incremental costs of fuel over time, to insure that the ‘safe harbor’ continues to be justified.”).

¹⁶ Dow Comments at 2.

¹⁷ See AECC Comments at 2.

¹⁸ See Union Pacific Comments at 10.

can benefit shippers;¹⁹ and (iii) periodic adjustments to base rates for longer-term movements will offset the impact of longer-term changes in the spread.

The Allied Shippers are the only party that attempts to quantify the effect of long-term changes in the spread, but their calculations of purported overcharges are severely flawed.²⁰ They incorrectly assert that railroad fuel surcharge programs were based on a presumption that “the differential (or ‘spread’) between railroad fuel price and HDF price is constant,”²¹ when it was well known that the spread is variable.²² The Allied Shippers thus failed to account for the three factors discussed above: the “original” spread is irrelevant for new rates; shorter-term variability in the spread can benefit shippers; and longer-term variability in the spread may be addressed by adjustments to base rates.²³ There is no basis for concluding that fuel surcharge programs have resulted in any shipper paying more than market rates for rail transportation.

II. The Board Should Reject Requests To Micromanage Fuel Surcharge Programs.

The Board should reject requests by shippers to expand its regulation of fuel surcharges. The requests are based on misleading math and irrelevant comparisons. Moreover, the expanded regulation many shippers request – which includes periodic reviews of railroads’ fuel surcharge programs and rules requiring surcharge programs to reflect more precisely the fuel consumption of particular movements and improvements in fuel efficiency – exceeds the Board’s authority to

¹⁹ As we discussed in our opening comments, from April 2007 through March 2014, the spread decreased approximately half the time. *See* Union Pacific Comments at 8.

²⁰ *See* Allied Shippers Comments, Crowley/Mulholland VS at 6-7 & Ex. C/M-3.

²¹ *Id.*, Crowley/Mulholland VS at 3.

²² *See* Union Pacific Comments at 7-8.

²³ The Allied Shippers’ calculations are also flawed because they are based on a much greater volume of traffic than was actually subject to a regulated fuel surcharge. For example, the Allied Shippers assume Union Pacific moved 1,703,000 carloads of coal as common carrier traffic in 2013. *See* Allied Shippers Comments, Crowley/Mulholland VS, Ex. C/M-3, lines 6b, 8b. In fact, most of our coal moves under contract rates.

regulate railroad practices. The Board may evaluate the reasonableness of specific fuel surcharge programs only on complaint, and it may not micromanage the programs' structure: its role "is to assure that the rail carrier's representation is not deceptive, rather than to order the rail carrier to make a different representation." *Cargill III* at 16.

A. Shippers paint a misleading picture of railroad fuel surcharge programs.

Several parties try to suggest a need for more regulation of fuel surcharge programs by presenting incomplete data and misleading calculations. A prime example is NITL's comparison of the percentage changes in fuel surcharge revenue per car with the percentage changes in fuel expense per car over time.²⁴ NITL paints a misleading picture in two ways:

First, NITL fails to address how much more traffic is subject to fuel surcharges in 2014 than in 2007. On Union Pacific, the share of traffic subject to fuel surcharges increased over time as older contracts without fuel surcharge provisions expired. As more traffic becomes subject to fuel surcharges, the amount of fuel expense recovered through fuel surcharges will naturally increase.

Second, NITL grossly exaggerates the increase in fuel surcharge revenue relative to fuel expense because it compares *percentage changes*. Comparing percentage changes is especially deceptive when one of the initial figures – here, fuel surcharge revenue per car in late 2007 – is relatively low. This is why: Imagine a movement for which the fuel expense is \$210, of which \$10 is collected via a fuel surcharge. Now imagine fuel prices rise, so the fuel expense is \$220, and the surcharge rises to \$20 to offset exactly the higher fuel expense. NITL would say: "Fuel surcharge revenue per car increased by 100% (*i.e.*, \$10 to \$20) while fuel expense increased by

²⁴ NITL Comments at 7. Other parties present similar data. *See* Dow Comments at 9; Comments of Consumers United for Rail Equity ("CURE Comments") at 6.

