

BEFORE THE  
SURFACE TRANSPORTATION BOARD

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STB Ex Parte No. 669  
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INTERPRETATION OF THE TERM "CONTRACT" IN 49 U.S.C. 10709  
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**UNION PACIFIC RAILROAD COMPANY'S REPLY COMMENTS**

Union Pacific Railroad Company ("UP") hereby submits its reply comments in connection with the Board's notice of proposed rulemaking served March 29, 2007 ("NPRM"). The opening comments filed by other participants in this proceeding reinforce UP's view that the Board should withdraw its proposal to define the term "contract" and that the proposed definition would call into question legitimate commercial arrangements that benefit railroads and shippers. Several participants specifically addressed the impact of the Board's proposal on UP's Circular 111. Many of those participants misunderstand or misrepresent the nature of Circular 111. In this reply, we first address comments regarding the proposal to define the term "contract," and then we correct the inaccurate portrayals of Circular 111 and show that it is a valid common carrier tariff even under the criteria applied by its detractors.

**I. THE BOARD SHOULD WITHDRAW ITS PROPOSAL.**

Most participants urged the Board to withdraw its proposal to define the term "contract" in 49 U.S.C. § 10709. Even the few participants that support the proposal in general raised significant concerns about the definition proposed by the Board.

The opening comments reinforce UP's concerns about the proposal. As many participants observed, the Board does not have jurisdiction to determine whether a railroad and a shipper have entered into a binding contract for the provision of rail services, and disagreements

must be resolved in court pursuant to state law. Only one participant claimed that the Board has jurisdiction over contracts. The National Grain and Feed Association (“NGFA”) observes that Section 10709 provides that courts have jurisdiction over contracts that are “authorized by this section” and argues that the Board can define the elements of “authorized” contracts and retain jurisdiction over all other arrangements.<sup>1</sup> NGFA has misinterpreted the statute. The contracts “authorized by this section” are defined as those contracts between “[o]ne or more rail carriers” and “one or more purchasers of rail services to provide specified services under specified rates and conditions.” 49 U.S.C. § 10709(a). Congress did not give the Board license to expand or contract that definition. As many shipper and railroad participants explained in their opening comments, legislative history and judicial precedent establish that all questions concerning the existence and validity of contracts are governed by the common law of contracts and are outside the Board’s jurisdiction.<sup>2</sup>

Moreover, the Board has no need to develop its own definition of “contract.” The only situation in which the Board properly can consider whether transportation is being provided under a contract is when a party before the Board claims that a dispute belongs in court rather than before the Board. In those circumstances, the Board can decide not to proceed until the issue is resolved in court in order to avoid expending resources on a matter that may fall outside

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<sup>1</sup> Comments of National Grain and Feed Association (“NGFA Comments”) at 14.

<sup>2</sup> See Comments of Ameren Energy Fuels and Services Co. (“Ameren Comments”) at 5-6; Comments of Canadian Pacific Railway Co. (“CP Comments”) at 3-4; Comments of Dairyland Power Coop. (“Dairyland Comments”) at 6-7; Comments of Entergy Services Inc. (“Entergy Comments”) at 8-9; Comments of Norfolk Southern Railway Co. (“NS Comments”) at 4-5; Comments of The Western Coal Traffic League (“WCTL Comments”) at 13-18.

its jurisdiction.<sup>3</sup> In making its decision, however, the Board should consider state law, not a special definition of “contract,” and the proposed definition is not even a useful summary of state law.<sup>4</sup>

**A. The Board Cannot And Should Not Prohibit “Unilateral” Contracts.**

A few shippers commented that the proposed definition would be useful because it appears to exclude what National Industrial Transportation League (“NITL”) called “contracts-that-look-like-tariffs.”<sup>5</sup> These appear to be the arrangements that, in their opening comments, UP called unilateral contracts, CSX called Private Price Quotations, and NS called signatureless contracts. UP does not believe that the Board intended to exclude these arrangements from the proposed definition of “contract.” As UP and other railroads observed, these arrangements serve legitimate commercial purposes, and precluding their use would be inconsistent with Congress’s intent in allowing railroads and shippers to enter into contractual arrangements and the specific language of Section 10709, which does not distinguish between “unilateral” and “bilateral” contracts.<sup>6</sup>

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<sup>3</sup> See WCTL Comments at 16-18 (citing *Toledo Edison Co. v. Norfolk W. Ry.*, 367 I.C.C. 869, 872-73 (1983) & *Cross Oil Refining & Mktg., Inc. v. Union Pac. R.R.*, STB Docket No. 33582 (STB served Oct. 27, 1998)).