less than 5% (*i.e.*, \$210 to \$220).” NITL’s focus on percentage changes obscures that in this situation the increase in fuel surcharge revenue merely offsets the incremental increase in fuel expense.²⁵

Dow makes similar errors by focusing on “percentage changes” when it notes that, under our general mileage-based fuel surcharge program, “a 56.7% increase in the HDF price, from \$2.50 to \$3.94 per gallon, results in a 311% increase in the per-mile fuel surcharge fee paid by shippers, from \$0.09 to \$0.37 per mile.”²⁶ Those figures actually show that a \$1.44 increase in fuel price per gallon results in a \$0.28 increase in the per-mile surcharge fee – which is what one would expect from a fuel surcharge program like ours that is designed so a \$0.05 change in fuel price per gallon results in a \$0.01 change in the per-mile surcharge fee.

In sum, the mathematical comparisons offered in the shippers’ opening comments provide no reason to consider additional regulation of railroads’ fuel surcharge programs.

²⁵ NITL, Dow, and Consumers United for Rail Equity (“CURE”) also fail to address a third issue: the improvements in fuel efficiency we have achieved through significant investments. To perform an accurate comparison over time, one must recognize that our current fuel expense would be higher if we had not improved our fuel efficiency. (As we discussed below, while our fuel efficiency has increased, it has not yet increased to the point where it is appropriate to change the assumptions we use in our fuel surcharge program. *See* p. 14, *infra*.)

NGFA and USDA purport to compare the percentage growth in grain fuel surcharges per car to the percentage growth in railroad fuel costs. *See* NGFA Comments at 6; USDA Comments at 4. They do not provide their underlying data, but it appears likely that their comparison suffers from the same basic flaws as those presented by NITL, Dow, and CURE.

Highroad also performs comparisons across time periods that fail to account for changes in fuel surcharge coverage and fuel efficiency. *See* Highroad Comments at 10-12.

²⁶ Dow Comments at 10.

B. The Board has no authority to rule on the reasonableness of particular railroad fuel surcharge programs except in response to a complaint.

Several parties urge the Board to institute periodic reviews of fuel surcharge programs and to require railroads to establish that their programs are reasonable.²⁷ None of those parties presents evidence of pervasive problems with fuel surcharge programs that would justify the resource intensive reviews they propose. Moreover, under the ICC Termination Act, the Board has no authority to determine whether a particular practice is reasonable unless it is acting on a complaint. Section 10702 requires railroads to establish reasonable “rules and practices.” 49 U.S.C. § 10702(2). Section 10704 authorizes the Board to determine whether a challenged practice is reasonable, but section 10704(b) states that “[t]he Board may begin a proceeding under this section only on complaint.” *Id.* § 10704(b). In fact, the Board acknowledged in *Rail Fuel Surcharges* that its “authority to determine whether any particular fuel surcharge applied by a specific railroad is an unreasonable practice . . . is limited to proceedings begun on complaint.” *Rail Fuel Surcharges* at 8. In addition, in such a proceeding, the complainant must prove that the challenged practice is unreasonable. *See, e.g., N. Am. Freight Car Ass’n v. BNSF Ry.*, NOR 42060 (Sub-No. 1), slip op. at 5 (STB served Jan. 26, 2007). The Board should reject all proposals involving periodic reviews of fuel surcharges.

²⁷ *See* CSU Comments at 10 (“[T]he STB should review all attributes of a fuel surcharge program and require the railroads to demonstrate that the surcharge program design, how it is being applied, the fuel use, and the incremental revenue collected are reasonable.”); CURE Comments at 14 (urging the Board to require “approval of [railroad] fuel surcharge programs”); Dow Comments at 17 (urging the Board to require railroads to make “regular filings . . . at the Board to show that their fuel surcharge programs appropriately recover only their incremental fuel costs,” after which “the Board could issue a decision on the fuel surcharge mechanisms used by the railroads”); NITL Comments at 10-11 (urging the Board to require railroads “to justify – up front – the reasonableness of [the] key assumptions used in their overall fuel surcharge program” and conduct “periodic proceedings to assure the shipping public” that railroads’ “fuel surcharge programs are reasonable”).