<sup>4</sup> See NS Comments at 5-8; Comments of CSX Transportation, Inc. (“CSX Comments”) at 10-12.

<sup>5</sup> Comments of the National Industrial Transportation League (“NITL Comments”) at 3-4; see also Comments of E.I. DuPont de Nemours & Co. (“DuPont Comments”) at 1-2; Comments of U.S. Clay Producers Traffic Association, Inc. (“Clay Producers Comments”) at 2-3.

<sup>6</sup> See CSX Comments at 3-8; NS Comments at 7-8; Comments of Union Pacific Railroad Co. (“UP Comments”) at 12-13.

CSX suggests that the Board could adopt a “bright line” rule that all “confidential” pricing arrangements are contracts. See CSX Comments at 16-17. However, that proposal is inconsistent with CSX’s (correct) statement that the Board cannot narrow Congress’s definition of “contract” in § 10709. See *id.* at 3-4. As BNSF observes in its comments, Congress did not (continued...)

Regardless of the Board's intent, the Board's proposed definition would not produce the result that the complaining shippers seek. As long as the arrangements at issue constitute valid contracts under state law, the Board cannot change that fact by adopting a different definition of "contract." Either party still could enforce the contract in court, and the Board would have no jurisdiction over claims involving transportation provided under the contract. *See* 49 U.S.C. §§ 10709(b), (c); *see also Rates on Iron Ore, Randville to Escabana via Iron Mountain*, 367 I.C.C. 506, 511 (1983) ("Because judicial enforcement of a contract will override our maximum reasonable rate determinations, our procedures must accommodate the court's jurisdiction.").<sup>7</sup>

NITL and other shippers that complain about unilateral contracts never explain how shippers would be better off if carriers were prohibited from offering such arrangements. The apparent consequence would be to reduce the range of options available to railroads and shippers – again, an outcome that would be the opposite of what Congress intended when it enacted Section 10709.

Moreover, shippers do not need the Board's assistance if they do not want to enter into particular types of contractual arrangements. NITL is wrong when it claims that rail carriers can force shippers into unwanted contracts "to immunize their activity from Board jurisdiction."<sup>8</sup>

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require that contract terms remain confidential, at least where a shipper consents to disclosure. *See* Comments of BNSF Railway Co. ("BNSF Comments") at 4-5; *see also* 49 U.S.C. § 11904.

<sup>7</sup> A few shippers argued that contracts between rail carriers and shippers often are contracts of adhesion that would not be enforceable. *See, e.g.,* NGFA Comments at 10-13; Comments of Edison Electric Institute at 5-7. A shipper's right to obtain common carrier rates should preclude any claim that a contract with a railroad is a contract of adhesion. In any event, this is not a matter for the Board: if a shipper believes its contract is an unenforceable contract of adhesion, it can and must make that claim in court.

<sup>8</sup> NITL Comments at 4.

A shipper with traffic that is subject to the Board's jurisdiction always can refuse to enter into a contract and demand that the carrier provide it with common carrier rates and service terms. 49 U.S.C. § 11101(b).<sup>9</sup> If a shipper is not satisfied by those rates and service terms, it can file a complaint with the Board. 49 U.S.C. § 11701.

**B. The Board Should Not Disclaim Jurisdiction Over Arrangements That Shippers And Carriers Have Long Regarded As Common Carrier Rates.**

Most participants in this proceeding, including most shippers that filed comments, expressed concern that the Board's proposal would prevent shippers and carriers from entering into mutually beneficial common carrier arrangements because it would classify "such common transportation arrangements as unit train transportation and annual volume rates" as "contracts."<sup>10</sup> The Board should respect this concern and withdraw its proposal.

Western Coal Traffic League ("WCTL") showed in its comments that traditional unit train tariffs and annual volume rates typically contain bilateral promises, including promises regarding minimum number of cars or tons per shipment, free time, placement and bunching of trains, provision of track facilities, use of dedicated locomotive power, use of shipper-supplied equipment, payments for failure to perform, force majeure provisions, as well as rates that apply for an extended period of time in exchange for volume commitments.<sup>11</sup> As WCTL and other coal shippers explain, treating such arrangements as common carrier transportation allows

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<sup>9</sup> Even shippers of exempt traffic can seek a partial revocation of an exemption in order to require a carrier to provide regulated rates and service terms. *See* 49 U.S.C. § 10502(d).

<sup>10</sup> WCTL Comments at 4; *see also* Dairyland Comments at 5-6; DuPont Comments at 2; Entergy Comments at 9-10; NGFA Comments at 6-9; NITL Comments at 6-7.