Several parties urge the Board to prohibit the use of fuel surcharges entirely.²⁸ However, that would be beyond the agency’s authority to police against misrepresentations.²⁹ The Allied Shippers argue that fuel surcharges are “a major step backwards in the evolution of rail pricing” and their use “runs afoul of the Staggers Act.”³⁰ They further argue that all railroads should use the Rail Cost Adjustment Factor to ensure the recovery of any increases in fuel costs.³¹ But they have their history wrong. A primary purpose of the Staggers Act was to give railroads greater freedom in setting rates and greater flexibility in structuring their business dealings – not to confine them to one uniform method of structuring rates.³² Nothing in the Board’s governing statute permits the agency to prohibit a non-deceptive method of pricing.

C. Shipper concerns have been addressed within the existing regulatory framework.

In their opening comments, some shippers seek expanded regulation of two specific aspects of fuel surcharge programs: how precisely the formulas address attributes of particular movements, and how precisely the formulas reflect improvements in fuel efficiency. However, the *Cargill* decision correctly rejected micromanagement of these issues as beyond the Board’s authority to prevent misrepresentations. The Allied Shippers ask the Board to reconsider rulings

²⁸ See Allied Shippers Comments at 78-81; Highroad Comments at 19.

²⁹ See *Rail Fuel Surcharges* at 7 (discussing the Board’s authority to regulate fuel surcharges).

³⁰ Allied Shippers Comments at 78.

³¹ See *id.* at 78-79. One of the main problems with relying on RCAF is that the weighting of cost factors is only done annually. As a consequence, in times of rising fuel costs, RCAF understates the weighting of the fuel component of the index and the impact of increases in fuel costs. The Board has recognized that RCAF has a “time lag” issue. *Rail Fuel Surcharges*, EP 661, slip op. at 6 (STB served Aug. 3, 2006).

³² See Staggers Rail Act of 1980, Pub. L. No. 96-448, § 101(a), 94 Stat. 1895, 1897 (establishing policies “to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail” and “to minimize the need for Federal regulatory control over the rail transportation system”).

in *Cargill* that require shippers to pursue most “over-recovery” claims through rate cases, rather than as unreasonable practices, but the Board correctly applied the law. Finally, several shippers call for more railroad reporting of fuel-related data, but given the limits on the Board’s authority to regulate fuel surcharges, no legitimate reason exists for these additional reporting burdens.

1. The Board has correctly rejected arguments that railroads must tailor their fuel surcharges narrowly.

Several parties urge the Board to require railroads to design fuel surcharge programs that apply to more narrowly defined categories of movements. For example, NGFA complains that “for many agricultural commodities the fuel surcharge per car is identical regardless of whether the shipment involves unit trains or single cars.”³³ Colorado Springs Utilities (“CSU”) says that fuel surcharges should account for different “commodity types” and “origination points.”³⁴ AECC says that railroads should be required to make various movement-specific adjustments to

³³ NGFA Comments at 3.

³⁴ See CSU Comments at 8. CSU claims that our fuel surcharge programs assume different rates of fuel consumption for Wyoming coal, depending on whether the movement occurs under a tariff or a contract. See CSU Comments at 8-9. In fact, the Wyoming circular CSU references, which includes a fuel surcharge program designed so a \$0.06 change in price per gallon results in a \$0.01 change in the per-mile surcharge fee, *can* apply to movements under tariffs. See UP Circular 6603-C, Item 100 (“The rules contained in this Circular apply on Coal Trains loading at UP-served Origins in Wyoming when such Coal Trains move i) under Tariff or Circular *unless such Tariff or Circular has more specific provisions . . .*”) (emphasis added). Exceptions to the Wyoming circular are sometimes made, however, to reflect atypical routes with different grades and locomotive requirements.