<sup>11</sup> WCTL Comments at 19-20; *see also* Entergy Comments at 9 ("Unit train coal movements often entail a series of mutual exchanges on many essential terms (e.g., train sizes, provision of railcars, annual volume commitments, and unloading), with the involved pricing intertwined with these commitments over specific time periods.").

carriers and shippers to design efficient services and obtain a measure of certainty regarding future rates and volumes while preserving the right to seek regulatory relief.<sup>12</sup>

Coal shippers were not the only shippers worried that the Board's proposal would preclude the use of efficient, mutually beneficial common carrier arrangements. DuPont and NITL also expressed concern that the proposal would preclude carriers and shippers from using traditional annual volume tariff rates.<sup>13</sup> NGFA expressed concern that the Board's proposal might undermine the various special rate offerings and equipment guarantee programs that railroads implement in the grain industry through tariff mechanisms.<sup>14</sup>

UP agrees with WCTL and the other participants in this proceeding that it would be counterproductive to restrict the types of provisions that can be included in common carrier arrangements. UP further agrees with WCTL and other participants that the critical distinction

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<sup>12</sup> See WCTL Comments at 20-21; Dairyland Comments at 5-6; Entergy Comments 9-10.

<sup>13</sup> See DuPont Comments at 2; NITL Comments at 7.

DuPont suggests that traditional annual volume rates, which include "fallback" rates that the shipper must pay if it fails to ship the stated volume, may fall outside the proposed definition because the shipper does not expressly promise to meet the volume requirement or pay liquidated damages. See DuPont Comments at 2. CSX makes a similar suggestion. See CSX Comment at 17-18 & n.15. However, NITL observes that, as a practical matter, a traditional volume rate is no different from a rate involving an express bilateral promise to meet a volume requirement or pay damages because a "promise can be implied, especially since the shipper is required to pay the 'fallback' rate if the stated annual volume is *not* shipped, and the difference between the annual volume rate and the fallback rate can easily be interpreted as a form of 'liquidated damages' for failing to ship the stated annual volume." NITL Comments at 7.

<sup>14</sup> See NGFA Comments at 17. BNSF expressed similar concerns and asked the Board to make clear that its "Certificates of Transportation Concerning Agricultural Commodities" will continue to be treated as common carrier arrangements. See BNSF Comments at 3. UP has a similar program, the "Grain Car Allocation System." If the Board addresses this issue, it should make clear that all similar programs will continue to be treated as common carrier arrangements.

between contract and common carrier arrangements is the parties' intent, not the types of provisions contained in the parties' arrangements.<sup>15</sup>

Several participants also expressed concern that the Board's proposal might lead to cases in which both the Board and the courts disclaim jurisdiction because an arrangement that constitutes a contract under the Board's proposal would not constitute a contract under state law.<sup>16</sup> UP agrees that such situations should be avoided. Withdrawing the proposal would eliminate this concern.

## **II. COMPLAINTS ABOUT UP CIRCULAR 111 ARE MISGUIDED.**

As UP observed in its opening comments, the Board's proposal is clearly intended to prevent carriers from establishing common carrier arrangements with the characteristics found in Option 2 of UP Circular 111. Ironically, coal shippers, who have complained so loudly about Circular 111, are defending the positions that UP has consistently taken: Option 2's provisions fall within the range of permissible common carrier offerings, and a contract cannot exist if the parties manifestly intend not to create a contract.<sup>17</sup> Indeed, UP's consistent position that Circular 111 rates are common carrier rates belies allegations by several participants that UP designed Circular 111 to provide "maximum flexibility to fend off any review by either the STB or the

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<sup>15</sup> See, e.g., WCTL Comments at 21-22; Entergy Comments at 10; NS Comments at 8.

<sup>16</sup> See, e.g., Entergy Comments at 10; NS Comments at 5-6.

<sup>17</sup> Compare WCTL Comments at 18-22 & Entergy Comments at 9-10, with UP Comments at 6-8 & UP's Brief in Response to Order to Show Cause, *Kansas City Power & Light Co. v. Union Pac. R.R.*, STB Docket No. 42095 at 6-8 (Sept. 25, 2006).

courts.”<sup>18</sup> As other participants correctly observed, UP has “adher[ed] to its position” and has “not succumb[ed] to the opportunity to back-track in an effort to escape accountability.”<sup>19</sup>