CSU also misinterprets a statement from a Union Pacific SEC Form 10-K filing as involving the relationship between strike prices and total *fuel revenue*. See CSU Comments at 9. In that filing, we explained that converting certain non-regulated traffic to a mileage-based surcharge did not materially change our *freight revenues*. See Union Pacific Railroad Co., Annual Report (Form 10-K) at 28 (Feb. 6, 2009) (“We also converted a portion of our non-regulated traffic to mileage-based fuel surcharge programs. The resetting of the fuel price at which the fuel surcharge begins, in conjunction with rebasing the affected transportation rates to include a portion of what had been in the fuel surcharge, did not materially change our *freight revenues*, as higher base rates offset lower fuel surcharge revenue.” (Emphasis added)).

their surcharges.³⁵ However, the Board has correctly recognized that it cannot require railroads to design their fuel surcharge programs to apply to any particular group of traffic. Railroads may design their fuel surcharge programs to apply to such traffic as they see fit, and such programs are lawful *unless* the fuel surcharge bears “no reasonable nexus to the fuel consumption *for the traffic to which the surcharge is applied.*” *Cargill III* at 3 (quoting *Dairyland* at 6) (emphasis added).

In *Cargill*, the shipper argued that BNSF’s fuel surcharge program was “fundamentally flawed” because it applied to agricultural *and* industrial products, and those two types of traffic allegedly had “significantly different fuel consumption characteristics.” *Id.* at 14. However, the Board explained that BNSF had the right in the first instance to establish which traffic would be subject to its surcharge, and there was nothing deceptive about the decision to apply a single, straightforward, transparent fuel surcharge to traffic with different fuel consumption characteristics:

BNSF could have designed any number of fuel surcharges, each with its own step function, given the numerous traffic categories with different fuel consumption characteristics that could exist But we do not find it unreasonable for BNSF to have adopted a single fuel surcharge equally applicable to agricultural and industrial products that is simple and easy for BNSF and its shippers to administer and use. . . . BNSF’s fuel surcharge program appears to be both straightforward and transparent. Thus we do not find unreasonable BNSF’s decision to apply a single fuel surcharge equally to all agricultural and industrial products, even if that meant the surcharge burden would not fall exactly equally on all types of traffic.

³⁵ See AECC Comments at 9-13 (adjustments for fuel consumed because of route circuitry); *id.* at 14-15 (adjustments for fuel consumed in passing sidings); *id.* at 16-18 (adjustments for fuel consumed because of differences in terrain).

Id.; see also *Cargill, Inc. v. BNSF Ry.*, NOR 42120, slip op. at 4 (STB served Jan. 4, 2011) (“*Cargill P*”) (“[I]t would be unreasonable to require railroads to incorporate every factor that affects fuel costs into their fuel surcharge formulas . . .”). Accordingly, the Board should reject calls for rules that would require railroads to develop commodity-specific or movement-specific fuel surcharge programs.

2. The Board has correctly rejected arguments that would require unrealistic precision in fuel surcharge design.

Several parties express concern that railroads have not modified their fuel surcharge programs to reflect improvements in fuel efficiency.³⁶ Our fuel surcharge programs accurately reflect our fuel consumption rates. The program that applies to most of our regulated traffic is based on a study that showed our trains consumed fuel at a rate of approximately one gallon for every five loaded car miles – that is why our general fuel surcharge for regulated traffic increases by \$0.01 for every \$0.05 increase in the HDF Index. We revisit the study every year, and while we have certainly become more fuel efficient, our fuel consumption rate has not improved enough to change the 1 to 5 relationship into a 1 to 6 relationship.

The Allied Shippers want the Board to require railroads to modify their fuel surcharge programs to reflect each incremental improvement in fuel efficiency. They say: “For every one (1) percent increase in fuel efficiency, there should be a corresponding one (1) percent increase in fuel surcharge program step length.”³⁷ However, the result would be more frequent, largely inconsequential changes to fuel surcharge programs that would increase administrative costs for railroads and shippers. Even if we could determine precisely when we have achieved each one-

³⁶ See, e.g., Allied Shippers Comments at 63-72; CSU Comments at 6-7; Dow Comments at 14-16.

³⁷ Allied Shippers Comments, Crowley/Mulholland VS at 26.

percent increase in fuel efficiency, as opposed to a transitory change due to fluctuations in traffic volumes or mix, it could mean, for example, changing the simple relationship of a \$0.01 change in the fuel surcharge for every \$0.05 change in the HDF Index to a more complex relationship of a \$0.01 for every \$0.0505 change, and then a \$0.01 for every \$0.051005 change, and so on. It also would mean publishing and implementing a new program of step increases based on the new relationships. Moreover, because our regulated fuel surcharge applies to a variety of traffic, frequent, small changes would produce a misleading sense of precision.

The Board rejected a similar argument for greater precision in *Cargill*, concluding that it was not deceptive – and in fact, it was actually *less* deceptive – for railroads to avoid reflecting fractional differences in fuel consumption rates in their fuel surcharge formulas:

Nor was it unreasonable for BNSF to select a whole number and avoid using fractional amounts for its MPG [miles per-gallon] Assumption. A whole number allowed BNSF to avoid giving the appearance that the estimate was more precise than it really was, which would help to avoid creating pressure for frequent changes in the fuel surcharge formula to account for relatively small changes in MPG estimates resulting from temporary fluctuations in traffic volumes or the mix of traffic subject to the fuel surcharge. Thus a whole number was a reasonable choice to promote BNSF's objective of simplicity and ease of administration.

See Cargill III at 16. The *Cargill* decision makes clear that the fuel consumption rates embodied in a railroad's fuel surcharge formula are subject to challenge under the "no reasonable nexus" test, but that the Board's "role in an unreasonable practice case is to assure that the rail carrier's representation is not deceptive, rather than to order the rail carrier to make a different representation." *Id.*

3. The Board has correctly ruled that claims alleging over-recovery of fuel costs must be brought in rate cases.

In *Rail Fuel Surcharges*, the Board concluded that a railroad would be making inherently inconsistent representations if it imposed a fuel surcharge while also increasing base rates using

an index that reflects fuel cost increases – the Board referred to such a practice as “double dipping.” *Rail Fuel Surcharges* at 10. In *Cargill*, the Board rejected the shipper’s claim that the prohibition against “double dipping” should also apply if a shipper can show that a railroad set base rates in a way that reflect higher fuel prices while also imposing a fuel surcharge. The Board explained that no unlawful, inherently inconsistent representation occurs unless the railroad has expressly represented that the base rate already accounts for higher fuel prices. *See Cargill I* at 5-6.

The Allied Shippers urge the Board to reconsider its decision in *Cargill*, but they cannot avoid the fundamental legal principle that applies here: absent an express misrepresentation, a shipper has no legal basis for challenging the process that a railroad uses to construct rates. As the Board recognized in *Cargill I*, it cannot circumvent this principle by regulating as a “so-called ‘practice’” railroad behavior that is “manifested exclusively in the level of rates that customers are charged.” *Id.* at 2 (quoting *Union Pac. R.R. v. ICC*, 867 F.2d 646, 649 (D.C. Cir. 1989)). The Allied Shippers argue that this leaves shippers without recourse, but if a shipper believes that its rates are unlawfully high, it may file a rate complaint.

The Allied Shippers also argue that the Board erred in failing to recognize that “double dipping” concerns apply whether or not the index railroads use to adjust base rates incorporates changes in the cost of fuel.³⁸ The Allied Shippers’ concern appears to apply to rates under multi-year contracts with rate escalator provisions, which are outside the Board’s jurisdiction. *See* 49 U.S.C. § 10709.³⁹ (Union Pacific does not include escalator provisions in our regulated rates.) In

³⁸ Allied Shippers Comments at 57-59.

³⁹ In *Rail Fuel Surcharges*, the Board recognized that it has “no authority to regulate rail rates and services that are governed by a contract.” *Rail Fuel Surcharges* at 13.

(continued...)

any event, the Allied Shippers' second "double dipping" argument suffers from the same flaw as the first: absent an express misrepresentation, if a shipper believes it is being charged too much, it may file a rate complaint.

4. The Board should reject calls to require reporting of additional fuel-related data because the data could not be used for a legitimate regulatory purpose.