Some participants have suggested a different way to attack Circular 111, arguing that Option 2 rates are not a proper response to a request for common carrier rates because some customers may not want rates based on volume commitments and other terms commonly found in unit train rates.<sup>20</sup> This criticism overlooks the fact that UP also established Option 1 rates for all customers covered by Circular 111. Option 1 rates are unit train rates but contain no volume commitment, liquidated damages provision, or service commitment. If a shipper does not want a rate based on the terms contained in Option 2, it always remains free to chose Option 1.<sup>21</sup> But as WCTL makes clear, coal shippers strongly prefer the rates and terms found in Option 2.<sup>22</sup>

At the same time, WCTL is the most strident participant in its complaints about Circular 111. So why is WCTL complaining? WCTL argues that UP’s Circular 111 is not a lawful common carrier holding out because Circular 111 rates are not “publicly disseminated.”<sup>23</sup> However, WCTL misstates the law. Section 11101(b) does not require rail carriers to “publicly

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<sup>18</sup> Entergy Comments at 10; *see also* WCTL Comments at 3 (asserting that UP has tried “to recast what are essentially contractual arrangements as common carrier offerings in an attempt to immunize them from scrutiny”).

<sup>19</sup> AECC Comments at 7.

<sup>20</sup> *See, e.g.*, Ameren Comments at 5-6; NS Comments at 1.

<sup>21</sup> *Cf.* NS Comments at 12 (“[A] common carrier rate provided in response to a customer’s formal request may include various restrictions so long as the customer is agreeable.”).

<sup>22</sup> WCTL Comments at 20 (“It is difficult to see how effectively prohibiting such customer commitments could be consistent with sound common carrier policy.”); *id.* at 24 (“[A] common carrier rate devoid of such provision would likely provide inadequate service or entail unacceptable rates.”).

<sup>23</sup> *Id.* at 8.

disseminate” their common carrier rates; rather, it requires rail carriers to “provide to any person, *on request*, the carrier’s rates and other service terms.” 49 U.S.C. § 11101(b).<sup>24</sup>

Moreover, despite its criticism, WCTL plainly does not want UP to disseminate publicly the rates contained in Circular 111. WCTL comments extensively about its concern that “public pricing facilitates collusion and higher rates.”<sup>25</sup> But, as WCTL must acknowledge, UP has not, in fact, publicly disseminated its rates under Circular 111. Instead, UP has provided Circular 111 rates to eligible customers only, which fully satisfies the two basic concerns that Congress sought to address by requiring railroads to provide rates on request: “(1) the shippers’ right to know in advance the rates they will be charged and (2) the [Board’s] responsibility to review tariff charges when there is a reason to do so.” *Electronic Filing of Tariffs*, 5 I.C.C.2d 279, 282 (1989).<sup>26</sup>

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<sup>24</sup> WCTL implies that UP prevented it from raising this argument in a federal district court proceeding in Texas by asking the court to dismiss WCTL’s complaint for lack of standing. *See* WCTL Comments at 2. In fact, however, the court considered the argument and concluded that WCTL had no standing because the argument was flawed. *See Western Coal Traffic League v. BNSF Ry. and Union Pac. R.R.*, No. 4:04-CV-679-Y, slip op. at 6 (N.D. Tex. Mar. 29, 2006) (“The statute WCTL cites does not require, however, that the rates be publicly propounded; instead, it requires that rail carriers ‘provide to any person, on request, the carrier’s rates and other service terms.’ 49 U.S.C.A. § 11101(b) (West 1997). WCTL’s complaint fails to allege any facts demonstrating that any of its members have been unable, upon request, to obtain a copy of the rates.”). UP also argued that disputes about whether Circular 111 is a lawful common carrier holding out were best addressed by this Board.

<sup>25</sup> WCTL Comments at 9-12. Congress has adopted a different view by providing that the antitrust laws do not apply to an agreement “that provides solely for compilation, publication, and other distribution of rates in effect or to become effective.” 49 U.S.C. § 10706(a)(4).

UP strongly denies WCTL’s assertion that its adoption of Circular 111 has “resulted in massive rate increases.” WCTL Comments at 3. After many decades of falling rates, rates are now rising as the result of market forces. As the Board explained in another proceeding: “Rail capacity is strained, demand for transportation service is forecast to increase, and railroads must make capital investments to meet that demand.” *Simplified Standards for Rail Rate Cases*, STB Ex Parte No. 646 (Sub-No. 1), slip op. at 11 (STB served July 28, 2006).

<sup>26</sup> By contrast, common carrier rates for agricultural products must be publicly disclosed. *See* 49 U.S.C. § 11101(d) (“With respect to transportation of agricultural products, . . . a rail (continued...)”).

In sum, WCTL's arguments are fundamentally at odds with each other. WCTL says that railroads should be allowed to offer common carrier rates with the provisions contained in Option 2 rates; it insists that such common carrier rates must be publicly disseminated, but it then complains that publicly disseminating such common carrier rates would facilitate collusion.<sup>27</sup>

So what does WCTL want? WCTL argues that the Board should allow shippers to elect, at an appropriate time, whether to treat Circular 111 rates as contract rates or common carrier rates.<sup>28</sup> However, Board action would not change the options available to shippers. Any shipper that would "elect" to treat Circular 111 as establishing common carrier rates would not meet resistance from UP: as discussed above, UP has made abundantly clear that it intended Circular 111 rates to be common carrier rates. Alternatively, any shipper that would "elect" to treat Circular 111 as establishing contract rates must make its case to a court, not the Board.<sup>29</sup>

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carrier shall publish, make available, and retain for public inspection its common carrier rates, schedule of rates, and other service terms . . .").

<sup>27</sup> WCTL is also being inconsistent when it criticizes UP and other carriers for protecting the confidentiality of contract information in rate cases and merger proceedings. *See* WCTL Comments at 6. Moreover, WCTL is wrong to say that UP insists on a Board order before it will produce contracts in discovery. UP is on record that its practice is not to require a Board order. Instead, UP notifies affected customers when it receives a discovery request and gives them an opportunity to object, pursuant to its obligations under the contracts and 49 U.S.C. § 11904. The customers can then decide whether to seek relief from the Board. *See* Reply Comments of Union Pacific Railroad Co. at 14, *Procedures to Expedite Resolution of Rail Rate Challenges to be Considered Under the Stand-Alone Cost Methodology*, STB Ex Parte No. 638 (STB June 19, 2003).

<sup>28</sup> WCTL Comments at 27; *see also* Entergy Comments at 10-11.

<sup>29</sup> WCTL incorrectly describes UP's recent dispute with Ameren regarding the application of Ex Parte 661 to Ameren's Circular 111 rates as a case in which the Board found that "there was a contract." WCTL Comments at 30. The Board found that there was a dispute regarding the parties' intent and that resolution of the dispute was a matter for the courts. *See Union Pac. R.R. – Petition for Declaratory Order*, STB Fin. Docket No. 35021, slip op. at 3 (STB served May 15, 2007).

WCTL also argues that the Board should treat Circular 111 as an unreasonable practice, with the similar result of “allow[ing] each adversely affected shipper to pursue an appropriate remedy.”<sup>30</sup> It repeats the contradictory and erroneous claims that Circular 111 creates a “potential for price signaling” and wrongly fails “to disclose the rates publicly.”<sup>31</sup> It also asserts that Circular 111 is unreasonable because UP established it “without any shipper request.”<sup>32</sup> However, UP has fully explained the sound commercial reasons for the creation of Circular 111.<sup>33</sup> Moreover, the Interstate Commerce Act does not preclude railroads from taking the initiative to establish innovative common carrier offerings. To the contrary, the law provides that a rail carrier “may establish any rate for transportation or other service provided by the rail carrier” unless the rate is specifically prohibited by the Act. 49 U.S.C. § 10701(c). Congress thus gave railroads “the freedom to explore new transportation programs and services.” *Nat’l Grain & Feed Ass’n v. Burlington N.R.R.*, 8 I.C.C.2d 421, 439 (1992). Accordingly, UP’s creation of Circular 111 cannot be regarded as an unreasonable practice.

Finally, WCTL wants the Board to make clear that “its actions are not intended and should not be construed to confer any antitrust or other form of immunity or other form of protection or deference to the railroads’ public pricing.”<sup>34</sup> UP would not object if the Board indicates that its decision in this matter should not be construed as having any such effect.

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<sup>30</sup> WCTL Comments at 31.

<sup>31</sup> *Id.* at 30.

<sup>32</sup> *Id.*

<sup>33</sup> UP Comments, Attachment A.

<sup>34</sup> WCTL Comments at 32.

### III. CONCLUSION

For the reasons discussed above, the Board should withdraw its proposal to define the term “contract” and resist joining in misguided criticisms of UP Circular 111.

Respectfully submitted,



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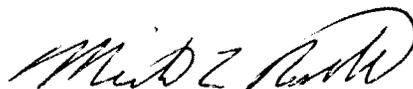
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August 2, 2007

**CERTIFICATE OF SERVICE**

I, Michael L. Rosenthal, certify that on this 2nd day of August, 2007, I caused a copy of the foregoing document to be served on all parties of record in this proceeding by first-class mail, postage prepaid.



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Michael L. Rosenthal