Railroads already file quarterly reports that disclose their total fuel costs, total gallons of fuel consumed, total increase (or decrease) in fuel cost as compared to the previous quarter, total revenue from fuel surcharges, and revenue from fuel surcharges on regulated traffic to comply with the Board's decision in *Rail Fuel Surcharges*, EP 661 (Sub-No. 1) (STB served Aug. 14, 2007). Several parties want railroads to report even more fuel-related data, but the data they request could not be used for any legitimate regulatory purpose, and in many cases, the data simply do not exist.

Most parties that request additional reporting want the Board to use the data to perform periodic reviews of railroads' fuel surcharge programs and declare whether they are reasonable. However, as discussed above, the Board has no authority to conduct such proceedings. *See* p. 10, *supra*. Along similar lines, some parties want railroads to report fuel-related data separately for different commodity groups and various other traffic groupings – presumably to support claims that fuel surcharges should focus on narrower categories of traffic.⁴⁰ However, as discussed above, railroads are not required to establish separate fuel surcharge programs for different

Highroad and Mercury argue that the Board should partially revoke class exemptions to apply its fuel surcharge rules to exempt traffic, but the Board concluded in *Rail Fuel Surcharges* that there was no support in the record for re-regulating exempt traffic, *see Rail Fuel Surcharges* at 13, and neither Highland nor Mercury presents any evidence that the marketplace has materially changed for any of the exempted categories of traffic. *See* Highroad Comments at 14; Mercury Comments at 20.

⁴⁰ *See* NGFA Comments at 8; Allied Shippers Comments, Crowley/Mulholland VS at 31-33.

commodity groups or movements with different fuel consumption characteristics. *See* pp. 12-13, *supra*. Accordingly, there is no legitimate reason to require railroads to develop and report the requested data. *Cf.* 49 U.S.C. § 11161 (directing the Board to minimize burdensome data development requirements).

Finally, several parties want railroads to report data that do not exist – at least they do not exist for Union Pacific. One example is data regarding fuel consumption by commodity group. We do not routinely collect fuel consumption data for all our trains. And, even if we collected the data, we could not precisely assign fuel to the specific cars that carry different commodities and are switched on and off trains at different points along a route. As another example, USDA wants railroads to report “the total revenue allocated to fuel costs collected through the base rate.”⁴¹ Others make similar requests.⁴² But as the Board has recognized, there are many factors that carriers consider in setting their base rates, “such as general market conditions, carrier-specific financial condition, product demand and the competitive options available to particular shippers – all of which could influence how a carrier structures its pricing,” so it makes little sense “to attribute values to each component of rail pricing actions . . . on a component-by-component basis.” *Cargill I* at 6.

III. The Board Should Reaffirm The HDF Index Safe Harbor And Terminate This Proceeding.

The opening comments provide no basis for modifying or removing the HDF Index safe harbor. The HDF Index continues to be “a reasonable index to apply to measure changes in fuel costs for purposes of a fuel surcharge program.” *Rail Fuel Surcharges* at 11. No party has identified a superior index.

⁴¹ USDA Comments at 7.

⁴² *See* Dow Comments at 17; NGFA Comments at 8.

Shipper requests for increased regulation of fuel surcharge programs unrelated to the HDF Index safe harbor ignore the Board's decisions in *Rail Fuel Surcharges*, *Dairyland*, and *Cargill*, and also ignore the limits on the Board's authority over pricing practices. The Board's current rules, including the "no reasonable nexus" test, strike the right balance in addressing the concerns raised in this proceeding that are unrelated to the HDF Index safe harbor. Shippers also have not established any need for expanded reporting that justifies increased burdens on railroads.

Accordingly, the Board should reaffirm the HDF Index safe harbor and terminate this proceeding.

Respectfully submitted,

GAYLA L. THAL
LOUISE A. RINN
REBECCA B. GREGORY
Union Pacific Railroad Company
1400 Douglas Street
Omaha, Nebraska 68179
Phone: (402) 544-5291



MICHAEL L. ROSENTHAL
Covington & Burling LLP
1201 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
Phone: (202) 662-6000

*Attorneys for Union Pacific
Railroad Company*

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